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Banco Itaú S. A.

ITAU

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Board of Governors of the Federal Reserve System
20th Street & Constitution Avenue, N. W.
Washington, DC 20551.

Re: Docket No. OP-1257
Consultation Paper on Intraday Liquidity Management and Payment System Risk Policy

Dear Ms. Johnson,

For purposes of Payment System Risk Policy, in US we are classified as *U.S. branches and agencies of Foreign Bank.* In regard to that, we do not have access to Fed Window to enter into Day Light Overdraft or Overnight Facilities because we do not have the appropriate account for that with FED. However, we are planning to do our payments by ourselves, and for that, open an account in our New York branch to access Fed Window and maybe use the FED services to do our own payments, instead of using third parties.

We believe that some of the changes proposed on the document might improve fluidity of liquidity trough the system and improve efficiency, reducing risks in the system. Please find below our responses to the questions proposed on the document.

Questions:

1. What intraday liquidity conservation strategies and technologies does your institution use (such as controlling the timing of payments and introducing queuing techniques to conserve on liquidity)?

For purposes of Payment System Risk Policy, in US we are classified as *"U.S. branches and agencies of Foreign Bank"*. Currently, we do not have access to Fed Window to enter into Day Light Overdraft or Overnight facilities because we do not have the appropriate account for that with FED. So for settlements we have to adopt strategies to face liquidity constraints, such as fraction tickets, use overdraft facilities with commercial banks, delay payment orders or in some cases anticipate them, wait until we have enough liquidity etc. In our local currency, as we access a "Fed Window equivalent", if we have liquidity available, we release the order.

How do these affect your institution's timing for sending payments?
Especially in the F/X market, some payments may be delayed in consequence of waiting for incoming liquidity. In general, in our New York Branch, we anticipate the larger orders to guarantee the limits with our Clearing Banks.
What, if any, changes are you planning with regard to intraday liquidity management?
We are planning and implementing internal policies like: limiting large tickets in the F/X and bond markets, creating rules for large payments, developing a pool of different sources of overdrafts and overnight facilities, establishing minimum cash levels according to our operational needs. One major manner that we are also planning to develop is to open an account in our New York branch to access Fed Window and maybe use the Fed services to do our payments.

2. How do the concentrated demands for intraday central bank money by private sector systems influence intraday liquidity management by depository institutions throughout the day?
Private sector systems tend to damp up liquidity until they settle transactions and release liquidity for the market. This problem is more critical when large payments are being hold into the system.
Are there significant concentrated sources of demand for intraday central bank money beyond those already mentioned in the text and how does this demand affect intraday liquidity management?
I do not see any other important source of demand for intraday central bank money than those mentioned in the text.

3. Is the concentration of payments late in the day a concern for your organization? If so, what is the nature of your concern?
Yes. Especially in transactions related to F/X markets, some settlements need a substantial amount of liquidity at the beginning of the day, but some counterparties tend to release their money late. This fact leads to a situation in which we have to be plenty of liquidity early in the morning, principally when the counterparties wait for our own payments to release our money.
Does it include operational risk from late-in-the-day payments, and has operational risk to your organization from such payments been increasing or decreasing?
Concerns include operational risk, and these risks have been increasing with the ticket size and amount of transactions.
What are the key drivers of late-in-the-day payments? How has your organization responded to the late-in-the-day concentration of payments?
Establishing operational rules for ticket sizing, planning liquidity, increasing sources of overdrafts and overnight credit facilities, both in volume and number of different sources, investing in products with some differentiation in terms of during the day schedule of investment and withdrawal, planning a schedule of the larger orders and larger volumes with our Clearings Banks.

4. For the market, operational, and PSR Policy changes discussed in this document and listed as follows, how might the timing of payments and the demand for daylight overdrafts be affected? What advantages or disadvantages do you see for these changes?

