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LIQUIDITY CONDITIONS AND MONETARY POLICY OPERATIONS FROM MAINTENANCE PERIOD 1 TO MAINTENANCE PERIOD 5 OF 2019

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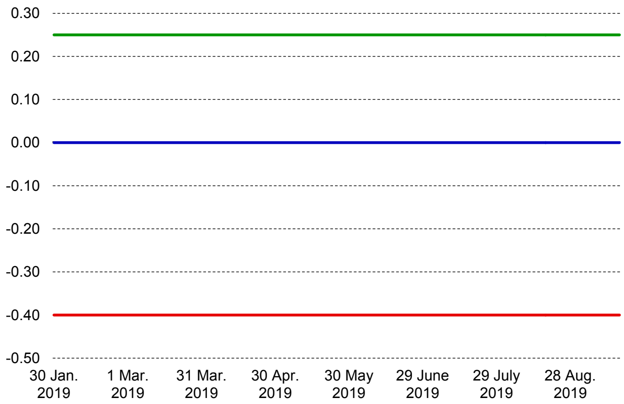
BOX 3: LIQUIDITY CONDITIONS AND MONETARY POLICY OPERATIONS FROM MAINTENANCE PERIOD 1 TO MAINTENANCE PERIOD 5 OF 2019[1,2]

Introduction

Chart 1
KEY INTEREST RATE DEVELOPMENTS
(per cent)



Source: Central Bank of Malta.

This box describes the liquidity conditions in the Maltese banking system and monetary policy operations conducted by the Central Bank of Malta, as part of the Eurosystem's single monetary policy framework during the first five maintenance periods (MP) of 2019, covering the period between 30 January and 17 September 2019. The period under consideration follows the beginning of the reinvestment phase of the APP, resulting in the Eurosystem purchasing public sector debt securities, covered bonds, asset-backed securities as well as corporate sector securities to replace maturing assets bought under the APP. In this regard, the Bank only participates in the Public Sector Purchase Programme (PSPP) component of the APP.

During the period under review, the key ECB interest rates, that is, the rates on the MROs, the marginal lending facility and the overnight deposit facility, remained unchanged at 0.00%, 0.25% and -0.40%, respectively (see Chart 1).

Excess liquidity

Throughout the period reviewed, the Maltese banking system was characterised by high levels of excess liquidity. Excess liquidity is defined as the amount of deposits placed by banks at the overnight deposit facility of the Central Bank of Malta, net of the recourse to the marginal lending facility, plus current account holdings, in excess of the minimum reserve requirements (excess reserves).

At the beginning of the period, excess liquidity stood at €4,487.4 million and remained relatively stable throughout the period reviewed, with a daily average of €4,263.8 million.

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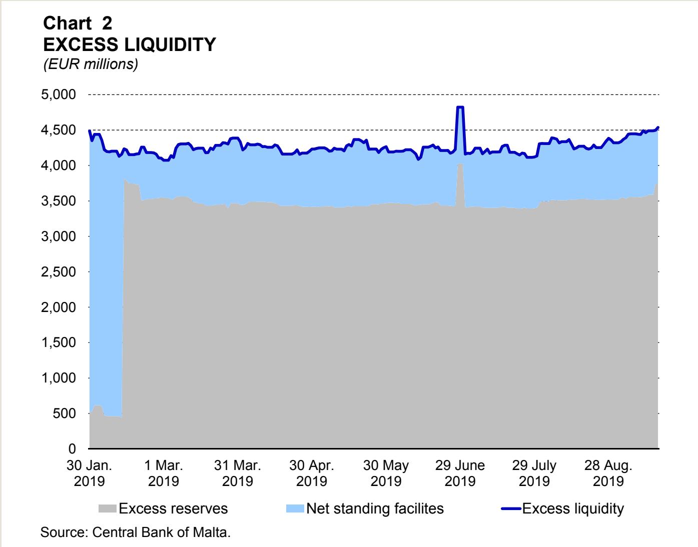
1 MP201901 (30 January-12 March); MP201902 (13 March-16 April); MP201903 (17 April-11 June); MP201904 (12 June-30 July); MP201905 (31 July-17 September).

