

TARGET2-Securities – settlement in central bank money of securities transactions in Europe

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- I. Why does Europe need T2S?
- II. What exactly is T2S?
- III. Current status of the project
- IV. What are the challenges ahead?

Why does Europe need T2S?

- Europe's securities markets are too fragmented and inefficient.
- Lack of competition in services related to settlement
- Europe needs a single pool of securities to stimulate competition and harmonisation.
- There is no other realistic Europe-wide approach to creating this single pool.

**Making Europe a better place to invest and trade
(in line with the Lisbon agenda)**

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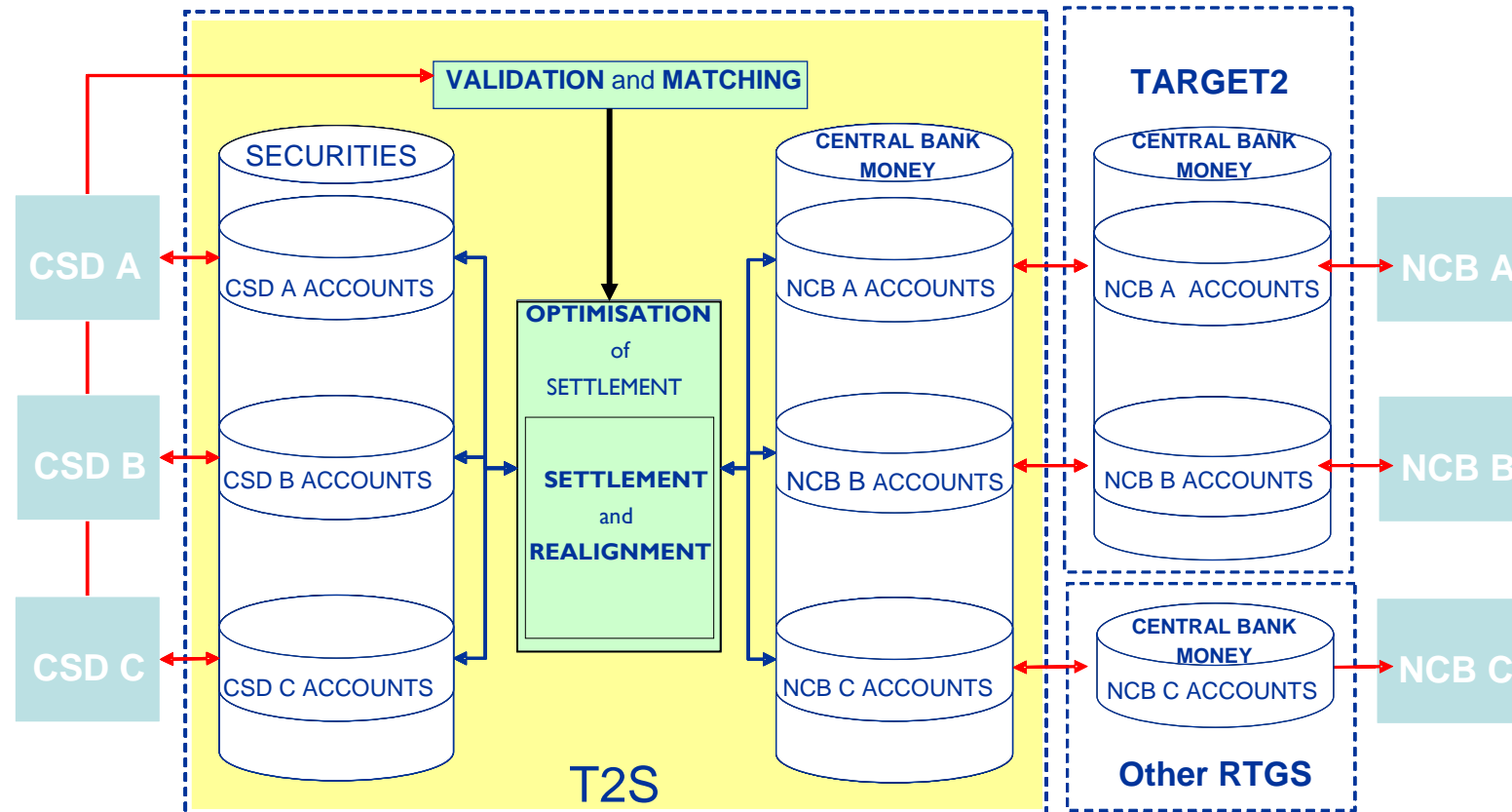
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What is T2S? - A cooperation between CSDs and NCBs



