Issue Nº7

Newsletter
November 2023

The European Money Markets Institute

Evolving dynamics

Insights into Euro markets and finance innovations

Dear readers,

As we enter the final weeks of 2023, we at EMMI have a couple of reasons to celebrate. Two key initiatives have been keeping us busy: the consultation about the proposed changes in the Euribor methodology, and the growth of the STEP (Short-Term European Paper) label on commercial paper.

Euribor is our main benchmark used in a wide array of financial products. EMMI's proposal to reformulate Level 2.3 and drop Level 3 is a milestone in our history. Your feedback is paramount to this process. With that in mind, we ask you to take part in the consultation period, which will stay open until December 11, 2023.

The other great news is that many large issuers now use the STEP label for short-term European paper.

Elsewhere, The European Central Bank's recent decisions caused significant changes in the money markets. In October, the plan was to maintain interest rates and reduce excess liquidity by repaying TLTROs and shrinking the APP portfolio.

Influenced by ECB expectations, Euribor rates have recently stabilized after displaying an upward trajectory. As a result, Euribor underlying volumes still continue to increase. For more on developments in the European money market and Euribor read "Echoes from the Money Market" in the newsletter.

Finally, don't miss our exclusive interview with Carlos Ocaña Pérez de Tudela, Director General at Funcas, as he shares his views on economic and social research on the Eurozone.

Kind regards,
Jean-Louis Schirmann
CEO – The European Money Markets Institute

Shaping the future
EMMI proposes changes to Euribor methodology

In a significant development, the European Money Markets Institute (EMMI) has unveiled a consultation paper detailing proposed changes to the Euribor methodology, a pivotal benchmark in the global financial system. The proposed reforms aim to fortify the benchmark's integrity while simplifying operational processes for Panel Banks.

Proposed changes for a resilient benchmark

EMMI's commitment to upholding the integrity and reliability of Euribor has led to a meticulous review of its methodology. The proposed changes focus on two key elements:

1. Reformulation of Level 2.3: This includes enlarging the starting point for calculation and redefining the Market Adjustment Factor (MAF) to better reflect changes in interest rates and perceived credit risks.
2. Discontinuation of Level 3: The reformulation of Level 2.3 allows for the discontinuation of Level 3 in the current hybrid methodology. This move is anticipated to significantly reduce operational and cost burdens for Euribor Panel Banks, creating an opportunity for panel expansion without compromising the benchmark's reliability.

Collaboration and feedback

EMMI emphasizes the importance of industry feedback in shaping these changes. The consultation paper invites stakeholders and market participants to provide input, ensuring that modifications align with the best interests of the financial community. This collaborative approach underscores EMMI's commitment to transparency and inclusivity.

How to participate

Interested parties are encouraged to review the consultation paper and submit feedback via email to hybrid2023@emmi-benchmarks.eu, with "Euribor Consultation 2023" as the subject. Submissions should include the full name of the respondent, job position, organisation, country, and contact telephone number. The consultation period is open until December 11, 2023.

A summary of stakeholder feedback will be released by the end of February 2024, maintaining anonymity while providing valuable insights. EMMI will then communicate the conclusions of the proposed enhancements and implementation plans.

For further details, refer to EMMI's website: emmi-benchmarks.eu

Stay tuned as EMMI shapes the future of Euribor with these proposed changes, aiming for a more robust and efficient benchmark.

Bridging economic realities

A conversation with Carlos Ocaña Pérez de Tudela

We had the privilege of engaging in conversation with Carlos Ocaña Pérez de Tudela, the Director General at Funcas. Funcas is a pivotal think tank dedicated to economic and social research and the dissemination of insightful knowledge, fostering a bridge between academia and the practicalities of the real economy. Carlos Ocaña assumed the role of Director General at Funcas in 2011. Before that, he helad positions in the fields of finance and economics, namely as Spanish Secretary of State of Finance and Secretary General of the Budget, with stints at the OECD's International Energy Agency, the Spanish Electricity System Commission, and the Tribunal for the Defence of Competition.

Could you elaborate on Funcas' core mission and the specific role it plays in shaping and analysing macroeconomic trends, particularly within the Eurozone context?

Funcas is a thinktank dedicated to economic and social research. We are particularly well known in the field of economic forecasting and macroeconomic policy in Spain and the Euro Area. But we are also increasingly active in two other areas: finance and social issues, including financial education. After 40 years, we have built a strong reputation as an independent and solid centre of analysis.
A large part of our analysis is available in English in our Web page, including the section Funcas Europe, specifically devoted to European issues.
www.funcas.es/en/home/

EMMEC has enjoyed the privilege of high-quality presentations from strategists, economists and market experts who share their expertise and analysis. Funcas has been a regular presenter as well. Where do you see the added value for such interventions, both for EMMEC and Funcas?

In terms of value, we think it's important to disseminate our analysis and, in parallel, engage in a constructive dialogue with a wide range of professionals, decision-makers and society at large.

In the EMMEC September meeting, Funcas discussed trends in the inflationary process. Could you share some key insights or trends that were highlighted during this presentation, and how these might impact the economic landscape in the near future?"

In our view, recent trends suggest that a disinflation process is underway in the eurozone. Whether one looks at recent CPI data, or its underlying wage-profit dynamics, the outlook is for further moderation. That said, we believe that the disinflation process will be both gradual and vulnerable to exogenous shocks, such as possible energy price hikes or a reversal of the tax cuts that were adopted by governments as part of their 2022 anti-inflation packages . And, in any case, the ECB will want to ensure that a return to the 2% target is on the horizon before cutting interest rates. ■

> ***"We believe that the disinflation process will be both gradual and vulnerable to exogenous shocks, such as possible energy price hikes or a reversal of the tax cuts."***

The minutes of the EMMEC meetings can be consulted here.

