Euribor EBF

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Edito

Guido RAVOET

Contributing to a sound and robust European financial system

Since the beginning of the second crisis wave, in the wake of the sovereign debt crisis in a number of European countries, the overall European financial system has been put under serious stress. As a result, it is now facing a critical period which, it is hoped, will lead to reinforced integrated governance.

Euribor-EBF is constantly working on supporting the transparency and efficiency of short-term debt and interbank money markets in order to help the euro area economy be financed by funds other than those made available by the European Central Bank.
In contrast to the way the general public currently perceives banking institutions, the latter play clearly a key role in financing the real economy through their traditional activities. Furthermore, well-functioning interbank markets are at the source of banks' liquidity. Therefore, their output has an impact on individual European citizens.
Given the current environment, Euribor-EBF believes that the only way to offer EU regulators a clear vision of what can, or cannot be done when regulating the banking industry, is to gather as much expertise and evidence as possible on key issues and to share information with all stakeholders.

This is the reason why Euribor-EBF has been working more and more closely with other associations such as The Financial Markets Association (ACI) Europe, Euribor ACI, and the European Fund and Asset Management Association (EFAMA) over the last few months. This collaboration should in turn pave the way for improved cooperation with the EU authorities.

Furthermore, Euribor-EBF has been working in partnership with the European Central Bank on interbank and short-term debt markets for many years and is willing to share its knowledge with the other European Institutions, in particular, the European Commission and Parliament.

It is a way for bankers and money market specialists to contribute to a transparent, robust and sound European financial system.

Guido Ravoet, Chief Executive Euribor-EBF European Banking Federation

EUROPEAN BANKING FEDERATION EBF
EURIBOR

Philippe JEANNE

Building the After Crisis Environment

The Financial Markets Association (ACI) groups more than 13,000 finance professionals in 64 countries around the world. ACI Europe is very active within the ACI, with 33 countries working together alongside other financial, regulatory and supervisory associations to continue improving the standards of the Financial Markets.

The ACI focuses on training (staff certification), on Ethics, and on Dispute resolutions, and works with regulatory authorities, central banks, to give insight into the best ways to adapt to changes of environment. Needless to say that present times are challenging in this matter!

Cooperation with Euribor-EBF has been very close for a long time. Milestones have been reached with the creation of the Euribor fixing, the STEP label and an ongoing communication with the European Commission and the European Central Bank.

Our common ambition is to make sure that the ongoing developments in the industry are technically sound and viable in the long term, to maintain the competitivity of Europe with the rest of the world, and to emphasise that Financial institutions are key players in the economic field.

In times of crisis, it is all the more important to take the right decisions, especially when they drive the future. The number of members in the ACI and their vast expertise in all the segments of the industry, as well as the strong cooperation with Euribor-EBF and other associations, constitute a guarantee that regulators and politicians can obtain all the advice they need to be able to make the right decisions.

Let's hope that this opportunity will be fully exploited.

€URIBOR ACI
THE FINANCIAL MARKETS ASSOCIATION

Philippe JEANNE is European President of ACI-The Financial Markets Association, representing 34 countries in Europe.

He is Global Head of Forex Trading at Natixis, and has a strong expertise in Derivatives and Emerging Markets, developed at Calyon, ASLK-CGER and Barclays.

He has been based in London, in the US, and now in Paris.

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The Repo Market: there has to be some funding alternatives for European Banks

Cédric QUEMENER

Given the ongoing sovereign debt crisis, along with the growing regulatory need for banks to find pools of liquidity for funding purposes, the Repo market is currently playing a key role in Europe.

The Repo market is not only used by commercial banks, but also widely used by Central Banks to process their open markets operations within the aim of taking liquidity from the financial system.

It is more and more difficult for a bank to operate lending/borrowing transactions in a cautious market, with a strong appetite for collateralized (credit risk reduced) lending deals.
The concept of a Repo deal, seen from the borrower's side, consists in lending a security for a determined period (maturity) to another bank. At the end of the period, the borrower pays the cash plus the repo interest rate and receives its security back.

Most of the collaterals used in the repo market are government bonds, sometimes blue chips equities or corporate bonds.

Since the creation of the Euro, Euribor–EBF has been fulfilling its scientific mission towards the European Banking Industry by providing the market actors with an accurate, representative benchmark of the European Repo market, called Eurepo.

Nonetheless, as the market is constantly evolving, closely following the macro economic and political evolutions, financial actors are focusing more and more on an "as secure as possible" market, using the same kind of indicators.

This is the reason why the Euribor-EBF Secretariat and the Eurepo Steering Committee have worked on completing the service brought by the Eurepo benchmark, by creating an "overnight" European Repo benchmark. The concept is to give each day a sense of the market reality through a fixing made of the average calculation of the executed transactions on the most important repo markets across Europe, taking into account deals with as many types of collateral as possible.

