

Cleared OTC Credit Default Swaps

Extending Security to OTC Markets Through Open Clearing

Security. Neutrality. Transparency.

October 2009

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CLEARED OTC CDS
CURRENT STATUS

Status of CME Group's Cleared OTC CDS Initiative

CME Group is currently engaged with dealers and customers with the intent of meeting the goals and commitments that market participants have made with respect to achieving buy-side access to CDS clearing

CME Group's offering is now a clearing only solution

A group of dealers and customers kicked off on October 6th a pre-launch program to:

- Discuss and resolve current open questions/issues and agree on product offering
- Establish clearing member and customer on-boarding documentation and protocols
- Develop an implementation plan for product rollout, testing cycles and full product launch
- Provide forum for sharing feedback and results to broader buy side audience in preparation for Q1 2010 launch

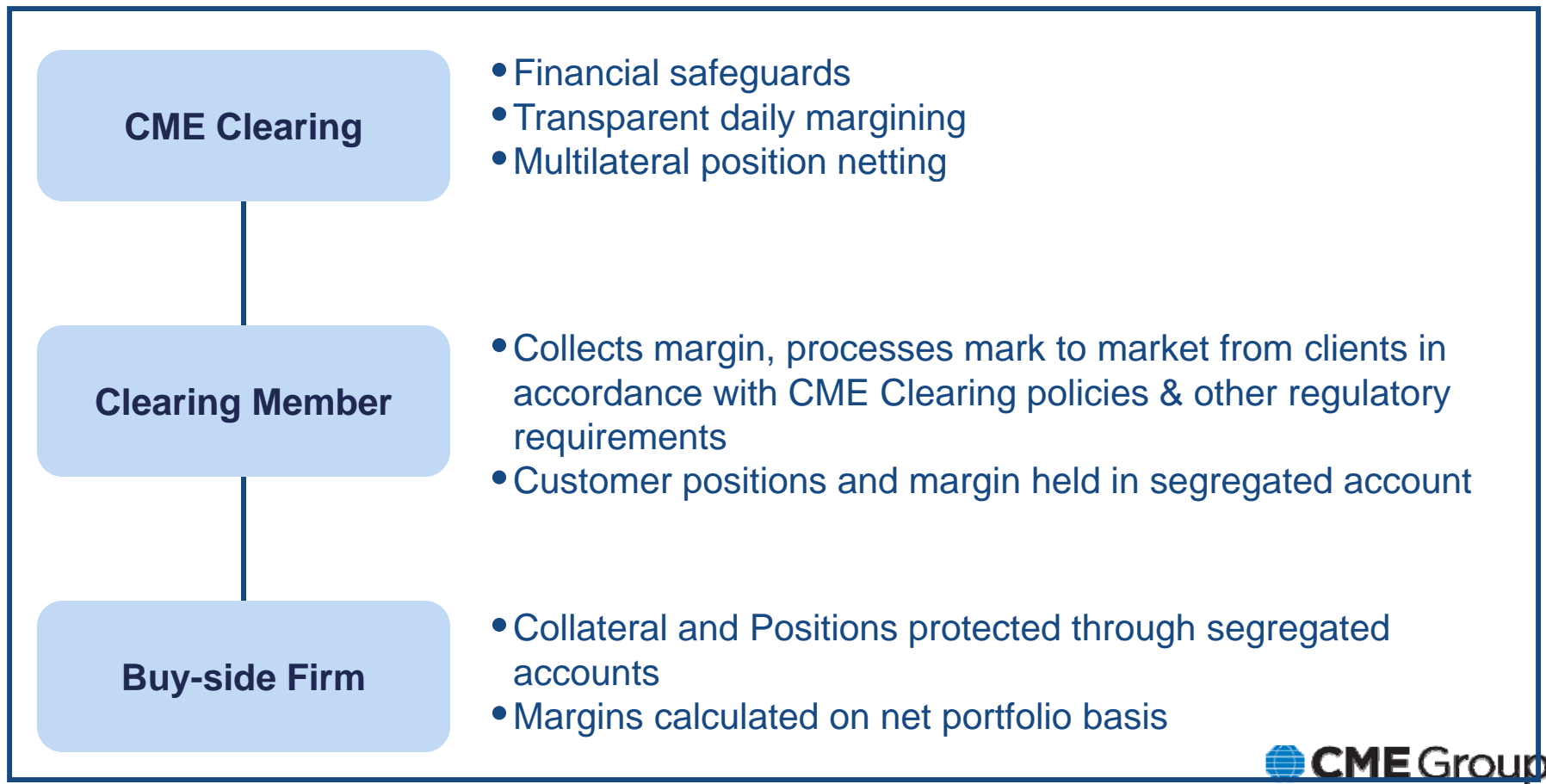
Additional clearing members and customers are expected to be on-boarded in Phase 2, which will begin in Q1 2010

