Market expectations for TLTRO-III and PELTRO

ECB – Money Market Contact Group – 16 June 2020
### TLTRO and PELTRO: Current figures

<table>
<thead>
<tr>
<th>Maturity</th>
<th>TLTRO-II (mar-20)</th>
<th>TLTRO II jun-20 Repayment</th>
<th>TLTRO June Repayment</th>
<th>Bridge LTRO</th>
<th>TLTRO-III 91 day LTROs</th>
<th>PELTRO</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>jun-20</td>
<td>157,1</td>
<td>157,1</td>
<td>389</td>
<td>0,6</td>
<td>546,7</td>
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<td>sep-20</td>
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<td>28</td>
<td>41,5</td>
<td>192,2</td>
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<td>mar-21</td>
<td>192,2</td>
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<td>jun-21</td>
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<td>mar-23</td>
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<tr>
<td><strong>Total</strong></td>
<td><strong>418,2</strong></td>
<td><strong>47,1</strong></td>
<td><strong>371,1</strong></td>
<td><strong>216,1</strong></td>
<td><strong>1,9</strong></td>
<td><strong>1</strong></td>
<td><strong>1026,2</strong></td>
</tr>
</tbody>
</table>

#### TLTRO-III

- 1trn outstanding (TLTRO-II, TLTRO-III and LTRO bridge), total capacity of close to 3trn

### Euro area

<table>
<thead>
<tr>
<th></th>
<th>Germany</th>
<th>France</th>
<th>Italy</th>
<th>Spain</th>
<th>Portugal</th>
<th>Euro area</th>
</tr>
</thead>
<tbody>
<tr>
<td>TLTRO borrowing allowance*, bn</td>
<td>760</td>
<td>673</td>
<td>462</td>
<td>322</td>
<td>47</td>
<td>2906</td>
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<tr>
<td>T/LTROs (apr-20), bn</td>
<td>116</td>
<td>232</td>
<td>278</td>
<td>174</td>
<td>21</td>
<td>949</td>
</tr>
<tr>
<td>Remaining capacity, bn</td>
<td>643</td>
<td>441</td>
<td>183</td>
<td>148</td>
<td>25</td>
<td>1957</td>
</tr>
<tr>
<td>Remaining capacity, %</td>
<td>85%</td>
<td>66%</td>
<td>40%</td>
<td>46%</td>
<td>54%</td>
<td>67%</td>
</tr>
</tbody>
</table>

* 50% of NFC loans and Total loans to households excluding Mortgages (2019-03)
Market expectations for PELTRO and TLTRO-III

TLTRO and PELTRO: Key points

- **TLTRO-III**
  - **Have become very appealing for any kind of bank** (not only peripheral ones), which can now finance a larger part of their balance sheet at cheap rates. **Mainly due to recent easing conditions**:
    - Lowering the rate to -1%
    - Bringing forward the starting date for the benchmark from 1st April 2020 to 1st March is favorable as loan books have increased in March
    - Few constraint on banks, in part by the temporary easing in collateral rules via the 20% reduction in haircuts on all eligible assets and the expansion of the eligibility criteria for credit claims should not constrain banks
    - Single operation limit was removed
  - **Banks will focus on the June operation** so as to benefit from the entire period of generous -1% rate. This is a strong incentive to use June than later operations.
  - **Early repayment on September-21 is an additional attractive feature** for the operation, as give banks a chance to reduce their borrowing when no bonus rate is applied.
  - **Government guarantee schemes** ensure that the majority of banks qualify for the lowest rates
  - Early repayment of almost entire TLTRO II outstanding suggest a roll into TLTRO III given the better conditions. Also a full rollover of the bridge LTRO is expected.
  - **Reduction of USD borrowing** could suggest banks focusing on EUR funding
  - Banks could obtain a **risk-free carry of 50bps** placing TLTRO borrowing in the ECB account.
  - **Carry trades in government bonds is limited** at current yield levels (apart from Italy)

