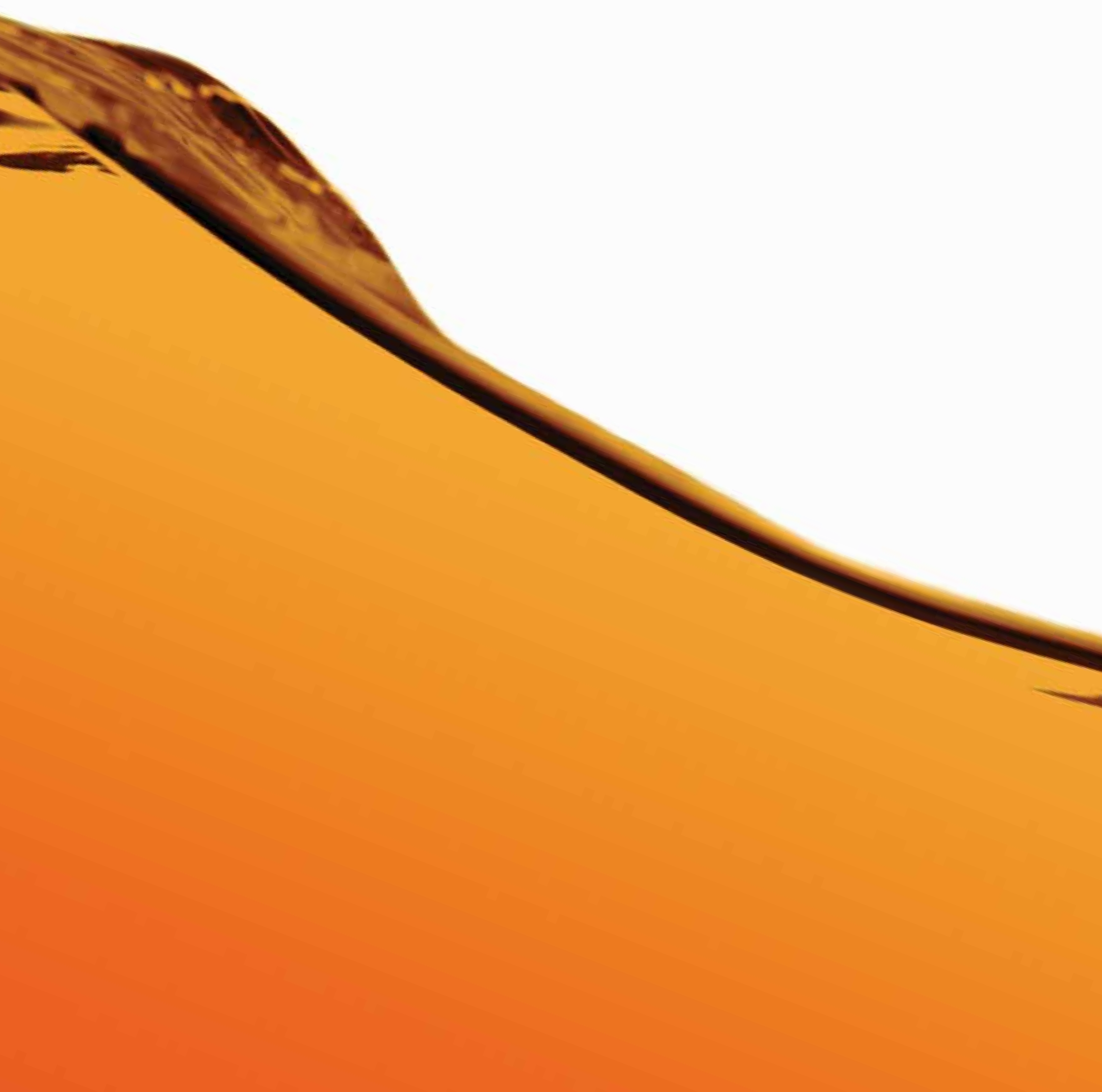
euroclear

Post-trade made easy

Collateral management

When liquidity matters



A new dawn in collateral management

The aftermath of the global financial crisis has caused a seismic shift in the way the market views collateral management. Collateral has not only become an integral tool to mitigate counterparty risk, but also a vital source of much-needed liquidity.

The move from unsecured to secured funding has now become a reality worldwide. At the same time, tough new regulatory measures have greatly amplified demand for collateral from new market segments. Concerns over a global shortage of high quality collateral continue to make the headlines.

In today's climate, it is little wonder that the optimisation of collateral resources is high on the agenda of firms seeking to mitigate their liquidity risks and minimise their overall cost of funding.

Achieving this goal presents a major operational headache to the industry as a whole. Indeed, many firms still hold separate collateral pools dependent on geography, asset type or business line. A prerequisite to portfolio optimisation is the efficient management of collateral across asset types, geographical borders and multiple counterparties.

That is why Euroclear is committed to investing in the development of an open collateral management model to support your business needs in these challenging times.

The explosion in collateral demand is set to continue

The ever increasing demand for collateral is universal across all industry segments and is set to intensify in the future. At the same time there is a real need for firms to fully exploit all options available to them to manage their liquidity requirements. As a consequence of both these market forces, it is no longer acceptable for market players to have precious collateral resources 'locked away'.

