Summary of the ECB OMG
Global Operations Managers' Conference

Treasury operations: striking the balance between efficiency and resilience

23 and 24 April 2007, Frankfurt am Main

Opening remarks

Mr Francesco Papadia, Chair of the ECB Foreign Exchange and Money Market Contact Groups (FXCG and MMCG) – joint parent groups of the ECB Operations Managers Group (OMG) – opened the conference and invited Ms Tumpel-Gugerell of the ECB Executive Board to give the formal welcome speech.

Welcome speech
Speaker: Ms Tumpel-Gugerell, Member of the Executive Board of the ECB.

Ms Tumpel-Gugerell welcomed participants to the third Global Operations Managers' Conference hosted by the ECB Operations Managers Group. She made reference to the earlier conferences in this series hosted by the operations managers groups of the New York Foreign Exchange Committee in 2003 and the London Foreign Exchange Joint Standing Committee in 2005. In this regard she pointed to the ongoing need for addressing operations issues at a global level in view of the unregulated nature of the FX market and its substantial size and emphasised the advantages of having a well-functioning communication and cooperation framework via the various global FX market groups.

Ms Tumpel-Gugerell then provided some background on the ECB market groups, namely the FXCG, MMCG and the OMG as well as the wider participation to the conference. In terms of conference participants, Ms Tumpel-Gugerell expressed her delight to see so many representatives from the FX market at the conference – drawn from key financial institutions across Europe, the US and Asia, critical infrastructure providers, wire services, electronic broking providers, buy-side representatives, legal associations, data providers and more. As the ECB OMG is a sub-group to both the FXCG and MMCG, she further noted that there were a number of representatives from the money market side – an aspect which she felt would add to the debates at the conference given the obvious link between FX and money markets.

With regard to the conference theme "Treasury operations: Striking the balance between efficiency and resilience", Ms Tumpel-Gugerell commented on the importance of both components for properly functioning markets and the improvements in both areas over recent years. In addition to addressing the difficulties sometimes associated with achieving a high level of resilience while still remaining efficient, she noted the intention of the conference organisers to view resilience in the broader context of robustness and not purely business continuity.

Ms Tumpel-Gugerell concluded her speech by expressing her hope that the conference would provide a further opportunity to continue moving towards global solutions.

I. Ensuring readiness and resilience

Panel discussion on resilience in operations

Moderator:
Eloy Lindeijer (De Nederlandsche Bank, Member of the OMG)

Panel speakers:
Harry Newman (SWIFT)
Joe Halberstadt (CLS)
René Steenhart (Rabobank)
Filip de Wolf (Ascure)

This session examined resilience in operations from the perspective of critical infrastructure providers and financial institutions. Eloy Lindeijer moderated the session which commenced with the following presentations:

SWIFT Resilience (Harry Newman, SWIFT)

The built-in resilience of SWIFT was presented ("Failure is not an option"), covering:

- SWIFT Operating Centres resilience based on a layered-approach;
- the SWIFT crisis co-ordination and communication group which aims to promote operational order in the financial community in the extreme situation of a total SWIFT outage and while SWIFT is busy restoring services;
- the resiliency of the IP network based on a multi-vendor approach;
- the increasing level of customer resilience; and
- the ongoing efforts of SWIFT to increase central and customer resilience.

Ensuring readiness and resilience (Joe Halberstadt, CLS)

The presentation provided:

- a summary of CLS'current market position which revealed an average $3 trillion daily settlement volume on the basis of around 300,000 instructions per day;
- the CLS resiliency infrastructure which is based on duplication of systems, a suite of failure management tools and procedures, regular testing (internal/external) and analysis of varied scenarios.

Ensuring readiness and resilience (René Steenhart, Rabobank)

The presentation examined the topic from the perspective of a single global financial institution and focussed on:

- defining resilience for an individual institution;

- the implications of failures involving critical infrastructures for an individual institution; and
- the differing approaches from the regulatory side to resiliency (Europe v US for example) and the question of whether there should be a move to a uniform approach.

Basics of crisis management (**Filip De Wolf, Ascure**)
The presentation reviewed the basic elements of sound crisis management, covering such aspects as:

- the need to ensure abilities to carry out activities manually despite the move towards greater automation over time and the resulting lack of familiarity with manual procedures;
- the need to ensure that the team being put together to handle the crisis can (and ideally has) work(ed) together;
- the risks to sound crisis management;
- traditional versus modern approaches ("fight the crisis" versus "manage the crisis"); and
- operational structure of crisis management, with a particular focus on the importance of communication and soft factors and a list of the don'ts to be considered in crisis management.

