



**Eurofi 2008 -
Thursday 11/09/08**

**Session [12B] - SECURITIES
INFRASTRUCTURES: ARE
IMPROVEMENTS IN EU
POST TRADING ON TRACK?
Improvements brought on
and expected by on-going**

**actions of the public and private sector, potential limits,
priorities and solutions to speed up and facilitate progress.**

The Panel

Moderator: **Bob Wigley**, Chairman EMEA, Merrill Lynch International

Panellists: **Alain Closier**, Global Head of Securities Services, Société Générale;

Satvinder Singh, Managing Director & Head of Direct Custody and Clearing EMEA GTS, Citi;

Katja Rosenkranz, Member of the CBF Executive Board, Clearstream Banking;

Paul Symons, Director and Head of Public Affairs, Euroclear

Mario Nava, Head of Unit, Financial Markets and Infrastructure, DG Internal Market and Services, European Commission;

Jean-Michel Godeffroy, Director General, Payment Systems and Market Infrastructure, European Central Bank (ECB);

The Debate

This second session of two on EU securities infrastructures, moderated by **Bob Wigley**, Chairman EMEA at Merrill Lynch, focused on progress towards the delivery of solutions to the issues in EU clearing and settlement.

Answering Mr Wigley's opening question as to what had changed so far and what were the concrete benefits of the Code, of the lifting of the barriers and of MiFID, **Alain Closier**, Global Head of Securities Services, Société Générale, and **Satvinder Singh**, Managing Director & Head of Direct Custody and Clearing EMEA GTS, Citi, agreed that much progress had been made in transparency and unbundling of services, potentially benefiting clients.

The industry had to be closely involved with the Code, said Mr Closier, and was generally supportive of it. Transparency had progressed and intensive

work was happening in the area of unbundling. But there were difficulties in developing interoperability. Some questions remained unanswered, particularly whether it was possible to implement interoperability before harmonisation had taken place eg of risk management in the clearing space. Also whether there was a probability that this may lead clearing houses to compete on risk and whether this was reasonable. There was also debate within the industry on whether competition and consolidation could be developed at the same time.

S. Singh thought that clients had benefited a lot from on-going reforms already. MiFID had opened up the trading market to new entrants in the MTF space and a lot had been done to unbundle services. The ripple effect from new players in the industry had already had an effect on the fees levied by established players. There had also been progress on price transparency. The industry was nevertheless struggling with interoperability which remained an open question: how many of the 80+ links granted so far were really useful? to what extent was interoperability preferable to a pan-European CCP and was this alternative feasible? these questions still remained to be answered according to Mr Singh.

The market had seen certain benefits in terms of price competition, said **Katja Rosenkranz**, Member of the CBF Executive Board, Clearstream Banking, which was healthy. "If we have competition, we can work in an interoperability environment," she added. The Link Up Markets project which would bring more interoperability was progressing well and would be ready by the end of 2009. Progress on Giovannini barriers was mainly dependent on the public sector acting. More could have been achieved if the public sector had kept pace with the private sector, Ms Rosenkranz believed. But she thought that Target 2 Securities could bring pressure on the public sector to act.

Paul Symons, Director and Head of Public Affairs, Euroclear, noted that there had been a change of emphasis on these kinds of panels over the last five years. Before, the pressure was on the private sector, and on CSDs, to find a solution to the Giovannini barriers. Now, there was still a certain amount of pressure on the private sector, but it primarily had shifted to the public sector too. The focus was also much more on the CCP layer than on the CSD layer, said Mr Symons. Over 80 links had been granted so far, perhaps as many as 100 and most were centred around CCPs, requesting access to new settlement systems or requesting access to exchanges.

He confirmed a lot had been done on price transparency and unbundling which were in the hands of the signatories of the Code of Conduct, but noted that interoperability and access needed cooperation, which was difficult to force in a voluntary environment especially when links may not be in the business interest of both parties. It was challenging "to compel someone to marry", Mr Symons said.

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For the first time since the Code was introduced it was possible to see the fee schedule of every CSD. "This may seem like a small win but it is progress nevertheless," said Mr Symons. The European Central Depository Association (ECSDA) had done a lot of work on comparing prices across a set of services with consistent definitions. Despite the lack of progress in the interoperability area, Mr Symons said it would be too hasty to assume the Code was a failure; this was a very technical area. But there needed to be considerably more work done on removing the barriers to open access and interoperability.

Mario Nava, Head of Unit, Financial Markets and Infrastructure, DG Internal Market and Services, European Commission, was asked to consider whether he was satisfied with the progress to date on the Code. Price reductions had already been delivered but in order for them to be maintained, effective competition needed to be in place, he said. At the CSD level, there was some degree of competition, albeit in clusters. The real spotlight was at the level of the CCPs. He felt that although there were regulatory impediments in some cases to putting in place links this was not always the case. The Commission had given a mandate to CESR to describe regulatory impediments and to figure out how to breach the gaps that existed. "It is true that if we are blocked by national regulators, we are in the hands of national states," said Mr Nava. The blockage was quite often to do with commercial issues he thought.

