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CORE ANALYSIS

# The legal nature of market neutrality in the euro area's monetary policy

Javier Solana[†] and Marco Goldoni[††]

University of Glasgow, Glasgow, UK
**Corresponding author:** Javier Solana; Email: javier.solana@glasgow.ac.uk

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**Abstract**
European Central Bank (ECB) staff have repeatedly justified the carbon bias of the Asset Purchase Programme (APP) in terms of "market neutrality". Yet this term is not included in the Treaties so its meaning and legal nature are unclear. To clarify the meaning of market neutrality in the euro area's monetary policy we develop a summative content analysis of the textual data contained in relevant legal and policy documents that are publicly available. We conclude that, in the context of monetary policy, the ECB and its staff have used the term market neutrality with two meanings: (i) the minimisation of any impact on the operation of markets and, in particular, on the operation of the price discovery mechanism; and (ii) the mirroring of the composition of a particular market to guide asset purchases. We then examine the legal nature of market neutrality in each of these two meanings. In its first meaning, we argue that market neutrality is the ECB's definition of the so-called 'principle of an open market economy' ('OME principle') and it is therefore primary law. In its second meaning, we argue that market neutrality operationalises the OME principle and is therefore secondary law. Our conclusions differ from those reached by the first academic enquiries into the legal nature of market neutrality and open an academic debate on the matter. A clear understanding of the legal nature of market neutrality is also essential to assess the validity of the ECB's climate change action plan.

**Keywords:** market neutrality; ECB; unconventional monetary policies; secondary objective; market efficiency; climate change

[†]Senior Lecturer in Commercial Law, University of Glasgow. He is responsible for the conceptualisation, data curation, investigation, formal analysis, methodology, visualisation and writing of the summative content analysis presented in Section 2. He is also responsible for the conceptualisation, investigation and writing of the doctrinal analysis in Sections 3 and 4, and for the writing (review and editing) of the doctrinal analysis in Section 5. He is jointly responsible for the writing of the Introduction and the Conclusion.

[††]Professor of Philosophy of Law, University of Glasgow. He is responsible for the conceptualisation, investigation and writing of the doctrinal analysis in Section 5, and for the writing (review and editing) of Sections 2–4. He is also jointly responsible for the writing of the Introduction and the Conclusion.

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## 1. The question of market neutrality

In recent years, and more specifically after the launch of the European Central Bank (ECB)'s Asset Purchase Programme (APP) in mid-2014, 'market neutrality' has become a recurrent formula in monetary policy debates in the euro area. Most notably, in December 2016, the revelation that the Eurosystem was purchasing assets from corporations in carbon-intensive sectors under the Corporate Securities Purchase Programme (CSPP), one of the iterations of the Eurosystem's APP,[1] spurred numerous questions from Members of the European Parliament at Monetary Dialogues with the President of the ECB on the reasons for purchasing assets from companies in carbon-intensive sectors in light of the current climate emergency. Since the start of the controversy, the unanimous response from ECB staff in various fora was the same: outright purchases, under the CSPP, need to follow market neutrality, which guides the design and implementation of the Eurosystem's monetary policy.[2] In other words, market neutrality justified any potential carbon bias of the CSPP, and, more generally, the legality of what were known at that time as 'unconventional monetary policies'.

Yet, in spite of the popularity of market neutrality in monetary policy debates, there is no legal definition of the term: market neutrality is not mentioned in the Treaties and the only express reference to it is in an ECB Guideline,[3] an act of secondary law, that simply mentions it without giving it any substantial content.

The lack of a legal definition of market neutrality contributed to the uncertainty about its legal nature. The various ways in which ECB staff have characterised market neutrality since the start of the controversy around the carbon bias of the CSPP evidence the lack of certainty about the legal nature of market neutrality. The most recurrent characterisation of market neutrality refers to it as a 'principle'. For example, in her testimony before the European Parliament on 6 February 2020, when describing the composition of the APP, President Lagarde affirmed: 'On monetary policy itself, over the portfolio as a whole, in simple terms about 80 per cent of the portfolio is in sovereign bonds – so there is no major impact there – and 20 per cent corresponds to purchases of corporate assets, and here, yes, the principle of [market] neutrality is observed.'[4] In his opinion in *Weiss*, Advocate General Wathelet also characterised market neutrality as a principle.[5] But this is not the only available characterisation. In another testimony before the European Parliament, President Lagarde referred to market neutrality as a 'concept' and an 'idea'.[6] In a recent letter responding to an MEP on a question on climate change, President Lagarde further characterised market neutrality as a 'concept' and a 'notion'.[7] A principle, an idea, a concept, a notion: each of

[1]See A Neslen, 'ECB's Quantitative Easing Programme Investing Billions in Fossil Fuels' *The Guardian* (9 December 2016) available at <http://www.theguardian.com/environment/2016/dec/09/ecbs-quantitative-easing-programme-investing-billions-in-fossil-fuels> accessed 19 February 2024.

[2]For one of the first references to this argument, see President Draghi's testimony in the Monetary Dialogue on 29 May 2017, at 20. Transcripts of Monetary Dialogues are available <https://www.europarl.europa.eu/committees/en/econ/econ-policies/monetary-dialogue> accessed 19 February 2024.

[3]Guideline (EU) 2019/671 of the European Central Bank of 9 April 2019 on domestic asset and liability management operations by the national central banks (recast) (ECB/2019/7), OJ L 113/11, 29.4.2019, ELI: <http://data.europa.eu/eli/guideline/2019/671/oj> accessed 19 February 2024.

[4]See the transcript of the monetary dialogue with President Lagarde on February 6, 2020, available here: <https://www.europarl.europa.eu/cmsdata/197707/CRE_Monetary_dialogue_06022020_EN.pdf>, at p 18 accessed 19 February 2024.

[5]See Case C-493/17 (*Weiss*), Opinion of the Advocate General Wathelet, para 74.

[6]'So the idea of market neutrality is not something that is embedded in the Treaty. And what the Treaty says is 'principle of an open market economy with free competition', yes, 'favouring an efficient allocation of resources'. So the market neutrality concept has been used to operationalise this principle'. See Christine Lagarde's testimony in Monetary Dialogue, 2 December 2019, p. 20, available <https://www.europarl.europa.eu/cmsdata/207680/1.%20CRE_Monetary%20dialogue_02.12.2019-original.pdf> accessed 19 February 2024.

[7]'[T]he *notion* of market neutrality has been considered by the ECB as an appropriate and useful *concept* to help guide our monetary policy framework'. (Emphasis added.) C Lagarde, 'Letter from the ECB President to Mr Markus Ferber, MEP, on Climate Change' <https://www.ecb.europa.eu/pub/pdf/other/ecb.mepletter210205_Ferber~382cd05490.en.pdf> accessed 19 February 2024. Other ECB staff in decision-making bodies have also characterised market neutrality as a 'concept'. Most

these categories has a different weight in legal reasoning and legal decision-making. What legal nature market neutrality actually has can have significant implications for what the ECB can and cannot do in unconventional monetary policies.

