

19 March 2013

**UniCredit Group's reply  
to the EBA Consultation on Defining Liquid Assets in the LCR under the draft  
CRR**

UniCredit is a major international financial institution with strong roots in 22 European countries, active in approximately 50 markets, with about 9.500 branches and more than 155.000 employees. UniCredit is among the top market players in Italy, Austria, Poland and Germany. In the CEE region, UniCredit operates the largest international banking network with around 4.000 branches and outlets, and is a market leader.

## General considerations

### UniCredit proposal to EBA

UniCredit has analysed the detailed suggestions of the proposed methodology by the European Banking Authority (EBA), acknowledging the importance and the difficulty of this exercise. Based on the consideration that the specific methodological aspects for combining different liquidity metrics and for providing a relative ranking are not disclosed in the discussion paper, UniCredit believes that the EBA and the national supervisory authorities could substantially benefit from using what is already in place and well tested in terms of the liquidity categories for marketable assets in the context of the Eurosystem credit operations<sup>1</sup>.

### Arguments in favor

By relying on what is already in place and well tested in terms of the liquidity categories for marketable assets in the context of the Eurosystem credit operations, the EBA would achieve the following objectives:

-> to promote a smooth financial market functioning, under normal and stressed conditions, by **reducing as much as possible the uncertainty** on the EBA liquidity definition work, both in terms of its length and the final outcome. This would contribute **to minimize any unintended negative consequence** on market functioning, since any unjustified divergence from the standards of the Eurosystem credit operations is going to have a remarkable impact inter alia:

- on the repo market, and in particular on the asset categories eligible for certain baskets and on the related haircuts;
- on any collateral management, margined business and central counterparties (CCP) activities, both in terms of eligibility criteria and risk control framework;

<sup>1</sup> [http://www.ecb.int/ecb/legal/pdf/L\\_33120111214en000100951.pdf](http://www.ecb.int/ecb/legal/pdf/L_33120111214en000100951.pdf) table 6

- on the activities related to the management of the securities included in the Liquidity Coverage Ratio (LCR) definition.
- > To efficiently and effectively **leverage on the several years of experience and testing by the Eurosystem**, and especially the ECB risk management. As proven by the EBA consultation paper, the liquidity measurement is a sensitive and difficult subject, which in our view should neither be subject to banking supervisory discretion nor diversified by country, at least in the EU. The EBA approach risks going in this direction.
- > To **leverage on the competence accumulated over years** on an issue where securities supervisors and central banks may have an important experience to share. Central banks are knowledgeable mainly because of the expertise gathered in the implementation of monetary policy (collateral management, risk management), which requires, to be effective, a smooth market functioning, financial integration and financial stability.
- > To further **promote cooperation between the EBA and the ECB** in view of the forthcoming supervisory responsibilities of the ECB.
- > To **cope with the likely criticisms** that the approach presented in the discussion paper is subject to some major flaws such as:
  - Regime shift: statistical evidence based on 2008-2012 period would not bring meaningful results for predicting future behavior of potentially liquid assets, since there will be a major regime change with the introduction in the EU of the Financial Transactions Tax (FTT) that will cause a serious distortion in the functioning of private financial markets. Moreover the new Basel 3 regulation itself will create a drastic change, since any asset that will be classified by Regulators as highly liquid will benefit of increased liquidity and any asset not eligible as highly liquid will experience a less liquid market place.
  - Data availability: transactional data may only be available for a limited set of asset classes and financial instruments (e.g. not for repo transaction, not for many assets that are liquid but not “actively traded” since they are priced in relative value terms,...). Especially from a liquidity perspective quantitative repo data is necessary for a correct assessment of the underlying liquidity characteristics.
  - Qualitative or quantitative analysis? Many of the explanatory characteristics (e.g. large number of market makers, traded via additional platforms and markets, wide range of potential buyers) cannot be handled in quantitative terms, since they are more qualitative (e.g. five not very active market makers could be much less effective in providing liquidity than two big ones; number of buyers is largely depending on pricing and risk taking capabilities in a specific moment)<sup>2</sup>.
  - Biased and not replicable results: the proposed approach might bring to biased results since it is not taking into account that many assets are priced and traded in relative value

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<sup>2</sup> See also question 4 of the discussion paper.



terms: even if the actual volumes traded are low, certain assets could be very liquid because highly correlated with other liquid assets. It is also to be mentioned that the proposed approach could never be replicated or back-tested by the banks (because of data availability and resources) so the institutions would not be in the position to challenge it or improve it<sup>3</sup>.

**Additional considerations for possible objections to UniCredit proposal:**

**On the scope:** One may argue that the scope of the Eurosystem list of eligible assets is not consistent with the EBA exercise. In contrast, the list of ECB eligible assets is sufficiently broad in terms of issuer location (EEA plus G10), issuer type (all), asset type (most of the relevant ones), currency denomination (most relevant currencies) and creditworthiness. This implies that the Eurosystem scope is compatible with the EBA scope, since there should be sufficient information for the EBA to make use of the Eurosystem classification for most of the relevant assets to be included in the LCR. The EBA could focus its efforts on those asset categories (gold, equities and commodities) not included in the broad list of ECB eligible assets.

**On the objective:** it could be argued that the objective and time horizon of the ECB risk management differs from those of the banking supervisory authorities. In the event this applies, this should not be leading to a different methodology to assess the market liquidity of asset categories. The methodology should be exogenous from the banking supervisors activity. It would become endogenous, and therefore no longer market neutral, if it was diverging from the Eurosystem methodology, without justification.

**On the data:** one may argue that the ECB is not equally empowered as the other European supervisors, in particular the ESMA, in terms of data collection and availability for the executed transactions. This seems a valid counterargument. It is positive that the EBA is willing to use, as primary source of data for debt securities, the transaction reporting databases held by national authorities, which were created due to mandatory reporting requirements under the Markets in Financial Instruments Directive (MiFID). It would be even better if a single centralised database was set-up and used by the ESMA and the EBA. As preferred option, UniCredit would encourage a fruitful cooperation between the European supervisory authorities and the ECB in terms of data exchange, also for the purpose of defining liquidity measurement methodologies.

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<sup>3</sup> See also question 5 of the discussion paper.



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