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International Capital Market Association

Welcome

Godfried De Vidts

Chairman of the European Repo Council

Brussels, 8 April 2013

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ERC work – a sample

- 25 May 2012
  ICMA European Repo Council (ERC) Repo Margining Best Practices 2012*
- 20 August 2003
  Repo Trading Practice Guidelines of 20 August 2003
- 12 July 2012
  Floating-rate repo conventions
- 25 July 2011
  ERC recommendation on Repo matching as a driver for risk reduction (25 July 2011)
- 9 November 2007
  Resolution by the ERC Committee on the Harmonisation of GMRA mini close-out provisions and ICMA buy-in rules (9 November 2007)
- 16 November 2004
  Recommendation regarding fails in negative interest rate repos, approved by the International Repo Council on 16 November 2004
- 19 April 2004
  Confirmation of second leg of buy/sell back transactions (Letter from the ERC committee chairman to firms active in the repo market, dated 19 April 2004)

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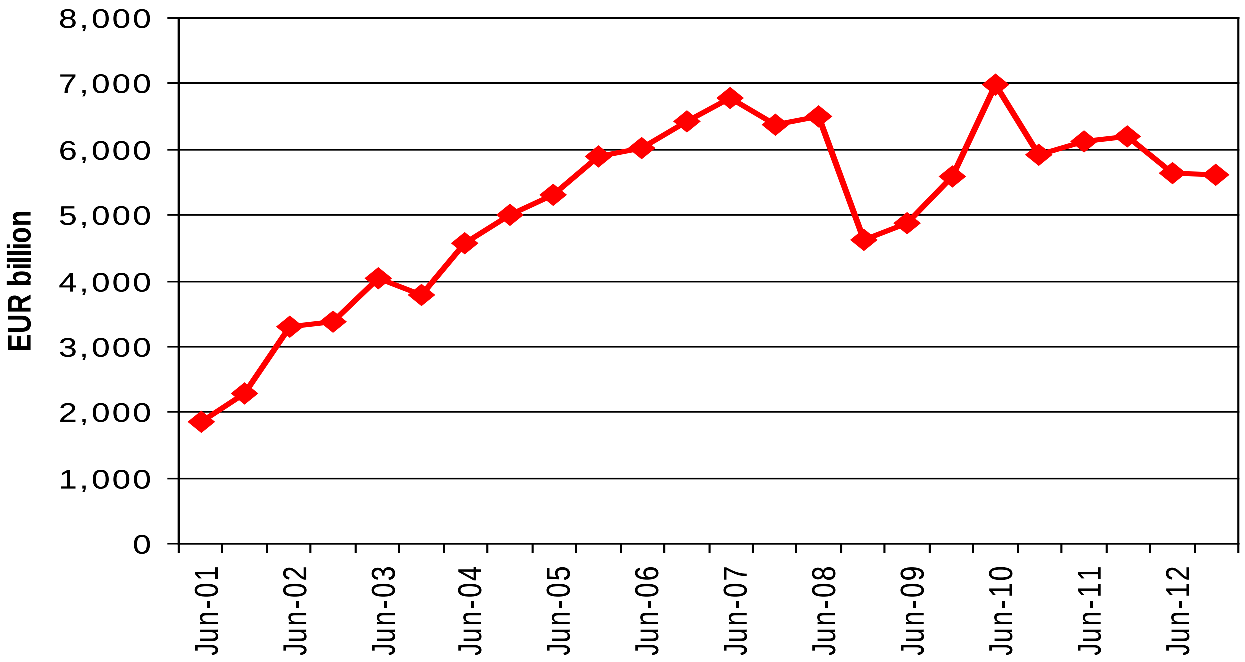
24th European repo market survey, conducted in December 2012