The uncertainty surrounding the definition and legal nature of market neutrality favoured the proliferation of different views among ECB staff. Jens Weidmann, then President of the Bundesbank and Member of the ECB's Governing Council, argued that 'Skewing asset purchases to green bonds, say, would run counter to this principle [of market neutrality], which is anchored in Article 127 of the [Treaty on the functioning of the EU ("TFEU")]'.[8] Implicit in his statement there seems to be an argument that market neutrality is a principle of primary EU law and one that trumps any climate change considerations. Soon after Mr Weidmann's speech, Ms Isabel Schnabel, a member of the Executive Board of the ECB, affirmed that 'While the concept of market neutrality is related to the Treaty principle of 'an open market economy with free competition, favouring an efficient allocation of resources', it is not per se a rule in primary law'.[9] Mr Frank Eldersson, another Member of the Executive Board of the ECB, arguably went even further: 'The principle of market neutrality is not part of the Treaty'.[10]

Given the absence of a consensus over the legal nature of market neutrality, it does not come as a surprise that the term quickly became one of the main points of debate in the controversy around the climate bias of the CSPP. Perhaps for this reason, the controversy around market neutrality has attracted a growing attention in academic circles. For example, there have been some extensive analyses of market neutrality in the political science literature and in economic journals, but quite predictably they do not examine the legal nature of the term.[11]

Despite this growing interest, the analyses of the legal nature of market neutrality in legal scholarship remain very few. The first articulation of the legal nature of market neutrality that we are aware of is a draft chapter by René Smits published in September 2021.[12] In his draft, Smits argues that market neutrality and the 'principle of an open market economy, favouring an efficient allocation of resources' (the 'OME principle'[13]), which is laid down in Article 127(1) TFEU, are different. For him, market neutrality is 'a self-imposed rule' and the OME principle is a 'public-law injunction to the European central banking system'.[14] Based on this characterisation, he reaches the conclusion that 'there is no legal requirement to operate market neutrality under the Treaty-given [OME] principle'.[15]

Three papers that explored different legal issues underpinning the relationship between climate change and the euro area monetary policy were published in an issue of the Common Market Law

notably, see B Coeuré, 'Embarking on Public Sector Asset Purchases' (*European Central Bank*, 10 March 2015) available <https://www.ecb.europa.eu/press/key/date/2015/html/sp150310_1.en.html> accessed 19 February 2024.

[8]See the Address by Mr Weidmann (President of the Bundesbank) at the Bundesbank's second financial market conference, available here: <https://www.bis.org/review/r191029a.htm> accessed 19 February 2024.

[9]See I Schnabel, 'From Market Neutrality to Market Efficiency' (14 June 2021) available <https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp210614~162bd7c253.en.html>. (Footnotes omitted) accessed 19 February 2024.

[10]See F. Elderson, 'Market Neutrality Is not a Legal Requirement', <https://www.youtube.com/watch?v=JSmbIlonreg> accessed 19 February 2024.

[11]See eg J van 't Klooster and C Fontan, 'The Myth of Market Neutrality: A Comparative Study of the European Central Bank's and the Swiss National Bank's Corporate Security Purchases' 25 (2020) New Political Economy 865; D Lombardi and M Moschella, 'The Government Bond Buying Programmes of the European Central Bank: An Analysis of Their Policy Settings' 23 (2016) Journal of European Public Policy 851. Although not exclusively focussed on market neutrality, this intervention also addresses the topic: M Thiemann, T Büttner and O Kessler, 'Beyond Market Neutrality? Central Banks and the Problem of Climate Change' 8 (2022) Finance & Society 1–21.

[12]See R Smits, 'Elaborating a Climate Change-Friendly Legal Perspective for the ECB' (September 2021) available <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3913653> accessed 19 February 2024.

[13]References to this principle in policy debates do not always include the efficiency formula, ie 'favouring an efficient allocation of resources'. As we shall argue below, this formula is a central element in the OME principle. Thus, we use the term 'OME principle' to refer to all the elements that are captured in the quote unless stated otherwise.

[14]See Smits, Elaborating (n 12) 33.

[15]Ibid., 34.

Review (CMLR) in 2022.[16] In the first of these papers, Steinbach proposes a view similar to Smits' and identifies market neutrality as 'a self-imposed policy practice rule that central banks apply to their operations'.[17] He expressly rejects the possibility that market neutrality imposes a legal duty upon the ECB. In the second paper, Zilioli and Ioannidis reach a similar conclusion: they characterise market neutrality as 'an operational concept' and therefore conclude that '[it] is not a legal rule'.[18]

Smits, Steinbach, and Zilioli and Ioannidis all characterise market neutrality as an operational concept that is not binding on the ECB. In the third CMLR paper, Dietz offers a different reconstruction: market neutrality is 'a general principle requiring the ECB to abstain from setting policy incentives other than those directly linked to price stability'.[19] For Dietz, the source of market neutrality's legal force goes beyond the OME principle: she points to the principle of non-discrimination[20] and to the price stability objective and the central bank's independence.[21] Nevertheless, she expressly rejects the argument that market neutrality is primary EU law.[22] Therefore, rather than a 'general principle', market neutrality may be better characterised as a 'general functionality' (a slightly unclear concept) of monetary policy and a reflection of the institutional set-up of the ECB.[23]

Another important and recent explanation of the appearance and nature of market neutrality is provided by a two-part article published by Ramos, Cabrales and Sánchez.[24] They agree with the general consensus that market neutrality has no legal salience and therefore cannot be considered a legal norm. Their explanation for the centrality of market neutrality is not limited to the ECB but covers other Western central banks, and it signals that the spread of market neutrality across different jurisdictions is 'evidence of central bankers' proclivity to abide by 'social norms'.[25] In this reconstruction, market neutrality is a social norm that has been adopted because of the transmission of norms in social networks, especially professional ones. Social norms do not create legal obligations, but they guide behaviour and they express ways in which social institutions adapt their preference and expectations to their changing environment. However, Ramos, Cabrales and Sánchez hypothesise that the adoption of market neutrality has impacted on the credibility of the ECB because of the increased presence of climate change talk in several networks. Through empirical analysis of the recurrence of environmental concerns in different social spheres and in several central banks (and especially the ECB), they show how we are witnessing a move from one social norm to another whereby central banks (lacking support from the mainstream economic science) might position themselves as a leading institution. Hence, 'what was once a minority view is now becoming a mainstream view against "market neutrality" (or at least a rigid conception of it) that an increasing number of officials position themselves against'.[26] The reason for this mutation is that market neutrality has proved to be a 'maximalist and uncompromising' social

[16] A Steinbach, 'The Greening of the Economic and Monetary Union' 59 (2022) Common Market Law Review 329; C Zilioli and M Ioannidis, 'Climate Change and the Mandate of the ECB: Potential and Limits of Monetary Contribution to European Green Policy' 59 (2022) Common Market Law Review 363; S Dietz, 'Green Monetary Policy between Market Neutrality and Market Efficiency' 59 (2022) Common Market Law Review 395.

[17] See Steinbach, The Greening (n 16) 352.

[18] Ioannidis and Zilioli, Climate Change (n 16) 389.

[19] Dietz, Green Monetary Policy (n 16) 430.

[20] Ibid.

[21] '[Market neutrality] is a general functionality of monetary policy and closely linked to the consequences of the institutional set-up of central banks as independent institutions. [ . . . ] [I]t is contrary to the foundations of monetary policy, with its primacy on price stability, to distinguish between market participants on the basis of any other policy criteria': see Dietz, Green Monetary Policy (n 16) 430.

[22] Dietz, Green Monetary Policy (n 16) 421.

[23] See Dietz, Green Monetary Policy (n 16) 430.

[24] D Ramos, A Cabrales and A Sánchez, 'Central Banks and Climate Change (Part 2), Can Central Banks Intervene Now? And How? Arguments of "Opportunity" and "Suitability"' 6 (2023) The Business and Finance Law Review 261–7.

[25] Ibid., 294.

[26] Ibid., 296.

norm, and therefore unsuitable for addressing the complex challenges for financial stability brought about by climate change. Although they introduce a sophisticated model of norms transmission, their main legal argument reaches very similar conclusions to the legal scholarship presented above. Market neutrality is a social norm and can be abandoned without any legal change, but simply in virtue of an adaptation to a changing environment.

All these previous works,[27] despite their differences in methodology and focus, converge on one key point: market neutrality is not a legal norm. In this paper, we develop a different view on the meaning and legal nature of market neutrality. For the sake of clarity, we want to specify what we mean by meaning and legal nature: the latter concerns the question of whether market neutrality is a principle, an objective or a rule, while the former is the determination of the content of the principle/objective/rule. In the absence of a formal definition of market neutrality, we look at the institutional practice and discourse involving the term to find out how it has been 'used'. For this reason, we have developed a summative content analysis of relevant policy documents to reconstruct how the ECB and its staff have been using the term in the euro area's monetary policy.[28] A summative content analysis is a research method commonly used in anthropology and other social sciences to understand the contextual use and meaning of terms. To the best of our knowledge, we are the first to apply this research method to the area of monetary policy.[29]

In Section 2, we describe in greater detail the methodology we have adopted, and we discuss the findings from the analysis. In our summative content analysis, we identify three meanings with which the ECB and its staff have used 'market neutrality' and related terms.

