



GLOBAL MARKETS IN CLEAR VIEW

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# **Introducing Centralized Clearing to the Credit Derivatives Industry**

February 6, 2009

[www.theice.com](http://www.theice.com)

# LEGAL DISCLAIMER

## Safe Harbor Statement

Statements in this presentation regarding IntercontinentalExchange's business that are not historical facts are "forward-looking statements" that involve risks and uncertainties. For a discussion of additional risks and uncertainties, which could cause actual results to differ from those contained in the forward-looking statements, see ICE's Securities and Exchange Commission (SEC) filings, including, but not limited to, the risk factors in ICE's Annual Report on Form 10-K for the year ended December 31, 2007, and ICE's Quarterly Reports on Form 10-Q for the quarters ended June 30, 2008 and September 30, 2008, as filed with the SEC on February 13, 2008, August 4, 2008, and October 30, 2008, respectively.



# AGENDA

- ICE Introduction
- OTC Markets Overview
- Credit Default Swaps Introduction
- ICE Trust
- Summary



# ICE INTRODUCTION: OVERVIEW

ICE is a leading, global derivatives exchange operator. Through our sophisticated trading and clearing technology infrastructure, we offer benchmark futures and options contracts for energy, soft and agricultural commodities, equity indexes and currencies, as well as the leading electronic global OTC energy marketplace.

## **Global Reach**

- Screens and customers in 55 countries
- 3 regulated futures exchanges: ICE Futures Europe, ICE Futures U.S. and ICE Futures Canada
- 3 regulated clearing houses (Europe, U.S., Canada )
- 2 OTC Platforms

## **Diverse Products and Markets**

- Energy, agricultural, financial products
- Futures, options and OTC markets

## **Superior Technology**

- Sophisticated, scalable & widely distributed trading platform
- Focus on innovation, customers and technology

## **A History of Innovation**

- ICE was the first to introduce clearing to the power markets, which were the domain of voice brokered, bilateral transactions similar to how credit default swaps markets operate today



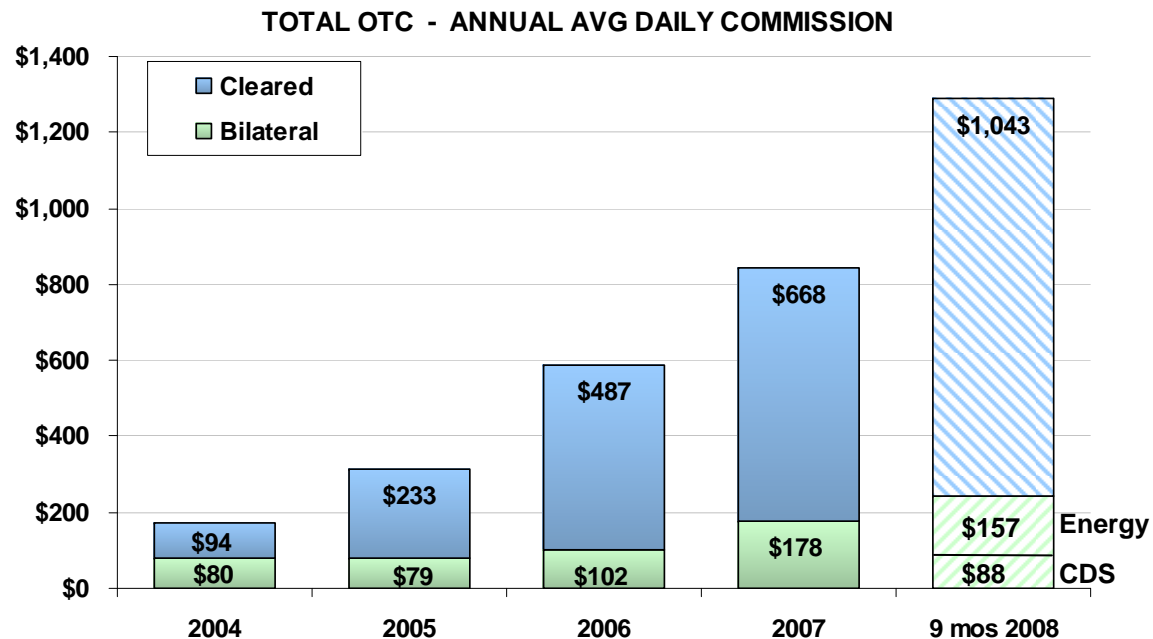
A Global Exchange:  
Today ICE has 11 offices throughout  
Asia, Canada, the U.K. and the U.S.