Headline numbers



EUR 5,611 bn

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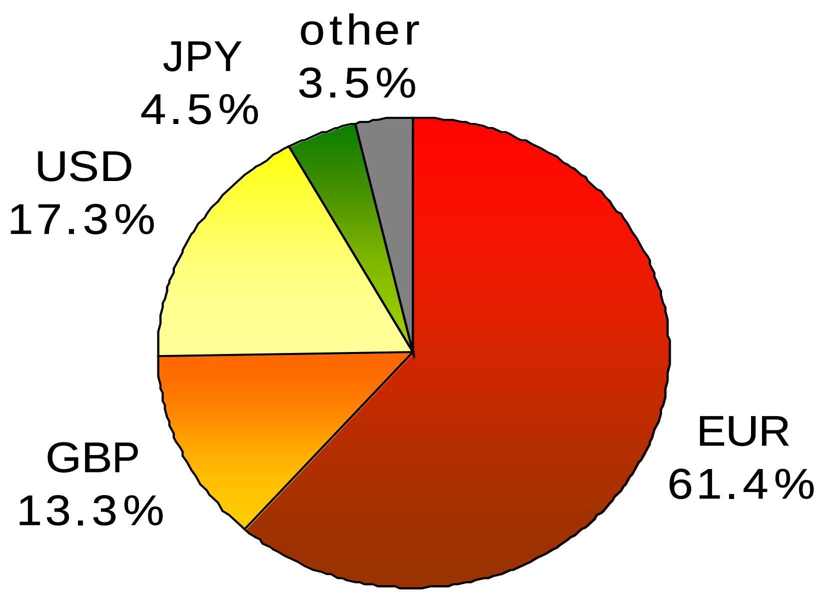
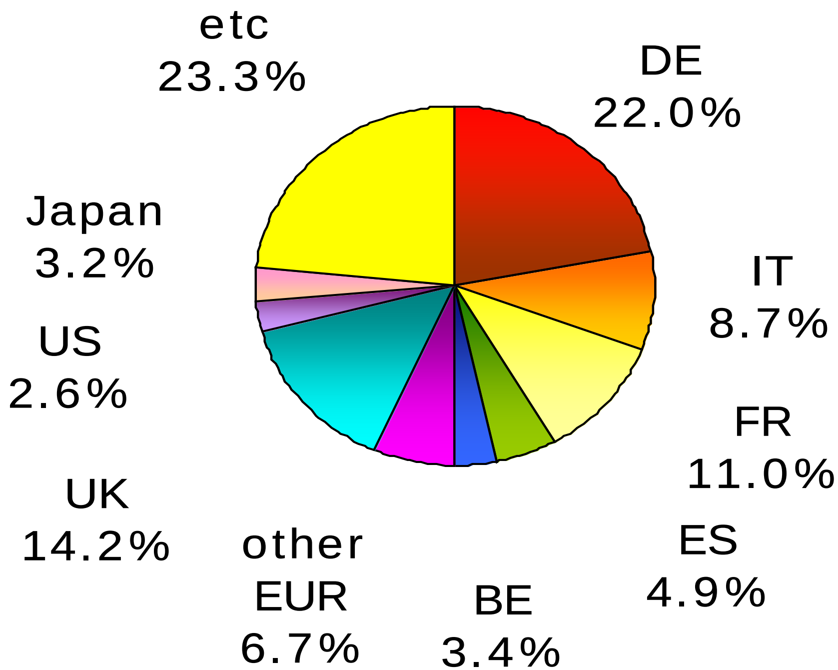
24th European repo market survey, conducted in December 2012

