ERC Annual General Meeting

Wednesday, February 25, 2009
Godfried De Vidts
Chairman, European Repo Council
Opening & Update on recent developments

Godfried De Vidts, Chairman of the ERC

European Repo Council General Meeting

Marbella 25 February 2009
Recent market events/issues

- CESR MiFID Markets Sub-Group re non-equities markets transparency
- ESCB/CESR recommendations for SSS and CCP
- ISIN code issue
- STEP project, fully supported by the ERC
Eurepo – new definition

« Eurepo is the rate as which one prime bank offers funds in Euro to another prime bank if in exchange the former receives from the latter the best collateral in terms of rating and liquidity within the Euro GC basket »
Recent market events/issues

- Letter to Italy re competition in repo markets
- Money Market Clearing Fund launched in Italy
- Interoperability between triparty agents
- Eurosysteem work on lessons from the Lehman case
Members questions?

- Rating downgrades in term GC transactions – what is the market practice?
  Response: The Committee agreed that the lowest rating of the 3 rating agencies (S&P, Moody’s & Fitch) is what needs to be taken into account. That means that if a country drops out of the AAA ratings, additional collateral from countries who keep the same rating has to be given.

- If you substitute one bond for another which value do you take?
  Response: Market practice is that the original market cash value is taken into account. A legal reference will possibly be added when the GMRA is revised.
Thank you, Ladies and Gentlemen

Contacts and information:

http://www.icmagroup.org/about1/international1.html
erc@icmagroup.org
ERC AGM 2009:
GMRA Related Matters

Lisa Cleary, Association Counsel, ICMA Zurich
2009 ICMA/SLRC COMBINED LEGAL OPINION SEEKING AND UPDATING EXERCISE
GMRA opinions available on ICMA’s website at:
Funding & availability of combined opinions:

- 68 GMRA opinions
  - funded solely by ICMA.

- GMSLA/GESLA/OSLA opinions
  - funded by the SLRC subscriber group with access via subscription.
Sovereign wealth funds and supranationals:

- Named sovereign wealth funds and supranationals to be covered in various jurisdictions.

- Cost and feasibility currently being assessed.

- Agreed costs to be split equally with the SLRC.
• NSMA GMRA produced by NSMA for domestic transactions between the Bank of Russia and Russian market participants.

• ICMA intends to inform members about this domestic repo agreement in due course, but is not planning to endorse it.

• NSMA have confirmed that the GMRA is intended to be used to document cross border repo transactions with Russian counterparties.

• ICMA continues to monitor developments in Russia with regard to the GMRA.
GMRA ISSUES
• Developing a credit claims annex to the GMRA

• ECB meeting.

• Cost/time estimate being prepared.

• Feedback with regard to market interest welcome.
ICMA has requested the ERC committee to identify specific provisions of the GMRA which it feels it would be beneficial to review, in light of current market conditions.

All suggestions in this regard should be sent to lisa.cleary@icmagroup.org

Depending on the feedback received, such review may result in more robust GMRA guidance notes, ERC driven market guidance &/or amendments to the GMRA.
Election to the European Repo Committee

Godfried De Vidts
Chairman, European Repo Council
1. Tony Baldwin, Daiwa Securities SMBC Europe Ltd
2. Stefano Bellani J. P. Morgan Securities Ltd., London
4. Eduard Cia UniCredit Markets & Investment Banking
5. Herminio Crespo Urena Caja de Madrid, Madrid
8. Johan Evenepoel Dexia Bank Belgium NV/SA, Brussels
10. Thomas Hansen Credit Suisse, London
11. Eric Lepore Deutsche Bank AG, London branch
15. Jessica McDermott Merrill Lynch International (MLI), London
17. Dina Noelle Rabobank, London
18. Simon Parkins BNP Paribas, London branch
20. Luis Soutullo Confederación Española de Cajas de Ahorros (CECA), Madrid
21. Simon Tims UBS AG, Zurich
22. Stefaan Van de Mosselaer Fortis Bank, Brussels
ERC Operational issues
Godfried De Vidts
Chairman, European Repo Council
SLRC: Developments of the Bank of England’s market operations – report on consultation & other topics discussed

Tony Baldwin
Executive Director, Head of Repo Trading and Funding, Daiwa SMBC
European Repo Council update on Securities Lending and Repo Committee (SLRC) activities

Tony Baldwin
February 2009
Bank of England chairs a number of market committees
• Sterling Money Markets Liaison Group (MMLG)
• Foreign Exchange Joint Standing Committee
• Securities Lending and Repo Committee (SLRC)

SLRC
Formed in 1990 under name of Stock Borrowing and Lending Committee (SBLC). 2 name changes since lead to current title of the .... Securities Lending and Repo Committee

Meeting quarterly

Participants of SLRC
International repo and securities lending practitioners
Representatives of trade organizations
London Stock Exchange
UK Debt Management Office
Financial Services Authority
Background

Purpose

• Provide a forum in which structural developments in the securities lending and repo markets can be discussed, and recommendations made, by practitioners, infrastructure providers and the authorities.

• Co-ordinate the development of
  – Securities Borrowing and Lending Code of Guidance
  – Gilt Repo Code of Guidance

• Review the need for other market guidance relevant to the repo or securities lending markets

• Update the Gilts Annex to the Global Master Repurchase Agreement (GMRA)

• Liaise with similar market bodies and trade organizations covering the repo and securities markets and other financial markets, both in London and other financial centers

• Keep under review the arrangements for obtaining legal opinions on netting in the repo and sec lending agreements
Guidance

SLRC has been responsible for a number of codes of guidance:

• Securities Borrowing and Lending Code of Guidance
• Gilt Repo Code of Guidance
• Gilt Annex to the GMRA

Endorsed in June 2005
Securities Lending and Corporate Governance

Together with ACT, BBA, LIBA, LSE the SLRC sponsored an
Introduction to Securities Lending
Upcoming work topics (provisional)

- Gilt Repo Code
- Review of Securities Borrowing and Lending Code
- Review of Global Master Securities Lending Agreement (GMSLA)
- Combination of exercises in gathering legal opinions on securities lending and repo legal agreements as used in different jurisdictions
- LCH.Clearnet gilt DBV repo clearing project
- Euroclear term DBV product
- Impact of proposed regulatory changes affecting securities lending or repo markets, including MiFID, Transparency Directive
- Basel II and implications for securities lending and repo
Upcoming work topics (provisional)
Con’td….

• Promote publication on securities lending

• Target2Securities

• Case for new guidance on equity repo

• Monitoring corporate governance proposals affecting securities lending and repo

• UNCITRAL legislative guide on secured lending

• Monitor G-30 work where relevant to repo or securities lending

• Monitor work on tackling Giovannini barriers where relevant to repo or securities lending

• Open to suggestions on other relevant topics
Amendments to improve markets

One notable decision made last year in Gilt repo market was to make Bank of England sterling bills eligible in the CREST UBG DBV category from 11 December.

This decision was made after consultation between the Bank, DMO, Treasury, Crest as well as Gilt repo market participants.