In the discussion which followed, the moderator invited the panel members to reflect on their respective approaches to ensuring readiness and resilience against the background of every failure being unique. During the responses, reference was made to the need for making information widely available and carrying out "root cause analysis". In terms of communication, SWIFT made reference to its widespread use of its website as a means of communication to the market at large while CLS elaborated on their ongoing work on the crisis communication protocol and their intention to get the views of the market, possibly via regional FX groups as well as the traditional central bank channels.

Among the points raised by the audience was the issue of the overall dependency of the financial sector on infrastructures such as SWIFT and CLS but increasingly also on certain large commercial banks and whether there should be a limit placed on the share of the market given to the latter. This prompted debate on whether Europe in particular should move further and faster to harmonise business continuity requirements and the overall nature of business continuity testing. With regard to testing, one participant pointed to the general static nature of testing which should be seen in contrast to the more dynamic nature of crises and the panel member from SWIFT reaffirmed the benefits of unscripted tests which the organisation conducts. The discussion also reflected on the resilience of human resources, with one participant enquiring whether there were recommendations advocating the use of split offices. In response, the panel noted the merits of reducing dependency on main office sites and moving towards home offices for staff.

In his wrap-up for the session, the moderator acknowledged the need for all market participants to remain humble when assessing their respective level of business continuity preparedness. He recalled that despite the substantial investments in business continuity and the general high degree of preparedness for a major operational disruption, there is always room for improvement and maintaining a certain level of paranoia can serve one well. In terms of challenges for the market, the moderator referred to those in the regulatory sphere and indicated that it would be interesting to see how Europe moves in this regard in the coming years.

Ms Tumpel-Gugerell closed the session by highlighting the key messages she took from the presentations and panel discussion. In this regard she referred to the need for regular and good testing exercises, the need for standardisation and harmonisation across the market, the need for a better understanding of the interdependencies between infrastructures and the possibilities to learn from the best in the field. She concluded by expressing her hope to see a list of actions being developed on the basis of the earlier discussion and followed up in the aftermath of the conference.

II. Achieving operational efficiency

Panel discussion on strategies for reducing operational cost

Moderator:
Paul Abraham (ABN Amro Central Enterprise Services Private Ltd. (ACES))

Panel speakers:
Paul Abraham (ACES)
Niklas Bartelt (DZ Bank)
Andreas Gaus (ACI Education – Credit Suisse)
Ronald Vergeer (ABN AMRO Bank)

This session looked at strategies for reducing operational cost at specific financial institutions as well as the related need for having in place a team of competent and skilled staff. Paul Abraham moderated the session which commenced with the following presentations:

Strategic Sourcing – the efficiency game (Paul Abraham, ACES)

The strategic sourcing option as employed within the ABN Amro group to achieve efficiency was described with reference to:

- the initial motivation for the project, which stemmed from a recognition of the need to achieve smarter management of enterprise costs, especially for knowledge based industries and against a background of globalisation, advances in technology and a need for insulation against business cycles;
- the strategy as employed versus the end-result, with a particular focus on the additional and unexpected gains to emerge;
- the benefits and challenges of offshoring and how the model evolves over time to yield continuous gains;
- elements such as the concentration risk which is of a magnitude not previously known in the organisation and the quality and resourcing of staff (with 300 – 400 hires per month in the initial period); and
- the outlook for the future, where it is envisaged that operations will become a utility in its own right, standing apart from the organisation and becoming more of a revenue contributor.

Achieving operational efficiency – strategies for reducing operational cost (Niklas Bartelt, DZ Bank)

The presentation focussed on the potential for achieving operational efficiency via pro-active management of operations platforms along their life cycle and covered such aspects as:

- concentration on improving the input-output relationship (optimization of systems/processes, economies of scale/scope) rather than sole focus on input price reduction (off-shoring);
- the changing importance of the efficiency optimization levers along the typical phases of the operations platforms life cycle (innovation, growth, maturity) and how to leverage this changing importance.

The presentation concluded by illustrating this approach via DZ Bank's payment processing platform as an example which, inter alia, captures scale advantages through cooperation with other market participants.