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# ICE INTRODUCTION: OTC ENERGY & CREDIT MARKETS

ICE operates the leading global electronic OTC marketplace for natural gas and power and is a leader in the execution and processing of CDS.



## ENERGY PRODUCTS

- Over 800 products listed for natural gas, power and refined oil products
- Approximately 120 cleared products

## ENERGY CUSTOMERS

- Commercial energy companies ~50%
- Banks/Financial institution ~25%
- Liquidity providers (prop/algo/funds) ~25%

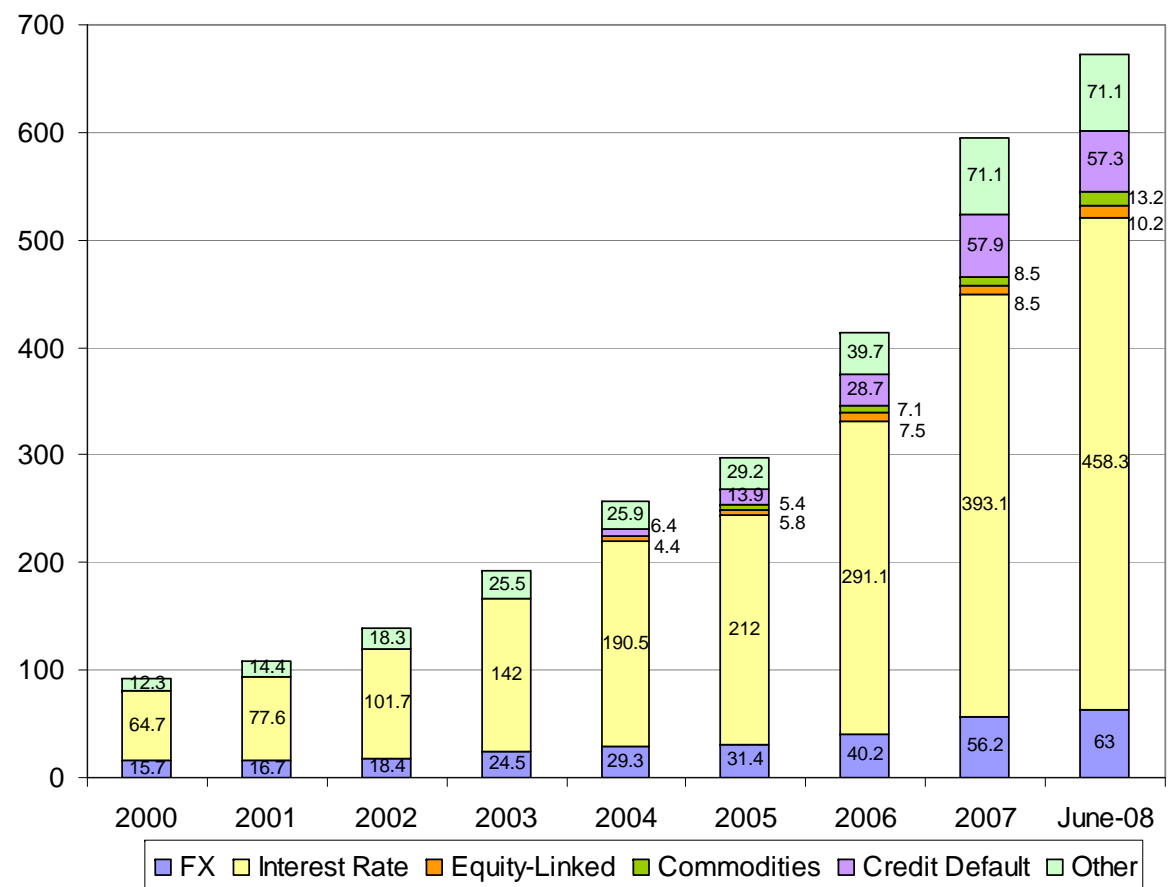


# OTC MARKETS OVERVIEW: TRACK RECORD OF GROWTH

- The OTC market is approximately 8 times the nominal value of the on-exchange derivatives market according to BIS estimates
- Substantial need and demand exists for OTC clearing in a range of asset classes where none is available today:
  - FX
  - Interest rates
  - Credit
  - Metals
- 99% of OTC derivatives are never cleared
- ICE has been the market leader in offering cleared OTC products due to its ability to aggregate opaque, brokered markets on a global trading platform



