



EUROPEAN CENTRAL BANK  
EUROSYSTEM

DG MARKET OPERATIONS

ECB-PUBLIC

24 November 2016

## ECB Money Market Contact Group

Frankfurt am Main, Tuesday, 27 September 2016, 15:00-19:00 CET

### Summary of the discussion

#### 1. Presentation of the main results of the quarterly MMCG euro money market survey

Julija Jakovicka presented the main findings of the quarterly Money Market Contact Group (MMCG) euro money market survey conducted in the second quarter of 2016. In spite of the increasing amount of excess liquidity, the survey data showed that euro money market turnover increased in the second quarter compared with the first quarter, led by the foreign exchange swap, foreign exchange forwards and the repo segments. Although, unsecured market turnover continued to decline in aggregate, there was a slight increase in unsecured borrowing for the first time since the first quarter of 2015. There was some evidence to suggest that the latter could be attributed to trades with counterparties with no access to the ECB deposit facility at levels below the deposit facility rate.

#### 2. Review of the latest market developments and other topics of relevance

Patrick Chauvet reviewed the main developments in the euro money market since the last meeting. The presentation was followed by an exchange of views on those developments, as well as on a set of issues that had been submitted to members prior to the meeting. Issues for discussion included the following.

##### (i) The impact of the outcome of the UK referendum on EU membership on the money market

The impact of the UK referendum on financial markets had been short-lived. Some investors had reduced their exposure to British banks, but this was quickly restored. In addition, banks had been well prepared to withstand the short-term increase in market uncertainty and had built buffers in anticipation.

##### (ii) The impact of higher costs of US dollar funding and of the US money market fund reform on European banks

The recent surge in USD funding costs was attributed to three factors: (a) the impact of the US money market reform, (b) expectations for a rate hike by the US Federal Open Market Committee and (c) the upcoming quarter-end related tensions. Although preparations for the money market fund reform had already started last year, the full impact only started to be felt as the implementation date on 14 October approached. In anticipation of the implementation date, US prime money market funds started hoarding cash and reducing maturities of their investments to cater for possible redemptions. This led to a reduced availability of term USD funding globally, which was most visible in the increase in the three-month LIBOR rates.

European banks have been less affected, as they had deleveraged since 2011 and had become less reliant on US money market funds for funding. European banks continue to receive funding from other money market funds which were not affected by the reform, even in three, six and nine-month tenors. Other investors had also reportedly been entering the market, benefitting from wider spreads. The lack of USD funding tensions experienced by European banks was also reflected in the limited use of the ECB's USD liquidity-providing operations.

##### (iii) Expectations of participation in the future operations of the TLTRO-II series

MMCG members anticipated that the take-up in the March 2017 operation in the second series of targeted longer-term refinancing operations (TLTRO-II) was likely to be larger than in December 2016, but that it would depend on loan growth and the price of other funding alternatives in the market. So far, Eurosystem asset purchases and

the TLTRO-II operations had helped to reduce banks' funding costs in the market, which had then been transmitted to the cost of loans to the real economy.

**(iv) The outlook for the evolution of excess liquidity and its impact on money markets**

The MMCG noted that market liquidity had decreased in various asset classes and further declines could not be excluded. It anticipated that, as a result of the increasing amount of excess liquidity and rising asset prices, market participants would increasingly prefer to deposit excess funds in the ECB's deposit facility instead of investing them in market assets. Yet some MMCG members said that high -deposit facility holdings are perceived negatively by market analysts owing to their direct impact on the net interest margin, which in turn deterred banks from using the deposit facility.

**3. Recent trends in repo rates in the euro area: possible drivers and implications for banks' liquidity management**

The gradual decline in repo rates to levels significantly below the ECB deposit facility rate reflected, in the MMCG's view, a combination of two factors: a strong demand for high-quality collateral and a shrinking supply of high-quality assets in the market, in particular German AAA-rated collateral. On the demand side, a higher demand for collateral was supported by various factors, including the need to meet margin requirements for centrally-cleared and OTC-traded derivatives. Furthermore, a number of custodians charged punitive rates for cash margins, thus favouring the use of securities. A further factor contributing to downward pressure on repo market rates was lack of access to the ECB deposit facility for some cash investors, who face lower levels of remuneration in the market.

