

# Yves Mersch: Digital transformation - Europe's integrated market of tomorrow

Speech by Mr Yves Mersch, Member of the Executive Board of the European Central Bank, at the Joint ECB and European Commission Conference "Into the future: Europe's digital integrated market", Frankfurt am Main, 31 January 2017.

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## Introduction

For over a decade the European Commission, the Eurosystem and the market have been working towards transforming what has up to now been a very fragmented financial market infrastructure in Europe into a more integrated one. This work is still ongoing and requires more effort. However, we are at a point now when progress has become tangible. In the first part of my speech, I will briefly take stock of where we stand, particularly with regard to the post-trade area. I will then address two areas where I still see gaps that are in the way of our achieving a truly integrated European financial market. The first area is securities issuance, the second instant payment settlement. In both these areas, digitalisation is opening up new opportunities, which requires action. We at the ECB stand ready to take action accordingly.

## Integration in the post-trade area

Following the launch of T2S in summer 2015 and two further migration waves in 2016, the German market is due to migrate to T2S in less than a week's time. This latest development is expected to bring a big increase in the volume of securities transactions being settled on the platform. More particularly, we anticipate an increase of up to 90% of the total volume expected by the time all participating central securities depositories (CSDs) connect to the platform. The next migration wave will also lead to an increase in the use of links between T2S markets that facilitate cross-border transactions.

T2S has significantly contributed to the integration of post-trade processes across all participating markets. This has been achieved by the gradual implementation of the single rulebook, i.e. standards, rules and procedures, in the T2S market. Harmonisation measures necessary for ensuring efficient and safe cross-CSD settlement in T2S are fairly advanced. Monitoring has shown that, by the time they migrate to T2S, market communities are close to achieving full compliance with the T2S standards.

Nevertheless, some gaps in compliance remain, for example in the area of corporate actions. These are complex business processes for asset servicing, which involve rules and procedures developed by a range of different actors. The newly established Advisory Group on Market Infrastructure for Securities and Collateral (AMI SeCo) will address these gaps in compliance, among others. This advisory group will also look at ways in which the existing methodology could be used as a blueprint for building a methodology to harmonise collateral management.<sup>1</sup>

In addition, the T2S harmonisation agenda has identified a number of regulatory and legal barriers to post-trade harmonisation that fall under the regulatory agenda. These relate, among others, to issues such as conflict of law and withholding tax procedures, which are expected to be tackled this year. While the regulatory and legal barriers have proved to be thorny issues, I expect that the Commission, as part of its capital markets union (CMU) action plan, will not be dissuaded from its efforts.<sup>2</sup>

## Integration of securities issuance

With T2S, the Eurosystem has created the basis for an efficient and effective settlement

mechanism for securities in Europe. At the same time, by adopting the CSD Regulation (CSDR), the Commission has contributed to further harmonisation of the CSDs' regulatory framework. However, to be able to reap the benefits of these efforts, market participants and corporates need to have full and direct access to the entire EU securities market at a low and harmonised cost.

A European securities market should offer the possibility of issuing, settling and holding securities in the same way, regardless of where issuers and investors are located. A fully harmonised system of securities issuance could reduce the transaction costs for capital financing, make the European securities market more attractive in the global economy, and allow an effective redistribution of private risk across the EU markets. A sound and uniform pan-European securities issuance mechanism would also be conducive to the creation of the CMU.

Despite efforts to overcome the fragmentation of the securities market by providing a level playing field, there is still too little evidence of competition. The effects of competition have not been felt in terms of an actual geographical widening of services provided by the vast majority of issuers. The goal of having euro area markets where access is as easy and efficient as it is to the respective national market has – with few exceptions – not been met yet.

The remaining fragmentation is often the result of legacy and national rules. This fragmentation is an area that calls for action. It may be worth exploring the establishment of a truly European issuance service – at least for some supranational debt instruments. We could even think about the ECB/Eurosystem playing an active role in setting up such an issuance service. And we could consider whether and to what extent new technologies, like distributed ledger technology (DLT), can be used in that process.

### **TARGET instant payment settlement (TIPS)**

Turning to the retail payments market, I have to say that, despite the introduction of standardised retail payment instruments and harmonised processing rules, the retail payments market infrastructure in Europe is still fragmented. Apart from a few exceptions, automated clearing houses (ACHs) still primarily focus on their respective national markets.

The availability of a safe and efficient market infrastructure that can guarantee the processing of instant payments across Europe is a prerequisite for the launch of pan-European instant payment solutions. Payment service providers should have the choice to either clear their instant payments through ACHs or use a settlement service for instant payments.

Earlier this month, the Eurosystem launched a market consultation on user requirements and the expected volumes for a settlement service for instant payments in central bank money. The proposed TARGET instant payment settlement (TIPS) service would offer a series of benefits to the payment service providers. First, it would guarantee pan-European reachability for instant payments. Second, it would give payment service providers the possibility to use their credit lines stemming from their collateralised positions in TARGET2. Third, it would eliminate credit risk, thus leading the way to faster and efficient settlement. Last but not least, it would give payment service providers more choice: they could either connect directly to TIPS or channel their payment instructions for instant payments through their respective ACH.

The Eurosystem will take a decision by June 2017 on whether to develop the service, based on the results of the public consultation. TIPS could commence operations as soon as 2018.

### **Conclusion**

Let me conclude.

With the migration of the German market to T2S next week, the time has come to reap the actual

benefits of harmonisation in the post-trade area in Europe. But this does not mean we can slacken in our efforts. There is still a need for further and coordinated action in the harmonisation of post-trade processes. There are also gaps that remain in the financial market integration process when it comes to securities issuance. And there is a need for action in instant payment settlement across Europe. The ECB, together with market stakeholders, has to explore how to best take action in these areas. Thank you for your attention.

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<sup>1</sup> This work covers issues such as collateral mobility and cross-border interoperability (i.e. collateral messages, workflows, cut-off times, settlement cycles, etc.).

<sup>2</sup> With regard to the conflict of law issue, the ECB welcomes the Commission's "legislative initiative" to determine with legal certainty which national law should apply to security ownership. The ECB will contribute to the forthcoming public consultation with a view to strengthening the legal environment for cross-border settlement services. With regard to the withholding tax procedures, the Eurosystem welcomes the Commission's announcement that a Code of Conduct on withholding tax procedures will be published in 2017. The AMI SeCo predecessor – T2S Advisory Group – has contributed substantially to the work of the Commission in analysing the possible harmonisation on withholding tax procedures and stands ready to further contribute to this work, if required.