



EUROPEAN CENTRAL BANK
EUROSYSTEM

DG MARKET OPERATIONS

13 March 2008

Money Market Contact Group

Frankfurt, Friday 29 February 2008, 13:00 – 16:00

SUMMARY OF THE DISCUSSION

At the beginning of the meeting the Chairman mentioned that the annual review of the composition of the MMCG had resulted in three changes. Subsequently the three new members, Mr. Luc Caytan (KBL Luxembourg); Mr. Geert Wijnhoven (ING Bank); and Mr. Jan Misch (LBBW), introduced themselves briefly to the group.

1. Review of the latest developments in the repo markets

The Chairman mentioned that this item addressed two issues of the group's 2008 work programme, namely "main features of the repo markets" and "electronic trading". He added that it was the first time that an external party, namely Eurex Repo, had been invited to give a presentation at the MMCG. He stressed, however, that the ECB has, of course, a neutral stance towards the various providers of electronic trading platforms. Therefore the ECB was willing to provide a similar opportunity to other relevant platform providers in some future MMCG meetings and he asked the members of the group to make potential suggestions in this regard to the Secretary.

The two representatives from Eurex Repo presented a quick overview of the development of outstanding amounts in Eurex Repo. This was followed by an overview of the main features of their GC pooling product and some statistics about GC pooling. At the end of the presentation they provided an outlook on expected future developments.

Following the presentation there was a discussion about the strengths and weaknesses of the GC pooling product. The main strengths identified by members of the group were the feature that Eurex Repo acts as a central counterparty (which implies a 0% risk weighting for the trades) and the possibility to re-use received collateral. Moreover, the pool of accepted collateral is very wide (around 8,000 securities) and determined by the ECB's eligible asset's database – ABSs and uncovered bank bonds are, however, excluded (in the latter case because of the "close links" problem, which is difficult to solve when collateral is available for re-use). The most important limitation identified by the group was the need to have an account with the Bundesbank, which left GC pooling mainly being used by domestic German banks, with only a few international banks participating.

In the context of the discussion, there were also three remarks concerning the ECB: First, one member asked, if T2S or CCBM2 would make it possible to participate in a tool like GC pooling even without having to have an account with the Bundesbank – the Secretary of the COGESI replied that this issue was currently under investigation in the CCBM2 project (see next item). Second, another member mentioned that the SNB was using Eurex Repo for its own operations and was wondering, if the ECB was considering doing something similar in order to have a harmonised appearance to all market participants, regardless of their location. The Chairman replied that the Eurosystem was indeed currently working on a project to harmonise its IT platforms. Third, a French member informed the group that the pooling of collateral (incl. credit claims) was now also possible in France, reminding everyone that this positive development originated from an earlier initiative of the MMCG.

The discussion then turned to some more general repo market developments and in this context the Chairman asked whether someone would be interested to present the findings of the upcoming ICMA repo market survey to the group. The report will be published in March 2008 and might be quite interesting as it covers December 2007 data and should thus reveal the impact of the money market turmoil. Johan Evenepoel (Dexia) and Danielle Sindzingre (SocGen), who had already provided such a presentation in the past, volunteered to prepare again something for the next meeting.

2. Latest developments regarding the CCBM2 project

Dirk Bullmann (ECB) provided the group with an update on the latest developments as regards the CCBM2 project, mentioning that it was a very topical presentation, as the ECB had just launched the second public consultation on this project.

Dirk first presented the objectives and principles of the project before mentioning the market expectations as gathered in the first consultation round. Thereafter he mentioned some details on the current consultation process on the CCBM2 User Requirements, before elaborating on the interlinks between TARGET2, T2S and CCBM2. He finished with the currently envisaged timetable.

The following discussion revealed a number of interesting points. First, some members mentioned that the launch date of CCBM2 should be as early as possible and need not necessarily be linked to the go-live of T2S. Second, a large number of banks argued that the full benefits of this project could only be reaped, if all euro area NCBs participated. On this point Dirk clarified that no NCB would be forced to join this project, but that national users could of course try to exercise some soft pressure on “their” respective NCBs to participate. He added that so far no NCB had indicated that it was not willing to participate and that after the summer of 2008, i.e. once the detailed user requirements are clear, NCBs would be asked for a firm commitment whether they want to join the project or not. Moreover, there were also some questions about the foreseen inclusion of a contingency module which would be able to deal with non-euro collateral. The Chairman clarified that currently the Eurosystem views the possibility of accepting foreign-denominated assets as collateral as a contingency measure, which implies that in normal times this type of collateral will continue not to be eligible. Nevertheless, CCBM2 will be designed in such a flexible way that it would be able to handle foreign-denominated collateral in emergency situations or in case there should be a shift in the ECB’s stance on this topic.

