REPORT ON MONETARY POLICY IMPLEMENTATION

Lisboa, 2023

Report on Monetary Policy Implementation | 2023 • **Banco de Portugal** Rua do Comércio 148, 1100-050 Lisboa | 1100-150 Lisboa • www.bportugal.pt • **Edition** Markets Department • **Design** Communication and Museum Department | Design Unit

Executive summary

In 2022, the euro area experienced a significant and widespread increase in inflation, which markedly influenced policy actions by the European Central Bank (ECB). In this context, the ECB announced the end of net purchases under the asset purchase programme (APP) as well as the phasing-out of reinvestments and started raising key interest rates.

The first increase in key ECB interest rates, by 0.5 p.p., took place in July and marked the end of the negative interest rate environment that had been in place since 2014. Official interest rates continued to increase at the three subsequent monetary policy meetings and, at the end of the year, the interest rate on the deposit facility stood at 2%, the interest rate on the main refinancing operations at 2.5% and the interest rate on the marginal lending facility at 2.75%.

The ECB also established the Transmission Protection Mechanism (TPI), a tool designed to prevent fragmentation, especially during the monetary policy normalisation process. The Eurosystem may use the TPI to conduct secondary market purchases of securities issued in jurisdictions experiencing an unjustified deterioration in financing conditions that poses a serious threat to the transmission of monetary policy in the euro area.

The rate to be applied to TLTRO III and the remuneration of credit institutions' minimum reserves and government deposits held with the Eurosystem were also revisited, as the process of monetary policy normalisation progressed and interest rates entered positive territory.

In March 2022, the ECB also announced the gradual phasing-out, between July 2022 and March 2024, of the temporary collateral easing and risk control measures adopted during the pandemic crisis.

In line with the tightening of monetary policy, the amounts obtained by Portuguese counterparties from the Banco de Portugal in liquidity-providing monetary policy operations decreased considerably. At the end of 2022, it amounted to €16 billion, almost all of which under TLTRO, compared with €41.8 billion at the end of the previous year. This decrease in credit granted was also reflected in the assets provided as collateral for these operations, which decreased noticeably towards the end of the year, both in Portugal and in the euro area. In Portugal, at the end of 2022, the total value of the assets used as collateral amounted to €61 billion, a €12 billion decrease (-17%) from the end of 2021. Despite this decrease, the collateral buffer increased considerably, given the much larger reduction in credit granted.

Recourse to the deposit facility increased significantly, both with the Banco de Portugal and the Eurosystem, driven by its positive remuneration and the context of excess liquidity, with almost all excess reserves being transferred to this facility in the last months of the year.

At the end of 2022, securities purchased for monetary policy purposes recorded on the Banco de Portugal's balance sheet amounted to €86 billion, 98% of which corresponded to public debt and debt issued by supranational entities. Portuguese public debt securities accounted for 2.2% and 2.3% of total government securities held by the Eurosystem under the PSPP and PEPP respectively, close to the Banco de Portugal's share of the Eurosystem capital key (2.34%).

The normalisation of monetary policy had implications for the Banco de Portugal's balance sheet, impacting its size, mainly due to the decrease in funding to credit institutions through early repayments of TLTRO III. At the end of 2022, the Banco de Portugal's balance sheet totalled €198 billion, compared with €219 billion at the end of 2021.

Monetary policy implementation **2022**

MONETARY POLICY DECISIONS

APR

End of net purchases under the PEPP
(Dec 2021 decision)

