X-pand into the Future

e u r e x *circular 167/03*

Date: Frankfurt, November 26, 2004
Recipients: All Eurex members and vendors
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Introduction of Dynamic Haircuts for Collateral Valuation

Related Eurex Circulars: 148/04

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Content may be most important for:	**Attachments:**
➲ All Departments	none

Summary:

The Executive Board of Eurex Clearing AG decided to introduce a calculation method to dynamically adapt the haircut rates of bond positions being accepted by Eurex Clearing AG as collateral. In the course of this introduction the Executive Board of Eurex Clearing AG has additionally decided to accept government bonds issued by Japan, Canada and Australia as admissible collateral pursuant to section 1.3.5 (2) of the Clearing Conditions for Eurex Clearing AG. The new calculation method and the acceptance of the additional admissible collateral will be introduced on **December 3, 2004** and will lead to a better and fairer risk assessment of the collateral haircut calculation for clearing members.

So far, Eurex Clearing AG has used a static calculation method for determining a haircut with respect to the acceptance of bond positions as collateral in the Eurex Clearing System. To better reflect a bond's individual risk characteristics, a dynamic calculation method will be introduced. This dynamic method accommodates the price sensibility of bonds as a function of a shift in the yield to maturity. In addition to the dynamic calculation method minimum haircut rates are defined for the different security types. This will not only result in a better risk assessment but also in a higher valuation of the collateral in comparison to the previously applied static haircut calculation and, consequently, in significant savings for clearing members.

At the point of introduction the additional admissible collateral denominated in the currencies AUD, JPY and CAD needs to be evaluated. Therefore we are providing you with this circular a list of the additional currency haircuts that will be applied. Please note that the currency haircuts are not deducted twice as the collateral haircuts have already been adjusted accordingly. The additional currency haircuts will become effective on **December 1, 2004**.

Introduction of Dynamic Haircuts for Collateral Valuation

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The following table shows the minimum haircut rates and the yield shift defined for each security type:

Collateral Type	MIN Haircut	Yield Shift
Bunds/Confederation Bonds & Federal State Bonds/Canton Bonds	2 %	0,8 %
Local Government Bonds & Agencies	3 %	1,0 %
Corporates & Bank Bonds & Other Bonds	8 %	3,2 %
Foreign Government Bonds (USD/GBP/DKK/NOK/SEK/AUD/CAD/JPY)	2 %	0,8 %

A yield shift of one percent for example will be defined for every security type (government bonds, bank bonds). Based upon this, the haircut is calculated in two steps:

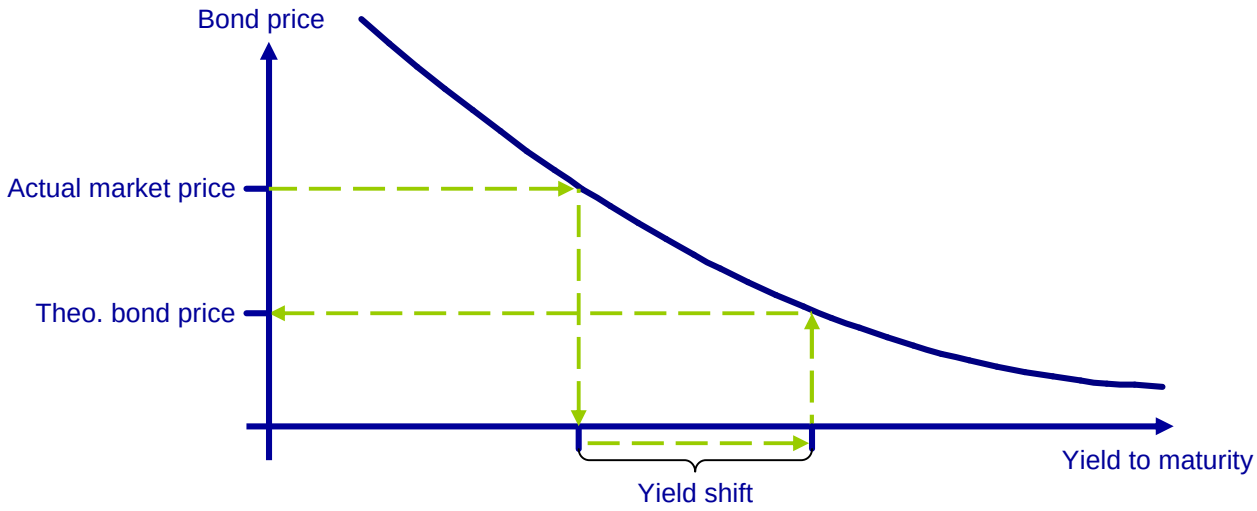
1. The actual yield of the bond is calculated based on the current market price and the yield is then shifted by using the yield shift factor.
2. A theoretical bond price is calculated by using the shifted yield.

The graphic on the following page illustrates the calculation of the haircut percentage which is calculated for each individual bond belonging to one of the security types mentioned above.

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The difference between the theoretical price and the current market price is set into relation to the market price in order to obtain a percentage. This percentage serves as the new haircut, which will be used for the valuation of all collaterals which are individually accepted by Eurex Clearing. Should the haircut calculated fall under the defined minimum haircut, the minimum rate will be used for the calculation. Compared to the currently applied static calculation method, this will lead to significantly lower haircuts.

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Overview - Cross Currency Haircuts at Eurex Clearing AG

EurexCurrency	Currency	CrossCurrencyHaircut
CHF	**AUD**	**3,00%**
EUR	**AUD**	**3,00%**
CHF	**CAD**	**2,00%**
EUR	**CAD**	**2,00%**
CHF	CHF	0,00%
EUR	CHF	1,00%
CHF	DEM	1,00%
EUR	DEM	0,00%
CHF	DKK	1,00%
EUR	DKK	1,00%
CHF	EUR	1,00%
EUR	EUR	0,00%
CHF	GBP	1,00%
EUR	GBP	2,00%
CHF	**JPY**	**2,00%**
EUR	**JPY**	**2,00%**
CHF	NOK	2,00%
EUR	NOK	2,00%
CHF	SEK	2,00%
EUR	SEK	2,00%
CHF	USD	2,00%
EUR	USD	2,00%

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