STEP label triumph

Cultivating transparency in diverse organisations' short-term finance initiatives

In recent years, there has been a significant shift toward more sustainable and transparent finance practices. As such, a number of financial entities have embraced EMMI's STEP label (Short-Term European Paper), which aims to foster transparency in short-term finance. Below, is an overview of the most recent issuers that have been granted the STEP label.

Holcim Sterling Finance (Netherlands) B.V. and Holcim Finance (Luxembourg) S.A.

Leading the charge, Holcim Sterling Finance (Netherlands) B.V. and Holcim Finance (Luxembourg) S.A. have chosen the STEP label for their Euro-Commercial Paper Programme, emphasising transparency not only in their short-term finance operation, but also through the integration of Environmental, Social, and Governance (ESG) factors in their other financial instruments.

London Stock Exchange Group plc, LSEGA Financing PLC, and LSEG Netherlands B.V.

Continuing the trend, the London Stock Exchange Group plc, LSEGA Financing PLC, and LSEG Netherlands B.V. have opted for a Guaranteed Euro-Commercial Paper Programme under the STEP label. This choice reflects the finance sector's active engagement in promoting transparency, aligning with STEP's mission to converge market standards and practices.

Santander Consumer Bank AG

Santander Consumer Bank AG joins their peers, implementing the STEP label in their Euro-Commercial Paper Programme. The decision underscores the bank's commitment to transparent short-term finance practices, resonating with STEP's objectives of enhancing market standards and practices across the European short-term paper landscape.

Asian Development Bank

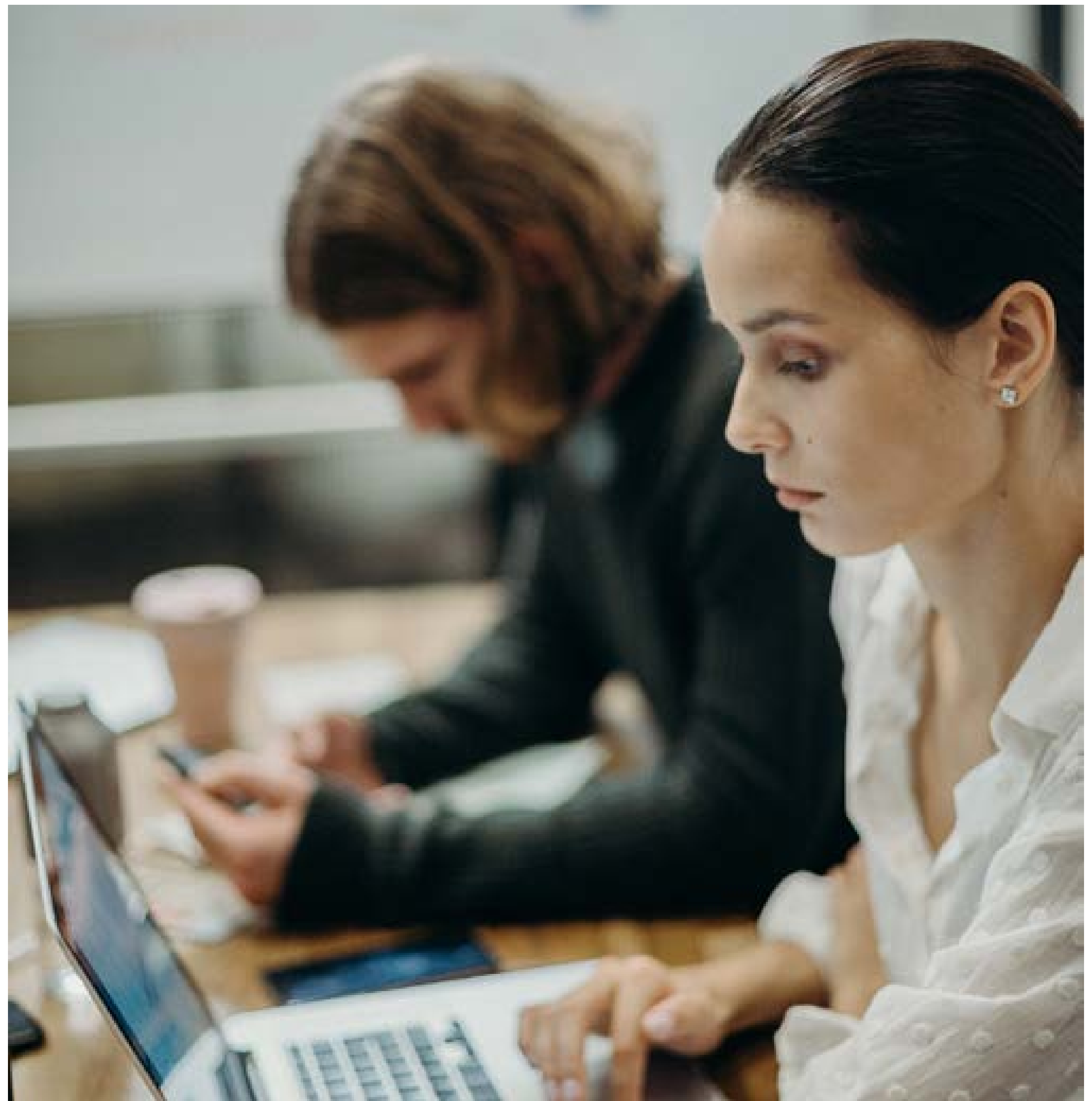
The Asian Development Bank's participation in the STEP label's Euro-Commercial Paper Programme underscores the label's reach across regions and industries. By embracing

transparency in their short-term finance initiatives, the Asian Development Bank exemplifies the global impact of STEP in promoting harmonised standards.

Esprinet S.p.A.
A technology solutions provider, Esprinet S.p.A., integrates the STEP label into its Euro-Commercial Paper Programme, showcasing that regardless of the sector, organisations recognize the importance of transparent short-term financial strategies.

