

Main Developments in Euro Money Markets & ECB Policy Outlook

RECENT TRENDS AND FUTURE PROSPECTS

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Key Developments in Euro Money Markets



ECB Balance Sheet Reduction

The ongoing ECB's balance sheet reduction has further decreased excess liquidity, impacting euro money market dynamics.

ESTR Fixing

Slow but gradual increase of spread vs DFR. Underlying volume for ESTR fixing initially increased after incorporating MMSR data of 24 new banks by 1st July but did not reach April peak and declined again as the repo market seems more attractive for liquidity sourcing.

Repo Market Attraction

The repo market gained appeal, shifting activity away from unsecured segments. Spreads for funding in repo have narrowed, particularly for lower-rated securities. Shift from collateral-driven to cash-driven repo markets impacts spreads vs OIS

Volatility in EURIBOR Fixings

Significant volatility in EURIBOR fixings have led to some discomfort in markets. This erratic fixing behaviour can be observed nicely for example when looking at 1s-3s-6s EURIBOR vs. €STR flies.



CP Issuance, Repo Market & MRO/LTRO

Robust Commercial Paper Issuance

Commercial paper issuance remains strong, driven by high demand from money market funds, with slight fluctuations in volume and tenors week by week.

Avg spread of new issues vs. €STR swap also pretty stable through out the different tenors.

Repo Market Dynamics

Refinancing GC has become more expensive in recent months, but the spreads between issues have converged.

In the long-term repo market, we are seeing less activity in retained covered bond refinancing compared to recent months, while government bonds (e.g., Spanish, French) are still being refinanced for longer periods.

In general, we are currently observing that many banks have already stocked up on liquidity (LCR and NSFR), and demand is lower than in the same period last year.

MRO/LTRO uptake

Uptake volumes still quite low as market financing is still cheaper, however forecasts of EURIBOR and GC term repo show that, if the current trend continuous, spreads over OIS could reach those of MRO/LTRO during 2026.



FX Swap Dynamics & Quarter-End Funding

Calm FX Swap Markets

EURUSD FX Swap levels rather driven by rate expectations and increased activity/levels in US GC repo over the last weeks than any change on the cross currency basis.

We have seen a quite tight trading range in EURUSD xccy basis during the last weeks and do not expect much change in dynamics there in coming weeks.

Quarter-End Pre-Funding Stability

Recent quarter-end pre-funding activities have been stable and so it is also expected for September's quarter-end.

There is always some uncertainty at this time of the year regarding the year-end funding in fx swap markets but with currently priced spread of roughly 200bp for the two day turn the usd implied rate expectations are rather on the lower end of that what we have seen in recent years.



ECB Policy Outlook & Terminal Rate

Terminal Rate Expectations

Market expectations for the terminal rate remained stable post July ECB meeting, with potential for one more (25bp) cut in late 2025 and stable during 2026.

Price Stability Focus

Headline inflation is already at the ECB's inflation target, and the ECB's forecasts also expect inflation to remain stable at 2% or just below in the medium term, while service sector inflation is still well above the target.

Additional focus is on economic developments since the outbreak of the tariff conflict with the US.

Quantitative Tightening

With no active bond sales expected the quantitative tightening progress will stay predictable and gradual, avoiding market disruptions. The impact of less excess liquidity and more collateral availability should further impact money market spreads.

Liquidity Management

Market spread developments and ECB's aim of stigma reduction might lead at some point to gradually higher takeup of MRO/LTRO but no significant change seen in near future.

Risk Factors Ahead



Geopolitical Tensions

Trade/Tariff uncertainty and regional conflicts threaten financial market stability and create risks for euro money markets.

Also further discussions on USD central bank swap line could impact cross currency markets world wide and therefore also the euro money markets.

Fragile political situation in France could also have further negative impact on EURO and Eurozone markets.

ECB Balance Sheet Reduction

The ECB's shrinking balance sheet may cause liquidity fragmentation and higher volatility during 2026 due to uneven reserve distribution among institutions.

Macroeconomic Shock Risks

Unexpected global financial volatility remain major concerns affecting market stability and policy responses.