Mr Nava had explained the aims of the Code at Sibos in 2006 and described it as a "line of credit". In other words, the Commission had put faith in the industry to deliver. "We should not call it a failure," said Mr Nava. "It has worked in some areas." He said there had been 80 requests for access, but not all of them had been relevant. Maybe as little as 4 or 5 links were really worthwhile. The problem was that there had been no user checks on these requests, but this was the way that the industry had chosen to proceed. He understood the competition concerns related to interoperability, but pointed out that the initial objective was to increase the market for all players. There would be a report made to the Ecofin Council of Ministers in December that could represent a turning point in the process.

Several participants in the audience were invited by Mr Wigley to comment on what had been said by the panellists. D. Chan from EuroCCP confirmed that users needed to be involved in the prioritization of links. At present it was first come first served and this needs to be reconsidered. C. Tupker from LCH Clearnet said that he needed help from the Commission in solving the blockages to get access to the German market as this was becoming urgent and LCH Clearnet had had no recent response from the German authorities. A. Merriman from BBA (the British Banking Association) expressed disappointment with the lack of progress of interoperability and thought that the access / interoperability guidelines drafted by the

industry in the context of the Code had not met their purpose. F. Fontan from BNP Paribas Securities Services added that answers had to be found on the risk side: since the level of protection differs across CCPs, inter-linking of CCPs impacts the level of protection of investors and this needs to be analyzed.

Mr Wigley then moved the debate to evaluating the potential benefits and impacts of Target 2 Securities (T2S) and related initiatives in settlement, such as Link-Up Markets, and Euroclear's Single Platform and User Choice Model (UCM)..

Société Générale in particular and the French marketplace in general was in favour of T2S as a driver of consolidation and harmonization, said Mr Closier. "We are strong believers as users that the competitiveness of securities infrastructures in the EU will come from consolidation, and not from fragmentation. "And everyone agrees harmonisation is the key," Mr Closier added. Société Générale, as a significant player in asset management, investment banking and custody, was always looking to lower prices, which required optimizing activities along the value chain. Again, T2S was a good tool to achieve this.

However, from a practical point of view, implementation would not be easy. "It could be 2013, perhaps earlier, perhaps later," Mr Closier said. That meant that for the next five or six years there would not be an environment in which consolidation could take place in Europe.

The drawback for users such as Société Générale was that they would have to work in a non consolidated environment in the coming years. He also saw possible conflicts between the political perimeter and business perimeter of the proposals made. For example Société Générale as a regional player could be more interested in a consolidation perimeter covering some major EU countries such as France, the NL, Belgium, as in the ESES project, than in the political perimeter of consolidation at the EU level. There was also a debate around access to T2S: direct, via a CSD or via the Euroclear platform (with the "user choice" principle put forward by Euroclear).

Mr Singh said Citi had been heavily involved in providing industry insights from a users' perspective regarding the establishment of T2S. He said since the announcement in July 2008 all stakeholders all stakeholders are now in the process of discussing a definite timeframe for the project and this seems to build-up some momentum. There had been wide-scale interest from clients on T2S developments as this could change the market structure fundamentally. But he also sounded a note of caution about the timeframe of the project, pointing out that five years ago few people would have predicted the changes that had come about in Europe. So making a firm prediction for roll-out in 2013 was hard, because it could be overtaken by the pace of changes. "The plan must not be out of sync with where the European market has headed by 2013," said Mr Singh.

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Between now and then it should be continually assessed whether it offered clients the ultimate solution to their requirements. There was also the issue of the impact on back office and settlement arrangements. "And what will operational flows really look like?" Mr Singh asked. From a custodian's perspective, Europe was changing dramatically. "Industry costs and revenues in 2013 are likely to be lower than today and all initiatives will need to adapt to nimbly to ongoing change," Mr Singh added. He thought that T2S would also have an impact on the business models of intermediaries leading them to focus on how respective services will change and adapt to the changes and challenges ahead. For this reason, solutions always had to take the ever-changing landscape into consideration

P. Symons said Euroclear was supportive of T2S as long as it delivered a low-cost and efficient platform both for Euroclear and its clients. But Euroclear would ideally prefer to give clients a choice and "the best of both worlds" ie T2S or using the Euroclear single platform which was 70% developed to deliver settlement and asset servicing covering 5 EU markets and proposed a unique multi-currency service. If T2S was successful, Euroclear expected a large part of client business to migrate to it, but it was up to users to make the choice. Concerns about T2S centred on the legal structure of the project and its governance, such as how CSDs could influence the provision of settlement and other services. There needed to be common consensus about these kind of legal and governance issues, Mr Symons added.

