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Is T2S on track?

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Ladies and gentlemen,

I am very happy that the ECB and the Commission have been able to organise this conference. I have been asked to tell you whether T2S is on track. I will answer this question in the end. My purpose today is clearly not to summarise the technical design of T2S; if you want to know more on this aspect of the project, I invite you to read the executive summary of the draft user requirements document that you can easily find on our website. I would like, instead, to address the following paradox: why is it not easier to "sell" T2S given that, as it was nicely put, in a bilateral discussion, by an American banker, "everybody knows that there is a business case for a project which consolidates many IT platforms and provides a single interface to all European CSDs".

I think the first reason is to be found in the origins of T2S. T2S is clearly one of the most powerful tools to integrate post-trading activities in Europe. But many of you know that the origin of T2S was not directly linked to this objective, but rather to an internal debate within the Eurosystem on whether or not the integrated model was acceptable. In France (and in the United Kingdom) the integrated model has been in existence for several years, which means that the Banque de France agreed to outsource the technical operation of some of its accounts to Euroclear France, so that Euroclear France could move central bank money from one of its members to another as payment for delivery of securities. In Belgium and in the Netherlands, the national central banks (NCBs) decided to do the same. As the integrated model is considered more efficient, CSDs in other countries of the euro area asked “their” central banks to outsource cash accounts onto the CSD platform as well, in order to maintain a level playing-field.

The Eurosystem had a long and intensive discussion on whether to expand the integrated model in this way. Some perceived financial stability concerns in outsourcing central bank accounts to a private entity, and concluded that the integrated model should be abandoned where it existed or was planned. Others favoured the generalisation of the integrated model for efficiency reasons. My team was asked to find a technical solution to a problem which was deeply rooted in the fundamental objectives of central banking.

The solution was obvious, but rather revolutionary. We should pay tribute to Marc Bayle, now the project manager for T2S, for thinking of it. If central bank accounts should not be outsourced, and the integrated model is more efficient, then it is logical from both a risk and an economic perspective to in-source the CSDs’ securities accounts into the central bank IT environment. Marc also invented the name TARGET2-Securities, to indicate that the idea was not unlike Fedwire Securities – the system run by the Federal Reserve which settles US government and other bonds, closely linked to the Federal Reserve’s RTGS system for wholesale dollar payments.

In fact, it soon became clear that the project should differ in one important respect from Fedwire Securities. We received a very strong message from the market: “Your project has no value if you add a 26th platform to the 25 which already exist; but if you replace all of them with a single one, then your project has tremendous value”. In other words, unlike Fedwire Securities, the T2S platform needed to cover all securities.

Moreover, we in the Eurosystem never had the intention of replacing the CSDs – we only wanted to offer a technical outsourcing solution for their settlement engines. Unlike Fedwire Securities, T2S will not be a fully-fledged CSD; CSDs will continue to hold all accounts for users of T2S settlement, and to provide custody and issuing services, as well as collateral management and stock-borrowing facilities. The Eurosystem does not have expertise in these fields: they do not lie within our legal competence, nor does T2S need to offer them in order to deliver to market users the prize of integration across Europe.

I now realise that we were like Christopher Columbus looking for India and discovering America. We were looking for another route to safe and efficient integrated securities settlement, and we discovered T2S! Today, the reason why T2S was invented matters much less than the reason which now justifies its existence: European integration. But I acknowledge that the message is not easy to communicate

– even though we transmit it rather a lot. Our announcement of the concept in July 2006 came as a surprise to many, including the CSDs who are the ones most directly affected by it. We came straight out of our internal debate and did not consult sufficiently; I believe we have learnt that lesson, and I hope you will agree with my assessment that market users now feel that our thinking is both extremely transparent and very much affected by the generous and frank feedback we receive.

The underlying market demand for financial market integration is not new. Integration is one of those magic words that everybody uses but rarely defines. For me, integration means contributing to a genuine single market for securities in three complementary ways. First, thanks to T2S and the Code of Conduct, there will be enhanced competition to provide asset servicing for the securities held in a single pool in T2S. Second, this competition will create additional pressure for harmonisation in the many areas covered by the Giovannini work. Third, addressing those major sources of cost will greatly increase liquidity and choice for savers and borrowers alike, and lead to higher market volumes which will in turn create new opportunities for intermediaries to improve their economies of scale and develop new offerings. This is the world we need to move rapidly towards. T2S is a vital ingredient in such a policy.

