ICMA International Capital Market Association

ERC Annual General Meeting

Paris, 11 March 2013

Welcome remarks

- **Martin Scheck**
  Chief Executive, International Capital Market Association (ICMA)

Opening remarks and an overview of recent developments

- **Godfried De Vidts**

  Chairman, European Repo Council

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Recent Developments 1.

- Increased regulatory focus on repo markets
- Positive: collateral in demand (EMIR / Dodd-Frank)
- Less positive: danger of overregulation / unintended consequences
- Basel moved interbank financing from unsecured to secured
- Regulatory trap: 1st risk remains counterparty not collateral !
- Eurepo no longer suitable
- Market initiatives like RepoFunds Rate welcome by ERC
- ECB repo facility

Recent Developments 2.

- Use of centralised clearing embedded in repo – but worrying signs of overcollateralisation by CCPs
- Cost of clearing & settlement remains too high
- Appeal to authorities to step up actions (see January article)
- European Post Trade Group (EPTG) shows no real progress. Need for more concrete initiatives / breaking down of national barriers
- Keynote speech Mr. Benoît Cœuré, ECB Governing council
- ECB Cogesi workshops - Keynote speech D. Russo
- Public Sector Industry Forum (PSIF) meeting with ERC delegation – FTT
- FSB Shadow Banking WG with ERC delegation

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Speech by Mr. Benoît Cœuré - Luxembourg 16th Jan 2013

The resilience and proper functioning of market infrastructures is of paramount importance to ensure well-functioning money markets. Public authorities and central banks have both an interest and an obligation to ensure that market infrastructures have a high level of security and operational performance. The market infrastructures in the euro area are performing well in this respect and, as we have heard, there are a number of initiatives under way to further enhance this (in particular as regards the collateralisation processes).

I would, however, urge industry representatives to further pursue the triparty interoperability project, and seek to find ways to address the issues which have recently appeared. In particular, where these issues are not going to be addressed by T2S, I would encourage the industry to find a solution now. It is of great importance that collateral can flow freely, regardless of its location.

FTT

- Unsecured lending non-existent for interbank purposes
- Secured (repo) lending favoured by Basel
- Central banks provide liquidity to interbank market, but should not be the counterparty to every bank all the time

- Wholesale markets are intermediaries to real economy
  - Distribution of liquidity across sell-side (wholesale markets)…
  - …provide buy-side with necessary funding (DMOs & real economy)

- FTT of 0.10% counterproductive as repo markets should allow an efficient distribution of collateral for various regulatory purposes
- All collateral movement will be subject to the FTT, unsustainable cost on tri-party
- Wider spreads will lead to less liquid bonds
- Need for internal discussions at Ministries of Finance departments as FTT will increase cost of funding of government debt

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FSB Workshop - Trade Repository

The ERC supports the move towards improved transparency

- The ERC has long promoted transparency through its semi-annual survey
- Haircuts can create a perception of the credit quality of a counterparty; and thus in certain situations can be highly sensitive – there is, therefore, an important question regarding the confidentiality of any reporting

  Hence, the ERC recommend a public sector approach to enhance, aggregate and merge current surveys – which should be advanced as a matter of priority

The ERC is already actively engaged in on-going work with the ECB/BoE that will aggregate numbers for European markets

- This work will serve as a sound basis from which to further develop understanding, allowing informed specification of incremental transparency requirements; and calibration of any, appropriate, specific regulations
- Avoid duplication (ESRB, EBA/ESMA, etc.) as costs may outweigh benefits
- Simple collection of (daily) transaction data is not seen as helpful to regulators; whereas gathering market intelligence on a regular basis is more likely to provide appropriate colour on trends in the market combined with enhanced survey information
- A mixed approach may be appropriate, e.g. regularly gathering data from large firms, periodically supplemented by broader market surveys

FSB Workshop: Mandatory Minimum Haircuts

The ERC urges caution in the case for mandatory minimum haircuts

- Not appropriate for **interbank repos**? (i.e. those between regulated financial firms), whether CCP cleared or bilateral > essentially financing transactions
  - **Regulated banks** are already subject to capital charges, liquidity regulations etc. so the ERC considers that the methods to mandatory haircuts are unnecessary and could be counterproductive to market liquidity (i.e. don't accept either option 1 or 2 for interbank repo transactions)
- **For sovereign bond trading**, liquidity may be curtailed if the repo market is adversely affected – if there is to be a minimum haircut regime it should focus on illiquid securities rather than impacting on high quality government bonds (and similar)
- Haircuts are **customised in response to several variables** and can thus fluctuate responsive to changes in the applicable risk inputs
  - It is important to remember that the primary risk is the counterparty, whose creditworthiness must be suitably assessed – collateral serves to mitigate credit losses and fluctuation in its realisable value is a secondary risk
  - If minimum haircuts are applied where higher haircuts may be more appropriate to manage risk, there is also a **risk that the market defers risk management to the regulators**.

Application of a minimum standard methodology for repo business executed outside the regulated interbank sector may have a place but should not be over prescriptive so as to allow firms to manage counterparty and collateral risk accordingly

FSB Workshop: Repo Margin Standards

Revised ERC Repo Margining Best Practices – published H1 2012

- Revision headlines:
  - Margin to be based on actual rather than assumed settlement (portfolio value based on call date -1 end of day)
  - Ensure mutual documented agreement of elective GMRA provisions
  - Guidelines on minimum transfer amounts and interest
  - Avoid netting of consecutive days margin movements and bad practice of trading out of a margin call
  - Migration towards a call date +0 settlement of margin
- Current status:
  - Mixed state of readiness and adoption across the market
  - Technology / budgetary dependencies

ESMA’s first risk report on EU securities markets

ESMA’s 2012 report focuses on:

- **Collateral concerns in financial markets**: the collapse of unsecured markets during the financial crisis, as well as regulatory initiatives, have led market participants to rely increasingly on collateral as a means of mitigating counterparty risk, stimulating the demand for collateral. Additional demand for collateral will exceed the additional supply of collateral in 2013-2014, making collateral comparatively scarcer.
- **Hedge funds and prime brokers**: financial intermediation provided by hedge funds and prime brokers may be vulnerable to any negative impacts on the price of assets pledged as collateral, which may lead to scarcer collateral, reducing liquidity and ultimately hamper repo financing.

Avoiding collateral damage – on-going Eurosystem developments to underpin the efficiency and effectiveness of secured financing

- **Daniela Russo**

  Director-General of Payments and Market Infrastructure, European Central Bank

Table of Contents
What are the issues at stake?

- Facilitating collateral delivery and mobilisation: why?
- Facilitating collateral delivery and mobilisation: how?
  - increase transparency
  - increase liquidity
  - increase flexibility/efficiency

Facilitating collateral delivery: why?

Increasing demand for collateralised transactions due among other issues to:

- Regulatory requirements: affecting both quality and quantity
- Shrinking uncollateralised money market
- Address pro-cyclicality.

Need to **make collateral available where needed** and not where stored due among other issues to;

- Different collateral requirements
- Increasing internationalisation/globalisation
- Potential collateral-based interdependencies

Facilitating collateral delivery: how?

Three main streams of work to strengthen collateralised markets, and repo market in particular:

- Increasing transparency
- Increasing liquidity
- Increasing flexibility/efficiency

Strengthening the [EU] repo market

Increasing transparency of the market:

- Need for mandatory reporting requirements also for securities transactions and not only for derivatives
- Scope of the initiative
  - repo versus other similar transactions
  - geographical scope (EU versus global)
- Adequate infrastructure to support it
  - data warehouse(s) – aggregator
- Role of public authorities

Strengthening the [EU] repo market

Increase liquidity of the market (I):

Creation of the “virtual” single pool of collateral.

Three initiatives of the Eurosystem:

- Interoperability amongst the Eurosystem and (I)CSDs collateral pools (2014)
- Abolition of repatriation requirements (2014)
- T2-S will provide a single platform for settlement in central bank money

Strengthening the [EU] repo market

Increasing liquidity of the market (II)

A challenge for the market: improve interoperability of triparty facilities

- Improve the bridge – Euroclear - Clearstream
- Quickly integrate new providers (e.g. BONY)
- Improve interoperability CSDs – CCPs (focus on removing access barriers) where this is a condition for full interoperability of CSDs

Strengthening the [EU] repo market

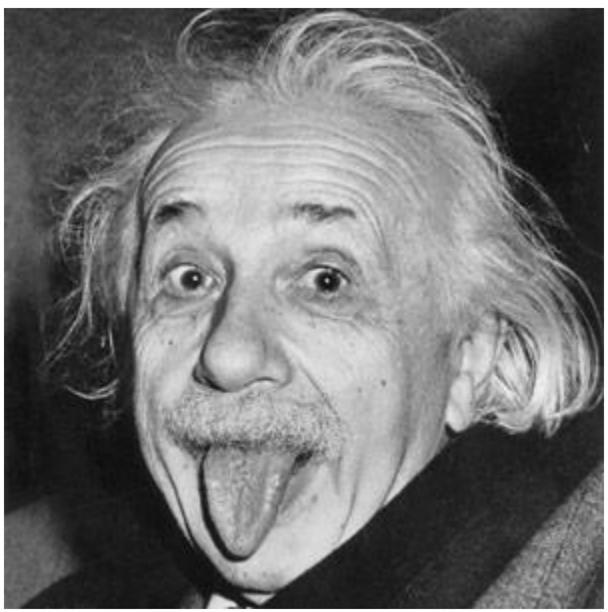
Increase flexibility/efficiency of the market:

- Remove infrastructure barriers preventing the extension of the operating hours of the repo market;
- Increase the assets accepted (secondary market for credit claims should remain an objective even if with less priority)
- Promote and facilitate use of CCPs
- Harmonisation efforts (e.g. settlement cycles)

Conclusion

A lot of important actions in progress:

… but still a lot to do. Following…



"We must **find** the way" [to urgently address the outstanding issues] …

"or …

we have to **make** (a new) one!"

Elections to the European Repo Committee

1. **Simon Kipping,** Bank of America Merrill Lynch, London
2. **Herminio Crespo Urena,** BANKIA, S.A., Valencia
3. **Eugene McGrory,** BNP Paribas, London
4. **Stephen Malekian,** Barclays Capital Securities Limited, London
5. **Grigorios Markouizos,** Citigroup Global Markets Limited, London
6. **Andreas Biewald,** Commerzbank AG, Frankfurt
7. **Luis Soutullo Esperon,** Cecabank, S.A., Madrid
8. **Romain Dumas,** Credit Suisse Securities (Europe) Limited, London
9. **Tony Baldwin,** Daiwa Capital Markets Europe Limited, London
10. **Ronan Rowley,** Deutsche Bank AG, London
11. **Olly Benkert,** Goldman Sachs International, London
12. **Jean-Michel Meyer,** HSBC Bank plc, London
13. **Godfried De Vidts,** ICAP Securities Ltd, London
14. **Andrea Masciovecchio,** Intesa Sanpaolo S.p.A, Milan
15. **Stefano Bellani,** J.P. Morgan Securities plc, London
16. **Ed McAleer,** Morgan Stanley & Co International plc, London
17. **Ulf Bacher,** Newedge Group SA, Paris
18. **Michel Semaan,** Nomura International plc, London
19. **Sylvain Bojic,** Société Générale, Paris
20. **Guido Stroemer,** UBS AG, London
21. **Eduard Cia,** UniCredit Bank AG, Munich

Update on triparty settlement interoperability between the ICSDs and Collateral Management Systems

- **Godfried De Vidts**

  Chairman, European Repo Council

The European credit claims project – an update

- **Philippe Mongars, Deputy Director for Market Operations Directorate, Banque de France**
  Will outline the progress of the Banque de France's project regarding the collateralisation of credit claims.

- **Lisa Cleary, Director, Associate Counsel, International Capital Market Association**
  Will provide an update on the ERC's loan repo project

- **Panel discussion:**

Moderator:	Godfried De Vidts, Chairman, European Repo Council
Panellist:	Jean-Michel Meyer, Managing Director, Global Head of Repo, HSBC Bank plc
Panellist:	Olly Benkert, Managing Director, Goldman Sachs International
Panellist:	Grigorios Markouizos, Global Finance Desk Head, Citigroup Global Markets Limited

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Repo and liquidity management

- **Andreas Biewald**

  Managing Director, Head of Secured and Unsecured Funding, Treasury Department, Commerzbank

COMMERZBANK

Simplified model

High quality liquid assets

- Level 1 assets (unlimited)
  - Level 1 assets
- Level 2 assets (up to 40% of stock)
  - Level 2A assets
  - NEW: Level 2B assets (up to 15% of stock)

LEVEL 1 Assets

PRIMARILY

- Cash & Central bank reserves
  HC 0%
- Sovereigns a. o. assigned a 0% risk-weight under the Basel II Standardised Approach
  HC 0%

LEVEL 2A Assets

PRIMARLY

- Sovereigns a. o. assigned a 20% risk-weight under the Basel II Standardised Approach
  HC 15%
- Corporate bonds and covered bonds rated AA- or higher
  HC 15%

LEVEL 2B Assets

PRIMARILY

- Corp bonds rated BBB- or higher
  HC 50%
- Certain MBS rated AA or higher
  HC 25%
- Certain equities
  HC 50%

Update on roadmap to CRD IV

Last Update: 05.03.2013

min.6 months

27/02/13

EU agrees upon Basle III deal - in principal.