2 Prepared by Ritlen Abela, Officer II, Monetary Operations and Collateral Management Office, and Nathan Chatland, Officer II, Monetary Operations and Collateral Management Office of the Central Bank of Malta and reviewed by Josette Grech, Manager, Monetary Operations and Collateral Management Office. The views expressed in the box are the authors' own and do not necessarily reflect the views of the Bank.

At the end of the period, excess liquidity stood at €4,536.9 million. The spike in excess liquidity that is illustrated in Chart 2 stemmed from excess reserves and is explained below.



At the beginning of the period, excess reserves stood at €511.9 million. Although they subsequently fluctuated slightly, excess reserves remained relatively stable around a daily average of €512.1 million up until mid-February. Following a shift from overnight deposits to excess reserves by one credit institution, excess reserves grew substantially, reaching €3,814.8 million on 13 February. Over the next few days, excess reserves fell gradually to €3,508.1 million, stabilising thereafter until the end of the fifth MP, averaging at €3,308.0 million. This stability was interrupted only temporarily by a significant current account deposit occurring on 28 June that boosted excess reserves to €4,027.7 million (refer to Chart 2). This deposit and subsequent withdrawal were the result of one bank temporarily depositing a higher amount in the current account at the end of the second quarter.

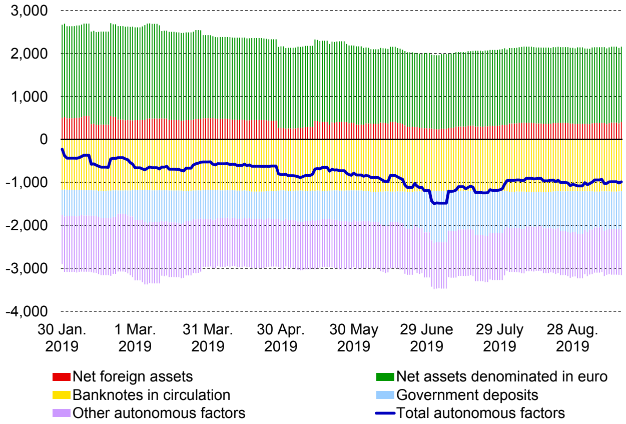
Developments in excess liquidity also reflect the use of standing facilities. Standing facilities are monetary policy instruments that facilitate the provision and absorption of overnight liquidity. The Eurosystem provides two types of standing facilities: the marginal lending facility and the overnight deposit facility. The marginal lending facility allows counterparties to borrow in order to meet short-term liquidity needs. On the other hand, the deposit facility allows counterparties to deposit overnight funds with the Eurosystem.

During the period reviewed, there was no utilisation of the marginal lending facility by local credit institutions.

During MP1, the balance on the overnight deposit facility stood at €3,975.5 million and remained relatively stable, with a daily average of €3,775.1 million until 12 February. Following the aforementioned shift from the overnight deposit facility to the current account, this figure fell to €420.4 million as at 13 February. Subsequently, the balance held in the overnight deposit facility followed an upward trend for the first few days and subsequently settled into a stable path, averaging €995.9 million for the period under consideration. By the end of the period, this figure stood at €790.7 million.

Autonomous liquidity factors

Chart 3
AUTONOMOUS FACTOR EVOLUTION BETWEEN MP1 AND MP5 2019[1]
(EUR millions)



Source: Central Bank of Malta.
[1] Liquidity-providing factors are shown in positive figures while liquidity-absorbing factors are in negative figures.

Autonomous liquidity factors are items in the central bank balance sheet that are neither monetary policy operations nor current account holdings of credit institutions. As the transactions driving autonomous factors involve central bank money, they have a liquidity-providing or liquidity-absorbing effect.[3,4] Essentially, increases in central bank assets entail the provision of liquidity, while increases in central bank liabilities involve the absorption of liquidity, and vice-versa.