As the Interbank Markets representative for European Banks, Euribor-EBF is the best positioned association to lead this kind of project, benefiting from the extensive expertise of its Steering Committee Members, the vast network of European banks, and the recognized governance principles of its structure.

Given that the regulatory environment is becoming stricter, and ever more demanding for banks in terms of funding whereas the economy needs banks to spread liquidity by lending to its actors, we believe that the repo market usage and its instruments should be eased by the European authorities.

Yet, as seen from the ongoing Financial Tax Transaction being discussed by a few EU Member States, this is decidedly not the current trend. On the contrary, the Repo market would technically be the victim of the new tax pressure on banks. What is more, European companies would be affected by the clear potential lack of liquidity available on the market; even States would be too.

In conclusion, we would strongly wish that the continued efforts made by European Banks to improve the market knowledge and therefore help the Repo market development would not be annulled by a lack of support from our leading European Institutions.

Cédric Quéméner, Director EURIBOR-EBF

DEVELOPMENTS IN THE STEP MARKET

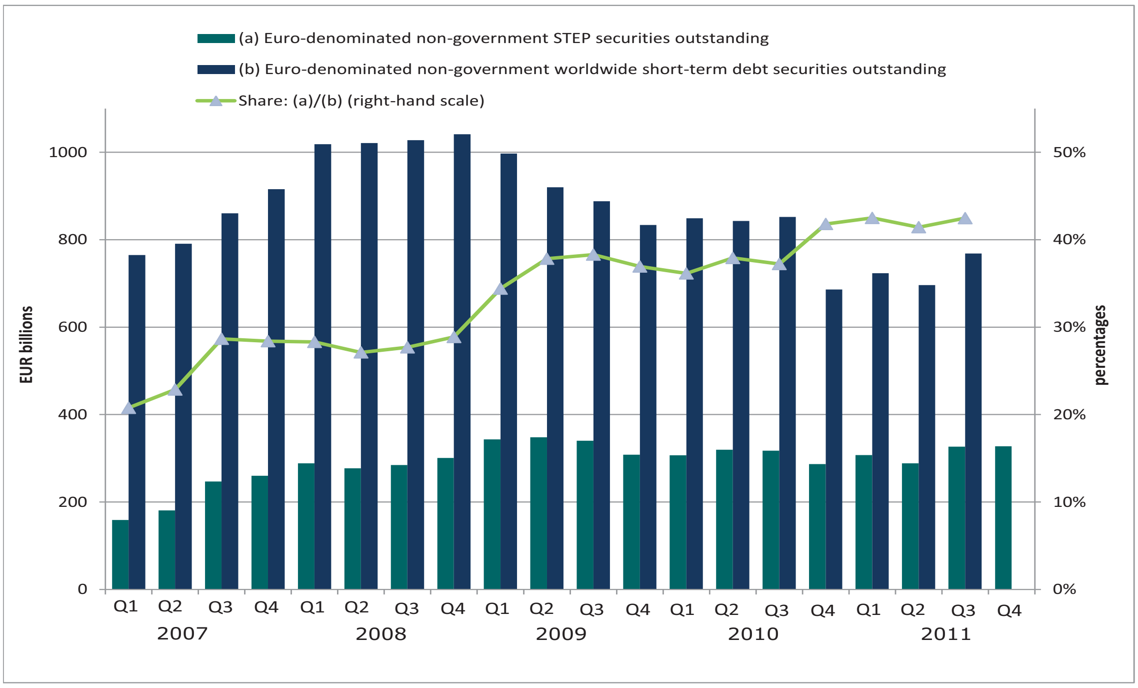
The European Central Bank (ECB) and the Eurosystem national central banks continue to support the Short-Term European Paper (STEP) initiative that was launched in June 2006 by acting as catalysts, thereby fostering the integration of the euro area's financial system. The regular publication of detailed statistics on the STEP market by the ECB contributes to the transparency in this market and allows the impact of related decisions taken by the ECB's Governing Council to be assessed.

In October 2008, the ECB's Governing Council decided to temporarily expand the list of assets eligible as collateral in Eurosystem credit operations to include STEP-labelled securities issued by credit institutions, i.e. certificates of deposit. This measure was discontinued at the end of 2010. The end of this exceptional measure could thus have had a negative impact on the development of STEP securities, especially those issued by monetary financial institutions (MFIs), as shown in the analysis conducted for the first months of 2011 in the previous article[1].

The detailed STEP statistics published by the ECB on a weekly basis[2] however show that the STEP market has proved its robustness following the discontinuation of the specific measure at the end of 2010.

The total outstanding amounts of STEP-labelled programmes fell for the first semester of 2011, but have since risen sharply, to reach €443.5 billion at the end of December 2011 stemming from 169 STEP-labelled programmes. This level almost corresponds to the highest level observed during the first three quarters of 2009. The relative positive development of STEP-labelled securities needs to be compared with an adequate benchmark for euro-denominated short-term debt securities (Chart 1) in order to assess the developments in the STEP market in 2011. Chart 1 highlights the decrease in the ratio of STEP securities denominated in euro and issued by non-government sectors to euro-denominated issuance of debt securities by worldwide non-government in the second quarter of 2011. However, the strong increase in the outstanding amounts of STEP programmes for the third quarter and even more for the fourth quarter can be seen as a further sign of the success of the initiative in supporting financial market integration.