One of our main findings is that the ECB and its staff have used 'market neutrality' and related terms with at least three different meanings: (i) the minimisation of distortions on market functioning, (ii) an investment strategy that aims to obtain profits regardless of general movements in markets and (iii) the characteristic of portfolios that mirror the composition of a reference market. In our opinion, only the first and third meanings are directly relevant for monetary policy. Here lies one of the main contributions of this Article: understanding market neutrality as a polysemous term distinguishes our analysis from existing legal scholarship, which conceives market neutrality as having only one meaning: the third meaning identified in our summative content analysis. The risk entailed by the collapse of all meanings of market neutrality into one is not only a lack of nuance but a failure in identifying some of the legal obligations of the ECB in designing and implementing unconventional monetary policies.

The polysemy of market neutrality poses an important question to our understanding of the legal meaning and nature of the term. Is the legal nature of market neutrality the same regardless of the meaning with which the term is used? We think not. In Section 3, we develop an analysis of the legal nature of the first and third meanings of market neutrality and reach different conclusions: in its first sense, ie the need to minimise distortions on market functioning, market neutrality defines the OME principle in the specific context of the euro area's monetary policy and it is therefore primary law; in its third meaning, ie the characteristic of portfolios that mirror the composition of a reference market, market neutrality is an operational measure used to implement the OME principle and other legal principles that are binding on the Eurosystem. In its third meaning, market neutrality falls short of primary law, but because it is based on a decision of the Governing Council it should be regarded as secondary law. In light of these conclusions, our

[27]Other works only mention or discuss market neutrality in a cursory way. Another recent work that exemplifies the same view, but addresses market neutrality briefly, is C Calliess and E Tucun, 'The Role of Art. 11 TFEU in Greening of the ECB's Monetary Policies' (2023) German Law Journal (First view). At page 23, the authors conclude that 'it appears that, from a legal point of view, the market neutrality principle may not constitute a legally relevant limitation [to climate-change related considerations]'.

[28]Although strictly speaking these are not legal sources, they represent the only formal articulation of the meaning of market neutrality, and they come from the institution directly using the term in its own legal acts.

[29]This assessment is of course related to the legal analysis of monetary policies.

analysis indicates that the legal nature of market neutrality is more complex than the way existing legal scholarship understands it.

In Section 4, we use the framework presented in Section 3 to assess the ECB's new monetary policy strategy; in particular, its climate change action plan and the emergence of the idea of market efficiency. The aim of this section is to question the main frame which has informed the analysis of the new strategy review, one of juxtaposition of neutrality and efficiency. We claim that having put market efficiency at the forefront of the ECB's decisions concerning climate-related financial risks does not exclude or invalidate market neutrality. The latter continues to inform the ECB's monetary policies and we provide an argument to show that – under current EU primary law – this makes sense. In Section 5, we explore the implications of the complex nature of market neutrality for the ECB and the euro area monetary policy. In particular, we reflect on whether market neutrality might compromise the legitimacy of the ECB and its independence from political institutions. Section 6 presents a summary of our main conclusions and potential avenues for future research.

## 2. The meanings of market neutrality in the euro area's monetary policy

### *A. Methodology*

A condition for our analysis of the legal nature of market neutrality was the clear identification of the meaning of the term. Because the term has been introduced by the ECB, we wanted to understand the sense in which the ECB and its staff have used it. In order to interpret the contextual meaning of the term 'market neutrality', we designed a summative content analysis of textual data[30] contained in relevant ECB legal acts and publications, and statements from ECB staff to answer the following question: In what sense (or senses) have the ECB and its staff used the term 'market neutrality' in the context of the euro area's monetary policy?

In particular, we examined the textual data contained in the following sources:

- Primary EU law: the Treaty on the Functioning of the European Union (TFEU) and the Statute of the European System of Central Banks (ESCB) and the ECB
- Secondary EU law: Relevant legal acts of the ECB, such as those enumerated in Article 132 TFEU and 34 of the Statute of the ESCB and the ECB,[31] and other legal instruments such as those enumerated in Article 17 of the ECB Rules of Procedure[32]
- Minutes from the meetings of the Governing Council
- Press releases regarding the announcement of monetary policy decisions[33]

[30]Summative content analysis is a qualitative research tool that allows researchers to explore word usage or to discover the range of meanings that a word can have in a specific use. See eg H F Hsieh and SE Shannon, 'Three Approaches to Qualitative Content Analysis' 15 (9) (2005) Qualitative Health Research 1277–88, at 1285.

[31]These include Regulations, Decisions, Recommendations and Opinions.

[32]These include Guidelines and Decisions adopted by the Governing Council, and Instructions adopted by the Executive Board. See Decision of the European Central Bank of 19 February 2004 adopting the Rules of Procedure of the European Central Bank (ECB/2004/2) (2004/257/EC) (as amended), Art 17.

[33]Communication tools such as speeches, interviews, press conferences, regular publications of reports and even the ECB's website have become increasingly important to understand the monetary policy measures of the Eurosystem, especially after the sovereign debt crisis in the euro area at the start of the 2010s. See, 'The European Central Bank' in F Antembrink and C Hermann (eds), *EU Law of Economic and Monetary Union* (Oxford University Press 2020) para 14.82. In its evaluation of whether some of these communication tools would be subject to judicial review, the Court of Justice of the European Union ('CJEU') has confirmed the legal value of press releases and press conferences, especially those concerning Decisions of the Governing Council. See eg *Weiss* (n 5), para 37. See also the AG Opinion in C-62/14 *Gauweiler and Others v. Deutscher Bundestag* ECLI:EU:C:2015:400, paras. 6 and 82-90; AG Opinion in *Weiss* (n 5), paras. 90 and 148, and nn12, 23, 33, 42, 51, 81, 82.

- Descriptions of monetary policy measures published on the ECB's website
- Statements from the President of the ECB, in particular those made in[34]:
  - Press conferences to announce monetary policy decisions, including the introductory statement by the President of the ECB and the Q&A following it
  - Monetary Dialogues with the European Parliament's Committee on Economic and Monetary Affairs (ECON)[35]
  - Letters in response to questions made by Members of the European Parliament (MEPs)
  - Speeches at conferences and other relevant events
  - Interviews
  - Posts on the ECB blog
- Statements from other members of the Executive Board of the ECB, in particular those made in[36]:
  - Speeches at conferences and other relevant events
  - Interviews
  - Posts on the ECB blog
- The ECB Annual Report[37]
- Other relevant ECB publications, including:
  - Reports other than the ECB Annual Report ('Other reports')
  - The Monthly Bulletin (1999–2014)[38]
  - The Economic Bulletin (2015–2023)[39]
  - The Financial Stability Review
  - The Macroprudential Bulletin
  - The Research Bulletin[40]
  - Other research papers written by ECB staff that are not included in the Research Bulletin, in particular:
    - Working papers
    - Discussion papers
    - Occasional papers
    - Legal working papers

[34]The ECB President's introductory statement at the beginning of press conferences, following the Governing Council monetary policy meetings, has become a particularly iconic instrument of monetary policy since the start of the sovereign debt crisis in the euro area. See Ioannidis, 'The European Central Bank' (n 33) at 14.82.

[35]See Art 284(3) TFEU.

[36]For a succinct analysis of the legal value of these statements to understand the Eurosystem's monetary policy measures, see n 34.

[37]For a succinct analysis of the legal value of the ECB Annual Report and other reports to understand the Eurosystem's monetary policy measures, see n 34.

[38]The Monthly Bulletin was published from January 1999 to December 2014. It was published one week after each monetary policy meeting of the Governing Council. 'It explained the monetary policy decision and provided a detailed analysis of the current economic situation and risks to price stability'. See <https://www.ecb.europa.eu/pub/economic-bulletin/mb/html/index.en.html> accessed 19 February 2024. To mirror the new six-week cycle for monetary policy meetings that started in January 2015, on 16 December 2014 the Governing Council announced that a new Economic Bulletin would replace the ECB Monthly Bulletin. See <https://www.ecb.europa.eu/press/govcdec/otherdec/2014/html/gc141219.en.html> accessed 19 February 2024.

