
SCP – Scandinavian Cash Pool

SCP is an automated system for the pledging of cross-border collateral between Denmark, Norway and Sweden. The system was developed in order to facilitate the Scandinavian CLS¹ participants' access to intraday liquidity in the Scandinavian currencies.

The main principle of SCP is that liquidity raised at the central bank of one country may be pledged as collateral for loans from the central bank of another country. The participant pledges collateral at the national central bank by transferring liquidity to a special account that is pledged to the foreign central bank. The latter is notified automatically of the pledged amount and on that basis grants credit to the participant. When the participant has repaid the loan to the foreign central bank, the national central bank is informed automatically that the collateral may be released, i.e. the amount on the pledged account is automatically transferred back to the participant's current account. SCP may only be used to pledge collateral for intraday credit.²

SCP is based on existing structures and systems. The liquidity is raised at the national central bank according to national procedures and within national systems. The liquidity is pledged to the foreign central bank via an ordinary transfer between accounts in the national RTGS system. The communication between the central banks is automated and based on existing standards (SWIFT). This structure ensures that cross-border collateral can be pledged via SCP in less than one minute.

BACKGROUND TO AND USE OF SCP

The Scandinavian currencies became part of CLS in September 2003. As a consequence the requirements of the participants' procurement of liquidity in these currencies have been expanded. Moreover, three of the Scandinavian participants have made a commitment to contribute to the CLS Liquidity Facilities in all three currencies, which means that they must be able to raise large amounts in one or several of the Scandin-

¹ CLS (Continuous Linked Settlement) is an international foreign-exchange settlement system. For further information, see *Financial Stability*, 2003 page 97.

² For further information on SCP reference is made to www.nationalbanken.dk under Tasks/Payment systems/Collateral. For a description of the legal basis for SCP, see Niels C. Andersen and Kirsten Gürtler, The Provision of Collateral to Danmarks Nationalbank in a Legal Perspective, Danmarks Nationalbank, *Monetary Review*, 3rd Quarter 2003.

avian currencies at short notice. CLS is the primary reason for the establishment of SCP.

However, the use of SCP is not limited to CLS purposes, and the system is open to other than the CLS banks. For instance, SCP will make it possible for banks with activities in more than one Scandinavian country to centralise the pledging of collateral and liquidity management in one country and nonetheless still cover their intraday liquidity requirements in the two other countries.

Today four of the five Scandinavian CLS participants also participate in SCP. During the first month after the Scandinavian currencies became part of CLS, SPC was primarily used to pledge collateral in Denmark in order to obtain intraday liquidity in Norway and Sweden. The explanation may be that the participants primarily hold their collateral in Denmark, or that the payments to CLS are relatively larger in Sweden and Norway compared to the liquidity available in the country in question.

FOCUS ON CROSS-BORDER PLEDGING OF COLLATERAL

The establishment of CLS has generally increased focus on the possibility of pledging cross-border collateral. Particularly the large international banks are motivated by other factors besides CLS to require easier access to cross-border intraday liquidity. In March 2003 a task force under The Payments Risk Committee set up by the Federal Reserve Bank of New York with participants from 13 large international banks published a report on cross-border pledging of collateral and access to intraday liquidity.¹

According to the report, the need for cross-border intraday liquidity is increasing. The internationalisation of the financial markets entails that banks increasingly operate beyond their domestic markets. The banks represented in the task force state that around half their payment activities take place in foreign markets, and therefore they require cross-border liquidity. Over the years payment and settlement systems have moreover been introduced which in many ways enhance the overall security of the financial system, but which also make higher demands of the participants' liquidity procurement. CLS is only the most recent example.

The task force recommends that the central banks for the CLS currencies to a larger extent accept securities denominated in foreign currencies as collateral for intraday liquidity. In addition, the task force set

¹ The Payments Risk Committee, Report by the Cross-border Collateral Pool Task Force, Managing Payment Liquidity in Global Markets: Risk Issues and Solutions.

MODELS FOR PLEDGING CROSS-BORDER COLLATERAL	Box
<p>In the Risk Committee's report the proposed facilities for pledging cross-border collateral are collectively referred to as Cross-border Collateral Pool Facilities. Three basic models are described. For two of them different options are presented:</p> <ul style="list-style-type: none"> • <i>Securities Collateral Pool</i>: In this model, market participants would be able to utilise foreign securities as collateral for intraday credit at a central bank. The report recommends an option where all central banks open custodian accounts with one or perhaps two international central securities depositories (CSDs). A bank requesting credit in a given currency transfers securities to the account of the relevant central bank. The CSD notifies the central bank that securities have been pledged as collateral, after which the central bank grants the credit. • <i>Cash Collateral Pool</i>: In this model, market participants would be able to pledge foreign currency to a central bank as collateral for intraday credit. One option entails that all central banks open accounts with each other. A bank wishing to pledge collateral in e.g. US dollars and obtain intraday credit in e.g. pounds sterling, transfers dollars to the Bank of England's account at the Federal Reserve Bank. Against collateral in this deposit the Bank of England provides credit in sterling. A drawback of the Cash model is that it cannot be used if one of the central banks is closed. • <i>Central Bank Guarantee Model</i>: This model is based on the central banks guaranteeing each other that collateral has been pledged, either as securities or cash. When a bank has transferred the collateral to a special guarantee account at a central bank, the central bank granting the intraday credit is notified. This model also requires that the central banks are open at the same time. <p>The overall recommendation in the report is the establishment of a Securities Collateral Pool. Securities and CSDs are well-known elements of the existing arrangements for pledging collateral to central banks, and the model functions across time zones.</p> <p>SCP is a combination of elements from the Cash Collateral Model and the Central Bank Guarantee Model.</p>	

out a number of models for how the central banks might build up an infrastructure for the pledging of cross-border collateral. The models are described in the Box.

On the basis of the report, the opportunities and requirements for facilitating access to cross-border liquidity are being discussed among the central banks. It is clear that in the first instance the need for a facility for pledging cross-border collateral is greatest among the large international players participating in payment settlement in the USA, Europe and Asia. On the other hand, easier access to cross-border intraday liquidity may serve as an incentive to smaller banks to increase their international activities.