Currency analysis

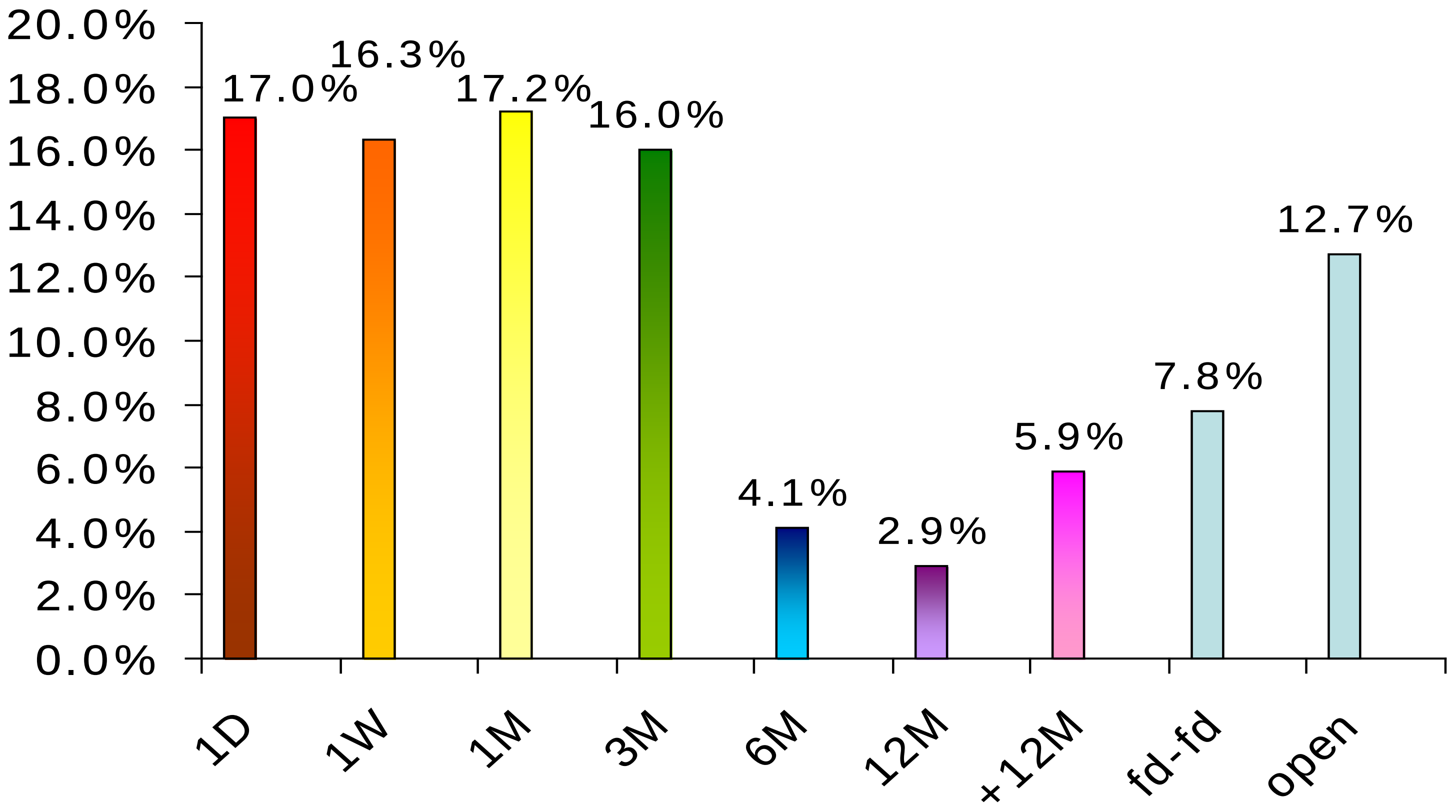


Collateral analysis



24th European repo market survey, conducted in December 2012

Maturity analysis



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Presentation

Richard Comotto

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Brussels, 8 April 2013

The impact of the FTT on the repo markets and its consequences

- much analysis has started from the wrong point
- this is the non-fiscal objective of the FTT --- to curtail financial intermediation
- direct issuer-investor interaction in primary market
- limited secondary market, passive investment strategies, agency brokers
- could inspiration be the equity market --- order-driven, commission-paying, exchange-traded?
- terms of the debate are focused on the utility of secondary markets

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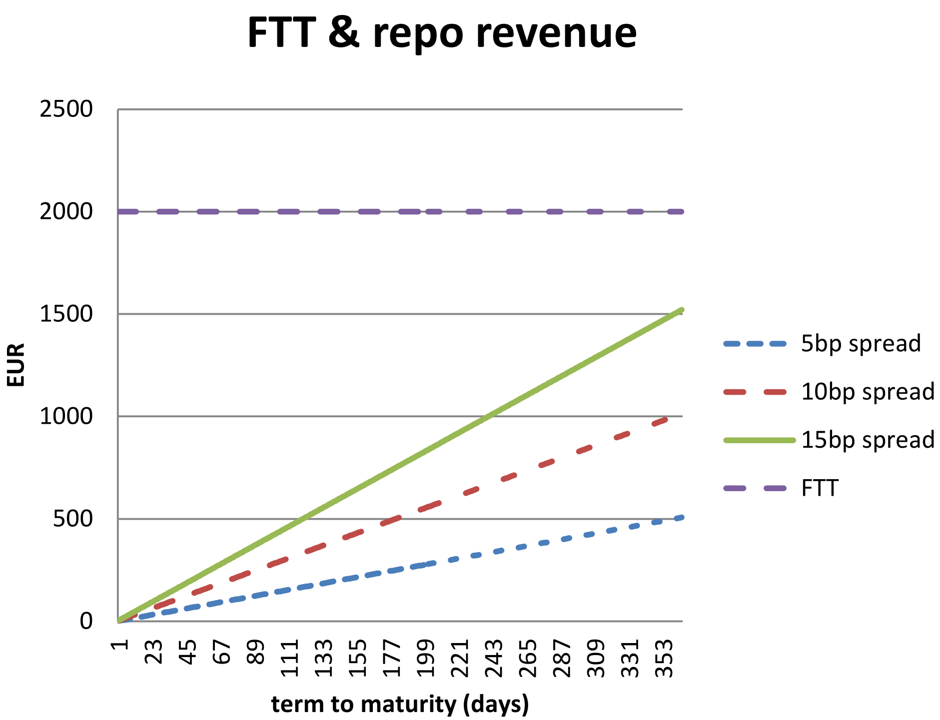
The impact of the FTT on the repo markets and its consequences