- Additional index and single name contracts will be rolled out
- Contact CME Group and / or clearing members now to discuss participation in Phase 2

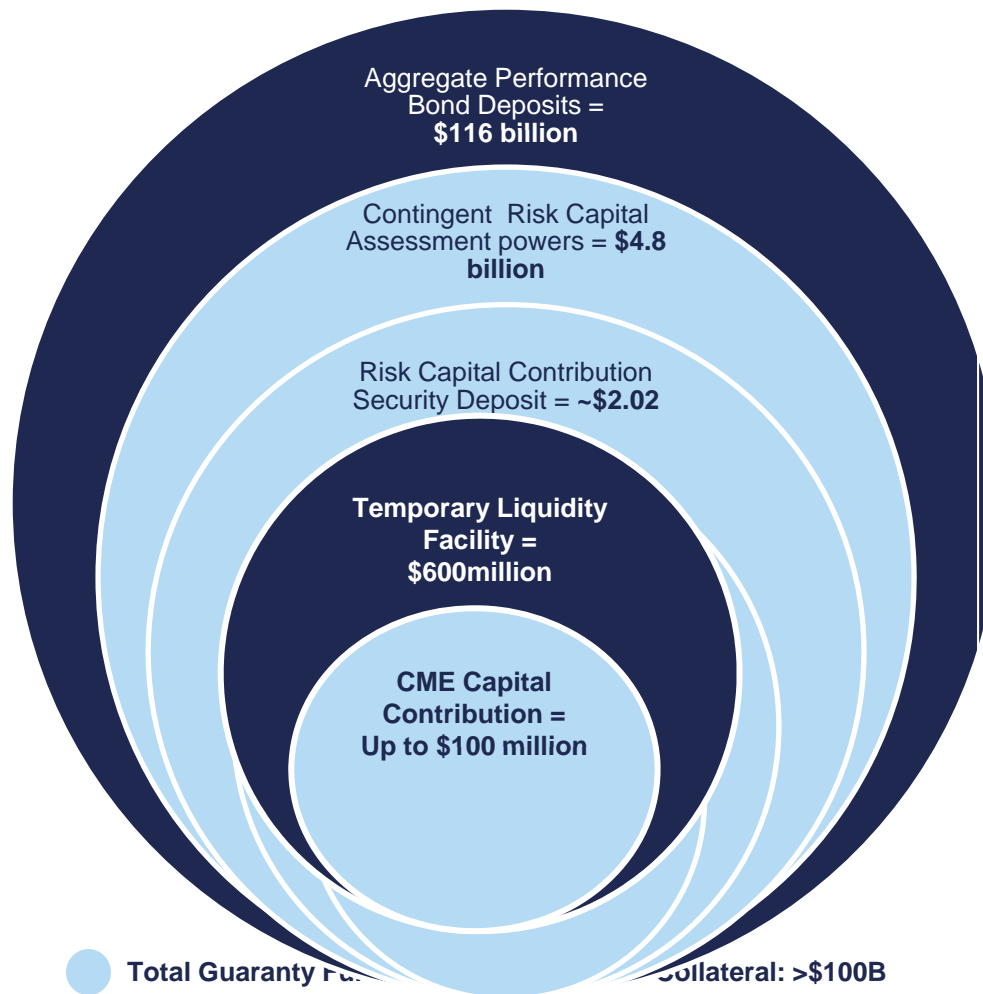
CLEARED OTC CDS
BUY-SIDE SOLUTION

CME Group Buy-Side Solution Model

In the more than 110-year history of CME Clearing, there has never been a failure by a clearing member to pay settlement variation or meet a performance bond call, nor has there ever been a clearing member failure resulting in a loss of customer funds



Benefits of CME Group's Cleared OTC CDS Solution



Total Financial Safeguards Package Overview

- CME Group's Financial Safeguards Package is Being Extended to CDS Products