Bringing on one technical platform all securities and cash accounts to settle all securities transactions

What is T2S? – A new concept

- T2S will be a single IT platform enabling settlement of securities in central bank money in the euro area/EU/EEA.
- CSDs will delocalise their securities accounts to T2S, which will perform the processing of their settlement instructions on these accounts.
- CSDs will keep their customer base and continue to perform non-settlement related functions (e.g. issuance, corporate actions, custody, etc.).
- Settlement in commercial bank money out of the scope of T2S

What is the scope of T2S?

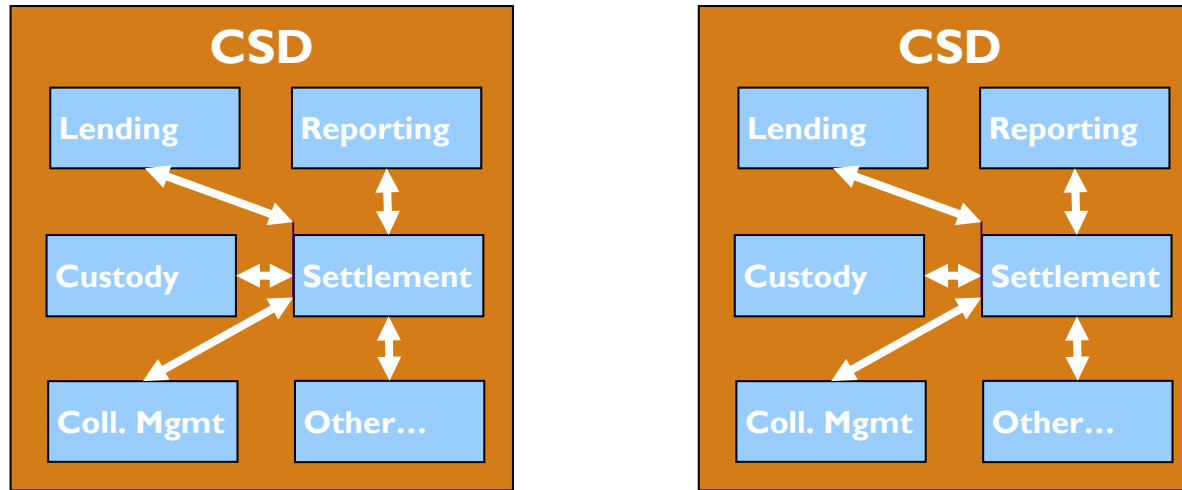
T2S concerns only the settlement function of CSDs!

		Type of intermediation
Notary function	Registration of issuer indebtedness and investor holdings	issuer / investor
Custody and asset-servicing function	e.g. coupon payments, redemptions, stock splits	
Settlement function	Change of ownership among investors	buyer / seller
Banking function*	e.g. lending and borrowing	lender / borrower