SLRC website
http://www.bankofengland.co.uk/markets/gilts/slrc.htm
Clearing and settlement issues

Godfried De Vidts
Chairman, European Repo Council
LoanReach: Towards the delivery of a structural solution for the European loan markets

Olivier Grimonpont, Director, Euroclear SA
LoanReach

A market vision becoming reality

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Agenda

• Euroclear’s involvement in the loan market
• Euroclear services: A phased approach
• Main features of LoanReach
• Collateral management services
• Detailed roll-out plan
• Market take-up
• Contact information
Euroclear’s involvement in the loan market

- Request from Collateral User Group to support the use of credit claims as collateral
- Request from the ERC and ECB to use credit claims in interbank and central bank collateral operations
- Request from the Euroclear Board to streamline and automate post-trade processing in the loan market space
- The Loan Market Association provided Euroclear with a mandate to bring standardisation and automation in the syndicated loan market

5 dimensions in the LMA RFI

- Standard reference data
- Electronic Agent messaging
- Central loan reconciliation
- Automated confirmation, closing and settlement of primary and secondary trades
- Sharing of key information
Euroclear Services: A phased approach

First phase (June 2008) – Building the foundation

- Loan Number allocation service
- Global Loan Database with static/dynamic data and balances
- Dynamic Agent/Lender reporting

Second phase (End 2008 – Q1 2009) – Providing transparency

- Portfolio Reconciliation [expanded from Lender reporting]
- Parties database (Agents and Lenders)
- Automated Trade Matching instructions (Secondary market)

Third phase (2009-2010) – Move towards increased STP and added-value services

- DvP settlement of primary and secondary trades
- Collateral Management services
- Agent notices
- Income and Tax services

Already implemented
Under development
Main features of LoanReach

A higher degree of standardisation
- Unique identifiers at deal, facility and contract level => free of charge
- Consolidated reporting across agents and lenders/sub-lenders
- Standardised process for matching and multi-currency DvP settlement

More transparency
- Central market loan database accessible to agents and lenders
- Easy interaction between loan market participants
- Central access to all loan events

Increased efficiency and straight-through processing
- Correct loan positions as basis for income calculation and matching
- Higher degree of automation in loan processing, reduction of back-office costs
- Reduction of trade cycle => increased liquidity
- Elimination of credit risk with DvP settlement
- Financing of the loan through repo agreements
Pre-requisites to offer Collateral management services

- **Unique loan identifiers**
  - ECB and ERC support to incorporate loans into the ISO 6166 standard (ISIN standard)
  - LMA advices to keep the number of NNA’s for loans limited

- **Centralised loan database**
  - LoanReach provides a centralised database to the market (agents and lenders)
  - ERC supports LoanReach as basis to build a European model for credit claims

- **Financial Collateral and Settlement Finality Directive**
  - Will need to recognise credit claims for bilateral and central bank collateral operations
  - Harmonisation of perfection rules to allow short-term repo’s

- **Global Master Repurchase Agreement**
  - To include credit claims as eligible collateral

- **Valuation service**
  - Market solutions/third party providers to provide proper valuation

- **DvP Settlement**
  - Allowing secure settlement of primary and secondary trades
Detailed roll-out plan for services

Timeline

2009

Q1

Q2

Q3

Q4

Trade Matching

Agent Notices

DVP Settlement

Collateral service

Launch in production

Development & testing

Analysis & consultation

Finalisation of requirements

Development & testing

Analysis & consultation

Finalisation of requirements

Development & testing

Analysis & consultation

Finalisation of requirements

Development & testing
Market take-up

Strong support from major agents and lenders

- Loan participants are actively testing services
- Extensive list amongst which Soc. Gen, BNP Paribas, BNY Mellon and UBS
- New agents are to sign up soon

LMA Euroclear working group

- Chaired by Crédit Suisse, to steer the direction of the LoanReach initiative
- Working group is closely following up new developments and testing results
- Open working group – new participants are welcome

ECB and ERC

- Discussions ongoing to build a European model for interbank and central bank credit requests collateralised by loans
- Model allows for financing of the loan through repo’s
Contact information

- Olivier Grimonpont – Head of Product Management Fixed income, Collateral and Loan services – Tel: 32 2 326 4320 – Email: olivier.grimonpont@euroclear.com

- Jurgen De Weghe – Product Management – Loan Servicing – Tel: 32 2 326 4932 – Email: jurgen.deweghe@euroclear.com

- Olivier Léonard – Product Management – Loan Servicing – Tel: 32 2 326 4657 – Email: olivier.leonard@euroclear.com
Giovannini barriers 2, 4, 7 and 10

Godfried De Vidts
Chairman, European Repo Council
Barriers 4 & 7, 2 & 10
Update
Progress since last CESAME Meeting (I)

- ECSDA provided comprehensive mapping report on cut-off times for same-day settlement on time and in line with agreed methodology.
- Joint Working Group on Barrier 7 set up with representatives from (I)CSDs, ECB, EC and users including agent banks; analysis of issues in meetings in December 08 / January 09.
- ERC/EPDA continued analytical work in context of Barriers 2 & 10 with impact also on Barriers 4 & 7.
Progress since last CESAME Meeting (II)

- Coordination meeting Barriers 2 & 10, 4 & 7:
  - Separate but mutually informed analysis of issues
  - Close coordination in the development of solutions

- First conclusions of links analysis of 5 markets:
  - Significant areas of potential issues overlap of the 4 Barriers
  - Cross-border / cross-CSD issues caused by inadequate compliance with relevant standards, not by indirect links including sub-custodians / agent banks
### ERC Interoperability Evaluation (I)

**FEATURE** | ITALY | FRANCE | GERMANY | UK | SPAIN | BELGIUM (BNB) | NETHERLANDS | GREECE
--- | --- | --- | --- | --- | --- | --- | --- | ---
DvP and FoP link | Y | Y | Y | Y | Y | Y | Y | Y
Early input of Instructions | Pre-matching by phone before 17.30 on S-1 so instructions only sent to Monte Titoli after 17.30 on S-1 | Y | Y | Y | Y | Y | N | Y
Settlement early in day | Most settlement occurs during the overnight before value date | Most settlement occurs during the overnight before value date and early in the RTS | Y | Y | Most settlement occurs during the overnight before value date | Y | Most settlement occurs during the overnight before value date and early in the RTS | N | Most settlement occurs during the overnight before value date and early in the RTS | N | Most settlement occurs during the overnight before value date and early in the RTS
Timely settlement throughout day | Settlement finality for overnight batch at 07.00 and for daytime batch is at 13.15 | RTS system from 01.00 to 17.00 | CBF provides real time feedback except during two 30 min batches where feedback is at the end of the batch | Y | New instructions are not presented for settlement until 13.00/13.30 | RTS system from 01.00 to 17.00 | Y | New instructions must be pre-matched and generally not presented for settlement until 13.30 | N | By the time Greek bonds are received in the local market it is too late to use them to reimburse loans or for treasury
Supports use for collateral management purposes | Y | Y | Y | N | Y | Y | Y | Y
Multiple settlement attempts | Unsettled instructions are recycled to the daytime batch if still unsettled to the RTS | Continuous instruction recycling | But the SDS process does not recycle instructions into the RTS process | Y | Y | Hourly batches throughout day with immediate feedback | Y | Continuous instruction recycling | Y
Same day instruction input deadlines | Y for RTGS only with counterparty agreement special flag higher credit needs | Participant input deadline allows user to take settlement feedback into account | Y | Y | Y | Y | Participant input deadline allows user to take settlement feedback into account | Y | The deadline is before the bulk of local market settlement
Unified settlement system | Different requirements including credit usage for RTGS and Net cycles | Y | Y | Y | Y | Y | Y | Y
Full use of settlement window | Y | Y | Y | N | Settlement with finality 14.30 and 16.00 is reserved for own account activity of direct Iberclear participants only | Window between 8am and 11am is only available for settlement between Primary dealers with direct accounts at BNB | New instructions can be input by any party until the end of the day | Y | Extra cost for settlement between 13.30 and 14.30 and settlement between 14.30 and 16.00 is for CCBM only
Finality of settlement | Y | Y | Y | N | Settlement with finality is deferred by 60 mins. To be be fixed in Nov'09 | Settlement finality for overnight batch is at 7.00 | Y | Y | Y

**CESAME2 Group Meeting 9 February 2009**

**EUROPEAN REPO COUNCIL**

**ECSDA European Central Securities Depository Association**

**SIFMA European Securities Services Association**

**Draft for Discussion**
# ERC Interoperability Evaluation (II)

<table>
<thead>
<tr>
<th>FEATURE</th>
<th>PORTUGAL</th>
<th>SWEDEN</th>
<th>AUSTRIA</th>
<th>DENMARK</th>
<th>FINLAND</th>
<th>IRELAND</th>
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<td>Timely settlement throughout day</td>
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<td>Supports use for collateral management purposes</td>
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<tr>
<td>Multiple settlement attempts</td>
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<td>Same day instruction input deadlines</td>
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<td>Unified settlement system</td>
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<td>Full use of settlement window</td>
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</table>

- **Y**: Yes, information is available.
- **N**: No, information is not available.
- **M**: Missing, information is not available.