Total autonomous factors were net liquidity-absorbing and stood at an average of -€531.0 million during MP1.[5] Autonomous factors continued to decline throughout MP4 reaching an average of -€1,161.5 million, before increasing slightly to an average of -€979.6 million during MP5 (see Chart 3).

The decline in autonomous factors was mainly the result of a drop in liquidity-providing factors, partially offset by a decrease in liquidity-absorbing factors. For the period under review, the average amount of liquidity provided via autonomous factors decreased by €485.0 million. This effect was mainly driven by a drop in net assets denominated in euro from an average of €2,163.6 million in MP1 to €1,764.3 million in MP5, as well as a fall in net foreign assets from an average value of €461.4 million in MP1 to €374.6 million in MP5. The average amount of liquidity absorbed via autonomous factors decreased by €36.3 million. This effect was mostly attributable to the effect of 'other autonomous factors' decreasing from €1,345.1 million in MP1 to €1,040.0 million in MP5. This decline was partially offset by increases in government deposits held with the Central Bank of Malta from an average value of €636.6 million in MP1 to €875.1 million in MP5 and in banknotes in circulation from an average of €1,182.3 million in MP1 to €1,212.6 million in MP5.

Monetary policy instruments

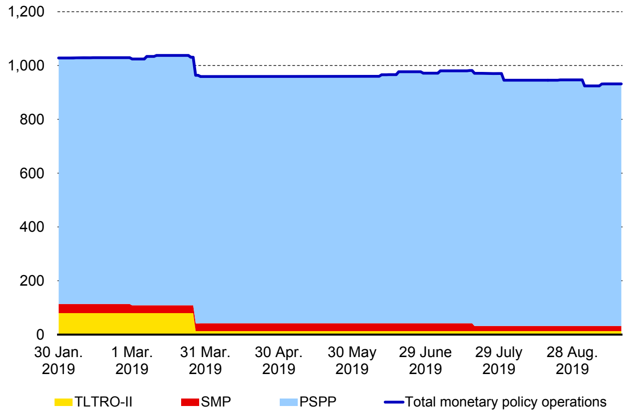
Open market operations

The Eurosystem uses open market operations to provide liquidity to monetary policy counterparties. During the period reviewed, given ample liquidity in the domestic banking

[3] Liquidity-providing factors include net foreign assets and net assets denominated in euro.
[4] Liquidity-absorbing factors consist of government deposits, banknotes in circulation and other autonomous factors.
[5] Given that total autonomous factors were net liquidity-absorbing, figures are depicted with a negative sign.

system, there was little participation by Maltese counterparties in such operations. In fact, there was no participation by Maltese banks in MROs except on 17 July when participation amounted to €1.0 million. Regarding the longer-term refinancing operations (LTRO), at the beginning of the period under review, there was an outstanding balance of €80.0 million from the TLTRO-II. On 27 March, voluntary early repayments for the TLTRO-II operations lowered the outstanding balance to €13.0 million. There was no participation by local banks in the 3-month LTRO during the period (see Chart 4).

Chart 4
EVOLUTION OF MONETARY POLICY OPERATIONS[1]
(EUR millions)



Source: Central Bank of Malta.
[1] There was minimal participation in the MRO and no participation in the 3-month LTRO.

Asset purchases

During MP1, the Central Bank of Malta's holdings of debt instruments under the Securities Markets Programme (SMP) stood at an average of €32.5 million.[6] These holdings subsequently declined, reflecting the maturing of securities, falling to an average value of €19.0 million in MP5.

PSPP holdings under the APP stood at an average of €916.6 million in MP1. These holdings remained relatively stable throughout, standing at an average value of €908.1 million in MP5. This change in volume reflects the net effect of the purchase of securities as well as the redemption of maturing securities that occurred in the interim.

[6] The SMP was announced by the Governing Council of the ECB on 10 May 2010, with the intention of ensuring depth and liquidity in malfunctioning segments of the debt securities markets and to restore an appropriate functioning of the monetary policy transmission mechanism. The SMP was terminated as from 6 September 2012 with the purchased securities held to maturity.