ECB MMCG March 13th 2025

A) Main developments in money markets and ECB policy outlook

Frankfurt, March 2025, Oliver Deutscher

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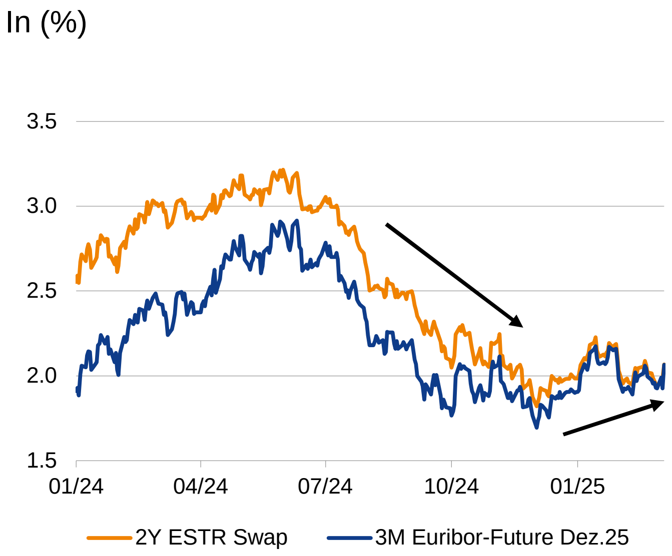
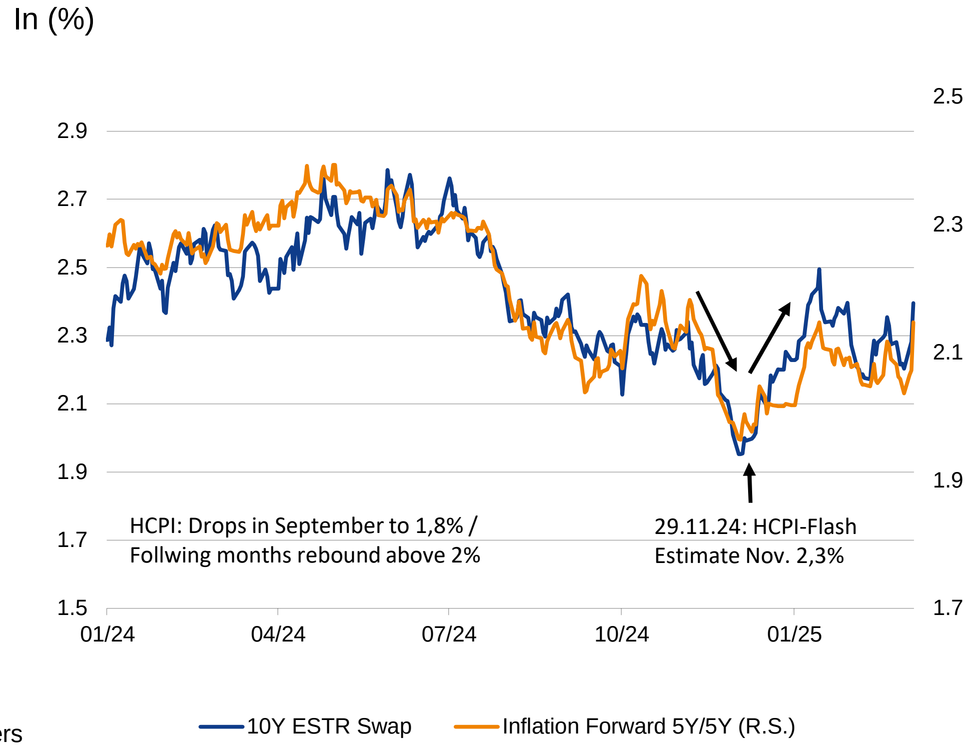
Inflation outlook subject to high uncertainty (Trade War)

ECB interest rate cuts no longer on autopilot





- Main drivers for risk free rates (e.g. 2Y ESTR Swap) driven by market expectations of far lower and faster ECB‘s path and melting inflation figures.
- 2025, rates drifted upwards due to sticky inflation data in both economic blocs (US/EUR)
- Term premium also impacted by negatve impacts e.g.geopolitical risks, US global tariffs and rising uncertanties for global debth demands
- Focus on possible monetary policy divergences betwen FED vs.ECB, handling of spillovers effects
- Reference to this weeks German debt brake, possible EU-Taxonomie changes etc.

