



ECB Money Market Contact Group

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Rabobank

TLTRO-III assessment, expectations and its future.



1. TLTRO-III Modalities, critical changes.
2. March 2021 TLTRO-III take up.
3. Two types of TLTRO-III users.
4. Expectations for TLTRO-III.8-10 operations.
5. TLTRO-III conclusions.
6. For discussion: *TLTRO-IV*.

1. TLTRO-III modalities, critical changes.



TLTRO-III.1-7

- These can benefit from lower interest rate by exceeding thresholds in one or more of the 3 lending assessment criteria:
 - Initial Criterion: 1.15% from Apr'19-Mrch '21
 - Special Criterion: 0% from Mrch'20 – Mrch'21
 - Additional Special Criterion: 0% from Oct'20 – Dec '21
- Partly explains the high take up, March (nr.7) was the last possibility to have the benefit based on 3 lending criteria.

TLTRO-III.8-10

- These can only benefit from lower interest by exceeding the threshold of the additional special lending criterion.
 - Previous criteria cannot be applied as they have expired at the time of participation.

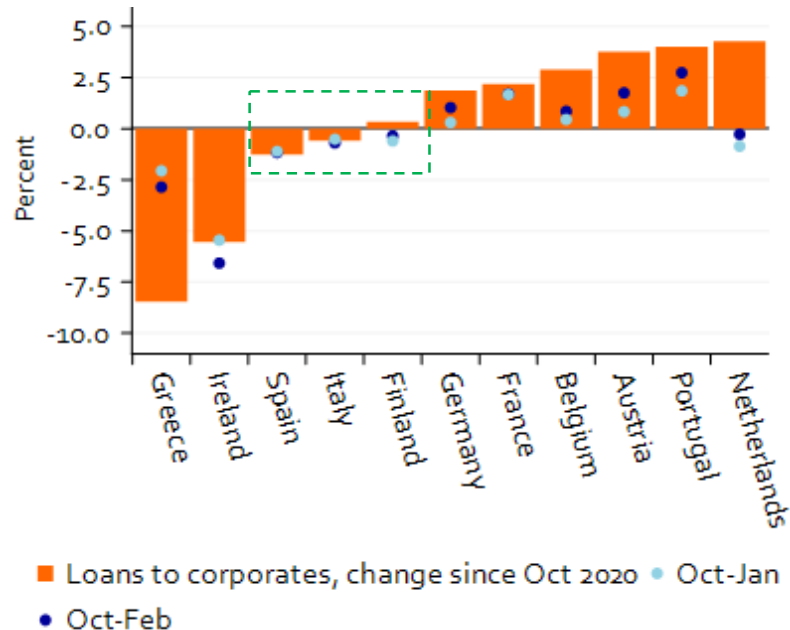
2. March take-up surprised everyone.



Take up TLTRO-III.7

- March demand (EUR 330bn) was much higher than expected (EUR ~50-200bn).
- Critical changes support this.
- Banks expectations of a surge in loan demand when the economy reopens in combination of extension of lower interest rate from Jun '21 – Jun '22.
- Yet demand remains relatively limited so far.
- Many banks have closed in on their new benchmarks, but in some key countries gaps remain.

Evolution of loans to corporates

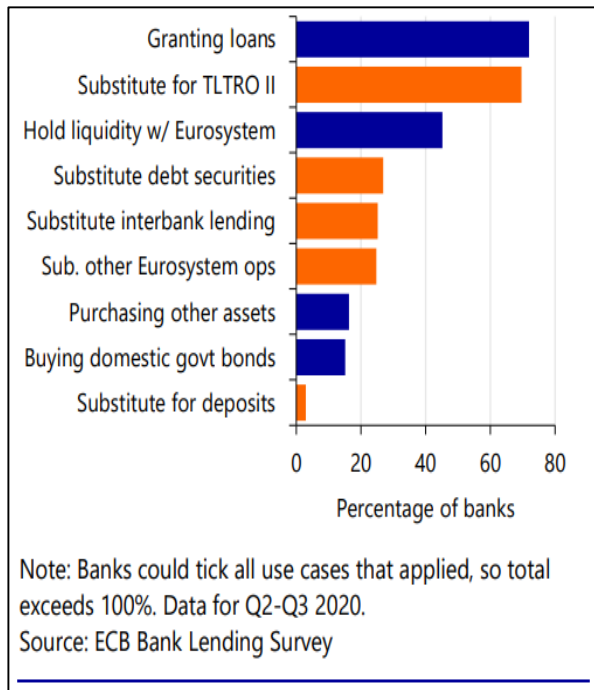


3. Two types of TLTRO-III users.



A. Funding/structural:

- Substitute for market-based funding.
- Included this ECB tool into their funding mix.
- Price insensitive (as long as it is comparable/better than market).
- Bulk seen in early-TLTRO-III's.
- Likely to keep the funds beyond the discount periods.



B. Opportunistic:

- Using TLTRO-III as carry.
- Price sensitive, keeping the funds is a contingent on the discount (to a lesser extent developments in market rates, relative to base TLTRO-III rate).
- Bulk seen in TLTRO-IIIs post-discount announce (4 and 7).
- Large III.7 take-up likely driven by expectations that benchmark will be met.
- Likely to repay (partially) after discount periods.

4. Expectations for TLTRO-III.8/9/10 operations.



Benchmarks and discounts mostly relevant for the opportunistic group:

- Banks replacing TLTRO for market based funding (**A. group**) assumed to be less sensitive for the extra discount, as base TLTRO-III rate already attractive for them relative to market rates.
- December '21 (III.10) may see a bulky allotment, only in gross terms as banks switch out of earlier TLTRO-III's to extend funding by up to 2 years .
 - Banks can make a very good assessment in December of the eligible loans for the period oct-20 dec-21 which are applicable for the discount on III.10.
- This switch should give an indication of how sticky TLTRO-III is post-discount, (**B. group**) will likely be (partly) out.
- Upside risk to expectations:
 - Rising market-based rates on back of market environment.

5. TLTRO-III conclusions.



- Introduction is a success, reliance on the TLTRO-III is high.
 - Important to separate 'funding' from 'opportunistic' motive.
- Meeting lending benchmark.
 - European wide competition leads to:
 - Lower margin/higher (credit) risk acceptance.
- Reduced reliance of bank issuance as TLTRO-III becomes part of the funding mix.
 - Creates markets anomalies:
 - (money market) investors forced to look at alternative investment opportunities.
 - EURIBOR methodology, level 3 contribution high.
 - Certain (longer, >10yrs) tenors are targeted when banks issue.
- Dependency imposes cliff risk.
 - Concentrated substitution TLTRO-III funds with market-based funding on large scale could result in higher funding costs.

6. For discussion: TLTRO-IV



A. Funding/structural:

- Longer-term operations to remain a regular ECB instrument from banks perspective, in order to avoid/manage liquidity cliff effects?
 - Long, flexible maturity to allow a long-term backstop, while banks can switch to market-based at opportune moments.
- Discount-scheme will either disappear, or first make way for a new incentive post-pandemic?

B. Opportunistic:

- Opportunistic TLTRO users will be disincentivised when DFR and hard to reprice retail deposits return to normal levels.
- Supervisory angle: not extending leverage ratio exemption for CB deposits, will push out the banks that have constraints in this metric?

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