Hungary, Ferrovial SE, TRATON, and more
National governments, exemplified by Hungary's Euro-Commercial Paper Programme, and industry leaders like Ferrovial SE, TRATON, Credito Emiliano S.p.A., Landwirtschaftliche Rentenbank, Ferrovie dello Stato Italiane S.p.A., and The OPEC Fund for International Development, participating in the Euro-Commercial Paper Programme, demonstrate how the STEP label's principles extend to diverse entities, fostering transparency in their respective short-term finance initiatives.

Global transparency movement
The STEP label's triumph lies in cultivating transparency across a spectrum of organisations, transcending sectors, regions, and sizes. By converging market standards and practices, STEP ensures that short-term finance becomes transparent. As more organisations embrace the STEP label, the finance landscape is poised to become a beacon of transparent practices, setting the stage for a future where transparency is inherent in short-term financial decision-making.



> ***"The finance landscape is poised to become a beacon of transparent practices."***

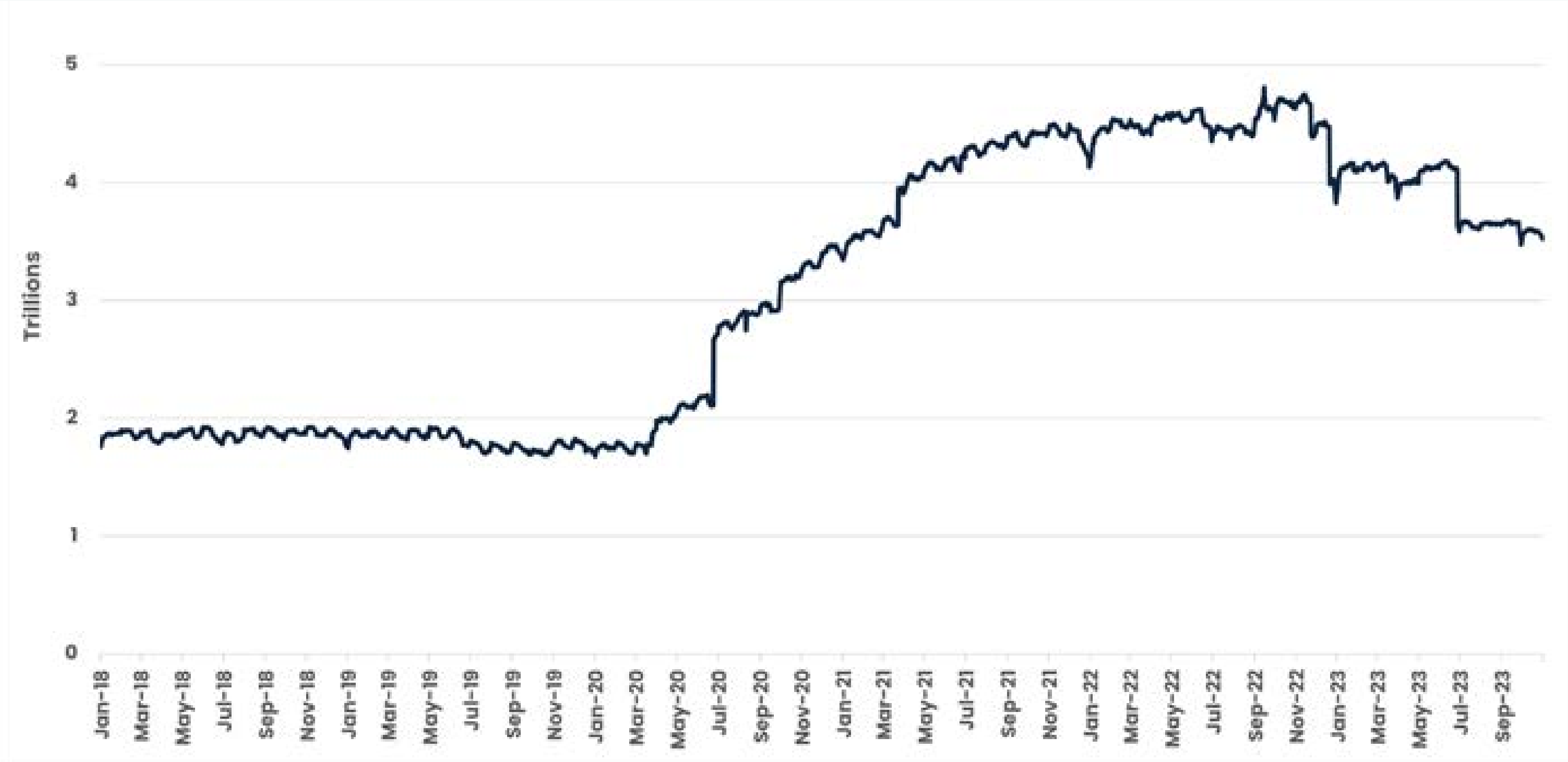
Echoes from the euro money markets

Key events closely related to the money market

Recent developments in the European money markets have been significantly influenced by key events and decisions made by the European Central Bank (ECB). Notably, the ECB opted to maintain the three key interest rates in its monetary policy meeting in October, adhering to a "higher for longer" strategy. The Deposit Facility Rate (DFR) stands at 4%, the Main Refinancing Operations Rate (MRO) at 4.50%, and the Marginal Lending Facility Rate (MLF) at 4.75%.

One pivotal event affecting the money market was the substantial reduction in euro area excess liquidity in June 2023. This decline was attributed to the repayment of the largest operation of targeted longer-term refinancing operations (TLTRO III.4), amounting to approximately EUR 34 billion. This trend is expected to persist, with ongoing early repayments in TLTROs, and the current outstanding TLTROs amount slightly below EUR 500 billion.

Chart 1 – Excess liquidity



Source: ECB

Simultaneously, there has been a gradual decrease in the size of the Asset Purchase Programme (APP) portfolio, contributing to the reduction in excess liquidity. The current scenario marks a shift in the money market landscape.