Source: Bloomberg, DZ BANK

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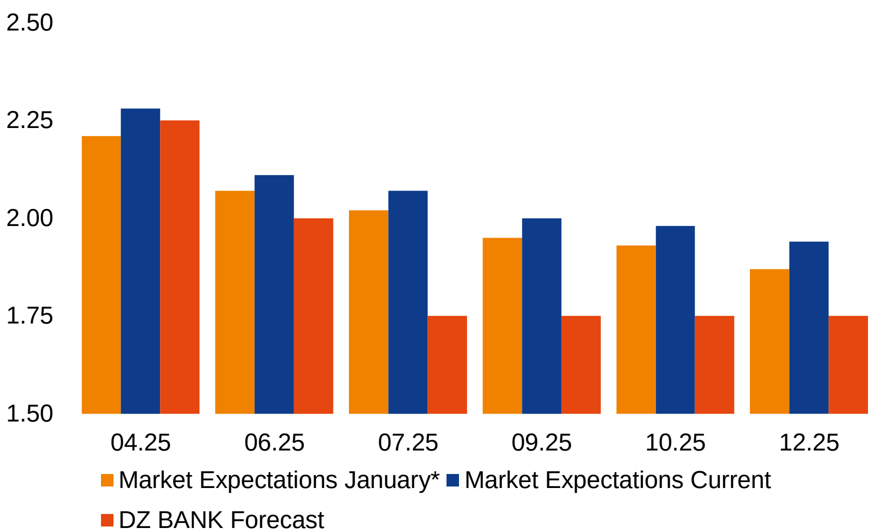
Market Participants expect further monetary easing

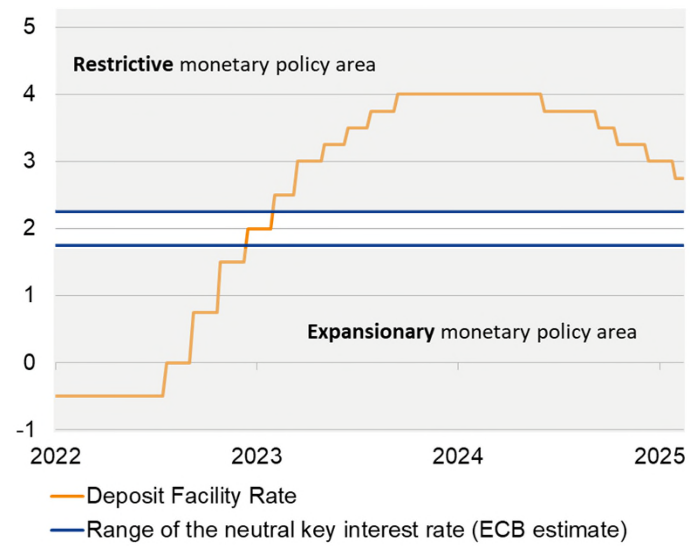
The discussions within the Governing Council are likely to be more controversial

In (%) Overnight Index Swaps



- **DZ BANK AG research expectations are tending towards 1.75%** at EoY versus market observed
- Expectations based on difference in Eurozone economic growth <1% (DZ) vs. > 1.2% (ECB)

In (%) **



- ECB's future policy **terminal / neutral rate** expected at or around +/- 2%
- Meeting target of inflation rate at or around 2%

Source: Bloomberg, DZ BANK *(6. January / **(Natural rate estimates for the euro area: insights, uncertainties and shortcomings – Economic Bulletin 1, 2025