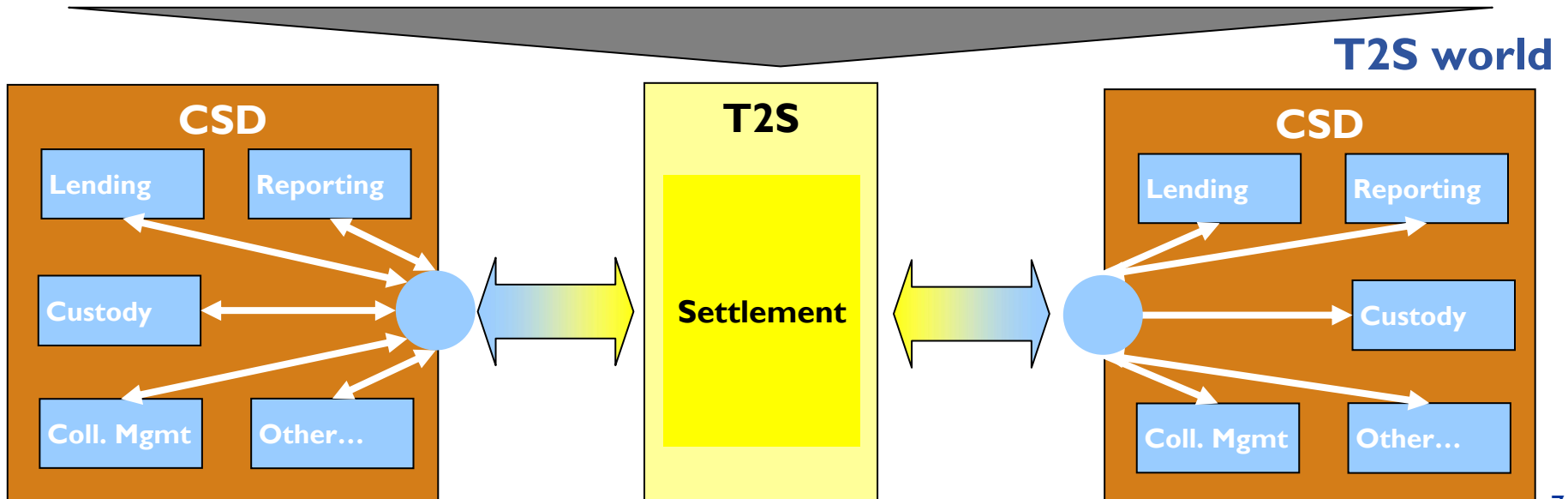
*only in some (I)CSDs

What is T2S?

It is a service to CSDs, not a CSD.



Today



Settlement T2S

- ✓ Volume-based
- ✓ More commoditised
- ✓ Closer to central bank expertise
- ✓ Benefits from achieving a single pool of liquidity/collateral
- ✓ Settlement fees (in particular CSD component) not the largest chunk of the costs, but cross-border fees are high

Scale

Custody/Corporate events CSDs

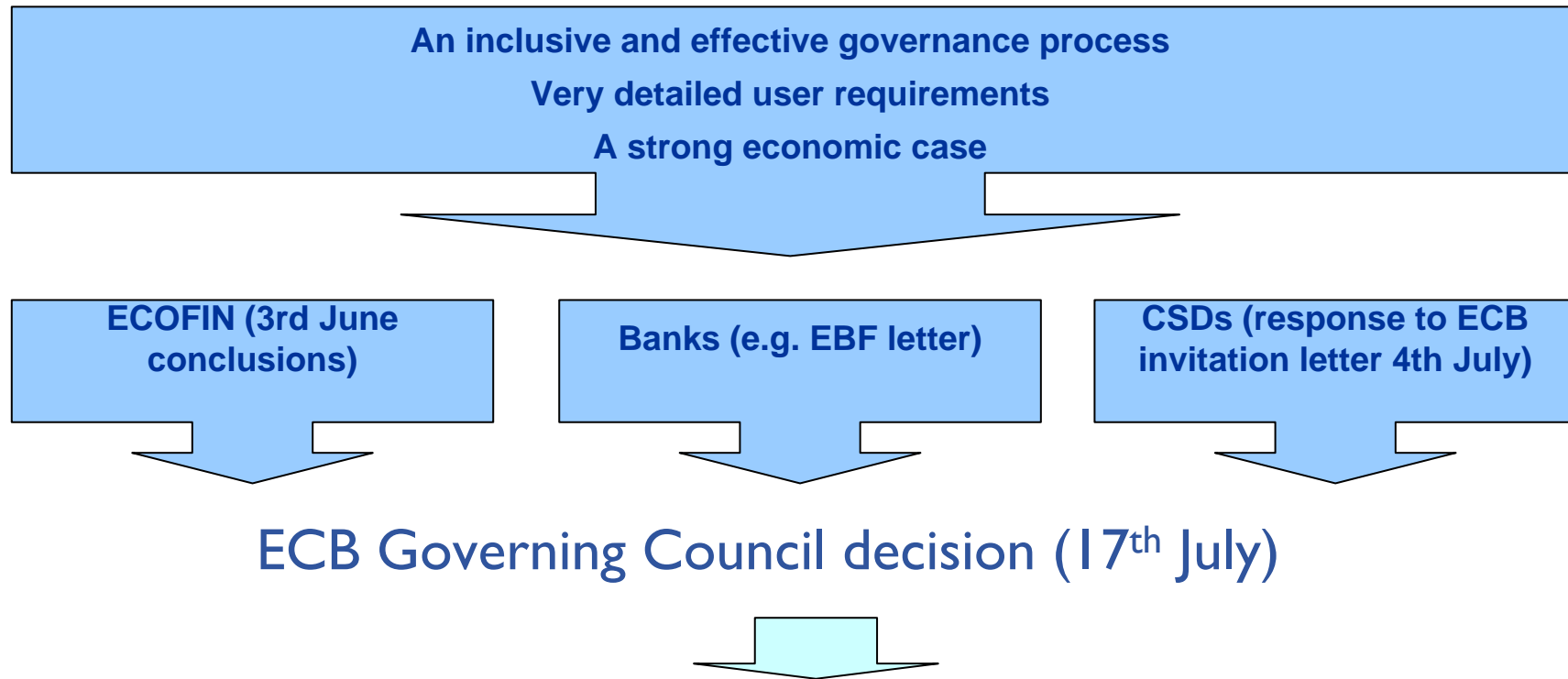
- ✓ Value-based
- ✓ More innovation / calls for harmonisation
- ✓ Less central bank involvement (in particular for equities)
- ✓ Large cost-saving opportunities