JUL

End of net purchases under the APP

First increase in key ECB interest rates

TPI announcement

SEP

Interest rate increase

Adjustment of remuneration of government deposits

Tiering system suspension

NOV

Interest rate increase

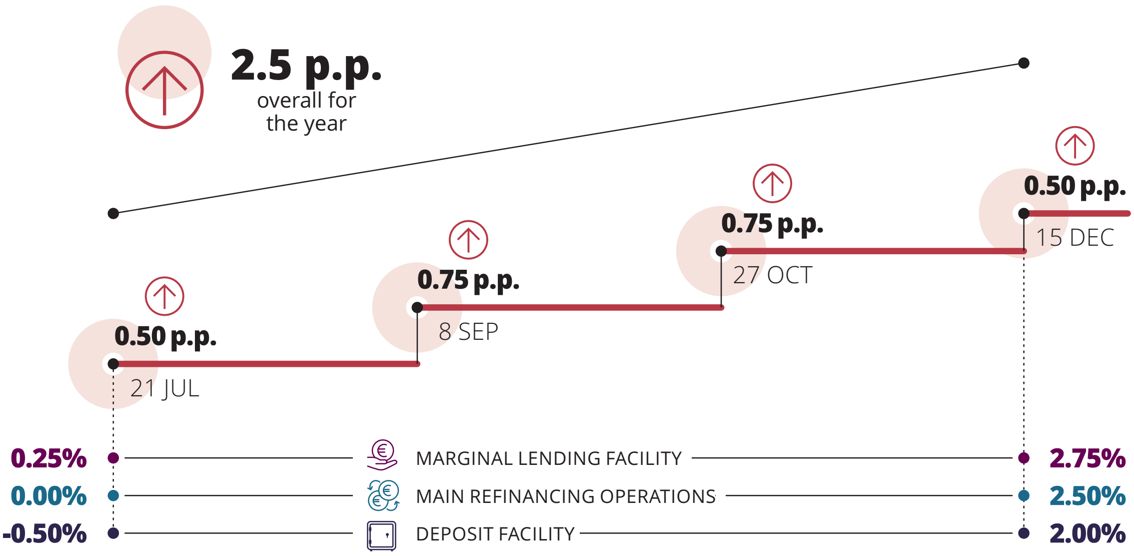
Adjustment of TLTRO III interest rate

DEC

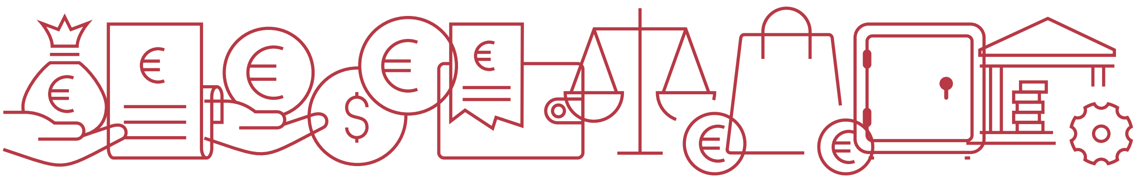
Interest rate increase

Adjustment of remuneration of minimum reserves

Increase in key ECB interest rates



The inflation surge in the euro area markedly influenced the ECB's monetary policy decisions. In 2022 the ECB continued the monetary policy normalisation process initiated at the end of 2021, raising key interest rates by 2.5 p.p. over the year.



MONETARY POLICY IMPLEMENTATION IN PORTUGAL

Monetary policy counterparties

36 counterparties ↑ **3**

Among the existing counterparties at the end of 2022, 11 had outstanding liquidity-providing operations, four less than in 2021.

Banco de Portugal's balance sheet

€ 198 billion ↓ **9.7%**

2022 | 2021

The reduction observed is mostly explained by the decrease in long-term financing to credit institutions, namely early repayments of TLTROs.

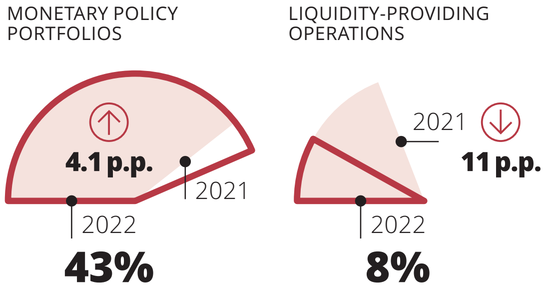
Liquidity provision

€ 16 billion ↓ **61.7%**

2022 | 2021

Almost all the liquidity-providing operations were TLTROs. The reduction compared to 2021 was mainly due to the early repayment of those operations.

Share of monetary policy portfolios and liquidity-providing operations in the Banco de Portugal's balance sheet



The two items represented around 52% on the asset side of the Banco de Portugal's balance sheet (59% in 2021).

Collateral

€ 61 billion ↓ **16.9%**

2022 | 2021

Covered bonds and bank loans are the asset types most used by Portuguese counterparties.

Average balance of the deposit facility

€ 80 billion | **€ 56 billion**

2021 | 2022

The use of this instrument went from occasional in 2021 to considerably higher amounts as of 14 September 2022, when its interest rate became positive.

Stock of securities acquired in purchase programmes

€ 86 billion ↓ **0.2%**

2022 | 2021

Of this amount, 98% corresponded to Portuguese public debt and debt issued by supranational institutions.

Net purchases of Portuguese public debt

€ 3.1 billion ↓ **84.5%**

2022 | 2021

The net value of government debt securities purchased by the Banco de Portugal decreased relative to previous years, reflecting the end of net asset purchases.

Excess liquidity in the Portuguese banking system

€ 42.3 billion ↓ **24.5%**

2022 | 2021

The reduction in the average excess liquidity of the banking system reflects the use of part of banks' excess liquidity to finance early repayments of TLTRO III operations.