"Focussing on risk management and fostering a standing dialogue with our users on risk-related issues are key priorities on our agenda"

Reducing the risk exposure of EURO1 Participants towards the system has been a major agenda item on which EBA CLEARING made tangible progress over the past 12 months. Gilbert Lichter, CEO of EBA CLEARING, provides an update.

Q: Over the past 12 months, EBA CLEARING has carried out a comprehensive review of the risk profile of the EURO1 system, where do we stand now?

The objectives of the program were threefold: firstly, to improve the risk management tools available to the participants combined with an important reduction of the mandatory credit risk taking on the part of each participant in the system; secondly, to protect the system's integrity – and through this the position of its participants – in the case of severe turbulence in the market, potentially resulting from political uncertainties; thirdly, to maintain the very high level of liquidity efficiency of the system which is seen as one of its key benefits.

Q: What are the improvements to the participants' capability to manage their credit risk in the system?

Participants can now review and reduce the bilateral limits granted to the other participants up until 7:00 CET in the morning for effect on that day. This allows them to react promptly to overnight developments in the financial markets. Additionally, we have reduced the mandatory minimum amount for bilateral limits from EUR 5m to EUR 1m.

This means that in a situation of a serious deterioration of a participant's credit standing, the other participants are able to reduce their exposure on that stricken participant to the minimum of EUR 1m before the start of the operating day.

> "We have adopted a catalogue of measures that we will action in case of severe problems in the market to protect the participants in the system."

Q: How did the Company prepare for protecting the integrity of the system in case of severe problems in the market?

Under the guidance of the Board Risk Committee, we have analysed a number of scenarios in relation to potential developments of a disruptive nature in the financial markets and the political environment. This has led us to adopt a catalogue of measures that we will action in case of such developments, again with the objective to protect the participants in the system.

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Q: Can you tell us more about this?

The Board Risk Committee has decided to refrain from communicating details on this matter, which by the way is in line with the approach taken by most of the banks as regards their own contingency planning.

Q: But can the Company afford not to communicate at all on this subject?

We fully recognise that there is a legitimate interest on the part of the participants to understand the Company's approach in dealing with these issues and we are convinced that a dialogue with the risk managers of the participating banks is of real mutual benefit. The Board therefore decided to create a Risk Managers Forum – as a platform for a standing dialogue between the Management and interested risk managers from the banks. We think that such an environment will facilitate an exchange of information on emergency planning.

“We are putting in place a Risk Managers Forum – as a platform for a standing dialogue between the Management and interested risk managers from the banks.”

Q: Will the Forum limit its scope to an exchange of information on emergency scenarios and potential implications?

No, the Risk Managers Forum has a much broader scope. When we implemented our risk management framework, we decided that we wanted to open up a wider dialogue with our participant community on risk management and risk mitigation in FMIs. So we agreed to put in place a forum that would allow interested participants to engage in this exchange with us. We certainly would like to take the opportunity of such a dialogue to present in greater detail the risk profile of the EURO1 system; at the same time we will explain the risk management tools provided to the participants to mitigate their risks related to participating in the system. We would as well like to discuss in the Forum issues arising from the implementation of the new CPSS IOSCO Principles for FMIs. We believe that it would be highly beneficial to address a number of oversight requirements – such as stress testing, recovery and resolution planning and others – together with the participants and, in particular, their risk managers.

Q: When will the Forum be launched?

We are planning a first meeting for mid-December. Invitations will be sent to all EURO1 Participants in the coming days.

Q: You said the third objective is about maintaining the high liquidity efficiency of the system – what is the approach on this item?

This is a very important aspect; there is no doubt that efficient liquidity management tools are critical. When reducing the mandatory minimum amount for bilateral limits, we were very much aware of the risk of deflating the liquidity available in the system. We therefore increased the maximum amount for the discretionary element of the bilateral limits – in addition to the mandatory amount – from EUR 25m to EUR 50m.

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In this way, participants can generate their required liquidity and payment capacity while at the same time pursuing a highly differentiated credit risk approach.

Q: Does this mean that the review of the risk profile of the EURO1 system is now closed or will the mandatory minimum limit be further reduced to zero?

The Board came to the view that the question of abandoning the mandatory bilateral limits requires first an in-depth analysis of possible consequences, not least on the liquidity in the system and the risk sharing philosophy underlying the system. The Future Development Group (FDG) has been assigned to examine the matter. I could foresee that this question is addressed as part of the FDG's broader proposals to evolve the EURO1 system in the light of the new Principles for FMIs and – inevitably – of the migration of the payments industry to SEPA and ISO 20022. I should add that we expect an increase of the collateralisation requirements as a result of the upcoming implementation of the Principles for FMIs, which will add pressure to eliminating "multiple" participation in EURO1 by different entities of the same banking group.

"EURO1 Participants are able to generate their required liquidity and payment capacity while at the same time pursuing a highly differentiated credit risk approach."

Q: When do you expect these proposals to be delivered?

The FDG together with the Management is working towards presenting first results at the next Shareholders meeting in May 2013.