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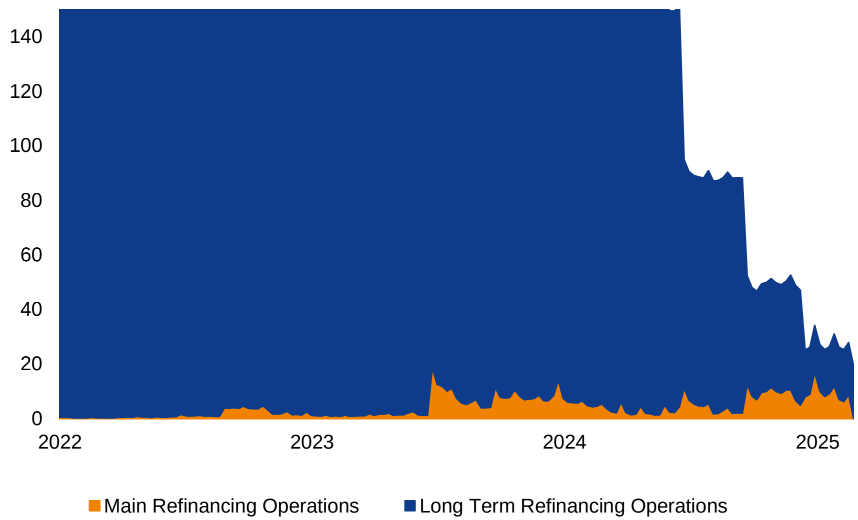
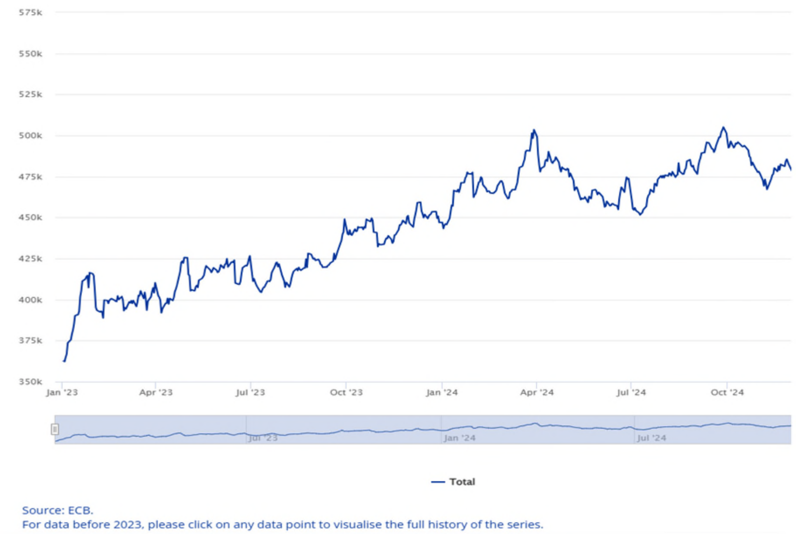
European banks less active in ECB tender operations

TLTROs thing of the past

In Billion Euro



STEP Market Outstanding CP Volume (in Mio.)



- **ECB'**s standing facilities indicate currently **no signs of negative impacts resulting from QT Policy**
- **No negative market disturbances** have been observed **over EoY** or **past quarter-end-turns** and are not yet foreseen
- Short-term money market funding, investor demands sufficient.
- **STEP-Market volumes (450-500 Bln Euro)** are still indicating healthy market environment, meeting funding demands
- Cross-border US-short-term market accessibility comfortable

Source: Bloomberg, DZ BANK; Disaggregated financial statement of the Eurosystem / Reference Date 3.1.2025

Source: Amounts outstanding by residual time to maturity | ECB Data Portal

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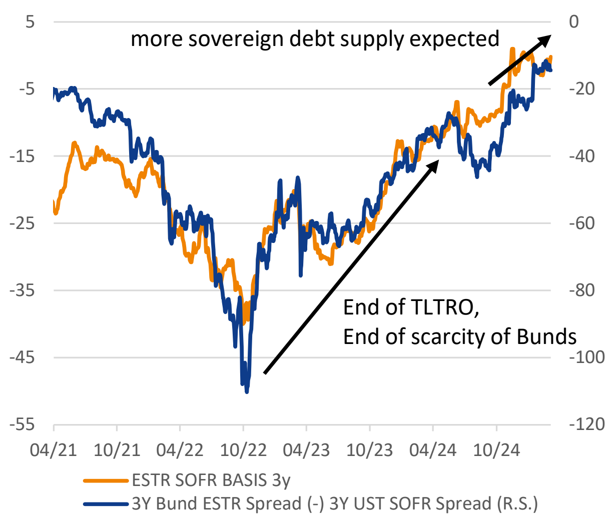
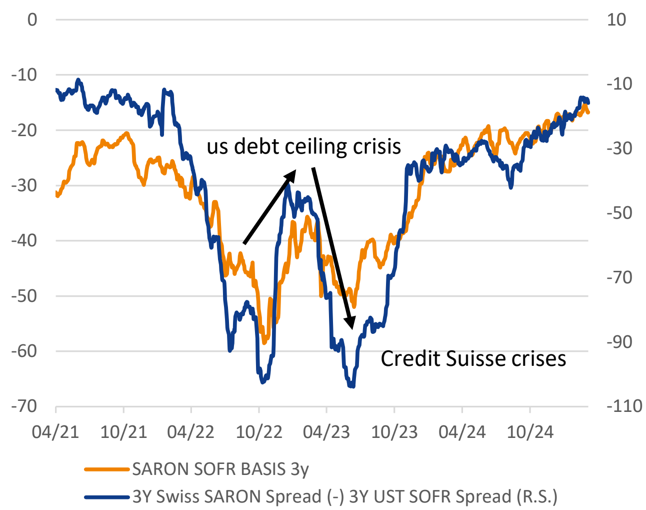
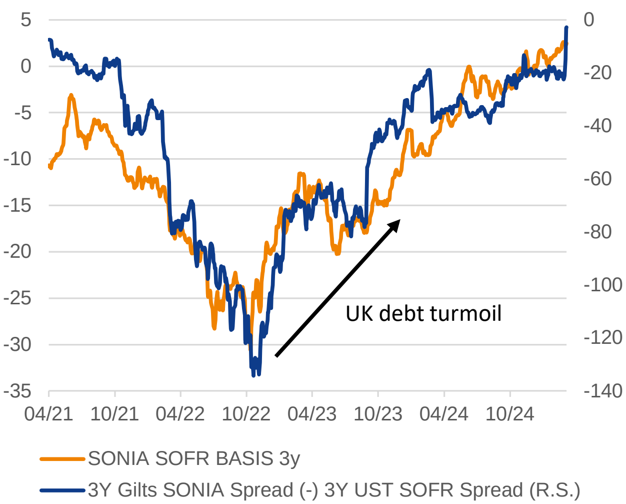
Spill-over effects of sovereign debt supply and monetary tightening

