



EUROPEAN CENTRAL BANK

EUROSYSTEM

DG MARKET OPERATIONS

19 March 2024

ECB Money Market Contact Group (MMCG)

Thursday, 14 March 2024, 12:00-17:30 CET, Frankfurt am Main, hybrid meeting

Summary of the discussion¹

ECB Executive Board member Isabel Schnabel addressed the MMCG with a speech on [**“The Eurosystem’s operational framework”**](#).

MMCG members welcomed the announcement on the operational framework review, in particular the prospect of structural longer-term operations and the continuation of the broad Eurosystem collateral pool, which they viewed as allowing for a smooth path towards an environment where liquidity would gradually decline. Members expressed mixed views on the narrower spread between the deposit facility rate (DFR) and the rate on Main Refinancing Operations (MRO). Most members appreciated that the narrower spread supported bidding in the ECB’s standard refinancing operations and limited the scope of fragmentation in euro area money markets, as rates with maturities up to three months would be capped by the MRO rate (or slightly above). MMCG members discussed, from the perspective of liquidity coverage ratio (LCR) fulfilment, the relative attractiveness of MROs in view of the 15 basis points spread to the DFR, compared with market-based instruments. Some members expected that the narrower spread would not be sufficient to reinvigorate money market activity, while acknowledging that this depended on the market segment and collateral. All in all, many members did not expect the lower spread to engender an excessive reliance on central bank funding, as a diversified funding mix was viewed favourably by supervisors, investors and rating agencies as well as banks’ management bodies. Members also described the market reaction to the framework announcement as a non-event.

Money markets adapted well to the ongoing reduction of the ECB’s balance sheet with signs of reactivation. Members did not envisage difficulties for banks in fulfilling regulatory liquidity ratios, also due to the gradual and well-anticipated approach of the ECB. Thanks to ample investor appetite, banks with lower excess liquidity holdings were able to acquire market funding. This explained the limited participation in standard refinancing operations so far. There were no signs of stress in banks’ bond markets, with credit spreads tightening across countries to multi-year lows. Retail deposits remained an important funding source for euro area banks, even though some members saw this as being challenged by digital innovations and public sector retail bond issuance.

Members expected repo rates to remain above the €STR and discussed potential drivers. Among the drivers of a lower €STR, members stressed that regulatory requirements, such as the LCR and the net stable funding ratio (NSFR), were more binding than operational cash needs. As overnight unsecured deposits had no regulatory value and high balance sheet

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

costs, banks had no interest in retaining them and were pricing them away. Non-banks preferred holding deposits with highly-rated banks, that were able to price those deposits at a spread to the DFR. While money market funds (MMFs) increased their investments in the repo market owing to more attractive rates, unsecured deposits remained important for MMFs, in part due to the different trading hours of these markets. At the same time, the upward pressure on repo rates could be explained by (i) the current ample availability of collateral in repo markets and (ii) the demand for short-term funding, notably by the positioning of leveraged investors (particularly hedge funds) in the cash bond market. The additional liquidity invested in the repo market by the new reverse repo facility of the Spanish debt management office was well absorbed and had a limited impact on repo rates due to the broad collateral that was accepted. Members highlighted that repo transactions would become more costly in terms of the NSFR from June 2025 onwards, which could add upward pressure to repo rates. The asymmetric treatment of open repos in the LCR (they count as outflows but not inflows) was also mentioned as a disincentive for open repo transactions.

The unsecured interbank market was not expected to be revived. Instead, the repo market had been fulfilling the function of reserve redistribution, albeit with some limitations. Members highlighted the benefits of using central counterparties (CCPs), which were estimated to intermediate about half of the repo transactions in the euro area. These benefits included access to broad liquidity, operational efficiency, counterparty risk mitigation, and regulatory cost relief. At the same time, several challenges remained, including potentially procyclical collateral and counterparty limits. Members also mentioned the issue of asymmetric access to the centrally cleared repo market. While large banks across the euro area had good access to CCPs, smaller banks in some countries did not. CCP usage also entailed costs, including in the form of higher margin requirements, which had an impact on the LCR. The bilateral repo market was also growing, including for term transactions, and was facilitating collateral upgrades from non-high quality liquid assets (HQLA) into HQLA. Members highlighted that some infrastructure challenges remained in particular for developing more cross-border transactions in the repo market. One example of this was fragmented collateral pools due to the lack of a European central securities depository. The lack of a harmonised insolvency framework in the euro area also made cross-border liquidity redistribution more complicated.

Members discussed different drivers of demand for central bank reserves and potential metrics that could be used to assess reserve scarcity. Members' choice of optimal liquid buffer size, as well as the composition of the buffer (preference for cash versus securities), depended on minimum reserve requirements and predicted cash outflows, as well as regulatory and internal risk management considerations, and opportunistic motives, i.e. the opportunity cost of holding central bank reserves versus other securities. With regard to the composition of the liquid buffer, liquidity considerations, i.e. how quickly the HQLA can be monetized, played an important role. There was reportedly a substitution limit between holding central bank reserves versus securities due to the volatility in accounting metrics and exposure to term risk and, potentially, credit risk implied by holding securities. MMCG members emphasised that demand for reserves was dynamic and prone to sudden spikes in a stress environment. With regard to regulatory drivers, the LCR-driven demand was not expected to recede due to pressure stemming from the benchmarking to peers, even if the liquidity was not strictly needed. Members mentioned several potential indicators that could be used to monitor reserve scarcity, such as the spread between the EURIBOR and overnight index swap rates, sovereign bond, asset swap and credit spreads, an increased number of fails and an upward pressure on repo rates, as well as a sudden increase in the ECB's standard refinancing operations.

Participant's organisation**Name of participant**

Amundi Asset Management	Mr Patrick Simeon	
Banco Santander	Mr Luis Barrigon Rodriguez	
Barclays	Mr Isaac Davies	
Belfius Bank	Mr Werner Driscart	
BNP Paribas	Mr Patrick Chauvet	
BPCE/Natixis	Mr Olivier Hubert	
CaixaBank	Mr Xavier Combis	
Commerzbank AG	Mr Andreas Biewald	
Crédit Agricole/CACIB-CASA	Mr Pierre Le Veziel	
Deutsche Bank AG	Mr Jürgen Sklarczyk	
DZ Bank AG	Mr Oliver Deutscher	
Eurobank	Mr Dimitris Psychogios	
Eurex Clearing AG	Mr Frank Odendall	
HSBC Continental Europe	Mr Harry-David Gauvin	
ING Bank	Mr Jakob Wahl	
Intesa Sanpaolo	Ms Maria Cristina Lege	
JP Morgan Asset Management	Ms Olivia Maguire	
Unicredit	Mr Michele Montani	
Coöperatieve Rabobank	Mr Frank Beset	
Erste Bank	Mr René Brunner	Remote
Société Générale	Mr Frederic Pailloux	Remote
European Central Bank	Mr Thomas Vlassopoulos	Chairperson
European Central Bank	Ms Pamina Karl	Secretary
European Central Bank	Mr Helmut Wacket	
European Central Bank	Ms Julija Jakovicka	
European Central Bank	Mr Raúl Novelle Araujo	
European Central Bank	Ms Marta Skrzypińska	