**Nominal OTC Derivatives Outstanding (\$Tn)**

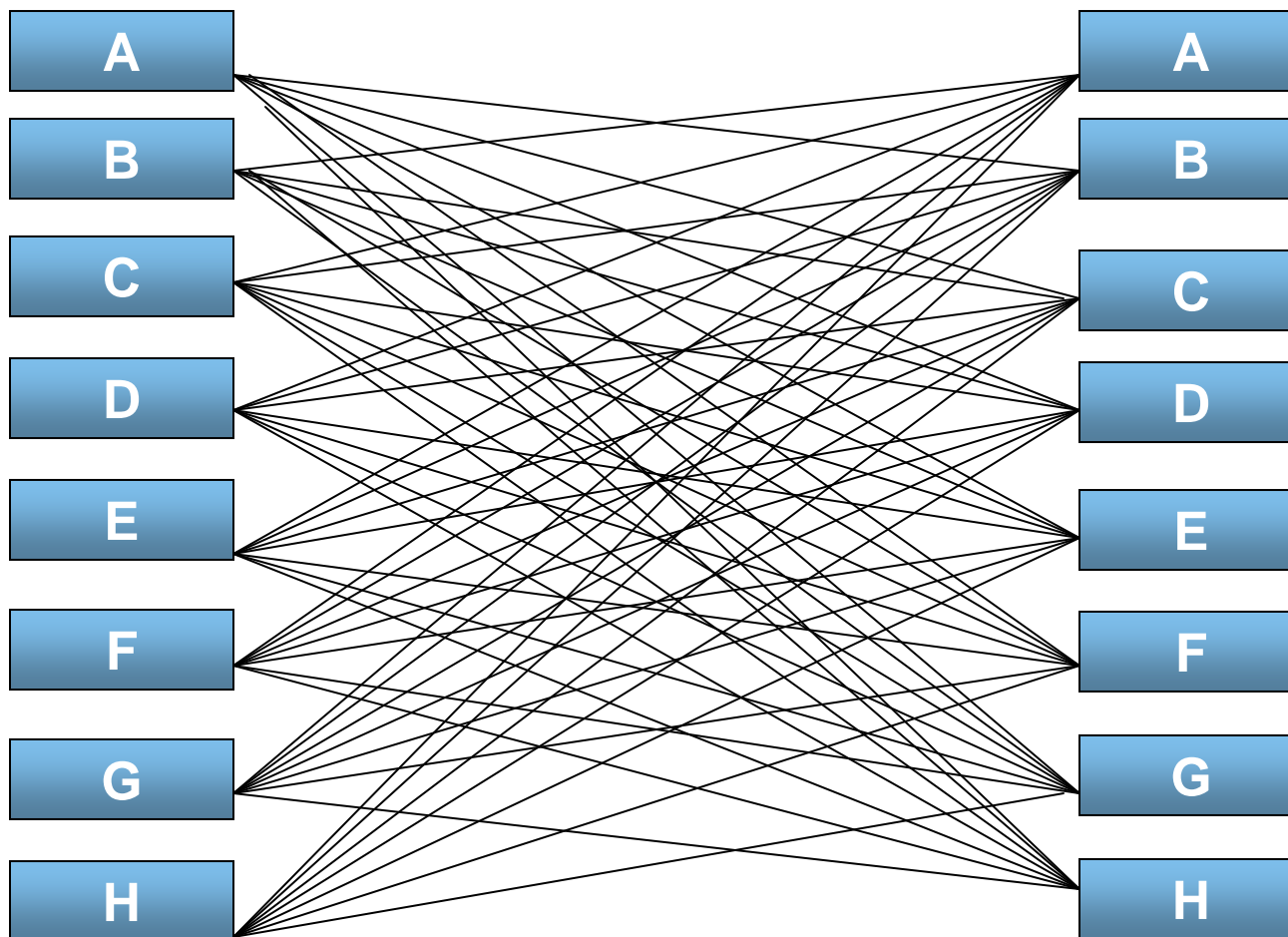


Source: BIS

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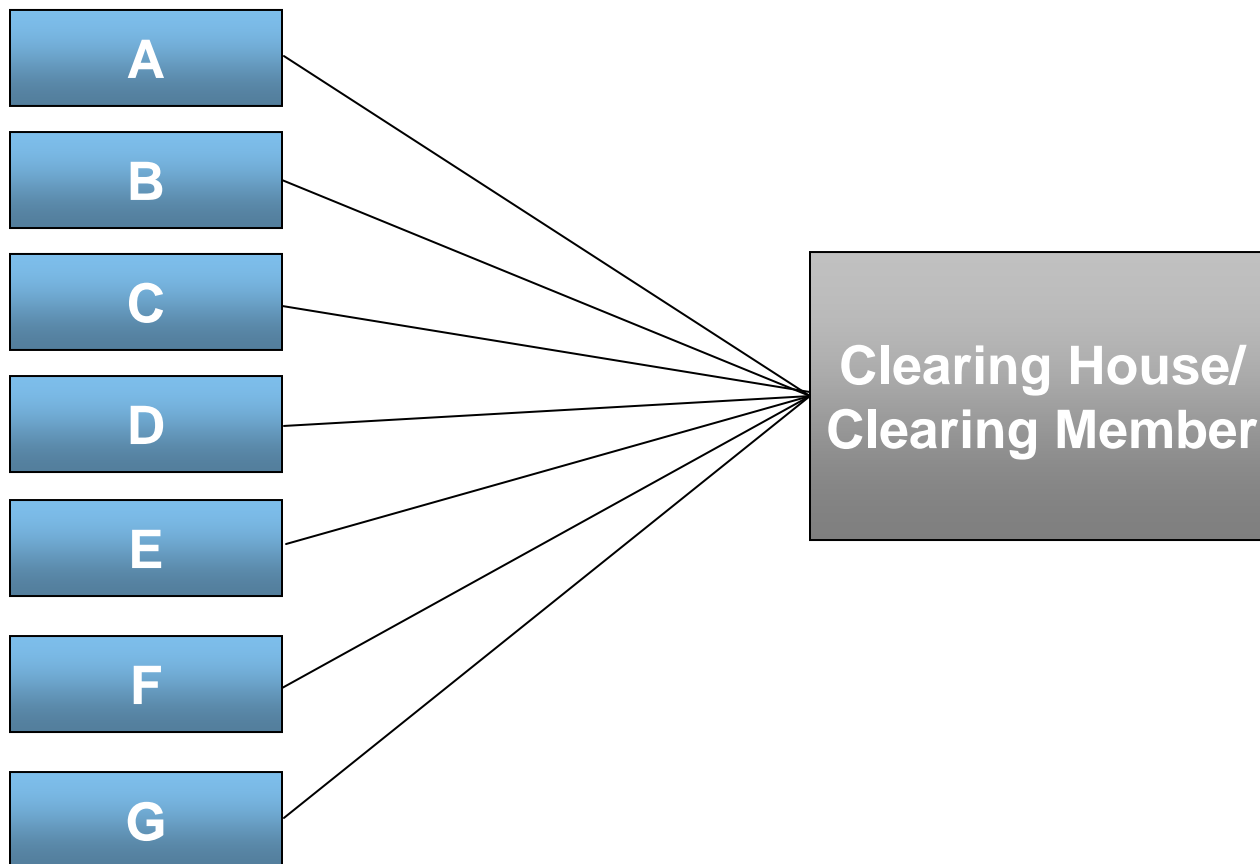
# OTC MARKETS OVERVIEW: NON-CLEARED TRADING

In the bilateral markets, participants maintain direct credit lines with one another.



# OTC MARKETS OVERVIEW: CLEARED TRADING

A centralized clearing house serves as the seller to every buyer and the buyer to every seller, eliminating direct counterparty risk found in the bilateral market.



