

12 December 2007

TENDER PROCEDURE FOR PROVISION OF US DOLLARS TO EUROSYSTEM COUNTERPARTIES UNDER THE TERM AUCTION FACILITY FOR SETTLEMENT ON 20 AND 27 DECEMBER 2007

Following a decision by the ECB's Governing Council, the Eurosystem central banks shall conduct two operations with the following characteristics.

Type: Provision of US dollar funding to Eurosystem counterparties against ECB-eligible collateral as set out in Chapter 6 of the General Documentation on Eurosystem monetary policy instruments and procedures¹ (the 'GD'), in accordance with the procedures set out for long term refinancing operations, in particular in sections 3.1.3 and Chapter 5 of the GD with the deviations contained in this statement of tender procedure:

Maximum amount: USD 10 billion

Pricing: Fixed rate tender

Auction details: Fixed rate tender, with the rate not being known by market counterparties at the time of bidding: market counterparties would be informed that the rate they would pay on the allotted amount would be equal to the marginal rate of the simultaneous Federal Reserve tender.

The minimum bid amount is equal to USD 10 million; the maximum bid amount is equal USD 1 billion. The publication of the announcement of the tender and the allotment will take place on wire services.

Eligible counterparties: In the euro area, all institutions which are eligible for the ECB's marginal lending facility and which have provided their US dollar standard settlement instructions (SSIs) and a Statement of Acknowledgement (specified below) to their respective national central bank (NCB) in advance of the bid submission are deemed eligible.

¹ Annex I of Guideline ECB/2000/7 of 31 August 2000 on monetary policy instruments and procedures of the Eurosystem (OJ L 310, 11.12.2000, p. 1) Guideline as last amended by Guideline ECB/2007/10 (OJ L 284, 30.10.2007, p. 34).

Risk control measures: In the euro area, the usual haircuts as defined in Section 6.4 of the GD will be applied and in addition an initial margin of 17 % will be applied to cater for foreign exchange rate risk. The euro value of the USD liquidity provided will be computed once, on the allotment date, using the ECB reference rate on the allotment date. While the collateral position will not be subject to any daily revaluations or margin calls due to movements in the exchange rate, it will be subject to the normal daily mark to market valuation and variation margins applied to Eurosystem eligible collateral. The 17 % haircut therefore caters for the foreign exchange risk to which the Eurosystem will be exposed for the whole of the duration of the operation (up to 35 days) and the expected time required for the liquidation of the assets in case of a default of a counterparty.

Background information on risk control measures please refer to the Annex to this note.

Settlement details: Similar to the settlement of other Eurosystem credit operations, there must be a delivery of euro-denominated collateral by the counterparty in advance of the provision of credit by the NCB. For the *first leg of the operation*, market counterparties are required to deliver eligible euro-denominated collateral to their local NCB by 16:00 CET on the value date; on receipt of such collateral, the NCB will submit the corresponding US dollar payment instruction to the Federal Reserve Bank of New York (FRBNY) as soon as possible thereafter and ideally before 20:00 CET (14:00 EDT/EST) on the value date. For the *second leg of the operation*, market counterparties are required to pay back US dollar funds to the accounts of NCBs at the FRBNY by 16:00 CET (10:00 EDT/EST) to ensure adequate time for return of euro-denominated collateral by NCBs to market counterparties before close of business on the value date. Market counterparties are advised that in case US dollar funds are repaid after 16:00 CET (10:00 EDT/EST), the respective NCB cannot guarantee return of euro-denominated collateral on the value date but will aim to do so on a 'best effort' basis.

Legal requirements: The operations set out in this note will take place in principle using existing legal documentation between the respective NCB and its eligible market counterparties. If certain NCB amendments are needed to such legal documentation, the NCBs will implement such amendments for the purposes of such operations.

Following the announcement of the tender procedure, market counterparties wishing to participate in this Term Auction Facility are required to provide, before bidding, to their respective NCB their US dollar SSIs and a Statement of Acknowledgement. In such Statement of Acknowledgement, market

counterparties will be required to explicitly acknowledge – as a condition of participation in the tender –

- that they are bound by the conditions of the tender set out in this note and communicated in the tender announcement; and
- the applicability of existing legal documentation between the counterparty and the NCB to the operation in question (unless amendment of the legal documentation is necessary).

The provision of US dollar SSIs by market counterparties to their respective NCB should be effected via SWIFT. The Statement of Acknowledgement may similarly be communicated via SWIFT or in another form as required by applicable national laws.

The dates of the first operation are as follows:

Maturity: Thursday 17 January 2008 (28 days)

Schedule and timing: Tender announcement: Friday 14 December 2007 at 15.30 CET

Deadline for submission of bids by counterparties to NCBs: Monday 17 December 2007 at 9.30 CET

Tender results: Wednesday 19 December 2007 at 16.00 CET

Settlement date: Thursday 20 December 2007

The dates of the second operation are as follows:

Maturity: Thursday 31 January 2008 (35 days)

Schedule and timing: Tender announcement: Wednesday 19 December 2007 at 15.30 CET

Deadline for submission of bids by counterparties to NCBs: Thursday 20 December 2007 at 9.30 CET

Tender results - **tentative**: Monday 24 December 2007 at 16.00 CET

Settlement date: Thursday 27 December 2007

ANNEX:

BACKGROUND INFORMATION ON THE METHODOLOGY APPLIED TO DEFINE THE FOREIGN EXCHANGE ADD-ON MARGIN TO BE APPLIED TO EURO COLLATERAL UNDERLYING US DOLLAR LIQUIDITY PROVISION

Collateral assets underlying Eurosystem credit operations are subject to risk control measures. These risk control measures are applied to protect the Eurosystem against the risk of financial loss if the collateral has to be realised owing to the default of a counterparty. For US dollar liquidity backed by euro denominated collateral, the Eurosystem incurs a foreign exchange rate (FX) risk relating to possible movements in the US dollar exchange rate, in addition to the risk of change in value of the euro denominated collateral.

The FX risk is catered for by adding an initial margin computed on the amount of the US dollar liquidity provided. The euro value of the liquidity provided in US dollars is computed on the allotment day using the current exchange rate and is frozen for the duration of the operation (four or five weeks). This results in a longer exposure to FX risk and a higher margin than would normally be experienced in an operation with shorter maturity (e.g. one week).

To obtain an adequate level of risk control for this FX risk in line with best market practices, first the volatility of the USD/EUR exchange rate is estimated for the relevant period. Then, Value at Risk (VaR) is estimated on the basis of the initial margin needed to reflect the maximum loss of market value due to adverse movements in the exchange rate with a given level of statistical confidence over the relevant period. The length of this period corresponds to the duration of the operation plus the time expected to be required for the liquidation of the assets in case of default by a counterparty.