[39]The Economic Bulletin has been published since January 2015, when it replaced the Monthly Bulletin. The Economic Bulletin is published eight times a year, two weeks after each monetary policy meeting. '[It] presents the economic and monetary information which forms the basis for the Governing Council's policy decisions.' See <https://www.ecb.europa.eu/pub/economic-bulletin/html/index.en.html> accessed 19 February 2024.

[40]The Research Bulletin features a selection of recent work on policy-relevant topics by ECB economists. It is published on a monthly basis and covers a wide variety of economic and financial topics. See <https://www.ecb.europa.eu/pub/economic-research/resbull/html/index.en.html> accessed 19 February 2024.

Not all of the sources enumerated above can be attributed to the ECB. Statements made by the Governing Council, the President and the members of the Executive Board of the ECB can be attributed to the ECB.[41] Certain publications aim to represent the view of the ECB and can therefore be attributed to the ECB, too: (i) press releases regarding the announcement of monetary policy decisions; (ii) descriptions of monetary policy measures published on the ECB's website, (iii) the ECB Annual Report, (iv) the Monthly Bulletin, (v) the Economic Bulletin, (vi) the Financial Stability Review and (vii) the Macroprudential Bulletin. Other statements, such as those made by other ECB staff in research papers contained in the Research Bulletin or elsewhere, cannot be attributed to the ECB. Nevertheless, we have decided to examine these statements too in order to evaluate the extent to which the ECB's position, as represented in those statements that can be attributed to the institution, is shared within the institution or not.

Moreover, two of the sources enumerated above are not directly relevant for the Eurosystem's monetary policy. The Financial Stability Review provides an overview of potential risks to financial stability in the euro area.[42] The Macroprudential Bulletin describes the ECB's work and thinking in the field of macroprudential policy.[43] Nevertheless, these two documents sometimes discuss monetary policy issues from their respective perspectives. We have decided to include these two documents in our summative content analysis to capture those discussions, but we acknowledge that their value for the purposes of our research is relatively lower than the value of other sources, which are directly relevant for the Eurosystem's monetary policy. We take this into account in our discussion of the results of the summative content analysis that we present in Section 2.E.

We collected all the sources listed above from three databases: (i) we used the EUR-lex database[44] to collect all primary and secondary EU law; (ii) we used the ECON's website[45] to collect the transcripts of Monetary Dialogues between the President of the ECB and ECON and (iii) we used the ECB's website to collect all the other sources. We examined all the sources enumerated above that were dated between 1 January 1999 and 15 May 2023, and that were available in these three databases as of 15 May 2023.

### B. The sample

In order to define our sample, we began our analysis by searching for appearances of the term 'market neutrality' and related terms such as 'market neutral', 'market-neutral' and 'market-neutrality' in all the sources identified above.[46] In the reminder of the paper, we shall refer to these terms as 'related terms'.

[41]Nevertheless, it is important to note that, ultimately, final decisions of monetary policy are the responsibility of the Governing Council. The President and the members of the Executive board of the ECB integrate the Governing Council alongside the governors of the national central banks of the Member States whose currency is the euro. See Articles 10.1 and 13.1 of the Statute.

[42]See the definion of financial stability review on the ECB's website: <https://www.ecb.europa.eu/pub/financial-stability/fsr/html/index.en.html> accessed 19 February 2024. See also Art 13k of the Decision of the European Central Bank of 19 February 2004 adopting the Rules of Procedure of the European Central Bank (ECB/2004/2) (2004/257/EC) (as amended) ('ECB Rules of Procedure').

[43]See the definition of the macroprudential bulletin: <https://www.ecb.europa.eu/pub/financial-stability/macroprudential-bulletin/html/index.en.html> accessed 19 February 2024. See also Art 13k of the ECB Rules of Procedure.

[44]See Eur-Lex Database, <https://eur-lex.europa.eu/homepage.html> accessed 19 February 2024.

[45]See Econ Committee Website, <https://www.europarl.europa.eu/committees/en/econ/econ-policies/monetary-dialogue> accessed 19 February 2024.

[46]This is often referred to as a 'manifest content analysis'. It is the essence of quantitative content analysis, and it is often the first step in summative content analysis, which goes beyond mere word count and aims at uncovering latent content. See eg Hsieh and Shannon (n 30) at 1283 and the resources cited therein. In summative content analysis, this initial quantification aims to explore usage rather than to infer meaning. The interpretation of contextual meaning takes place at a later stage of the analysis. See eg Hsieh and Shannon (n 30) at 1284–85.

In order to search for these related terms, we used the following search terms: 'market neutral*' and 'market-neutral*'.[47] In the remainder of the paper, we shall refer to these terms as 'key terms'.

In order to ensure the construct validity of our sample, we registered all the sources that contained at least one reference to 'market neutrality' or related terms on a Microsoft Excel file. For every relevant source, we identified a series of relevant aspects, including the date when the source was published, its title, its author, the database and url where we found the source and the date when we accessed the source.[48] This Microsoft Excel file served as a repository for the database.

In order to identify the relevant textual data for our sample, we used a different technique for each of the three databases. In EUR-lex, we searched for the key terms in all of the documents available on the database. The search returned 40 results. We then filtered by author to identify those documents that had been prepared by the ECB. This filtered the search to one result.[49]

On ECON´s website, we manually identified the transcripts of all the Monetary Dialogues and downloaded a PDF version of their transcripts. We then searched each PDF document for the key terms using the 'Find' function of Adobe Acrobat Reader PC. If a document was not available in PDF format, we viewed it in HTML format using an internet browser and used the 'Find' function of the browser to search for the same key terms. Market neutrality and related terms appeared in the transcripts of four Monetary Dialogues. We inspected each of the appearances to confirm that market neutrality and related terms had been used by the President of the ECB (rather than by MEPs or the Chair of the ECON, for example). We identified 11 references by the President of the ECB.

On the ECB's website, we searched for the key terms using the ECB's website search engine, which covers all of the content published there, including uploaded files and text displayed on the ECB's website. The search of 'market neutral*' returned 2804 results; the search of 'market-neutral*' returned 2763 results. The search engine on the ECB's website did not recognise the use of quotation marks as Boolean operators so the search engine returned documents that contained the words 'market' and 'neutral*' rather than the exact phrase 'market neutral*', for example. We concluded that manually examining each of these results individually would be very time-consuming, so we adopted three different approaches depending on how time-consuming it would be to manually search all the relevant documents for a specific type of source.

First, we searched the ECB's website for specific datasets of any of the sources that remained unexamined. We found that the ECB had compiled a specific dataset for two of the sources identified above: Speeches of the President of the ECB and of the members of the ECB Executive Board (hereinafter, the 'Speeches dataset').[50] This is a precompiled dataset containing the content

[47]Our choice of key terms was driven by the intention to identify only those circumstances in which the ECB and its staff had referred to 'market neutrality' as a unique concept. We expressly avoided the use of narrower key terms such as 'neutral*' to distinguish 'market neutrality' from any references to the 'neutrality of markets'. The results of our summative content analysis confirm that the 'neutrality of markets' is not a related term of 'market neutrality'. The meanings of market neutrality that we present in Section 2.D either refer to the effects of monetary policy operations on markets (ie the first meaning of market neutrality) or to the composition of a reference market to guide certain investment and monetary policy strategies (ie the second and third meanings of market neutrality, respectively). The 'neutrality of markets' is often used to describe the perceived effects of market activity on a parameter of reference, eg any ethical or political considerations. See eg R Keat. 'Ethics, Markets, and MacIntyre' 30 (2008) Analyse & Kritik 243–57, especially 243–4. Avoiding 'neutral*' as a key term also allowed us to exclude from our search results other uses of the term 'neutral' that, albeit common in monetary policy, are not directly relevant for our research question, eg 'monetary neutrality', the 'neutrality of the fiscal stance', the 'neutral real interest rate', 'actuarial neutrality' or 'tax neutrality', among others.

