



IV

ANNUAL REPORT 2002



PAYMENT AND SECURITIES SETTLEMENT SYSTEMS

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4 PAYMENT AND SECURITIES SETTLEMENT SYSTEMS

4.1 LIPS-Gross

4.1.1 Membership of RTGS-L Gie

The real time gross settlement system, LIPS-Gross, Luxembourg's interbank gross payment system, started operations on 4 January 1999. In 2002, a new bank joined the system and the RTGS-L Gie, operator of the system, now has 31 members.

4.1.2 Operations in 2002

4.1.2.1 Domestic payments

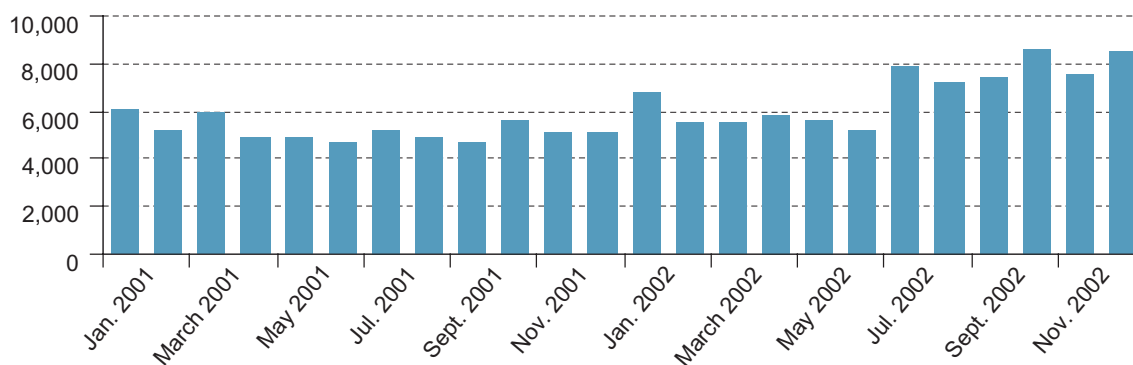
In 2002 and on a domestic level, LIPS-Gross participants sent a total of 81 749 payments (62 336 in 2001) for a total value of 1 231 billion euros (1 208 billion in 2001). In comparison with 2001, the volume increased by 31% and the value exchanged by 2%.

Average value per payment was 15.1 million euros against 19.4 million in 2001, the decrease reflecting the strong increase in volume and the rather stable value exchanged. A monthly average of 6 812 domestic payments for a total value of 102.6 billion euros passed through LIPS-Gross.

On a daily basis, an average of 320 domestic payments for a total of 4.83 billion euros were processed.

The following graphic shows the evolution of domestic payment volumes on a monthly basis.

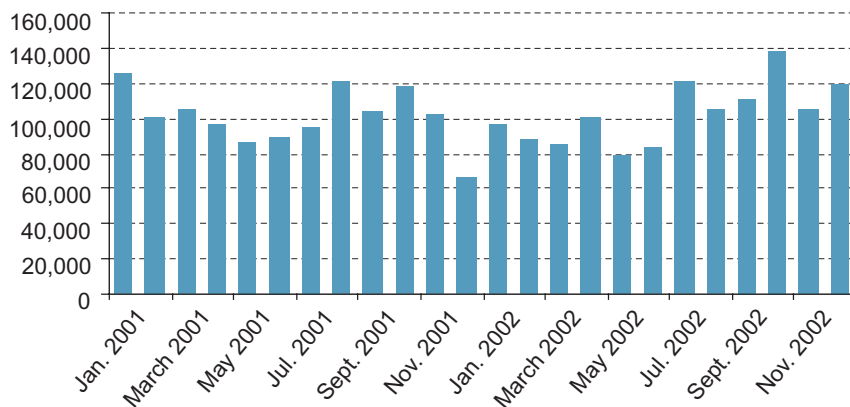
GRAPH 1 DOMESTIC PAYMENTS: MONTHLY VOLUMES IN 2001 AND 2002



From February to June, lower volumes followed the strong increase of volumes of January 2002; the last months of the years showed again much higher volumes. On a global scale volumes increased strongly. Concerning the value of domestic payments, the BCL first noted a downward trend until June 2002 followed by increases starting in July. Globally, the value exchanged remained rather stable.

One reason for the increase of domestic volumes results from the fact that the depository Clearstream used LIPS-Gross from 1st July 2002 on as an interface for the cash accounts which Clearstream manages on behalf of its Luxembourg-based customers. This, however, had no effects on total value exchanged.

