

Joachim Nagel: Launching a trading desk in Tokyo

Welcoming remarks by Dr Joachim Nagel, Member of the Executive Board of the Deutsche Bundesbank, at the opening of the enlarged office of the Deutsche Bundesbank in Tokyo, Tokyo, 6 September 2012.

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1. Introduction

Governor Shirakawa,
Vice Minister Nakao,
Ladies and Gentlemen,

I would like to convey my sincerest gratitude to all those who have helped us to establish a trading desk in Tokyo, especially the Bank of Japan. I would also like to thank the Ministry of Finance and the Financial Services Agency very much for their support.

Our decision to start trading operations in Tokyo has attracted some attention. I think it would therefore be useful to provide you with some background information on this matter.

2. The Deutsche Bundesbank's foreign reserves

As trading operations in Tokyo form part of the management of foreign exchange reserves, let me first provide you with some basic information on the Bundesbank's foreign reserves. Foreign reserves have three main components: foreign exchange, the position with the IMF and gold. Germany's foreign exchange reserves amount to around EUR 31 bn., of which the majority is invested in US dollar, and also a share is invested in Japanese yen. For many years, the total volume of the foreign exchange reserves has been kept quite stable. Due to the valuation at market prices, the share of gold within the Bundesbank's reserves has increased significantly during recent years. The composition of the reserve assets is less the result of a portfolio optimisation strategy than, first and foremost, a response to gold transfers under the Bretton Woods System and to foreign exchange interventions prior to the launch of European monetary union.

The management of the Bundesbank's US dollar und Japanese yen portfolio is based on the principles of safety, cost efficiency and liquidity. The trading office in Tokyo will essentially be responsible for executing purchases and sales of Japanese government bonds during Tokyo trading hours. The Bundesbank's Central Office in Frankfurt will remain responsible for making strategic decisions and coordinating investment activities.

3. On-site reserve management

In April 2009 the Bundesbank started to use the premises of its Representative Office in New York to launch a trading desk for reserve management operations in US Treasuries and money market instruments such as repos. So why do we also trade outside of Frankfurt?

Trading activities create contacts with market partners and enable Bundesbank traders and analysts to increase their knowledge of financial market developments on site. Through their physical presence at financial centres, they gain access to additional market information and benefit in other ways through having local contacts. The Deutsche Bundesbank's Markets Department condenses this information and makes it available internally through its daily market reports from New York. The Bundesbank expects the trading desk to strengthen contacts with local banks and institutions. A physical presence on site and a network of contacts will contribute in many respects to a better understanding of financial market developments both in and beyond Japan. The Bundesbank will benefit from this, not only with regard to the management of its foreign reserves. The provision of regular market

reports and the establishment of contacts will also benefit the Bundesbank's internal bodies. This will strengthen the Bundesbank's hand when contributing its expertise to international committees (BIS, IMF, G7) and when fulfilling its role in the Eurosystem.

In addition to business relationships with local market participants, the trade contacts will provide a "springboard" for making new contacts. Experience gained operating our trading desk in New York shows that a physical local presence intensifies contacts with market participants for both the trading desk itself and the Representative Office. Particularly during the current crisis, the Bundesbank has benefited from an enhanced flow of information.

4. Business case for an Asian trading desk in Tokyo

Looking at the time difference, it is clear that the positive experience in New York is an equally convincing argument for an office in Asia. The trading day in Tokyo ends when European trading hours begin. There was no doubt over which location would be most suitable in Asia, as the Bundesbank already has a Representative Office in Tokyo. The enlargement of our Tokyo office bears witness to the increasing economic and political importance of Asia. Maintaining and strengthening contacts with Japanese market players and the Bank of Japan – the central bank of Asia's traditional economic centre – will strengthen the Bundesbank's role in the Eurosystem and in international cooperation. One particular argument in favour of a local presence is the Japanese market, which has a high proportion of domestic investors and influences.

The Bundesbank has now had an office in Tokyo for 25 years. Japan is one of the largest economies in the world. Germany and Japan are closely connected. Most importantly, the investment of foreign reserves in Japan has forged a strong link between the Bundesbank and the Bank of Japan. The Japanese yen is an important reserve currency in view of its relevance in foreign exchange markets, where it has the third largest turnover of any currency after the US dollar and the euro. The USD/JPY currency pair is also one of the most frequently traded in the world, second to EUR/USD (BIS: Fx-Triennial Survey, 2010).

Furthermore, on-site trading in Japan will permit us to deepen our contacts with the trade and settlement sections of the Bank of Japan, which manages accounts and safe custody accounts for the Bundesbank within the context of foreign reserve management. The Bundesbank also expects this closer contact to yield additional knowledge about the functioning of the Japanese economy and monetary policy. Furthermore, it will enable contacts with the Bank of Japan to be strengthened at a political level, too.

The Bundesbank's trading desk in Tokyo will allow it to conduct trading during those hours when Tokyo's daily trading volumes are at their heaviest. Until now, the time difference has prevented the Bundesbank from trading during this market phase and it is therefore currently unable to directly respond to economic data or unexpected market events in Japan. In this respect, the opportunity to trade in Tokyo will minimise potential losses and help limit risks for investment committee and trading positions. Furthermore, trading during the Tokyo trading hours will create, in particular, significant scope for reducing transaction costs. Compared with the European trading hours, the bid-ask spreads will decrease significantly owing to the greater trading volume and higher level of market liquidity. We are taking advantage of this by shifting a part of our trading activity to this time zone.

5. Conclusion

There is no doubt that it is now more important than ever for us to gain a deeper understanding of Japan, Asia and the Pacific region. The Representative Office and the new trading desk will be our window to the Asia-Pacific region. Expanding our presence in Tokyo reflects the importance of the Japanese financial market and the growing influence of the region in the global economy.

The new trading desk will be a great enhancement to the Bundesbank's Representative Office, which already has a long and successful history. Today we want to celebrate this launch with you. I hope you enjoy the reception.