ACI – The Financial Markets Association – Operations Certificate (Andreas Gaus, ACI Education - Credit Suisse)

The presentation provided an overview of the new ACI Operations Certificate, with reference being made to:

- the overall ACI education programme;
- the business case for the new ACI Operations Certificate against the background of operations staff being required to act almost as pilots, especially in the area of crisis management;
- the aims and characteristics of the new qualification; and
- the next steps for implementation of the Operations Certificate, with the Go Live foreseen for June 18, 2007.

Treasury operations – Striking the balance between efficiency and resilience (Ronald Vergeer, ABN AMRO Bank)

The efforts and achievements of ABN Amro on the efficiency side were recalled during the presentation, focusing on the centralisation of its European treasury function from 2001 – 2005 and the offshoring of global treasury operations processing activities from 2004 to 2006. While trading may take place across a variety of ABN Amro European offices, the back office function is centralised in Amsterdam, with the processing taking place at the offshore site. The FTE savings achieved during the centralisation and offshoring projects were further elaborated, noting that the FTE savings during the centralisation project were achieved without any increase in staff in Amsterdam.

Following the individual presentations, a number of questions were raised to the panel by the audience, with a keen interest being displayed in the offshoring strategy applied by ABN Amro. The questions raised in this respect covered such aspects as the business functions transferred to the offshore site, the time to market for introduction of new products, whether processes were re-engineered before transfer, the capacity to handle more complex products, the before/after ticket price, the allocation of losses, service guarantees and cultural differences. The responses by the ABN Amro / ACES panel members elaborated on the functions transferred (namely banking processing and IT), the transfer process which included both the "pick and drop" approach as well as "improve then drop" approach, how the offshore site has moved on from plain vanilla to more complex products such as derivatives, cost pressures – in particular concerning staff given the popularity of the chosen offshore location, the expectation that gains will continue to materialise and thereby offset inflationary pressures and the importance of Service Level Agreements. In terms of cultural differences, it was acknowledged that these clearly exist and have played a role and remain a factor to be taken into account on an ongoing basis.

II. Achieving operational efficiency

Panel discussion on balancing operational efficiencies and regulatory controls within a changing derivatives market-place

Moderator:
Paul Dillon (AIB, Chair of the OMG)

Panel speakers:
Patricia Mosser (Federal Reserve Bank of New York)
Holger Hartenfels (Deutsche Bank)
Stuart McClymont (Deutsche Bank)

This session again examined operational efficiency, although with a specific focus on the derivatives market and the regulatory environment. Paul Dillon moderated and introduced the session, which commenced with the following presentations:

Remaining Challenges in OTC Derivatives Processing: A Federal Reserve Perspective (Patricia Mosser, Federal Reserve Bank of New York)

The presentation examined the achievements to date and work still to be carried out with respect to CDS and equity derivatives processing. In this respect, the following aspects were covered:

- underlying conditions in the CDS market – in particular, the high growth levels and the substantial confirmation backlogs as well as problems arising from novations without notifications;
- the regulatory response, with international regulators and the largest dealers meeting in September 2005, following which significant progress was made in reducing the confirmation backlog, increasing electronic confirmation processing and adopting the ISDA Novation Protocol, with further improvements anticipated via creation of an industry utility warehouse, the announcement of a cash settlement protocol and the development of processing guidelines; and
- an overview of the challenges that lie ahead as regards equity derivatives processing, with the lack of standardised documentation and lack of automation being among the key issues alongside outstanding confirmations.

Balancing Operational Efficiencies and Regulatory Controls Within a Changing Derivatives Market Place (Holger Hartenfels, Deutsche Bank)

The importance of trade confirmations was addressed in this presentation, looking in particular at:

- the purpose of confirmations, including evidential aspects and the requirement to confirm “without delay”;
- possibilities for financial institutions to enhance confirmation processes;
- the role of confirmations in close-out netting and the use of master agreements, with a reflection on the so-called bottom-up approach where the confirmation refers to the master agreement versus the top-down approach where the master agreement specifies that it governs all transactions irrespective of whether or not they refer to it; and
- the issue of unauthorised transfers and the improvements achieved via the 2005 ISDA Novation Protocol.