Various private sector initiatives have already gone in this direction, especially in the nine years after the creation of the. The most successful of these is being led by Euroclear, which has made excellent progress in harmonisation across five important EU markets. However, it had become clear that full European consolidation through private sector initiatives would take decades to be completed, because of various rivalries: financial centres, corporate interests, even personal incompatibilities. Europe very often appears overseas as a collection of tribes more interested in fighting against each other than in building something together. We should remember what Caesar and his successors did with the tribes in Gaul – and then in Germany, Spain, even Britain…

Europe needs a solution in years, not centuries!

T2S is a truly European project, led by an institution, the Eurosystem, which is authoritative, country-neutral and not for profit. These are, of course, important characteristics for the successful creation of a single, safe Europe-wide infrastructure. It has EU-wide support from policy bodies.

The European Commission, which was informed of the project just a few days before it was announced, was immediately supportive.

The European Parliament asked for reassurance in relation to whether a public authority should lead such a project, and whether the ECB was not overstretching its mandate.

The EU Council asked about a possible widening of the gap between the euro area and the rest of the EU.

But six months after the announcement of the project, it was clear that the three European law-making bodies had understood our project and were supporting it.

With market participants, the situation was more nuanced. The CSDs were, of course, the most affected. On the one hand, our project would help them to offer a better service to their customers but, on the other hand, it would cut their operational responsibilities, their revenues and possibly also their staff needs. So, it would have been naive to believe that they would immediately embrace this project with enthusiasm.

At the risk of upsetting my colleagues in the Eurosystem, I think it is fair to compare the reaction of the CSDs in 2006 with their own attitude in 1999 when, in a public speech, I called for the consolidation of the TARGET technical platforms. At the beginning only one NCB supported me, and that was because it was convinced that its technical platform would be adopted as the European platform. All the others were against the idea, with all the types of argument that you find today in some CSD comments on T2S: Europe is too diverse, the project will be too complex, too risky, too costly, etc. It took time for the idea to mature. In the end, all NCBs decided to join TARGET2, although, like the CSDs today, they had the possibility to opt out. The friendly pressure of their users played an important role. Today, I am not aware of any NCB which regrets TARGET2. I would even say that they are, rightly, proud of the success of our common endeavour.

Hence this message to my friends in the CSDs: I understand your hesitation, and I can easily understand how I would feel if I were in your position. But the more you accept that consolidation and harmonisation will inevitably happen in a context of European integration, and the more you think about how your CSD can deliver added value to your clients in the much larger and busier markets which will result, the more enthusiastic you will become about your role in using T2S in this fundamental and necessary change.

I look forward to the months ahead, when we will be able to work constructively with all European CSDs in order to build the future settlement engine of Europe, made possible only by the Eurosystem and the CSDs working in happy symbiosis. Some CSD officials are already in this mindset. I am sure the others will follow.

I’d now like to turn to the banks’ reactions. Banks are cold-blooded entities; sooner or later, in the context of their eventual bottom line, I am convinced that they will realise how much T2S can benefit them. But banks are nothing without bankers. And since the latter are human beings, the way they reacted, especially at the beginning, in some cases, appeared to me to be linked more to their own cultural environment than to the long-term interests of their institutions.

Let me explain. In considering the reactions to T2S, I noted differences between three main groups: the euro area bankers, the US bankers and the London bankers.

Of course, this is an over-simplification. First, because there are bankers from elsewhere – from Sweden or Switzerland, for example. But also because some bankers are linked to several constituencies: for example, some of them are citizens of a continental European country, working for an American bank in London. And of course, each individual is different and may have a personal reaction which is different from that of the group to which he or she belongs. But with these reservations, let me tell you how I might caricature somewhat bankers' reactions.

The typical euro area banker was very quickly in favour of the project. For him or her, consolidating 20 or more IT platforms into one makes sense and one does not need to be an IT expert to judge that the project brings value for the users. Moreover, for them, the success of TARGET2 was a clear indication that the Eurosystem has the technical competence and the political drive to conduct the project. The typical euro area banker trusts the Eurosystem, with regard to monetary policy and market infrastructures as well. My own conclusion is that if TARGET2 exists today, and if T2S exists five years from now, it is because this group of bankers convinced the NCBs to build TARGET2, and will convince CSDs to build T2S.