[48]The resulting dataset was too large to attach to the paper, but the Excel file can be shared with any interested parties upon request by contacting Dr Javier Solana.

[49]The Guideline (EU) 2019/671 of the European Central Bank of 9 April 2019 on domestic asset and liability management operations by the national central banks (recast) (ECB/2019/7).

[50]See the 'Speeches Dataset' available at this address: <https://www.ecb.europa.eu/press/key/date/html/index.en.html> accessed 19 February 2024.

of all speeches together with limited metadata and it is available in CSV format. We searched the key terms in the dataset using the ‘Find’ function on Microsoft Excel. The search returned 15 speeches where the President or members of the Executive Board of the ECB used market neutrality or related terms 44 times.

Second, for those sources that (i) were easily identifiable on specific sections of the ECB’s website and (ii) had less than 250 individual items, we downloaded a PDF version of each publication and then searched each PDF document for the key terms using the ‘Find’ function of Adobe Acrobat Reader PC.[51] The ECB Annual Reports, Economic Bulletins, Monthly Bulletins, Research Bulletins, Financial Stability Reviews and Macroprudential Bulletins met these criteria. The search returned 34 documents where market neutrality or related terms had been used. Although the descriptions of monetary policy measures published on the ECB’s website are not archived as documents, these descriptions are easily identifiable on the ECB´s website under the ‘Monetary policy’ section so we adopted a similar technique: we navigated all the pages in the ‘Monetary policy’ section of the ECB’s website and searched the key terms on each page using the ‘Find’ function on the internet browser. We identified four pages containing at least one reference to market neutrality or related terms.

For all the remaining types of sources, we used the ECB website’s search engine, but we added words that appeared in the relevant type of sources on a consistent basis. Annex 1 details the additional search terms that we used to analyse these remaining sources.

As we did with ECON’s website, in each of these three approaches that we used to search the ECB’s website, we inspected all the sources that the search returned and excluded any that were not authored by ECB decision-making bodies or staff.

In this manifest content analysis, we identified a total of 100 sources containing at least one reference to ‘market neutrality’ or related terms. Within them, the term ‘market neutrality’ or related terms appeared 296 times.[52] Some of the appearances that we identified were contained in tables, diagrams and mathematical formulas. In one instance, for example, a single source contained 16 appearances of this kind. We concluded that, for the purposes of developing a quantitative analysis, giving the same consideration to all of these appearances could overemphasise the importance of the resources that contained this type of appearance and could therefore distort our conclusions. In order to address this problem, we decided to count all the appearances of market neutrality and related terms included in tables, diagrams and mathematical formula in the same source as a single appearance.[53] This reduced the number of appearances in our data sample to 216. Annex 2 identifies the number of appearances in each of the sources examined.

### C. Coding process

The purpose of our summative content analysis was to interpret the contextual meaning of the term ‘market neutrality’. In our first approximation to the data, we realised that, while in some cases the meaning of the term market neutrality was manifest in the words used by the ECB or its staff (eg because they made a reference to market neutrality or related terms and then provided an express definition of the term) and was therefore easily observable, in many other cases the

[51] All of these documents are available on the ‘Research & Publications’ section of the ECB’s website: <https://www.ecb.europa.eu/pub/html/index.en.html> accessed 19 February 2024.

[52] We expressly excluded from the data sample appearances of market neutrality and related terms that were in the titles of resources cited by the relevant authors. These citations, however, were useful to infer the meaning of market neutrality in some cases.

[53] Out of the 100 sources, 17 were affected by this measure. Most of them (13) were Financial Stability Reviews. One Working Paper and two Occasional Papers written by Other ECB staff, and one Monthly Bulletin were the other affected sources.

meaning of the term was latent in the way in which the ECB or its staff were using the term, including how they were constructing judgements.

When meaning is latent and the goal is to propose a new theory or interpretation, an inductive approach is more appropriate than a deductive approach.[54] So, in order to uncover the latent meaning of market neutrality, we began our analysis by reading the 100 documents in our sample with no preconceived notions or categories. In this first reading, we made a list of keywords relating to the use of market neutrality that we used as codes. We then organised these codes into categories based on the codes' similarity and regularity to facilitate the analysis of their connections. We compiled them into a codebook to guide our coding process. The first co-author acted as 'codebook editor'.[55]

Guided by the codebook, the first co-author proceeded to code the textual data to identify meaningful units of text. After this first coding exercise, the codebook prepared after the first reading of the data sample changed significantly, so the first co-author updated the codebook, and he developed a second coding exercise. To do that, he copied the relevant units of text identified in the first coding exercise and pasted them on a column in the Microsoft Excel file that served as a repository for the database. He then coded that textual data again by registering the relevant codes in an adjacent column. The final version of the codebook is included in Annex 3 for ease of reference.

After the second coding exercise, the first co-author tested the stability of the analysis by recoding a subset of the data sample.[56] There were no major differences between this stability test and the second coding exercise. After confirming the stability of the analysis, the second co-author coded a subset of the data sample guided by the codebook in order to test the reproducibility of the analysis.[57] There were no differences in the outcome of this reproducibility test and the outcome of the second coding exercise.

### *D. Interpretation*

We interpreted the connections between the different codes and categories taking into account the context in which they appeared, and we concluded that the ECB and its staff have used the term market neutrality with three different meanings. We present each of these meanings in the chronological order in which they appear in our data sample. In some cases, however, we were unable to infer the meaning of market neutrality from the context. We present these residual categories at the end of this section.

#### *Market neutrality means to avoid unnecessary distortions to market functioning*

The first use of market neutrality and related terms that we have documented expresses a concern with central banks' monetary policy measures impacting the operation of markets. In the Monthly Bulletin of April 2000, when describing some of the monetary policy operations of the Bank of Japan, the ECB referred to market neutrality in the following terms:

> The need to comply with the principle of market neutrality. The Bank of Japan conducts its open market operations directly in the market. Like the Federal Reserve System, it does not

[54]See W James Potter and D Levine-Donnerstein, 'Rethinking Validity and Reliability in Content Analysis' 30 (1999) Journal of Applied Communication Research 258–84, at 264; N Kondracki, N Wellman and D Amundson, 'Content Analysis: Review of Methods and Their Applications in Nutrition Education' 34 (4) (2002) Journal of Nutrition Education and Behavior 224–30, at 225.

[55]See K MacQueen, E McLellan-Lemal, K Bartholow and B Milstein, 'Team-Based Codebook Development: Structure, Process, and Agreement' in Handbook for Team-Based Qualitative Research (Rowman & Littlefield 2007) 119–35, at 132.

[56]The stability of the analysis is sometimes referred to as 'intracoder reliability'. See Kondracki et al (n 54) at 226.

[57]The reproducibility of the analysis is sometimes referred to as 'intercoder reliability'. See Kondraki et al (n 54) at 226.

> want to influence the interest rate or price conditions in the markets in which it operates. Since liquidity needs can be very large, the Bank of Japan has to spread its open market operations over a broad spectrum of markets to limit the impact on market prices and interest rates.[58]

For fifteen years after this reference in the Monthly Bulletin of April 2000, the only uses of market neutrality in this sense were two appearances in the Monthly Bulletin of April 2006.[59] On that occasion, the ECB referred to market neutrality as one of three overarching portfolio management principles that the ECB applied to the foreign reserve portfolio, the own funds' portfolio and the ECB's pension fund portfolio:

> First, the ECB applies a 'market neutrality principle': it endeavours, in its portfolio management activities, not to cause any undue distortion in market prices. In practice, this means that the ECB's portfolio management activities are only conducted in markets that are deep and liquid enough to ensure that portfolio management transactions are easily absorbed at market-determined prices.

