



**EUROPEAN CENTRAL BANK**  
EUROSYSTEM

**ECB-PUBLIC**

*COURTESY TRANSLATION*

Mario DRAGHI  
President

Mr Marco Valli and Mr Marco Zanni  
Members of the European Parliament  
European Parliament  
60, rue Wiertz  
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Frankfurt, 18 January 2017

L/MD/17/34

**Re: Your letter (QZ-120)**

Honourable Members of the European Parliament, dear Mr Valli and Mr Zanni,

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 8 December 2016.

As conveyed in my reply to your honourable colleague MEP Markus Ferber on 28 November 2016,<sup>1</sup> the recent increase in TARGET2 balances largely reflects liquidity flows stemming from the ECB's asset purchase programme (APP). TARGET2 balances have been increasing since the start of the APP owing, in part, to technical factors related to the structure of financial markets. In particular, settlement services are concentrated in some financial centres. Cross-border payments by national central banks for securities purchased under the APP give rise to changes in TARGET2 balances in the course of the implementation of monetary policy. Almost 80% of bonds purchased by national central banks under the APP were sold by counterparties that are not resident in the same country as the purchasing national central bank, and roughly half of the purchases were from counterparties located outside the euro area, most of which mainly access the TARGET2 payments system via the Deutsche Bundesbank. This, in turn, resulted in an increase in the

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<sup>1</sup> Monetary dialogue with Mario Draghi, President of the ECB, November 2016. A transcript is available at [https://www.ecb.europa.eu/press/key/date/2016/html/sp161128\\_1\\_Transcript\\_and\\_QandA.en.pdf?a3cfb1ef2628076b85170d60ff935127](https://www.ecb.europa.eu/press/key/date/2016/html/sp161128_1_Transcript_and_QandA.en.pdf?a3cfb1ef2628076b85170d60ff935127)

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Deutsche Bundesbank's TARGET2 balance vis-à-vis the ECB. This particular mechanism is explained in more detail in our Economic Bulletin and in the Bundesbank's Monthly Report.<sup>2</sup>

Furthermore, TARGET2 balances remain elevated as the liquidity created by our APP is largely concentrated in particular countries. This is a reflection of the financial structure in the euro area, in which banks with business models that attract more liquidity holdings are typically located in a small number of financial centres. Looking beyond the implementation of our policy, the purchasing of assets in the context of the APP encourages the underlying sellers of these assets to rebalance their portfolios. As the sellers also make other forms of investment or purchase other securities, including non-domestic securities, additional liquidity flows occur, which contribute to keeping TARGET2 balances elevated.

The current upward trend in balances is therefore distinct from the increase in balances observed from mid-2007 to late 2008, and again from mid-2011 to mid-2012. The increase in TARGET2 balances in those periods was rooted in the market stress and fragmentation that resulted from the financial and sovereign debt crises. As banks in certain countries lost access to market-based funding, they replaced private sources of funding with central bank liquidity obtained from their national central banks through repurchase operations. The subsequent redistribution of this liquidity, which was heavily influenced by market stress, led to higher TARGET2 balances. However, the current increase in TARGET2 balances is not a symptom of increased stress and is therefore inherently different from the previous episodes of rising balances. It follows that TARGET2 balances per se are neither indicative of market fragmentation, nor necessarily an indicator of imbalances that could affect a country's macroeconomic fundamentals. The ECB continues to monitor TARGET2 balances closely.

If a country were to leave the Eurosystem, its national central bank's claims on or liabilities to the ECB would need to be settled in full.

Yours sincerely,  
[signed]

Mario Draghi

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<sup>2</sup> See the box entitled "TARGET balances and the asset purchase programme", *Economic Bulletin*, Issue 7, ECB, 2016, available at <http://www.ecb.europa.eu/pub/pdf/ecbu/eb201607.en.pdf> and the box entitled "The impact of Eurosystem securities purchases on the TARGET2 balances", *Monthly Report*, Vol. 68, No 3, Deutsche Bundesbank, March 2016, available at [https://www.bundesbank.de/Redaktion/EN/Downloads/Publications/Monthly\\_Report/2016/2016\\_03\\_monthly\\_report.pdf?\\_blob=publicationFile](https://www.bundesbank.de/Redaktion/EN/Downloads/Publications/Monthly_Report/2016/2016_03_monthly_report.pdf?_blob=publicationFile).