### Additional Notes:
- Settlement only starts at 08:30, where 07:00 is the opening of Target2.
- Early input of Instructions is available up to 09:00.
- Settlement is possible until 14:00 for DVP and 17:00 for FOP.
- There are only 2 daytime settlement cycles at 10:15 and 12:00.
- RTS from 7am to 6pm with immediate feedback (but communication from agents to CSD is not SWIFT based).
- Remote membership requires domestic sponsorship. Remote member trades are considered executed by the sponsor. The domestic sponsor is responsible if the remote member defaults.
- Failed trades are not allowed and KDD will trigger buy-in. OTC trades are manually matched and released for settlement. If the trade is not settled by 15:30 on SD, it is removed from the settlement system and re-released the next day.
Way forward (I)

- ERC/EPDA to finalise analysis of 15 European markets
- ECSDA to assess compliance with Matching Standards and ESCDA Standards Barrier 4 & 7 based on ERC/EPDA analysis
- Users to agree on scope
  - primarily fixed income and repo markets, small number of most important equity markets
  - primarily links from CSDs to ICSDs
  - focus on most relevant issues / cases
Way forward (II)

- Future meetings to include concerned parties (CSDs et al)
- Presentation of targeted solutions (rather than set of standards) for both Barriers 2 & 10 and Barriers 4 & 7 at CESAME2 Group meeting of 8 June 2009.
- Bank of Greece changed a number of issues
- Iberclear has agreed to sit together
- Monte Titoli is working on certain changes already
- The ERC will constructively look with all CSDs where problems are identified for speedy solutions
CESR’s response to the crisis
Eddy Wymeersch
Chairman, CESR
Securities Regulation in Europe after the crisis

Eddy Wymeersch
chairman
Committee of European Securities Regulators
(CESR)
• Committee of 27 European agencies in charge of securities markets
• Similar committees for Banking (CEBS) and Insurance (CEIOPS)
• All competences are national
• Increasingly EU regulation (Directives)
• Coordination of national actions
Role of CESR

- Advisor to the EU Commission on regulation
- Convergence of national regulations
  - By: interpretations, standards, guidance etc.
  - Coordination of national supervisory action
  - CESR is not a supervisor
  - Its actions are not legally binding but de facto have much authority
Changes in the supervisory structure

- 25 February: *de Larosière report*
  - More centralised decision making
  - More homogenous rules
  - Institutional structure: agency or EU institution?
- More important for banking
  - Macroprudential will go to ESCB
  - Microprudential: Hub and spoke system, but how?
  - Problem of fiscal support is key
- Discussion in European Council, further developments, submission after election and with new Commission
Response to the crisis

• The crisis is essentially a banking and markets crisis
• Insurance indirectly affected
• Securities: where CESR was involved
  • Investment funds
    • Money market funds
    • Hedge funds
  • Madoff
  • Clearing and settlement
  • Equity and bonds: no deficiencies- disclosure
  • Cds: CCP for systemic risks
Specific Actions

- Credit ratings agencies
- Valuation of illiquid assets
- Hedge funds
- Short selling
- Lehman
- Madoff
- CDS and CCP
- Training and common culture
- Institutional questions
Credit Rating Agencies

- Credit rating Agencies
  - CESR undertook assessment on the basis of IOSCO code in 2004 and 2006
  - EU Regulation proposed and almost adopted
  - CESR as umpire of the process in the hand of the National authorities
    - No binding legal power
    - Coordination of action of the national supervisors
    - Secretariat
    - Advisory role – help in solving conflicts
Credit Rating Agencies

- Is there is going to be one centralised supervisory body, CRAs are like to be the first assignment of CESR.
- Requires CESR decision to have binding force in each of the member states
Valuation

- IRFS Fair value: comparable to US GAAP
- Process: Commission endorsement of IASB standards
  - Commission and Parliament could block = power struggle
- IAS 39 on derivatives: strict version of “fair value” but not very coherent: loans v. bonds.
- **November 08**: Reclassification allowed from the banking book to allow alternative accounting methods: essentially DCF
  - Fair value: market – but no markets anymore
  - Held to maturity
    - On the basis of discounted cash flow, or similar method
    - Considerable effect on the results: CESR study expected
    - Are these result fictitious: no if these assets had been booked in the banking book from the beginning.
Valuation

- **Revision requests**
  - Commission pressures IASB into changes e.g. on embedded derivatives, on fair value option, on insurance.
  - IASB reluctant to respond.
- **Political discussion**
  - Agreement EU-US aligned
  - Roadmap on introduction of IFRS in US: is it still valid?
  - Adopted for non US issuers: 3rd Q 2008
  - US issuers: process halted under new SEC
  - IFRS adopted by EU + promised by Japan, India, China, Canada, St Korea, etc.
  - To be revisited later
Hedge Funds

- Many managed from London, but established in the Caribian (Cayman islands e.g. = no taxes)
- Light regime: registration for managers, not strict follow up
- Fear that crisis would have started there: nothing happened, until recently
Hedge Funds

- Proposal by **Comm**: regulation, but what? Conference Friday
  - Systemic danger: leverage, effect on markets
  - Market abuse:
  - Remuneration? 20% up only.
- **Iosco** text adopted last week: regulators should know.
  - direct/indirect regulation esp. systemic funds
  - Extend market abuse rules
  - Should leverage be reduced

**Self regulation**

Hedge Fund Working Group: principles; systemic awareness.

- **US** will also act but how? Very soon
Short Selling

- Ban introduced in most states in October 2008
- At state level
  - Many had no clear legal basis
    - Market manipulation
    - Fair and orderly markets
    - No express mandate
- Urgent matter: downwards speculation against the banks
  - Clear case how not to do it:
    - Ineffective
    - Large differences
    - Not verifiable
    - etc
Short Selling

• CESR will opt for a disclosure regime
  • With aggregate disclosure to public upon crossing certain %
  • Only net positions
  • Immediate reporting, but delayed publication
  • Timely settlement: Stronger enforcement

• Later: work on settlement:
  • What is naked shorting?
  • If a ban has to be imposed, how should it work
  • How relate to derivatives, esp. CDS
Lehman

- Big shock: started the banking crisis in the EU
  - Start of confidence crisis in interbank market
- About 3000 companies in the EU: SPVs
- Liquidation under UK regime: administration
  - Will take years
  - CDS have been unwound in Clearnet: orderly unwinding
- Several major investor protection issue:
  - Lehman certificates presented as capital guaranteed
  - Were prospectuses used, what was a prospectus
  - Advise to investors, suitability
- Liability of selling banks: voluntary action
Lehman

• CESRs role: lessons to be drawn
  ◆ Obtaining information on effects of failure
  ◆ Determine what are the regulatory lessons: Mifid, clearing and settlement, rehypothecation, etc
  ◆ Misselling: did suitability test apply?
  ◆ No prospectus used
    • Above € 50.000: Free offering
    • Complex products: wide use of derivatives: what is complex
Madoff

- Upmarket damage
- Austrian Bank Medici: take over by state
- Santander: 2.5bn; BNP: 0.5 Bn.
- Investment funds: 1.8 bn
- Issues of subdepository
- Wide range of victims
  - Insurance, pension funds, foundations etc.
  - No small retail investors directly
Madoff

- Role of CESR
- Collecting information, analysis of what went wrong
- Regulatory lessons, eg. Sub-depository
- Cooperation from SEC
- Press release referring to Madoff Trustee
  - First case of effective investor protection
CDS

- **Systemic risks are considerable**: strong pressure from Central Banks and political authorities
  - Does it make sense to allow such a mountain no nominal contracts- should one not forbid cash settled CDS (derivatives)
- **G 20 and FSF**: reduce risk essentially by CCP
- **Central Counterparty** will reduce outstanding
  - Netting of positions can considerably reduce risk
  - See Lehman liquidation
  - Continuous netting needed: not on an x + 3 basis
CDS

- Controversy: one or several CCP? Competition!
- Industry: all in NY, DTCC subsidiary along with Warehouse
- The EU wants a European CCP for local CDSs
- Depend on which reference names: EU or US
  - Indexes
  - Single names: standardisation – isda proposal forthcoming

A cross system link US-EU would contribute to complexity
But efficient systems on both sides are needed
Links to Central Bank Money for payments
CDS

- Warehouse
- European “Warehouse” needed -
  ◆ registration, - safety of assets
  ◆ linked to CCP
  ◆ would deliver data for supervisory purposes
  ◆ would also make market more transparent- pricing for valuation.
The Present Supervisory Architecture

- Based on national competences: bottom up
- Coordination by mutual recognition, home-host arrangements and cooperation
- Has proved unsatisfactory: home host system has not worked in the crisis: ring fencing in some states
- New scheme needed
The New Supervisory Architecture

- Czech proposal
  - All financial business is local: to be put in a separate subsidiary with local supervision and fiscal support
- Home Host creates dangers for both home and host
- Double supervision, or gaps in the system
- Inefficient: increased cost, local regulation, no overall view.
A European Scheme?