Outcome of the trilogues with the European Parliament, the Council and the Commission

until 30/06/2013

Publication of CRD IV / CRR by EU

01/01/2014

CRD4 transposed into national legislation

Starting date of application for CRR (capital requirement regulation- focus on technical standards)

01/01/2015

LCR becomes binding

graduated phase-in of liquidity coverage requirement (LCR):
2015 - 60%,
2016 - 75%
2017 - 85%
2018 - 100%

Repo FAQs

- **Richard Comotto**

  Senior Visiting Fellow, ICMA Centre at Reading University

Understanding Repo and the Repo Market

1. What is a repo?
2. How is repo used?
3. Why is the repo market so important and why has the use of repo grown so rapidly?
4. How big is the repo market?
5. Who are the main users of the repo market?
6. What types of asset are used as collateral in the repo market?
7. What are the typical maturities of repos?
8. What is the difference between a repurchase agreement and a sell/buy-back?
9. Is repo in Europe the same as repo in the US?
10. What is 'rehypothecation' of collateral?
11. What is general collateral (GC) repo?
12. What is a 'special' in the repo market?
13. What is an open repo?
14. What is the difference between repo and securities lending?

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How Repos are Managed

15. Is repo riskless?
16. Does repo encourage lending to risky counterparties?
17. Who regulates the repo market?
18. Why is it important to document repo?
19. What is the GMRA?
20. How do repo parties ensure they have enough collateral?
21. What is a haircut?
22. Who is entitled to receive coupon or dividend payments on a security being used as collateral in a repo?
23. Who can exercise the voting rights on equity being used as collateral in a repo?
24. What is tri-party repo?
25. What happens if a party fails to deliver collateral in a repo?
26. What happens to repo transactions in a default?
27. What does a CCP do? What are the pros and cons?

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Topical Issues

28. What is ‘short selling’ and what is the role of repo?
29. Do repos allow for infinite leverage?
30. Do haircuts/margins exacerbate pro-cyclicality?
31. Do banks that lend through repo receive preferential treatment over other creditors?
32. Does repo ‘encumber’ a borrower’s assets?
33. Is repo a source of unstable short-term funding?
34. Was a ‘run on repo’ the cause of the financial crisis in 2007?
35. Is repo a type of ‘shadow banking’?
36. Is the repo market opaque?
37. Is repo used to remove assets from the balance sheet?
38. Could a repo rate index replace LIBOR or EURIBOR?

FAQs on the ICMA website

You can access the FAQs on the ICMA website at the link below:

http://icmagroup.org/Regulatory-Policy-and-Market-Practice/short-term-markets/Repo-Markets/frequently-asked-questions-on-repo/

ERC Operations Group Update

- **Nicholas Hamilton**
  Co-Chair, ERC Operations Group
- **Tony Platt**
  Co-Chair, ERC Operations Group

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ERC Ops Group: Agenda

- Affirmation Working Group
- T2S Focus Group
- Monte Titoli Working Group
- Consistent Fails Approach Working Group

Affirmation Working Group

Working group objectives:

- Encourage targeted community growth in affirmation building on current and new solutions to market participants
- Focus on low automated clients & counterparties to reduce risk and effort in processing
- Partner with external groups and forums to message best practice and benefits of automated solutions
- Encourage consistency of products coming to market against published best practices

2012 Deliveries:

- All key market vendors engaged to feedback on functional compliance with recommended best practice attributes and processes
- Regular industry and forum engagement – “spreading the word”
- Replay of affirmation survey to refresh on post trade actions from ERC firms

Affirmation Working Group: ERC OPS 2012 Survey Highlights

2012 vs. 2013

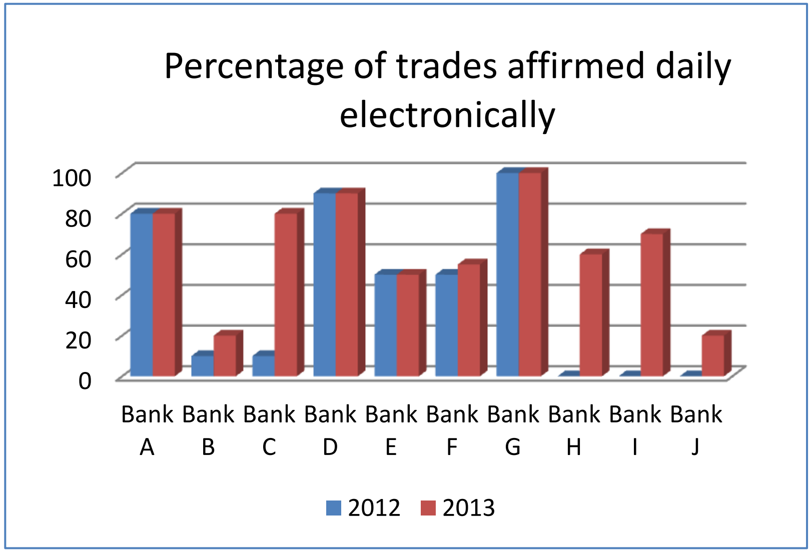
- Higher number of term trades which has had increased trade level affirmation & post trade lifecycle efforts
- All ERC working group firms have explored automated solutions
- 70% of firms with automated solutions have increased client on-boarding
- All vendor solutions have anchored core functionality in ERC best practice statement
- New vendor solutions are coming to market – targeting buy side and linking cross asset class
- Supported solutions provide the following functionality
  - Matching and settlement instruction reporting bringing affirmation and settlement processing together
  - Full service portfolio compare, settlement matching, re-pricing, billing

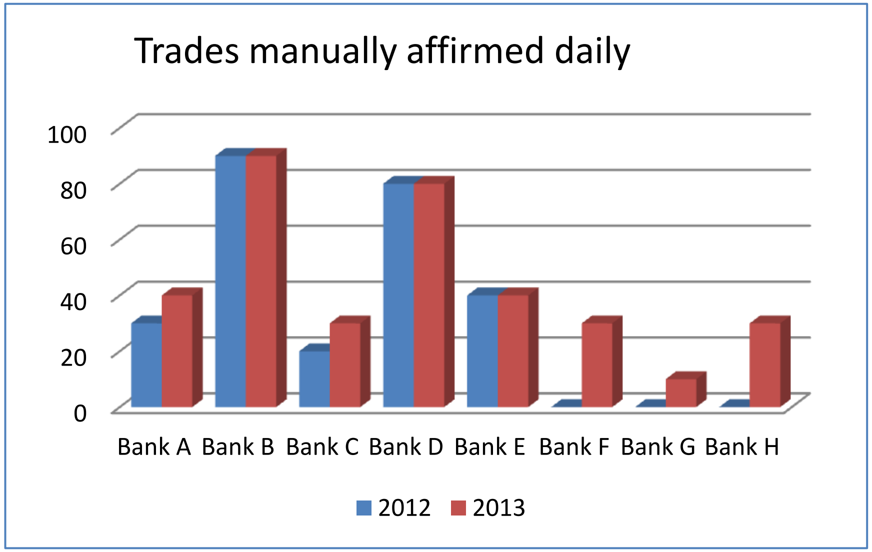
Challenges

- Multiple solutions & vendors prompting proliferation of pipes and spend in applications
- Establishing consistency & continuing to ensure best practice guidance and automation
- Resource and budget - investment spend is tight given regulatory and wholesale infrastructure changes at many firms
- Steady volume increase is creating more manual effort identified in more active phone affirmation.

Affirmation Working Group: Addendum – "Encouraging signs"

- 2nd annual survey
- 13 working group members & participants in survey population
- Barclays, BNP, BTEC, Citi, Danske, DB, GS, MS, JPM , RBC RBS, SG, UBS
- Encouraging signs (only 2 of the 20 slides shown below)
  - Most working group firms have increased amount of electronic execution and/or affirmation
  - Most firms are supporting manual affirmation to reduce gaps & risks in OTC bookings





Affirmation Working group - Next Steps

- Develop survey addendum for European Repo Council semi annual survey
- Partner with industry and regulatory groups to consider lifecycle management activity in deliveries
- Continue existing engagements with vendor and repo community initiatives for automated solutions for affirmation and lifecycle management
- Publicise groups survey work & best practice standards in industry forums

T2S Focus Group

Inception and workings of focus group to date

- T2S has been a key topic in the ERC Ops WG in 2011. The impact T2S will have on the functioning of the Repo market in Europe is key to understand;
- To analyse this further, a focus group was created comprising subject matter experts from Goldman Sachs, HSBC, JP Morgan, Morgan Stanley and RBS;
- The aim of this focus group is to share its knowledge and its research with the Repo community
- This research may help promote more debate in the community and to contribute ideas to the future of T2S;
- The first focus group meeting covered broad topic areas in T2S in a lively debate. Areas covered
    - How will T2S meet its aims of reducing cost of settlement, increase collateral liquidity and reduce "commercial bank money" risk? Are there risks to the community?
    - How will direct versus indirect work in T2S? What are the choices and what are the impacts?
    - How will Triparty work in T2S- particularly in the context of direct and indirect participation?
    - How will blocking/earmarking securities work in T2S? Are there risks?
    - How will using the Repo flag on instructions to T2S work? What benefits are there? Are there any as yet unidentified benefits we should aim for?
- Output was reported back to the ERC Ops WG for steer on the areas of most interest. Three were chosen;
    - How will Triparty work?
    - What does direct versus indirect participation mean for us all: costs, benefits, risks, opportunities
    - How will blocking/earmarking work? Are there risks for the community?

T2S Focus Group

The three areas of focus

Direct v. Indirect Participation

- The impact of T2S on firms who currently act as agent banks/sub custodians is more pronounced.
- These firms will need to understand the connectivity implications so that they can continue (if they choose) to offer agent bank/sub custodian services.
- A deadline to advise the ECB of wishing to be a direct participant is 15th October 2013. It is not known how many participants wish to be direct, but the number is expected to be low.
- Firms who currently use an agent bank/sub custodian can choose between agents/providers at a later date.
- Direct and indirect participation options may drive a reduction in “service providers” due to a CSD’s size offering economy of scale pricing opportunities.

Triparty

- T2S will not in itself deliver a Triparty product. However service providers will be able to offer their own Triparty products within the markets they support, eg CSDs.
- ICSDs will continue to operate their current services, offering access to collateral takers through “as is” Triparty models.
- Those accessing T2S as direct participants will have ability transfer assets to ICSDs for use in ISCD Triparty trades.
- Harmonisation of settlement deadlines through T2S; Interoperability and “Open Inventory Sourcing” should result in greater optimization of collateral and therefore positively impact Triparty.

Blocking & Earmarking

- It is not clear to the focus group why this has been proposed as a feature in T2S. It is not clear how the functionality will work- especially given direct/indirect connections.
- There are concerns that blocking could lead to supply issues: this then negatively impacts the liquidity of collateral in T2S.
- Further, blocking could be more pronounced for tight/illiquid bonds as firms look to facilitate most profitable settlement.
- Blocking/earmarking will need to be intuitive, manageable and scalable so as to prevent assets being "locked in" and creating settlement issues.

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T2S Focus Group

Next steps:

- Third T2S focus group to meet in March 2013
- Actions are with focus group members to expand on the three areas of focus
- The results of these actions will be presented to ERC Ops WG in April/May 2013
- Focus group Chair to continue to find and engage in other industry forums covering T2S; eg BBA NUG; AFME working groups
- Focus group Chair to continue to collate T2S news and share with focus group to determine impact; eg CSDR; repo repository implementation; financial transaction taxes
- Feasibility study underway looking at having an ICMA-hosted “open day” for the industry with keynote speakers, presentations on T2S, expansion on the three areas of focus and panel Q&A

Monte Titoli Working Group

MT Process

- Monte Titoli DvP/RTGS Optimizer:
  - Settlement optimisation/technical netting of unsettled instructions;
  - CCP-cleared and non-cleared repos in RTGS;
  - Non-cleared repos: offset maximum amount;
  - CCP-cleared repos: age-size offset priority – open issue.
- Mini-netting;
- Shaping;
- Penalties

MT Plans

- T2S;
- “ICSD” project

Next steps

Monte Titoli Working Group

Non-cleared repos: offset maximum amount for a given date

» Example. A has 30,000 nominal of security X in its account; B has 10,000. The following trades are queued.

Instructions	Seller → Buyer	Nominal
# 1	A → B	100,000
# 2	B → A	100,000
# 3	B → A	70,000
# 4	B → A	40,000
# 5	B → A	35,000
# 6	B → A	30,000

» The possible offsets are:

- #1 against #2 for 100,000
- #1 against #3 + #4 for 110,000 (drawing 10,000 from B's account)
- #1 against #4 + #5 + #6 for 105,000 (drawing 5,000 from B's account)

» The optimal offset is (2), because it offsets the largest nominal amount.

Monte Titoli Working Group

CCP-cleared repos: age-size offset priority

» Example. A has 10,000 nominal of security X in its account. Today is 10 April 2012. The following trades are queued.

Instructions	Seller → Buyer	Nominal	ISD
# 1	CCP → A	100,000	05/04/2012
# 2	A → CCP	100,000	08/04/2012
# 3	A → CCP	70,000	05/04/2012
# 4	A → CCP	60,000	07/04/2012
# 5	A → CCP	50,000	07/04/2012
# 6	A → CCP	35,000	04/04/2012
# 7	A → CCP	20,000	09/04/2012

NB CCP rule: deliveries-out can only be offset against earlier deliveries-in.