- would the DG Tax model work in fixed income?
- very different market:
  - high-volume risk-free government issues, typically plain vanilla --- challenge is rapid distribution
  - lower volume credit issues, typically complex structures --- challenge is pricing & smooth distribution
- key role for primary dealers & market-makers

The impact of the FTT on the repo markets and its consequences

- consequences for the repo market
- incidence of flat rate of 0.10% on short-term transactions

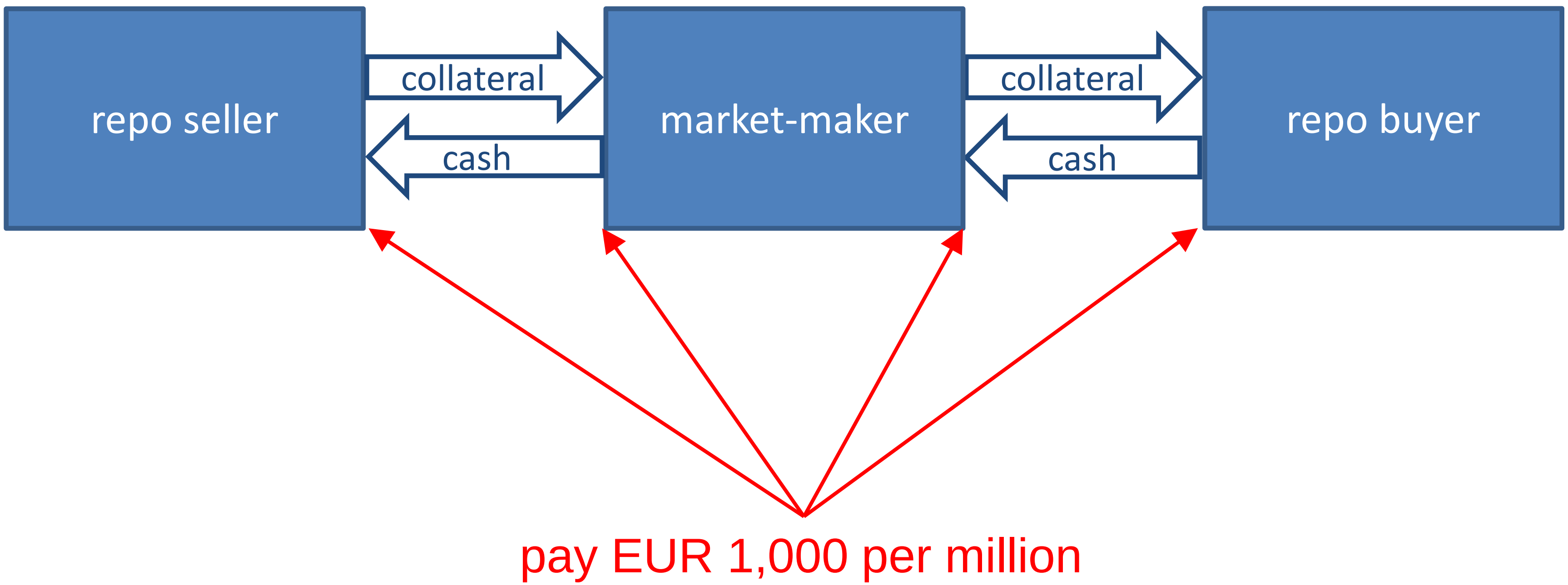
The impact of the FTT on the repo markets and its consequences