- Many solutions possible
- Improve the present cooperation scheme
  - More room of the Committees
    - Soft instruments: name and shame, but too soft
  - Colleges: in good times ok, not in bad times
  - Home Host creates dangers for both home and host
    - Double supervision, or gaps in the system
- Improve on enforcement but how?
  - QMV – Mediation, Delegation of tasks
  - Not legally binding
  - No enforcement against sovereign states or their agencies
Institutional schemes

- Create a European Institution
- Based on Hub and Spoke formula: see ECB
  - Stronger central regulation, local implementation
  - Solves question of fiscal support:
    - Local supervisors represents the state and taxpayers
  - Enforceable central decisions against Local Supervisor
- Requires change of the Treaty
- Integrate 3 pillars? Banking, Insurance, Securities
  - Or two peaks: Dutch model.
Institutional scheme

- Incorporate prudential supervision in the ECB
  - Art 105(6) allows to do so by unanimous decision of council and decision of Comm and EP
  - Would not include insurance: art 105(6) excludes insurance
  - What with securities?: Conduct of business for all sectors
  - No fiscal backing
  - Unlikely except for macroprudential matters
    - Upgrading the macro-prudential function of the ESCB eg.in the Banking Supervisory Committee
Institutional scheme

- **European Agency for CESR**
  - Reluctance
    - Strong position of the Commission: members on the board, financing, budget, policies
- **Agencies have no regulatory powers**
  - Only: Individual decision making, e.g. aviation agency
  - Here: CRA’s, Clearing & settlement, UCITS, Prospectuses
    - Not optimal: CESR become competitor of its own members and creates distrust with its members
    - Does not solve the problem that is “regulation”
Next Step

- De Larosière Report
- Inter institutional Dialogue
- Agreement of the Member States
- Separate workstream from the G 20 – world wide basis
Developments in the collateral framework of the Eurosystem

Mark Büssing-Lörcks
Senior Economist, European Central Bank
Developments in the collateral framework of the Eurosystem

Meeting of the European Repo Council (ERC), February 25, 2009
Mark Büssing-Lörcks, European Central Bank
Amendments to the Eurosystem Collateral Framework – Permanent Measures I

- Technical refinements of risk control measures
  - Refinements to the valuation haircuts applied to marketable assets,
  - Broadening of the close link definition to include also “financial close links”, applicable to ABS,
  - Refinements to the credit assessment framework (ECAF),

- were announced in September 2008,
- were published in Nov. 2008 (Gen. Doc.),
- measures taken effect on 1 February 2009.
Amendments to the Eurosystem Collateral Framework – Permanent Measures II

• Complementation to technical refinements of risk control measures
  – For ABS:
    • AAA level rating at the time of issuance,
    • underlying pool should not consist of other ABSs or tranches thereof (no “re-packaging”).
  – For uncovered bank bonds:
    • Limits on the use of uncovered bank bonds,
  – were announced in February 2009,
  – took effect on 1 March 2009,
  – Grandfathering period: until 1 March 2010
Amendments to the Eurosystem Collateral Framework – Temporary Measures

1. Marketable debt instruments denominated in USD, GBP, JPY
2. Euro-denominated syndicated loans under UK law,
3. Debt instruments issued by credit institutions which are traded on accepted, non-regulated markets,
4. Guaranteed subordinated debt instruments,
5. Lowered credit rating threshold to BBB- (except ABS),

Measures
• were introduced in October/November 2008,
• remain into force until end of 2009,
• Measure 2. was terminated end of November 2008
Temporary Measures – Quantitative Impact

- The (nominal) value of eligible marketable collateral increased from about EUR 10 trillion in September 08 to EUR 11 trillion in November 08, i.e. by about 10%.

- The value increased further to EUR 12 trillion in February 09.

- The value of (eligible) non-marketable assets increased significantly due to the lowering of the credit threshold to BBB-.
Trends in Use of Collateral

• The value of total collateral used with Eurosystem increased strongly when full allotment policy - and temporary expansion of collateral - was introduced – by similar rates as outstanding credit from Eurosystem.

• In the last four weeks value of collateral in use decreased significantly (in particular ABS, uncovered bank bonds and government bonds):
  – reduction in outstanding credit from Eurosystem (widening of facility corridor)
  – higher haircuts (ABS, bank bonds) as of 1 February reduce market value after haircut
  – ABS cannot be used anymore by currency hedge counterparty and significant liquidity provider.
Trends in Use of Collateral

Shares of asset types

- Non-marketable assets
- Other marketable assets
- ABS
- Corporate bonds
- Covered bank bonds
- Uncovered bank bonds
- Regional government
- Central government

Year:
- 2004
- 2005
- 2006
- 2007
- Q1 2008
- Q2 2008
- Q3 2008

Percentage:
- 100%
- 90%
- 80%
- 70%
- 60%
- 50%
- 40%
- 30%
- 20%
- 10%
- 0%

David Rule
Chief Executive, International Securities Lending Association (ISLA)
TMPG Fails Recommendations for Cash and Repos in U.S. Treasury Securities
U.S. Treasury Fails During Fall 2008

• Settlement Fails in the U.S. Treasury market spiked to $5 trillion during October 2008 (see http://www.newyorkfed.org/markets/pridealers_failsdata.xls, week ended 15 October).

• A number of factors fueled the increase in fails: (i) very low rate environment (Target Fed Funds Rate of 1.50%); (ii) massive flight to the quality of government debt; and (iii) counterparty credit aversion as normal suppliers of securities pulled back after the Lehman bankruptcy fearing exposure to financial firms.

• Fails increased in every security across the curve including both on-the-runs and off-the-runs. This was unlike prior incidents of high fails where the fails were focused in a single issue (In Summer 2003, fails spiked in the on-the-run 10-year security but were largely unchanged in other securities.)
TMPG: Role and Mission

- **The Treasury Market Practices Group (TMPG)** is a group of market professionals committed to supporting the integrity and efficiency of the U.S. Government Treasury market.

- The TMPG is composed of senior business managers and legal and compliance professionals from securities dealers, banks and buy-side firms and is sponsored by the Federal Reserve Bank of New York.

- The TMPG meets periodically to discuss Treasury trading issues and promote best practices in Treasury cash, repo and related markets.
TMPG Fails Recommendations

• In November 2008 the TMPG, noting “widespread and persistent settlement fails”, recommended the following changes in market practices (see http://www.newyorkfed.org/tmpg/PR081112.pdf):
  – Financial penalty on fails
  – Margining of settlement fails
  – Bilateral cash settlement
  – Support development of broader multilateral netting solutions
• Fails penalty implementation is set for May 1, 2009. The other recommendations do not yet have implementation timelines or documentation recommendations.
TMPG Recommendation: Fails Penalty

• TMPG noted that in low rate environments, fails may tend to increase because sellers, under existing market conventions, can deliver securities after the originally scheduled settlement date at an unchanged invoice price, i.e., without incurring any penalty.