- **PELTRO**
  - Participants with **limited TLTRO borrowing capacity**
  - **Used as a backstop**
  - Provide liquidity between TLTRO-III allotments
  - Could support Euribor levels for longer tenors
Comparison TLTRO-III and PELTRO rates

Comparison TLTRO-III and PELTRO rates

- TLTRO-III always cheaper: -0.25% vs maximum of -0.40%
  - TLTRO-III: -0.50% for jun-20 to jun-21 and 0% for july-sept-21 without meeting benchmarks; even lower rate when meeting benchmarks
- PELTRO more frequent: monthly PELTRO vs quarterly TLTRO allotments

Take-up Jun-20, with early repayment in Sep-21

- TLTRO-III
  - Benchmark 1 (OK): -0.90%
  - Benchmark 2 (OK): -0.50%
  - Without meeting benchmark: -0.40%
- PELTRO: -0.25%

Assuming MRO at 0% and DFR at -0.50% for the entire period

Benchmark 1: new lending benchmark
Benchmark 2: modified lending benchmark
**Carry trades** for TLTRO-III

- Place at the ECB account
  - Jun-20 to Jun-21: Borrow at -1.0% and **deposit at ECB** at -0.5%
- Invest in short **dated sovereign bonds**
  - Yields exceed -0.5% only in a few countries, like Italy, Spain, and Portugal
  - Yields exceed 0%: only in Italy
- Possible limited appetite by some banks to increase domestic sovereign exposure much further
  - High exposure to sovereign bonds
  - High concentration in domestic bonds

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### Sovereign bond yields (9-Jun-2020)

- Spain 1yr: -0.39
- Italy 1yr: -0.01
- Portugal 1yr: -0.42
- Germany 1yr: -0.58
- France 1yr: -0.49
- Spain 3yr: -0.23
- Italy 3yr: -0.25
- Portugal 3yr: -0.27
- Germany 3yr: -0.58
- France 3yr: -0.53

Yields exceed -0.5% only in Italy.
Market expectations for PELTRO and TLTRO-III

**TLTRO-III**
- **1trn outstanding** (TLTRO-II, TLTRO-III and LTRO bridge), total capacity of close to 3trn
  - **Philip Lane** (13-mar-2020): “...we have increased the volume of funds that banks can borrow from us in order to provide credit to firms and households by more than EUR 1 trillion. This raises the total possible borrowing volume under this programme to almost EUR 3 trillion”*
- **Rollover** of TLTRO II repayment and June maturity (371bn) and bridge LTRO (389bn) into TLTRO-III: **760bn**
- **Additional** demand, for example for carry trade: estimates range from **200 to 760bn**
- **Total TLTRO-III uptake of 960bn to 1500bn** (from current 216)

**PELTRO**
- **Small take-up**, only as a backstop

Annex
Borrowing conditions

### TLTRO-III
- Borrowing allowance is equal to 50% of eligible loans as of 28 February 2019 minus amounts borrowed under TLTRO II
- Interest rates:
  - Avg DFR - 50bp **(-1.0%)** between 24-jun-20 and 23-jun-21, and avg DFR **(-0.5%)** afterwards, if participants meet new lending benchmark (2020/2021)
  - Avg DFR **(-0.50%)** for all three years, if meeting initial modified lending benchmark (2019/21)
  - For participants meeting neither the new lending benchmark nor the initial modified lending benchmark: Avg MRO -0.50bp **(-0.50%)** between jun-20 and jun-21 and Avg MRO (0%) the rest of the period.
- Quarterly allotments until March 2021. Quarterly repayment option, after 1 year and starting in sept-2021

### PELTRO
- Interest rate: 25bps below MRO **(-0.25%)**
- Full allotment
- Without condition: does not depend on evolution of loan book
- Seven monthly operations, from may to dec-2020, with maturity between sep-2021 and jul-2021