EUR-USD basis swap is currently flat – due to the sharp increase in Bund-swap spreads

Basis Points







- The basis swap is influenced, among other factors, by the risk premium differential between sovereign bonds swap spreads (versus OIS).
- The developments in risk premiums in the (low-credit-risk) sovereign sector are mainly driven by supply and demand. The greater the difference in risk premiums, the larger the basis swap.
- When EUR bonds become cheaper, more attractive to Investors compared to USD Bonds (as they currently are), EUR investors no longer need to demand comparable bonds in USD. Therefore, the demand for basis swaps decline and lead to flattening of ESTR/SOFR Basis Swap Spread at or around 0bp
- For American companies/banks, funding in EUR is no longer as attractive as it was a few years ago. Conversely, funding for Europeans in USD has become cheaper.
- As a result, today, there is no real pick-up advantage for investors in USTreasury investments. SOFR/ESTR Spread neutral, hinting to far better credit-spread pick up for investing in EU Bonds/SSA
- (e.g.Dec'36 EUBonds and Z-Spread +60bp) due to increasing expected premiums for EU SSA's

Source: Bloomberg; DZ BANK

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EU's NSFR change on RSF-Required Stable Funding factors

NSFR - Net Stable Funding Ratio

Item	EU	Basel
Short-term SFTs with financial counterparties backed by Level 1 assets	0% RSF	10% RSF
Short-term SFTs with financial counterparties backed by non-level 1 assets	5% RSF	15% RSF
Unsecured loans with financial counterparties	10% RSF	15% RSF
Short-term liabilities provided by financial counterparties	0% ASF	0% ASF

- Envisaged **CRR changes due on June 28th 2025**
- CRR II / Regulation (EZ) No 2019/ 876 and amended CRR (Regulation (EU) No 575/ 2013)

Take-aways on ICMA's briefing note May"24* and ERCC bi-annual survey Dec.'24

- Impact on reverse-repos with terms < 6month
- Level 1 HQLA assets
- SSA's/Government Debts

	Dec.'24	Dec.'23	
• est.:	+11.10bn	(vs.10.90bn)	overall Gross Survey (80%)
• est.:	+13.85bn	(vs.13.68bn)	overall Impacted Gross Volume (100%)
• est.:	+ **7.29bn**	(vs. 7.18bn)	overall Reverse-Repos (52.5% vs.52.7%)
• est.:	+ 5.20bn	(vs. 5.26bn)	overall estimated maturity < 6month)

Impact:

• est.:	+ 241bn	(vs. 246bn)	impacted HQLA Level-1 with factor +10%

Costs p.a.:

- est.: - 1.3bn/54bp (vs.1.6bn/65bp)impacted annual costs ref.5yr iTraxx Sen.Un.