The third instance in which the ECB used market neutrality in this sense was in a speech made by Benoît Cœuré, Member of the Executive Board of the ECB, on 10 March 2015 apropos the launch of the Public Sector Purchase Programme (PSPP):

> One key principle underlying the implementation of the PSPP is the minimisation of unintended consequences, which can be ensured by obeying the concept of market neutrality. We do want to affect market prices but we will not suppress the price discovery mechanism. The Eurosystem will ensure a high degree of transparency around its interventions and will closely monitor their impact on market liquidity and collateral availability. Some market reports have suggested that we may not be able to buy the intended amounts of government bonds. While the effective supply of eligible securities is undoubtedly lower than the total amount outstanding, it will still be substantially higher than the amounts we intend to purchase. If this is the case, there will be a price at which we can buy the quantities needed to meet our monthly targets. In other words, we may face a scarcity of bonds, but we won't face a shortage.[60]

As these three quotes illustrate, when using market neutrality in this first sense, in some cases the ECB made general references to the 'normal functioning of markets' or similar expressions; in other cases, the ECB made references to specific aspects of market functioning, such as the formation of prices or prices themselves, a market's liquidity, the availability of collateral and the level of competition in a given market.

Mr Cœuré's use of market neutrality in that speech has become quite symbolic. In our dataset, we have documented several instances where the ECB or its staff cited Mr Cœuré's speech when using market neutrality or related terms.[61] This suggests that Benoît Cœuré's use of the term

[58]April 2000 Monthly Bulletin, page 61. Available <https://www.ecb.europa.eu/pub/pdf/mobu/mb200104en.pdf> accessed 19 February 2024.

[59]We have also documented a use of the term in this sense in an Occasional Paper published in August 2006.

[60]B Cœuré, 'Embarking on public sector asset purchases' (10 March 2015) available <https://www.ecb.europa.eu/press/key/date/2015/html/sp150310_1.en.html> accessed 19 February 2024.

[61]See eg I Schnabel, 'From Green Neglect to Green Dominance', intervention at the Greening Monetary Policy, March 3, 2021, transcript available here: <https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp210303_1~f3df48854e.en.html> accessed 19 February 2024.

market neutrality had a major impact on how ECB staff understand market neutrality.[62] The following quote from President Lagarde in her first testimony before the European Parliament supports this interpretation:

> Granted, in that small portion in our stock, which is private, there are multiple shades from green to brown, and I think it was predicated and it is predicated on the fact that we have to not disrupt the financial markets and comply with what has been defined as market neutrality.[63]

This sense of the term market neutrality is still very relevant today. For example, in its attempt to clarify the implementation of the PSPP, to the question of how the ECB weighs different maturity buckets for purchases under the PSPP, as of 15 May 2023 the ECB noted that:

> The goal is market neutrality. The Eurosystem wants to create as little distortion as possible.[64]

As the quote by Mr Cœuré reproduced above illustrates, the understanding of market neutrality as the need to minimise the distortion on market functioning aims to preserve the operation of the price discovery mechanism. In mainstream economic theory, prices in many markets result from the interaction between buyers and sellers, and the exchange of information that results from those interactions. Mr Cœuré's quote captures a common concern among ECB staff that the purchases under the APP could crowd out other potential buyers and favour (or disfavour) specific market segments. The following quote from the accounts of the Governing Council meeting that took place on 13–14 December 2017 provides an additional illustration of these concerns:

> With regard to the implementation of the APP, members welcomed findings indicating the effectiveness of the corporate sector purchase programme (CSPP) in easing market financing conditions and, hence, supporting the transmission of monetary policy. At the same time, these findings showed only limited evidence of distortions in market functioning or of a crowding out of bank lending, which had instead remained on an upward path, including for SMEs. Moreover, while risk premia in corporate bond markets had been compressed significantly, this applied both to corporate bonds eligible for purchase under the programme and to ineligible bonds, which suggested that the impact of the CSPP had been market-neutral and portfolio rebalancing had been effective across market segments.[65]

### *Market neutrality as a particular investment strategy*

The second use of market neutrality and related terms that we have documented corresponds to a series of references to a particular investment strategy, mainly in the ECB's Financial Stability Reports between 2004 and 2013. The following quote from the Financial Stability Review that was published in December 2004 illustrates this use:

[62]According to the accounts of the Governing Council's monetary policy meetings, Mr Cœuré was often in charge of leading discussions on this topic. See eg <https://www.ecb.europa.eu/press/accounts/2018/html/ecb.mg180111.en.html> accessed 19 February 2024.

[63]See n 6.

[64]FAQs on the PSPP, available <https://www.ecb.europa.eu/mopo/implement/app/html/ecb.faq_pspp.en.html> accessed 19 February 2024.

[65]'Account of the Monetary Policy Meeting of the Governing Council of the European Central Bank' (13-14 December, 2017): see <https://www.ecb.europa.eu/press/accounts/2018/html/ecb.mg180111.en.html> accessed 19 February 2024.

> In contrast to directional funds, market neutral hedge funds search for relative value or arbitrage opportunities to exploit various price discrepancies, and try to avoid exposure to market-wide movements. Such strategies are attractive owing to their lower volatility, but they require medium to high leverage in order to benefit from small pricing distortions, particularly in fixed income markets.[66]

Market neutral investment strategies aim to obtain profits regardless of general movements in markets. They typically achieve this through uncorrelated investments, ie investments that behave differently under similar market conditions.[67] One way in which fund managers can reduce their exposure to market-wide risks, ie to 'hedge' that exposure, is by combining long positions in securities that the fund managers believe to be undervalued and short positions in securities that the fund managers believe to be overvalued.[68]

### *Market neutrality is a characteristic of portfolios that mirror the composition of a reference market*

In other instances where the ECB and its staff used the term market neutrality, they did so to describe the composition of a specific portfolio as mirroring the composition of a reference market. The following quote by Mario Draghi, former President of the ECB, from his testimony before the European Parliament at the Monetary Dialogue that took place on 10 April 2018, illustrates the use of market neutrality in this sense:

> The universe of CSPP-eligible bonds is deliberately broad, and its composition is guided primarily by monetary policy and risk management considerations. In pursuing its objective of maintaining price stability, the [ECB] aims to implement the APP in a market-neutral manner. Consequently, CSPP purchases are conducted on the basis of a benchmark that proportionally reflects the nominal value of bonds in the CSPP-eligible universe.[69]

It is important to note that the references to market neutrality and related terms that we identified in our sample dataset which used market neutrality in this sense had different markets as a reference. For example, in the context of the APP, when used in this sense market neutrality was used in reference to the universe of eligible assets under the relevant APP.[70] In other cases, market neutrality was used to refer to a market in full, ie one where no eligibility criteria had been applied.[71] We might refer to the former type of market neutrality as 'relative' market neutrality and to the latter type as 'absolute' market neutrality.

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[66]ECB, 'Financial Stability Review December 2004', see <https://www.ecb.europa.eu/pub/pdf/fsr/financialstabilityreview200412en.pdf> (pp 123–4) accessed 19 February 2024.

[67]See J Nicholas, 'Market-Neutral Investing' (Bloomsbury 2000): for a summary see <http://dl.fxf1.com/files/books/english/Article%20-%20Market-Neutral%20Investing%20-%20Long-Short%20Hedge%20Fund%20Strategies_%20Joseph%20G%20Nicholas_%202000.pdf> accessed 19 February 2024.

[68]See page 2 of S Brown, W Goetzmann, 'Hedge Funds with Style' (2001) 8173 NBER Working Paper 1, available here: <https://www.nber.org/system/files/working_papers/w8173/w8173.pdf> accessed 19 February 2024.

[69]'European Parliament Monetary Dialogue', April 10, 2018: available here: <https://www.ecb.europa.eu/ecb/access_to_documents/document/correspondence/shared/data/ecb.dr.cor20180410Starbatty.en.pdf> accessed 19 February 2024.

[70]The following quote from the ECB Economic Bulletin Issue 4/2017 illustrates this well: '[T]he ECB aims for a market-neutral implementation of the APP, and therefore CSPP purchases are conducted according to a benchmark that reflects proportionally the market value of eligible bonds', at 40, available <https://www.ecb.europa.eu/pub/pdf/ecbu/eb201704.en.pdf> accessed 19 February 2024.

