EUROPEAN CENTRAL BANK

EUROSYSTEM

DIRECTORATE GENERAL MACROPRUDENTIAL POLICY AND FINANCIAL STABILITY

FINANCIAL STABILITY CONTACT GROUP

FRANKFURT AM MAIN, WEDNESDAY, 24 APRIL 2024

MEETING SUMMARY

1) Why is financial market sentiment so benign?

Nearly all Financial Stability Contact Group (FSCG) members thought financial stability conditions in the euro area had either improved or had remained unchanged since the November 2023 publication of the ECB's Financial Stability Review. Most attributed benign financial market sentiment to improved macroeconomic conditions in the euro area and the US. However, some members thought financial markets had been overly exuberant, going beyond the improvement of fundamentals. Rising geopolitical tensions and persistence of US inflation above 2% were seen as the most plausible triggers for a shift in financial market sentiment. Some members were anticipating abrupt asset price adjustments and increased volatility in euro area equity, credit and commercial real estate markets but did not consider upcoming challenges a threat to euro area financial stability. Historically high concentration of market capitalisations of individual firms in US and euro area equity markets were seen as leaving these markets vulnerable to large price swings in single name securities, the trigger for which could be earnings disappointments. Some members were anticipating a widening of spreads and increased volatility in euro area credit markets. However, they saw the challenges ahead as idiosyncratic rather than systemic. Experts on commercial real estate (CRE) markets saw problems in these markets as lying ahead, rather than being behind. They were anticipating further price declines once transactions picked up. However, most members were not especially concerned about the financial systems' exposure to CRE assets.

2) The financial stability implications of structural shifts in the economy and financial system.

Members discussed key structural macrofinancial trends that were considered important from a financial stability perspective. Many saw the shift that has been taking place to a more intangible economy and the constellation of lower reliance of businesses on debt-funding together with higher public sector funding requirements as being important structural trends from a financial stability perspective. They also discussed changing demographics, deglobalisation, maturity extension and a shift to more fixed-term structures in global debt and mortgage markets, increased market capitalisation concentration in global equity markets, and the growth of private credit and equity markets. The shift to a more intangible economy, reduced reliance on debt-financing by the private sector, and structural shifts in debt and mortgage markets were seen by some as contributing to reducing the effectiveness of monetary policy over time by making transmission lags longer and more variable.