- Designed to anticipate potential market exposures and ensure sufficient resources are available to cover future obligations
- Based on ability to cover at least the largest potential net debtor, accounting for collateral damage
- Wide variety of accepted security deposit collateral, including:
 - Cash (USD)
 - US Treasuries
 - CME-approved money market mutual funds

Benefits of CME Group's Cleared OTC CDS Solution

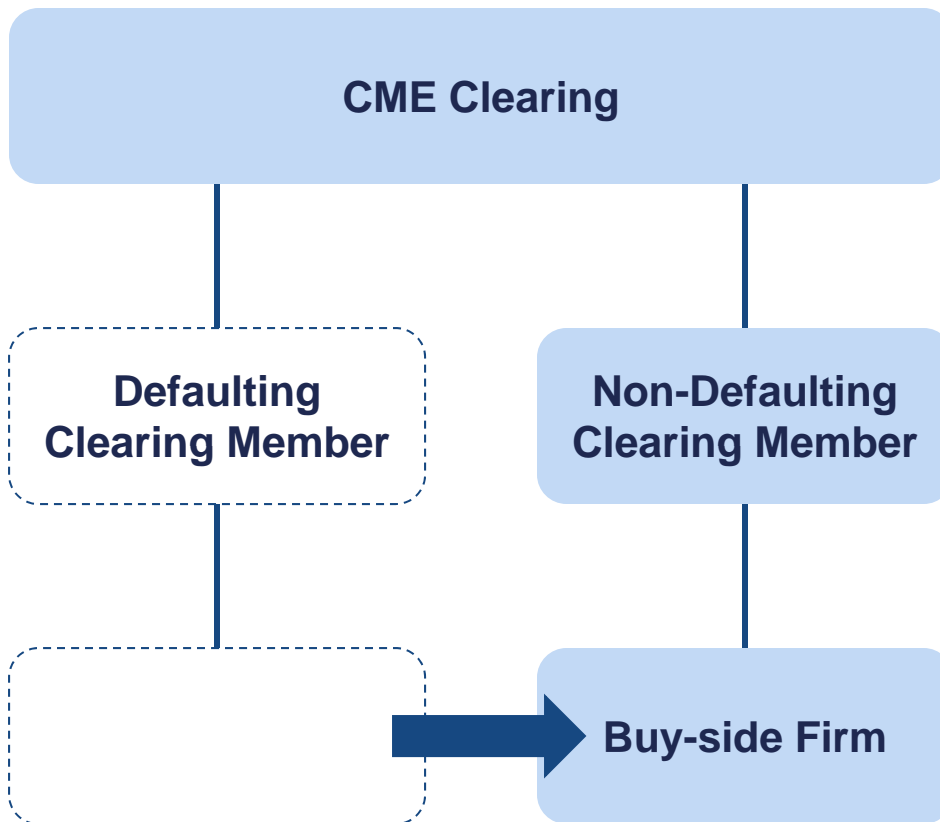
CME Group chose to offer CDS clearing in our DCO capacity precisely because it provides *superior protections* to all participants (and reduces systemic risk effects) in an insolvency of a CM, a customer or a custodian

