

Gertrude Tumpel-Gugerell: Priorities for integration

Speech by Ms Gertrude Tumpel-Gugerell, Member of the Executive Board of the European Central Bank, at the 13th Euro Finance Week, Frankfurt am Main, 15 November 2010.

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Good morning ladies and gentlemen,

I was reminded recently that it was only 140 years ago – in 1871 – that Germany created a monetary union replacing the Thaler in Prussia and the Gulden in Bavaria by the Goldmark.¹ Although it is said that relations between Berlin and Munich are complex, nobody has questioned that the Länder using one currency are also using the same standards for payments and settlements.

12 years ago the single currency was introduced in the euro zone replacing national currencies by only one means for cash payments – the euro.

Where do we stand on payment and settlement integration now?

Many harmonization and integration initiatives exist (on paper), but are not yet fully implemented and developed.

The financial crisis has shown that we have to substantially step up our efforts in this domain:

First, as the financial crisis has shown the crucial importance of liquidity and sound liquidity risk management, stable, sound and integrated payment and settlement systems can play a crucial role in ensuring a secure flow of liquidity and supporting banks to manage their liquidity risk.

Second, as we have seen that payment and settlement systems have functioned well during the recent crisis and have contributed to prevent worse outcomes, continuous work on further strengthening and harmonizing payment and settlement systems will enhance the resilience of the financial system.

And third, as more harmonized and integrated payment and settlement systems increase the efficiency of financial markets and ultimately lead to cost savings and welfare gains for the overall economy, these efficiency gains will free up more liquidity and capital for the financial industry. In fact, the cost savings from – for example – a more integrated retail payments market were estimated to be around EUR 18 bn. annually for the euro area.

When the Euro Finance week was established 13 years ago, we were at the beginning of a very rich period in terms of integration in the field of payment and securities settlement systems.

We established the European Monetary Union with a single currency and we started the integration of the European payments infrastructure by the creation of the Eurosystem large-value payment system TARGET/TARGET2. Today, TARGET2 is the first market infrastructure to be completely integrated and harmonised at the European level which has been instrumental to the integration of money markets and wholesale banking activities in Europe and has, hence, supported the smooth transmission of our common monetary policy across the euro zone.

Despite this achievement in the field of financial integration, it has become evident that this is not enough. In particular, in the field of retail payments and securities settlement I see a lot more to do!

¹ This monetary union was culminated with the establishment of the Central Bank under the Banking Act of 1875 and the introduction of the “Deutsche Mark” as single currency.

In my intervention today I will, therefore, focus on two projects that aim to address the fragmentation still present in the field of retail payments and securities settlement: the Single Euro Payments Area (SEPA) and Target2 Securities (T2S).

Let me start with SEPA. As you are certainly aware, just recently, we published the Eurosystem's 7th Progress Report on SEPA, in which we welcome the overall progress made in delivering SEPA but also indicate areas where more work is still needed.

Certainly, many stakeholders want to bring the SEPA project further and have contributed to its progress so far.

First, enormous progress has been made by the payments industry in delivering SEPA. In particular, the SEPA direct debit design and launch in November 2009 is, in my view, the most remarkable development on the payments industry side.

The SEPA Direct Debit is a key payment instrument as it is the first time that a utility company, like, for example, your telecommunications provider, can charge your account regardless of the country of its location and regardless of the location of the bank at which you have your account.

This represents a big improvement as it finally allows customers to conduct all euro payments within Europe from one single account. The SEPA Direct Debit is good for everyone. Companies and individuals will benefit from increased competition and will be able to get the payments provider that best fits their needs.

In Germany, the implementation of the SEPA Direct Debit should not represent a big challenge as the SEPA Direct Debit scheme is very similar to what already has been available at national level for a long time. In this respect, I encourage German stakeholders to find a pragmatic solution regarding the mandate migration. Such solution should limit the efforts for companies as well as for customers.

Second, I believe that we should not forget the role public authorities are playing to get SEPA up and running. All but one of the EU member states have finalised the transposition of the Payment Services Directive in their national legislation. This means that for payment service providers a harmonised legal framework is in place in almost the entire European Union. In some countries we see great progress by public authorities moving to SEPA standards.

Another aspect in which public authorities have been very active in the last months has been in the establishment of the SEPA Council. We, the ECB, and the European Commission recognised that having both the demand and the supply side around the same table discussing SEPA related issues in a transparent way is crucial for the success of the project. As for "tango", it takes two to SEPA, and to move in a co-ordinated way.

And third, the SEPA users have shown in the SEPA Council but also in many national SEPA fora an increased willingness to embrace the SEPA project.

Coming now to the areas for improvement, the progress report also indicates some of the barriers the SEPA project has to overcome to be a success. Let me stress only a few major issues.

First, I believe that to reap the benefits of SEPA there is a need to use only and exclusively the SEPA instruments. In our recent progress report on SEPA, the ECB has clearly spelled this out by stating that it "expects that a mandatory timeline for migration to SEPA instruments will significantly accelerate the pace of transition, enabling SEPA to be completed, preferably, by the end of 2012 for credit transfers and by the end of 2013 for direct debits".

I am looking forward to the European Commission to come in due course, after consulting the relevant stakeholders, with the necessary legislative proposal to make this possible.