Chart 1: Comparing outstanding amounts for STEP securities with a benchmark



In order to investigate further whether the discontinuation of the temporary measure of the ECB had a negative impact on STEP-labelled programmes issued by credit institutions, the developments of those securities relative to the overall issuance of STEP securities were assessed until the end of December 2011 for outstanding amounts (Chart 2) as well as for the number of programmes (Chart 3).

At the end of December 2011, 79% of the total outstanding amount of STEP securities was issued by MFIs and 15% by the general government sector. The MFIs' share has decreased since April 2011 almost back to the level in December 2010, while it was expected that the discontinuation of this exceptional measure at the end of 2010 might have a negative impact on securities issued by MFIs. The evolution of the share of the MFIs sector was mirrored by the evolution of the share of the general government sector. Indeed the share of the issuance by the general government sector increased from 5.8% in April 2011 to 15.1% in December 2011. The distribution among the sectors is thereby almost the same as that in December 2010, i.e. before the discontinuation of the ECB's temporary measure.

Chart 3 reinforces the fact that the sectoral distribution did not differ significantly from the figures at the end of 2010. Indeed 19 STEP labels were withdrawn by end December 2011 , of which 13 were MFIs but this was almost offset by new STEP labels granted during this period. Out of twelve new STEP labels, eight programmes refer to MFIs. The withdrawal of STEP programmes issued by MFIs does not seem to have had a negative impact on the volume of the STEP market, especially for the MFIs.

Chart 2. Outstanding amounts of STEP securities issuance by sector

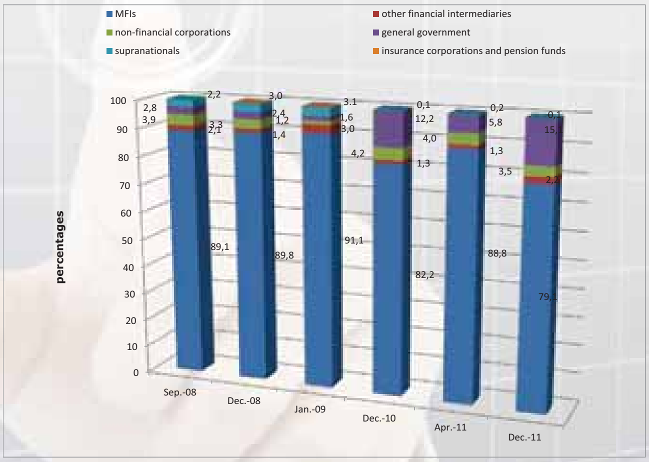
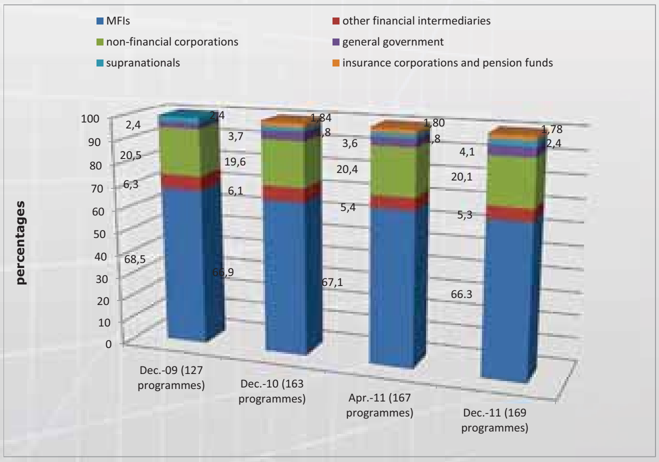


Chart 3. Number of STEP programmes by sector



The STEP statistics show that the development of the STEP market until the end of December 2011 supports the view that STEP securities have continued to develop robustly.

On 20 September 2011 the ECB's Governing Council approved a new version of "The implementation of monetary policy in the euro area – general documentation on Eurosystem monetary policy instruments and procedures"[3] and adopted Guideline ECB/2011/14 on monetary policy instruments and procedures of the Eurosystem. This means that STEP-labelled securities issued by credit institutions will be again eligible as collateral for the ECB's monetary policy operations as of 1 January 2012.