Euribor rates have experienced an upward trajectory since July 2022, with rates stabilizing at 3.88%, 3.87%, 3.97%, 4.09%, and 4.05% for the 1-week, 1-month, 3-month, 6-month, and 12-month tenors, respectively, as of 31 October 2023. The 12-month

Euribor is beginning to move below the six-month mark, driven by expectations of lower ECB interest rates. The stability in Euribor rates in recent months is primarily influenced by expectations surrounding future ECB monetary policy decisions.

Furthermore, the underlying volumes of EURIBOR rates have displayed stability across all tenors, except for the 1-week, which has shown a strong uptrend since the initiation of ECB rate hikes.

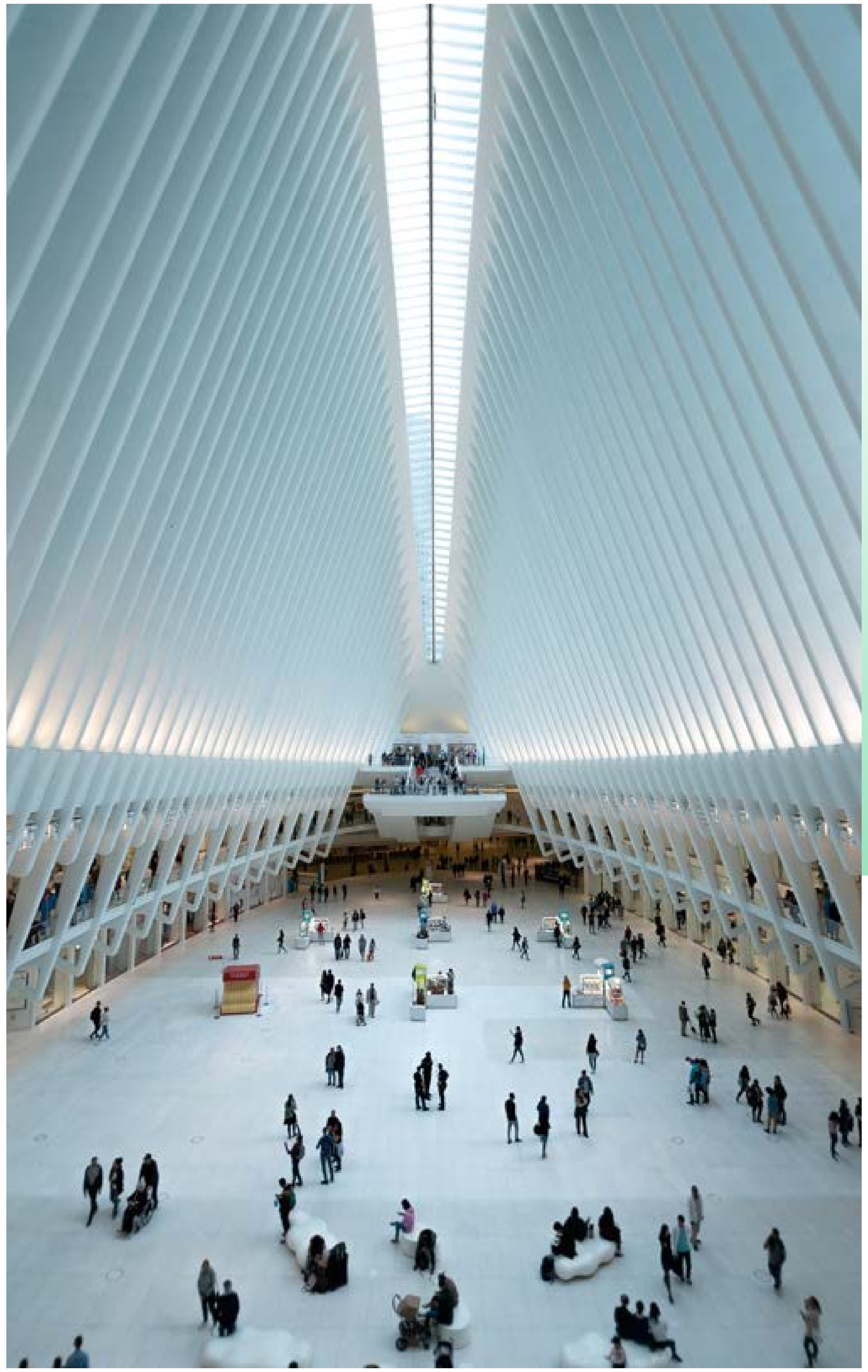
This increase in EURIBOR volume across tenors is linked to the steady decrease in excess liquidity, revitalising the unsecured market.

The Hybrid methodology has been employed to analyse these developments. Level 1 contributions show a strong uptrend in the 1-week tenor, confirming increased activity in the shorter tenors of the unsecured market. In contrast, Level 1 contributions in other Euribor tenors exhibit a slight uptrend or stability.

Examining the counterparty sector share of volumes, it is observed that Euribor transactions are predominantly executed with official sector

Chart 2 – Euribor rates

Source: The European Money Markets Institute



institutions and other financial intermediaries. Transactions with deposit-taking corporations exhibit a downtrend at the beginning and end of the money market curve but remain stable in other tenors.

Turning attention to MMSR rates, the 3-month Euribor moves above 3-month wholesale, unsecured, borrowing MMSR rates, indicating a co-movement between these two key rates. Of note, a fundamental difference between Euribor and MMSR determination is the inclusion of transactions with non-financial corporates counterparties in MMSR, which are not included in Euribor.