The possible offsets are:

1. #1 against #2 for 100,000
2. #1 against #3 + #7 for 90,000, leaving 10,000 of #1 failed.
3. #1 against #4 + #5 for 110,000 (drawing 10,000 from A's account)

The optimal offset is option #3. #6 is rules out because deliveries due to the CCP can only be offset against deliveries due from the CCP that have later ISD. #6 is then recycled to the RTGS system.

Monte Titoli Working Group

Monte Titoli mini-netting

- Mini-netting is a real-time function to minimise CCP cash balances (optimisation is a batch function that applies to securities);
- Wef 24 September 2012, MT extended the mini-netting process to CCP instructions with different intended settlement dates.

Monte Titoli shaping of ON CCP-cleared repos

- Wef 3 December 2012, spot legs of overnight CCP repos executed on electronic markets & cleared on a CCP are shaped into EUR 5 millions pieces before being routed to RTGS
- All shapes are now the same

Monte Titoli Working Group

Monte Titoli fails penalty calculation

- Currently fails at 16:00 are offset against balances at 18:00;
- Anomaly - instructions after 16:00 to cure fails will reduce balance at 18:00 & increase penalty;
- Change to comparison of fails at 16:00 with balances at 16:00;
- At the last PT-TUG meeting held (11 February), Monte Titoli announced a meeting with market participants to discuss possible changes to the penalty calculation.

Telephone pre-matching

- Said to cause poor settlement performance in the Italian market;
- It affects a small number of trades, but has high impact due to their large value;
- Monte Titoli are seeking to improve the situation by the introduction of a second-layer matching in September 2012 and a hold/release functionality expected in July 2013;
- Italian agent banks are now working on a market practice for the use of the two functionalities with ICMA ERC.

Monte Titoli Working Group

Agenda 27 February meeting:

- Introduction
- Monte Titoli presentation:
  - Work Programme 2013
  - Optimiser
  - Hold & Release functionality
  - Update on T2S
  - System performance and standard operating procedure
- CC&G presentation:
  - Preparing for EMIR
  - CCP for Eurobonds

Next steps:

- Preparations for T2S
- MT to keep the London & international market up to date

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Consistent Fails Approach Working Group

Background

- Market Conventions and GMRA designed for +Ve rate environment.
- Very low/-Ve rates create potential incentive to fail.
- ICMA recommendation of Nov 2004 and GMRA 2011 reduce incentive but do not compensate for party suffering fail.
- By comparison, when US repo rates dropped below 3% leading to systemic failure, TMPG imposed market-wide penalty framework.
- Europe has not seen systemic failure yet but regulatory pressure for settlement discipline persists.

Issues

- Bilateral compensation:
  - Fails on Purchase Date.
  - Fails on Repurchase Date.
  - Reinvestment rate of manufactured payments in sell/buy-backs.
  - Interest on cash margin.
- Floating-rate repo interest payments
- Systemic rate of fails in Europe.

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Consistent Fails Approach Working Group

Proposals for bilateral Repo compensation:

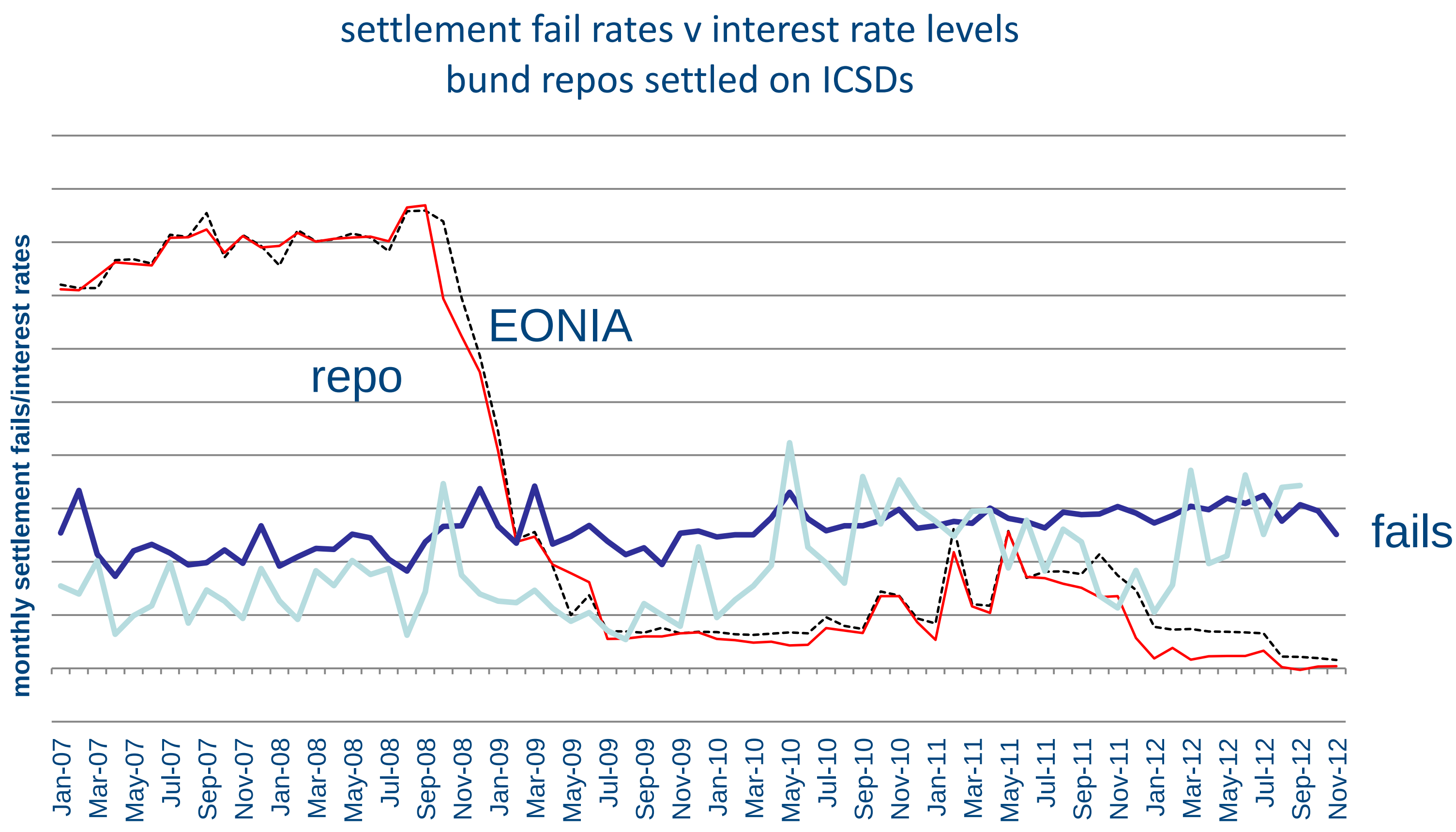
- Compensation = GC repo rate (or proxy) – failed repo rate.
- To be agreed bilaterally, in accordance with a signed protocol.
- Settled as per interest claims.
- Managed within thresholds.
- Advantages:
  - Reflects economic cost of each fail.
  - Works for both +Ve and -Ve rates.
- Challenges:
  - Claims mechanisms.
  - Cash market.
  - CCPs.
  - Consistent approach.
  - Interest on Cash Margin/Floating Rate Repo.

Proposals for Buy/Sell-Back & Cash Margin:

- Redefine the calculation of the reinvestment income on the manufactured payment:

Consistent Fails Approach Working Group

» No evidence of correlation between repo rates & fails in Europe



Legal Update

- **Lisa Cleary**

  Director, Associate Counsel, International Capital Market Association

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European Repo Council
24th European repo market survey conducted in December 2012

- **Richard Comotto**

  Senior Visiting Fellow, ICMA Centre at Reading University

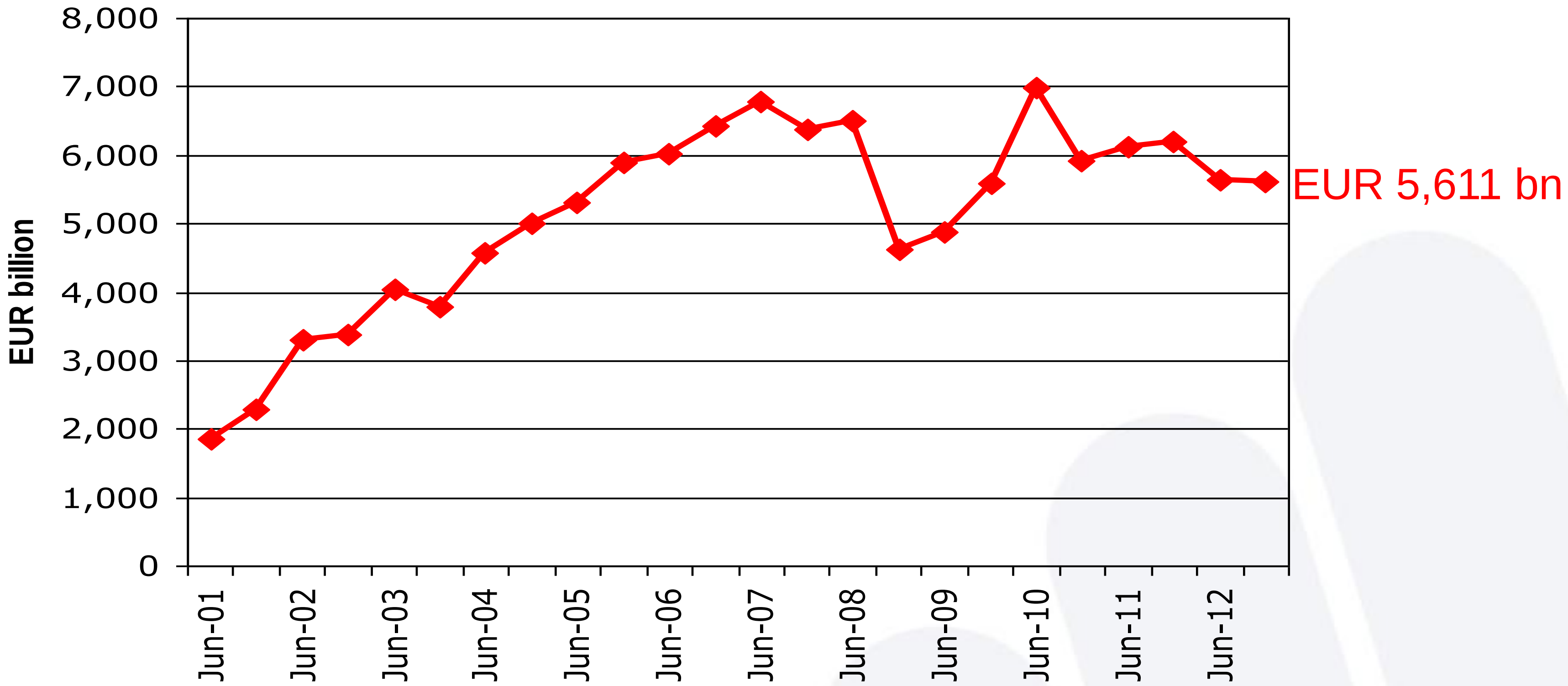
Survey overview

- Outstanding value of contracts at close of business on Wednesday, 12th December 2012
- 71 responses from 67 groups