➢ Adverse effects on Government Bond market velocity and market making
➢ Increase of costs for long term funding
➢ Increasing importance looking at fall of debt brakes and EU funding prospects

*Source: ICMA-ERCC_BN_NSFR-and-reverse-repo_May-2024_Final.pdf and ICMA-European-Repo-Market-Survey-47-conducted-June-2024-published-November-2024-121124.pdf

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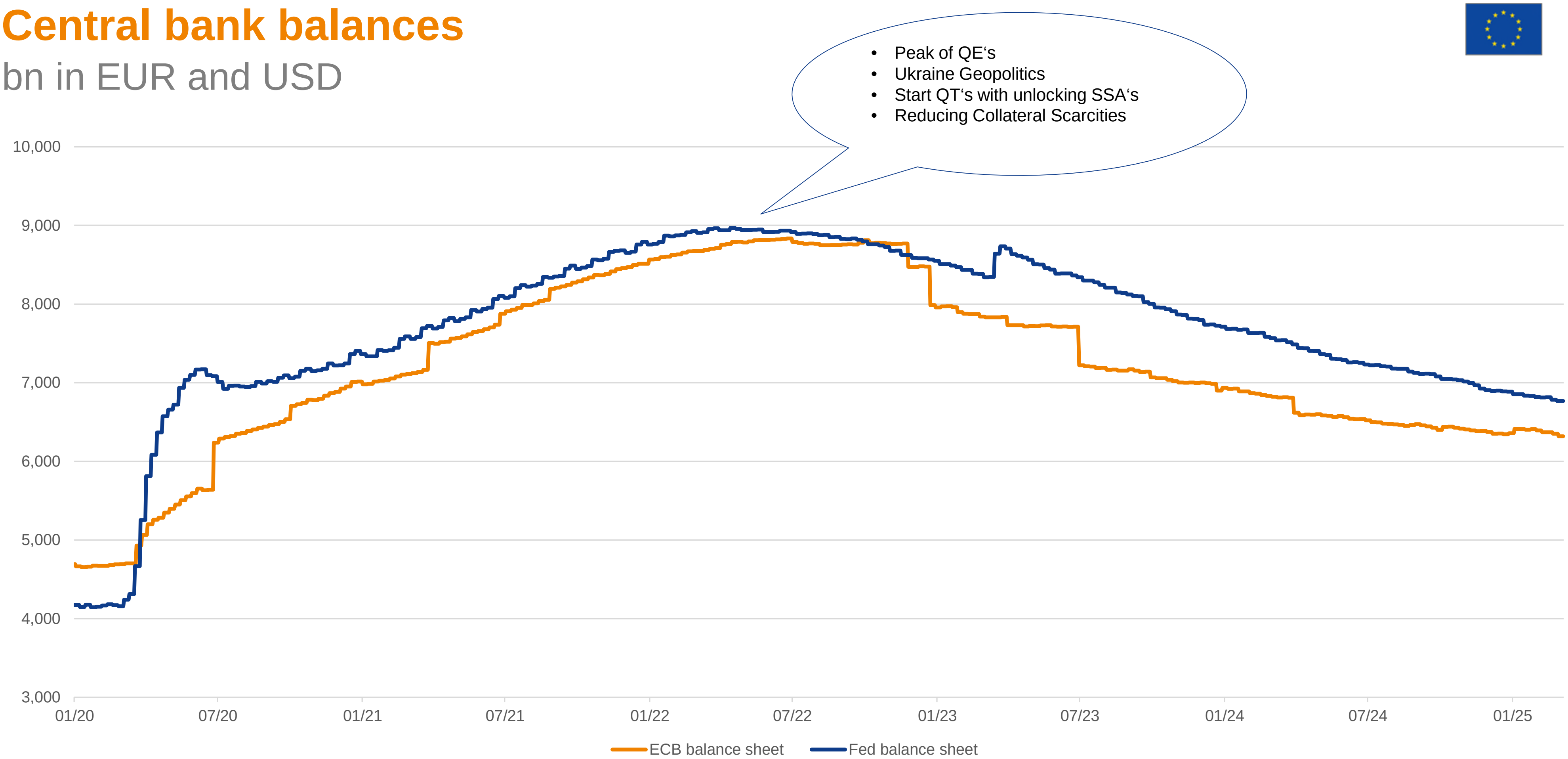
Questions and Back-Up

Central bank balances

bn in EUR and USD



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ECB MMCG Meeting

Questionnaire to Agenda A)

A) Main developments in money markets and ECB policy outlook

- What are the main drivers behind the increase in risk free rates.
- How do you assess the importance of spillovers from the US? What is driving the term premium?
- How do you see market expectations about the ECB's future policy rate path and the terminal rate?
- How is global policy uncertainty (e.g. on trade policy) affecting money markets and
- what are your expectations for the ultimate impact on offshore USD funding?
- What are your views on the NSFR treatment of short-term securities financing exemption, the call for evidence by the European Commission, and the possible impact on the short-term repo markets it may have?
- Do you see any risks in quarter-end pre-funding?
- Do you see a risk that in view of the mild year-end, some market participants might wait longer before covering the quarter-end (i.e. complacency)?