Instant Payment Regulation

Some uncertainties regarding impact of next implementation phase of instant payment regulation on financial stability still remain.

Disclaimer

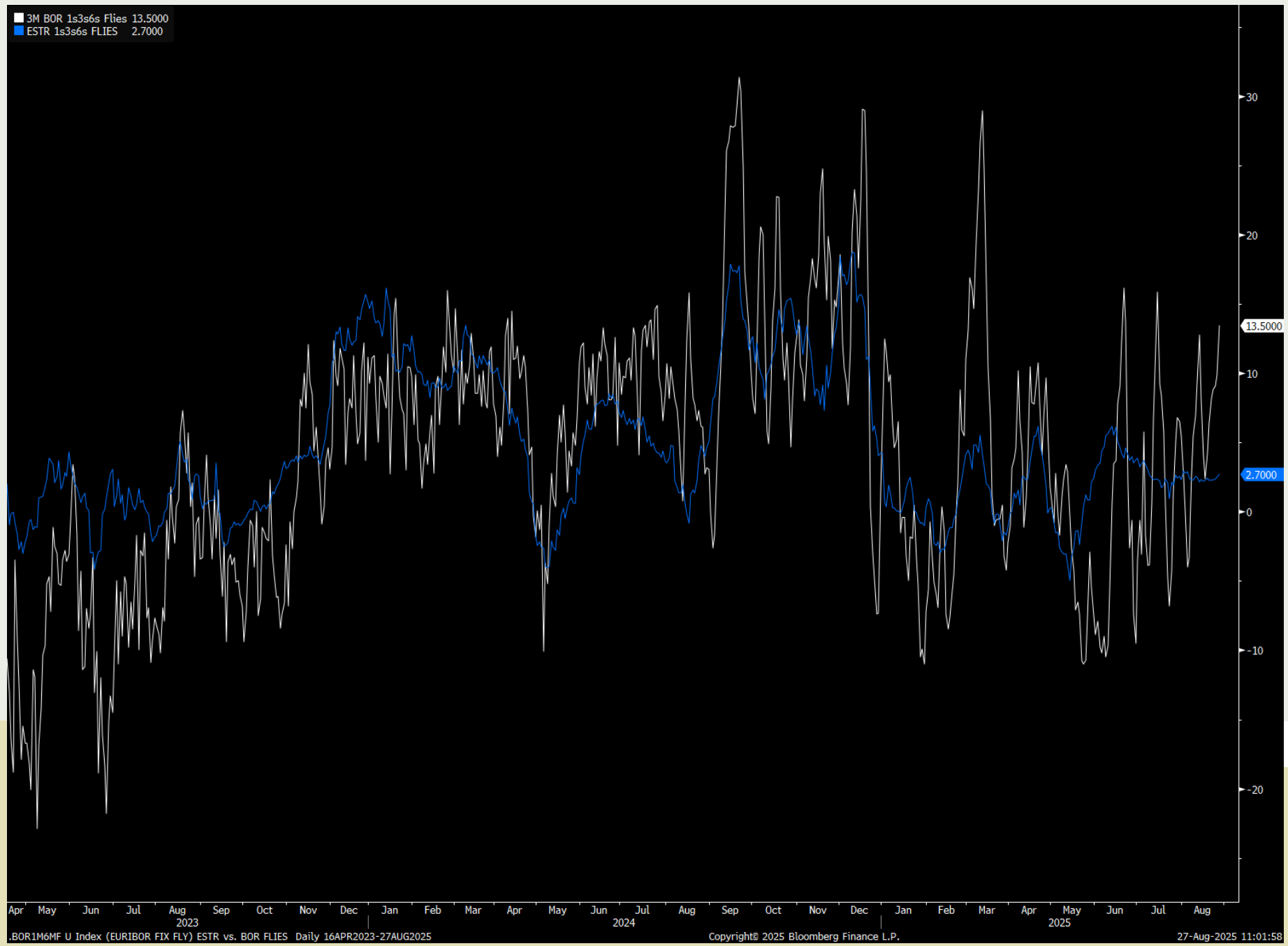
The views expressed in this document reflect my personal assessment of the current market and do not necessarily represent the views of ERSTE Group and should not be construed as advice.

