



EUROPEAN CENTRAL BANK

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PUBLIC CONSULTATION

SUMMARY OF COMMENTS RECEIVED ON THE MEASURES PROPOSED TO IMPROVE THE OPERATIONAL FRAMEWORK FOR MONETARY POLICY

The respondents were generally in favour of changing the timing of the reserve maintenance period and shortening the maturity of the main refinancing operations (MROs). It was agreed that the new reserve maintenance period calendar would reduce the costs to credit institutions since, first, it would avoid maintenance periods starting or ending on a weekend and, second, it would reduce the likelihood of underbidding in the MROs.

The shortening of the MRO maturity was seen as a complementary measure which would further reduce the likelihood of underbidding and promote stable interest rate expectations throughout the maintenance period, although some respondents mentioned that it could lead to higher bid rates in the MROs because of the higher liquidity risk incurred by bidders were they to receive a zero allotment. However, the respondents said that the relevance of this would be lessened if the longer-term refinancing operations (LTROs) were retained.

Most respondents were against a suspension of the LTROs, which still play an important role in liquidity management. Respondents said that first, LTROs enable credit institutions to diversify the maturity of their liabilities; second, if the MRO maturity were reduced at the same time as the LTROs were suspended there would be a significant concentration of refinancing on one date; third, LTROs are a key element of credit institutions' contingency plans for times of market stress; finally, they continue to be relevant in providing finance to smaller counterparties.

A more detailed account of the comments is given in the following paragraphs.

1. CHANGING THE TIMING OF THE RESERVE MAINTENANCE PERIOD

14 of the 17 banking and financial market associations and 33 of the 42 individual credit institutions which responded to the public consultation were in favour of changing the timing of the reserve maintenance period.

It was agreed that the new reserve maintenance period calendar would reduce costs to credit institutions, first, because it would avoid maintenance periods starting and ending on a weekend and, second, because it would reduce the likelihood of underbidding in the MROs. Most associations and credit institutions supported the proposal, saying that there would be no major technical problems and that the costs would be within reasonable limits.

Since the last MRO of the maintenance period would always be settled six days before the end of the maintenance period, some respondents argued that, unless the ECB carried out fine-tuning operations, this could increase the risk of large aggregate liquidity imbalances accumulating, potentially leading to greater volatility in interest rates and greater use of the standing facilities at the end of the maintenance period.

Regarding the variable length of the maintenance period, most respondents did not think it would cause problems, although they recommended minimising the variation if possible. Some said, however, that it could lead to higher excess reserves and discourage use of the averaging provision.

2. SHORTENING THE MATURITY OF THE MAIN REFINANCING OPERATIONS TO ONE WEEK

11 of the 17 associations and 22 of the 42 individual credit institutions were in favour of the proposal to shorten the MRO maturity, which was seen as a complementary measure in reducing the likelihood of underbidding and promoting stable interest rate expectations. Credit institutions were slightly less supportive of this proposal than of changing the timing of the maintenance period, and three associations were against it.

A drawback given by some respondents was the risk that shortening the maturity would lead to an increase in the rates at which counterparties bid in the MROs, especially in the last operation of the maintenance period and at certain times of the year, such as the year-end. At these times, credit institutions would be more concerned than usual about having enough liquidity and avoiding a zero allotment, which could potentially create greater interest rate volatility. Additionally, concerns were put forward regarding increased operational risk in the event of technical problems during the bidding or allotment process.

Respondents also said that an excessive concentration of operations on one day may give rise to tensions in the payment systems. Therefore, to ensure the efficient use of collateral following a potential zero liquidity allotment, market participants would rely greatly on the development of a smoother and more centralised securities settlement and custodian system for the euro market. They mentioned that the transfer of collateral between various custodian systems often implies that securities are unavailable for a day, thereby creating higher costs and operational risks.

In order to mitigate the operational risks associated with the rollover of very large MRO volumes – pending further development of the market infrastructure – some respondents recommended increasing the volume of the LTROs to some extent. Another proposal made by some respondents was

to introduce a “maintenance period tender” – in parallel to the weekly MRO – which would be allotted on the first day of the maintenance period and would mature on the last day.

3. SUSPENSION OF THE LONGER-TERM REFINANCING OPERATIONS

All of the associations were against suspending the LTROs, as were 31 of the 42 individual credit institutions. They said that the LTROs still play an important role in liquidity management; even many credit institutions which did not participate in the LTROs said it was important for them to be retained. Two main arguments were put forward.

First, LTROs enable credit institutions to diversify the maturity of their liabilities so as to better match the maturities of assets and liabilities. The respondents to the public consultation procedure also mentioned that LTROs play an important role in credit institutions’ liquidity contingency plans, i.e. their plans for obtaining liquidity during times of general market tension or when faced with individual liquidity problems. The respondents said that alternative sources of longer-term funding were not viable substitutes for the LTROs because of the different collateral requirements and a decline in the liquidity of the relevant segment of the money market.

Second, there were concerns that if the MRO maturity were reduced at the same time as a suspension of the LTROs there would be an even greater concentration of refinancing (approximately EUR 200 billion settled on one day) resulting in greater operational risks as well as more conservative bidding by credit institutions which could further force up refinancing costs.