



EUROPEAN CENTRAL BANK

EUROSYSTEM

DG MARKET OPERATIONS

03 March 2023

ECB Money Market Contact Group (MMCG)

Thursday, 2 March 2023, 13:30-17:30 CET

Hybrid meeting: in-person with the option of remote login

Summary of the discussion

ECB Executive Board member **Isabel Schnabel** addressed the MMCG with a speech on [“Quantitative tightening: rationale and market impact”](#).

Members discussed developments in euro money markets since the last MMCG meeting, noting that interest rate expectations had risen, in particular in the days preceding the MMCG meeting, while interest rate volatility had remained high. In that respect, uncertainty about the future path of interest rates had induced investors to invest in very short maturities. Moreover, members reported an influx of additional funds into the short-term deposit market from investors who had previously been less active in this segment. As these short-term placements had little regulatory value for banks, pricing remained geared towards disincentivising them. This was also reflected in the relatively slow adjustment of short-term (up to three months) unsecured interest rates to the rate hiking cycle when compared to overnight indexed swaps (OIS). Some members felt that the slower adjustment was likely to persist, as the factors underpinning it were seen as unlikely to reverse in the near future. On the other hand, some members highlighted that forward rates suggested that the slower adjustment would eventually dissipate and saw this as reflecting the expectation that future targeted longer-term refinancing operation (TLTRO) repayments would lead banks to step up their issuance of unsecured money market liabilities (e.g. in the form of commercial paper), thereby imparting some upward pressure on their pricing. Some members also commented on the persistent gradual widening of the deposit facility rate (DFR) to euro short-term rate (€STR) spread and the challenges this was posing for asset managers.

The situation in the euro repo market was viewed as having significantly improved in response to Eurosystem and government action. Views, however, diverged as to whether

collateral scarcity had been largely addressed and would therefore be largely confined to balance sheet reporting dates, or whether it could resurface on a more persistent basis. Members supporting the latter view motivated it by the expectation that domestic and foreign governments might invest in repo markets owing to the change in Eurosystem deposit remuneration. These members also noted the risk that the remuneration might be further adjusted downwards at a later stage and that government deposit holdings would be sensitive to such changes. Uncertainties were noted in relation to the demand for high-quality liquid assets (HQLA), which would be determined by, among other factors, the slope of the yield curve and the cost of holding HQLA, the amount of government spending and issuance, and the size of governments' liquidity buffers.

The future size of the Eurosystem's balance sheet, the set of tools for liquidity absorption and the (potentially green) collateral framework were seen as the most important aspects that the ECB may need to consider in the review of its operational framework for steering short-term rates. Members were split regarding preferences for either a floor or a corridor system for steering short-term interest rates. Those favouring a floor system stressed the lower volatility of rates and the simple and more stable liquidity management that it entails. Those favouring a corridor system stressed the benefits of higher intermediation activity of banks in such a system. Members cautioned on the difficulty to accurately estimate the amount of excess liquidity required to anchor short-term rates to the policy rate, while also pointing to the collateral scarcity that may be associated with a large central bank balance sheet. In terms of tools for liquidity absorption, ECB debt certificates were seen by some members as a more promising alternative in the Eurosystem context than a reverse repo facility (such as used in the United States). Moreover, debt certificates could be used as collateral in the repo market, helping to alleviate scarcity.

Regarding banks' funding strategies in the context of monetary policy normalisation, members noted the strong issuance of and continued demand for covered bonds, which might also be used to replace maturing TLTRO funding. Overall, the replacement of TLTRO funding was not considered particularly problematic for most banks, while the use of specific funding instruments might vary. Moreover, some members noted a deterioration in loan-to-deposit ratios but others expected loan growth to continue to decelerate on the back of lower demand, thereby providing relief. Overall, members did not see broad-based funding challenges as constraining bank lending capacity. Fulfilment of the minimum requirement for own funds and eligible liabilities (MREL) was largely seen as comfortable, although it was also highlighted that a possible deterioration in credit quality in the future, through an increase in banks' risk-weighted assets, could result in a need for further issuance of eligible liabilities.

List of participants

Participant's organisation

Name of participant

European Central Bank	Ms Isabel Schnabel	EB Member
European Central Bank	Mr Thomas Vlassopoulos	Chairperson
European Central Bank	Mr Tobias Blattner	Counsellor
European Central Bank	Mr Johannes Gräß	Counsellor
European Central Bank	Mr Christian Lizarazo	Secretary
European Central Bank	Mr Helmut Wacket	
European Central Bank	Ms Julija Jakovicka	
European Central Bank	Ms Pamina Karl	
European Central Bank	Mr Ole Gregarek	

Amundi Asset Management	Ms Cécile Mouton	
Banco Santander	Mr Luis Barrigon Rodriguez	
Belfius Bank	Mr Werner Driscart	
BNP PARIBAS	Mr Patrick Chauvet	
BPCE/Natixis	Mr Olivier Hubert	
CaixaBank	Mr Xavier Combis	
Commerzbank AG	Mr Andreas Biewald	
Erste Bank	Mr René Brunner	
Eurex Clearing AG	Mr Frank Odendall	
INTESA SANPAOLO SPA	Ms Maria Cristina Lege	
JPMorgan Asset Management	Ms Olivia Maguire	
Rabobank	Mr Eric di Scotto-Rinaldi	
Société Générale	Ms Ileana Pietraru	

Via Webex

Barclays	Mr Bineet Shah	
Caixa Geral de Depósitos	Ms Maria João Carioca	
Deutsche Bank AG	Mr Juergen Sklarczyk	
DZ Bank AG	Mr Oliver Deutscher	
HSBC CE	Mr Harry-David Gauvin	
ING Bank	Mr Leif Domeyer	