[71]This quote from Ms Schnabel, distinguishing between the bond market and the universe of eligible bonds within it, illustrates this well: 'The ECB already now deviates from market neutrality in several instances. For example, the application of eligibility criteria for purchases implies that the ECB's bond holdings are not necessarily proportional to market capitalisation': see I Schnabel, 'From Market Neutrality to Market Efficiency' (14 June 2021) available <https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp210614~162bd7c253.en.html> accessed 19 February 2024.

Interestingly, our analysis reveals that, when using market neutrality in this sense, the ECB and its staff referred to different market parameters that a specific portfolio was meant to mirror, including:

- 'market capitalisation', ie the total value of a company that results from multiplying the total number of assets being traded in the market, such as shares, by the price at which they trade at a given point in time[72];
- the 'nominal value of assets in the market', ie their redemption price[73];
- the level of issuance[74]; and
- the 'maturity spectrum', ie the different maturity profiles of assets being traded in a given market.[75]

The use of market neutrality in this third sense continues to be relevant to this day. For example, on 11 November 2022, President Lagarde, in her response to a written question raised by Mr Markus Ferber, MEP, affirmed:

> Regarding your first question, the corporate bond purchase limits continue to be based primarily on the market capitalisation of the issuer group in question to ensure a diversified allocation of purchases across issuers. Market neutrality is an operational tool, not a legal requirement. Generally, it helps to safeguard that the Eurosystem's interventions in the market comply with the Treaty principle of an open market economy with free competition, favouring an efficient allocation of resources.[76]

Our analysis also reveals that when the ECB and its staff use the term market neutrality in the sense of mirroring the composition of a particular market, they normally do so by reference to the ECB's need to ensure compliance with the OME principle. On 16 September 2022, in her response to a Letter from Mr Engin Eroglu, MEP, Christine Lagarde expressed this idea very clearly[77]:

> With regard to your last question on market neutrality, let me underline that this concept is an operational tool. It helps the ECB to ensure compliance of the Eurosystem's interventions in the market with the Treaty principle of 'an open market economy with free competition, favouring an efficient allocation of resources', which is binding on the ECB.

[72]'So far, the market neutrality principle has guided the implementation of our private sector asset purchase programmes' [FN: 'The operationalisation of this principle entails the ECB purchasing securities in proportion to their relative market capitalisation']: Schnabel, From market neutrality (n 71).

[73]'[T]he ECB aims for a market-neutral implementation of the APP and therefore CSPP purchases are conducted according to a benchmark that proportionally reflects the nominal value of eligible bonds in the CSPP-eligible universe': M Draghi, 'Letter from the ECB President to Mr Fabio De Masi, MEP' (29 August 2017) available <https://www.ecb.europa.eu/pub/pdf/other/ecb.mepletter170830_DeMasi.en.pdf?d28413c045c0d596415dd344009d2d57> accessed 19 February 2024.

[74]'Currently, private sector assets are purchased in accordance with the 'market neutrality' principle, which implies that those firms that issue more bonds tend to benefit more from our asset purchase programmes, ignoring broader portfolio rebalancing effects': I Schnabel, 'Societal responsibility and central bank independence' (27 May 2021) available <https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp210527_1~ae50e2be97.en.html> accessed 19 February 2024.

[75]'There is no maturity target for purchases. The purchases are conducted in a flexible manner across all eligible maturities in order to ensure market neutrality'. ECB, 'FAQ on the Public Sector Purchase Programme' (22 February 2023) available <https://www.ecb.europa.eu/mopo/implement/app/html/ecb.faq_pspp.en.html> accessed 19 February 2024.

[76]'European Parliament Monetary Dialogue: Letter from President Lagarde to Mr Markus Ferber, MEP' (November 11, 2022), letter available at this address: <https://www.ecb.europa.eu/pub/pdf/other/ecb.mepletter221111_ferber_1~1feffc15f9.en.pdf?30f53ff43764ad3cb8f28492b0d3abf0> accessed 19 February 2024.

[77]'European Parliament Monetary Dialogue: letter from President Lagarde to Mr Joachim Starbatty, MEP' (September 16, 2022), letter available here: <https://www.ecb.europa.eu/pub/pdf/other/ecb.mepletter220916_eroglu~950206f531.en.pdf> accessed 19 February 2024.

In other instances, when ECB staff used the term market neutrality with this meaning, they mentioned the need for the ECB to refrain from giving a differentiated treatment to specific market actors or sectors. The ECB and its staff normally made these references to market neutrality in the context of discussions about the carbon bias of the APP portfolios. The following excerpt from a Box that was published on the ECB Economic Bulletin Issue 7/2018 illustrates this well:

> The implementation of the APP is guided by the principle of market neutrality and does not positively or negatively discriminate on the basis of environmental or any other criteria. In the specific case of the corporate sector purchase programme (CSPP), which aims to further strengthen the pass-through of the benefits of the asset purchases to financing conditions in the real economy, the purchases of securities issued by non-bank corporations reflect proportionally the market value of all eligible bonds in terms of sectors of economic activity and rating groups.[78]

In the second sentence of the quote, the authors refer to market capitalisation as a way to guide purchases under the CSPP that will ensure that no firm receives a differentiated treatment. The following quote from a speech delivered by Isabel Schnabel, a member of the Executive Board of the ECB, on 17 July 2020, confirms this interpretation:

> One view is that central banks would overstep their mandate if they were to discriminate among investors on the basis of considerations that fall into the realm of fiscal policy. According to this view, market neutrality is the benchmark central banks should use when purchasing bonds issued by corporates.

In a speech delivered on 27 November 2018, also in the context of discussions about the carbon bias of the APP portfolios, Yves Mersch, a member of the Executive Board of the ECB, used the term market neutrality in the following way:

> Moreover, focusing purchases on green bonds would run counter to the requirement to respect the workings of an open market economy and be tantamount to industrial policy. The APP is a tool for macroeconomic stabilisation, not for microeconomic reallocation. *Deviating from market neutrality and interfering with economic policy* risks exposing the ECB to litigation. It is not up to the central bank but to elected governments to decide which industry is to be closed and when. As central bankers, we have to respect and implement legitimate decisions in this context. And the effectiveness of monetary policy has been bolstered by abstaining from normative judgments on the morality of markets and industries.[79]

There are at least three ways of interpreting the use that Mr Mersch makes of the term market neutrality in that speech. The first is to interpret his use of the term in the quote above to be synonymous with respecting the economic or industrial policy set by other institutions. Under this interpretation, in the words in italics, the conjunction 'and' equates rather than distinguishes the two actions that precede it and follow it, respectively. In the last sentence, Mr Mersch articulates the avoidance of any interference with economic policy in normative terms ('abstaining from normative judgements on the morality of markets and industries') and provides a justification for it: to bolster the effectiveness of monetary policy. If market neutrality is synonymous with respecting the economic policy set by other institutions, one could argue that when Mr Mersch

[78]See Economic Bulletin, 7/2018, available at this address: <https://www.ecb.europa.eu/pub/pdf/ecbu/eb201807.en.pdf>, at 21 accessed 19 February 2024.

[79]See the speech by Yves Mersch at the workshop 'Sustainability is becoming mainstream' (November 27, 2018), available here: <https://www.ecb.europa.eu/press/key/date/2018/html/ecb.sp181127.en.html> (Emphasis added) accessed 19 February 2024.

articulates the normative dimension of respecting economic policy he is also articulating a new meaning of market neutrality as moral neutrality. This is the second interpretation of his use of the term market neutrality, which depends on the first interpretation.

The third way is to interpret the reference to a potential interference with economic policy as a rationale of market neutrality rather than as a definition of that term. Under this interpretation, the conjunction 'and' connects an action ('[d]eviating from market neutrality') with the result of that action ('interfering with economic policy').