The typical US banker also endorsed T2S rather quickly. He or she likes the idea of simplifying access to European markets, some of which still appear very "exotic". Moreover, the typical US banker tends to consider that Europe is now consolidating its infrastructure, in the same way that the United States did 30 years ago. His or her vision is that the Eurosystem is in fact building "the DTC of Europe". I have already explained that this is not fully correct in technical terms. Politically, it is a bit simplistic, but not fundamentally wrong. The US banker is only worried because the typical London banker is sceptical, which gives him (or her) the feeling that he may have missed something. Europe is so complex !

The typical London banker remains – like the British voter – sceptical. London matters because it generates a very large part of the securities settlements in Europe. I have asked myself quite often why the typical London banker was so positive when Euroclear proposed to integrate some European markets, but is so sceptical when the Eurosystem proposes to integrate them all.

I think the most likely answer is that the typical London banker has difficulty in accepting that public authorities should ever intervene. They believe – with some justification – that there are plenty of examples of bad projects and bad project management in the public sector (but are there none in the private sector?). However, the typical London banker likes the way the Bank of England rescued the City from the Taurus project, and they can understand that the Eurosystem may be the only agent that could achieve rapid integration, by introducing T2S. But he/she would feel reassured if the Eurosystem promised to sell the platform to the private sector once it is in operation. However, there is a central banking constraint; we will not be able to do this because nobody wants to re-open the debate on the integrated model…

London bankers also like user governance. This is commonly regarded in the Anglo-Saxon markets as the best way of controlling powerful financial infrastructure which is not subject to competitive pressure to keep prices down, and to innovate only when the users are ready for the next step. I believe that the not-for-profit principle of T2S and the typical frugality of central bankers should be borne in mind! Accountability and sensitivity to market needs are addressed by frequent meetings of a large and vocal advisory group, by being receptive to ideas and criticism, and by us publishing our papers in great detail and rapidly.

Finally, they may perceive another governance problem: the ultimate decision-making body for T2S is the Governing Council of the ECB, in which the United Kingdom is not represented. I think it would be wrong to think that the Governing Council would take major cost or development decisions without considerable consultation and very careful consideration – which would include authorities in non-euro area countries. The interest of the ECOFIN Council in this project should be reassuring in this respect.

My message for the London bankers is twofold.

First, please do not hesitate to make suggestions concerning the future governance of T2S. Our framework entails a number of constraints which are unavoidable; however, they do not prevent the voice of London from being heard, as indeed it has been up to now. It seems to me that the way we have prepared the user requirements of T2S shows that our model leaves a lot of room for users to play a crucial role in the governance. If you feel that more should be done to ensure better governance, tell us. The definitive governance of T2S will not be decided until next year.

My second message to my London friends is that they should also consider what they would lose if T2S does not go forward: a single interface to all European markets, and a significant driving force towards harmonisation. T2S could, indeed, be the decisive factor in lifting many of the Giovannini barriers.

Before I finish my speech, I would like to come back to the original question: is T2S on track? My answer is: yes, definitely. We have received almost 70 responses to our public consultation on the draft user requirements document, involving more than 2,500 comments. Our team has already reviewed all of them. Many just require clarifications. The most difficult ones will be discussed in our contact groups with market participants. But I can already tell you that none of the comments really constitutes a “show stopper”. T2S already exists – on paper, of course, but its life has begun.

We are also gathering figures from market participants concerning the economic impact assessment and I can already tell you that a positive impact assessment will be confirmed very soon.

We are also defining the framework for the future legal relationships between T2S and the CSDs and drawing up a harmonisation plan to accompany T2S.

With the help of my colleagues in the Eurosystem, and with the help of the 200 market participants who are involved in the advisory group and in the technical groups, we hope to be able to submit the full “T2S dossier” to the Governing Council in May, so that CSDs can tell us in June whether they intend to join the T2S endeavour. If sufficient support is offered, then the Governing Council will be in a position to give the green light in July to mobilise the resources needed for this project to be brought to completion in 2013.

I would like to finish with a more personal view. I have never thought that T2S would be a project where there would be winners and losers. I sincerely think that if T2S were to fail, Europe would lose, and I am not sure that anybody would win in the long run. I am convinced that if T2S succeeds, Europe will win and all those who have helped us will also win in the decades ahead.

Thank you for your attention