Achieving Operational Efficiency in the OTC Derivatives Market (Stuart McClymont, Deutsche Bank)

The presentation looked at the specifics of how operational efficiency might be achieved in the OTC derivatives market. In this regard the presentation covered:

- the opportunities for achieving STP across the complete transaction chain and thereby minimising the current relatively high potential for error, in particular on trade date;
- the challenges to be faced in terms of the complexity of the market place, i.e. multiple institutions, processes and vendors and lack of interoperability between each; and
- the need for the OTC derivatives industry to change the way it supports and processes transactions by increasing automation at the level of trade execution and matching rather than in later processes such as collateral, settlement, documentation and middle office as tends to be the case.

In the discussion with the wider audience, there was a further reflection on the institutions behind the moves to enhance efficiency in credit and equity derivatives. In this regard Patricia Mosser explained how the FSA had released a letter earlier in 2005 on confirmation backlogs while the New York Fed took the initiative later that year to meet with key regulators and market players. For the current work on the equity derivatives side, 18 institutions are involved. While the New York Fed continues to host the meetings, the view of the regulators collectively is to ask the industry to come up with a solution. On the subject of having all confirmations issued and matched on trade date, there was a feeling from the audience that this was somewhat unrealistic however Stuart McClymont argued that it could be achieved through means such as better education of clients and assistance of clients with automation.

III. Industry developments - part I of II
TARGET2 & TARGET2-Securities
Speaker: Jean-Michel Godeffroy (ECB)

For the first of a two-part session on recent industry developments, an overview of TARGET2 and TARGET2-Securities (T2S) was provided by Jean-Michel Godeffroy of the ECB.

In the case of TARGET2, the presentation recalled the details of the current TARGET large value payment system for euro and the motivation supporting the move towards the new TARGET2. Reference was made to the decision-making process underlying the move to TARGET2 and the project organisation, with the main achievements of TARGET2 then elaborated (i.e. standard service via single price structure, full technical consolidation, advanced liquidity saving features and enhanced robustness and resilience). The presentation on TARGET2 concluded with an overview of the changes that might be expected from an overall European perspective in terms of competition, efficiency and consolidation.

The T2S presentation commenced by reviewing the current situation as regards the costs for domestic and cross-border settlement in the EU and US, with EU cross-border settlement costs dramatically higher than EU domestic or US settlement costs. In the absence of a market initiative to redress this imbalance over the eight years since the introduction of the euro, the ECB/Eurosystem has presented the T2S concept for securities and cash settlement in one platform and at a considerably reduced cost. An overview of settlement currently and under T2S was then presented, following which the governance of the current User Requirements phase and the project timeframe was elaborated, with current planning foreseeing final deployment of T2S by March 2013.

Panel discussion on developments in the FX prime brokerage arena
Moderator:
Andrew Grant (Morgan Stanley)

Panel speakers:
Andrew Coyne (Citigroup)
Roger Allen (Merrill Lynch)

Continuing on the topic of recent industry developments, this part of the session focussed on the FX prime brokerage arena and how developments in this field are impacting operational processes and associated risk. Andrew Grant moderated the session and provided an overview of the prime brokerage product and its evolution and outlined some of the risks and challenges which the product has brought to operations managers. Against the background of the rapid growth in the business, he referred to the fact that processes are not fully automated, how the increased ticket volumes bring a far greater potential for errors, and without real-time reconciliation tools, the processing of checking bank and client side notifications proves to be extremely labour intensive. He went on to explain how, related to the reconciliation risk, the legal agreements are established between prime brokers and executing banks to govern the service, as well as the progress achieved by the work of the New York Foreign Exchange Committee in publishing industry standard Master FX Give-Up Agreements which many banks have now adopted. As the FX prime brokerage service has matured and automation increased, most major market players are in a position to offer the product to their client base. As such, competition has increased, fees have compressed and prime brokers may no longer generate significant revenue from FX intermediation alone, leading to the offering been seen as part of a firm's overall strategy, in particular as clients extend their reach into more sophisticated products and services.

The individual presentations were as follows:

Developments in FX Prime Brokerage (Andrew Coyne, Citigroup)

The presentation looked at the following aspects of the FX Prime Brokerage (FXPB) market:

- the underlying growth, driven by such factors as FX eCommerce, anonymity on ECNs and new entrants to the market using high volume program trading;
- the role of direct market access insofar as FXPB provides clients with access to multiple liquidity venues as well as to banks;
- issues for FXPB and FX operations in terms of volumes and costs; and
- an outlook on future developments as regards reducing ticket volumes and developing a clearing model.