At the end of this item Dirk mentioned that there would be a special ad-hoc meeting of the COGESI on 6 March, which would exclusively deal with CCBM2 issues. He offered interested members of the MMCG the possibility to be invited to similar future meetings. The Chairman asked banks to contact the Secretary in case of interest.

3. Round up on market developments since the previous meeting

In his presentation the Secretary first recalled the situation that prevailed at the time of the last meeting, namely the significant concerns as regards the upcoming turn of the year. He reminded members of the various measures taken by the ECB in order to manage this difficult period as smoothly as possible. Thereafter Ralph elaborated on the substantial improvement that had taken place in the markets: the return of stability as regards short-term money market rates; the significant decline in 3m Euribor-OIS spreads and the noticeable decline in tender spreads. Afterwards he stressed, however, that some caution still seemed to be warranted as there was no full normalisation yet given the ongoing concerns in the credit markets and the fact that longer-term deposit-OIS spreads as well as forward spreads remained wide or even increased recently.

Following Ralph’s presentation, Isabel von Köppen-Mertes (ECB) presented a few slides on the use of collateral in ECB operations. She first recalled the positive performance of the ECB’s collateral framework during the turmoil and then showed some charts on the development of (i) aggregate amounts of unused collateral, (ii) eligible collateral by asset type, and (iii) types of collateral held with the Eurosystem. According to Isabel it appeared that while the financial market turmoil had reinforced already existing trends in the use of collateral, the time series did not seem to reveal major breaks. The final data for 2007 will be included in the ECB’s annual report, which will be published in April 2008.

The first part of the subsequent discussion centred on banks' funding possibilities. There was broad agreement that funding had become much more challenging. There was a feeling that the banking sector was in a general need for long-term funding, not least in order to be able to comply with regulatory liquidity ratios. Some banks argued, however, that raising longer-term funds was still possible, provided the respective bank was willing to pay the higher prices, and that there had been several examples of successful issuance also over the recent weeks and months.

The discussion on the ECB's EUR liquidity management, both before the turn of the year and also since the start of 2008, was relatively limited, as banks generally agreed that the ECB had taken a proactive stance and thus contributed to a smooth year-end and to a further improvement of the situation at the short end of the money market curve. Banks also welcomed the ECB's decision to roll-over the supplementary LTROs again, and were generally of the view that this should continue to be done for the time being. In fact some members said that the continued supply of significant amounts of 3-month funds might be one of the reasons why the deposit-OIS spreads have remained reasonably stable in EUR recently, while they re-widened in USD and GBP.

There was a somewhat longer discussion on the ECB's participation in the Federal Reserve's Term Auction Facility (TAF). While this participation was generally seen as having been very helpful for the banks, there was some surprise that the participation in these auctions was relatively modest, in particular in the roll-over operations conducted in January. The Chairman concurred with this assessment, stressing however that the rather low participation could be viewed as a positive sign, suggesting that the need for USD funds was not overly dramatic. A few members mentioned that the fact that banks did not know the allotment rate in advance and did not have the chance to impact this rate with their bidding behaviour might have contributed to this observed outcome. While there was generally a lot of understanding for the ECB's decision to suspend its participation in the TAF auctions, there was quite some criticism about the way this suspension had been communicated to the market. Still on the TAF, several members reported a slight re-worsening of the USD funding situation and suggested the ECB to be prepared to re-activate its participation in the TAF auctions should this recent trend continue further over the coming weeks.

Finally, there was a short debate about the upcoming end of quarter and some members said that they could imagine a re-worsening of the liquidity conditions in the money market in the second half of March. This view was supported, according to some members, by the continued stress in the credit markets and the fact that the Easter holidays are already in March this year.

4. Other items

- The Chairman introduced Orazio Mastroeni (ECB) as the new Secretary of the Operations Managers Group. Orazio presented a brief summary of the last OMG meeting, mentioning among others the group's assessment of the operational impacts of the financial market turmoil.
- Arturo Diez Caballero (ECB) presented the timetable for the upcoming Money Market Study and informed the members about some small changes in the questionnaire, which will be sent to the banks at the end of March.
- On behalf of Achim Krämer, the Chairman of the ACI Derivatives working group, the Secretary presented the latest developments as regards the Eonia swap market: The fixing time for the Eonia Swap Index will be moved from 16:30 to 11:00 as of 3 March 2008 and the FRA product based on Eonia swaps will be launched one week thereafter, i.e. on 10 March 2008.
- Finally the Chairman mentioned that the next meeting will take place on Tuesday, 27 May 2008 in Frankfurt; 13:00-16.00. Potential agenda items for this meeting are the regular review of recent market developments; a review of the results of the upcoming ICMA repo survey; and possibly a presentation on the various liquidity regulations in the EU.