Second, although a lot of progress has been witnessed with the delivery of the SEPA Credit Transfer and the SEPA Direct Debit, less has happened on cards and innovation.

On innovation, the ECB has been strongly supporting the emergence of SEPA wide online e-payment solutions like the ones already existing at national level, for example in Germany, Austria and the Netherlands. This will provide more payments alternatives to the users, but it will also address a problem which is a concern for central banks: safety. For “internet shopping” the payments industry needs to deliver something that permits the customers to conduct such activities in a safe way. Online payment solutions are suitable to achieve such safety.

T2S

Let me turn to the second major integration project: Target2 Securities (T2S), the Eurosystem’s technical platform for core, neutral and borderless multi-currency securities settlement in central bank money across Europe.²

T2S scope and benefits

Let me first emphasize that T2S is not only a project for the euro-area countries but is open for providing settlement services for securities transactions in other currencies as well. This European approach does not only make sense from a financial integration perspective but is also driven by strict economic rationale.

T2S will have network effects and generate economies of scale. This will not only be due to the very low settlement cost but also due to the liquidity savings for participants. In T2S, participants will only have to provide liquidity for one system, instead of 30 systems today. Further benefits will result from harmonised processes throughout Europe, and last, but certainly not least, T2S will – without doubt – introduce competition in the single market in general and in the post-trade industry in particular.

We have made a lot of progress in T2S so far and I would like to briefly recapitulate the major recent achievements as well as the main future milestones.

T2S recent achievements and future milestones

The T2S project started in summer 2006 and is currently half-way towards the go-live date in September 2014. Right from the start, the Eurosystem has closely involved the market in its deliberations on T2S such as for the development of the user requirements. Transparency and co-operation have become core assets of T2S. After signing a Memorandum of Understanding with 30 CSDs in Europe in 2009, the Eurosystem has worked on a Framework Agreement with CSDs and we hope to finalise the negotiations next year.

Regarding non euro area central banks participation in T2S we are currently discussing with the central banks of Denmark, Sweden, Norway, Iceland, Switzerland, the UK and Poland.

A crucial topic for all stakeholders is the “**pricing**”. The Eurosystem has been very transparent on its cost and on the way it intends to set its prices guided by the principle of full cost recovery that applies for T2S. The T2S Programme Board has proposed to the Governing Council to set the price for a DvP instruction in T2S at 15 cents and to guarantee this price until the end of 2018 under certain conditions. The Programme Board is confident that it will be able to further lower settlement fees after 2018 since its proposal is based on rather conservative assumptions. However, even in the most unfavourable circumstances, the Programme Board proposes that annual price increases will be not be more than 10% until 2022, the end of the cost recovery period.

² See also the recently published paper by the ECB in October 2010 called “T2S: Half-way to delivery” which explains in great detail the purpose, scope and benefits of T2S and answers relevant questions that are currently asked.

For the CSD customers, of course, it depends on the fees that CSDs will add on top for their services but I am convinced that the final settlement price in a T2S world will be lower than the current domestic prices in any European country. Prices for cross-border transactions should even decrease by around 90%. In an environment where CSDs will be able to compete with each other, they will not only need to adapt their systems to T2S efficiently but they also can reap first mover advantages, if they adapt their systems quickly and are able to offer pan-European securities settlement services to their customers as early after the opening of T2S as possible.

T2S and harmonisation

While cost reductions and lower settlement fees are direct benefits of T2S, further benefits relate to harmonization. The harmonisation of back office processes will be one of the core benefits of T2S. T2S will offer one single process for securities settlement throughout Europe, thus eliminating some of the Giovannini barriers. T2S will harmonise market processes and market practices throughout Europe and also for this reason, it is important that all European markets participate in T2S so that their requirements can be taken into account when harmonised processes are being defined.

T2S has already achieved a lot in terms of harmonisation and further initiatives are on the way. The T2S Advisory Group will have a discussion in December 2010 to identify the priorities in harmonisation. This will be an extremely important exercise since only harmonised procedures will allow for smooth and efficient settlement throughout Europe. Thus T2S will benefit from harmonisation and, vice versa, harmonisation initiatives in Europe will benefit from T2S.

Conclusion

Some weeks ago Commissioner Barnier asked the following question: "How is it possible that the single market is more and more necessary, yet less and less popular?"

I believe that the notion exists that opening markets for competition would challenge well functioning business models at national level. Also, people may believe that the fastest way to leave the crisis behind is protecting local markets.

However the opposite is true. The financial crisis has reinforced the need for greater financial integration. Moreover, European market integration is about growth, development and more business opportunities; Both T2S and SEPA have the potential to change and improve the way business is organised for cross border transactions. They will significantly facilitate to offer services abroad and thus introduce competition in a market segment where competition has been limited so far. It will lead to lower cost and thus generate dynamic effects to the benefit of all European citizens.

The Eurosystem fosters integration by different means: as catalyst, by helping market participants finding solutions or as operator by providing pan-European infrastructures that allow for fair and open access respecting the level-playing field amongst participants. The Eurosystem is determined to foster European integration in financial markets and it is willing to do this in close co-operation with the market. As Adolph Kolping a German priest active in social integration said in the 19th century: "we can achieve a lot together, if there is an imploring will".

Thank you very much for your attention.