• The introduction of a dynamic fails penalty with a finite cap rate would remedy this issue and would provide an incentive for sellers to resolve fails promptly. In addition it may give beneficial owners of Treasury securities an opportunity to earn as much as the cap rate regardless of nominal interest rates.
TMPG Recommendation: Fails Penalty

• The basic TMPG recommendation is that the fails penalty be determined as follows:
  – On any cash or financing transaction that fails to settle on the originally scheduled settlement date, a penalty will be imposed equal to the greater of (a) 3 percent per annum minus the Fed Funds target rate at 5:00 p.m., EST on the business day prior to the originally scheduled settlement date, and (b) zero.

• Note that the fails penalty begins to accrue from the originally scheduled settlement date, i.e., there is not aging requirement.

• The fails penalty and the recommended trading practices are recommendations only and the adoption of the penalty and the practices by any market participant is strictly voluntary.
TMPG Recommendation: Fails Penalty

- Formula for calculation of fails penalty:
  \[ C = \frac{1}{360} \times 0.01 \times \max(3-R,0) \times P \]
  
  - \( C \) is the fails charge amount
  - \( R \) is the TMPG reference rate. Currently the reference rate is the Fed Funds Target at 5:00 p.m. EST on the business day prior to the failed settlement.
  - \( P \) is, generally, the amount of funds due from the non-failing party

- Daily fails charges for a particular counterparty will be accrued during a calendar month and billed no later than the 10\textsuperscript{th} business day of the following month to the counterparty owing the charges with payment due by the end of the following month.

- Fails charges apply only to delivery-vs.-payment or delivery-vs.-transfer transactions, not free deliveries.
Fails Penalty: Implementation

- The TMPG published an implementation timeline on January 5 (See http://www.newyorkfed.org/tmpg/pr090105c.pdf) establishing May 1 as the implementation date.

- SIFMA and the TMPG published a “Fails Charge Trading Practice” on January 15 in order to aid market participants in developing both the legal and operational infrastructure to implement the fails penalty. The Trading Practice (see http://www.newyorkfed.org/tmpg/pr090105c.pdf) provides:
  - More specificity concerning the calculation of the charge;
  - Implementation details of the accrual process and the billing process.
  - Details on application to common transaction types (cash, repos, sec lending, options, forwards).
  - Documentation recommendations
Fails Penalty: Documentation

• The Trading Practice supplies a form of notice (Annex A to the Trading Practice) that parties may use to inform counterparties that they intend to adopt the fails charge and that entering further transactions with them will be deemed agreement to the new terms. Counterparties are not required to sign or return the notice.

• The Trading Practice also provided suggested language to be used in all confirmations that the transaction is “Subject to US Treasury Securities Fails Charge Trading Practice Published by TMPG and SIFMA at http://www.sifma.org/capital_markets/docs/Fails-Charge-Trading-Practice.pdf.”
Fails Penalty: Other Implementation Milestones

• FICC (clearing corp) will make a rule filing to permit an automatic charge process for members of FICC (dealers). This rule filing is expected to be approved prior to May 1.

• Dealers are developing internal systems to track and accrue the fails charges. A number of vendors are preparing solutions.

• Buyside continues to work with custodians to develop processes for work flows, tracking and responsibilities.
The 16\textsuperscript{th} repo survey

Richard Comotto
Visiting Fellow, ICMA Centre
Survey overview

- Outstanding value of contracts at close on 10th December 2008
- 61 responses from 56 groups
- Respondents headquartered in 14 European countries, US, Japan
<table>
<thead>
<tr>
<th>Date</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>December 2008</td>
<td>EUR 4,633 billion</td>
</tr>
<tr>
<td>June 2008</td>
<td>EUR 6,504 billion</td>
</tr>
<tr>
<td>December 2007</td>
<td>EUR 6,382 billion</td>
</tr>
<tr>
<td>June 2007</td>
<td>EUR 6,775 billion</td>
</tr>
<tr>
<td>December 2006</td>
<td>EUR 6,430 billion</td>
</tr>
<tr>
<td>June 2006</td>
<td>EUR 6,019 billion</td>
</tr>
<tr>
<td>December 2005</td>
<td>EUR 5,883 billion</td>
</tr>
<tr>
<td>June 2005</td>
<td>EUR 5,319 billion</td>
</tr>
<tr>
<td>December 2004</td>
<td>EUR 5,000 billion</td>
</tr>
<tr>
<td>June 2004</td>
<td>EUR 4,561 billion</td>
</tr>
<tr>
<td>December 2003</td>
<td>EUR 3,788 billion</td>
</tr>
<tr>
<td>June 2003</td>
<td>EUR 4,050 billion</td>
</tr>
<tr>
<td>December 2002</td>
<td>EUR 3,377 billion</td>
</tr>
<tr>
<td>June 2002</td>
<td>EUR 3,305 billion</td>
</tr>
<tr>
<td>December 2001</td>
<td>EUR 2,298 billion</td>
</tr>
<tr>
<td>June 2001</td>
<td>EUR 1,863 billion</td>
</tr>
</tbody>
</table>
European Repo Council
16th European repo market survey
European Repo Council
16th European repo market survey

Source: FRBNY
Organic growth

- 54 respondents in last 3 surveys
  - year-on-year = -27.3%
  - H1 = -1.3%
  - H2 = -25.7%
European Repo Council
16th European repo market survey

- repo 49.9%, reverse repo 50.1%
- repo books: 18 expand, 41 contract
European Repo Council
16th European repo market survey

Counterparty analysis

- Direct: 42.2%
- Triparty: 9.4%
- Broker: 20.2%
- ATS: 28.2%
Counterparty analysis

European Repo Council
16th European repo market survey
European Repo Council
16th European repo market survey

Geographical analysis

- Anonymous: 17.6%
- Domestic: 31.3%
- Non-eurozone: 26.9%
- Eurozone: 24.1%
Geographical analysis

- Anon.
- Noneuro
- Euro
- Domestic
ATS geographical analysis (1)

- Anonymous ATS 79.6%
- Non-anonymous ATS 20.4%
ATS geographical analysis (2)

- cross EUR: 41.7%
- intra EUR: 16.7%
- domestic: 39.6%
- extra EUR: 1.9%
European Repo Council
16th European repo market survey

Currency analysis

- USD 9.6%
- GBP 13.0%
- EUR 70.6%
- other 6.8%
European Repo Council
16th European repo market survey

Currency analysis

[Chart showing percentage distribution of currency usage from Dec-01 to Dec-08. The chart indicates a significant portion of transactions are in EUR, with lesser amounts in other currencies such as USD and GBP.]
Currency analysis

**Main survey**
- EUR: 70.6%
- GBP: 13.0%
- USD: 9.6%
- Other: 6.8%

**Triparty**
- EUR: 76.4%
- GBP: 6.8%
- USD: 16.1%
- Other: 0.7%
European Repo Council
16th European repo market survey

Currency analysis --- triparty repos

June 2007

- USD: 44.6%
- EUR: 39.8%
- GBP: 10.7%
- Other: 4.8%

December 2007

- USD: 18.2%
- GBP: 17.0%
- EUR: 62.7%
- Other: 2.1%
Currency analysis --- triparty repos

June 2008
- USD: 17.3%
- GBP: 10.5%
- EUR: 71.2%
- Other: 1.0%

December 2008
- USD: 16.1%
- GBP: 6.8%
- EUR: 76.4%
- Other: 0.7%
European Repo Council
16th European repo market survey

Currency analysis

**Main survey**
- USD: 9.6%
- GBP: 13.0%
- other: 6.9%
- EUR: 70.5%

**ATS**
- CHF: 8.5%
- GBP: 6.0%
- other: 2.4%
- EUR: 83.1%
Collateral analysis

- Japan: 2.9%
- US: 2.9%
- UK: 12.9%
- other EUR: 8.7%
- BE: 2.7%
- ES: 4.9%
- FR: 10.1%
- IT: 12.2%
- DE: 29.6%
- etc: 13.3%
Collateral analysis
Collateral analysis