***CME Clearing's
Customer
Protection
Mechanism for
CDS Products
Utilizes Time-
Tested Legal and
Regulatory
Frameworks***

- CME Group has asked CFTC for permission to keep CDS customer positions and related funds in CEA Section 4d/customer segregated account
- U.S. Bankruptcy Code and CFTC regulatory framework (including Part 190 Bankruptcy Rules) will apply
 - Section 4d mandates segregation of customer positions and property from the positions and property of the clearing firm
 - Claims of customers whose funds are held in defined account classes will have priority over proprietary claims and the claims of general creditors in an FCM bankruptcy

Benefits of CME Group's Cleared OTC CDS Solution

Portability of Customer Positions in the Event of a Clearing Member Default



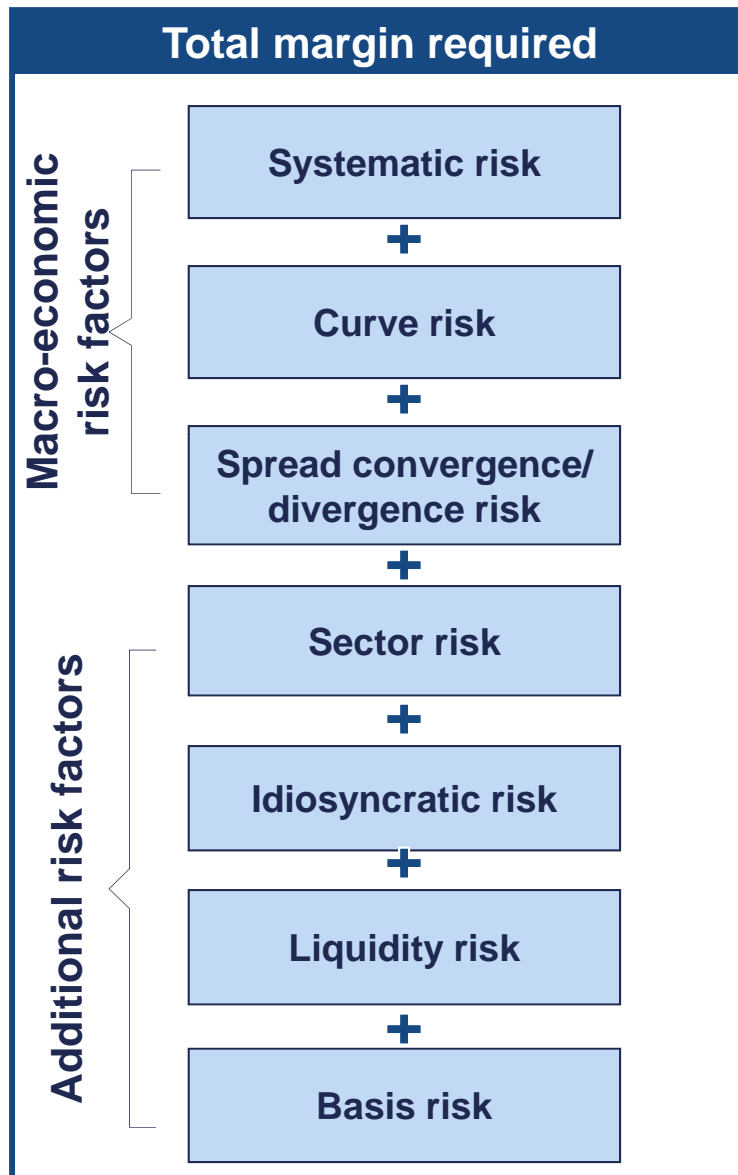
Defaulting members positions

- Market access restricted
- Collateral captured

Customer protection

- Collateral held in segregated account
- Positions maintained and moved to a new clearing member

