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The funding situation in the euro area – a few ECB remarks

ABI

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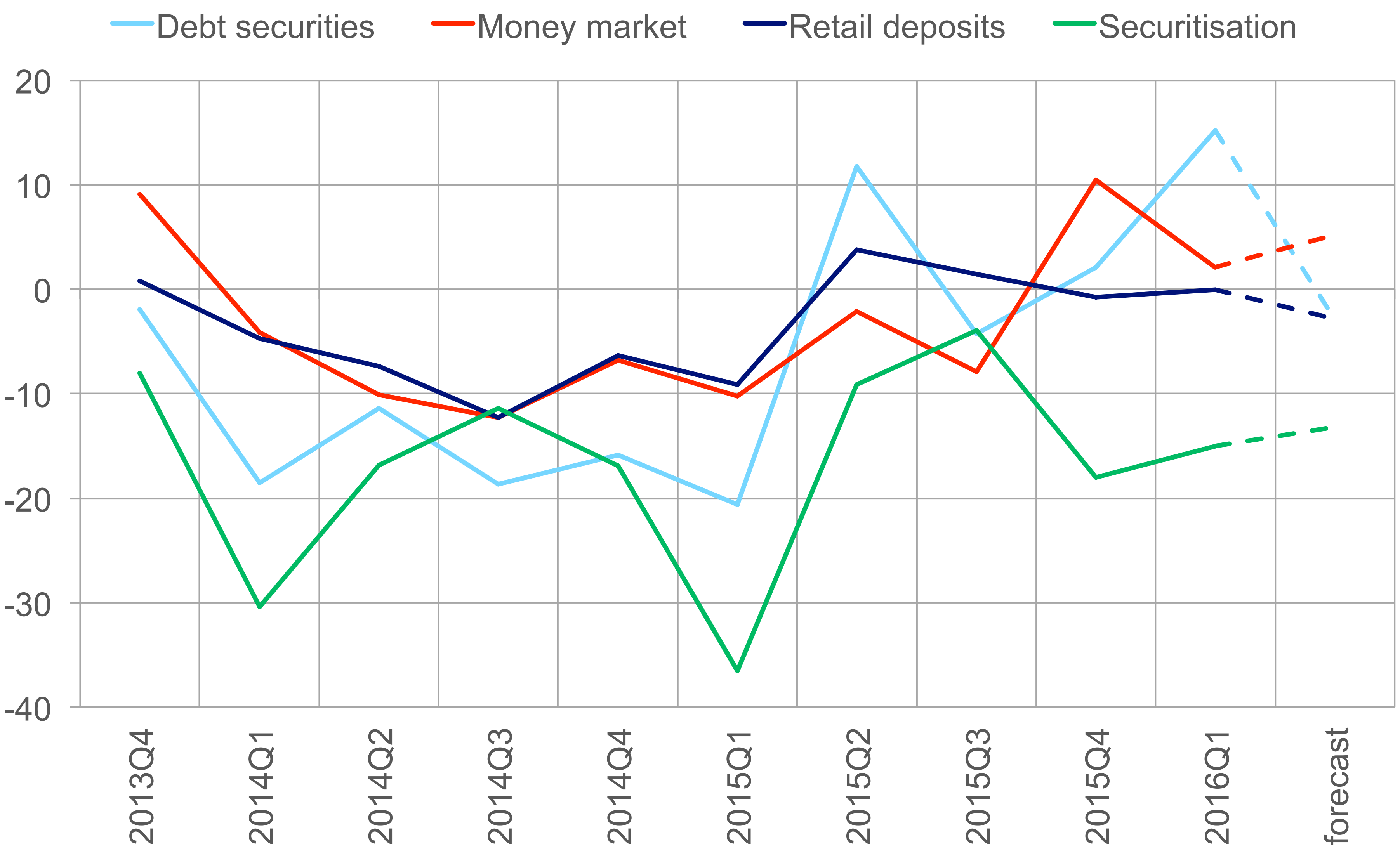
Overview

- The current funding situation
- The beauty of diversified funding
- EU policies affecting the funding environment
- Important for the euro area – risk sharing
- The Capital Markets Union (CMU)