Giuseppina Borea - Sandrine Corvoisier, European Central Bank

[1]*For more details, please refer to Corvoisier, S. and Petit, V., "Further signs of the robustness of the STEP market", Euribor EBF Newsletter, June 2011.*
[2]*http://www.ecb.europa.eu/stats/money/step/html/index.en.html.*
[3]*For more details, please refer to the Sections 6.2.1.5 and 6.2.1.6 of the General Documentation http://www.ecb.int/ecb/legal/pdf/en_ecb_2011_14_f_sign.pdf.*

Money Market Funds:

2012 presents great uncertainties for money market funds (MMFs). Indeed, the Financial Stability Board (FSB) has asked IOSCO to undertake "a review of potential regulatory reforms of MMFs that would mitigate their susceptibility to runs and other systemic risks." IOSCO is to propose policy recommendations by July 2012, with particular emphasis on the following reforms: (i) encouraging or requiring shifts to variable net asset value arrangements and (ii) imposing capital and liquidity requirements on MMFs which continue to promise investors constant net asset value.

Regulators' concerns about MMFs are directly linked with the difficulties of the Reserve Primary Fund shareholders, following the failure of Lehman Brothers. This event led the U.S. authorities to take government-supported measures to alleviate the pressure on MMFs. They also adopted new rules to reduce risks associated with MMFs. The U.S. authorities characterized these measures as "a first step" and noted that additional possible reforms would be considered to make MMFs less vulnerable to "runs". Clearly, there is a risk that this process will lead to the adoption of new requirements that are neither necessary nor helpful to MMFs in Europe.

It is true that the financial instability arising from the Lehman Brothers' bankruptcy, and the meltdown of credit and money markets, created pressures for MMFs in Europe. Ultimately, however, the pressures faced by MMFs started to recede in November 2008, without any government guarantees. The financial crisis also caused strains among MMFs in Europe in 2007 after the outbreak of the subprime crisis. However, investors' concerns about the quality of MMFs reflected the fact that a small number of "cash-enhanced" funds had purchased asset-backed securities to boost their returns. These funds were in fact not classified as MMFs.

These strains led EFAMA and the Institutional Money Market Funds Association to develop a pan-European definition of MMFs to clarify what the "MMF" label should include. Their joint work persuaded the Committee of European Securities Regulators (CESR) to issue guidelines which created the first common regulatory definition of the European MMF. The guidelines include restrictions on exposure to interest rate and credit risks, and also require that MMFs draw investor attention to the difference between the money market fund and investment in a bank deposit. The implementation of the CESR definition will enhance investor awareness about the exact nature of MMFs as well as strengthen the quality of their assets, thereby enhancing their resilience in crises.

Against this background, the European MMF industry is highly concerned about the impact that additional regulatory measures could have on MMFs. MMFs are already highly regulated investment products, which invest only in very short-term, high quality, marketable debt instruments, and do not use any leverage.

The cost that new regulatory rules would impose on MMFs and their sponsors would cause significant shifts of assets into bank deposits and/or other less regulated vehicles. Imposing capital requirements would reduce or eliminate their attractiveness as a cash management vehicle. In addition, the new rules would hamper the role played by MMF in providing funding to corporate and government borrowers in the money markets. Consequently, banks would have to play an even greater role in the European economy, which would run counter to the view that a mix of market and bank financing increases the economy's resilience to crises.

We therefore hope that the policy options will be reviewed by IOSCO taking into account the potential impact of additional costs and burdens on the availability of funding to the European economy, and the lack of evidence that MMFs pose risks to the European financial system.

The European Fund and Asset Management Association (EFAMA) in figures

- 26 countries (EU Members, Lichtenstein, Norway, Switzerland and Turkey).
- 57 Corporate Members.
- 20 Associate Members.
- Total Assets under Management (in Europe) = around EUR 13 trillion, of which
- EUR 7,7 trillion through over 54.000 investment funds (end September 2011).
- Money Market Fund Assets = EUR 1,1 trillion (end September 2011).

Bernard Delbecque,
Director of Economics and Research

efama

European Fund and Asset Management Association

State of EU banking integration in times of crisis

Economic globalisation led by the business sector around the world is now being echoed by regulatory globalisation orchestrated by the G20. Despite the fact that the G20 proposals are not binding, the EU leaders follow in their footsteps and transform into legislation almost to the letter the outcome of G20 discussions. This gives rise to a new dawn of regulatory environment around the world, especially if all countries (G20 and beyond) follow suit.

It is in this context that the integration of the EU financial services markets has been taking shape till now. Over a decade up till 2008, a number of important structural barriers to integration had been removed . However, it took a serious crisis to address a number of big stumbling blocks such as pan-European banking supervision, and EU Crisis Management and Resolution Framework. One could argue that these fundamental elements should have been put in place much earlier, in order to help sustain the process of integration of financial services from the outset, and help facilitate stability of the industry and, consequently, the entire economy.

