ESRB
European Systemic Risk Board
European System of Financial Supervision

Exploring systemic risks in European securities financing transactions markets: First steps to close data gaps

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Where to from Here? The case of European securities financing transaction markets

- Lack of transparency in repo and securities lending markets globally acknowledged (FSB)
- Data gaps in the European SFT markets larger than in the US markets
- Features of repo & securities lending markets
  - Market-based nature
  - Strong degree of interconnectedness
  - Individually low-risk activities at large scale, may require backstop
- Broad Implications for the closure of data gaps
  - Information must be sufficient granular to be risk-relevant
  - Information must be gathered at the entity-level

ESRB One-off data collection: Scope and Objectives

Fact-finding exercise on two topics:

1. Assessment of collateral management practices of credit institutions
2. Cash re-investment programs of agent lenders

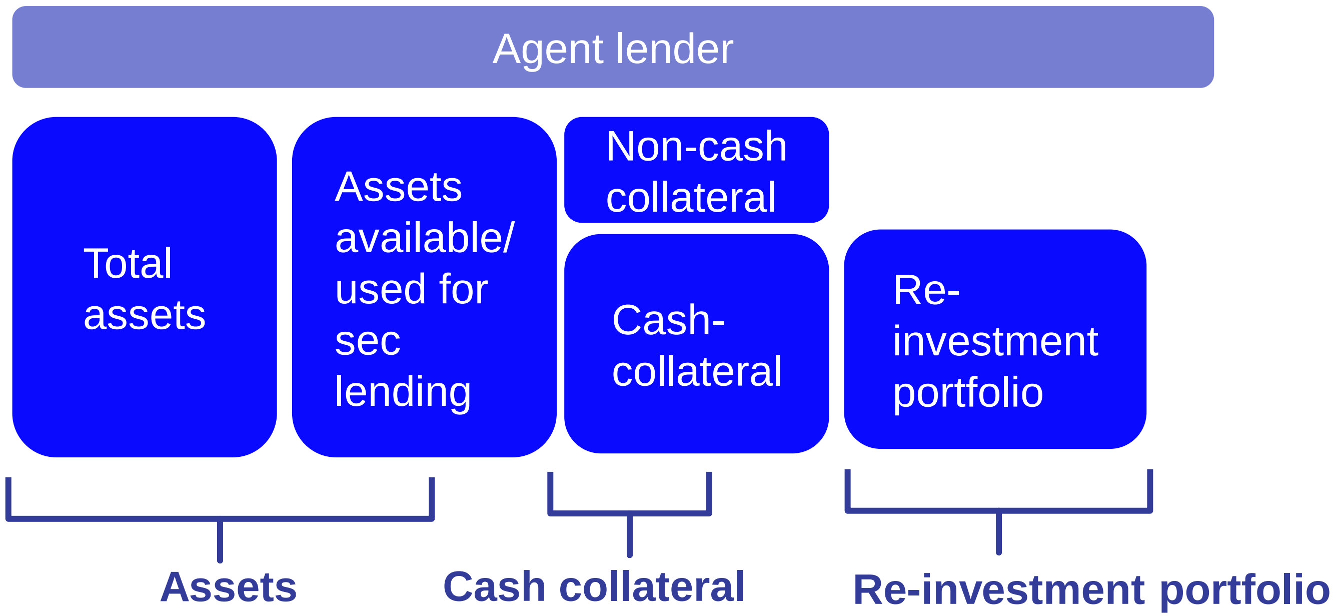
Scope

- Data collection addressed to 38 banking institutions and 15 agent lenders (separate samples)

First step towards monitoring framework

- Templates yielding desired information, assessment of risks
- Cost/benefit analysis; identification of desirable type of monitoring

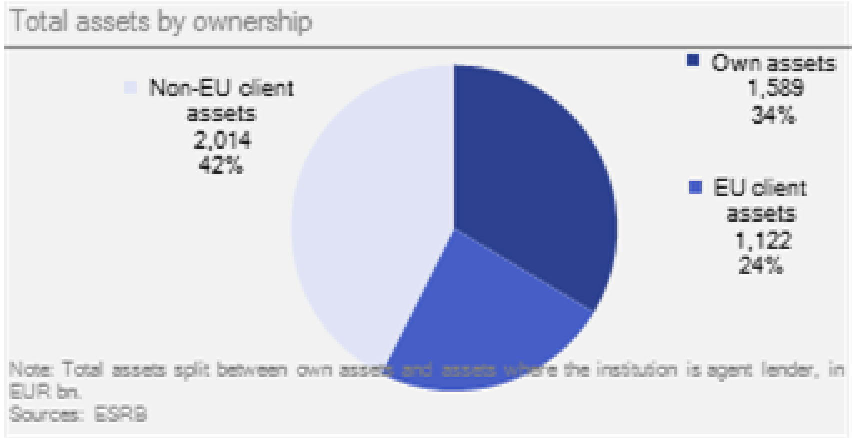
Data collection on re-investment of cash collateral