GRAPH 2 DOMESTIC PAYMENTS: MONTHLY VALUE IN MIO EURO IN 2001 AND 2002



4.1.2.2 Cross-border payments

In 2002, LIPS-Gross participants sent 265 757 payments to other RTGS systems related to TARGET (231 852 payments in 2001) for a global value of 3 197 billion euros (3 221 billion euros in 2001). They received 297 862 cross-border payments (267 751 payments in 2001) for a total value of 3 199 billion euros (3 224 billion euros in 2001).

As for domestic payments, volumes of cross-border payments increased strongly, by 14.6% and 11.2% respectively. The value of payments, however, remained stable and as a consequence the average value per payment decreased.

Due to the stronger increase of domestic payments, the part of cross-border payments (in and out) in all the payments treated by LIPS-Gross declined slightly in comparison with 2001 and made up 87.3% (88.9% in 2001) of the volume and 83.9% (84.2%) of the value of all payments exchanged.

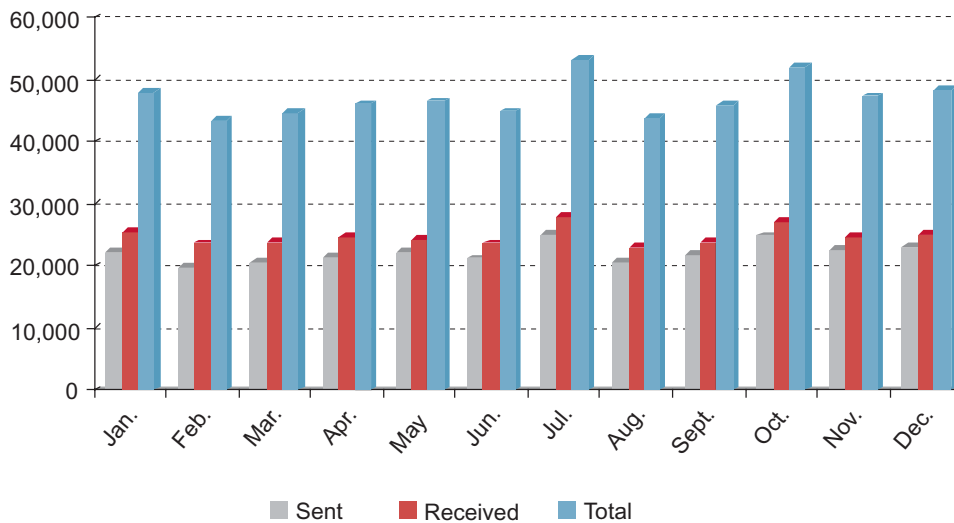
Average values for 2002 and annual variation rates in comparison with 2001 are indicated in the following table:

TABLE 1 CROSS-BORDER PAYMENTS

	Payments sent	Payments received	Value sent (EUR m)	Value received (EUR m)
Daily average	1 053	1 159	12 539	12 569
Monthly average	22 146	24 822	266 445	266 550
Variation	+14.6%	+11.2%	-0.7%	-0.7%

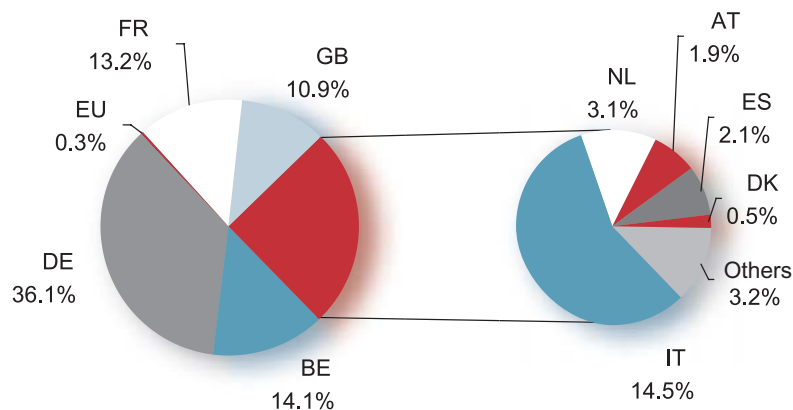
The following graphic shows the evolution of cross-border payments in volume. It confirms the traditional trend of RTGS-L members receiving more payments than they sent. After strong volumes in January, the further evolution turned out rather erratic, nevertheless showing a clear global upward trend.