**Main survey**
- DE: 29.6%
- other EU: 17.6%
- UK: 12.9%
- FR: 10.1%
- other: 17.5%

**Triparty**
- DE: 23.1%
- IT: 34.1%
- UK: 9.5%
- FR: 10.3%
- other EU: 5.7%
- other: 17.3%
European Repo Council
16th European repo market survey

Collateral analysis --- triparty repos

June 2007

- DE: 11.7%
- IT: 3.1%
- FR: 7.3%
- UK: 7.7%
- other: 51.8%
- other EU: 18.4%

December 2007

- DE: 12.3%
- IT: 3.4%
- FR: 7.4%
- UK: 9.1%
- other: 46.4%
- other EU: 21.4%
Collateral analysis --- triparty repos

**June 2008**
- DE: 17.1%
- IT: 7.2%
- FR: 9.7%
- UK: 11.7%
- other EU: 33.4%
- other: 21.0%

**December 2008**
- DE: 23.1%
- IT: 5.7%
- FR: 9.5%
- UK: 10.3%
- other EU: 34.1%
- other: 17.3%
Collateral analysis

other EU 16.4%

EU govis 83.6%
European Repo Council
16th European repo market survey

Collateral analysis

![Collateral Analysis Chart](chart.png)
Collateral analysis

Main survey
- EU govis: 83.6%
- Other EU: 16.4%

Triparty
- EU govis: 41.7%
- Other EU: 58.3%
European Repo Council
16th European repo market survey

Collateral analysis --- triparty repo

June 2007
- EU govis 43.6%
- other EU 54.4%

December 2007
- EU govis 43.8%
- other EU 56.2%
Collateral analysis --- triparty repo

**June 2008**
- EU govis: 33.7%
- Other EU: 66.3%

**December 2008**
- EU govis: 41.7%
- Other EU: 58.3%
European Repo Council
16th European repo market survey

Maturity analysis

- 1D: 18.3%
- 1W: 17.2%
- 1M: 19.9%
- 3M: 18.9%
- 6M: 7.6%
- 12M: 5.6%
- +12M: 1.8%
- fd-fd: 4.5%
- open: 6.1%
Maturity analysis

European Repo Council
16th European repo market survey
Maturity analysis

- 1D
- 1W
- 1M
- 3M
- 6M
- +6M
- open
- Line 9
European Repo Council
16th European repo market survey

Maturity analysis

- 1D, 1W, 1M, 3M, 6M, +6M, fd-fd, open
- Main
- Triparty

Bar chart showing maturity analysis with percentages for different maturities.
European Repo Council
16th European repo market survey

Maturity analysis --- triparty repos

![Bar chart showing maturity analysis for different periods and dates.](chart.png)
European Repo Council
16th European repo market survey

Maturity analysis

- 1D
- 1W
- 1M
- 3M
- 6M
- +6M
- fd-fd
- open

Red: main
Green: ATS
Maturity analysis --- ATS
Maturity analysis

- 1D: 40%
- 1W: 45%
- 1M: 25%
- 3M: 30%
- 6M: 10%
- +6M: 15%
- fd-fd: 20%
- open: 5%
European Repo Council
16th European repo market survey

Maturity analysis

- ATS
- Voice broker
Rate analysis

- Fixed: 85.6%
- Open: 5.1%
- Floating: 9.3%
European Repo Council
16th European repo market survey

Rate analysis

[Chart showing rate analysis from Dec-01 to Dec-08 with different colors for open, floating rate, and fixed rate categories.]

Legend:
- open
- floating rate
- fixed rate
Product analysis

- Lending: 12.5%
- Repo: 87.5%
Date of next survey

10th June 2009
Results of the elections to the European Repo Committee

Godfried De Vidts
Chairman, European Repo Council
1. Tony Baldwin, Daiwa Securities SMBC Europe Ltd
2. Stefano Bellani J. P. Morgan Securities Ltd., London
4. Eduard Cia UniCredit Markets & Investment Banking
5. Herminio Crespo Urena Caja de Madrid, Madrid
8. Johan Evenepoel Dexia Bank Belgium NV/SA, Brussels
10. Thomas Hansen Credit Suisse, London
11. Eric Lepore Deutsche Bank AG, London branch
15. Jessica McDermott Merrill Lynch International (MLI), London
17. Dina Noelle Rabobank, London
18. Simon Parkins BNP Paribas, London branch
20. Luis Soutullo Confederación Española de Cajas de Ahorros (CECA), Madrid
21. Simon Tims UBS AG, Zurich
22. Stefaan Van de Mosselaer Fortis Bank, Brussels
Next meetings
Professional repo and collateral management course

25-26 March 2009
Hotel Metropole, Brussels

www.icmagroup.org

Sponsored by: In Association with:
EONIA Futures
Paul MacGregor
Business Development Director, Liffe
One Month Eonia Futures &
Three Month Eonia Swap Index Futures

European Repo Council AGM
February 25 2009
Developments in Overnight lending vs. Term lending

• During 2008, NYSE Liffe researched demand amongst short term money market traders, for a centrally cleared very near term interest rate futures contract

• Customers told us OTC trading in Libor / OIS spread had grown exponentially, however recent flows have slowed during the current uncertainty

• There has been a sustained change in the relationship between the Eonia and Euribor, becoming more volatile since summer 2007, representing an interesting trading opportunity

• NYSE Liffe now offers a centrally cleared version of the Libor / OIS spread, in order to free up capital and reduce counterparty risk
The creation of a Euribor and Eonia ‘basis’

- 3 Month Euribor
- 3 Month Eonia Swap

02/01/2007 to 02/01/2009
Launched 16-Jun-2008: One Month Eonia Futures

- Referenced to EONIA, the Euro Over-Night Index Average rate, calculated by European Central Bank each night as weighted average of all overnight unsecured lending transactions undertaken in the inter-bank market.

- Eonia fixing is published daily between 18:45 and 19:00 (CET) to Reuters pages: <EONIA=> and <EONIARECAP>.


- Note: Last Trading Day for One Month Eonia futures is the last day of the relevant ECB maintenance period, as per futures convention.
Launched 16-Jun-2008: Three Month Eonia Swap Index Futures

- The Eonia Swap Index is quoted on a spot basis (T+2) by a representative panel of prime banks, actively providing prices in the EONIA swap market (many of which contribute to the Euribor benchmark)

- The Eonia Swap Index reference rates are calculated and published by Reuters on page: <EONIAINDEX3M=

- The Index has been crucial to the development of the Eonia Swap FRA and Eonia Index OTC Option markets

- *Three Month Eonia Swap Index future complements NYSE Liffe’s existing, highly liquid, Three Month Euribor futures contract, as the contract specifications match exactly*
Who are NYSE Liffe’s Eonia futures targeted at?

• Traders who have an underlying need for cash in the near term and who need to use short term futures as a risk management tool, e.g.
  ✓ Repo and Reverse Repo traders
  ✓ Short Term Money Market Traders
  ✓ Treasury Desks and Cash Managers
  ✓ Short Term Swaps traders

• Proprietary, Algorithmic and Hedge Fund traders who see an opportunity to trade the spread between the Eonia Swap Index and Euribor

• Customers may choose to take advantage of the spread between the Euribor future to the Eonia Swap Index future, using the Basis Trade Facility on LIFFE CONNECT®
Viewed by futures delivery month, since launch

- Sep-08 Spread
- Dec-08 Spread
- Mar-09 Spread
- Jun-09 Spread
- Sep-09 Spread
- Dec-09 Spread
- Euribor-Eonia 3-Month (Generic Futures Spread)
One Month EONIA Indexed Futures & Three Month EONIA Swap Index Futures

Aggregate Volume & Open Interest

- Eonia 3-Month Volume
- Eonia 1-Month Volume
- Eonia 3-Month OI
- Eonia 1-Month OI

Chart showing volume and open interest for One Month EONIA Indexed Futures and Three Month EONIA Swap Index Futures from June 2008 to January 2009.
Future Development of NYSE Liffe Eonia Futures

- ‘Young’ futures contracts have seen a rapid liquidity draw-down following the Lehman default.

- However, we intend to support and invest in the 3-month Eonia Swap Index future, as customers have asked us to maintain and grow the product.