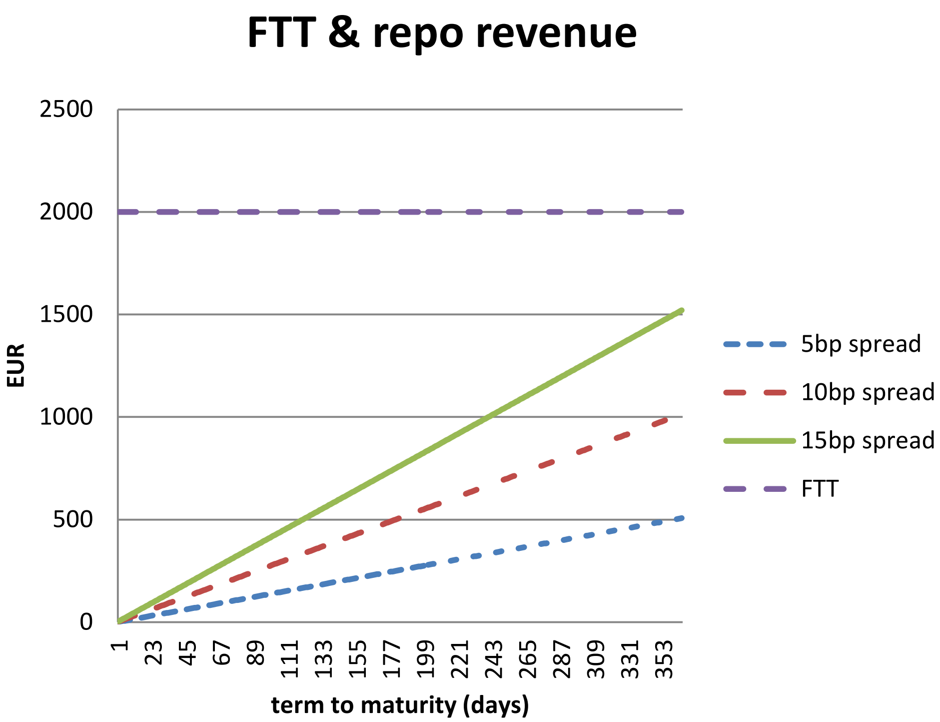
revenue from typical repo EUR per million

	bid/offer spread		
repo term	**0.05%**	**0.10%**	**0.15%**
1D	1.39	2.78	4.17
1W	9.72	19.44	29.17
1M	43.06	86.11	129.17
3M	126.39	252.78	379.17
6M	252.78	505.56	758.33
12M	506.94	1,013.89	1,520.83

The impact of the FTT on the repo markets and its consequences



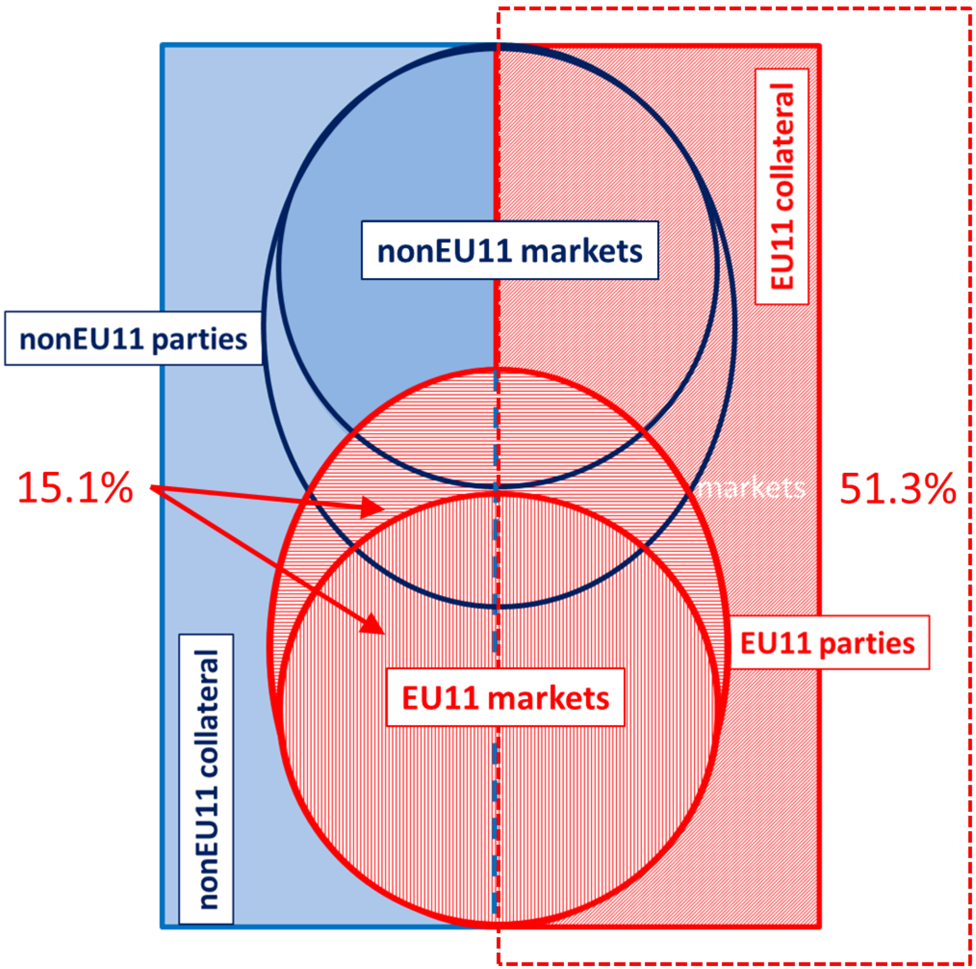
The impact of the FTT on the repo markets and its consequences