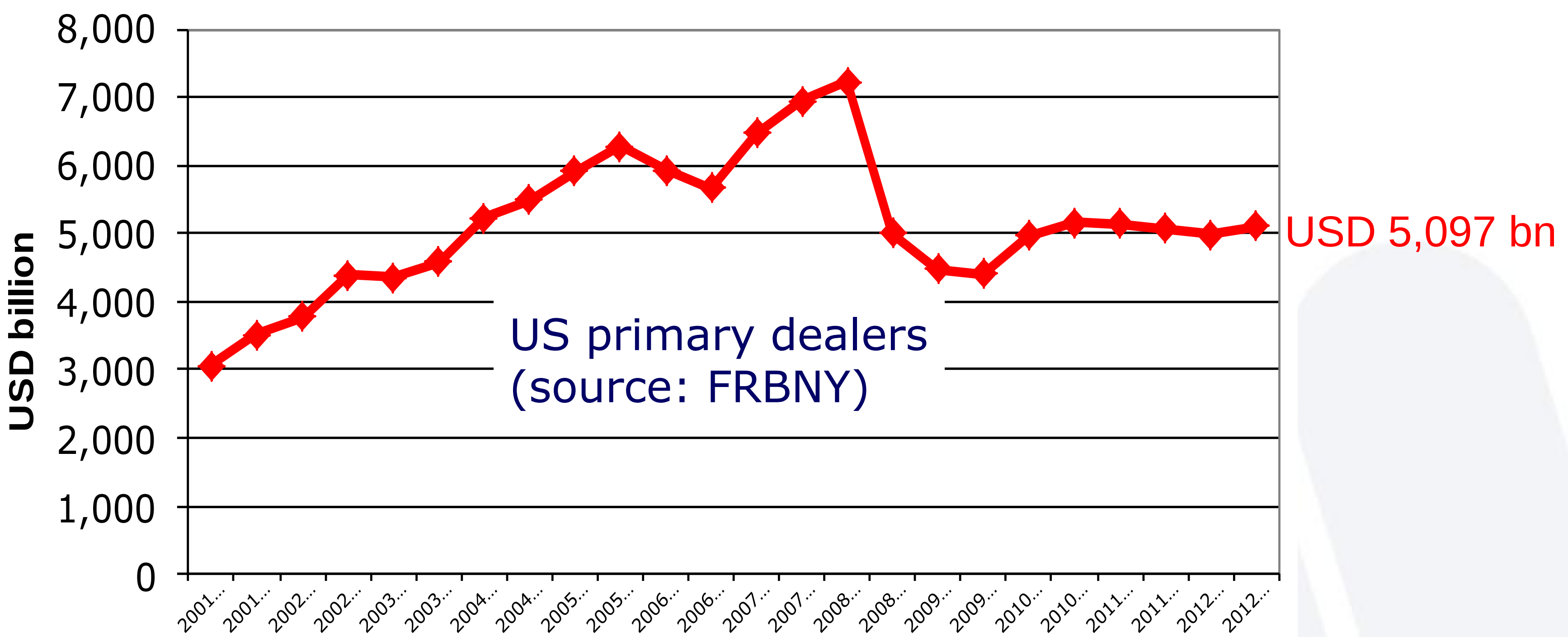
Headline numbers

December 2012	EUR 5,611 billion
June 2012	EUR 5,647 billion
December 2011	EUR 6,204 billion
June 2011	EUR 6,124 billion
December 2010	EUR 5,908 billion
June 2010	EUR 6,979 billion
December 2009	EUR 5,582 billion
June 2009	EUR 4,868 billion
December 2008	EUR 4,633 billion
June 2008	EUR 6,504 billion
December 2007	EUR 6,382 billion
June 2007	EUR 6,775 billion
December 2006	EUR 6,430 billion

Headline numbers



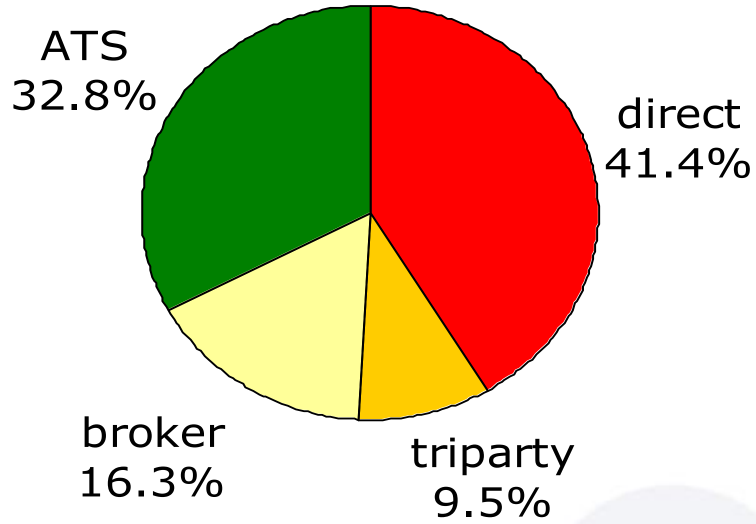
US market


8,000
7,000
6,000
5,000
4,000
3,000
2,000
1,000
0
USD billion
USD 5,097 bn
US primary dealers
(source: FRBNY)
2001…
2001…
2002…
2002…
2003…
2003…
2004…
2004…
2005…
2005…
2006…
2006…
2007…
2007…
2008…
2008…
2009…
2009…
2010…
2010…
2011…
2011…
2012…
2012…

Comparable market growth

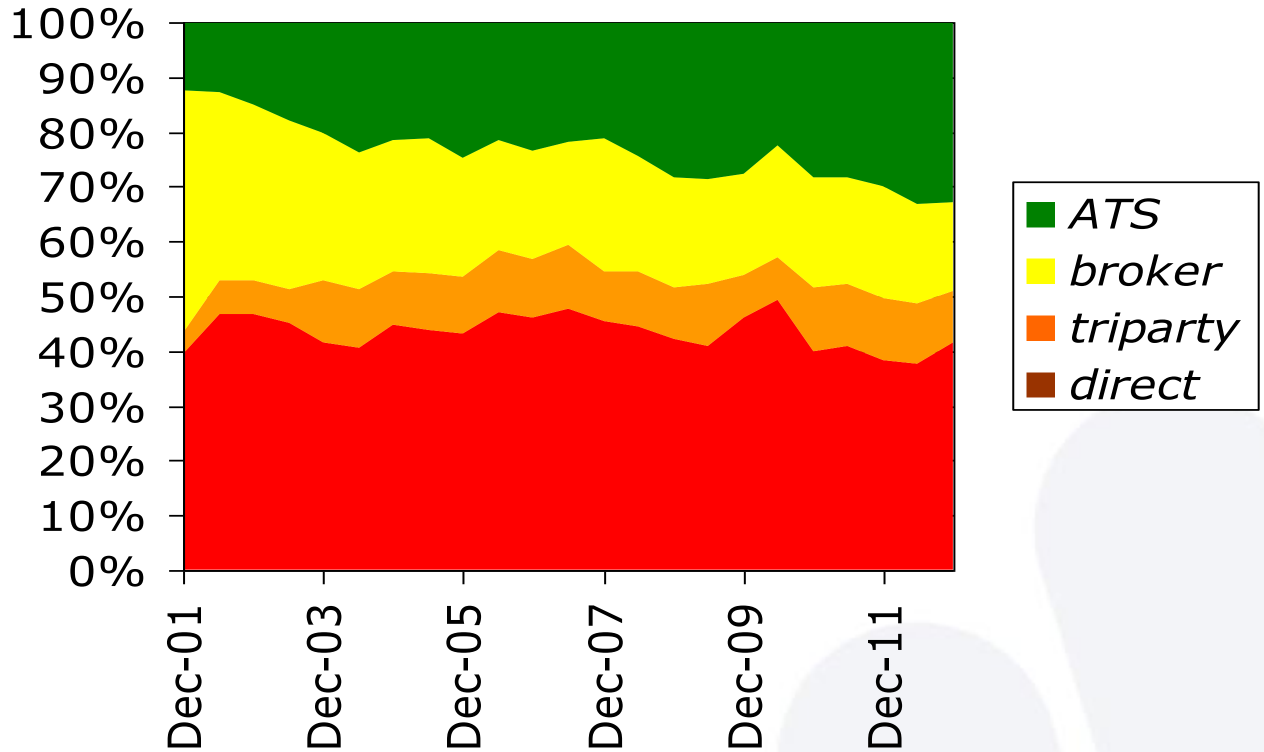
- 63 respondents in last 3 surveys
  - -6.6% since June 2012
  - -11.9% year-on-year