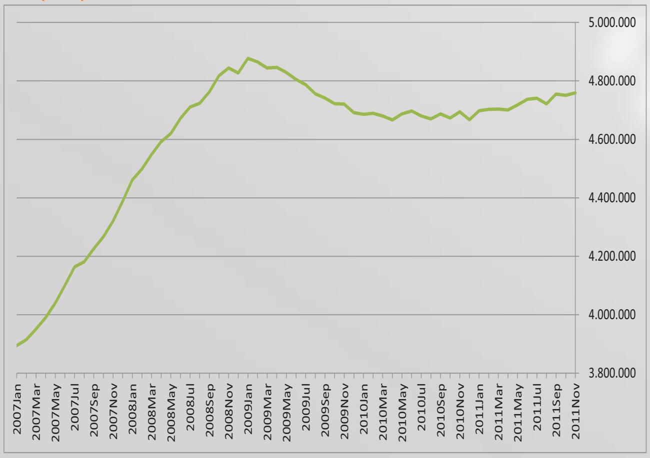
IMPACT OF THE CRISIS ON EUROPEAN BANKS' BUSINESS AND THEIR INTEGRATION

Over the past three years, Europe's banking sector has been affected by the financial, economic and sovereign debt crises in various ways.

- With the economic situation rapidly deteriorating, the ECB moved from the variable minimum rate of 4.25% in late 2008 to a fixed rate of 1% in May 2009.
- European inter-bank money market dried up early on in the crisis due to plummeted confidence and poor transparency of risks between the inter-bank lenders and borrowers.
- In Q3-2011, cross-border inter-bank loans and deposits are both down by around 9% compared with Q4-2008; also the nature of inter-bank lending had changed: shifting from unsecured lending to almost exclusively secured lending.
- In response, the ECB undertook a number of non-standard liquidity operations.
- A number of banks have had to rely on the ECB's main refinancing operations for access to liquidity at low cost (only in 2011, the amount of the ECB's main refinancing operations has more than doubled.)
- Encouragingly, cross-border MFI lending to non-MFIs is growing.
- Still, bank lending to households in the euro area plunged in 2009, recovering somewhat thereafter (in November 2011 it stood at € 5.1 trillion).

Figure 1: Total euro area MFI lending to households, € million (ECB)

Figure 2: Total Euro area MFI lending to non-financial corporations, € million (ECB)



- Lending to the corporate sector was badly hit in 2009 and is still below the peak level (in November 2011 it stood at € 4.8 trillion).
  Bank lending to the euro area governments has jumped during the crisis: in November 2011, euro area bank lending to governments stood at € 1.1 trillion, up by 16% from October 2008.

Figure 3: Total euro area MFI lending to governments, € million (ECB)

It has been reported by the European Commission DG ECFIN, and by the European Central Bank that during the crisis, cross-border banking activity weakened. The EBF is concerned with the lack of political ability to solve the ongoing sovereign debt crisis in a number of EU countries, which weighs heavily on the EU banks' ability to continue serving the economy. Furthermore, given the general economic sentiment and the heavy financial regulatory burden, large European banks' considerations to pull their subsidiaries out of Eastern Europe may put in jeopardy financial integration in Europe even further.

CALL FOR A BALANCE BETWEEN SYSTEMIC STABILITY AND BUSINESS EFFICIENCY

It should be recalled that prior to the crisis, the main focus of Europe's financial institutions was on efficiency gains, attainable, and indeed attained, to a larger degree at the EU rather than at national level. Today, the regulatory discussion focuses much more on financial sector stability, a very welcome approach, but which is, to a certain degree, in contradiction with the earlier goal of efficiency. Specifically, current regulatory framework implies that cross-border banking groups must ensure capital and liquidity standards in each branch or subsidiary, limiting the intra-group flows, thus making an impact on the choice of banks' business model. This impact does not necessarily favour deeper financial integration; neither does it help to improve banks' group-level efficiency, it does however facilitate greater financial stability of each of the banking group's entities.

Financial integration can only take place in an environment of financial stability and economic growth. The EBF realises that progress in retail integration will only be gradual, and it is prepared to continue its long-standing cooperation with the European Commission on elimination of artificial barriers to integration in retail as well as wholesale markets.

Over the past two years, the EU leaders have been tackling a range of highly challenging tasks. Not only have they faced the damage caused by the global economic and financial crisis, they have also been putting in place the missing elements of the underlying EU architecture in order to ensure that crisis management mechanisms, both in finance and at the sovereign level, can be resolved in the future.

It is hoped that strengthened economic governance will bring confidence back to the financial markets and economic growth back on track. This would greatly help the financial industry meet its new regulatory requirements as well as adjust to the new norm, which should contribute to financial integration, for the good of banks and citizens alike. Normalisation of the economic and financial situation will, eventually, create the right circumstances for banks to find a new and better level of efficiency in the new regulatory environment.

Viktorija Proskurovska, Adviser

European Banking Federation

Overview of the proposed FTT Directive

The Commission presented last September a proposed Directive to introduce a common system of financial transactions tax (FTT).

