EUROPEAN CENTRAL BANK

EUROSYSTEM

DG MARKET OPERATIONS

26 June 2023

ECB Money Market Contact Group

Wednesday, 21 June 2023, 14:00-16:30 CET, remote meeting

Summary of discussion[1]

The majority of MMCG members expected the ECB to reach a terminal deposit facility rate of 4.0% in September 2023, in line with market pricing. Views on the timing of a potential first ECB rate cut were more varied. Expectations for the policy rate path have been revised upwards since the June 2023 Governing Council meeting, with the risks skewed slightly to the upside. Expectations of a first ECB rate cut fell into two clear groups, with member expectations concentrated in either June 2024 or not until 2025 or later (see below). Members did not anticipate a new liquidity-providing facility being announced after TLTRO III matures.

Members perceived banks as being well prepared for the upcoming TLTRO III repayments, using a variety of replacement options. Excess liquidity holdings were expected to cover a large share of the repayments, although this would reduce banks' liquidity ratios. These were currently still well in excess of required levels, but also closely scrutinised by a wide range of stakeholders, including supervisors, investors, rating agencies and depositors. Some members mentioned that, in the wake of the banking stress seen in March, the possibility held-to-collect assets might no longer be counted as high-quality liquid assets (HQLA) was creating uncertainty and tilting banks' preferences towards holding central bank reserves to support their liquidity metrics.

Deposits are on a downward trend as depositors pursue higher-yielding savings opportunities and bank loans get repaid in some jurisdictions. The decline witnessed in March 2023 was reversed in April in most countries; depositors elsewhere too were reported to be shifting to higher yielding government securities in particular. Members also mentioned a shift from sight to term deposits, due to the better remuneration of the latter.

Members noted that bank funding markets had recovered remarkably well from the banking stress seen in March and demand for term investments had picked up. Volumes of bank bond issuance were reported to be back to pre-March levels, even though the spread between the cost of issuance for financials and non-financials remained wider. Members reported solid demand for bank bonds, not least due to the attractive remuneration. Issuance

[1] Disclaimer: The views expressed in this summary are those of the MMCG members and do not necessarily reflect those of the ECB.

of short-term securities such as commercial paper had also increased, mainly in longer tenors, as uncertainty over the future path for ECB policy rates had to some extent receded. However, members noted that funding availability in the European Commercial Paper market remained lower compared to before the March events.

Repo markets were functioning well and liquidity conditions were good; members had diverging views on the outlook for repo rates. Some expected a degree of upward pressure due to renewed funding needs after the TLTRO III repayments, at least in some markets, while others anticipated no material impact. Trading volumes in term repos were expected to grow further. The new remuneration of non-monetary policy deposits since 1 May 2023 had led to some of these deposits flowing into the repo market, which seems to be the preferred outlet, but these had been absorbed comfortably. Some members expressed expectations for a further reduction of these deposits, possibly on the back of a lower remuneration, without causing disruptions in repo markets.

Members expected some banks to use the ECB's standard refinancing operations (MRO/LTRO) going forward, mainly small ones. The current pricing of the MRO and LTRO was seen by some as disincentivizing the use of these operations. The MMCG Chair recalled the President's statement at the June press conference that standard refinancing operations such as the MRO and the LTRO were available to be used.

Members discussed the limited trading activity in the unsecured interbank market, concluding that the prospects for a revival in this segment were very limited. It was perceived as illiquid and used mainly for relationship management purposes. Liquidity tended to deteriorate further during periods of market stress. Regulatory costs, especially the calculation of risk-weighted assets, but also internal credit and counterparty limits, acted as a disincentive to unsecured lending. The result was underdeveloped market infrastructure for unsecured interbank lending: members reported that only a few of such lines were still in place and platforms for interbank unsecured trading were less developed than the infrastructure in other market segments. Members expected that digitalisation and innovation, including distributed ledger technology, would further support secured trading by making real-time collateral management more efficient. Members discussed several potential initiatives that might support the revival of the unsecured interbank market, without reaching any definite conclusion.

Members expected the premium for offshore US dollar funding to decline further for both shorter and longer tenors, reflecting the resolution of the US debt ceiling and reduced uncertainty over the Federal Reserve's policy rate path. Short-term US dollar funding costs for foreign banks had quickly and largely normalised after the banking stress seen in March. The pricing for longer maturities, however, declined more sluggishly and was not back to levels seen before the March events yet, partly because of the uncertainty over the US debt ceiling until a few weeks ago. The large T-bill issuance by the US Treasury was mainly expected to further reduce use of the Fed's overnight reverse repo (ON RRP). This would have only limited impact on bank reserves and therefore not create any funding tensions for US or euro area banks. T-bills were perceived as an attractive investment for MMFs, especially once rate cuts are largely priced into the yield curve, which would reduce use of ON RRP by MMFs. However, even if banks absorbed some of the T-bill issuance, they would most likely lend a part of these securities back to MMFs, again driving a decline in use of ON RRP.

75% of MMCG members expect a terminal DFR of 4.0%, to be reached in September, in line with market pricing

At which level do you expect the ECB to reach its peak deposit facility rate in this hiking cycle?

3.5%	3.75%	4.0%	4.25%	4.5% or higher
0	1	13	2	1

At which Governing Council meeting do you expect the ECB to reach this peak?

June 2023	July 2023	September 2023	October 2023	December 2023	January 2024	March 2024 or later
0	3	8	2	2	2	0

Source: 17 MMCG members, conducted 19-20 June 2023

More diverse views on the timing of a first rate cut after completing hiking cycle, inflation remains the main driver

When do you expect the ECB to announce a first deposit facility rate cut after completing the hiking cycle?

January 2024	March 2024	April 2024	June 2024	July 2024	September 2024	October 2024	December 2024	2025 or later
0	2	0	5	1	2	1	2	4

Sources: 17 MMCG members, conducted 19-20 June 2023

Which factors do you consider most relevant for the path of policy rates going forward?

systemic crisis
reassure creditbility
economic growth
monetary transmission
employment rate in europe
energy prices
federal reserve
credit crunch
growth outlook
services
inflation
lending conditions
wage setting
gdp ea
employment
fed
core inflation
wages
recession
pmi
growth
eurusd
excess liquidity
inflation expectations
exchange rate
financial stability

Participant’s institution	Name of participant	
Banco Santander	Luis Barrigon Rodriguez	
Barclays	Bineet Shah	
Belfius Bank	Werner Driscart	
BNP Paribas	Patrick Chauvet	
BPCE/Natixis	Olivier Hubert	
Caixabank	Xavier Combis	
Commerzbank	Andreas Biewald	
Coöperatieve Rabobank	Eric Scotto di Rinaldi	
Deutsche Bank	Jürgen Sklarczyk	
DZ Bank	Oliver Deutscher	
Erste Bank	René Brunner	
EUREX	Frank Odendall	
HSBC Continental Europe	Harry-David Gauvin	
ING Bank	Jaap Kes	
Intesa Sanpaolo	Maria Cristina Lege	
JP Morgan Asset Management	Olivia Maguire	
Société Générale	Ileana Pietraru	
Unicredit	Harald Bänsch	
European Central Bank	Thomas Vlassopoulos	Chair
European Central Bank	Pamina Karl	Secretary
European Central Bank	Helmut Wacket	
European Central Bank	Julija Jakovicka	
European Central Bank	Sofia Delgado	