Summary of the discussion

1. Review of the latest market developments and other topics of relevance.

Patrick Chauvet presented the main developments in the market since the last meeting, noting a number of positive developments as reflected both in the on-going tightening of credit spreads across markets and in declining volatility, which was further reinforced by the ECB Governing Council’s decisions of 5 June. Although general market volatility continued to decline to new lows, short-term euro money market rates exhibited higher volatility over the past maintenance periods. This was attributed to the volatility of autonomous factors, to the bidding behaviour of counterparties in the ECB’s liquidity-providing operations, which seemed to be driven by past liquidity developments and market interest rate developments, and to the unwillingness of some banks to use central bank operations as a liquidity management tool. Although the volatility of the EONIA has increased, it was generally not perceived to be a major concern and was seen as moderate in absolute terms. It was also noted that the repo market showed higher sensitivity to changes in liquidity conditions than the unsecured market, as repos remained the main channel of liquidity flows across core and non-core countries, and thus reacted more markedly to domestic liquidity shocks, e.g. domestic tax payments. Furthermore, internal stress scenarios that are applied in banks require repo desks to be funded independently, which could result in more strained repo markets and a greater divergence from unsecured money market rates.

With regard to the package of measures announced by the ECB Governing Council on 5 June, the negative deposit facility rate had facilitated a search for a positive yield and, reportedly, a more efficient allocation of excess liquidity internally within banks. Negative rates had already been observed in short-term repo markets for higher-quality collateral. Furthermore, as cash investors were trying to move into longer maturities, some MMCG members expected repo rates for such collateral to converge to zero for maturities of up to one year. Counterparties from non-core countries also reported tighter repo market spreads and higher interest from non-bank investors. However, it was considered to be too early to assess the full impact of the measures on the money market rates and on the level of excess liquidity. Similarly, the impact of negative rates on other investors, e.g. asset managers and corporates, still had to be assessed.

With regard to the targeted longer term refinancing operations (TLTROs), several MMCG members urged the ECB to release technical details of the operations soon, since those details would be an important factor in banks’ decisions to take part or not. Furthermore, some MMCG members pointed to the still prevailing negative perceptions of rating agencies and analysts with regard to central bank refinancing and urged the
ECB to communicate to the market that participation in central bank operations in general was an intrinsic part of the ECB’s monetary policy implementation, which operates with a liquidity deficit.

2. **Internal organisation of liquidity management between the treasury and repo desks in banks – MMCG survey**

Several MMCG members presented their internal organisational set-up for liquidity management and reflected upon the main findings of the MMCG survey on banks’ internal structures and their possible impact on money market developments. The survey revealed a very heterogeneous nature of internal set-ups across the MMCG members’ organisations, reflecting diversity in terms of business, size and internal considerations. Despite significant differences, the survey showed a wide use of the repo market by banks’ treasury functions, along with a broad range of other money market instruments, independent of the chosen set-up. Similarly, the ring-fencing of liquidity reserves and a segregation of mandates and collateral pools were considered important factors. Banks’ Treasuries had primary responsibility for the execution of liquidity management and administering liquidity buffers, and together with ALM and risk management functions they played an important role in governance and liquidity management policy issues. Furthermore, Treasuries seemed to be the sole point of access to the Eurosystem’s refinancing operations. Noteworthy for the majority of the MMCG members was that decisions to participate in central bank operations were seen as strategic, and were thus taken at the level of senior management. Finally, regulatory requirements were also a major driver of the internal organisation of liquidity management in banks, and of their participation in the repo market. In particular, some MMCG members reported that legal requirements to separate trading activities within a bank could lead towards a greater separation of treasury and repo desks. Going forward, the majority of the MMCG members, independently of their organisational set-up, expected a greater participation of banks’ treasury functions in the repo market and closer cooperation between the treasury and repo desks for collateral management purposes.

3. **Market participants’ views on the proposal for an EU regulation on reporting and the transparency of secured financing transactions**

Harald Endres presented a market practitioner’s view of the proposed EU regulation on reporting and transparency of secured financing transactions, and its potential impact on the repo money market.

MMCG members expressed concerns about particular aspects of this regulatory initiative. First, the reporting burden with respect to short-term repo trades and the re-use of collateral was perceived as too heavy, was expected to reduce market activity and, in particular, to deter smaller market players (e.g. smaller savings banks and corporates) from using the repo market. Savings banks might prefer instead to resort to central bank operations in order to avoid the reporting burden. Second, terms of re-hypothecation and re-use in the EU proposal should be brought into line with the recommendations of the Financial Stability Board (FSB). Some members mentioned that re-use was an intrinsic feature of repos due to the transfer of legal ownership, which added a layer of protection for the lender of cash.

In general terms, some MMCG members remarked that the EU proposal and the FSB recommendations on this issue should aim at limiting the risk of shadow banking and should, hence, be designed to target those transactions instead of the overall repo market. Shadow banking repo transactions tend to be medium to long-term in character, often involving special purpose vehicles, whereas repos used for liquidity management in banks were usually short-term business and would thus be hit mostly by the reporting requirements.
4. Other business:

a. Update on money market reference rates and the ongoing reform process

Luis Soutullo provided an update on an on-going market initiative on developing a new repo market benchmark. The number of banks contributing to the Eurepo® had declined to a minimum, risking a discontinuation of the index. In a survey conducted by Euribor/EBF in 2013, the respondents had confirmed that the index was not used, but had nevertheless expressed a need for a repo benchmark. Currently, market initiatives had been launched to discuss a number of options and parameters with regard to a possible design on an alternative index. MMCG members reacted positively to the idea to use CCP data for a new benchmark, as it will remove the reporting burden from market participants. The ECB suggested that the choice of methodology be determined by the market’s needs and by the possible use of a new index (e.g. for derivatives contracts, internal transfer pricing, hedging liquidity buffers or hedging specific positions in government bonds) and encouraged a thorough analysis of different options and needs based on real transaction data.

Roberto Schiavi informed the MMCG about the forthcoming FSB report on reforms of interest rate benchmarks and about the discussions at the Euribor+ stakeholder meeting on 6 June. Euribor-EBF was currently in the process of collecting feedback from various parties such as contributors, consumer protection bodies and the derivatives community on the definition, production and transition issues.

b. Feedback from the MMCG and BMCG survey on the draft EU regulation on banks’ structural measures

The MMCG members received an anonymised summary of the market feedback collected from among MMCG and BMCG members on the draft EU regulation on banks’ structural measures. The ECB gratefully acknowledged a high level of response on the part of the contact groups’ members.

On a separate topic, charts with the data of the MMCG’s quarterly survey on money market activity covering the first quarter of 2014 were distributed to the MMCG members.

c. Planning of the next meeting

The next MMCG meeting will take place on 9 September 2014 in Frankfurt, starting at 3 p.m., and will be followed by the annual MMCG dinner.