- Short-term development plans for the product are:
  
  ✓ Reduce Block Trade Thresholds and promote Asset Allocation

  ✓ Develop an Inter-Commodity Spread with Euribor futures

  ✓ Introduce a “Primary Market Making” scheme
Wholesale Trading Facilities

• Block Trade Facility – Minimum Volume Thresholds reduced by 50%

<table>
<thead>
<tr>
<th>Contract</th>
<th>Contract Month</th>
<th>Mini. Volume Threshold (lots)</th>
<th>New Mini. Volume Threshold (lots) as of 1 Mar 2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>One Month EONIA</td>
<td>Outrights in all months</td>
<td>500</td>
<td>250</td>
</tr>
<tr>
<td></td>
<td>Strategies involving all months</td>
<td>750</td>
<td>375</td>
</tr>
<tr>
<td>EONIA Swap Index</td>
<td>Outrights in all months</td>
<td>500</td>
<td>250</td>
</tr>
<tr>
<td></td>
<td>Strategies involving all months</td>
<td>750</td>
<td>375</td>
</tr>
</tbody>
</table>

• Asset Allocation Facility – allows OTC inter-contract spread trading with other NYSE Liffe contracts, e.g. Eonia vs. Euribor

• Basis Trade Facility – allows inter-contract spread trading with other exchange-traded (non-NYSE Liffe) interest rate contracts
Euribor / Eonia Inter-Commodity Spread (ICS)

• In February, NYSE Liffe made available a new strategy type on LIFFE CONNECT®, the ICS

• Trading the ICS allows a simultaneous long / short position to be taken in Euribor and the Eonia Swap Index futures, without legging risk

• The ICS is supported by Designated Market Makers (DMMs) to provide additional liquidity

• *NYSE Liffe is providing a 100% fee rebate to both the Euribor and Eonia legs of the ICS, to registered Liquidity Providers*
Euribor / Eonia ICS – trading example

- The Euribor / three month EONIA spread trades at a price of -0.770. The reference price for the Euribor is 98.255 and the reference price for the three month EONIA swap is 99.035. The difference between the 2 prices is -0.780, and the difference between this and the price the spread traded at (-0.770) is 0.010. This can therefore be equally distributed between each leg and prices allocated as below:

  - Euribor \( 98.255 + 0.005 = 98.260 \)
  - Eonia \( 99.035 - 0.005 = 99.030 \)

- If the spread traded at a price of -0.775, then the three month EONIA spread will be adjusted as below:

  - Euribor \( 98.255 + 0.005 = 98.260 \)
  - Eonia \( 99.035 - 0.010 = 99.025 \)
Euribor / Eonia Inter-Commodity Spread (ICS): free real-time prices
Three Month Eonia Swap Primary Market Making Scheme ("PMM")

- In December, we received regulatory approval to open negotiations for a new kind of “Primary Market Making” scheme

- A firm who signs up to be a “Primary Market Maker” would have higher obligations than a regular market making firm

- In return, they are entitled to a revenue share of up to 20% of net trading revenues, locked in for 5 years

- **NYSE Liffe is currently in negotiations with a number of parties in order to secure two Primary market makers**
Summary

- 1-month Eonia and 3-month Eonia Swap Index futures launched by NYSE Liffe, 16-6-08

- 3-month Eonia Swap Index future has gained some liquidity; however market is generally nervous of ‘new’ futures contracts in the current environment

- NYSE Liffe is developing the product through
  - Inter-contract spread facilities with Euribor,
  - Rebating 100% of trading fees via the spread,
  - Reducing block trade thresholds
  - Increased Market Making obligations in return for shared revenue
Appendix

Full Contract Specifications

Quote Vendor Codes

LCH-C Cross Margining
# One Month EONIA-Indexed Future Contract Spec

<table>
<thead>
<tr>
<th><strong>Unit of Trading</strong></th>
<th><strong>€3,000,000</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Delivery Months</strong></td>
<td>Consecutive delivery months each covering a European Central Bank (ECB) Reserve Maintenance Period. The number of available delivery months will be limited to the number of Maintenance Periods for which dates have been published by the European Central Bank. A maximum of twelve and a minimum of three consecutive delivery months will be available for trading.</td>
</tr>
<tr>
<td><strong>Quotation</strong></td>
<td>100.00 minus rate of interest</td>
</tr>
<tr>
<td><strong>Minimum Price Movement (Tick Size and Value)</strong></td>
<td>0.005 (€12.50)</td>
</tr>
<tr>
<td><strong>Last Trading Day</strong></td>
<td>18:00 hours (CET) Last day of ECB Reserve Maintenance Period</td>
</tr>
<tr>
<td><strong>First EONIA Accrual Day</strong></td>
<td>First day of ECB Reserve Maintenance Period</td>
</tr>
<tr>
<td><strong>Last EONIA Accrual Day</strong></td>
<td>Last Trading Day</td>
</tr>
<tr>
<td><strong>EDSP Published</strong></td>
<td>No later than 10:00 on the business day following the Last Trading Day</td>
</tr>
<tr>
<td><strong>Delivery Day</strong></td>
<td>Two business days after the Last Trading Day</td>
</tr>
<tr>
<td><strong>Trading Hours</strong></td>
<td>08:00 – 19.00 (CET)</td>
</tr>
</tbody>
</table>
One Month EONIA-Indexed Future EDSP

Exchange Delivery Settlement Price (EDSP):

Based on EONIA (Euro Over-Night Index Average) as published by the ECB in respect of each business day, the EDSP Rate represents the effective rate of interest achieved by reinvesting at EONIA for each day of the accrual period of the contract. The following formula shall be applied:

\[
EDSP\ Rate = \left[\frac{360}{N} \left( \prod_{i=1}^{x} \left( 1 + \frac{E_i \times d_i}{360} \right) - 1 \right) \right] \times 100
\]

where:
\( E_i \) = EONIA fixing on the \( i^{th} \) day of the accrual period
\( d_i \) = the number of days that the value \( E_i \) is applied
\( x \) = the number of EONIA fixings used in the Accrual Period
\( N \) = the total number of days for which the \( x \) fixings are applied
### Three Month EONIA Swap Index Futures Contract Spec

<table>
<thead>
<tr>
<th><strong>Unit of Trading</strong></th>
<th>€1,000,000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Delivery Months</strong></td>
<td>Mar, Jun, Sep and Dec, and four serial months such that eight delivery months are available for trading with the nearest six delivery months being consecutive calendar months.</td>
</tr>
<tr>
<td><strong>Quotation</strong></td>
<td>100.00 minus rate of interest</td>
</tr>
<tr>
<td><strong>Minimum Price Movement (Tick Size and Value)</strong></td>
<td>0.005 (€12.50)</td>
</tr>
<tr>
<td><strong>Last Trading Day</strong></td>
<td>11:00 hours Two business days prior to the third Wednesday of the delivery month</td>
</tr>
<tr>
<td><strong>Delivery Day</strong></td>
<td>First business day after the Last Trading Day</td>
</tr>
<tr>
<td><strong>Trading Hours</strong></td>
<td>08:00 – 19.00 (CET)</td>
</tr>
</tbody>
</table>

**Exchange Delivery Settlement Price (EDSP):** Based on the Three Month EONIA Swap Index, as sponsored by the European Banking Federation (EBF), at 11:00 hours CET on the Last Trading Day. The settlement price will be 100.00 minus the Three Month EONIA Swap Index level rounded to three decimal places. Where the EDSP Rate is not an exact multiple of 0.001, it will be rounded to the nearest 0.001 or, where the EDSP Rate is an exact uneven multiple of 0.0005, to the nearest lower 0.001.