GRAPH 3 LIPS-GROSS: CROSS-BORDER PAYMENTS



As in 2001, a majority in value of cross-border payments was exchanged with Germany (47.5% against 47.1% in 2001), Belgium (12.3% against 12.9% in 2001) and France (10.5% against 11.7% in 2001). The total part of the value exchanged with our neighbouring countries showed a decrease: 70.3% against 71.7% in 2001. Payments with the United Kingdom represented 10.8% of the total and those with Italy 5.2%. These percentages show some variations per volume and the most significant variations concern Germany and Italy.

GRAPH 4 LIPS-GROSS: CROSS-BORDER PAYMENTS PER VOLUME PER COUNTRY



In 2002, the Luxembourg banks achieved a positive balance of 1.3 billion euros with foreign banks. In 2001, this figure reached 2.1 billion euros. As in 2001, the ECB in Frankfurt as the clearing bank for EURO1, a multinational compensation system in euros, was an important supplier of liquidities – Luxembourg participants in this system have structural credit balances – whereas exchanges with Germany showed an important net transfer of funds in favour of our neighbour.

4.1.2.3 Aggregated figures of domestic and cross-border payments

The following table gives a global overview of daily average volumes and values exchanged per year. Volumes continue to increase whereas values exchanged remain stable at a high level.

TABLE 2 DAILY AVERAGES OF VOLUMES AND VALUES OF PAYMENTS EXCHANGED IN THE DIFFERENT YEARS

	Volume of payments			Total	Value of payments (EUR m)			Total
	Domestic	Cross-border sent	Cross-border received		Domestic	Cross-border sent	Cross-border received	
1999	206	624	702	1 532	2 805	8 675	8 657	20 137
2000	240	809	973	2 022	3 937	11 069	11 044	26 050
2001	246	915	1 056	2 216	4 750	12 717	12 726	30 193
2002	320	1 053	1 159	2 532	4 830	12 539	12 569	29 938

4.1.2.4 LIPS-Gross in comparison to other systems connected to TARGET

In 2002, all national RTGS systems together processed a total of 50.8 million of domestic payments (42.2 million in 2001) for a total value of 271 916 billion euros (201 428 billion euros in 2001). With 81 749 domestic payments for a total of 1 231 billion euros, Luxembourg represented 0.16 % of the volume and 0.45 % of the value.

In addition TARGET treated 13.7 million cross-border payments (11.5 million payments in 2001) for a total of 123 722 billion euros (128 481 billion in 2001). Luxembourg contributed by 1.94% to this volume and by 2.58% to the value exchanged.

4.1.2.5 Availability of TARGET

The global availability of TARGET reached 99.77 % in 2002 after 99.75% in 2001. The average figure for the 4 years of existence of TARGET is 99.60%.

After 99.98% in 2001, the availability of LIPS-Gross averaged 99.92% in 2002, reaching 100% during nine months out of twelve. In August, October and December minor incidents on the SWIFT network reduced the availability to 99.69%, 99.76% and 99.54%. The average availability for the 4 years of existence of LIPS-Gross is 99.55%.

4.2 Evolution of the Interbank netting system LIPS-Net

As 2001, 2002 may be considered as a year of consolidation for the electronic interbank netting system LIPS-Net, which has continued to offer to the Luxembourg banking community a fast and efficient tool for channelling domestic credit transfers and cheques. The European regulation on the harmonisation of fees for domestic and cross-border credit transfers will come into force in July 2003. This regulation will gradually change the European payments infrastructure landscape. Therefore, the consolidation process in the European retail infrastructure will require close monitoring and appropriate decisions will need to be taken with regard to the future evolution of the system in order to avoid isolation within the euro zone.

4.2.1 Operations in 2002

In 2002, the number of transactions exchanged through LIPS-Net has increased by 4.3% and reached a total of 13.69 million operations. The total value of operations has amounted to 48.16 billion euros (+ 0.88% compared with 2001). The daily average volume of transactions was of 54 541 operations. The highest volume has been recorded on 3rd of April with 112 472 operations.

Since October 2000, CETREL has introduced transactions related to the settlement of balances of debit and credit cards into LIPS-Net. Originally, these data were integrated with credit transfers and cheques figures and it was impossible to separate these statistics from the others. It is now possible, however, to distinguish figures related to the settlement of balances of credit and debit cards. This is why figures presented in the present annual report may differ slightly from the figures presented in the 2001 annual report.

Henceforth, operations of settlement of balances of debit and credit cards will be presented separately.