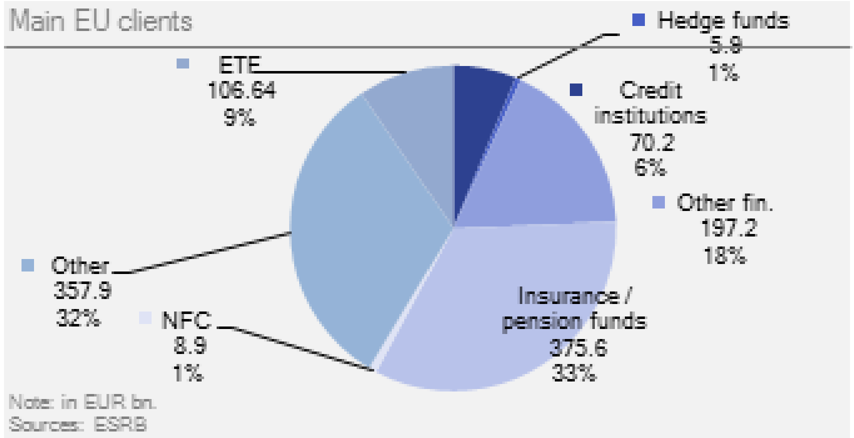
- Credit intermediation outside of the banking system
- Data gaps: Information available only at aggregate level by currency space

Re-investment of cash collateral : Lendable assets as source of cash collateral

- Cross-border linkages: High EU - non EU interconnectedness



- Main EU clients are insurances / pension funds, OFIs, Banks, ETFs, MMFs and HFs

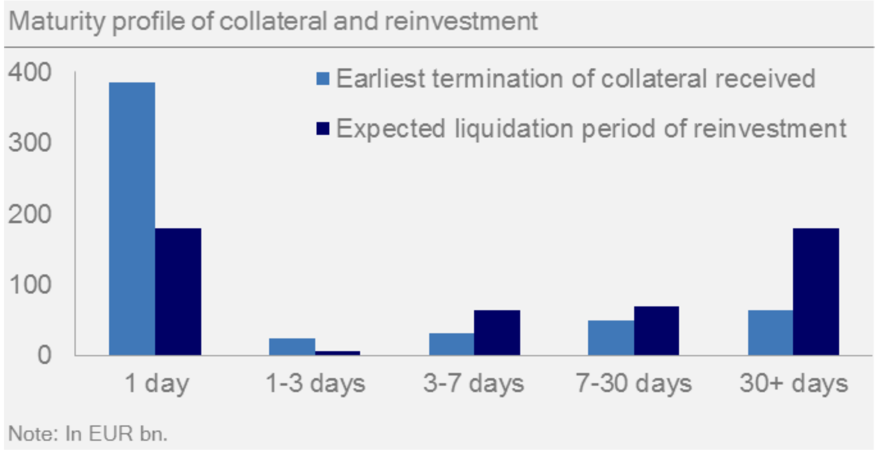


- ~ 75% of total assets are available for securities lending.
- ~ 64% of collateral is cash (mostly open maturity)