Benefits of CME Group's Cleared OTC CDS Solution

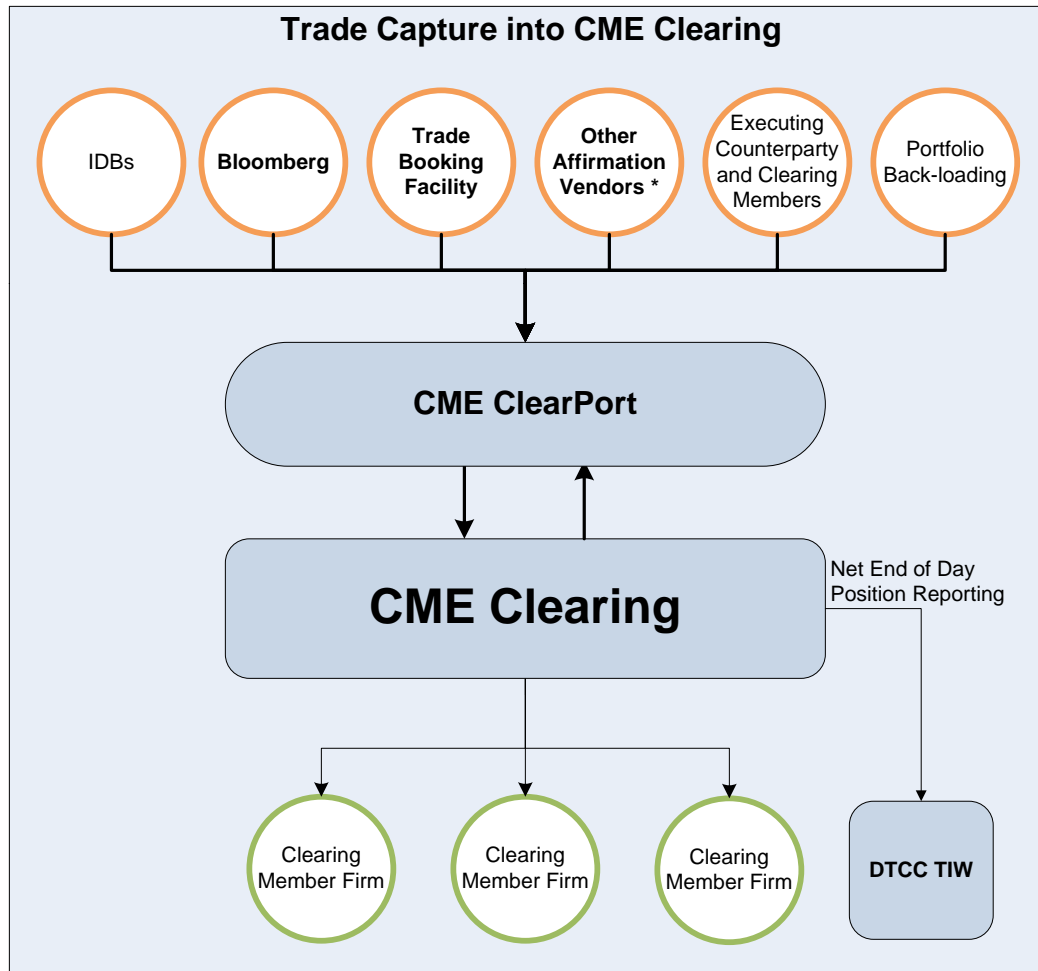


Multi-factor Margin Regime *Sound, transparent and replicable to efficiently and transparently assess risk*

- ✓ Addresses seven risk factors including the overall risk of credit market, portfolio risk, idiosyncratic risk, liquidity risk and basis risk
- ✓ Forecasts are presented as ranges with confidence intervals rather than as point estimates
- ✓ Isolates an asset's sensitivities to each risk factor
- ✓ ***Method is open, stable, and replicable***

Benefits of CME Group's Cleared OTC CDS Solution

Clearing CDS trades real-time throughout the day, every day providing immediate cleared trade confirmation, significantly reducing the credit exposure between bi-lateral parties