On the supply side, limited net issuance combined with central bank asset purchases and investment policies had reportedly contributed to lower availability of high-quality collateral in the market. Some MMCG members said that some of the public sector purchase programme (PSPP) securities lending facilities of the Eurosystem were of limited effectiveness in alleviating the scarcity of high-quality collateral in the market.

**4. Structural changes in the French commercial paper market: introduction of the NEU CP market, the impact on investor demand and market developments**

Olivier Hubert presented an overview of changes in the French commercial paper (CP) market, which became effective as of 30 May 2016. Within the Place de Paris 2020 framework, the Banque de France led a project to reform the French negotiable debt securities market, working with market participant associations, market infrastructures, law firms, rating agencies and regulatory authorities. This reform resulted in the creation of Negotiable European Commercial Paper (NEU CP), which simplified the legal framework and regulatory requirements, and brought the market in line with international standards, with the aim of opening the market up to a larger number of issuers in France and abroad, including mid-sized enterprises. These changes had been welcomed by the market but, in view of high levels of excess liquidity and reduced funding needs, had not had a considerable impact on the level of issuance activity in the NEU CP market.

**5. Update on the ECB's Money Market Statistical Reporting Regulation**

Holger Neuhaus updated the group on the progress in data reporting under the ECB's Money Market Statistical Reporting Regulation. He said that reporting agents had implemented decisive reporting improvements in July, opening the gate to publication, subject to further data quality enhancements. The next meeting with the reporting banks was envisaged for November and will focus on quality checks. The ECB is in continuous dialogue with the reporting banks, both via automated data quality checks and individual feedback reports, in order to prepare for the implementation of the compliance framework from 2017 onwards. Publication of data on the ECB's website could be considered, subject to further data quality enhancement.

Holger recalled that in order to reduce the reporting burden, the ECB euro money market survey had already been discontinued and the MMCG quarterly money market survey, which had been run as a pilot project, would be discontinued in the fourth quarter of 2016. The temporary overlap of the two data collection initiatives had been maintained to ensure quality and continuity of the data.

The decision to enlarge the sample of banks reporting under the Regulation will be taken at a later stage. In any case, reporting agents are given a 12-month period between notification of their obligation to report and the start of reporting to ensure sufficient preparation time.

**6. Update on money market benchmarks and the ongoing reform process**

The European Benchmark Regulation was published in summer 2016. It will come into effect in two stages: partially now, and fully from 2018. In line with some of the articles immediately applicable, EURIBOR has been declared a critical benchmark by the European Commission, leading to, among other things, a special regime of supervision. The new Regulation gives the Belgian Financial Services and Markets Authority, in consultation with a college of supervisors, the power to impose mandatory contributions to the critical benchmarks.

As a next step of the EURIBOR reform, on 1 September the European Money Markets Institute (EMMI), which administers the EURIBOR, launched a pre-live verification exercise, whereby banks will voluntarily transmit their data to EMMI for an assessment of the feasibility of the transaction-based benchmark. The first data transactions are expected to be delivered from mid-December 2016, after which EMMI should start the data analysis and test the reporting infrastructure.

MMCG members emphasised that broad-based participation in the recently launched pre-live verification exercise for the new transaction-based EURIBOR was crucial and once again called for the participation of all systematically relevant banks in the critical benchmarks to be mandatory.

## **7. Other business: the next meeting**

At the annual MMCG dinner, ECB Executive Board member Benoît Cœuré delivered opening remarks emphasising the importance of market support for the benchmark reform process. The [full transcript](#) of the speech is available on the ECB's website.

The next meeting of the MMCG will take place on 12 December 2016 in Frankfurt am Main.