Note: Results presented here are preliminary

Re-investment of cash collateral : Maturity and liquidity transformation

- Earliest termination
  - 1 day for 70% of transactions



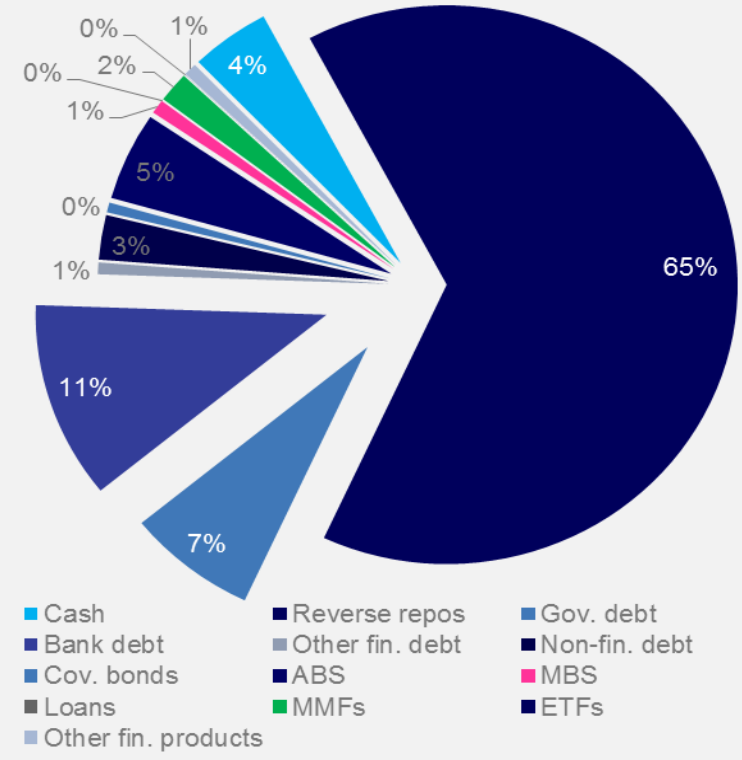
- Risks
  - Liquidation risk: open maturity of cash received vs term maturity of cash reinvested
  - Maturity risk: earliest termination of liabilities shorter than expected liquidation of assets

Note: Results presented here are preliminary

Re-investment of cash collateral : By asset type

- Mainly in
  - reverse repos (65%)
  - MFI debt (11%)
  - Sovereign debt (7%)
- Reverse repos expected liquidation period shorter than for other instruments
- Collateral reinvested in high credit quality instruments (92% IG)
- Interconnectedness between securities lending and repo markets: Most cash collateral received from securities lending transactions is reinvested in reverse repo

Cash collateral reinvestment by asset type



Note: In % of total.