- Negotiate, execute, and submit trades through multiple venues to CME Clearing
- Straight through processing and T+0 confirmation
- Full life cycle trade management by CME Clearing
- Back-loading of legacy bilateral trades to CME Clearing
- More than 100 years of experience in clearing, settlement and risk management

Initial Product Scope

CME Group's Cleared OTC CDS contracts are designed to mirror and be economically equivalent to bilateral OTC contracts:

- Consistent with ISDA definitions and adhere to ISDA determinations
- Eligible for participation in ISDA auctions
- Standardized fixed coupons, as defined by ISDA

Initial Products include:

- CDX IG, HVOL, and HY Indices
 - ✓ Series 8 and higher
 - ✓ 3, 5, 7, and 10 year tenors
- iTraxx Europe, HVOL, and XO
 - ✓ Series 7 and higher
 - ✓ 3, 5, 7 and 10 year tenors
- iTraxx Financial Senior and Financial Subordinate
 - ✓ Series 7 and higher
 - ✓ 5 and 10 year tenors
- Single Name constituents of the CDX and iTraxx indices, plus select liquid single names
 - ✓ IMM maturity dates up to 10 years

Cleared OTC CDS: Overview of Contract Comparison

	Bilateral Contracts Today	CME Group Cleared Contracts
Credit event determination	<ul style="list-style-type: none"> • ISDA will hardwire credit event determinations 	<ul style="list-style-type: none"> • Will adhere to ISDA determinations
Cash settlement for non-Restructuring credit events	<ul style="list-style-type: none"> • Cash settlement hardwired based on ISDA auction 	<ul style="list-style-type: none"> • Will adhere to ISDA cash settlement processes
Physical settlement for non-restructuring credit events	<ul style="list-style-type: none"> • ISDA auction protocol hardwired into contracts • Participants will have right to take part in the auction 	<ul style="list-style-type: none"> • Physical settlement is an option through the ISDA auction
Succession event determination	<ul style="list-style-type: none"> • ISDA will hardwire Succession event determinations 	<ul style="list-style-type: none"> • Will adhere to ISDA determinations
Calculation agent	<ul style="list-style-type: none"> • Bilaterally agreed upon 	<ul style="list-style-type: none"> • CME Clearing
Restructuring	<ul style="list-style-type: none"> • ISDA DC determines whether restructuring has occurred • ISDA DC determines for which maturity buckets to hold an auction 	<ul style="list-style-type: none"> • Will adhere to ISDA DC determinations

Cleared OTC CDS Solution Overview

US Regulatory/Industry Approval Status:

- Petitioned CFTC for an order permitting customer funds used to margin, secure or guarantee CDS to be held in CEA Section 4d segregated customer accounts
 - Pending the 4d order, customer funds will be held in separate accounts in accordance with CFTC Reg 30.7
- Received special exemption from SEC to clear CDS through CME Clearing
- Licensed Markit credit default swap indices and Markit RED identifiers
- Licensed ISDA credit definitions, and will follow ISDA declaration/settlement processes
- Will clear CDS using combined guaranty fund
- Completed Fed, SEC and CFTC risk management reviews
- Received all necessary approvals to clear single name CDS on Day 1

European Clearing House

European Regulatory / Industry Approval Status

- Designated Recognised Overseas Clearing House (ROCH) today; working with FSA to apply for Recognised Clearing House (RCH) status
- CEO hired and building team
- Pending approval, CME RCH intending to clear CDS initially
- Once clearing CDS, will seek permission to clear additional asset classes through CME RCH with a combined default fund across products