Trading analysis

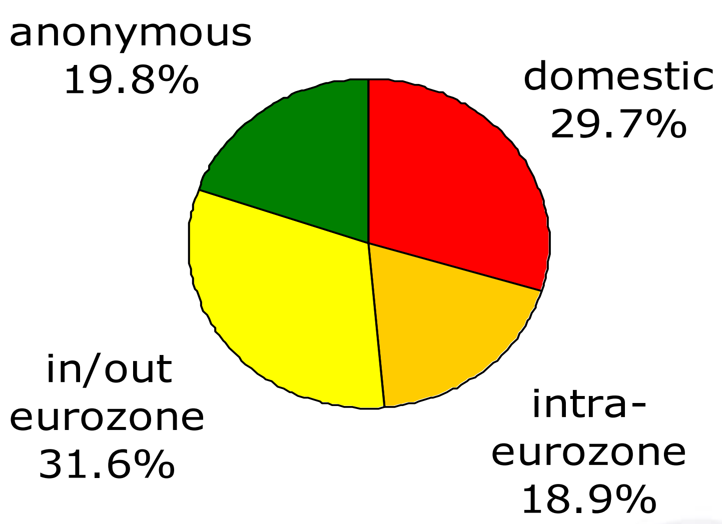


24th European repo market survey conducted in December 2012

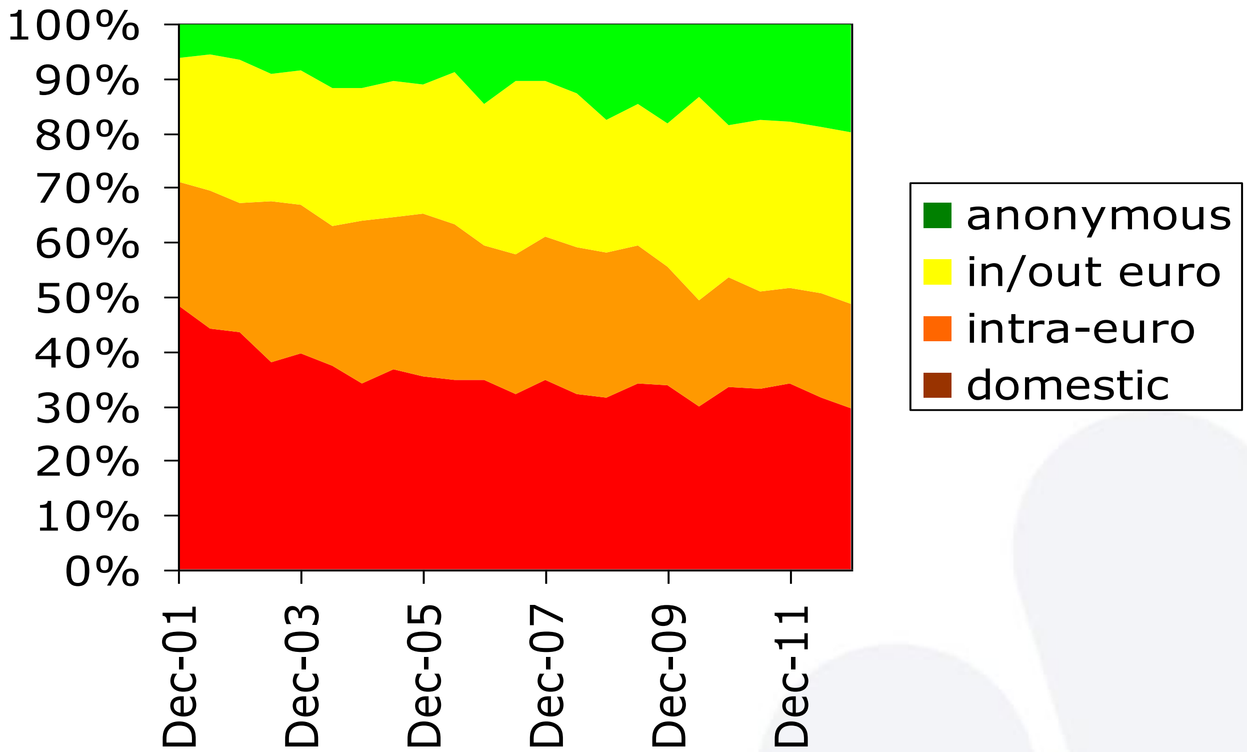
Trading analysis



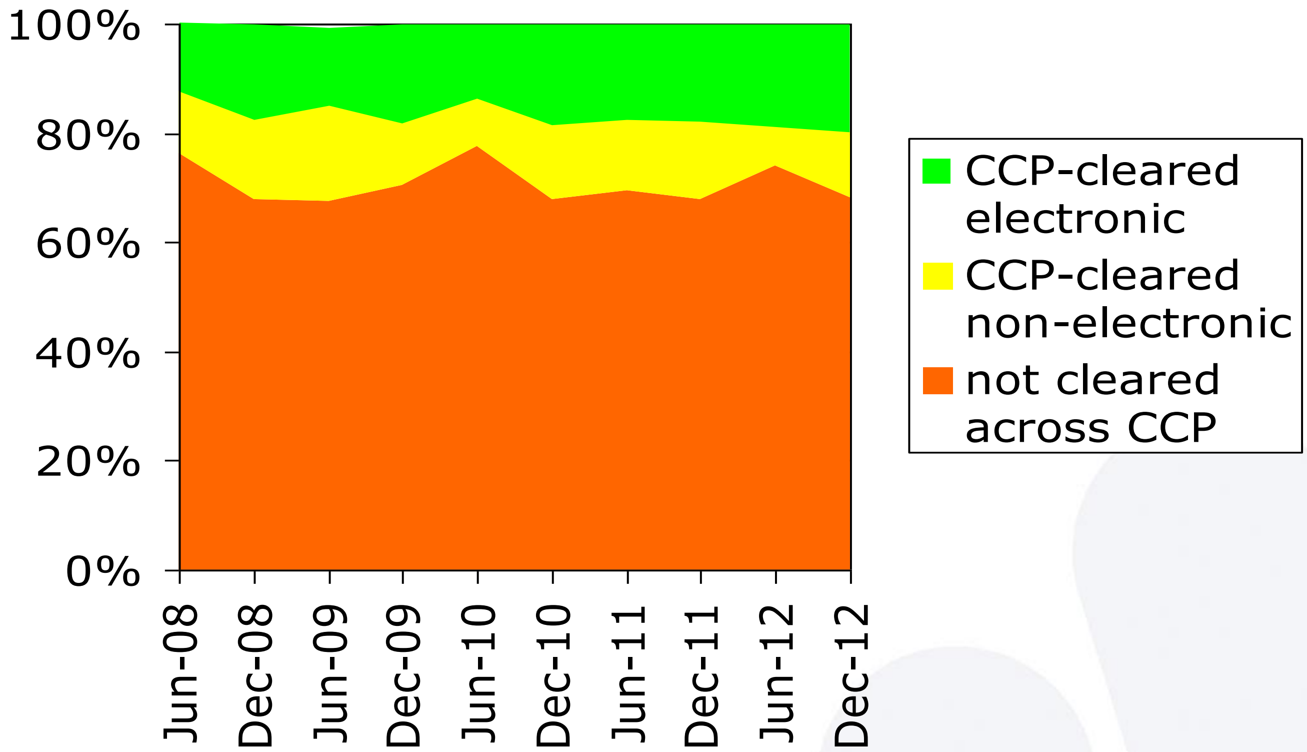
Geographical analysis



Geographical analysis

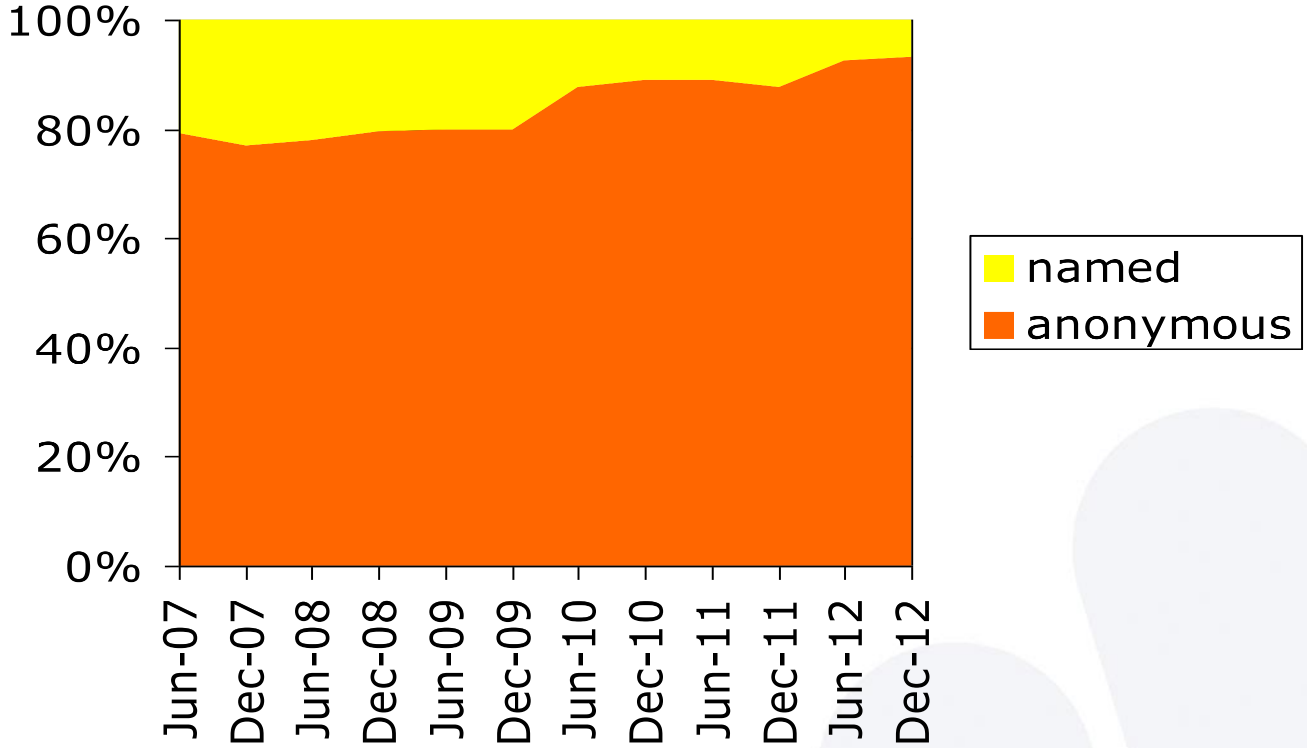


Business cleared across CCP

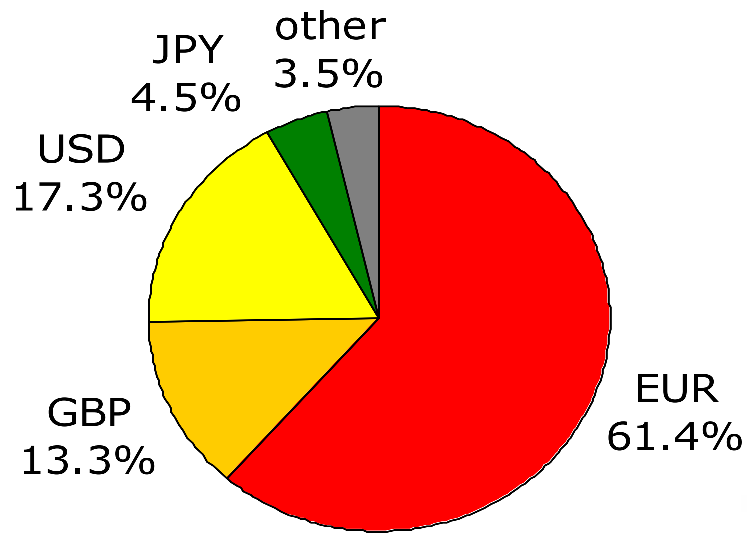


24th European repo market survey conducted in December 2012

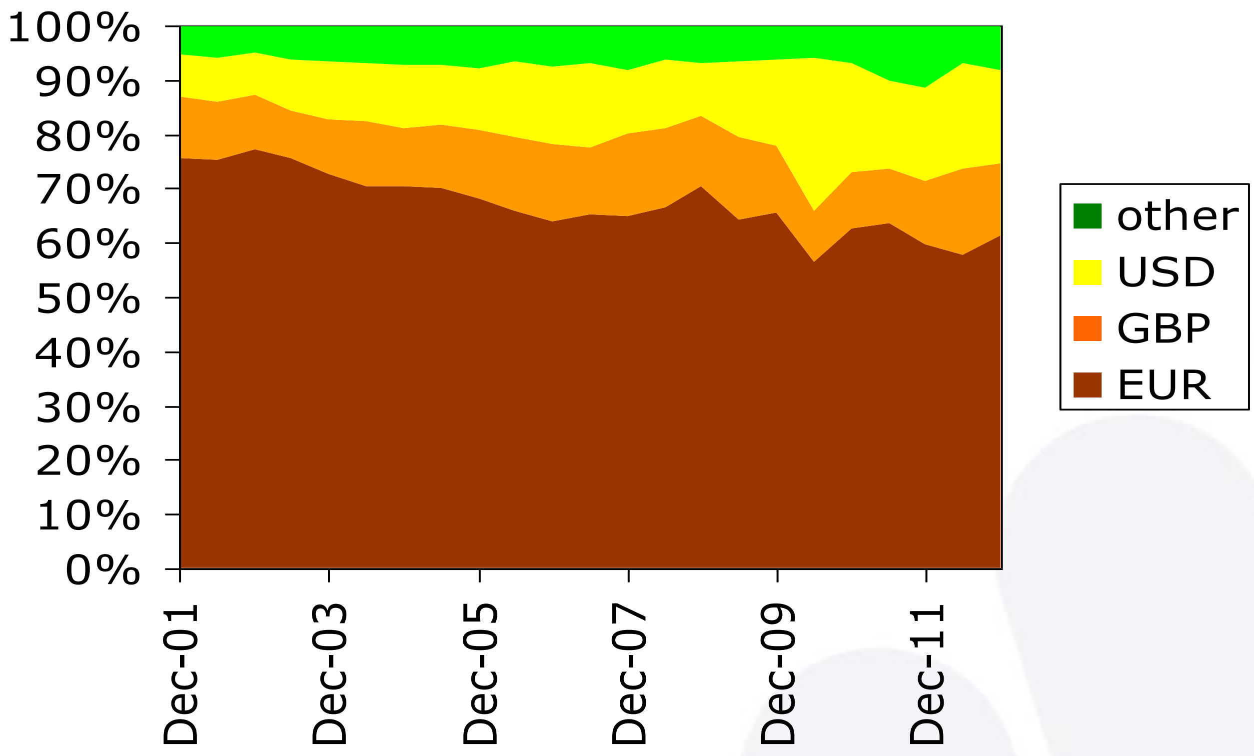
Anonymous ATS business



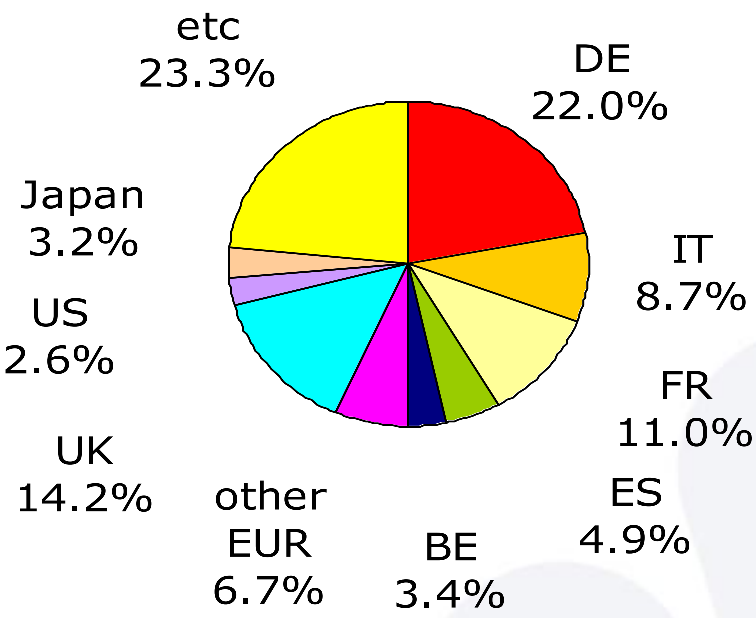