- **An intraday market to exchange liquidity between institutions that hold positive balances at the Reserve Banks and those that run negative balances.**
  I think it is very hard to establish such a market for some reasons. First, there are some operational restrictions in terms of time, there is also the problems that banks plenty of

liquidity may feel worried about lending money, even if intraday, for short of liquidity institutions. Finally, banks that are short of liquidity may not want to show to others institutions their condition.

- **A market for the early return of federal funds or other money market investments.**
  I think market is already working on that direction. We see some initiatives in which the appeal is the time schedule in terms of liquidity. Certain funds are able to receive investments or withdraws until 5 pm, and maybe later. Creating a specific market for that needs, I believe, could help institutions in the operational liquidity management, and bring a relief for late-in-the-day settlements. Institutions also do a selection of payments that should be done earlier.
- **Enhancements by private settlement systems that further economize on the use of central bank money, for example multiple settlement periods to release liquidity earlier in the day**.
  This is one of the most important initiatives, since it can improve the fluidity of liquidity through the system, avoiding puddles of liquidity in certain vehicles.
- **Liquidity saving mechanisms for the Fedwire funds transfer system.**
  These measures may improve both efficiency and reduce risks in the system, since it will allow releasing liquidity for the system.
- **Throughput requirements for the Fedwire funds transfer system.**
  Again, this measure may improve both efficiency and reduce risks, as it allows quicker settlements. Also latency, and responsiveness affect system efficiency.
- **Greater use of voluntary or required collateral to cover partially or fully daylight overdrafts in depository institution accounts at the Reserve Banks.**
  In my opinion, this may be the most effective measure, once it allows access to liquidity, bringing more liquidity to the system. It also allows settlements early in the day, at a low cost.
- **Two-tiered pricing for collateralized daylight overdrafts, with a fee charged for collateralized daylight overdrafts set lower than the rate for uncollateralized overdrafts.**
  Combined with the previous measure, this can improve efficiency for the system.
- **Time-of-day pricing of daylight overdrafts.**
  This is a fair approach to pricing for intraday liquidity. By this way, it is possible to give incentives for early-in-the-day settlements and to penalize late-in-the-day settlements, fostering fluidity, and avoiding liquidity puddles.

5. What are other possible approaches to consider to reduce delays in payments and to manage efficiently and effectively the Federal Reserve's exposure to increasing daylight overdrafts as well as depository institutions' exposure to intraday liquidity and credit risks?
Fostering private sector and governments to coordinate liquidity movements, organizing movements among different markets and countries (by extending and increasing the number of common windows between Europe and USA, so that, creating mechanisms of communications among different markets) and also creating insurances for operations localized in a free zone.

Are there other market or operational changes in the private sector that could help reduce intraday liquidity and credit risks?
By taking into account liquidity available in other currencies (cash, bonds etc) as collateral for daylight overdrafts, this may require better coordination between private sector systems, and even

build a wider legal framework, supportive for such environment. Also fostering private sector, systems and products, which allow such cross-border consideration.

6. Congress is currently considering legislation that would allow the Federal Reserve to pay interest on reserve balances held by depository institutions at the Reserve Banks. How would the payment of interest on reserves affect depository institutions' intraday liquidity management, including the demand for daylight overdrafts at the Reserve Banks? Obviously, this is positive, first because it improves the system efficiency, but also it may lead to higher levels of deposits at Federal Reserve Banks. But the level of such deposits depends on the level of interest being paid to depositors, and there is a trade off between those deposits and the amount of short-term debt placed by treasury (Bills, Notes etc)

Could the payment of interest on reserves be utilized to reduce the value or timing of daylight overdrafts?

I believe the effect of this measure may not be the most relevant, but it can be a useful way to improve efficiency and reduce risks for the system.

We appreciate the opportunity to provide comments on this consultation paper. We hope these comments and answers are helpful. If you have any questions on this letter, please contact Dino Sani at 212 486-1280 or Carlos Eduardo Lara at 55 11 5029-2534.

Sincerely,

Dino Sani Jr (General Manager – New York Branch)
Carlos Eduardo de Souza Lara (General Manager Treasury - Banco Itaú)