In summary, the current state of the European money market reflects a dynamic interplay of ECB

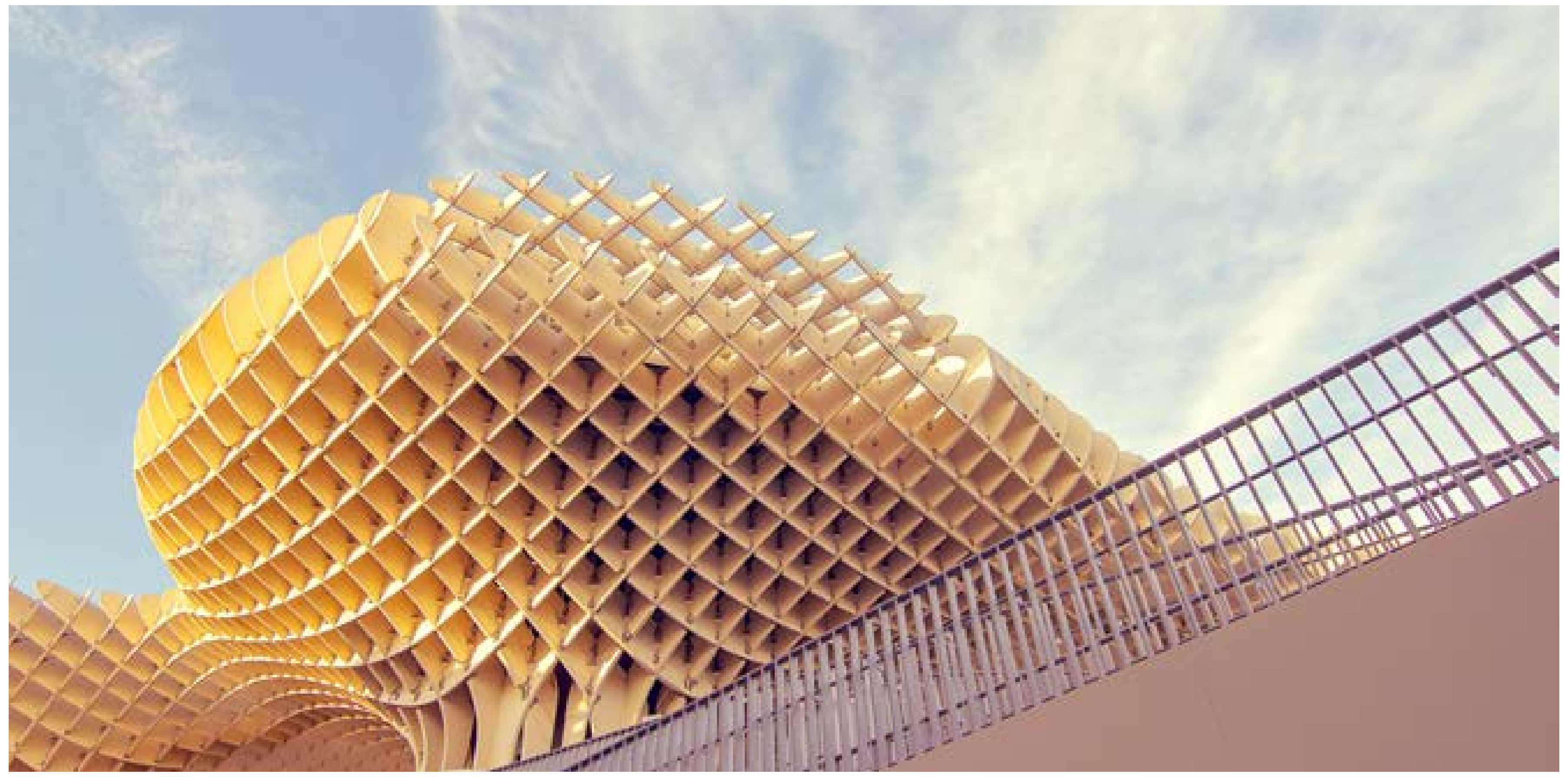
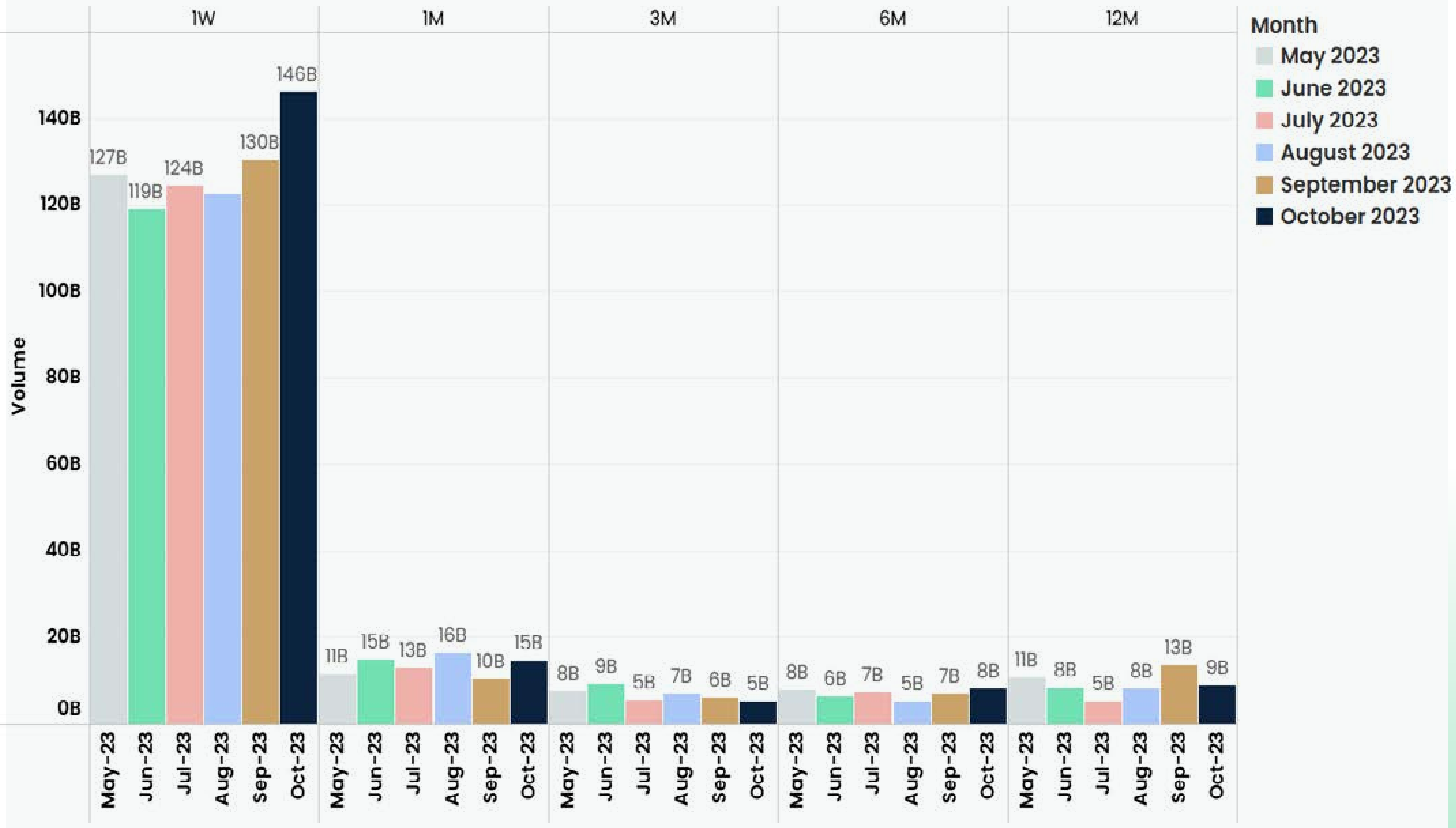