Currency analysis



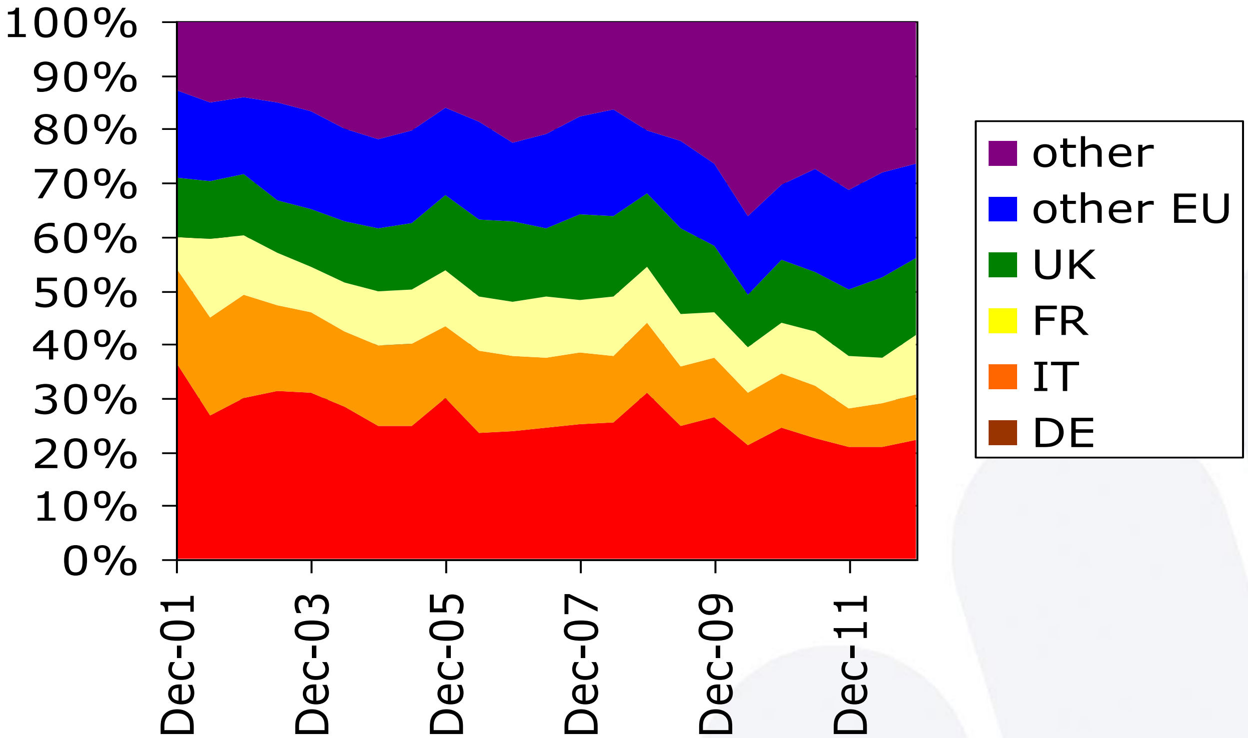
Currency analysis



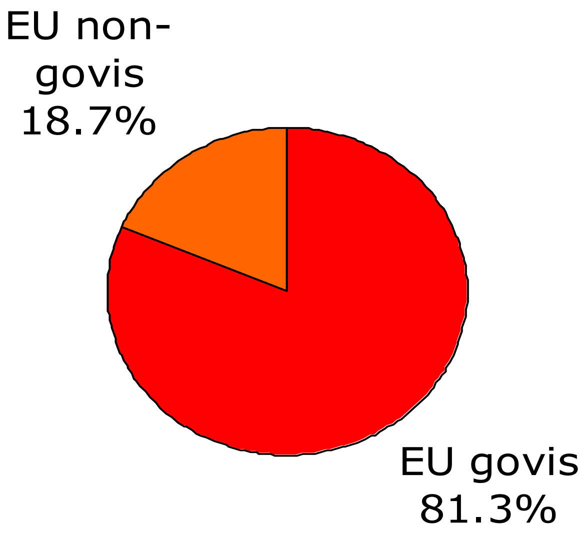
Collateral analysis



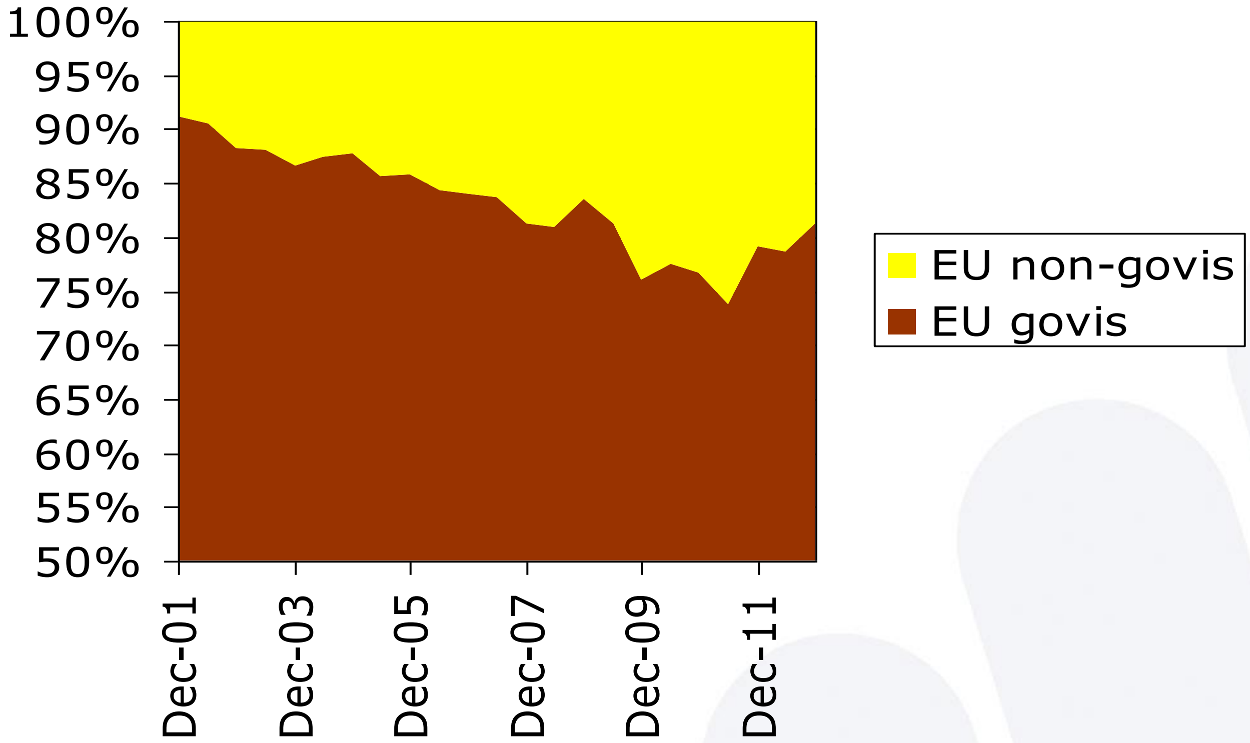
Collateral analysis



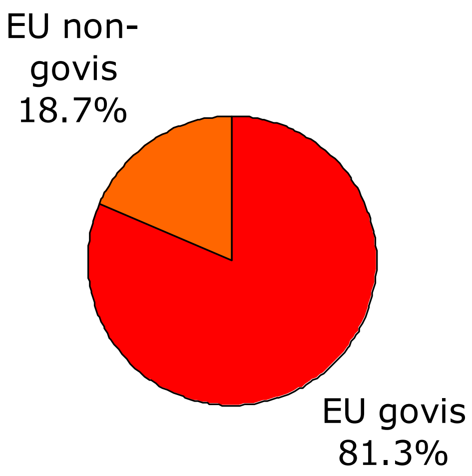
Collateral analysis



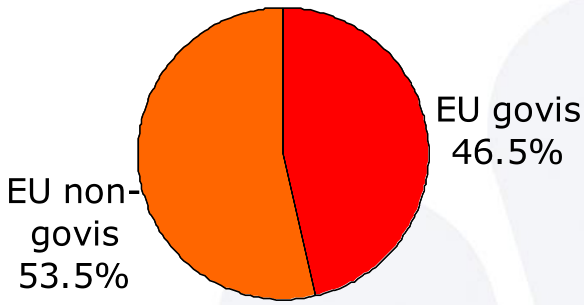
Collateral analysis



Collateral comparison

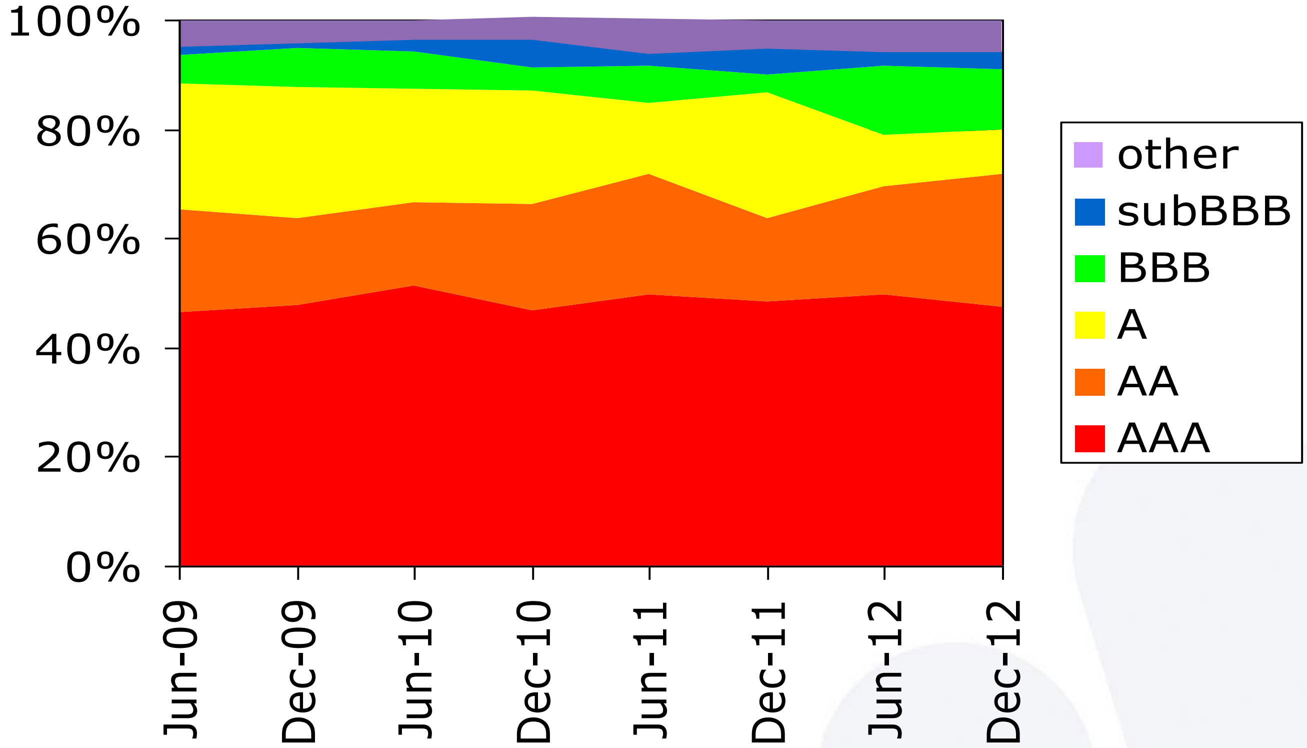


banks

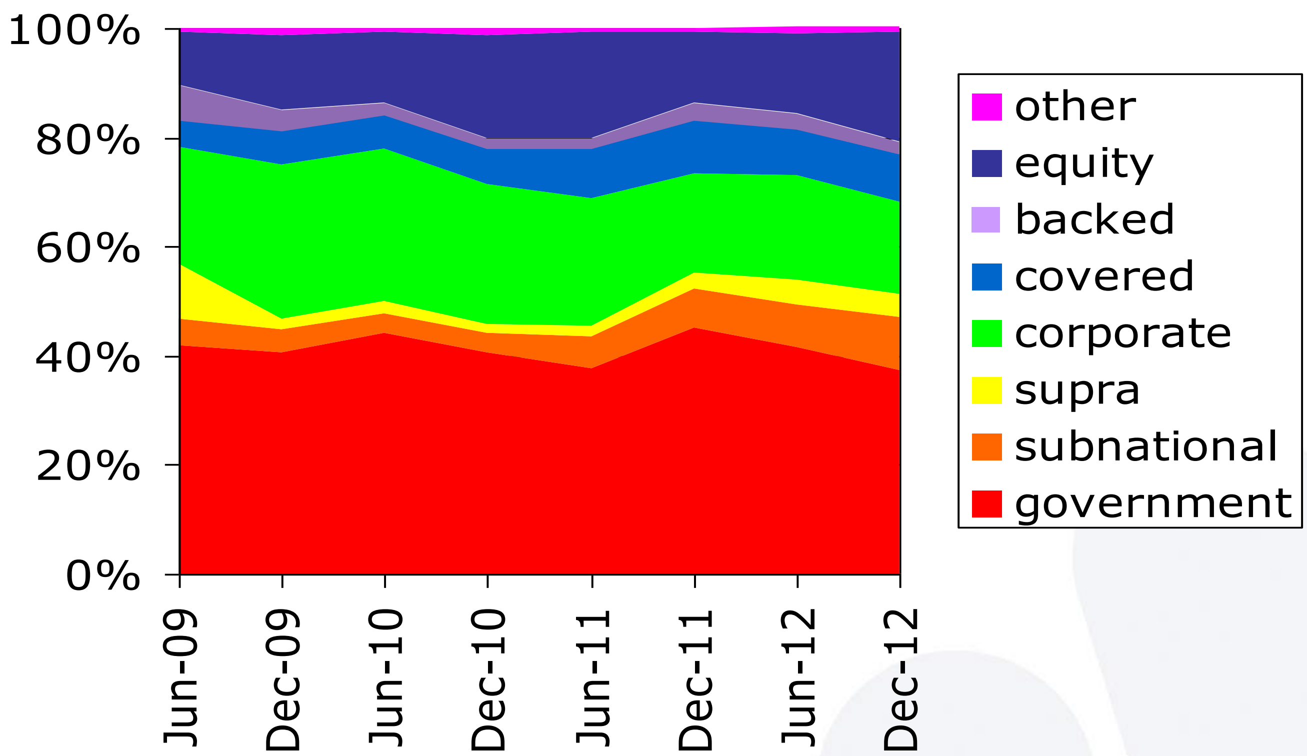


tri-party

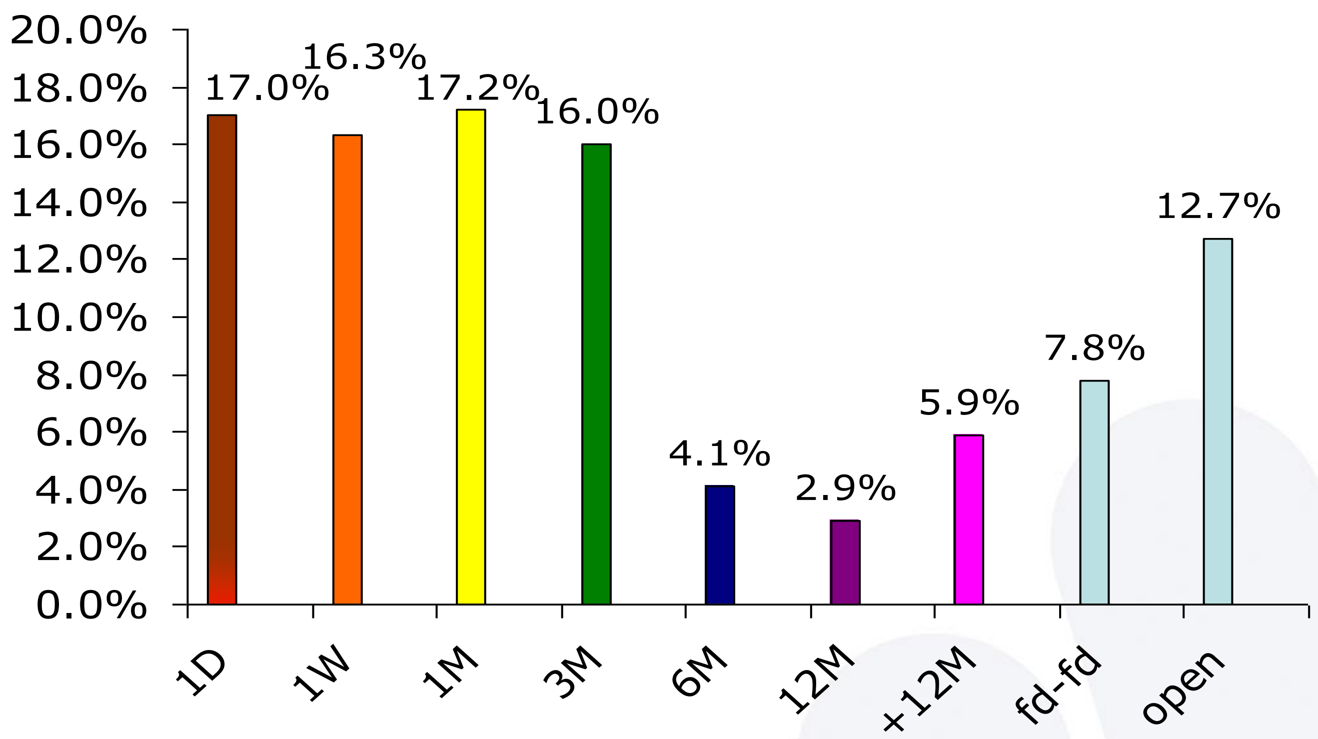
Collateral analysis (tri-party)