This document is only intended to serve as a basis for discussions within ECB Money Market Contact Group in order to exchange potentially differing views on current market developments.

APPENDIX

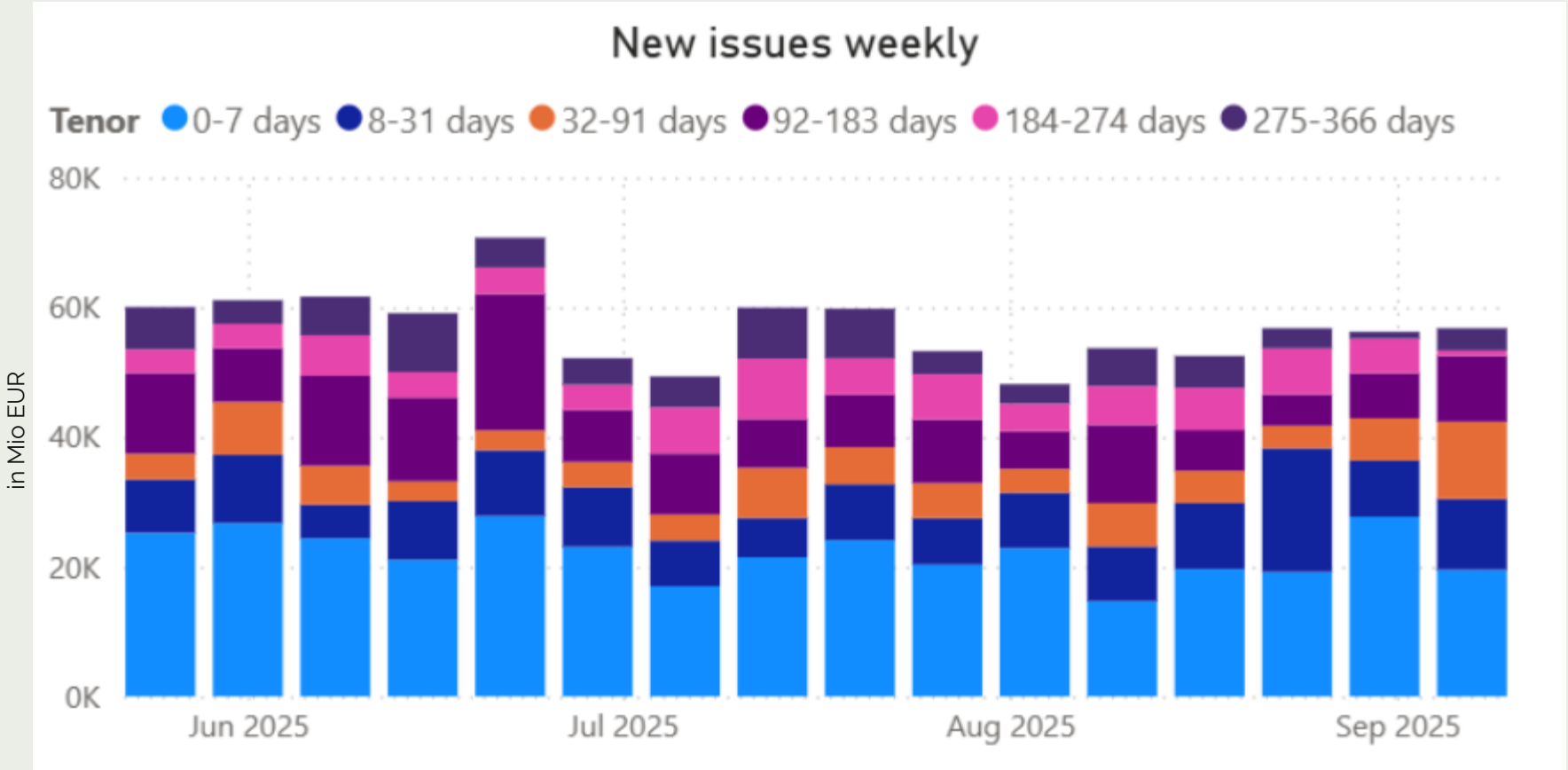
1s – 3s – 6s
flies

EURIBOR and
€STR



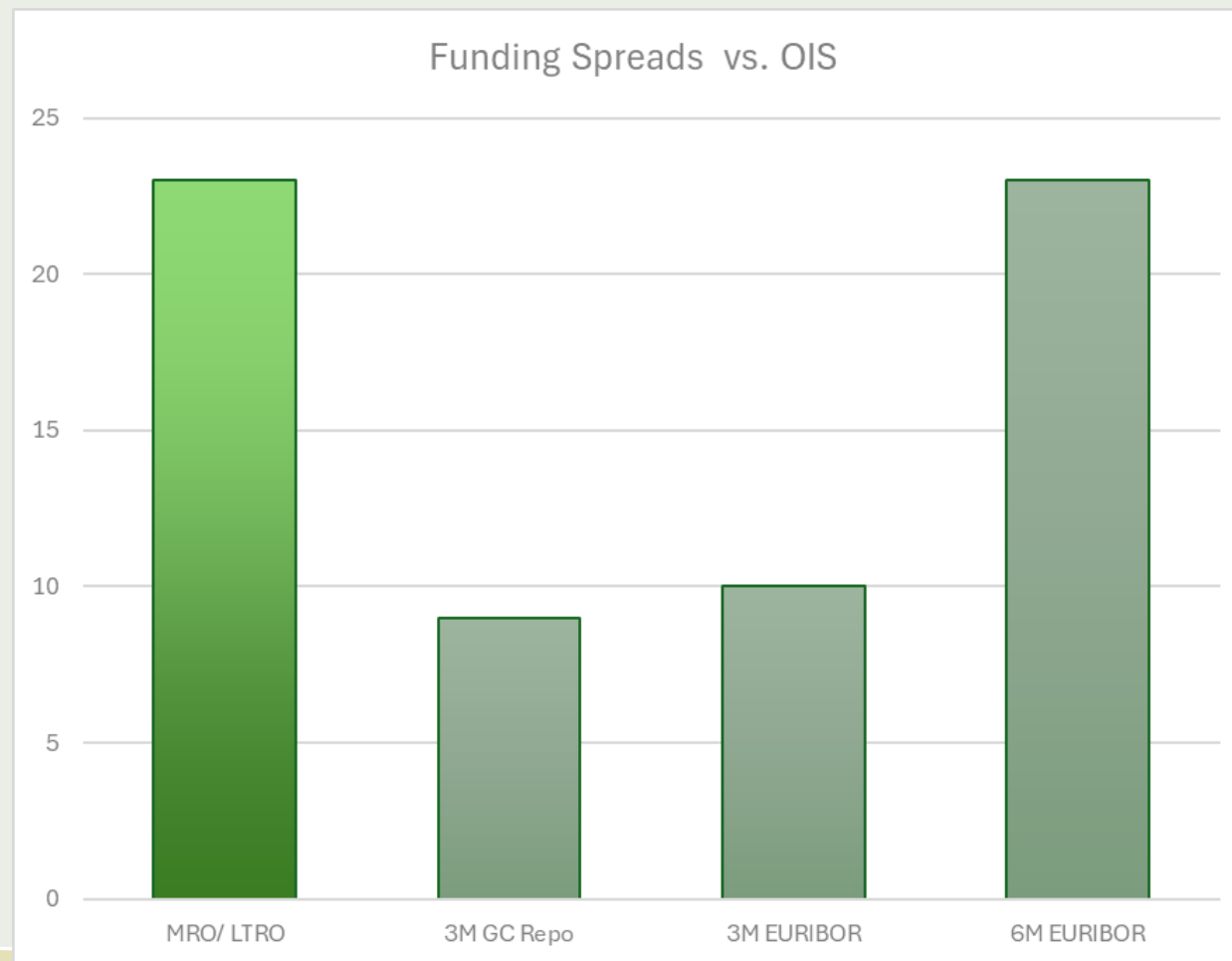
Source: Bloomberg

CP Issuance