implied break-even spreads %pa

	normal bid/offer spread		
repo term	**0.05%**	**0.10%**	**0.15%**
1D	72.05%	72.10%	72.15%
1W	10.34%	10.39%	10.44%
1M	2.37%	2.42%	2.47%
3M	0.84%	0.89%	0.94%
6M	0.45%	0.50%	0.55%
12M	0.25%	0.30%	0.35%

The impact of the FTT on the repo markets and its consequences



The European repo market will contract by at least 66%.

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The impact of the FTT on the repo markets and its consequences

- repo is pivotal to:
  - secondary market-making
  - primary dealing
  - short-term institutional investment
  - bank funding
  - monetary policy implementation
  - financial stability (eg CCP, liquidity buffers)

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The impact of the FTT on the repo markets and its consequences

- loss of repo & money market securities --- secondary market
  - DG Tax says securities volume down 15% --- optimistic
  - loss of repo plus direct impact of FTT
  - flight of foreign investors
  - how to distribute high-volume government debt?
  - how to distribute low-volume corporate debt?
  - portfolio valuation become more difficult
  - delivery failures increase

The impact of the FTT on the repo markets and its consequences

- loss of repo & money market securities --- primary market
  - DG Tax says securities volume down 15% --- optimistic
  - DG Tax says buy primary issues, follow long-term investment strategies
  - pricing become more difficult
  - issuer & investor overheads & risk rise

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The impact of the FTT on the repo markets and its consequences

- loss of repo & money market securities --- investors
- DG Tax says central bank repo & secured loan --- not feasible
- EU11 investors' choice:
  - overnight unsecured deposits
  - capital flight outside the EU11

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The impact of the FTT on the repo markets and its consequences

- loss of repo & money market securities --- banks
  - banks lose wholesale funding
  - banks lose bond debt funding
  - accelerated, perhaps disorderly deleveraging
  - shortage of working capital in real economy

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The impact of the FTT on the repo markets and its consequences

- loss of repo & money market securities --- central banks
  - no collateral framework for monetary policy implementation
  - no market mechanism to monitor & signal
  - further fragmentation of eurozone
  - EU11 collateral at ECB becomes illiquid

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The impact of the FTT on the repo markets and its consequences

- loss of repo & money market securities --- financial stability
  - movement of collateral too expensive, only cash collateral
  - no collateral market
  - de-collateralisation reverses impact of Basel
  - liquidity buffers more expensive & difficult to build
  - operational risk increased

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The impact of the FTT on the repo markets and its consequences

- loss of repo & money market securities --- real economy
  - capital flight
  - shortage of working capital
  - investment capital more expensive
  - long-term growth potential
  - competitive disadvantage
  - relocation of financial services

The impact of the FTT on the repo markets and its consequences

- some final remarks
  - relationship with the non-EU11
  - cost of transition
  - tax as a regulatory tool
  - how (not) to redesign the financial system