Competition

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What lead to the decision?



Provides certainty to all actors that T2S will be built

ECOFIN perspective

ECOFIN (3rd June conclusions)

ECOFIN invites ECB and CSDs to focus on:

- **Costs:** Explore all opportunities to continue to trim down end-to-end costs
- **Risks:** Risk of cost and time slippage to be minimised
- **Governance:** Explore advantages/disadvantages of setting up T2S as a separate legal entity
- **Certainty:**
- Interested CSDs take a clear and unambiguous position on T2S in consultation with their participants and with issuers
- Eurosystem to make a clear offer in the shortest possible timeframe

Banks' perspective

Banks (e.g. EBF letter)

- **Governance:** Commend ECB for inclusive and transparent consultative process. Continue to rely on technical expertise made available by market stakeholders
- **Certainty:** From CSDs on their position towards T2S and on end-costs/pricing
- **Harmonisation:** ECB to leverage T2S to support harmonisation initiatives
- **Beyond euro:** ECB to continue its efforts to accommodate other currencies from day one

CSDs' perspective

CSDs (response to ECB
invitation letter 4th July)

Pending issues to be resolved:

- **Governance:** How will T2S deal with change requests from multiple CSDs?
- **Pricing:** What portion of T2S costs can each CSD expect to pay in fees?
- **Choice of settlement location:** Settlement in central bank money in one platform or multiple?
- **Certainty:** If one CSD breaks its commitment to join, another CSD and its users pay the cost.

Known knowns

- The Eurosystem will deliver T2S and push for post-trade harmonisation
- CSDs will offer T2S to their users

