ECB-PUBLIC

Mario DRAGHI
President

Mr Fabio De Masi
Member of the European Parliament
European Parliament
60, rue Wiertz
B-1047 Brussels

Frankfurt, 4 April 2016

L/MD/16/166

Re: Your letter (QZ-020)

Honourable Member of the European Parliament, dear Mr De Masi,

Thank you for your letter, which was passed on to me by Mr Roberto Gualtieri, Chairman of the Committee on Economic and Monetary Affairs, accompanied by a cover letter dated 2 March 2016.

Since March 2015, the Eurosystem has been buying eligible sovereign and private sector bonds at a pace of, on average, EUR 60 billion per month under the expanded asset purchase programme (APP). The two largest programmes under the APP so far are the public sector purchase programme (PSPP) and the third covered bond purchase programme (CBPP3). Both the PSPP and the CBPP3 are implemented in a decentralised manner by the Eurosystem. The smallest programme under the APP is the asset-backed securities purchase programme (ABSPP), which is implemented in a more centralised manner, with asset managers purchasing asset-backed securities on the instructions of the European Central Bank (ECB).

To be eligible for purchase under the APP, bonds need to meet strict criteria. First, as a rule they need to be eligible as collateral for monetary policy operations, as specified in Guideline ECB/2014/60.[1] Second, they must satisfy certain additional requirements, depending on the specific programme under which they are to be purchased.

[1] Guideline (EU) 2015/510 on the implementation of the Eurosystem monetary policy framework (ECB/2014/60), available on the ECB's website at: https://www.ecb.europa.eu/ecb/legal/pdf/oj_jol_2015_091_r_0002_en_txt.pdf

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In particular, in order to be eligible as collateral and for purchase under the PSPP and CBPP3, at least one of the bond ratings, as rated by one of the credit rating agencies accepted by the ECB, should, as a rule, be investment grade (BBB- or equivalent, or above). In the case of government-linked assets, this rating requirement can be waived by the Governing Council if the country of the government issuing or guaranteeing such assets is under a financial assistance programme which is "on track". This is provided for in Article 8 of Guideline ECB/2014/31[2] which applies to eligibility under both the Eurosystem's collateral framework and the PSPP. In the case of covered bonds issued in Greece (and in Cyprus) which carry no investment-grade rating, additional requirements must be satisfied in order to achieve risk equivalence; this allows, allowing certain of these covered bonds to be eligible for the CBPP3. [3]

In the case of purchases of asset-backed securities (ABS) under the ABSPP, two credit assessments on an asset basis corresponding to credit quality step 3 in the Eurosystem credit assessment framework (BBB- or equivalent) are required, and additional eligibility criteria as specified in Article 2 of Decision ECB/2014/45 [4] apply. Furthermore, prior to the purchase of any ABS fulfilling the eligibility criteria, the ECB conducts a credit risk assessment and due diligence of the ABS, as set out in Article 3 of Decision ECB/2014/45. For ABS with no investment-grade rating, where the obligors of the cash-flow generating assets are located in Greece or in Cyprus, additional requirements must be satisfied in order to achieve risk equivalence (see Article 2(8) of Decision ECB/2014/45).

According to Guideline ECB/2014/60 mentioned above, and as can be seen in the list of eligible marketable assets that the ECB publishes daily on its website (except on TARGET2 closing days)[5], Deutsche Bank covered bonds are eligible as collateral and for purchase under the CBPP3. As is the case for any eligible bond, these covered bonds must comply with the eligibility criteria described above and laid out in the Decision on the implementation of the CBPP3 (ECB/2014/40), referred to above. Let me add that I have already had the opportunity of discussing the criteria for the eligibility of Greek government-related debt instruments as collateral for Eurosystem credit operations in a letter I sent to your colleague, Ms Paloma López Bermejo, on 13 April 2015.[6]

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[2] Guideline on additional temporary measures relating to Eurosystem refinancing operations and eligibility of collateral and amending Guideline ECB/2007/9 (ECB/2014/31), available on the ECB's website at: https://www.ecb.europa.eu/ecb/legal/pdf/ecb_2014_31_f_signed.pdf

[3] See Article 2 of the ECB's Decision on the implementation of the third covered bond purchase programme (ECB/2014/40), available on the ECB's website at https://www.ecb.europa.eu/ecb/legal/pdf/oj-jol_2014_335_r_0010-en-txt.pdf

[4] Decision on the implementation of the asset-backed securities purchase programme (ECB/2014/45), available on the ECB's website at: https://www.ecb.europa.eu/ecb/legal/pdf/en_ecb_2014_45_f_sign.pdf

[5] See http://www.ecb.europa.eu/mopo/assets/html/index.en.html

[6] The letter is available on the ECB's website at: https://www.ecb.europa.eu/pub/pdf/other/150415letter_bermejo.en.pdf

Concerning your question as to whether the ECB is considering a change in collateral policy regarding bank bonds, please note that the ECB is, as always, closely observing developments in EU legislation and markets, including in the Bank Recovery and Resolution Directive (BRRD) and the Single Resolution Mechanism Regulation. With a view to maintaining and enhancing the effectiveness of monetary policy and providing for a level playing field between eligible counterparties, the Eurosystem may adjust its collateral framework from time to time, taking into account policy, legal and risk management considerations.

In addition, as part of its advisory function, the ECB may highlight the possible implications of draft legislative provisions on collateral policy or other areas of its field of competence. For example, in paragraph 3.3 of its Opinion on the draft German law on bank resolution[7] the ECB explained that, according to Article 64 of Guideline ECB/2014/60, eligible debt instruments must not give rise to rights to the principal and/or the interest that are subordinated to the rights of holders of other debt instruments of the same issuer. Therefore, bank debt instruments subject to a statutory subordination of the kind proposed in the draft German law would no longer be eligible as collateral for Eurosystem credit operations (under the then-current rules of the Eurosystem). The ECB also noted, in its opinion on the draft French law on the hierarchy of creditors of credit institutions[8], that, under the law as proposed, newly issued French senior non-preferred debt instruments would also not be eligible as collateral for Eurosystem credit operations under the current rules of the Eurosystem, because of the subordination of senior non-preferred debt instruments to senior preferred debt.

To complete the answers to your questions, let me clarify that there is no general exemption in the BRRD for bonds held by a central bank, provided that they are unsecured and have a remaining maturity of more than seven days. Similarly to other creditors in the same situation, central banks would only be protected by the "no-creditor-worse-off" safeguard. Therefore, if a bank enters into resolution and the bail-in is applied, the bonds held by the ECB would be bailed in alongside other bonds of equal creditor ranking insofar as this would be needed to ensure an orderly resolution.

Yours sincerely,

[signed]

Mario Draghi

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[7] Opinion of 2 September 2015 on bank resolution (CON/2015/31), available on the ECB's website at: https://www.ecb.europa.eu/ecb/legal/pdf/en_con_2015_31_f_sign.pdf

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[8] Opinion of 23 February 2016 on the hierarchy of creditors of credit institutions (CON/2016/7). The document is available on the ECB's w ebsite at: https://w w w .ecb.europa.eu/ecb/legal/pdf/en_con_2016_7_f_sign.pdf