In the context of the current crisis, many EU Member States believe that additional taxation of the financial sector may generate immediate public revenue at the expense of financial institutions and, at the same time, help restore financial stability and economic growth. In addition, it is also aimed at ensuring that the financial sector makes a fair contribution to public finance. The underlying hypothesis is that the sector is currently under-taxed vis-à-vis other sectors. This assumption is based, at least partially, on a biased perception of advantages that are considered inherent in the VAT exemption of financial services.

The Commission believes that the proposed FTT Directive would be able to strengthen the EU Single Market by setting up a harmonized framework to FTT. In their view, it would help reduce competitive distortions, deter financial institutions from excessive risk-taking activities, complement regulatory measures aimed at preventing future crises and promote common rules for the introduction of a FTT at global level. To a certain extent, these objectives, however, appear to be conflicting. Indeed, there seems to be a paradox between the requirement for banks to rebuild and strengthen their capital base, lend more and pay more taxes at the same time.

According to the residence principle which determines the territorial scope of the proposed legislation, the key connecting factor for the collection of the tax would be the involvement in a financial transaction of a financial institution established in an EU Member State. A financial institution will be deemed to be established in the territory of a Member State if it is authorised in that Member State, has its registered office in the Member State, is resident in the Member State or is acting through a branch located in the Member State. The FTT will apply to a financial institution irrespective of whether it is acting in a principal or agency capacity. Hence, where a financial institution established in a Member State is a party to a financial transaction, it will be subject to the FTT irrespective of the location of the counterparty or the location of trading.

Focusing on financial institutions, the proposed FTT legislation broadly defines those institutions by including investment firms, organised markets, credit institutions, insurance and re-insurance institutions, collective investment schemes and their managers, pension funds and their managers, holding companies, leasing companies and special purpose vehicles. The draft Directive provides for a number of carve-outs, ring-fencing SMEs and private households, primary markets, issuing of government bonds, as well as monetary policy and post-trading activities.

Technically, the tax chargeable event is defined as the execution of a financial transaction involving an EU financial institution. The latter will be liable for the payment of the FTT to the local tax authorities. Each Member State will be required to adopt domestic measures to ensure that the FTT is paid immediately if the transaction is carried out electronically and within three working days in all other cases. There is in addition a joint liability of each party to the transaction, resulting in significant practical issues and costs associated with enforcing collection and compliance, as well as legal uncertainty for presumed collectors of the tax.

The wide scope of the FTT legislation will include transactions in all kinds of financial instruments, i.e. equities, bonds, foreign currency (excluding spot contracts) and derivatives. The scope will cover all kinds of transactions, whether conducted on regulated markets or on an OTC basis, including purchase and sale, repos (sale and repurchase) and securities lending transactions. The FTT will apply both to transactions between third parties and intra-group transactions. This broad based approach is the most difficult aspect of the legislation. Indeed, as acknowledged by the Commission in its impact assessment, this will have a huge impact on the volumes of transactions. Therefore, by including repos, the FTT will seriously impact the liquidity of markets. By including derivatives, it will impact the major risk management tool used by banks. In a nutshell, the FTT is likely to create a "structural break" of financial markets.

In the case of financial transactions other than derivatives, the taxable amount will be the consideration payable between the parties for the transfer of the financial instruments under the transaction. However, if this is lower than the market price, than the tax base will consist in the market price. The taxable amount in relation to derivative transactions will be the notional principal amount specified in the contract at the time the derivative is entered into.

The tax rate of the FTT will be fixed by each Member State subject to a minimum rate of 0.1% for financial transactions other than derivatives and 0.01% for derivatives.

The implementation of the FTT legislation, the adoption of which requires unanimity at Council level, is tabled for the 1st of January 2014. When fixing this date, the Commission has ignored the necessary lead-time for financial institutions to adapt their systems and procedures, a process which can only start when they know the details of the legislation. But this is not the only flaw in this initiative. The worse is that policy-makers seem to ignore that the financial sector operates on a global basis with capital able to move freely and easily and trading carried out electronically and in many jurisdictions. Consequently a real risk of the imposition of an EU wide FTT is that the tax base would be immediately eroded through the migration of transactions outside the scope of the legislation.

Roger Kaiser, Senior Adviser

European Banking Federation

Maintenance periods is an old issue no longer discussed yet its import should be understood in order to determine the demand and supply of money, interest rate direction and purpose employed through market mechanisms such as Eonia and Euribor in Europe and Fed Funds in the United States. Maintenance periods for central banks define monetary policy by pricing a nation's demand and supply of reserves to an interest rate. Yet each central bank that employs a maintenance period deploys those periods in different ways.

A maintenance period for the Eurozone is the time between governing council meetings, an ECB policy rate meeting in market parlance with a purpose to price excess reserves placed by banks on account at the European Central Bank. Reserves are averaged monthly over the maintenance period term. The ECB then provides liquidity to the banking system by bankers who bid for Euros through weekly and three month auctions at the Main Refinance Rate, also termed the Minimum Bid Rate. The Refi rate is the most important interest rate in Europe because it influences prices in market interest rates such as Eonia and Euribor to satisfy ECB policy to bring price stability to the European system. More importantly, the Refi rate is also termed the base rate because it establishes at what interest rate reserves are expected to grow or contract and appears in M3 money supply forecasts. Reserves are also termed the money supply and interest rates are termed reserve rates.