Known unknowns

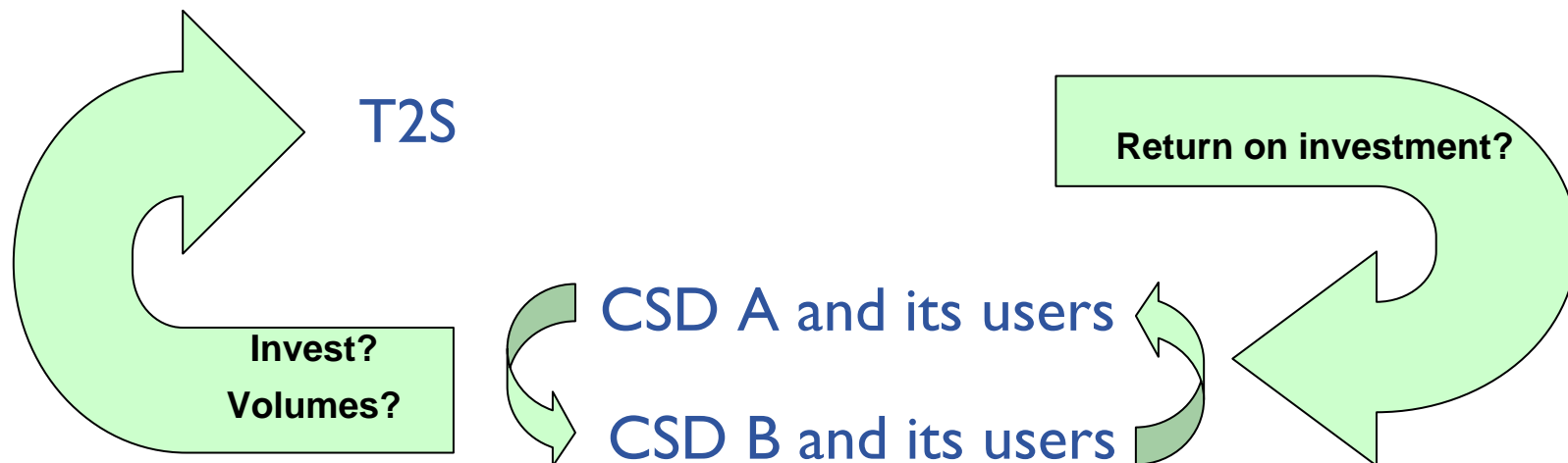


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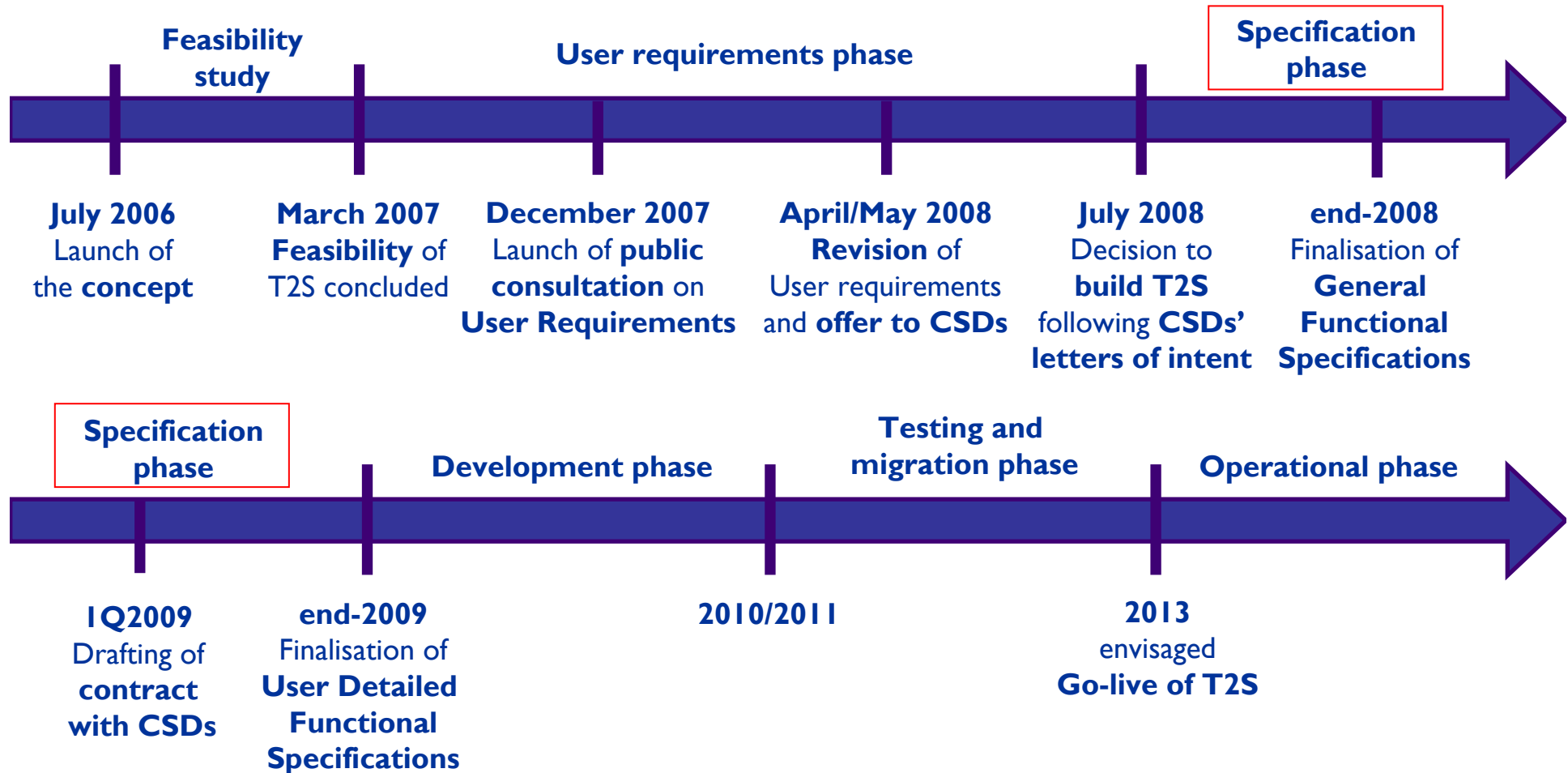
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Where are we?