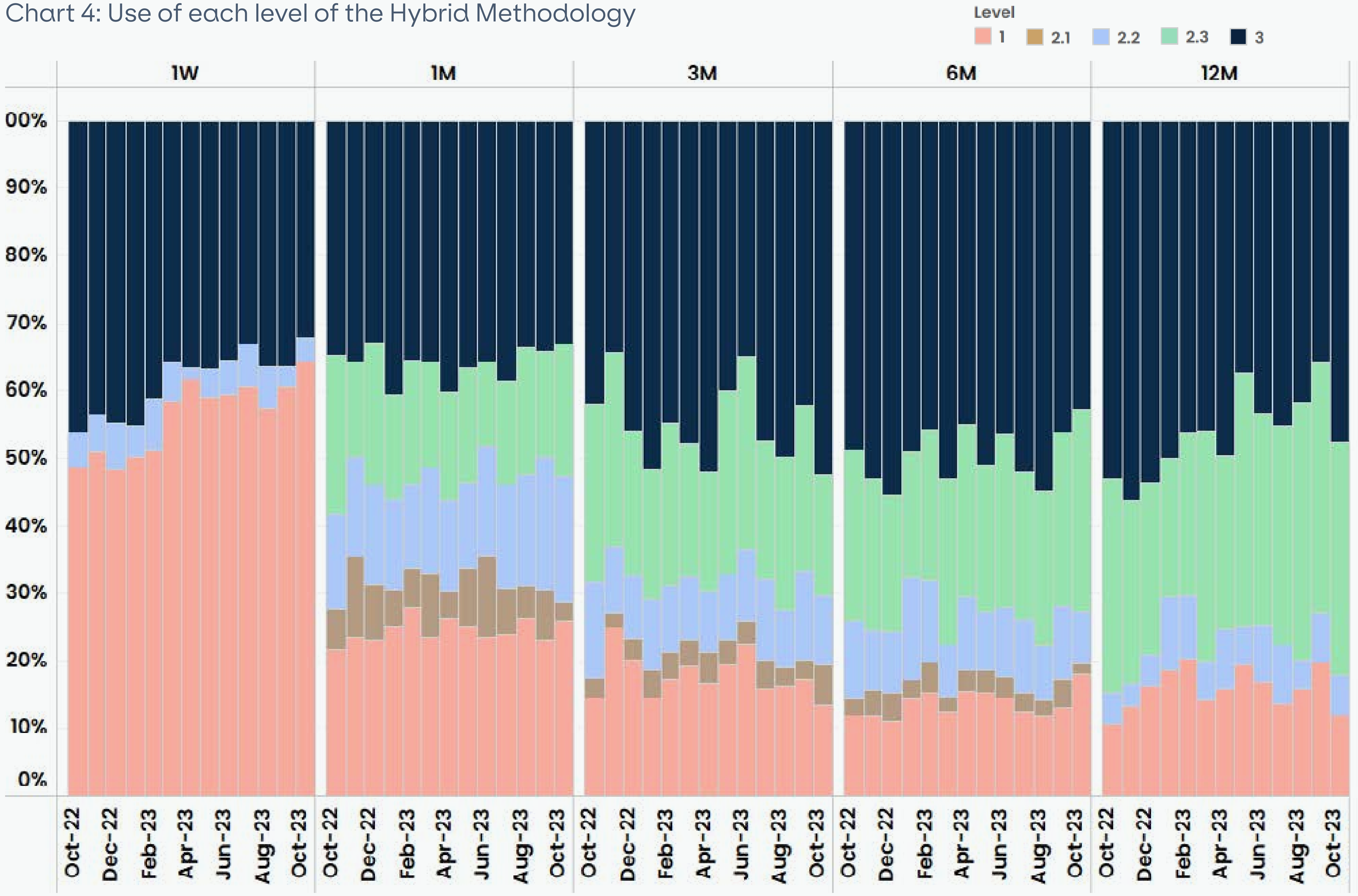
Chart 3 – Euribor underlying volumes



Source: The European Money Markets Institute

monetary policy decisions, TLTRO repayments, changes in excess liquidity, and shifts in interest rates and volumes across various tenors, all contributing to a nuanced and evolving financial landscape.

