

NATIONAL USER GROUP ITALY

Triparty collateral management services interaction

In today's markets, collateral is an essential component of liquidity risk management. At the same time the need to limit credit risk exposure influences a secured Money Market choice. The banks have the possibility to efficiently allocate, use and invest their collateral through one of the market's leading technological platforms for collateral management: Triparty Repo Service. The advantages for this market could be the re-use possibility, other than further secure Money Market transactions, within the framework of ECB open market operations or intraday pledge (such as the German financial community).

In a Triparty collateral management transaction, CCBM2 could act as a unique entry point to use a single pool of securities to be collateralised by Eurosystem refinancing operations via National Central Bank. The introduction of some innovations, which optimise the use of collateral to make liquidity available, must be one of the main objectives of the Eurosystem. CCBM2 could lead the Eurosystem to reach these objectives.

This initiative could be implemented with a strict cooperation among Eurosystem and CSD's (Triparty agents) to define the integrated process of allocating, delivering and servicing collateral. In this regard, we think that the final decision about the interaction model(s) with CCBM2 (standard and/or interfaced) is to be taken by the Eurosystem, which should be in charge of evaluating the right perimeter of outsourcing. In this respect, the availability of both interaction models could help additional CSDs develop Triparty services. Collateral deriving from different market segments should be treated with a high level of automation in a whole context of substitutions, margining and eligibility criteria, in order to reduce operational risks impacts and to obtain an easier access to ECB operations than current CCBM, with release of credit in T2 on a real time basis. The access of banks to Triparty services provided by foreign (I)CSDs could be based on a "CCBM-like approach", i.e. allowing the direct or custodian-based transfer of collateral by the counterparty to a Correspondent NCB.

Foreign collateral usage

As for T2S recommendations, CCBM2 must foresee a full participation of National Central Banks, at an European Economic Area level, in order to obtain all advantages in pooling collateral in a single location for Eurosystem credit operations.

In addition, we strongly support the possibility to accept foreign collateral, for instance in emergency situations, or to use CCBM2 to deliver eligible euro collateral with the domestic Central Bank to obtain credit in other currencies outside the euro area. Current tender procedures for provision of dollars to Eurosystem counterparties, under the Term Auction Facility, could be included in this process, to facilitate the collateral transfer in due time and to reduce operational risks impacts.

International banks need to manage their collateral in different currencies to avoid possible extraordinary local liquidity needs. CCBM2 could be instrumental in developing new techniques to make the release of intraday and overnight credit easier.

In a financial markets integration context, the use of collateral with different currencies in one country to obtain liquidity in another is essential to mitigate potential liquidity risks in different markets and to strengthen financial stability. In general, accepting foreign collateral held abroad might increase the flexibility of banks when it comes to receiving credit and reducing its overall collateral cost. Moreover, increasing the collateral basket could introduce additional sources of liquidity in a local payment system in the respect of the Monetary Policy responsibility of each Central Bank.

CCBM2 could manage all aspects related to collateral delivery, including cut-offs for National Central Banks' credit access. In the Eurosystem the use of collateral is currently limited to euro denominated collateral issued in the EEA but held in the euro area. We emphasise that CCBM2 could consider euro denominated collateral or other currencies held in the EEA

The emergency use of cross-border collateral has the potential to support financial stability during a local crisis. At the same time, with CCBM2 market participants could have a larger pool of collateral to which to resort in case of an emergency situation.

The CPSS report on Cross Border collateral arrangements describes possible generic cross border arrangements, each of which requires actions by central banks. In this context the current CCBM might be implemented and applied for normal or emergency situations. CCBM2 could represent the natural evolution in terms of Collateral Management System.

Credit Claims module

With the introduction of a “single list” of eligible collateral with common criteria for the whole Eurosystem, credit claims (i.e. bank loans) eligibility has been very important to manage liquidity through access to ECB credit operations.