Past and future milestones



Milestones ahead

Deadline	Deliverable
End-2008	<p>Inclusion of non-euro currencies to impact the economics of T2S for end-users.</p> <p>➔ Pre-requirement: Role of these central banks in the governance to be specified.</p>
End 1st quarter 2009	<p>Contractual arrangement in 1st quarter 2009: Basis for a stable Eurosystem/CSDs partnership to deliver T2S under the users' scrutiny.</p> <p>➔ Objective: Increase certainty on investment to be made by all parties: i.e. that all parties have a private interest to make T2S a success.</p> <p>➔ Pre-requirements: Eurosystem to define:</p> <ul style="list-style-type: none"> ▪ CSD rights/obligations in future governance ▪ Pricing parameters (max/min each CSD can expect to pay) <p>CSDs (or their users) to secure critical mass</p> <p>Penalties to be agreed</p>

Milestones ahead

Deadline	Deliverable
End-2008 (GFS) and end-2009 (UDFS)	Deliver General Functional Specifications (GFS) and User Detailed Functional Specifications (UDFS) consistent with URD. Eurosystem to review by early 2009 in view of GFS: <ul style="list-style-type: none"> -Budget (€200mio currently foreseen) -Launch date (2013 or 2012?)
End 2009	Implement harmonisation action plan to increase the benefits from T2S. Focus on corporate actions and efficient settlement process.
End-2009	Establish migration plan to T2S

Harmonisation

- **T2S must comply with National Regulations.**
- **T2S has largely avoided the development of Specific Functionalities.**

How?

- **CSD to support the National Specificities within its internal processes.**

Why?

- Maximum flexibility: National Specificity may have disappeared by 2013
- CSD knows its National Specificities better
- **The Eurosystem has committed to use its influence to promote harmonisation on areas beyond settlement (e.g. corporate actions) in order to maximise T2S benefits.**

Reverse current incentive structure: Place a cost in maintaining National Specificities

Maintaining CSD commitment

- **All Euro CSDs have committed (as well as SIS, Euroclear UK & Ireland, NCSD Sweden for euro and VP for DKR and euro)**
 - **The Eurosystem has committed firmly to deliver T2S no later than 2013**
 - **The CSDs' commitment needs to be made firmer, so that:**
 - CSDs which invest in the T2S world do not find their investment plans destroyed by others withdrawing their volumes
 - The Eurosystem gets a “fair” matching response from the industry.
 - **Can CSDs commit volumes several years ahead? Can even their clients do so?**
 - **Are realistic penalties for breach feasible?**
 - **Suggestions:**
 - Provide economic incentives for parties taking the risk of early commitment
 - commitment means planning, and publishing the plans, for system changes, migration, pricing etc
- CSDs should embrace the change, to meet banks' needs**
- no special T2S deals, even for the last CSD to deliver its volumes

Conclusion

Summary of the main challenges

- **Building T2S:**
 - In time: 2013 at the latest
 - Within budget: approximately € 200 million
 - According to the User Requirements: 800 pages
 - Governance to be further discussed / Separate legal entity?
- **Maintain/Increase commitment:**
 - Binding contract with CSDs
 - CSDs and users to invest to adapt to T2S

The five big wins of T2S

- Making cross-border settlement fees as inexpensive as domestic fees
- Reducing users' collateral/liquidity needs
- Harmonising settlement to make Europe a true Single Market
- Create new opportunities for competition
- Market users will only need an account at one CSD to settle any transactions in securities within T2S

The Eurosystem and the market believe in T2S and are ready to take the challenge and invest in it.