Multi-Asset Class Prime Brokerage (Roger Allen, Merrill Lynch)

The focus for this presentation was on the development of multi-asset class prime brokerage and included:

- a reflection on the Merrill Lynch approach via a single platform across all asset classes together with cross margining and netting in a collateral efficient way, financing solutions, derivatives intermediation and strong supply in both equities and fixed income securities to facilitate stock lending and repo;
- an overview of the operational and reporting features of the supporting technical solution for multi-asset class prime brokerage and the client services provided; and
- an assessment of FXPB in terms of technology, automation and service requirements.

In the course of the follow-up discussion, the panel was invited to elaborate on the strategy of large hedge funds in employing prime brokers. In this regard the panel clarified that the larger hedge funds tend to have around 3 to 4 prime brokers, mainly for confidentiality reasons, while the smaller hedge funds would tend to have 2 for due diligence purposes. Reference was also made to the difficulties associated with changing prime brokers, prompting many clients simply to add rather than replace. A question was also raised on the implications of the MiFID for prime brokerage clients, with the panel noting the complications arising from the fact that different countries are at different stages of implementation of the Directive. Pre-operational netting was also touched on in the discussion, together with the implications this has for the use of CLS, although the panel members pointed to the preference of prime brokers generally to see CLS as part of any solution. With regard to collateral management in a multi-asset class environment, it was noted that one central system is required to collate all the information and it has taken years to achieve the current levels of automation on the collateral side. Another element raised in the discussion was how the development of prime brokerage has impacted competition among ECNs, with the panel drawing attention to the efficiency that has been achieved and how the situation has evolved to effectively become almost an exchange.

IV. Reflections from international committees

The role of international treasury committees in striking the balance between efficiency and resilience

Moderator:
Francesco Papadia (ECB, Chair of the FXCG, MMCG)

Panel speakers:
Richard Mahoney (FXC – The Bank of New York)
Leigh Meyer (FXJSC Operations sub-group – Citigroup)
Werner Studener (FXCG – ECB)
Tetsuya Inoue (TFEMC – Bank of Japan)
Bill Chua (SFEMC Operations Sub-committee – United Overseas Bank)
Kitty Lai (TMA – Hong Kong Monetary Authority)

In inviting the representatives from the international committees to reflect on their respective committees' role in striking the balance between efficiency and resilience, Francesco Papadia, as moderator, posed 3 questions covering:

- the challenge of responding to a continuously changing market place;
- developments such as prime brokerage and the opening up of the buy side; and
- the role of the committees in ensuring a robust and fair functioning of the FX market.

With regard to the challenge of responding to a continuously changing market place, the panel members elaborated on the nature of their committees, the type of activities each engages in and specific topics where they have directed their attention over the past couple of years. Among the topics referred to were business continuity, liquidity, electronic trading, IT platforms, educational needs, market and product development, operational risk, industry consolidation, entrance of new players to the market, NDFs, trade confirmations, standard settlement instructions and SWIFT mandates.

In response to the question on prime brokerage and the opening up of the buy-side, reference was made to FX margin trading in Tokyo which has become famous in the context of the so-called "carry trades". It was further noted that the impact of such FX margin trading is not negligible, with around JPY 3.5 trillion in outstanding positions as at end-September 2006.

The third question concentrated on ensuring a robust and fair functioning of the FX market, with the panel members again pointing to specific activities they have addressed in this sense as well as codes/best practices/recommendations etc. as established or endorsed by their respective committees. They also highlighted their underlying intention of supporting and facilitating new developments in the markets and reference was made to how the committees have also given attention to the specific participants in each market and not only the instruments being traded. One panel member referred to the fact that although the FX market could be considered to be very mature, there is a large swathe of new currencies coming in, giving rise to the need for greater collaboration which can be achieved through more extensive sharing of views and ideas between international treasury committees. Focussing on the back office level, the increase in bespoke products as well as certain currencies which are more difficult to settle were identified as topical subjects where the establishment of common protocols for the settlement processes could benefit the market overall. Some ideas were also exchanged on the possibility of moving towards a global code or global set of best practices based on the existing codes/practices established by individual treasury committees.

