EUROPEAN CENTRAL BANK

EUROSYSTEM

DG MARKET OPERATIONS

12 May 2020

ECB Money Market Contact Group (MMCG)

Monday, 4 May 2020, 11:00-12:00 CET

(meeting held by teleconference)

Summary of the discussion

1. Money market conditions

The Money Market Contact Group noted that movements in EURIBOR rates were being driven largely by arbitrage opportunities in the foreign exchange (FX) swap market and low levels of trading activity. According to MMCG members, EURIBOR rates had moved in line with conditions in the US dollar funding market. The increase in the three-month LIBOR had created an incentive to borrow funds in the euro unsecured market and swap them into US dollars, thus resulting in upward pressure on the three-month EURIBOR. In the same vein, the MMCG also attributed the recent decline in EURIBOR rates to the relief experienced in the US dollar LIBOR funding market, which had reduced arbitrage opportunities in the FX swap market. Some MMCG members voiced concerns about the representativeness of the EURIBOR in terms of reflecting the funding costs of euro area banks, given the low levels of market liquidity at longer horizons. The EURIBOR's hybrid methodology requires panel banks to rely on other market rates and expert judgement when no eligible transactions are conducted, with expert judgement often drawing on market prices in the FX swap market and estimates of credit risk based on internal models.

The MMCG considered that the 7-day and 84-day US dollar operations provided by the ECB both remained necessary as an effective backstop for the US dollar funding market, despite declining usage. The swap network established by major central banks – specifically, the ECB's swap line with the Federal Reserve providing US dollar funding to euro area banks – was regarded by MMCG members as the main contributor to the easing of US dollar funding pressures, especially in the offshore US dollar market. MMCG members were strongly in favour of continuing with those operations, as the improvements in funding markets were still tentative and an effective backstop was still needed.

2. Feedback on the ECB's recent decisions on 7 and 28 April 2020

The MMCG welcomed the latest enhancements to the pricing and modalities of TLTRO III operations. As a result of those changes, MMCG members anticipated a very high level of take-up in the forthcoming TLTRO III operation in June, with banks now expected to make full use of their bid limits. While the Governing Council had left official interest rates unchanged, some MMCG members were of the view that the reduction in the price of the TLTROs was broadly equivalent to a rate cut of 25 basis points. MMCG members also welcomed the ECB's decision to change the start date of the lending performance period from 1 April to 1 March 2020, considering that banks had already satisfied high levels of demand for corporate credit in March.

MMCG members regarded the new pandemic emergency longer-term refinancing operations (PELTROs) as an effective backstop. Despite them being priced less attractively than TLTRO III operations, MMCG members appreciated the value of PELTROs as an effective backstop for term funding and a way of helping banks for which TLTROs may not be suitable. Most MMCG members expected their banks to participate more actively in TLTRO III operations than in PELTROs. Unlike the bridge LTROs, the PELTROs offer term funding, avoiding cliff effects thanks to their digressive maturities.

Given the high levels of take-up expected for TLTRO III operations, some MMCG members were concerned about a potential shortage of high-quality liquid assets (HQLAs) for liquidity management or regulatory purposes. The MMCG discussed the effect that a large take-up would have on the availability of HQLAs. Some MMCG members felt that the eligibility of credit claims and additional credit claims (ACCs) under the ECB's collateral framework was important in order to allow illiquid assets to be used as collateral in the June TLTRO and free up space on banks' balance sheets for additional lending. While credit claims are accepted by all national central banks (NCBs), not all NCBs have yet established a framework governing the acceptance of ACCs, which are subject to larger haircuts since they do not fulfil all of the standard criteria applicable under the general collateral framework. Recent collateral easing measures adopted by the ECB have facilitated the eligibility of both credit claims and ACCs. For ACCs with COVID-19–related public guarantees, requirements relating to internal ratings and loan-level reporting have been eased. In jurisdictions where an ACC framework has been established, banks are expected to save their HQLAs for liquidity management via repo operations and for compliance with regulatory ratios (such as the liquidity coverage ratio), whereas in jurisdictions without an ACC framework, banks may need to use a large percentage of those assets as collateral in TLTRO III operations. The establishment of ACC frameworks is subject to decentralised decision-making by the NCBs of the various countries. As a result, MMCG members said that there was an urgent need to establish ACC frameworks in those countries where they did not yet exist, in order to foster transparency and a level playing field across the euro area.

The MMCG also discussed the effect that a large take-up would have on other regulatory ratios (such as the leverage ratio) and risk-weighted assets. Some MMCG members thought that the flexibility announced by ECB Banking Supervision would be enough to alleviate potential constraints as regards compliance with the leverage ratio or capital ratios. However, some other MMCG members felt that the exclusion of central bank reserves from the calculation of the leverage ratio should be formalised by regulators in order to ensure that banks participated fully in TLTRO III operations and lent central bank funds to the private sector.

List of participants

Money Market Contact Group meeting

Participant's organisation	**Name of participant**
Bank of Ireland	Mr David Tilson
Barclays Bank	Mr Bineet Shah
Bayerische Landesbank	Mr Harald Endres
BBVA	Mr Miguel Monzon
Belfius Bank & Insurance	Mr Werner Driscart
BNP Paribas	Mr Patrick Chauvet
BPCE/Natixis	Mr Olivier Hubert
Caixabank	Mr Xavier Combis Comas
Caixa Geral de Depósitos	Mr António Paiva
Commerzbank	Mr Andreas Biewald
Coöperatieve Rabobank U.A.	Mr Frank Beset
Deutsche Bank	Mr Jürgen Sklarczyk
DZ Bank	Mr Michael Schneider
Erste Group Bank	Mr René Brunner
HSBC	Mr Harry Gauvin
ING	Mr Jaap Kes
Intesa Sanpaolo	Ms Maria Cristina Lege
LBBW	Mr Jan Misch
Nordea	Ms Jaana Sulin
Société Générale	Ms Ileana Pietraru
UniCredit Bank	Mr Harald Bänsch
European Central Bank	Ms Cornelia Holthausen (Chair)
European Central Bank	Ms Maria Encio (Secretary)
European Central Bank	Mr Helmut Wacket