

Integration and efficiency in collateral markets - a central bank perspective

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Brussels, 1 March 2005

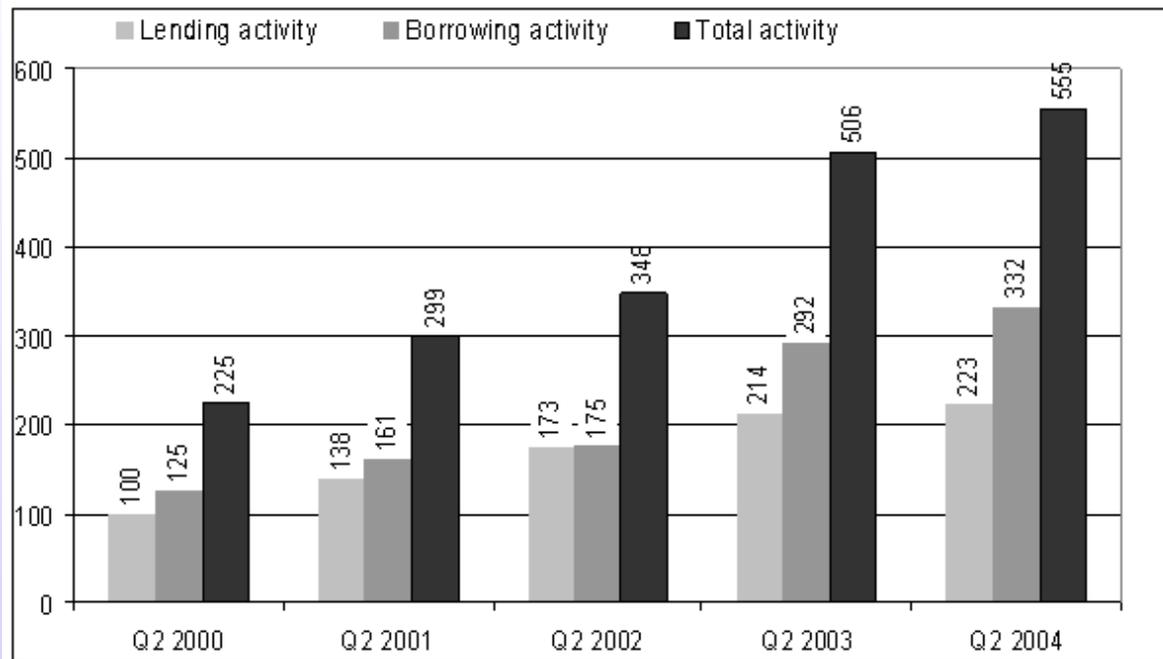


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1. Introduction

Average daily turnover in euro repo markets



Base 100 for cash lending activity in Q2 2000

Source: ECB Money market study (forthcoming) – (provisional data for 2004)



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1. Introduction

Obstacles to better integration of secured (repo) money market

- Large range and diversity of issuers and securities
- Diversity in market practices and documentation
- Fragmentation of the infrastructure
- Outstanding legal and tax issues



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Overview

1. Introduction
2. Role of collateral and its management in counterparty operations
3. Role of collateral in central bank operations
4. The need for an efficient settlement infrastructure
5. The ECB's stance on collateral issues



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2. Role of collateral in counterparty operations

- **Theoretical understanding of the role of collateral**
Work by 2001 Nobel laureates Akerlof and Stiglitz
- **Practical approach to the use of collateral**
ISDA Margin Survey
- **Development of collateral management techniques**
Credit risk mitigation, Triparty agreements, etc



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3. Role of collateral in central bank operations

