SUOMEN PANKKI EUROJÄRJESTELMÄ FINLANDS BANK EUROSYSTEMET

A new dawn, a new day, a new life for monetary policy implementation

Bank of Finland & SUERF Conference on Monetary Policy Implementation: Old Wisdoms and New Trends

11 June 2025

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Where we stand: the ECB's March 2024 OFR Decisions

We know there are several approaches to control short-term rates…

Fed	Supply-driven floor, "ample" reserves
BoE, ECB	Demand-driven floors
Riksbank, Norges Bank	Corridor systems
BoC, BoJ	Floor systems

Clearly, the framework choice must be guided by also other considerations than rate control!

What did the ECB GovC decide on March 2024?

1. Deposit facility rate (DFR) confirmed as **main instrument**; narrower spread but **incentives for market activity**.

2. **Mix of instruments** to supply reserves; **structural operations** introduced.

3. Balance sheet to **adjust gradually** towards new normal; **next review** in 2026.

Natural vs. Optimal Balance Sheet size, and how to Get There?

- ***Natural* balance sheet size**: fulfills structural liquidity deficit
- ***Optimal* balance sheet size**: reflects also policy objectives
- Natural and optimal do not often coincide; balance sheet size depends on past and present policy needs
- If policy needs fulfilled by solely steering short rates, can move gradually towards the natural size

Illustration for the ECB case: moving towards natural

Stylised breakdown of reserve supply over time

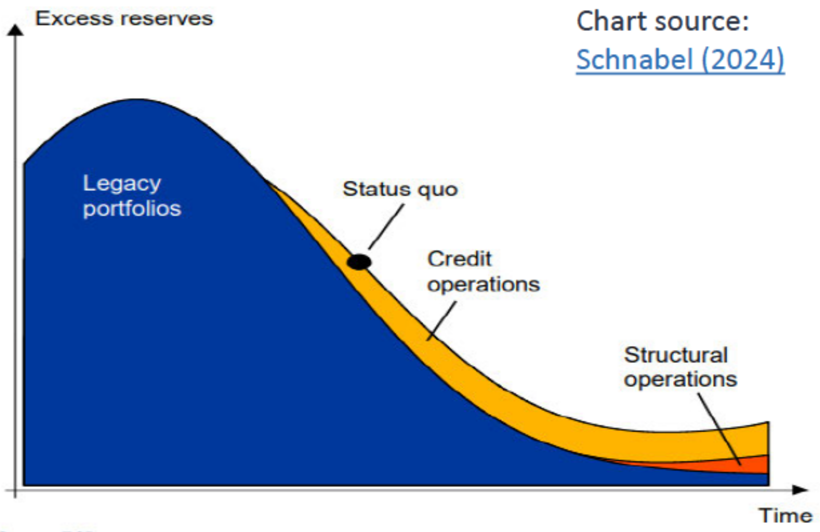


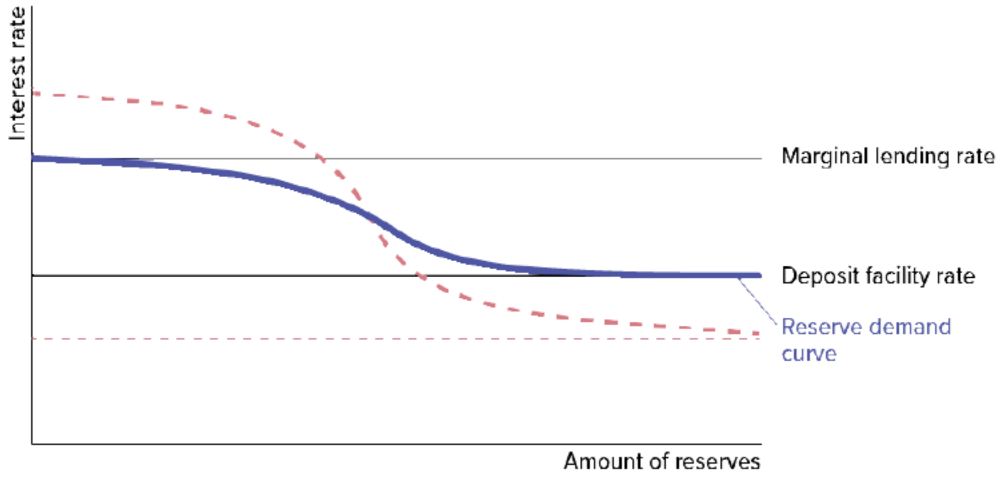
Chart source: Schnabel (2024)

Source: ECB.

To monitor during transition: Activity in money markets and credit operations, QT absorption

Designing Central Bank Liquidity Tools

- A good principle would be to use separate tools for separate purposes: *rate steering* operations vs. *financial stability* operations
- Using the euro area as an example, this would mean something like this:
  - Rate steering operations: flexible with short maturity, fixed-rate full alloment (FRFA), HQLA collateral
  - Financial stability operations: longer maturity, competitive bidding, broader collateral
  - Essential: no stigma!



Additional choice: corridor width, depending on central bank preferences

What Is the Role of Reserves?

Minimum reserve requirements (MRR)

- In a corridor system with a lean balance sheet, MRR help limit volatility and can be market neutral
- With ample reserves, MRR is not really needed
- Instead of MRR, liquidity regulation is taken care of by LCR and enhanced supervision
- Whatever the purpose of MRR, we should be clear and transparent about it

Interaction: reserves and transmission

- Implementation affects reserves, does it matter for policy transmission?
- Interest rates remain our main tool, can compensate stance effects of reserves, if they exist
- Pre-GFC, credit intermediation worked well even with little reserves
- If banks want to hold more reserves as safe assets, we should let them do so—but in a market neutral way

Concluding remarks

The Eurosystem's operational framework is solid but evolving.

Many questions remain open—as highlighted throughout this presentation.

The ECB's review in 2026 is a shared opportunity—your contributions matter!

Thank you!

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