Chart 4: Use of each level of the Hybrid Methodology



Source: The European Money Markets Institute

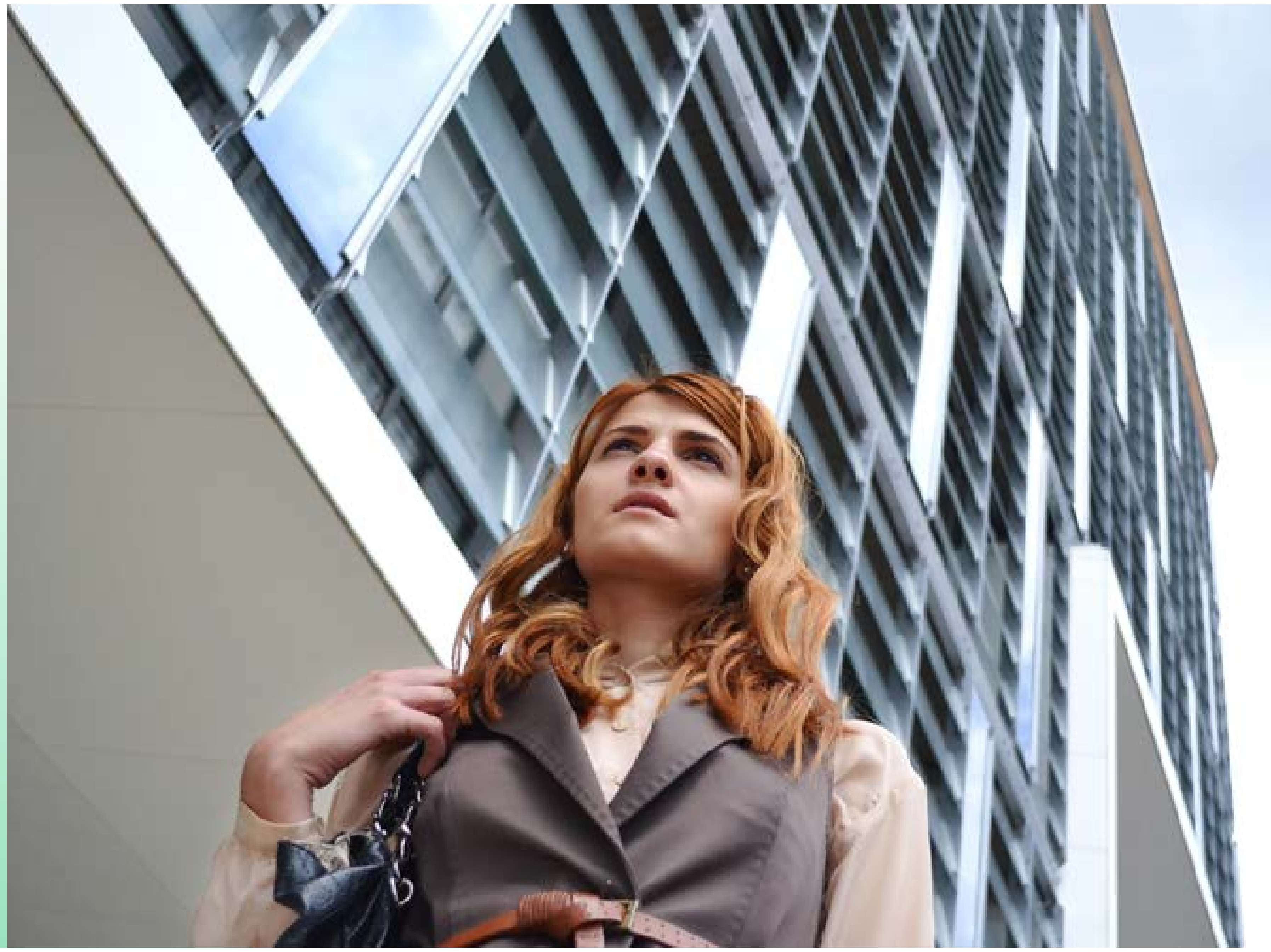
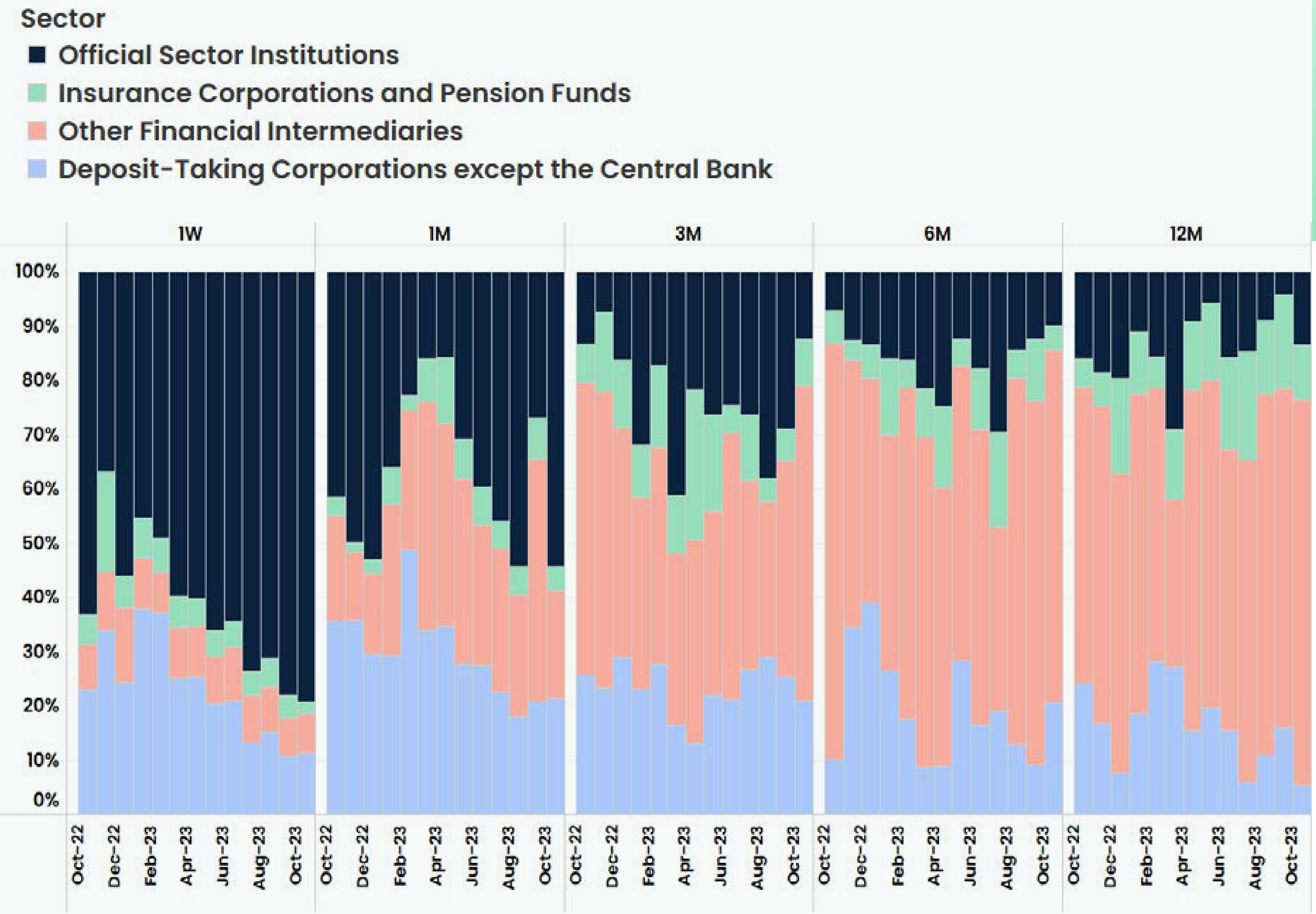
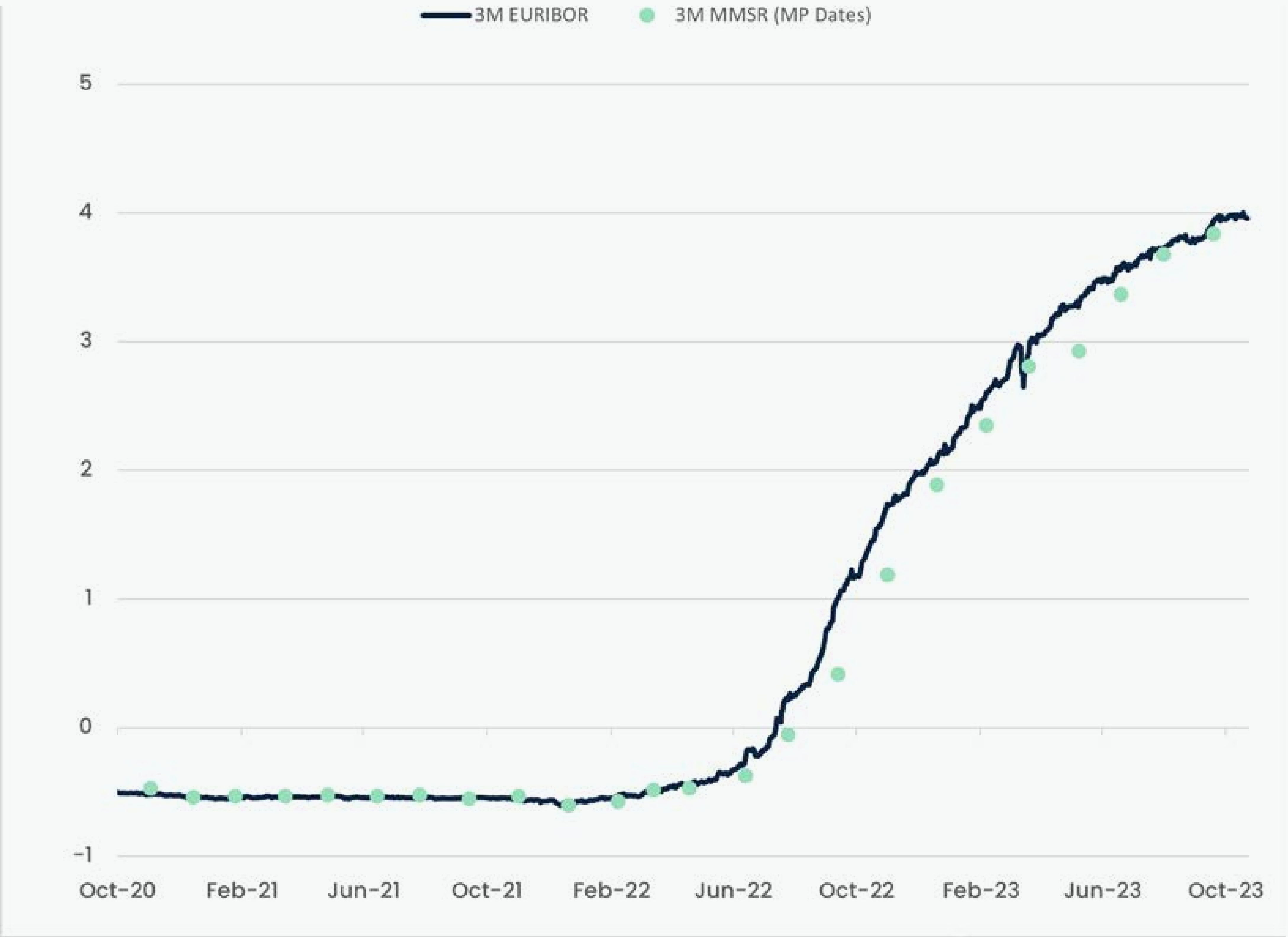


Chart 5: Counterparty sector share of volume in Euribor



Source: The European Money Markets Institute

Chart 6: 3-month compared to MMSR data.



Source: ECB, The European Money Markets Institute

Any questions?

For any enquiry or question related to our activities, please do not hesitate to contact us:

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The European Money Markets Institute