EUROPEAN CENTRAL BANK

EUROSYSTEM

DG MARKET OPERATIONS

18 March 2020

ECB Money Market Contact Group (MMCG)

Friday, 13 March 2020, 10:45-11:40 CET

Teleconference

Summary of the discussion

1) Feedback on the ECB's package of measures announced on 12 March 2020

A majority of MMCG members were positive about the package of monetary policy measures announced by the ECB on 12 March, but they were disappointed by the communication during the press conference. A few members were concerned about the strong negative market developments, which were partly attributed to the ongoing liquidity strains in the US dollar funding markets.

Although the ECB's package of measures did not include the expected deposit facility rate cut, this was not perceived negatively by MMCG members. On the contrary, MMCG members praised the elements of the package as being supportive for bank lending to the economy at a time when the corporate sector was the most severely affected by the COVID-19 shock. MMCG members also welcomed the capital relief measures announced by ECB Banking Supervision and considered them to be crucial in the current circumstances. With regard to the ECB's monetary policy measures, MMCG members welcomed in particular (i) the more favourable terms applied to the TLTRO III operations, with a 25 basis point reduction in the TLTRO rates and a change in the benchmark conditions, and (ii) the announced collateral easing measures. MMCG members considered these measures to be effective and that, together, they represented a powerful and adequate response to the ongoing deterioration of corporate creditworthiness. Some members believed that the take-up in the June TLTRO III operation could be very large if other public institutions were to add guarantee schemes to share credit risk with banks and if the ECB were to relax the eligible collateral criteria. Additional TLTRO III operations with longer maturities could help in the future if market and economic conditions deteriorated further. Other members believed that the additional asset purchases of €120 billion might not be enough if the current limits (e.g. the capital key) were kept in place.

On the communication elements, MMCG members believed that the ECB had missed a good opportunity to better explain the background to its decision. They would have appreciated a clear explanation of why the ECB did not follow other central banks in cutting policy rates. This was interpreted by some market participants as a reflection that the ECB may have reached its limits in terms of policy measures. Presenting ECB Banking Supervision's capital relief measures as an isolated decision rather than as part of a wider series of measures by the ECB's Governing Council also contributed to the less positive perception. MMCG members noted that market reaction was more "psychological": the market had been pricing in a high probability of a rate cut and, in the absence of one, it embarked on selling risky assets. According to MMCG members, the ECB could have been more effective in its communication by signalling that there was an effective rate cut of 25 basis points, implemented through the TLTRO III pricing. Moreover, markets reacted badly to the remark about the rising Italian-German government bond spread. All of these factors contributed to the less positive market perception of the ECB's decision. MMCG members noted that people more closely involved in the banks' liquidity management and funding were able to better understand the nuances of the announced measures than markets in general, which explained the divergence in perceptions. MMCG members highlighted two aspects of the ECB's measures which they saw as being helpful to safeguard funding conditions: (i) the enhanced conditions for the TLTRO III operations, which reduced the funding cost for banks lending to the real economy by 25 basis points; and (ii) the additional asset purchases of €120 billion by the end of 2020, which were expected to put downward pressure on the yields of government, corporate, asset-backed and covered bonds. According to MMCG members, it would take some time until the positive effect of the ECB's measures was fully understood by the market.

2) Current market conditions

MMCG members had noted an acute deterioration in US dollar funding conditions since the previous day. It was reported that the market became nervous in anticipation that bank corporate customers would massively draw on their committed credit lines (for both short and long tenors) to check that US dollar funds were available to them. At the same time, institutions usually in demand of US dollar liquidity also seemed to be hoarding US dollar buffers for precautionary reasons, given the current uncertainty. The situation was aggravated by business continuity reasons (limitations to trading in the home office environment) and/or fears of a possible lockdown of markets. According to the MMCG, the existing US dollar liquidity operations provided by the Federal Reserve System as well as the one-week US dollar operations via the swap line arrangements of major central banks were insufficient to calm markets in current conditions. MMCG members believed that a more permanent and unlimited US dollar liquidity facility would be needed.

List of participants

Money Market Contact Group meeting

Participant's organisation	Name of participant
Barclays Bank	Mr Bineet Shah
Bayerische Landesbank	Mr Harald Endres
BBVA	Mr Miguel Monzon
BNP Paribas	Mr Patrick Chauvet
BPCE/Natixis	Mr Olivier Hubert
Caixabank	Mr Xavier Combis Comas
Caixa Geral de Depósitos	Mr António Paiva
Commerzbank	Mr Andreas Biewald
Coöperative Rabobank U.A.	Mr Frank Beset
Deutsche Bank	Mr Jürgen Sklarczyk
DZ Bank	Mr Michael Schneider
Erste Group Bank	Mr René Brunner
HSBC	Mr Harry Gauvin
ING	Mr Jaap Kes
Intesa Sanpaolo	Ms Maria Cristina Lege
LBBW	Mr Jan Misch
Société Générale	Ms Ileana Pietraru
UniCredit Bank	Mr Harald Bänsch
European Central Bank	Ms Cornelia Holthausen (Chair)
European Central Bank	Ms Maria Encio (Secretary)