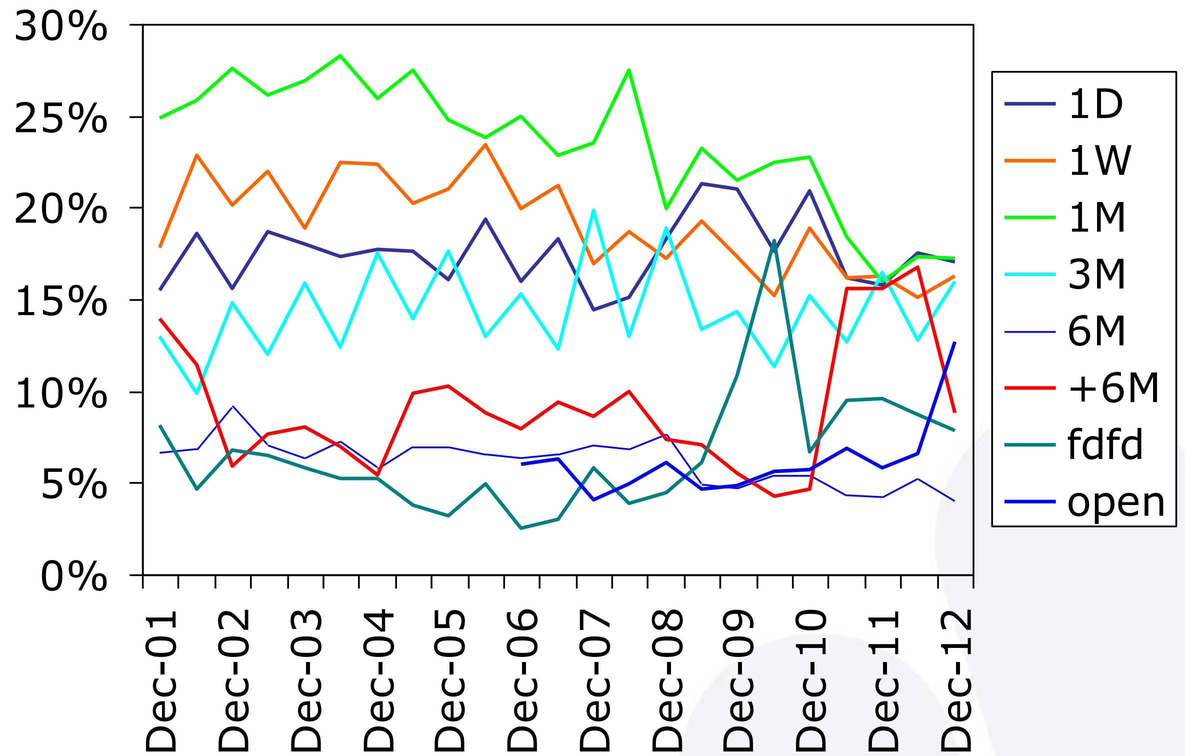
Collateral analysis (tri-party)