During the open discussion, questions were addressed to the panel on such aspects as the emergence of FXMarketSpace and its likely impact on the market and how to ensure that best practices are consistently followed by all market participants and the extent to which they should be made obligatory. Regarding FXMarketSpace, the panel generally took the view that it was a welcome development that would lead to greater transparency and resilience and could be easily embedded into operational practices. On the issue of obligatory best practices, the panel felt this would be difficult to achieve, with one panel member indicating a preference to move more towards establishing global best practices than in the direction of obligation. In response to a further question on monitoring of compliance, one panel member recalled the heavy regulation of financial institutions and their need therefore to comply with best practices versus the absence of regulation for other categories of market players.

In wrapping up the session, the moderator noted that from a general financial market perspective, it can be said that the different global committees have appropriately dealt with the substantial changes that have taken place and can even be said to have acted proactively and guided developments. From a more philosophical or intellectual perspective, he concluded that the discussion allows one to draw some idea on the ability of markets to self-regulate and that this is not connected only to the FX market. Against the background of these two developments, the moderator went on to mention the references to a more global approach during the earlier discussion – a progression that could be considered as natural given that we operate in global markets – and he concluded with the suggestion that this aspect might be taken up on a more detailed basis at the next global operations managers conference.

V. Industry developments – part II of II
Panel discussion on electronic trading

Moderator:
Johan Evenepoel (Dexia, Member of the MMCG)

Panel speakers:
Mark Dearlove (Barclays Capital)
Ulf Bacher (Dresdner Bank)
Philip Harris (FXMarketSpace)
Godfried de Vidts (ICAP)

This session examined industry developments in the field of electronic trading. Johan Evenepoel moderated and introduced the session, recalling regulatory developments such as MiFID and Basle II which have supported the increased use of electronic trading as well as the drive within the industry towards greater STP as a means of operational risk reduction and cost reduction. The individual presentations were as follows:

Electronic Trading (Ulf Bacher, Dresdner Bank)

The presentation focussed on electronic trading in the repo market, commencing with a review of the original motivation for electronic trading and then moving on to assess progress to date. In this regard, the following aspects were covered:

- repo activity levels over recent years, highlighting the 95% growth in overall repo activity between June 2002 and December 2006 (ICMA Repo Survey);
- the range of electronic trading platforms in Europe and an overview of the key features of each; and
- future perspectives.

The Impacts of Electronic Trading (Mark Dearlove, Barclays Capital)

In assessing the impact of electronic trading, the presentation looked at:

- initial concerns over electronic trading in terms of potential job losses, margin compression and excessive transparency versus the reality of electronic trading which has successfully overcome the concerns and offered gains via support of increased volumes and new opportunities, "size-discovery", security and efficiency and the potential to reach out to all clients;
- the importance of having in place an appropriate level of STP to support the further processing of transactions executed electronically;
- the impact of electronic execution on trading volume in the US Treasury markets, where average daily trading volumes increased substantially between 1998 and 2005 despite only a modest increase in outstanding US Treasuries;
- electronic trading in the FX market and in interest rate swaps; and
- the state of electronic trading in money markets and its development as regards liquidity, client traction and efficiency improvements.

Electronic market making – efficient and robust operations (Godfried de Vidts, ICAP)

The presentation provided an overview of the ICAP electronic broking service, looking in particular at the markets covered and to be covered and STP as a driver for continued development. The presentation concluded with a reflection on the impact of electronic trading on liquidity.

Electronic trading (Philip Harris, FXMarketSpace)

The presentation commenced by looking at the evolution in the FX market towards a more open trading alternative and went on to illustrate how the FXMarketSpace product meets the emerging needs of customers. In this regard it was explained how the platform aims to bring together two pools of liquidity that would not normally meet on a daily basis (namely Reuters and CME). The presentation continued with an overview of trade flows – both in terms of direct trading and using a Prime Broker – and went on to examine progress to date and future product rollout.

During the wider discussion with the audience there was a reflection on the extent to which other electronic trading initiatives for repo may emerge, with the panel anticipating further scope for development given that not all collateral or customers are currently covered. The importance of STP and its role in ensuring success for electronic trading again came to the fore during the wider debate.