Excess reserves are paid an interest rate to manage liquidity. For the European system, the overnight rate termed Euribor or the Euro Interbank Offered Rate is paid on excesses for the short term. Reserve deficits are charged an interest rate termed Eonia, Euro Overnight Index Average and a weighted average of Euribor. Eonia is the rate bankers charge each other for overnight loans and represents the floor of interest rates. Eonia is an effective rate to Euribor and the Refi rate.

Excess reserves once priced are loaned throughout the banking system by borrowing at the Eonia rate and lending at Euribor. Euribor establishes loan rates and are indexed since 2008. This represents what is known as the interest rate corridor or channel for the European system that establishes a floor and ceiling of daily interest rates. The purpose of the 1999 introduction of short rates is to price reserves on a daily basis and gives indication of the demand and supply of Euros to meet the three month, money supply refi target rate. Above the target means inflation and an erosion prices, below means deflation. Both are a cost to reserves.

Euribor and Eonia are tradeable market rates that trade as futures contracts on Euronext. Euribor/Eonia Swap Index futures is one such contract. Since 2008, the one month Eonia contract and the three month Eonia swap index aligned in terms of trade and settlement to central bank maintenance periods. The Eonia three month contract trades normal International Money Market dates while the one month contract is aligned to European maintenance periods.

Figures 6.8 and 6.9 are charts of the interest rate corridor for the ECB, US, Japan and the BOE. Each nation has various means to achieve the desired three month money supply target. For the short term, the Japanese employ Call rates, the BOE remunerates and indexes reserves at the Bank rate with Sonia rates as the daily operational guide and the US employs the Fed Funds rate. The Japanese, ECB and the US employs maintenance periods while Australia, Canada and New Zealand do not. Most important for the Japanese, ECB and the US maintenance period time is short rates establishes the start of the day's yield curve. The interest rate releases answers the question long or short a currency pair and/or which pair to swap in interest rate terms.

Europe vs the United States

Brian Twomey

The Federal Reserve Board established in 2008 what it calls maintenance periods. These are weekly periods during which banks must maintain required reserves. Maintenance periods cover 14 consecutive days. Required reserves began as Reg D that appeared first in the Federal Reserve Act of 1978 then carried forward to the 1980 Monetary Control Act that imposed mandatory reserve requirements. All governments then imposed reserve laws and this gave rise to the need for the British Bankers Association as reserves had to be priced and balanced in line with central bank target rates.

To pay interest on reserves was scheduled for 2011 with passage of the Financial Services Regulatory Relief Act of 2006 but moved forward by Congress to 2008 with passage of the Emergency Economic Stabilization Act of 2008 (Federal Reserve 2010).

In conclusion, maintenance period is an important time between the US and Europe because lend and borrow rates, bids and offers, yield curves and direction of financial market instruments are established for a particular day's trade not only in the US and Europe but between the US and Europe in terms of a Euro/USD exchange rate. The most important aspect of maintenance periods is the determination in the demand and supply of Euros vs US Dollars. It is an indicator and a valued market tool that should be a regular focus for those involved in the markets.

Fig. 6.8

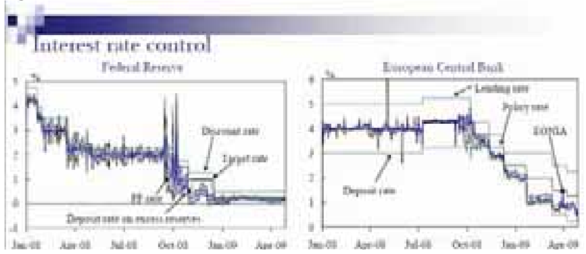
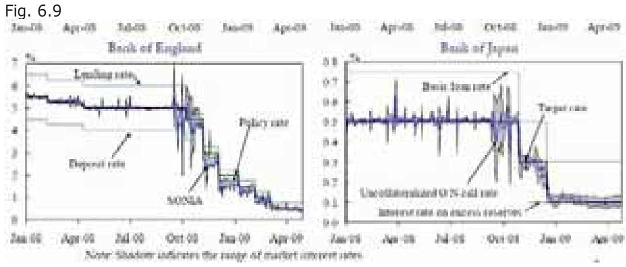


Fig. 6.9



Brian Twomey is an independent trader and a prolific writer on trading, having authored over sixty articles in Technical Analysis of Stocks & Commodities and Investopedia. His article on Welles Wilder is one of the most heavily accessed pieces in Technical Analysis of Stocks & Commodities in recent years. Through his writings, Twomey has established a strong following among traders and market analysts. He is an Adjunct Professor of Politics at Gardner-Webb University. Twomey has a BA in journalism and a master's in political science and public administration from the University of Central Florida.