**Contract Standard:** Cash settlement based on the Exchange Delivery Settlement Price.
Quote Vendor Codes

One Month Eonia
• Reuters  0#EON:
• Bloomberg  OMA <Comdty> CT <Go>

Three Month Eonia Swap Index
• Reuters  0#EO3:
• Bloomberg  TMOA <Comdty> CT <Go>
Reminder: Cross Margining Benefits

• One Month Eonia and Three Month Eonia Swap Index futures are eligible for cross-margining with other NYSE Liffe STIR futures

• Margin offsets between Three Month Euribor and Eonia futures are as high as 65%

• Details can be found on the LCH.Clearnet web site:

  www.lchclearnet.com/risk_management/ltd/margin_rate_circulars
Global Managed Funds
Kathryn Kerle
Vice President, Senior Credit Officer, Moodys
Repo in European money market funds: Trends and outlook

Presented by:
Kathryn Kerle,
Team Leader
Global Managed Investments Group

February 25, 2009

Moody’s Investors Service
Agenda

- Moody’s fund ratings
- Trends in asset allocation of European money market funds
- Outlook for repo in European money market funds
Moody’s Managed Funds offices

- UK
- US
- Mexico
- Brazil
- Taiwan
Global Managed Investments ratings
Breakdown by region

- USA: 57%
- Europe: 26%
- Latin America: 14%
- Asia: 3%

Moody's Investors Service
Global Managed Investments ratings
Breakdown by rating type

- 66% Open-End Funds (400 MMFs / 238 BFMs)
- 31% Closed-End Funds
- 1% Pension funds
- 1% Equity funds
- 0% iMQ
Reverse repo and European money market funds

- Emergence of first European Treasury-style money market funds
- Indications of increased interest in reverse repo as an asset class in Euro and Sterling money market funds
- Increased investment in reverse repo in US dollar money market funds
- Collateral limited to Aaa-rated government securities.
Trends in repo allocation February 2008 - January 2009 / Percent of total assets under management

Source: iMoney Net
Trends in repo allocation February 2008 - January 2009 / Percent of assets under management

Source: iMoney Net
Trends in repo allocation February 2008 - January 2009 / Absolute amount of investment ($ millions)

Source: iMoney Net
Rated European government funds

- Aviva Sterling Government Liquidity Fund
- BGI Euro Government Liquidity Fund
- BGI Sterling Government Liquidity Fund
- Euro Government Liquidity Fund
- Sterling Gilt Liquidity Fund
- Goldman Sachs Euro Government Liquidity Reserves Fund
- Goldman Sachs Sterling Government Liquidity Reserves Fund
Repo: credit considerations

- Counterparty credit quality
- Creditor’s ability to perfect a security interest
- Type of collateral
- Amount of collateral
Outlook for repo in European money market funds

- Outlook is for continued growth
  - Risk aversion on the part of investors
  - Risk aversion on the part of fund sponsors
  - Resolution of many legal issues
  - Improved returns profile

- Caveats
  - Increased counterparty risk
  - Untested legal framework

David Rule
Chief Executive, International Securities Lending Association (ISLA)
TMPG Fails Recommendations for Cash and Repos in U.S. Treasury Securities
U.S. Treasury Fails During Fall 2008

- Settlement Fails in the U.S. Treasury market spiked to $5 trillion during October 2008 (see http://www.newyorkfed.org/markets/pridealers_failsdata.xls, week ended 15 October).

- A number of factors fueled the increase in fails: (i) very low rate environment (Target Fed Funds Rate of 1.50%); (ii) massive flight to the quality of government debt; and (iii) counterparty credit aversion as normal suppliers of securities pulled back after the Lehman bankruptcy fearing exposure to financial firms.

- Fails increased in every security across the curve including both on-the-runs and off-the-runs. This was unlike prior incidents of high fails where the fails were focused in a single issue (In Summer 2003, fails spiked in the on-the-run 10-year security but were largely unchanged in other securities.)
TMPG: Role and Mission

• The Treasury Market Practices Group (TMPG) is a group of market professionals committed to supporting the integrity and efficiency of the U.S. Government Treasury market.
• The TMPG is composed of senior business managers and legal and compliance professionals from securities dealers, banks and buy-side firms and is sponsored by the Federal Reserve Bank of New York.
• The TMPG meets periodically to discuss Treasury trading issues and promote best practices in Treasury cash, repo and related markets.
TMPG Fails Recommendations

• In November 2008 the TMPG, noting “widespread and persistent settlement fails”, recommended the following changes in market practices (see http://www.newyorkfed.org/tmpg/PR081112.pdf):
  – Financial penalty on fails
  – Margining of settlement fails
  – Bilateral cash settlement
  – Support development of broader multilateral netting solutions

• Fails penalty implementation is set for May 1, 2009. The other recommendations do not yet have implementation timelines or documentation recommendations.
TMPG Recommendation: Fails Penalty

- TMPG noted that in low rate environments, fails may tend to increase because sellers, under existing market conventions, can deliver securities after the originally scheduled settlement date at an unchanged invoice price, i.e., without incurring any penalty.

- The introduction of a dynamic fails penalty with a finite cap rate would remedy this issue and would provide an incentive for sellers to resolve fails promptly. In addition it may give beneficial owners of Treasury securities an opportunity to earn as much as the cap rate regardless of nominal interest rates.
TMPG Recommendation: Fails Penalty

• The basic TMPG recommendation is that the fails penalty be determined as follows:
  – On any cash or financing transaction that fails to settle on the originally scheduled settlement date, a penalty will be imposed equal to the greater of (a) 3 percent per annum minus the Fed Funds target rate at 5:00 p.m., EST on the business day prior to the originally scheduled settlement date, and (b) zero.

• Note that the fails penalty begins to accrue from the originally scheduled settlement date, i.e., there is not aging requirement.

• The fails penalty and the recommended trading practices are recommendations only and the adoption of the penalty and the practices by any market participant is strictly voluntary.
TMPG Recommendation: Fails Penalty

• Formula for calculation of fails penalty:
  
  \[ \text{C} = \frac{1}{360} \times 0.01 \times \max(3-R,0) \times P \]

  • \( \text{C} \) is the fails charge amount
  • \( R \) is the TMPG reference rate. Currently the reference rate is the Fed Funds Target at 5:00 p.m. EST on the business day prior to the failed settlement.
  • \( P \) is, generally, the amount of funds due from the non-failing party

• Daily fails charges for a particular counterparty will be accrued during a calendar month and billed no later than the 10th business day of the following month to the counterparty owing the charges with payment due by the end of the following month.

• Fails charges apply only to delivery-vs.-payment or delivery-vs.-transfer transactions, not free deliveries.
Fails Penalty: Implementation

• The TMPG published an implementation timeline on January 5 (See [http://www.newyorkfed.org/tmpg/pr090105c.pdf](http://www.newyorkfed.org/tmpg/pr090105c.pdf)) establishing May 1 as the implementation date.

• SIFMA and the TMPG published a “Fails Charge Trading Practice” on January 15 in order to aid market participants in developing both the legal and operational infrastructure to implement the fails penalty. The Trading Practice (see [http://www.newyorkfed.org/tmpg/pr090105c.pdf](http://www.newyorkfed.org/tmpg/pr090105c.pdf)) provides:
  – More specificity concerning the calculation of the charge;
  – Implementation details of the accrual process and the billing process.
  – Details on application to common transaction types (cash, repos, sec lending, options, forwards).
  – Documentation recommendations
Fails Penalty: Documentation

• The Trading Practice supplies a form of notice (Annex A to the Trading Practice) that parties may use to inform counterparties that they intend to adopt the fails charge and that entering further transactions with them will be deemed agreement to the new terms. Counterparties are not required to sign or return the notice.

• The Trading Practice also provided suggested language to be used in all confirmations that the transaction is “Subject to US Treasury Securities Fails Charge Trading Practice Published by TMPG and SIFMA at http://www.sifma.org/capital_markets/docs/Fails-Charge-Trading-Practice.pdf.”
Fails Penalty: Other Implementation Milestones

• FICC (clearing corp) will make a rule filing to permit an automatic charge process for members of FICC (dealers). This rule filing is expected to be approved prior to May 1.

• Dealers are developing internal systems to track and accrue the fails charges. A number of vendors are preparing solutions.

• Buyside continues to work with custodians to develop processes for work flows, tracking and responsibilities.
ERC Annual General Meeting
Wednesday, February 25, 2009