TABLE 3 OPERATIONS EXCHANGED IN THE INTER-BANK NETTING SYSTEM

	2001	2002	Variation
Number of credit transfers	12 556 252	13 292 580	5.86%
Value of credit transfers (1)	40 145	40 026	-0.30%
Average value per credit transfer	3 197	3 011	-5.82%
Number of cheques	544 699	379 373	-30.35%
Value of cheques (1)	3 639	3 334	-8.39%
Average value per cheque	6 681	8 788	31.53%
Number of transactions related to the settlement of balances of debit and credit cards	20 311	17 938	-11.68%
Value of transactions related to the settlement of balances of debit and credit cards (1)	3 958	4 803	21.34%
Average value per transaction related to the settlement of balances of debit and credit cards	194 893	267 775	37.40%
Total number of operations	13 121 262	13 689 891	4.33%
Total value of operations (1)	47 743	48 163	0.88%
Average value per operation	3 639	3 518	-3.31%

(1) millions of euro

4.2.1.1 Credit transfers

The total volume growth is exclusively due to credit transfers, which have increased by 5.9% to reach 13.29 million operations. The value of credit transfers, however, remained stable (-0.30%) to reach a total value of 40.03 billion euros. Concerning volume, credit transfers represented 97.1% of transactions exchanged in 2002 (95.7% in 2001). On the other hand, the value of credit transfers represented only 83.1% of the total value (84.1% in 2001).

4.2.1.2 Cheques

Concerning cheques, the withdrawal of the Eurocheque guarantee at the end of 2001 explains the strong decrease in volume (-30.4% compared with 2001). The decrease was smaller in value terms (-8.4% compared with 2001) and the average value of cheques increased from 6.681 to 8.788 euros.

4.2.1.3 Operations related to the settlement of debit and credit cards

Insofar as these operations are not retail operations but settlement operations between cards issuing institutions, it is important to mention them separately.

The total value of these operations was very high as it represented 10% of the value of total operations exchanged through LIPS-Net.

4.2.2 Technical changes

From a technical point of view, the new security infrastructure installed at the end of 2001 has been upgraded in order to meet the security level initially foreseen. This last step closed the security architecture replacement project.

4.2.3 Membership

On 31 December 2002, the number of direct participants connected to LIPS-Net amounted to 13, the same figure as at end-2001.

4.3. Eligible assets and their use for monetary policy operations

4.3.1. Categories of collateral

All Eurosystem credit operations are based on adequate collateral provided by the counterparties. In order to protect the Eurosystem from incurring losses in its monetary policy operations, and in order to ensure an equal treatment of counterparties throughout the euro area, collateral has to fulfil precise and common criteria.

Owing to existing disparities in Member States' financial structures, a distinction has been made between two categories of assets eligible for ESCB monetary policy operations. These two categories are referred to as "tier 1" and "tier 2".

Tier 1 consists of marketable debt instruments fulfilling uniform euro area wide eligibility criteria specified by the ESCB. Tier 2 consists of additional assets, marketable and non-marketable, which are of particular importance to national financial markets and banking systems. Eligibility criteria are established by the NCBs, which become thereby guarantors. The specific eligibility criteria for tier 2 applied by the respective NCBs are subject to approval by the ECB.

4.3.2. Collateral in Luxembourg and in the euro zone

At the end of December 2002, the domestic counterparties deposited eligible assets for a value estimated at 42.7 billion euros at the BCL. They were essentially made up of tier 1 assets (98.3%). 57.8% have been issued by credit institutions, 29.7% by central governments or local communities, 9.7% by corporations and 1.2% by supranational issuers.

Luxembourg counterparties significantly use eligible cross-border collateral. In 2002, 37.9% of all eligible collateral deposited by Luxembourg counterparties were used via the Correspondent Central Banking Model (CCBM) and 31% via the eligible links between national custodians. The proportion of domestic securities has increased in 2002 (31%) following a significant increase in eurobond issues, which reflect the considerable international activity of banks established in Luxembourg.

In December 2002, the average usage of CCBM in the euro zone was of 26.7% whereas domestic securities held with the national custodians represent 68% and securities held through links between securities settlement systems represent 5.3%.

4.4. Securities settlement systems

Article 18 of the statutes of the ESCB and the ECB provides that "In order to achieve the objectives of the ESCB and to carry out its tasks, the ECB and the national central banks may conduct credit operations with credit institutions and other market participants, with lending being based on adequate collateral".

In order to ensure "adequate collateral", the ESCB ensures that the securities settlement systems are of a high standard. These standards include technical, legal and operational safety. They maintain the safety of domestic securities but also the safety of the cross-border use of collateral.

