

Changes of risk control measures in Eurosystem credit operations

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Outline

- 1. Recall: changes announced on 4 September 2008 to become effective on 1 February 2009**
- 2. New changes: announced on 20 January 2009, and to become effective on 1 March 2009 / 1 March 2010:**
 - ABS AAA rating thresholds at issuance**
 - No double layer securitizations**
 - Limit for bank bond use by one issuer (and closely linked issuers)**

I. Change in haircuts for marketable assets as of 1 Feb 09

Old haircut schedule:

| Levels of valuation haircuts applied to eligible marketable assets in relation to fixed and zero coupon instruments (%-ages) | | | | | | | | |
|--|----------------------------|-------------|---|-------------|---|-------------|----------------------|-------------|
| Liquidity categories | | | | | | | | |
| | Category I (govt bonds) | | Category II (local and reg. govt, agencies, supras, Jumbo cov. Bonds) | | Category III (trad. Cov. bonds, unsec. bank bonds, corporate bonds) | | Category IV (ABS) | |
| Res. mat. (years) | Fixed coupon | Zero coupon | Fixed coupon | Zero coupon | Fixed coupon | Zero coupon | Fixed coupon | Zero coupon |
| 0-1 | 0.5 | 0.5 | 1 | 1 | 1.5 | 1.5 | 2 | 2 |
| 1-3 | 1.5 | 1.5 | 2.5 | 2.5 | 3 | 3 | 3.5 | 3.5 |
| 3-5 | 2.5 | 3 | 3.5 | 4 | 4.5 | 5 | 5.5 | 6 |
| 5-7 | 3 | 3.5 | 4.5 | 5 | 5.5 | 6 | 6.5 | 7 |
| 7-10 | 4 | 4.5 | 5.5 | 6.5 | 6.5 | 8 | 8 | 10 |
| >10 | 5.5 | 8.5 | 7.5 | 12 | 9 | 15 | 12 | 18 |

New haircut schedule:

| Levels of valuation haircuts applied to eligible marketable assets in relation to fixed and zero coupon instruments (%-ages) | | | | | | | | | |
|--|----------------------------|-------------|---|-------------|---|-------------|------------------------------------|-------------|---------------------|
| Liquidity categories | | | | | | | | | |
| | Category I (govt bonds) | | Category II (local and reg. govt, agencies, supras, Jumbo cov. Bonds) | | Category III (trad. Cov. bonds, corporate bonds) | | Category IV (unsec. bank bonds) | | Category V (ABS) |
| Res. mat. (years) | Fixed coupon | Zero coupon | Fixed coupon | Zero coupon | Fixed coupon | Zero coupon | Fixed coupon | Zero coupon | all coupons |
| 0-1 | 0.5 | 0.5 | 1 | 1 | 1.5 | 1.5 | 6.5 | 6.5 | 12* |
| 1-3 | 1.5 | 1.5 | 2.5 | 2.5 | 3 | 3 | 8 | 8 | |
| 3-5 | 2.5 | 3 | 3.5 | 4 | 4.5 | 5 | 9.5 | 10 | |
| 5-7 | 3 | 3.5 | 4.5 | 5 | 5.5 | 6 | 10.5 | 11 | |
| 7-10 | 4 | 4.5 | 5.5 | 6.5 | 6.5 | 8 | 11.5 | 13 | |
| >10 | 5.5 | 8.5 | 7.5 | 12 | 9 | 15 | 14 | 20 | |

*Assets in this liquidity category that are given a theoretical value will be subject to an additional valuation markdown of 5%.

I. Extension of the definition of “close links” for ABS + rating transparency requirement as of 1 Feb 09

- **In case of ABS, prohibition of:**
 - **Providing liquidity support of more than 20% of the asset-backed security’s nominal value.**
 - **Entering into a currency hedge with the ABS issuer.**
- **All ECAI (rating agency) assessments must be based on public ratings. In particular for ABS:**
 - **credit ratings reports (pre-sale or new issue report) must be published that include:**
 - **comprehensive analysis of structural and legal aspects**
 - **detailed collateral pool assessment**
 - **rating reviews to be published at least quarterly**
 - **In principle as of 1 February, but one quarter “grace period”**

I. Eurosystem discretion as of 1 Feb 09

- **Made more explicit that the Eurosystem has discretion in excluding or limiting the use of certain assets, also at the level of individual counterparties, to ensure adequate risk protection.**
 - **In line with Article 18.1 of the ESCB Statute.**
 - **Common market practise, also enshrined in the Basle II rules, to regard as adequate collateral only collateral that is not (or is only limitedly) correlated with the counterparty that provides the collateral.**

2. Measures announced on 20 January 2009

ABS:

- **Eurosystem will require a rating at the AAA/Aaa level from an accepted external credit assessment institution (ECAI) at issuance as an additional eligibility criterion for all ABSs issued as of 1 March 2009. Over the lifetime of the ABS, A minimum rating threshold would have to be retained.**
- **For ABSs issued as of 1 March 2009, the underlying pool should not consist, in whole or in part, of tranches of other ABSs. ABSs issued before 1 March 2009 will be exempted from the latter requirement until 1 March 2010.**

2. Measures announced on 20 January 2009

- **Uncovered bank bonds:**
 - **As of 1 March 2009, the value assigned to uncovered bank bonds issued by an issuer, or any entity with which this issuer has close links as defined in Chapter 6.2.3 of the General Documentation, must be less – after the application of haircuts – than a share of 10% in the value of the collateral pool of a counterparty (unless the market value of the assets referred to above does not exceed EUR 50 million).**
 - **The limitation does not apply to uncovered bank bonds that are government guaranteed.**

2. Measures announced on 20 January 2009

- Uncovered bank bonds – **grandfathering rule**:
 - “Uncovered bank bonds submitted as collateral to the Eurosystem until 20 January 2009 are subject to this limitation as from 1 March 2010.”
 - If a counterparty was in breach of the limit on 20 January 2009, it may continue to use the bank bonds of this issuer (and closely linked issuers) on this day until 1 March 2010. It can neither increase the total absolute value of bank bonds from this issuer (and closely linked issuers), nor can it increase the percentage share of the bank bonds from this issuer (and closely linked issuers) in its total collateral pool beyond the share as of 20 January 2009. The latter implies that a bank may have to remove such bank bonds in case its total collateral portfolio shrinks.
 - In case of a merger between two or more issuers of uncovered bank bonds or the establishment of a close link between such issuers, these issuers are treated as one issuer group, in the context of this limitation, only one year after the date of the merger or the establishment of a close link.

2. Change of close links definition as of 1 February 2009

- “Close links between two issuers” means a situation in which one of the issuers owns directly, or indirectly through one or more other undertakings, 20% or more of the capital of the other issuer (analogy to close link definition of page 39 of the GD).
- (Previously: CLOSE LINK if A owns 20% or more of the capital of B, or one or more undertakings in which A owns the majority of the capital own 20% or more of the capital of B, or A and one or more undertakings in which A owns the majority of the capital together own 20% or more of the capital of B.)
- In total three changes relating to close links: (i) close links between issuers was introduced as a new relevant case; (ii) the definition was generally simplified (direct or indirect 20% ownership); (iii) Certain close links between ABS and counterparties were prohibited.