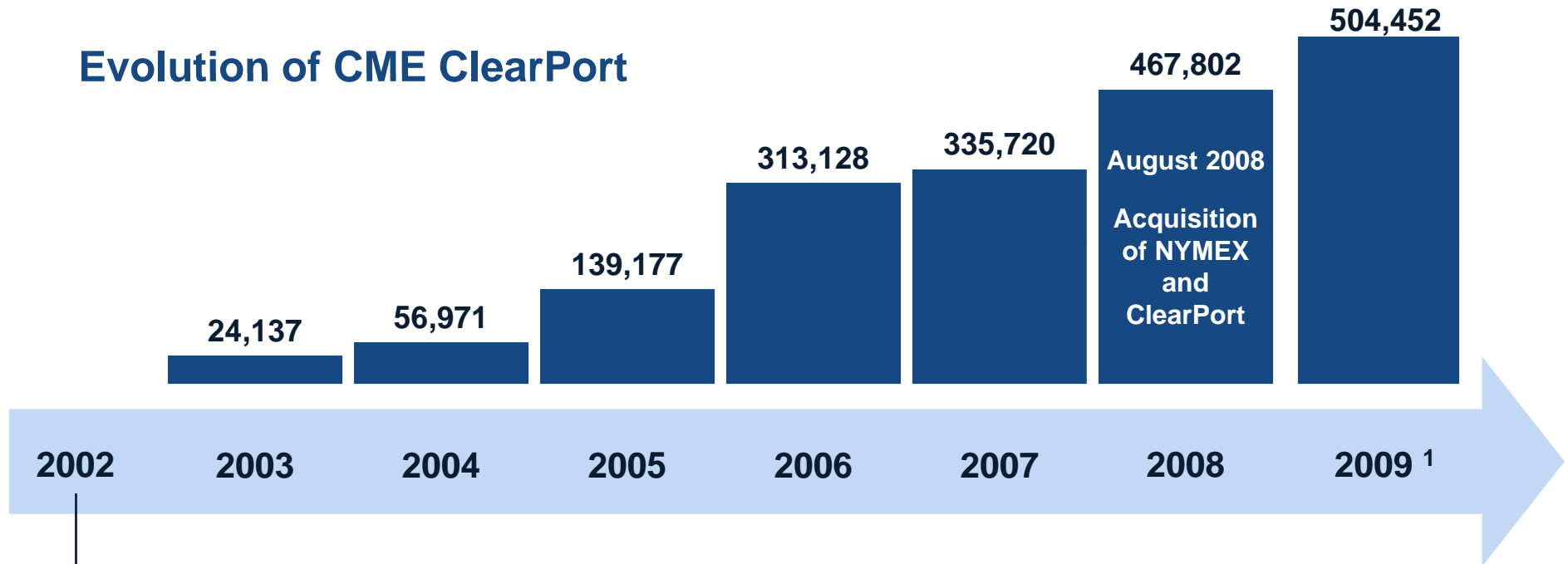
CLEARED OTC CDS
***BENEFITS OF CENTRAL COUNTERPARTY
CLEARING***

Role of A Central Counterparty

- **Improve overall systemic security of capital markets**
- **Present neutral, regulated venue offering information and access to all issuers, investors and intermediaries**
- **Significantly mitigate counterparty risk**

Market Participants Seek Safety and Soundness of Regulated, Centrally Cleared Markets

Evolution of CME ClearPort



- December 2001, Enron bankruptcy
- May 2002, ClearPort launched

(Bar chart illustrates average daily volume in round turns)

¹ 2009 YTD ADV through October 1, 2009

CME ClearPort: Expanding Across Asset Classes

Flexible clearing services open to all OTC market participants

- More than energy
- Independent of execution
- Security from significant mitigation of counterparty risk
- Certainty of independent, neutral settlement prices
- Efficiencies for capital and operations
- Complementary to existing OTC trade capture systems
- 100+ years of risk management experience and financial safeguards



CLEARED OTC CDS
NEXT STEPS

Next Steps and Contact Us

Getting Started

- **Establish a relationship with a participating CME CDS Clearing Member**
 - Discuss and agree on trade capture options and trade flow
 - Complete required Clearing Member Customer Documentation
 - Work with Clearing Member throughout testing cycles
 - Begin clearing trades

For more information, please contact:

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Visit www.cmegroup.com/cds to learn more

CME Group's Cleared OTC CDS Solution

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