Box 14

T2S – EUROPE'S INTEGRATED SECURITIES SETTLEMENT PLATFORM, AND ITS CONTRIBUTION TO FINANCIAL STABILITY

On 17 July 2008, the Governing Council decided, after two years of intense cooperation with users and providers of settlement services, to build a new settlement platform, TARGET2-Securities (T2S). The Deutsche Bundesbank, the Banco de España, the Banque de France and the Banca d'Italia will build and operate T2S; an ECB team will continue to manage the overall programme, and its relationship with all stakeholders inside and outside the Eurosystem. T2S is expected to become operational in 2013.

T2S is a single, sharable, multi-currency platform for the settlement of securities transactions in central bank money. Participation in T2S will be voluntary and its services will be provided on a full cost recovery basis to participating Central Securities Depositories (CSDs), which will adjust their business models accordingly, in particular by reducing or eliminating investment in their own settlement engines.

The figure below illustrates the key features: CSDs will keep securities accounts for market users just as they do today, with the balances retained in T2S for settlement purposes, while central banks will provide and maintain central bank money balances in T2S, via an interface to TARGET2 (or another RTGS system in the case of non-euro currencies). Settlement (and cross-CSD matching) will be handled by T2S, and will be subject to the existing legal regimes of the relevant CSDs.

On top of the financial gains from a sharp reduction in the number of settlement platforms, market users will benefit from significant process harmonisation in that there will be no difference between domestic and cross-border settlement in Europe.

Moreover, T2S has the potential to act as a catalyst for the wider harmonisation of post-trading processes, with the Eurosystem adding its weight to the existing initiatives in such areas as legal change and corporate actions.

All euro area CSDs have committed to participate in T2S, and there is strong interest from markets in several other countries. There are clear signs that CSDs are taking active steps to prepare for a future in which they can continue to offer their current range of services, business and legal relationships with customers (all using the same single settlement platform), but will face the threat of competition and have the opportunity to enlarge the range of assets they offer and service.

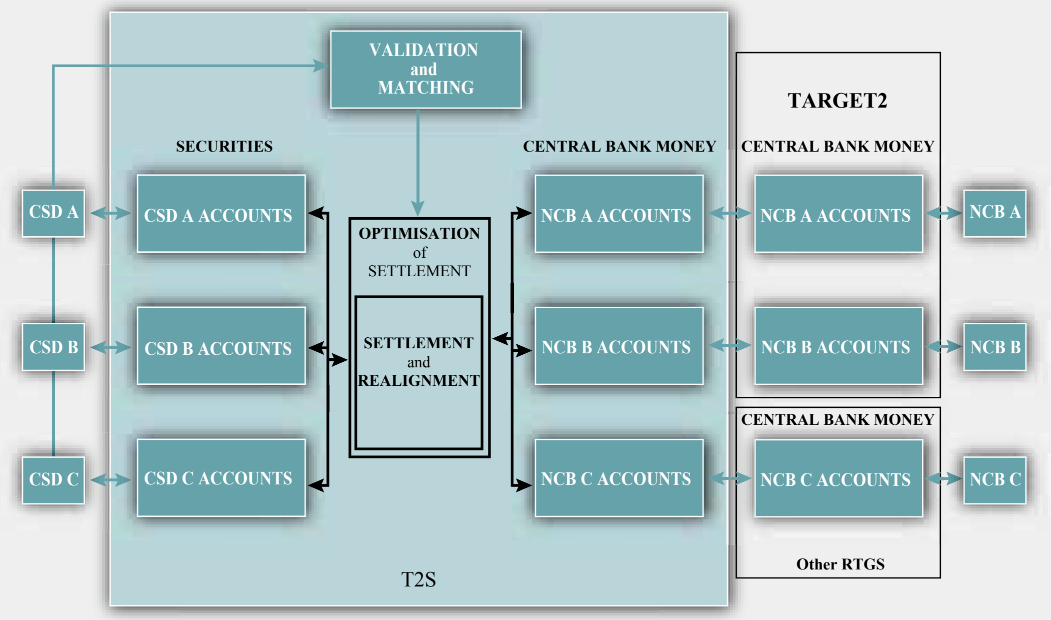
The Eurosystem has a strong interest in the smooth functioning of settlement infrastructures in terms of preserving financial stability; a disruption in a settlement system, particularly at a time of financial stress, may constitute a source of contagion risk by inhibiting the timely exchange of collateral and payments. Europe has multiple, often interdependent, trading and post-trading systems. Consequently, the operational risks of each system are directly linked to those of other systems within the value chain; a failure in any one system may result in disruption passing swiftly across systems and their participants, with second-round effects on other market activities.

The cooperation between the Eurosystem and the European CSDs to deliver and run T2S will bring a robust, efficient and resilient securities settlement infrastructure, efficiently coupled to TARGET2 and to other RTGS systems. T2S will provide a single platform, replacing the different settlement platforms of those CSDs that join T2S, and it will significantly simplify today's settlement interactions across markets. An important dimension of crisis management will thus become simpler, more transparent and more secure for market users and public authorities alike.

The work on wider harmonisation will contribute to this improvement, by simplifying the necessary processing. The greater the harmonisation, the better the prospects for a more timely identification of risks – and the corrective measures required – to safeguard the stability of financial markets.

Of course, T2S will create a concentration risk in securities settlement, which has to be mitigated. T2S will have state-of-the-art business continuity and contingency models, exploiting the architecture and infrastructure already in place for TARGET2, so that the Eurosystem can continue to operate even after a variety of unpredictable events ranging from local equipment failures to a regional disaster.

Cooperation between the Eurosystem and CSDs in using one technical platform for all securities and cash accounts to settle securities transactions



Source: ECB.
Note: Exchanging the securities (in the CSD securities accounts in T2S) for the cash payment (in the NCBs' cash accounts in T2S) are linked in T2S, for delivery versus payment in a synchronised and safe environment in central bank money. In addition to all euro area CSDs, Danmarks Nationalbank and VP (the Danish CSD) intend to use T2S to offer settlements in euro and Danish krone. Other European currencies and CSDs are expected to do likewise.

T2S will follow the concept of two regions, two sites, as is already in place for TARGET2. If the "live and operating" T2S system fails, the other T2S system in the same region will immediately take over without impacting smooth operations.

Two additional sites will be available in a second region within the euro area, and T2S will be able to resume operations at these sites as required.

Furthermore, T2S will adopt prudent risk management principles, which will include performing stress-testing exercises to ensure the resilience of the links between T2S, the CSDs and major market participants.

There is a further systemic advantage of T2S. T2S will facilitate the possibility of market participants across Europe pooling all of their securities into one system for settlement purposes – just as cash is now pooled in TARGET2 – no matter which CSD they choose; there will be no need to manage the allocation of securities and central bank money across many national platforms. This increase in the settlement efficiency of collateral management (and the reduction of collateral and liquidity needs) will make it easier to quickly mobilise securities for other purposes. This has ongoing economic value – but is of systemic benefit in a financial crisis, when credit institutions need to mobilise liquidity against collateral.

The single securities settlement environment using central bank money will be delivered by 2013, and will contribute to the safety and efficiency of the single market for capital.