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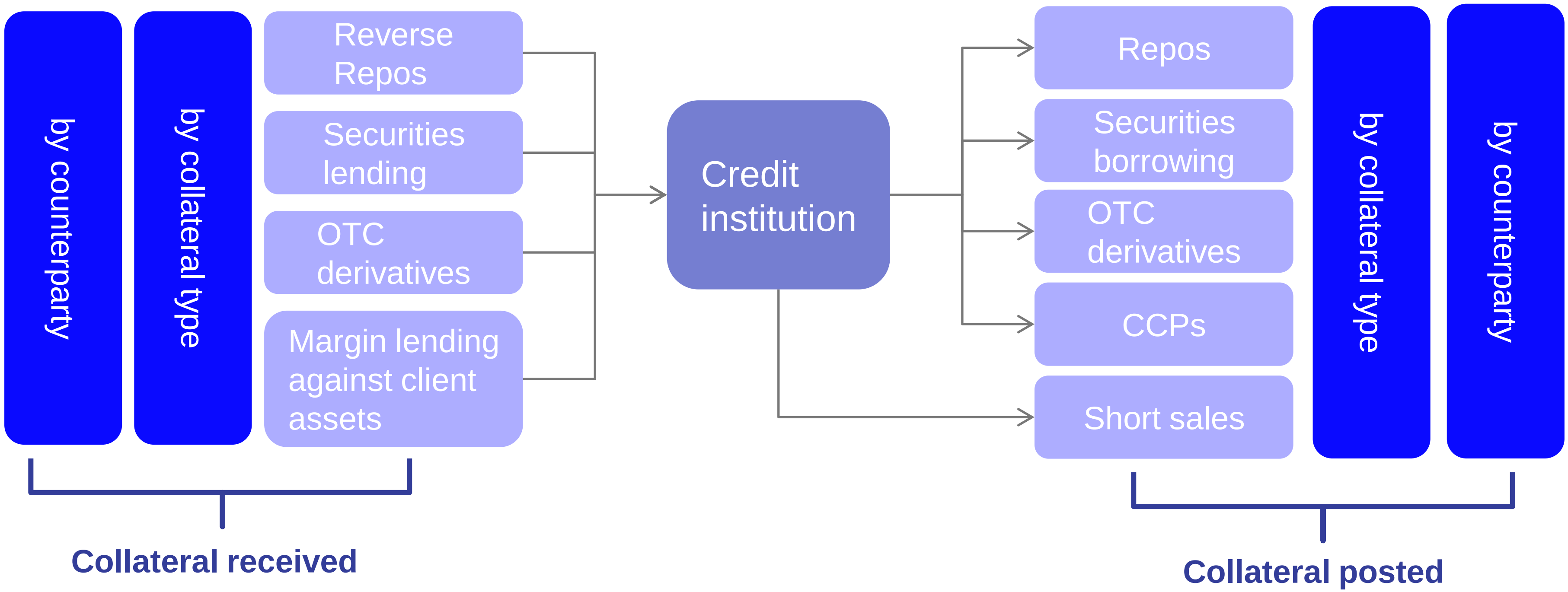
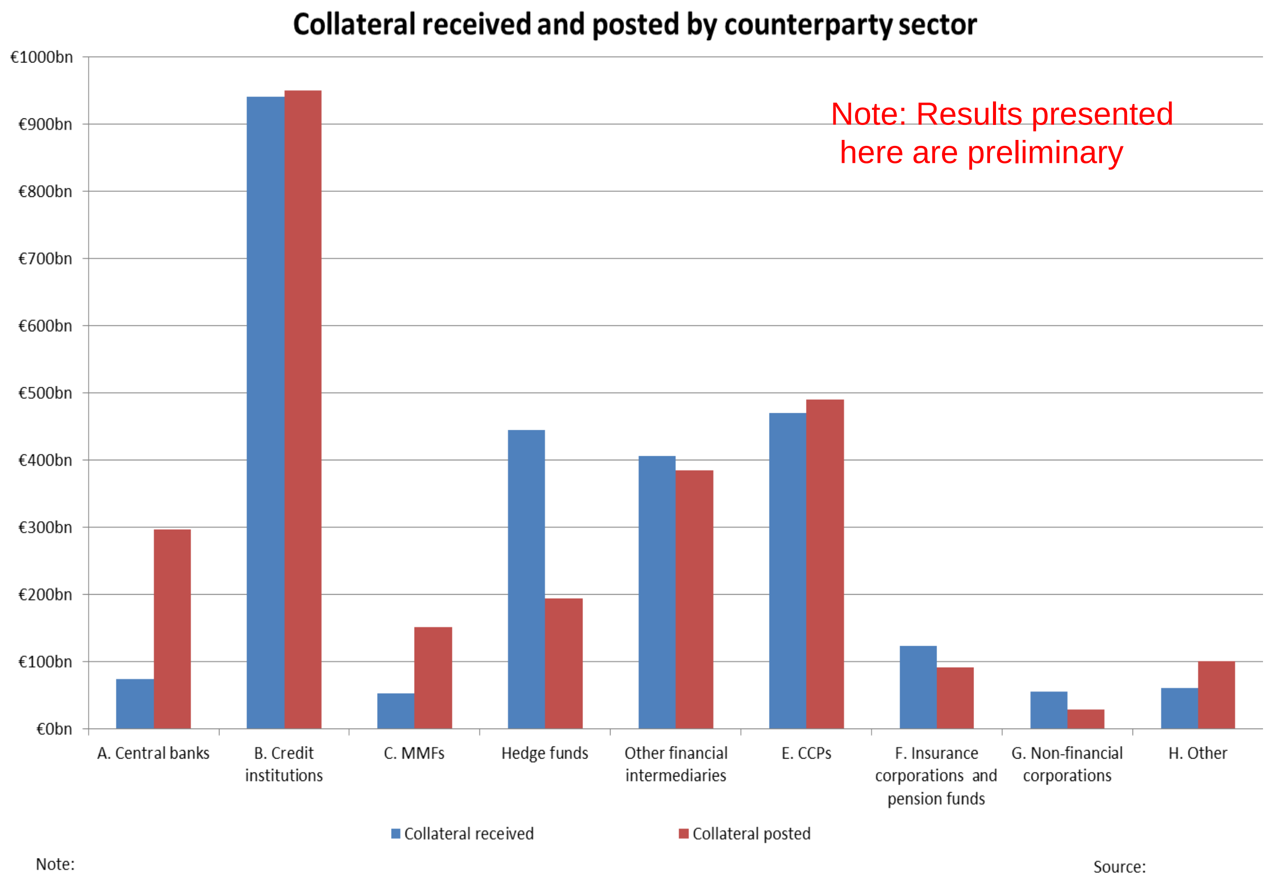
Data collection on non-cash collateral



- Potential macro-prudential risks:
  - Interconnectedness
  - Increase of opaqueness
  - Exposure to collateral market fluctuations
  - Increase of leverage and pro-cyclicality (velocity of collateral)

Non-cash collateral: Counterparty sectors

- Credit institutions and CCPs are the largest counterparty sectors
- Hedge funds are largest net collateral providers
- Central banks and, to a lesser extent, MMFs are largest net collateral takers



