APB's Response to

EBA/DP/2013/01

DISCUSSION PAPER

On Defining Liquid Assets in the LCR under the draft CRR

February 2013 - 21 March 2013

20 March 2013

I – Preliminary Notes

This document contains the comments to the above mentioned Discussion Paper which was published by EBA on 21 February 2013.

II – Answers to the Questions

Q1. Given the difficulties with obtaining transactional data outlined here, do you think a data sample cover 2008-2012 is sufficient for this analysis? Would you see merit in extending the sample in those countries where more data is available?

The 2008-2012 is a highly stressful period. Although interesting to use for stress purposes analysis it may lead to some biased results in the sense that some type of assets might have been deeply hurt than others due to the type of crisis (sovereign + financial crises). For instance, dot-com stocks were probably less impacted liquidity wise than euro peripheral bonds but the opposite might have been true in the 2001 dot-com burst. Hence conclusions drawn from the 2008-2012 data need to take into consideration the type of macroeconomic stress that was involved and that underlies the current fragmentation of European markets. We see some advantage in extending this period in those countries that have available data, as it recovers the performance in a pre-crisis scenario.

Q2. Do you have additional data sources to suggest? Specifically, can you suggest a source of repo data and gold that would fit our needs?

Data on Asset Classes:

a. MiFID Transaction Reports - data for debt securities

b. Equity Data - data for equity markets

c. Data on gold - difficult to obtain from public sources

d. Additional Data Sources - data on securities trading should be supplemented with data on turnover in repo markets; however the EBA has concluded that a source that would enable examination of the volume of trading at an ISIN level across the asset classes covered in the EBA report is not available.

Although there is still a big part of repo transactions that is done OTC, it is possible to obtain information in LCH and CC&G.

There are also platforms of negotiation of repo's that might have available information about these transactions, namely Brokertec and MTS Repo.

Q3. Do you agree with the list of liquidity metrics under consideration to be used in the EBA assessment, as mentioned in this section and Annex 5? Can you suggest further metrics the EBA should make use of, where information would be available?

Liquidity metrics seem to be biased by dimension, since bigger markets and higher volumes seem to benefit from the definitions proposed. But liquidity is a relative concept, it needs to be assessed *vis a vis* the relevant market. A small outstanding by, let's say, a US *standard*, might be an highly liquid issue let's say in Portugal or other Member States. So, some harmonization or "scale" adjustment might be reasonable to consider when assessing liquidity metrics. The same would apply to spreads; these should be considered as proportion of the issue price.

DP is much oriented to a buy/sell assets perspective, but if we extend these metrics to repo transactions we should introduce the analysis on repo rates, haircuts and maturities of the deals.

These are the items that support the transaction and the possibility of transforming that asset in liquidity.

Q4. Do you agree with the list of explanatory characteristics whose linkage to liquidity it is proposed to be tested in the EBA assessment? Can you suggest further characteristics the EBA should assess?

We agree with this list of explanatory characteristics, but we add the comments that were mentioned in Question 3.

Further characteristics EBA should assess:

1. Liquidity Metrics:
a. Minimum trade volume of the assets;
b. Minimum outstanding volume of the assets;
c. Transparent pricing and post-trade information;
d. Credit quality steps referred to in part three, title ii, chapter 2 (credit ratings);
e. Proven record of price stability;
f. Average volume traded and average trade size (trade volume / number of trades);
g. Maximum bid/ask spread;
h. Remaining time to maturity;
i. Minimum turnover ratio (trade volume / outstanding volume).

2. Explanatory Characteristics:
2.1. General explanatory characteristics that refer to the market structure would include:
 * Presence of a large number of market makers
 * Trade via additional platforms and markets
 * Wide range of potential buyers
 * Transparency
2.2. General explanatory characteristics specific to an asset would include:
* Collateral eligibility
* Credit rating
* Issue size
* Remaining time to maturity

Q5. Do you agree with the methodology proposed? Do you have alternative approaches that might be used?

- **Liquidity metrics and ranking of asset classes** - analyse combinations of liquidity metrics with a view to producing an ordinal ranking of the relative liquidity of asset classes.

- **Explanatory characteristics and ranking within asset classes** - This analysis will help further refine the ordinal rankings that will have been produced, enabling to differentiate the liquidity of different groups of assets according to their explanatory characteristics.

Under a theoretical view, we agree with the methodology proposed, but putting it in practice generates some comments. In fact, this methodology is based in two components -rating and liquidity - which are the characteristics of HQLA buffer. The application of these criteria to Portuguese banks has a complicated effect as their portfolios have Portuguese Sovereign Bonds and these securities don't comply with the defined requirements of rating and liquidity.

If the methodology is very strict, Portuguese Bonds would be classified not as Level 1 Assets, with 0% hair cut, but as Level 2 Assets with 15% hair cut (according to actual hair cut) or as non liquid assets.

This becomes quite absurd as banks that have those assets can use them to obtain liquidity in other banks or in ECB, through repo.

As such, this question has to be taken into consideration when an asset is classified as liquid