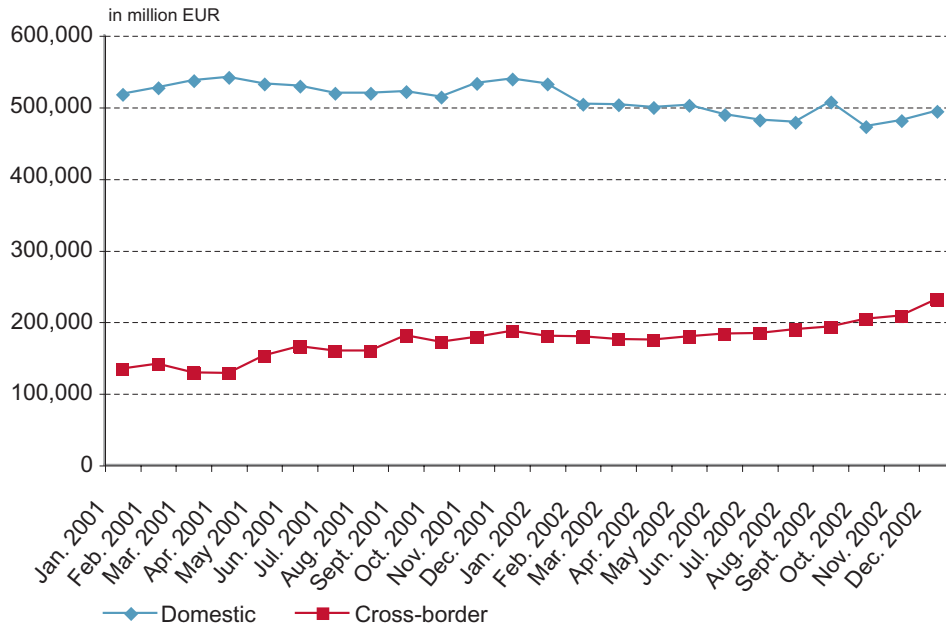
Besides using eligible domestic securities settled via the national Central Securities Depository (Clearstream Banking Luxembourg for the Luxembourg counterparties, CBL), the ESCB counterparties may receive credit from their local NCB by using collateral located in another Member State of the ESCB. Cross-border collateral can be mobilised by using either the CCBM, or links as described in 4.3.2.

Since 1999, following regular in-depth assessments, the Governing Council of the ECB has approved the use of some unilateral and / or bilateral links between different Securities Settlement Systems (SSS). These links enable counterparties to use securities held in one SSS of the EU but issued in another European country as collateral in credit operations in the ESCB. Thus, a Luxembourg bank can pledge to the BCL German securities, which were issued in Clearstream Banking Frankfurt (CBF), since the link CBL – CBF has been formally authorised by the ESCB.

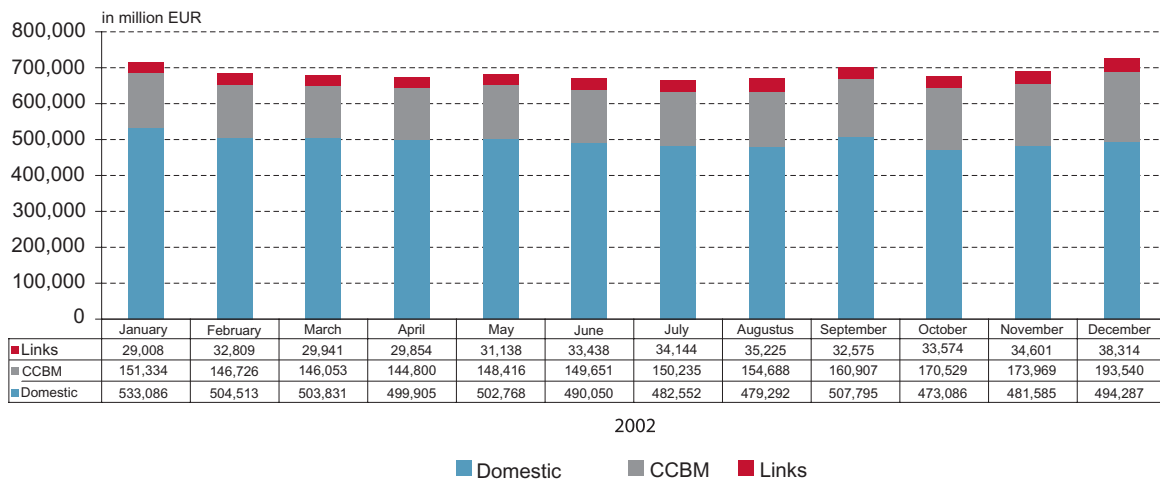
CBL has approved links with Euroclear, the National Bank of Belgium, Monte Titoli (Italy), VP (Denmark), OeKB (Austria), Euroclear Netherlands and CBF. The approval of these links enables Luxembourg counterparties to use securities issued in these systems as collateral.