## OTC MARKETS OVERVIEW: CLEARING BENEFITS

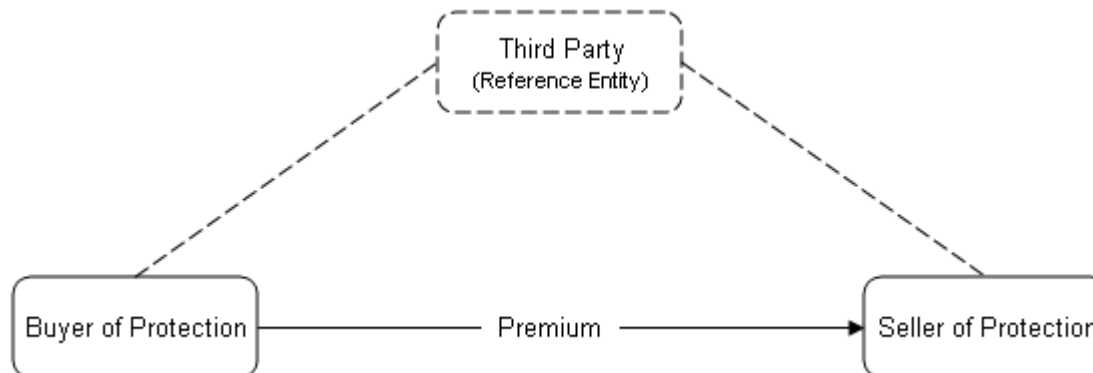
- Reduced counterparty credit risk
- Increased market liquidity
- Standardized contracts
- Free up bilateral credit lines
- Common collateralized default fund
- Multilateral netting: capital efficiency across multi-market positions
- Streamline front- and back-office operations
- Mark to Market
- Block Trades



# CDS INTRODUCTION: WHAT IS A CDS CONTRACT?

- An agreement between two counterparties to insure one of them against a credit event occurring in a third party, for a given premium
- Agreement has two different states – ‘No Default’ and ‘Default’

How a CDS contract operates in a state of no default



## CDS INTRODUCTION: TRADING CDS

- Standard contract size (amount of protection) usually \$5MM or \$10MM for single names
- CDS Index trades standard size is usually much larger – between \$25 and \$100MM
- Standard quotation of premium cost is x basis points per annum
- Most liquid maturity is 5Y; the longer the duration, the more expensive the premium
- Standard maturity dates based on IMM dates – 20 Mar, 20 Jun, 20 Sep, 20 Dec



# CDS INTRODUCTION: TRADE EXECUTION

## Voice Brokers

- Tullet Prebon, Tradition

## Hybrid Brokers (Voice + Electronic)

- Creditex, ICAP, GFI, MarketAxess, etc.

## Market Participants

- Dealers/large investment banks (sell-side)
- Bondholders (buy-side)
- Institutional investors
- Index funds
- Hedge funds (buy and sell-side)



# ICE TRUST: OUR CDS EXPERTISE

**ICE has an established track record of leading the CDS market in critical industry initiatives.**

•**T+0 Trade Processing:** Same-day processing of CDS affirmations and novation consent; interconnectivity among prime brokers, buy-side firms, dealers and the DTCC trade warehouse

•**Credit Event Auctions:** ICE is the official co-administrator of auctions used to settle CDS contracts following default - auctions have been used recently in connection with the defaults of Fannie, Freddie, Lehman, etc.

•**Portfolio Compression:** ICE provides the industry standard platform for multi-lateral termination of single-name CDS contracts -- since August, over \$2 trillion in notional have been compressed

•**Electronic Trading:** ICE was the first to launch electronic trading for CDS in Europe and continues to lead the market with innovative electronic trading solutions



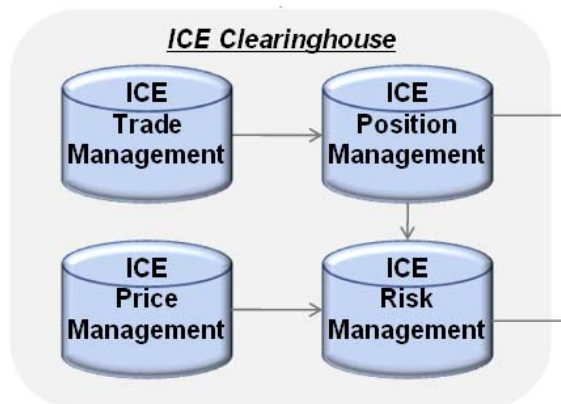
## ICE TRUST: BACKGROUND INFORMATION

ICE is working closely with industry and regulators to develop a central counterparty clearing solution.