A number of radical business modification changes would take place if T2S came to fruition. It would change the structure of CSDs in Europe probably leading some CSDs to merge or move up the value chain. "If they are left with custody and asset servicing, they may start to compete with their own customers and other CSDs," he believed. This would necessitate greater links and could possibly be the catalyst for greater interoperability. Certainly, CSDs were looking at their strategic options for 2013 and beyond.

K. Rosenkranz explained that an interoperable concept could work with a consolidation concept. Both could be done and in the end users could choose what is best for them. Consolidation meant acquisition of CSDs. T2S meant consolidation but T2S would still operate in an interoperability world. Indeed CSDs would remain and still compete and have to enter into link contacts. Euroclear also had to develop interoperability between its Single Settlement Platform and T2S.

She questioned why it would be necessary to wait until 2013 to have interoperability. The issue had already been initiated by Link Up Markets, a joint venture between seven European securities depositaries, including Clearstream. Link Up Markets will offer access into 7 markets but also direct connectivity into T2S through the CSDs that will be linked up with

T2S. It was not a closed shop, so it was up to users to express their opinions to CSDs on whether they wanted it to gather momentum. Euroclear also was invited to join Link Up Markets.

Link Up should enable to bring some benefits for users before 2013 and set the scene for T2S. There could be a direct technical connection and T2S and Link Up could be combined. "Link Up will absorb the differences in standards," said Ms Rosenkranz. She thought that rather than waiting for many years to figure out the target, intermediaries should help to define in what way Link Up can help to support T2S.

K. Rosenkranz also questioned whether there should be competition for settlement in central bank money, she thought that competition should be limited between commercial and central bank money. With Euroclear migrating from an integrated to an interfaced model, T2S will be the only integrated platform.

T2S was firmly on track, according to **Jean-Michel Godeffroy**, Director General, Payment Systems and Market Infrastructure, European Central Bank (ECB), even if there was much work ahead for market participants. Now that the decision had been made, resources have been secured for the development. Many users had been involved in the definition of requirements. He pointed out that the European Central Bank was a facilitator more than a participant in the process and that the User Requirements document expresses the wishes of the market, not necessarily of the ECB. On July 4, the CSDs had indicated that they wished to continue with the project, with just a single exception, Mr Godeffroy said. "We talked to the CSD in question and it changed its mind when it discovered it could not be a member of the advisory group if it did not wish the project to continue."

CSDs should have a contract with T2S meaning that the "user choice model" [adopted by Euroclear] is more difficult to put in place. Initially CSDs were meant to be partners and not competitors. "We understand it was a contract between partners with the same vision of success. If they are competitors it could be difficult, though, because there is suspicion from all sides. The question of governance would be hard."

He confirmed that T2S would be driving harmonization in two ways: the procedures necessary to use the T2S tool, but users had asked harmonization of user requirements to go beyond this first level. This should be done in close cooperation with the Commission with CESAME II serving as the umbrella and be helped by resources from the market. The ECB will be presenting a harmonization plan to the Ecofin at the end of the year with the main priorities that need to be achieved. In particular the relaunching of the ESCB-CESR standards.

There was interest beyond the euro area, Mr Godeffroy continued. In Denmark, for instance, the central bank was greatly interested in the idea

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Sweden and Switzerland were also considering whether to outsource to T2S. In the UK, users were asking whether the Bank of England would agree to outsource the activity. In the UK, however, there was a choice between using T2S and Euroclear. The next step, given the agreement to carry on with the project, was to define the specification of the nascent system. After that, it would be possible to understand whether it could be delivered in 2012 or 2013, and a more precise date could be targeted.

The way in which the platform could be delivered across currencies, in the case that the UK, Sweden and Denmark joined had to be assessed in greater detail. "We opened our system to non-euro currencies at the request of Ecofin," said Mr Godeffroy. "I have changed my mind slightly on this issue." At first, he was convinced that the migration process would deal with the non-euro countries joining. Not all of them would need to migrate on Day 1 so there should not be a problem. The issues involved were not technical and a separate engine, which cloned the original, would fulfil the task. But, on reflection and having discussed the issues further, Mr Godeffroy was less convinced it would be possible.

"Outsourcing the currency from the central bank is a delicate matter so I would presume they are carefully reviewing it." Although he had been convinced by technical advisers it would be possible, it was now up to the central banks concerned to decide if it was desirable. "I have discussed it with the deputy governor of the Bank of England and he is still considering it." There was support in London from users for the idea but politically it was less popular. There was a feeling that it might be seen as acting as pressure to join the euro, which was not politically popular with the UK. "The media makes it hard in London for the government to join our project," concluded Mr Godeffroy.

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