Inside the Currency Market

Brian Twomey

Inside the Currency Market: Mechanics, Valuations and Strategies, published by John Wiley and Sons and Bloomberg Press is a book that literally covers all facets that comprise a currency pair equation from market to market of the eight major nations as well as factors to consider to properly trade any currency pair in any market.

It is a deeply detailed and comprehensive study into every nation's financial market that offers a full load of information that hasn't been seen nor properly explained together in one volume. Much of the information is original. The Japanese Yen for example transforms itself from Asia to Europe to the US to Canada and attaches itself to various instruments in order to move in the markets. The Yen is tracked through the various markets almost by an hourly basis with explanations and operational guidance in order to employ a trade strategy.

All currency pairs are addressed market to market in terms of trade weight indices, methodologies, formulas and calculations, index methodology and histories, weights and constituents in every index. How to view currency pairs in each market is considered as well as major imports and export markets, major products and important destinations. All accompany charts and graphs

British Bankers Association Libor as well as each nations interest rates are fully explained, fully outlined, fully addressed in terms of movement, direction, purpose, histories, times of trade, seasonality, overnight rates and always accompanied by currency pair charts and graphs as well as each nation's interest rate charts for comparision.

Yield curves in terms of histories, each nation's curve, bonds vs yields in each market, yield spread formulas and calculations between two nations as well as single nation bond maturities are explained and factored to a currency pair. Each nation's bonds are listed and calculated at every maturity. Carry trades and yield spreads are explained and accompanied by examples and charts.

Interest Rate Swaps, Cross Currency Basis Swaps, Foreign Exchange Swaps and outright forwards in each nation is explained, trade strategies offered and explained as well as methodologies and histories. OIS swaps are also explained. A deep discussion of forward points is offered as well as two examples to calculate a forward point to a yield curve.

Each nation's stock market, calculations of each index, types of index to know for economic and market purposes, currency pairs in terms of stock, bond and yields are offered as trade strategies and methodologies nation to nation.

This is only a small portion of the many varied categories found within these pages. It is a book with a focus on the understanding of currency pairs yet it is a book for all traders in all markets, in all traded instruments. Fair value for example is calculated as an example to factor the S&P's. Fair value is defined as futures priced to cash yet theoretical value is also calculated as an example. Theoretical value is defined as a long or short in one index or a long or short in a stock that comprises the index.

A reader will have a full understanding of not only the international system but a firm comprehension of each nation's market in order to trade and understand the purpose, functions and trade of currency pairs.

STEP

STEP programmes issued by monetary financial institutions are again ECB eligible from January 2012

Since January, STEP programmes issued by monetary financial institutions have become eligible assets for collateral in European credit operations. This was already the case for STEP programmes issued by non-financial corporations. Concretely, credit institutions, benefitting from the STEP label, will not have the obligation to list their programme in order to be ECB eligible. As such, they reduce their outlay significantly given the lower costs of the STEP label (€5000 entry fee and €2000 annual maintenance fee). Euribor-EBF welcomes the ECB's decision and believes that STEP should not only be a label of transparency and harmonisation but become a standard in the Short-Term European Paper market.

STEP statistics to be improved the coming months

The ECB statistical Team and the STEP Statistics' Task Force are currently working on the development of STEP statistics, both on the content and the format, in order to offer the buy and the sell side, increased information on the STEP market. STEP statistics are calculated and published by the ECB website. (http://www.ecb.int/stats/money/step/html/index.en.html) and also displayed on the STEP

Fixings

Euribor-EBF pursues its work to offer a better view of the interbank market in Europe

Over the last years, the European banks have been expressing the need to create a Euribor-like benchmark for dollar-funding purposes. As a response to the market demand, Euribor-EBF has been developing a USD Euribor, which has been tested over the last six months. The launch of the new benchmark is planned for 2012.

The Eurepo Steering Committee and Euribor-EBF have been working on the creation of an overnight repo benchmark, reflecting the effective transactions on the repo market (see p.5).

Changes in the composition of the Euribor panel

Since its creation in 1998, the Euribor panel has continuously adapted to the European banking industry evolution.

Following a common decision of WestLB and the Euribor Steering Committee, WestLB is no longer contributing to the Euribor and Eonia fixings since 1 January 2012. The Euribor-EBF team would like to thank West LB for the rewarding years of collaboration.

The Euribor-EBF Team and the Steering Committee welcome the inclusion of UBI Banca on to the Euribor/Eonia panel since February 2012.

The Euribor-EBF editorial Team would like to thank most warmly the ACI Europe President, Mr Philippe Jeanne, the ECB Statistics Team, the EFAMA Director of Economics and Research and the EBF advisers; as well as Mr Brian Twomey (as an independent writer), for collaborating on this publication. A special thank to Ms Florence Ranson, EBF Head of Communications.

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