The revitalisation of the Japanese money market
Speaker: Tetsuya Inoue (Bank of Japan)

Tetsuya Inoue of the Bank of Japan provided an informative account of the revitalisation of Japan's money markets following the end of the quantitative easing policy (QEP). In this regard he elaborated on how the money markets functioned under QEP and then moved on to list the challenges facing the money markets at the conclusion of this period and the subsequent improvements in the functioning of money markets. The presentation concluded with an overview of the challenges facing the future of money markets and the Bank of Japan's efforts to support the smooth functioning of money markets.

In the question and answer session after the presentation, questions were raised on the persistent 5 – 6 basis point spread between general collateral and the overnight collateral market as well as on the existence of a triparty repo market. In response to the former question, the speaker explained that the persistent spread arose because of foreign banks shifting their funding requirements from the Bank of Japan to the repo market as well as due to the inelasticity of lenders in the market. On the issue of triparty repo, the speaker recalled that this is one of the future challenges to be addressed, with one of the existing problems being that the current Bank of Japan Net system is not totally consistent with triparty repo.

VI. Providing better client services
Panel discussion on the value chain in trade services from a client perspective
Moderator:
Joerg Isselmann (BHF, Member of the FXCG)

Panel speakers:
Tony Centofanti (Banque Pictet & Cie)
Kurt Schaefer (Daimler-Chrysler)
Martin Bagshaw (Detica)
Martin Wiedmann (Quaesta Capital)

The session opened with a presentation from Martin Bagshaw of Detica – a business and technology consultant firm which have worked with various players in the financial industry. The presentation provided an overview of how new services, changing players and shifting investment profiles are realigning the overall market and service model, with in essence, a real melting of the market place having taken place. In particular, hedge funds and asset managers are changing the way in which they were trading – constantly seeking alpha and increasingly pursuing institutional money. Although highly sophisticated on the trading side, these entities are considerably less knowledgeable on the operations side and their need for assistance in this respect, with single/minimised points of contact, underscores the growth of the prime brokerage business. In response to these developments, banks are changing their approach to client business, distinguishing in particular between platinum and other clients. With the increasing complexity of investment strategies however, products, investment decision drivers and information needs are also increasing in complexity. A strong need for real-time information exists and the requirements of hedge funds in terms of daily valuation reporting and collateral management can be too complex even for some prime brokers. Getting the overall operations component of the buy-side supported accurately is becoming more important for banks as clients become more cross product and real-time in their demands, and service providers strive to support and maintain their hedge fund clients.

Following the opening presentation, Joerg Isselmann as moderator posed a variety of questions to the panel members. In the first instance, he invited Kurt Schaefer, Tony Centofanti and Martin Wiedmann representing a corporate treasury, private bank and hedge fund respectively to define their requirements for a banking relationship. For the corporate treasurer and private bank, aspects such as pre-trade services and expert advice were rated highly while for the hedge fund community, the outsourcing of risk control was considered to be the main driver. The moderator then invited Martin Bagshaw to reflect on the view that hedge funds like to trade at low margins and expect that the further processing of operations be carried out by the banks essentially without charge. In response, Martin Bagshaw noted the need to distinguish between the products being traded and the aggression at which the services are required by individual clients. In this regard, asset managers were seen to be relatively close to hedge funds in terms of aggressiveness while corporate treasures were considered to be the least demanding.

On the subject of electronic trading, the moderator invited the panel to express their preferences for this means over direct calls. While there was a general preference to avoid being tied to one bank, on the private banking side, direct calls remained the preference. The panel members also commented on the strong competition among and even within banks to gain client business.

With regard to the idea that a certain disintermediation of banks by some hedge funds is taking place, the panel argued that it was rather the case that some hedge funds feel the banks cannot meet their service expectations and consequently, they are moving towards providing the service themselves.

Concerning error tolerance, the panel members referred to ongoing improvements in terms of staff training and enhanced risk and control systems, however scope remained to enhance trade confirmation practices across the market and to extend the use of SWIFT beyond the banking community.

In concluding this session, the moderator reflected on the different profile of customers and their respective levels of development. He also recalled the importance of operational efficiency for banks and customers alike, with error reduction and sound confirmation practices being key elements.

Conference conclusions

Francesco Papadia (ECB, Chair of the FXCG, MMCG)
Paul Dillon (AIB, Chair of the OMG)

Francesco Papadia as Chair of the FXCG and MMCG and Paul Dillon as Chair of the OMG, recalled the key points raised in the various sessions over the two days and the interesting exchanges among the diverse range of conference participants.