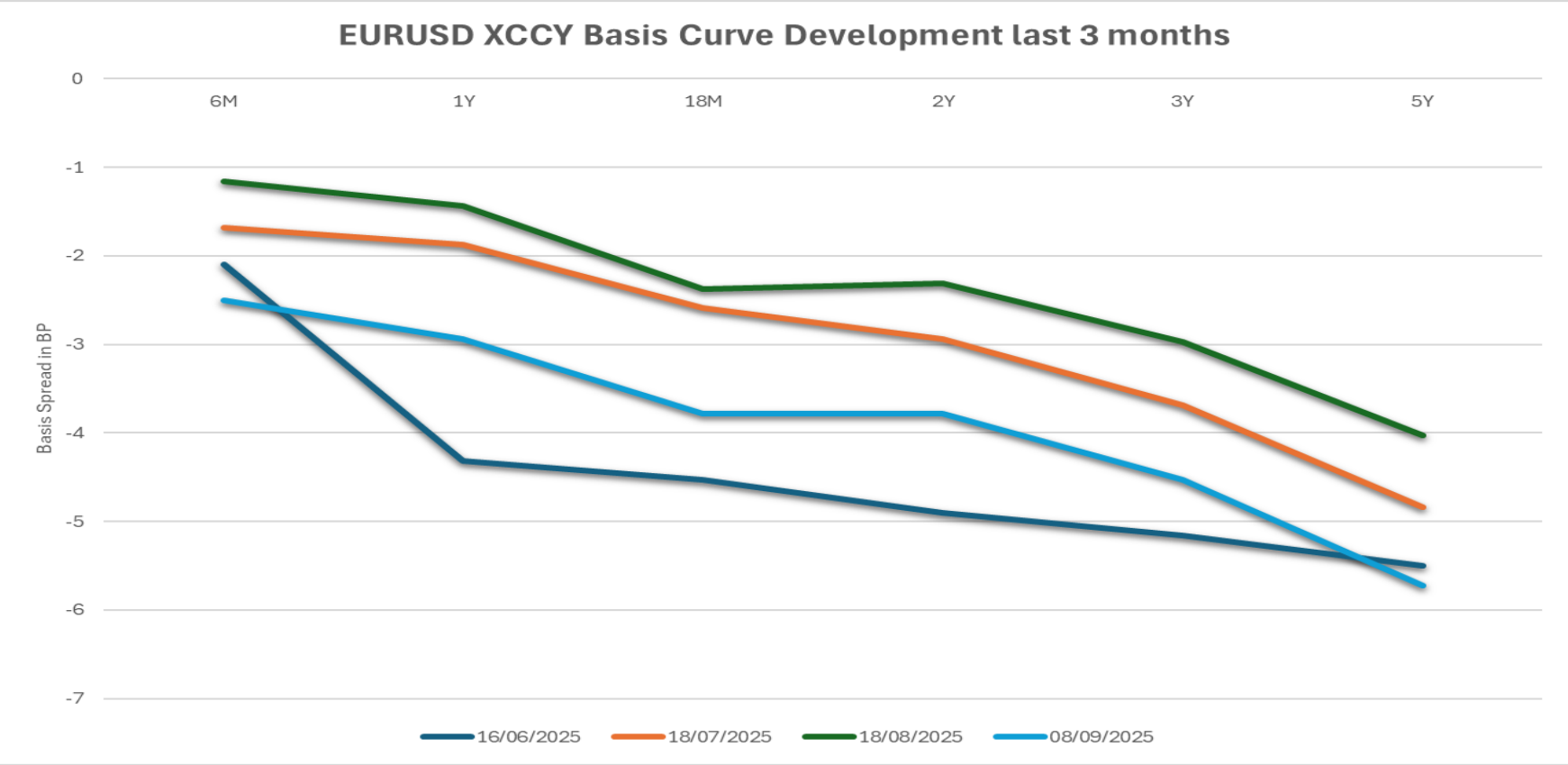
Source: ECB, ERSTE

Short-Term Funding Spreads vs. OIS



Source: Bloomberg, ERSTE

EURUSD Cross Currency Basis



Source: LSEG, ERSTE