The funding situation

- Funding is about risk and return, affected by three broad areas:
  - i) the prevailing economic business cycle, ii) current and future financial regulation, and iii) innovation and creativity in the industry.
- In addition, the CMU project has the potential to amend the funding situation, either through legislation or through promotion of market best practices.
- Financial markets are constantly innovating, and firms are constantly adapting to the new rules. Regulators are adapting to innovation (behind the curve) and future potential risks (ahead of the curve).
- We know that regulation is and will alter the funding situation for banks:
  - LCR, NSFR, BRRD, TLAC (G-SIBs), MREL (all banks)

Banks’ assessment of funding conditions



The Eurosystem in the funding environment

- In the past, the Eurosystem was generally a small player in the funding industry.
- This has changed during the crisis;
  - LTRO in late 2011 and early 2012
  - TLTRO I and TLTRO II => provides and will provide attractive stable funding for those banks that can channel it towards lending to the real economy.
  - Current holding in the APP: EUR 918 billion
- The monetary policy package has been effective:
- Since June 2014, we have seen a broad-based easing in money market conditions, long-term government bond yields, corporate and bank bond yields, bank lending rates to firms and households, and the growth of money and credit.

The CMU project

- We highly welcome the work on the CMU which aims at mobilizing capital by creating deeper and more integrated capital markets;
  - Will enhance the resilience of EMU and also contribute to smoother transmission of monetary policy across the euro area.
- Improve cross-border risk-sharing;
- Increase the shock-absorbing capacity => financial stability
- Target a vast number of items relevant for the funding, for both banks and non-banks, including both regulatory and non-regulatory actions.
- CMU will be key to supporting European growth by diversifying sources of funding and increasing companies’ access to financing, and unlock capital for sound lending.

Simple, Transparent and Standardised Securitisation

- Securitisation provides a unique and versatile nature as a funding tool.
- The ECB has a strong interest in the sustainable revival of the EU securitisation market. As an asset-based financing with the capacity both to channel flows of credit to the real economy and to transfer risk, securitisation has particular significance for the transmission mechanism of monetary policy.
- The development of a common set of rules across the EU regulatory framework for all securitisations is a significant step towards regulatory harmonisation and consistency.
- The ECB supports the establishment of criteria to identify a subset of STS securitisations.
- The proposed regulations strike the right balance between the need to revive the European securitisation market by making the securitisation framework more attractive for both issuers and investors, and the need to maintain the prudential nature of the regulatory framework.
- European securitisations with features broadly similar to the proposed STS securitisations suffered low levels of losses during the financial crisis. Consequently, it is appropriate for the regulatory framework to distinguish between them and more complex, opaque and bespoke securitisations.

What is holding back ABS issuance?

- Weak demand for credits creates lower funding needs;
- If used for funding, competing with other (cheaper) instruments and channels;
- Non level playing field compared with near-substitutes?
- Uncertain regulation - delayed processes for banks and insurers;
- Still perceived as a complex instrument

Improving the covered bond market

- The ECB is in favour of a high-quality and transparent EU covered bond market, and sees potential for harmonisation of some standards and practices across the EU.
- The ECB generally considers the existing covered bond frameworks to be well-functioning and recognises that many national legal frameworks for covered bonds are long-established.
- Common minimum standards should be introduced in areas where the benefits of harmonisation have been established. A sufficient degree of flexibility should remain to account for some diversity across national regimes where this would not endanger the objective of having a common framework that facilitates cross-border covered bond comparisons and market activity.
- Such initiatives should be coherent with other EU-level policy agendas and projects to promote high standards in European capital markets and instruments.
- The EC consultation revealed that a more integrated market for covered bonds could deliver a number of benefits in terms of better comparability between Member States and, as a result, deeper, more liquid and more robust national markets.

Potential structured changes to covered bonds

- Regulation and spill-over effects on covered bonds;
- EC consultation on a more integrated EU covered bond framework based on high quality standards and best market practices;

- Changes in covered bond structures:
  - Number of Conditional Pass Through Covered Bond programmes has increased, as well as number of soft bullet structures
    - ➢ More to come?
- Market-led initiatives (ECBC label and its HTT)
    - ➢ The covered bond label; Harmonized Transparency Template
    - ➢ The potential introduction of European Structured Notes