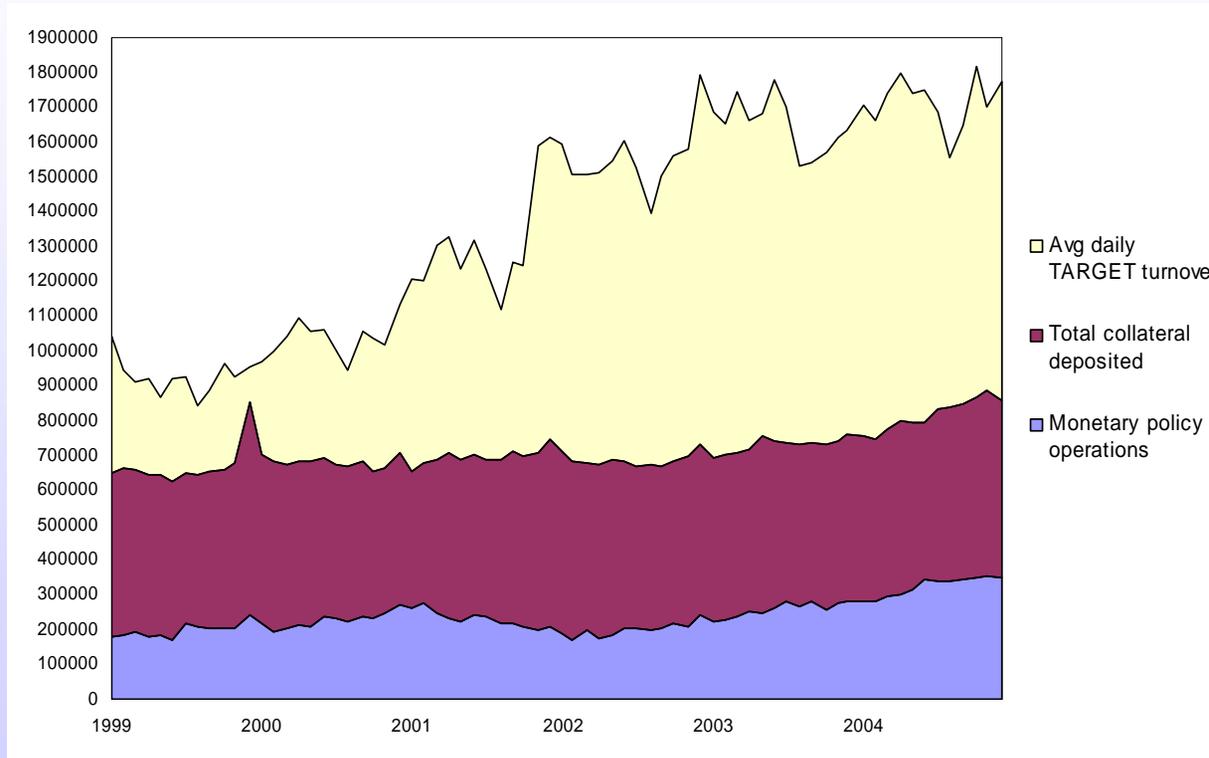
- Monetary policy operations ideally risk-free
- Central banks want to avoid credit assessment of monetary policy counterparts
- Thus: collateralisation and adequate risk control measures (daily valuation, margin calls, haircuts)
- Use of reverse repos for the bulk of monetary policy operations



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3. Role of collateral in central bank operations

Collateral deposited with the Eurosystem NCBs by counterparties



Source: ECB



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4. The need for an efficient settlement infrastructure

- The Eurosystem as “user” of settlement systems
- The Eurosystem’s possible role as overseer and as regulator
- Domestic settlement relatively efficient.....
-but cross border settlement complex and costly
- Further integration desirable – EU Commission and CESAME



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5. The ECB's stance on collateral issues (1)

- Fully integrated financial markets contribute to productivity growth in the euro area
- Market-led solutions should be driving force towards integrated markets.....
- but public authorities have a role to play



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5. The ECB's stance on collateral issues (2)

The ECB's role:

- Acting as catalyst and fostering solutions (European Master Agreement)
- Assessing state of integration + research
- Promoting harmonisation measures aiming at general efficiency of markets (e.g. “single list”)
- Supporting public policy in financial integration



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