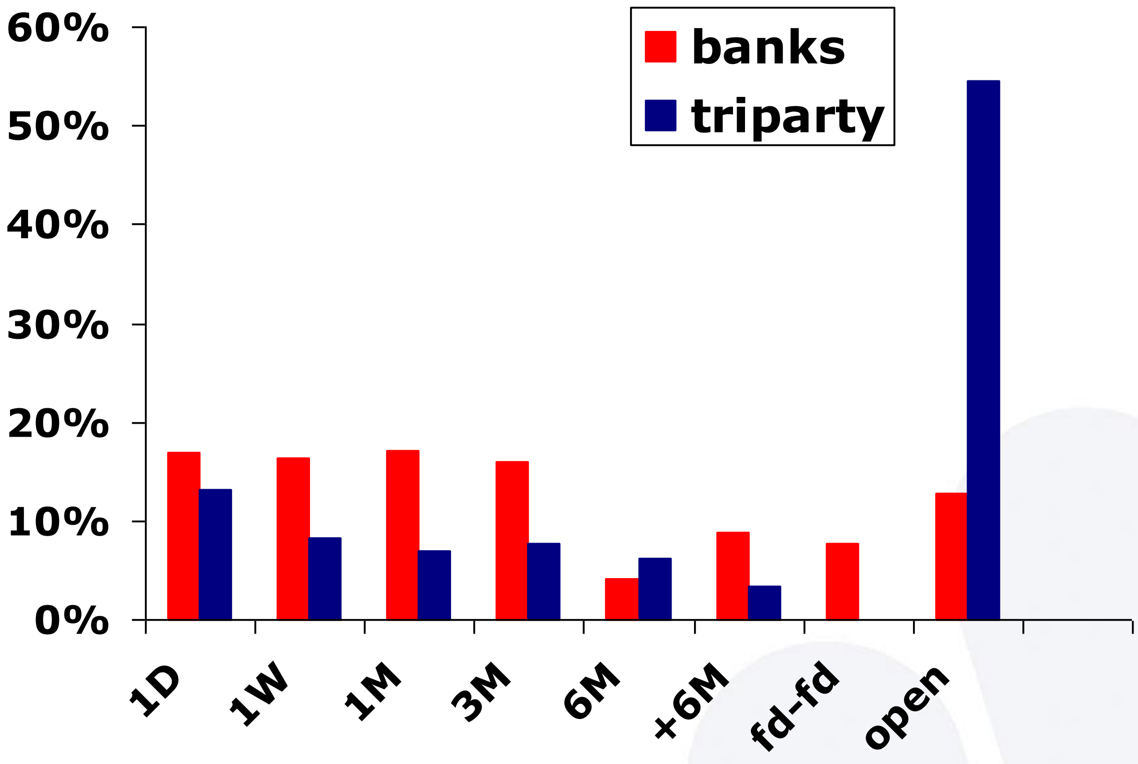
Maturity analysis



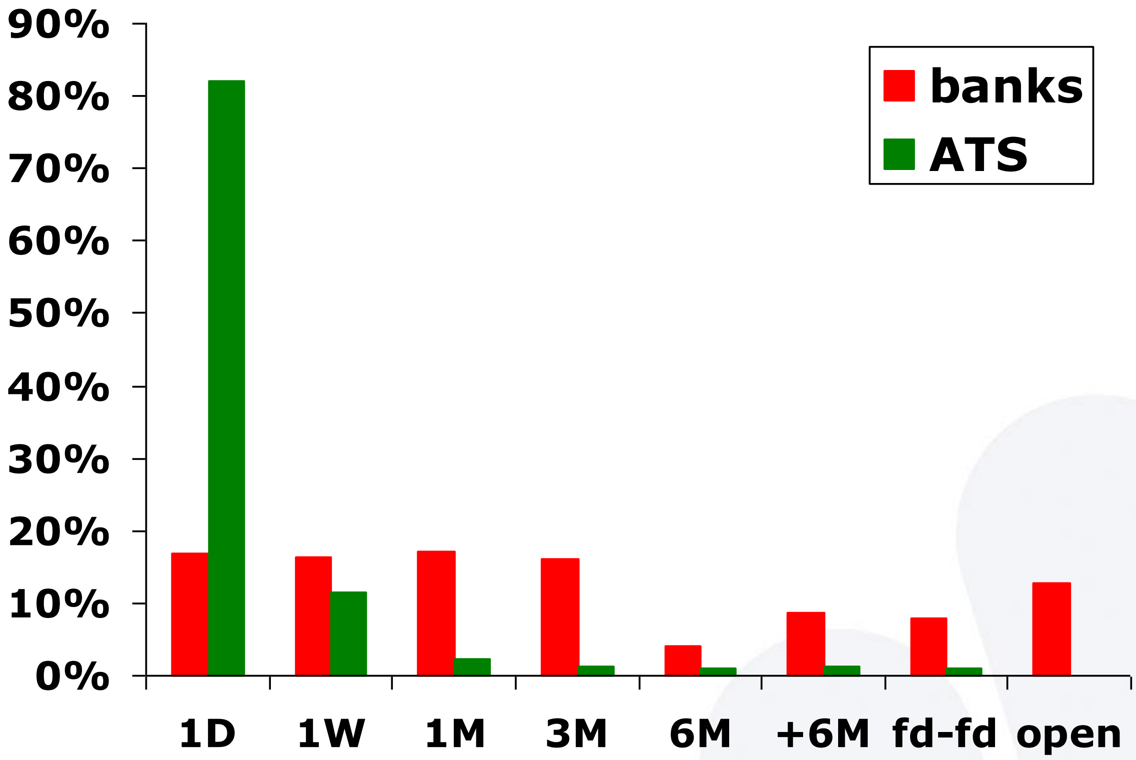
Maturity analysis



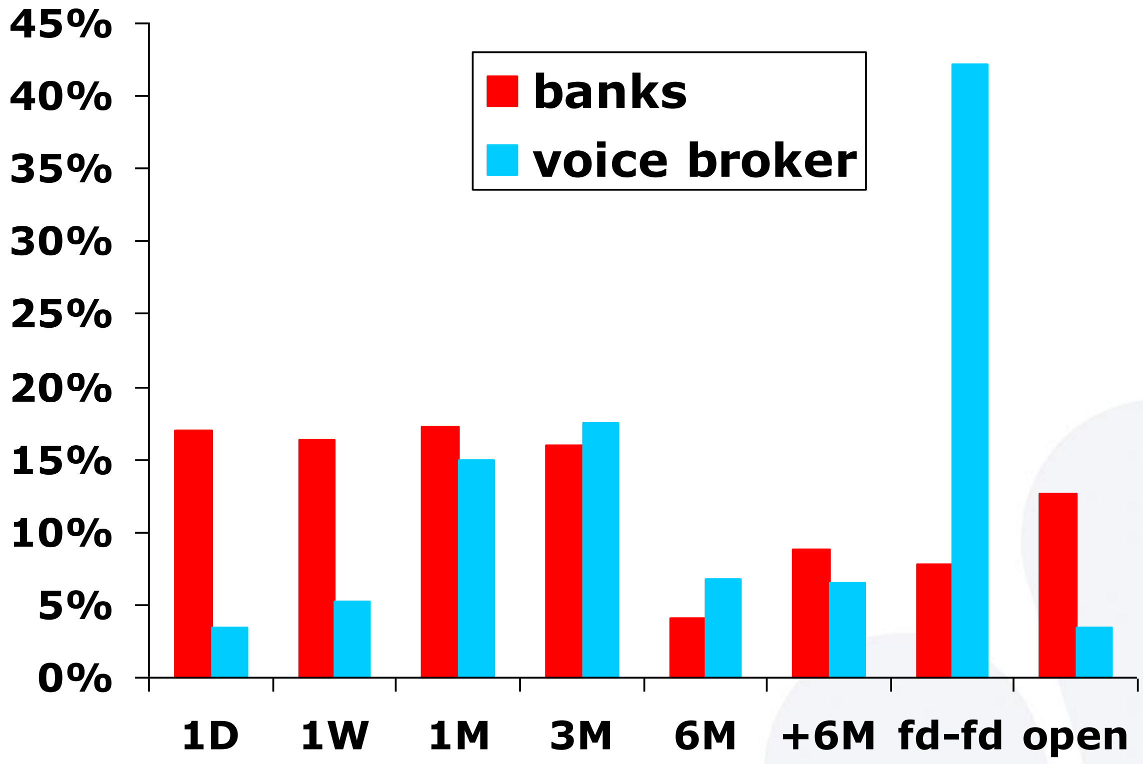
Maturity comparison



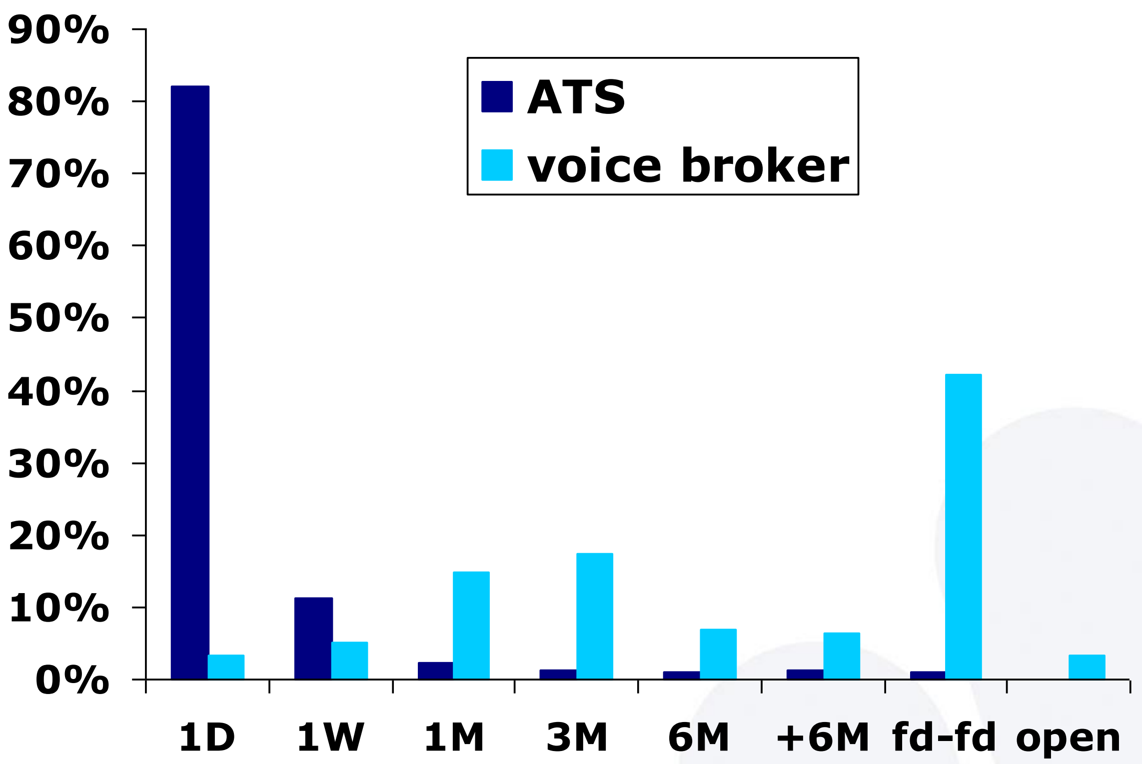
Maturity comparison



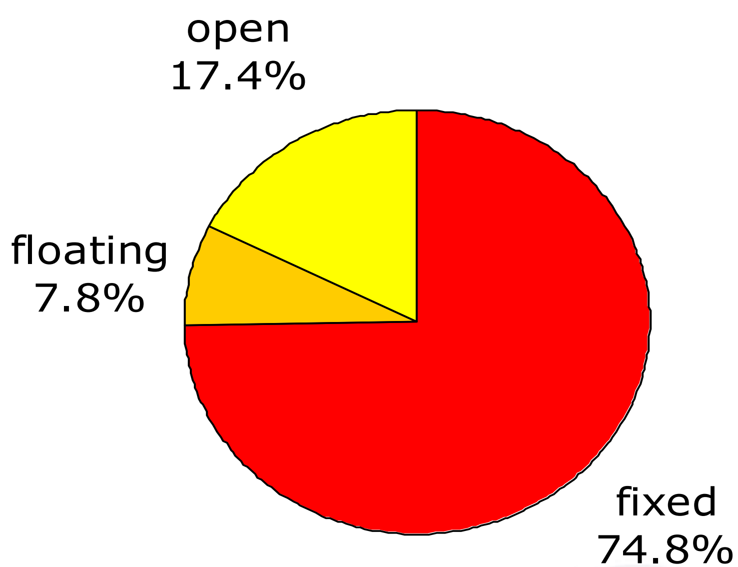
Maturity comparison



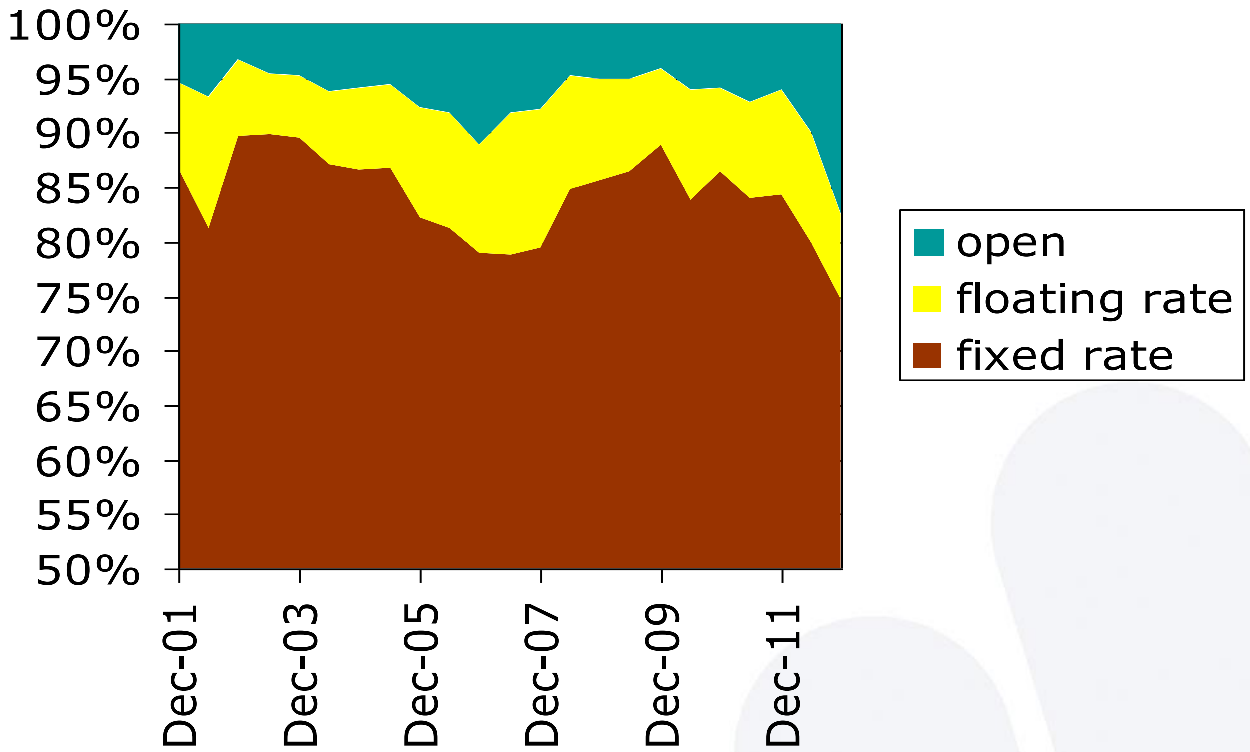
Maturity comparison



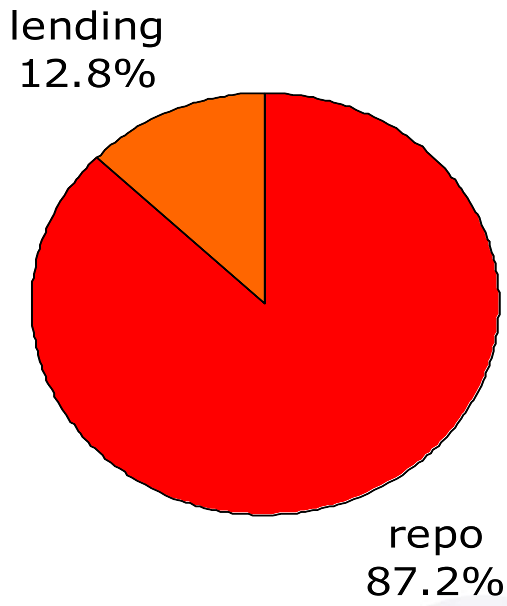
Rate analysis



Rate analysis



Product analysis



Next survey

Wednesday, 12th June 2013

ICMA International Capital Market Association

Regulatory Update

- **David Hiscock**

  Senior Director, International Capital Market Association

Repos – an aspect of shadow banking

- FSB shadow banking workstream related to securities lending/repos
  - 18 November consultation re 13 proposed policy recommendations on securities lending/repos
    - Improvements in the areas of transparency; regulation; and structure
  - ERC response submitted 14 January
  - 29 January FSB workstream meeting in New York
    - Attended by ERC Chairman

- Final FSB recommendations to be delivered September 2013

- Parallel European Commission project continues

- Active and on-going ERC engagement in efforts at both international and EU levels

ICMA International Capital Market Association

Shadow Banking - Repos

- Trade Repository
  - The ERC supports the move towards improved transparency
  - The ERC is already actively engaged in on-going work with the ECB/BoE that will aggregate numbers for European markets

- Mandatory Minimum Haircuts
  - The ERC disputes much of the case for mandatory minimum haircuts
  - Application of a minimum standard methodology for repo business executed outside the regulated interbank sector may have a place but should not be over prescriptive so as to allow firms to manage counterparty and collateral risk accordingly

- Repo Margin Standards
  - Revised ERC Repo Margining Best Practices – published H1 2012

- Re-hypothecation
  - As a general matter for repo, the ERC strongly consider that the use of collateral should not be restricted
  - For the specific and limited case of re-hypothecation of client assets, the ERC accept the case for additional requirements to be imposed

Recovery and Resolution

- EU framework for bank recovery and resolution
  - Commission proposal published June 2012
  - Debate continues in Parliament & Council, with questions raised over points of specific concern
    - Bail-in of creditors – subject to ex-ante exclusion of secured liabilities (repos)?
    - Temporary stay of close out rights (until no later than 5pm on next business day)?

Collateral

- Basel Liquidity Coverage Ratio (LCR)
  - Package of amendments to the formulation of LCR announced early January, including:
    - Revisions to the definition of high quality liquid assets, including expansion to allow inclusion of:
      - Certain highly rated RMBS, with a 25% haircut; and
      - Corporate debt securities rated A+ to BBB and certain unencumbered equities, with haircuts of 50%
    - Phase-in: LCR will be introduced as planned on 1.1.2015, but the minimum requirement will begin at 60%, rising in steps of 10 percentage points p.a. to reach 100% on 1.1.2019)

- BCBS/IOSCO Margin Requirements
  - Consultation re near final international standard covering margin for non-centrally-cleared derivatives, announced mid-February
    - Allow for the introduction of a universal initial margin threshold of €50 million
      - QIS indicates could reduce the total liquidity costs by 56% relative to a zero threshold
    - Requirement to collect and post initial margin proposed to be phased in over a four year period beginning 2015
      - Begin with the largest, most active/systemically risky derivative market participants

- Collateral Fluidity: CICF White Paper issued 7 November

MiFID II and CSDR

- MiFID II package
  - Hot topics in Council Working Group (CWG) include:
    - Scope of OTF;
    - Pre-trade transparency (post-trade is largely settled);
    - Access to infrastructure;
    - A possible obligation to trade liquid shares only on organised venues
  - Timetable: earliest date for completion of ‘Level 1’ process now Q4 2013
  - In anticipation, Level 2 work getting under way:
    - ESMA has 9 Task Forces: 4 on secondary markets; 3 on investor protection; and 1 each on commodities and transaction reporting

- CSD Regulation
  - Timing: Parliament took a position in February; the next CWG is not scheduled until May; ECB and some market participants concerned about the impact on T2S
  - ICSDs: Parliament’s compromise text allows for the continuation of the ICSD business model for now; but not clear where the Council will come out nor what the final position will be

Contact

- Thank you, Ladies and Gentlemen

- Contacts and information:
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    - David.Hiscock@icmagroup.org
    - Tel: +44 (0)20 7213 0321 (Direct Line) / +44 (0)7827 891909 (Mobile)

    - ICMA Ltd.
      23 College Hill, London EC4R 2RP
      www.icmagroup.org

Results of the elections to the European Repo Committee

1. **Simon Kipping,** Bank of America Merrill Lynch, London
2. **Eugene McGrory,** BNP Paribas, London
3. **Stephen Malekian,** Barclays Capital Securities Limited, London
4. **Grigorios Markouizos,** Citigroup Global Markets Limited, London
5. **Andreas Biewald,** Commerzbank AG, Frankfurt
6. **Romain Dumas,** Credit Suisse Securities (Europe) Limited, London
7. **Tony Baldwin,** Daiwa Capital Markets Europe Limited, London
8. **Ronan Rowley,** Deutsche Bank AG, London
9. **Olly Benkert,** Goldman Sachs International, London
10. **Jean-Michel Meyer,** HSBC Bank plc, London
11. **Godfried De Vidts,** ICAP Securities Ltd, London
12. **Andrea Masciovecchio,** Intesa Sanpaolo S.p.A, Milan
13. **Stefano Bellani,** J.P. Morgan Securities plc, London
14. **Ed McAleer,** Morgan Stanley & Co International plc, London
15. **Ulf Bacher,** Newedge Group SA, Paris
16. **Michel Semaan,** Nomura International plc, London
17. **Sylvain Bojic,** Société Générale, Paris
18. **Guido Stroemer,** UBS AG, London
19. **Eduard Cia,** UniCredit Bank AG, Munich

Any other business and next meetings

- *The Future of the European Repo Market: a conference of experts from regulators, academia and the market* – Will be held on June 11th in London, hosted by Thomson Reuters.

- The next ERC General Meeting will be held on October 16th in London, hosted by JP Morgan