There is an increase in the use of cross-border securities (securities held in a country different from the issuance country) as collateral within the euro area. This increase, although gradual, indicates the development of a single capital market (see graphic below).

GRAPH 5 VALUE OF DOMESTIC SECURITIES COMPARED TO CROSS-BORDER SECURITIES



GRAPH 6 TOTAL VALUE OF SECURITIES DEPOSITED WITH THE EUROSISTEM



4.5 Correspondent Central Bank Model (CCBM)

In the framework of the CCBM each NCB acts on behalf of the other central banks as a custodian for securities accepted by its national Central Securities Depository or by its SSS. The correspondent central bank (CCB) receives the securities in custody and the home central bank (HCB) grants the credit.

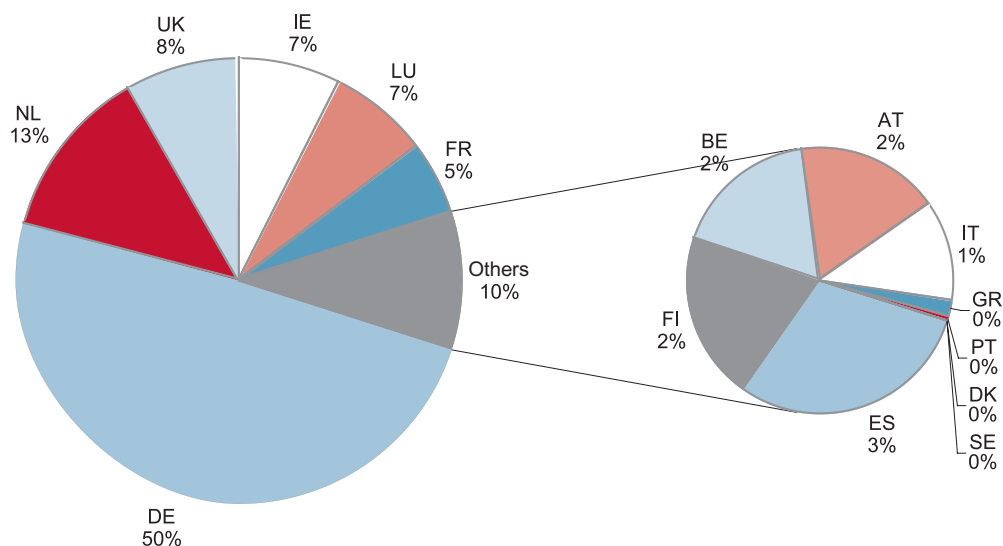
The model has been operational since the start of EMU. Experience acquired during the first years has shown that the CCBM is successful with the counterparties. Indeed, the value of securities in deposit has been steadily growing to 193.54 billion euros at the end of 2002. 26.7% of all eligible assets in the Eurosystem are held via the CCBM.

In 2002, the use of the CCBM has been very asymmetrical. The most active correspondent central banks have been Italy (26%), Luxembourg (21%), Belgium (15%) and Germany (14%).

Among the biggest users of the CCBM appeared the counterparties from Germany (50%), the Netherlands (13%), Great Britain (8%), Ireland (7%), Luxembourg (7%) and France (5%).

The cross-border use of tier 2 assets remains marginal.

GRAPH 7 HCB-2002



4.6 Night Time Link with Clearstream Banking Luxembourg

During the second half of 2002, BCL and CBL have introduced a new procedure enabling Luxembourg Banks to improve the use of their assets deposited with BCL while increasing the financial safety of their security settlements with CBL during the night processing.

This procedure called Night Time Link (NTL) consists of 2 parts:

1. CBL's client can use the assets available at BCL (securities and cash) to guarantee intraday credit which CBL grants in order to settle its securities transactions carried out during the night processing.
2. At the end of CBL's night processing, the reimbursement of overnight credit is carried out automatically through a book entry on the client's account with BCL.

BCL considers that NTL, while offering new collateralisation possibilities to the banking community, contributes to the improvement of the security of transactions. This procedure also allows the banks to centralise their treasury management.