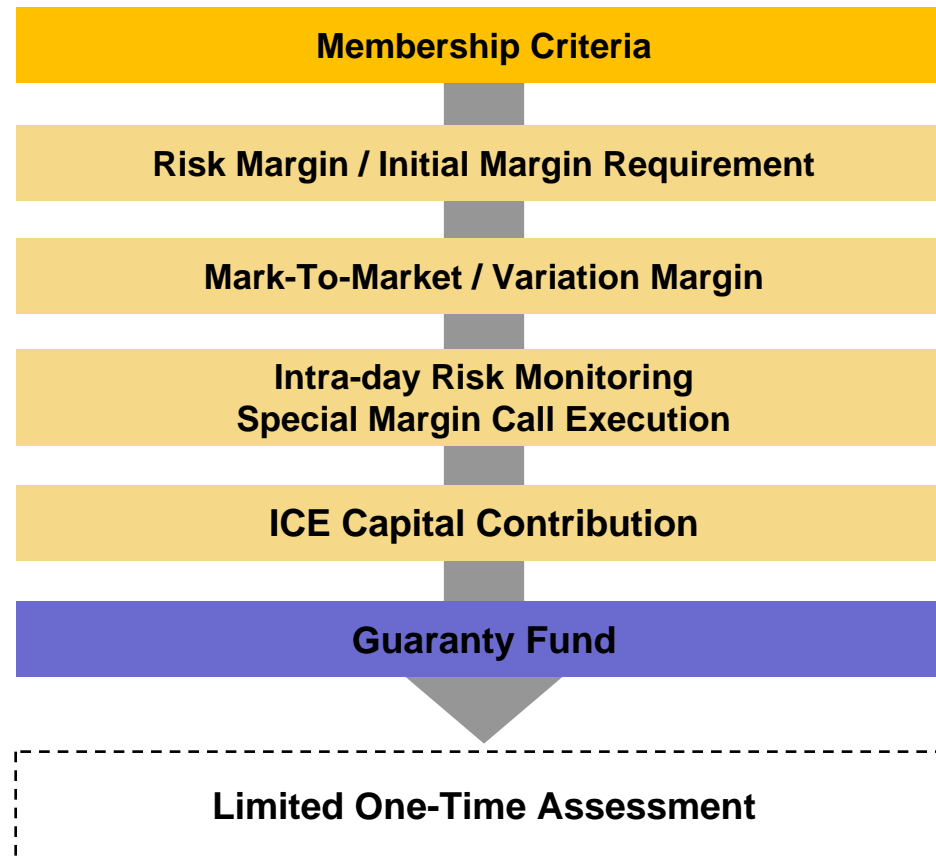
- Announced in October plans to develop a global clearing solution in conjunction with 9 major CDS dealers, The Clearing Corporation and Markit
- CDS will be cleared through ICE Trust, a New York limited trust company; ICE Trust has applied to become a member of the Federal Reserve system
- CDS clearing to be separated from futures clearing
- Once regulatory approvals are received, ICE Trust will begin clearing CDS index contracts initially, with large single name contracts to follow