Even though credit claims are more complex than marketable securities both in legal and in administrative terms, their mobilization by market participants as collateral in credit operations with the National Central Bank will allow a fast and decentralised access to liquidity instruments. The CCBM2 credit claims module would reinforce harmonisation concepts in terms of mobilisation processes and legal aspects to facilitate their use in markets transactions. Moreover, the conditions for the cross-border use of credit claims in relation to progressive international extension of banking presence will increase the expectation from banks that the cross-border use of credit claims in credit operations could accelerate the CCBM2 start-up.

We recognise that an efficient use of credit claims at a European level requires some degree of legal harmonisation. CCBM2 can provide harmonised procedure for the operational use of credit claims but not for the legal transfer, which on the other hand should be analysed against the backdrop of a complex Eurozone harmonisation processes.

Finally, though knowing the potential synergies among CCBM2, T2 and T2S that could be reached through the use of a single technical platform for all these projects, we think that the CCBM2 project could be developed separately before the T2S launch. The final decision should consider a profitable business case to avoid possible impacts on end users. Moreover, as stated above, given the absolute need for cross border mobilisation of credit claims, market participants are interested in an early implementation of the CCBM2 credit claims module.

CCBM2: liquidity management enhancement

The Target2 platform, among other comparable high value payment systems, is the one that offers the most comprehensive and efficient optimization and liquidity management tools. From a collateral management point of view we think that CCBM2 could support T2 system with two important liquidity management instruments (credit freezing facilities):

- Collateral saver in the event of T2 Contingency Module activation (fresh collateral delivery);
- Collateral saver for CLS system;

CM activation

The sources of liquidity for the Contingency Module represents a possible problem for the banks in terms of collateral provision. As stated in the UDFS, the Contingency Module will start with a zero balance. The processing of contingency payments will therefore require the activation of additional collateral. To do this, CCBM2 could play a double role:

- A collateral saver role to preserve eligible assets. In this context we think that credit claims collateral has to be considered good for delivery;
- An automatic operative bridge to connect to the Contingency Module.

CLS system contingency procedures

CCBM2 could also play the role of collateral saver, useful for CLS early settlement in case of technical problems faced by a participant or CLS system liquidity needs. This collateral should be pledged, through National Central Banks either to settle via

TARGET2 into CLS system euro legs on behalf of the “failing” participant, or to help participants to make contingency pay-ins via TARGET2 in case of CLS system liquidity needs . We think that these functionalities could be developed by the Eurosystem defining the correct activities to perform.

The Monitoring

In order to generate efficiency, we reinforce, as for T2S project, the expectation of a single interface. Key features and operational procedures will need to be standardized allowing end users to access a single interface for monitoring their activities in CCBM2, T2 and T2S. This interface should be the ICM. These needs are directly referred to the possible critical intraday movement of collateral to facilitate the access of liquidity by market participants and to optimize Treasury liquidity management.

We think that the network interconnection should use the same infrastructure adopted in SSP offering both A2A and UtoA mode to interact with all CCBM2 modules. The web architecture should provide several advantages for both accesses in terms of functionalities and security aspects to allow the banks, in case of AtoA usage, to collect needed information.

Additional comments by Monte Titoli

Chapter 1.4 Interfacing with CCBM2

In addition to the SWIFT connectivity, CCBM2 should offer dedicated connections with CSDs. This option will allow CSDs to reduce the transport cost of the messages, which they would sustain for the most.

Chapter 3,4 and 6

Monte Titoli is ready to support CCBM2, should it start before T2S. In this case Monte Titoli would expect that CCBM2 develops its communication protocols regarding custody, matching and settlement services according to the technical rules defined by CSDs; hence, Monte Titoli would provide all the information that may be required by the Eurosystem.

As for the auto-collateralisation facility, if CCBM2 starts before T2S Monte Titoli would update the communication procedure in agreement with Banca d’Italia when necessary.

Monte Titoli is available to develop a Triparty collateral service only if the service is strongly supported by the Italian banking community.

Chapter 6 static data

In order to prevent settlement errors, Monte Titoli suggests that CCBM2 carries out a daily realignment of the static data of eligible collateral with the list of securities managed by each CSD.

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