The current collateral demand landscape

The Eurosystem continues to take steps to improve the stability of the banking system via fully collateralised credit operations

Recent months have seen the European Central Bank (ECB) inject around €1 trillion of cheap cash into the eurozone. The ECB is implementing its monetary policy via fully collateralised Eurosystem credit operations which are not only boosting the demand for collateral but also leading to greater collateral diversification. An increasing proportion of the collateral posted to the Eurosystem (up to 18% in 2010) is made up of non-marketable assets such as credit claims. This trend is set to continue, particularly in view of specific national temporary measures recently approved by the ECB.

The enforced mandatory clearing of OTC derivatives will not only increase the demand for collateral exponentially but will also heighten the need for collateral transformation

The regulatory changes brought about by the European Market Infrastructure Regulation (EMIR) and the Dodd–Frank Wall Street Reform and Consumer Protection Act means that CCPs will play a wider role in a number of markets, OTC derivatives in particular. This impacts trillions of euros' worth of collateral held worldwide. OTC derivatives margins alone are expected to grow from €1.6 trillion today to €2.6 trillion once new CCP arrangements are in place. In addition, the strong emphasis on high-quality collateral will increase need for flexible ways of upgrading collateral.

The move from unsecured to secured funding is here to stay and will continue to bolster demand in the Interbank repo and securities lending markets

The need to limit credit risk exposure is leading to an increase in secured money market transactions in the interbank repo markets and there is a growing prevalence of General Collateral (GC) basket trades. This means there is a greater need for access to high quality securities collateral (80% of repo collateral is in EU government bonds). Collateral transformation, including liquidity swaps, will continue to feature in these markets.

Managing complex operational tasks

Collateral management needs to combine multiple inter-related operational tasks

To achieve collateral optimisation, certain operational complexities need to be tackled. The main factors that currently create difficulties include:

- Multiple types of assets to be delivered and valued as collateral
- Various types of events to be processed on the collateral
- Different operational practices applied across different market segments and companies

"We look forward to fully extending our triparty services across the group and to other markets from Europe and beyond. Our triparty collateral management services are sufficiently flexible to allow for the mobilisation of collateral wherever it is held, even outside the Euroclear group, to mitigate any credit exposure, including those relating to derivative transactions. Discussions are already taking place with potential partners."

Jo Van de Velde, Managing Director and Head of Product Management, Euroclear

Building for the future on solid foundations

The Euroclear group provides leading collateral management services which enable market counterparties to increase efficiency and mitigate operational risks related to the processing of day-to-day collateral management tasks.

The industry is facing many challenges as well as a much stronger scrutiny from regulators. The ever increasing amount of collateral required by market players represents a considerable operational challenge.

The need to access new sources of liquidity with new counter-parties will mean that market players will increasingly opt to mobilise collateral in locations different from where assets are held in safekeeping.

In response to these important market changes, Euroclear is in the process of opening its collateral management services to interact with multiple settlement platforms. Several milestones have already been delivered.

Keep control of pools of eligible collateral delivered outside Euroclear Bank

Our 'Collateral Allocation Interface' service currently allows you to deliver the securities you hold in Euroclear Bank as collateral to another settlement platform – be it domestic or international.

Mobilising domestic assets as collateral with domestic counterparties

In 2011 we delivered a fully fledged triparty collateral management service in domestic CSDs. Collateral is transferred from domestic accounts of collateral givers and collateral takers held in a domestic settlement platform. The service is fully operational in Euroclear France, settling in the ESES settlement platform, and in Euroclear UK & Ireland through Deliveries by Values (DBVs). We are working to roll out the service to other markets.

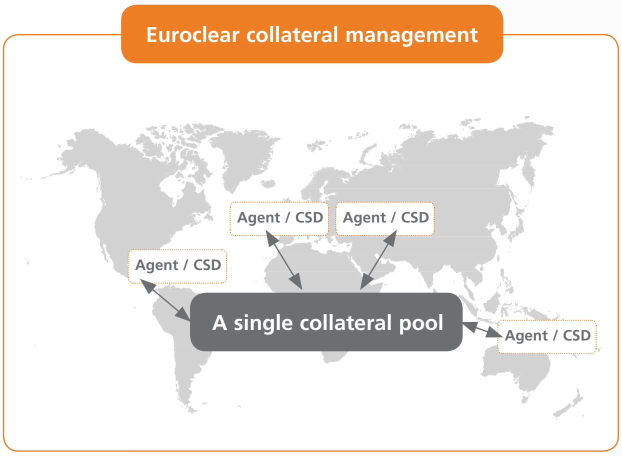
Facilitating cross-border movement of assets in triparty

Inventory management made easy!

In June 2012, we will complement Euroclear Bank triparty collateral management services with a new inventory management service.

This will facilitate the cross-border mobilisation of pools of assets held with domestic agents and CSDs. By pooling these assets in Euroclear Bank you can benefit from using them as collateral in Euroclear Bank's triparty environment.

Cross-border triparty in Euroclear



Bridging existing liquidity gaps through triparty interoperability

Linking Euroclear group infrastructures to optimise collateral pools

We are continuing to improve interoperability between Euroclear Bank and ESES, to allow you to get the most from your collateral portfolios within the Euroclear group.

Working with the market to make GC basket repo trading independent of collateral pool location or collateral service provider choice

Euroclear Bank is involved in a market-driven initiative with the European Repo Council (ERC) to implement a triparty interoperability model in Europe. This triparty interoperability model will be open to transactions feeds from any participating CCP. A decision is expected in June this year.

"To support you through important market change, Euroclear is working on a series of initiatives that will give you the freedom to collateralise any exposure, anywhere."

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