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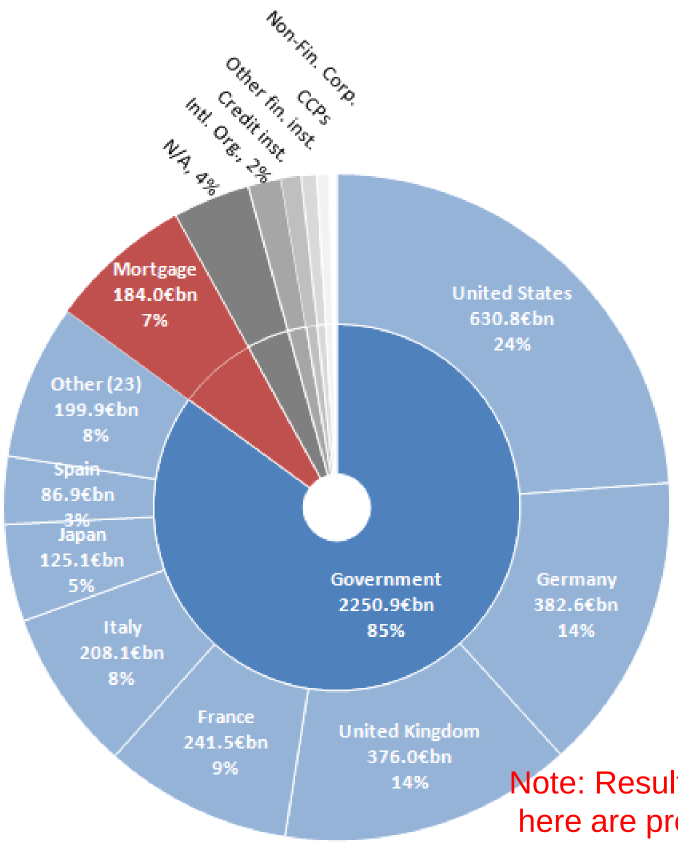
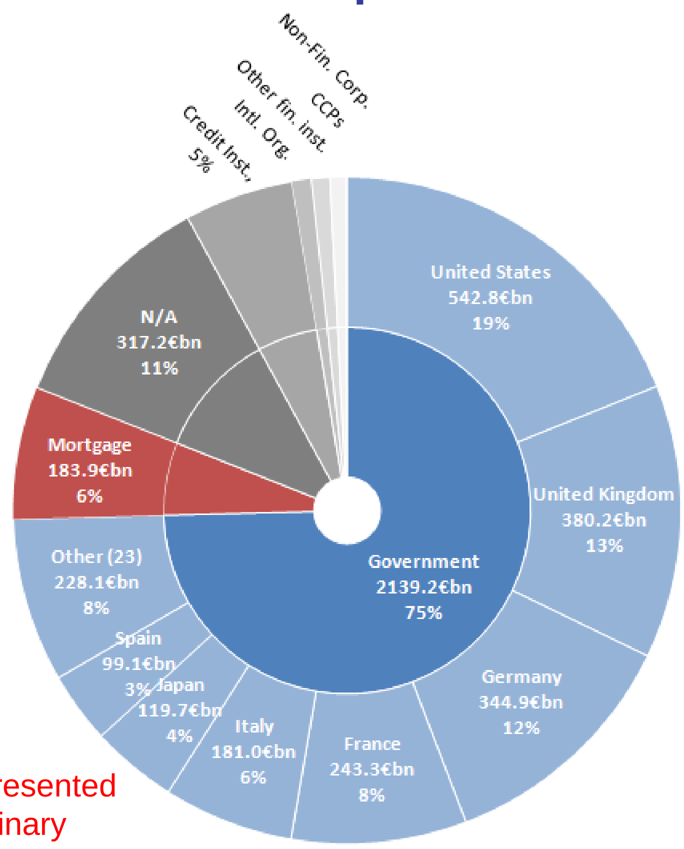
Non-cash collateral: Collateral transformation by banks

Collateral received



Collateral posted



Indication of collateral transformation: Relatively more (less) higher (lower) quality collateral is received than posted

Note: Results presented here are preliminary

Concluding remarks

- Closing data gaps is a policy objective in itself in the shadow banking sector
- Large scale efforts in well-identified areas worthwhile (e.g. trade repositories for SFTs)....
- ...but "small step" data collection efforts can offer valuable intermediate input for macro-prudential supervision by providing:
- Entity-level information
  - Identification of cash reinvestment chains
  - Mapping of sectoral linkages and network structure in collateral markets
- Granular and risk-relevant information
  - Assessment of degree of maturity and liquidity risk of cash reinvestment programmes
  - Assessment of collateral transformation and maturity profile of collateral trades