

Money Market Report for the week ending 28 July 2023

ECB Decisions

Inflation continues to decline but is still expected to remain too high for too long. The Governing Council of the European Central Bank (ECB) is determined to ensure that inflation returns to its 2% medium-term target in a timely manner. Therefore, on 27 July 2023, it decided to raise the three key ECB interest rates by 25 basis points. Accordingly, the interest rate on the main refinancing operations (MRO) and the interest rates on the marginal lending facility and the deposit facility will be increased to 4.25%, 4.50% and 3.75%, respectively, with effect from 2 August 2023.

This rate increase reflects the Governing Council's assessment of the inflation outlook, the dynamics of underlying inflation, and the strength of monetary policy transmission. The developments since the last meeting support the expectation that inflation will drop further over the remainder of the year but will stay above target for an extended period. While some measures show signs of easing, underlying inflation remains high overall. The past rate increases continue to be transmitted forcefully: financing conditions have tightened again and are increasingly dampening demand, which is an important factor in bringing inflation back to target.

The Governing Council also decided to set the remuneration of minimum reserves at 0% effective as of the beginning of the reserve maintenance period starting on 20 September 2023. This decision will preserve the effectiveness of monetary policy by maintaining the current degree of control over the monetary policy stance and ensuring the full pass-through of the interest rate decisions to money markets. At the same time, it will improve the efficiency of monetary policy by reducing the overall amount of interest that needs to be paid on reserves to implement the appropriate stance.

As concerns the pandemic emergency purchase programme (PEPP), the Governing Council intends to reinvest the principal payments from maturing securities purchased under the programme until at least the end of 2024. In any case, the future roll-off of the PEPP portfolio will be managed to avoid interference with the appropriate monetary policy stance. The Governing Council will continue applying flexibility in reinvesting redemptions coming due in the PEPP portfolio, with a view to countering risks to the monetary policy transmission mechanism related to the pandemic.

The Governing Council stands ready to adjust all of its instruments within its mandate to ensure that inflation returns to its 2% target over the medium term and to preserve the smooth functioning of monetary policy transmission. Moreover, the Transmission Protection Instrument is available to counter unwarranted, disorderly market dynamics that pose a serious threat to the transmission of monetary policy across all euro area countries, thus allowing the Governing Council to more effectively deliver on its price stability mandate.

ECB Monetary Operations

On 24 July 2023, the ECB announced the 7-day MRO. The operation was conducted on 25 July 2023 and attracted bids from euro area eligible counterparties of €11,035.50 million, €1,011.00 million more than the previous week. The amount was allotted in full at a fixed rate equivalent to the prevailing MRO rate of 4.00%, in accordance with current ECB policy.

On 26 July 2023, the ECB conducted the three-month, longer-term refinancing operation to be settled as a fixed rate tender procedure with full allotment, with the rate fixed at the

average MRO rate over the life of the operation. The operation attracted bids of €3,165.00 million from euro area eligible counterparties.

Also on 26 July 2023, the ECB conducted the 7-day US dollar funding operation through collateralised lending in conjunction with the US Federal Reserve. This operation attracted bids of \$223.70 million, which was allotted in full at a fixed rate of 5.58%.

Domestic Treasury Bill Market

In the domestic primary market for Treasury bills, the Treasury invited tenders for 91-day and 273-day bills for settlement value 27 July 2023, maturing on 26 October 2023 and 25 April 2024, respectively. Bids of €285.93 million were submitted for the 91-day bills, with the Treasury accepting €7.01 million, while bids of €57.37 million were submitted for the 273-day bills, with the Treasury accepting €13.06 million. Since €54.91 million worth of bills matured during the week, the outstanding balance of Treasury bills decreased by €34.84 million, standing at €846.25 million.

The yield from the 91-day bill auction was 3.014%, decreasing by 24.20 basis points from bids with a similar tenor issued on 20 July 2023, representing a bid price of €99.2439 per €100 nominal. The yield from the 273-day bill auction was 3.168%, decreasing by 1.10 basis points from bids with a similar tenor issued on 11 May 2023, representing a bid price of €97.6540 per €100 nominal.

During this week, there was no trading on the Malta Stock Exchange.

This week the Treasury will invite tenders for 91-day and 182-day bills maturing on 2 November 2023 and 1 February 2024, respectively.