# ICE TRUST: TRADE PROCESSING & CLEARING



# ICE TRUST: RISK MANAGEMENT FRAMEWORK

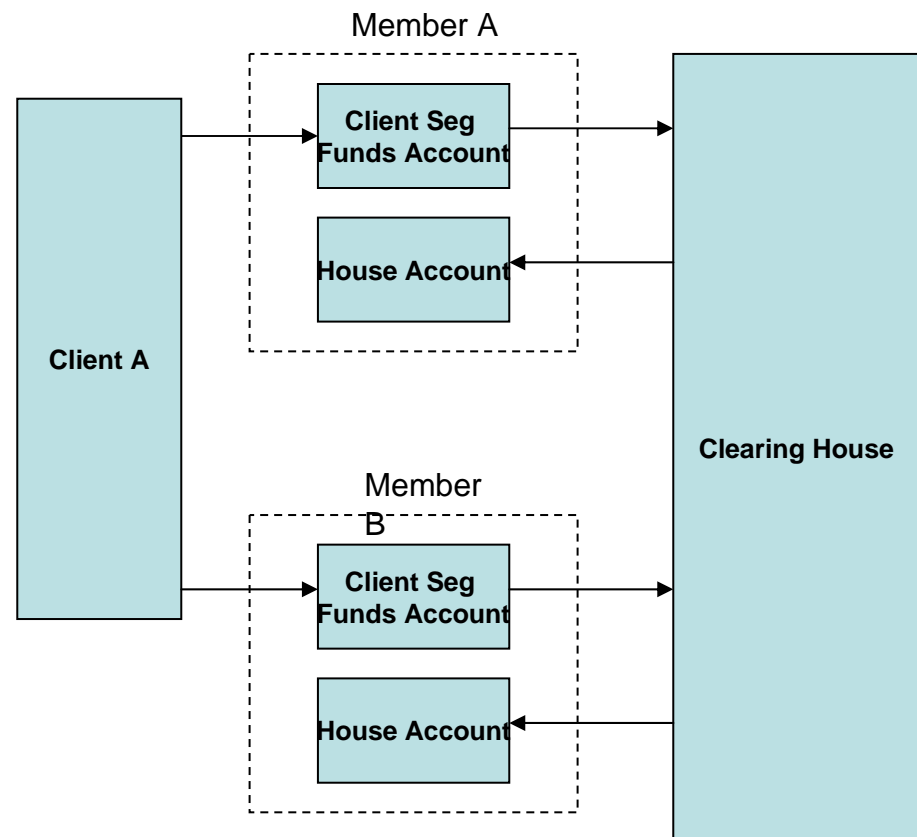


# ICE TRUST: END OF DAY PRICING & MARGINING

## Proper risk management requires robust end-of-day pricing

- Combination of Markit/ICE Trust market data provides breadth and depth of pricing data unmatched in the marketplace
- Margin exchanged between Clearing Participants based on ICE Trust marks
- Intraday exposures to ICE Trust are monitored and action taken as needed
- Regulators are provided with additional level of transparency

## End-of-day pricing helps determine daily mark-to-market requirements



# ICE TRUST: CORPORATE STRUCTURE

## ***Open Membership***

- ICE Trust membership is open to all market participants that meet the clearinghouse's financial criteria
- Third-parties that do not meet the criteria of ICE Trust membership will be able to clear trades through clearinghouse members

## ***Open Clearing Platform***

- ICE Trust allows delivery of trades directly from multiple venues including T-Zero, MarkitWire, GFI, ICAP, etc.
- Integration and co-existence with other elements of CDS processing infrastructure, including DTCC Trade Information Warehouse (TIW) and buy-side access to independent Warehouse record
  - TIW is the only trade information repository in the CDS market. Therefore, most Clearing Participants, including buy-side, currently use DTCC's TIW in both Europe and the US

## ***Independent Governance***

- ICE Trust will be managed by an independent Board of Directors



# ICE TRUST: LEGAL & REGULATORY REQUIREMENTS

## Statutory & Regulatory Considerations

- ICE will comply with all necessary legal and regulatory requirements to build a robust global clearinghouse

### NYBD

- ICE will be organized as a NY State chartered limited purpose trust company

### SEC

- CDS transactions qualify as “security based swap agreements”; not subject to “Security Exchange Act” and “Securities Act”
- Seeking SEC exemption

### FRBNY

- ICE will be a member of Federal Reserve system
- ICE will be subject to direct supervision and examination by the Federal Reserve
- ICE will be subject to comprehensive ongoing regulatory oversight by FRBNY and NYBD
- Contemplated that FRBNY and NYBD will review and approve ICE Rules; review and approve Policies & Procedures and raise questions and recommend improvements, as appropriate

### FSA (UK)

- Will meet FSA legal and regulatory requirements

### CFTC

- ICE will comply with any CFTC requirements



# ICE TRUST: SUMMARY

- ICE is launch ready; a phased approach will be utilized
- ICE is uniquely qualified to provide a global clearing solution
- ICE has extensive CDS domain expertise
- ICE has a complete risk management framework in collaboration with Clearing Participants
- ICE is deploying an open architecture model that enables integration with multiple execution / matching venues and participation from both buy and sell-side firms
- ICE will protect customers through segregated client accounts
- ICE will be sensitive to global legal and regulatory requirements