Given the context in which Yves Mersch used the term of 'market neutrality', ie the policy debate about the possibility of the ECB tilting the APP towards green bonds, and his express concern with litigation risk, we find the third interpretation more convincing. This interpretation rests on the understanding that Mr Mersch is using the term market neutrality in the sense of relying on the composition of a relevant market to guide asset purchases, even if only implicitly: the act that would deviate the ECB from market neutrality is the tilting of asset purchases under APP towards green bonds that opens the quote ('focusing purchases on green bonds'). Under this light, avoiding any interference with economic or industrial policy stands as a rationale for market neutrality: deviating from market neutrality amounts to interfering with economic or industrial policy; adhering to it ensures that the ECB refrains from interfering in economic or industrial policy, which is clearly outside the ECB's mandate.[80]

Based on our analysis of the dataset, (i) an open market economy, (ii) discrimination and (iii) economic policy considerations illustrated in the preceding quotes do not describe meanings of market neutrality that are different from the meaning described in this section, ie market neutrality as mirroring the composition of a particular market. Instead, we will argue that, when the ECB and its staff refer to an open market economy, discrimination and economic policy considerations, they are justifying the decision to use the composition of a relevant market as the guiding criterion of the ECB's asset purchases. In other words, an open market economy, discrimination and economic policy considerations do not evidence new meanings of market neutrality; they are rationales of market neutrality when the term is used in the sense of mirroring the composition of a relevant market.

### Residual categories

In some cases, we were unable to infer the meaning of market neutrality because the authors did not articulate their understanding of market neutrality expressly or there was nothing in the context that would allow us to infer such meaning. We classified these appearances as 'Not available' or 'N/A'. The following excerpt from an ECB Guideline illustrates this kind of appearance:

> The remuneration of non-monetary policy deposits other than government deposits shall take into account the principles of proportionality, market neutrality and equal treatment.[81]

In other cases, lacking an express articulation of the meaning of market neutrality, we were unable to infer that meaning from the context in which the relevant author used the term because they had used the term with different meanings in the same context albeit inconsistently. We categorised these appearances as 'Unclear'. The following quote from a speech delivered by Isabel Schnabel, a member of the Executive Board of the ECB, on 14 June 2021, illustrates the lack of an express articulation of the meaning of market neutrality:

[80]See Arts 119 and 127(1) TFEU.

[81]See Guideline (EU) 2019/671 of the European Central Bank of 9 April 2019 on domestic asset and liability management operations by the national central banks (recast) (ECB/2019/7), Art 4.2.

> While the concept of market neutrality is related to the Treaty principle of 'an open market economy with free competition, favouring an efficient allocation of resources', it is not per se a rule in primary law.[82]

In the same speech, Ms Schnabel used the term market neutrality in the first sense, ie the avoidance of unnecessary distortions of market functioning,[83] and in the third sense, ie the characteristic of a portfolio that mirrors the composition of a reference market.[84] This made it impossible for us to infer the implicit meaning with which she had used the term market neutrality in the quote above.

With these two residual categories, 'N/A' and 'Unclear', we do not mean to suggest that the relevant uses of market neutrality lacked a meaning, including a latent meaning. Instead, they group all of those appearances whose meaning we were not able to infer from the textual data in our data sample.

### E. Discussion

A basic quantitative analysis reveals that speeches from the President and the members of the Executive Board of the ECB are the main source of references to market neutrality and related terms (Diagram 1). This was particularly the case when we narrowed down the scope of the analysis to views that can be attributed to the ECB (Diagram 2).[85]

A basic quantitative analysis also reveals that the ECB and its staff have made a significant use of the three meanings of market neutrality identified in the preceding section. At the end of the coding process, out of a total of 216 appearances, we categorised 58 appearances as uses of market neutrality in the first sense, ie the avoidance of unnecessary distortions of market functioning, 31 appearances as uses of market neutrality in the second sense, ie a particular investment strategy, and 83 appearances as uses of market neutrality in the third sense, ie the characteristic of a portfolio that mirrors the composition of a reference market. Moreover, we classified 23 as N/A and 21 as Unclear. Diagram 3 provides a graphic description of the result of this basic quantitative analysis.

An analysis of these five categories over time reveals interesting facts. Diagram 4 shows that 2021 is the year where we registered the highest number of appearances of market neutrality and related terms. Diagram 5 illustrates that the use that the ECB and its staff have made of market neutrality in its second sense is very concentrated in time: with the exception of seven references, which appeared in two sources,[86] the use of market neutrality in its second sense is concentrated between December 2004 and May 2013. For the past ten years, the ECB and its staff have used market neutrality almost exclusively in one of the other two senses; two meanings, which save for occasional appearances, had never been used prior to 2015. In its first sense, market neutrality marked an all-time high in 2020. In its third sense, it marked an all-time high in 2021.

[82]Schnabel, From market neutrality (n 71), available <https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp210614~162bd7c253.en.html> accessed 19 February 2024.

[83]'For example, the Bank of England's Corporate Bond Purchase Scheme (CBPS) follows a principle similar to market neutrality. The CBPS is conducted with the objective of minimising the impact of asset purchases on the relative borrowing costs across sectors': Schnabel, From market neutrality (n 71).

[84]'The ECB already now deviates from market neutrality in several instances. For example, the application of eligibility criteria for purchases implies that the ECB's bond holdings are not necessarily proportional to market capitalisation[.]': Schnabel, From market neutrality (n 71).

[85]This narrower dataset excludes all uses of the term made by staff of the ECB whose views do not represent the views of the ECB. To distinguish between uses of market neutrality that could be attributed to the ECB and those that could not, we classified each use according to the 'Type of author'. We registered those authors whose views cannot be attributed to the ECB as 'Other ECB staff'. Out of a total of 216 appearances, we registered 77 by Other ECB staff and 139 that can be attributed to the ECB.

[86]A Working Paper published in March 2014 and an Occasional Paper published in November 2017.

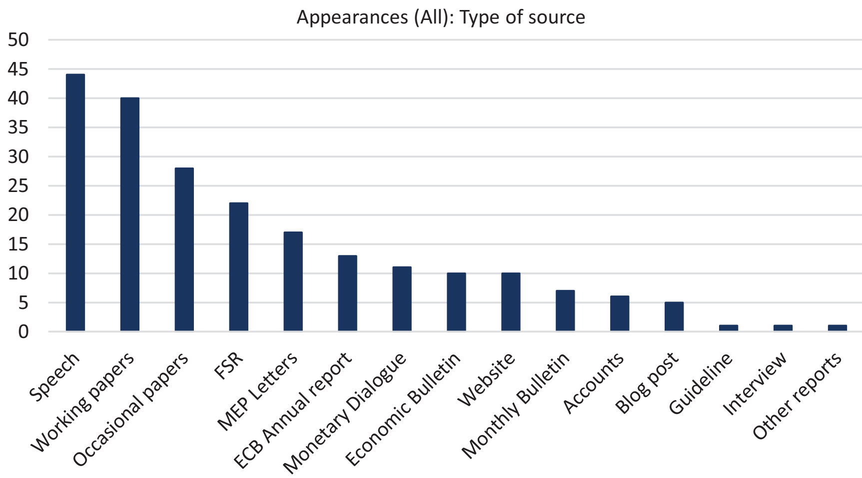


**Diagram 1.** Number of appearances per type of source (All views).

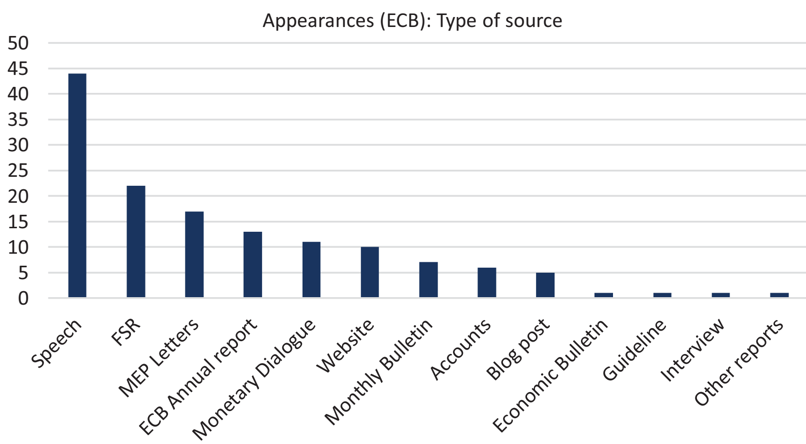


**Diagram 2.** Number of appearances per type of source (ECB views).

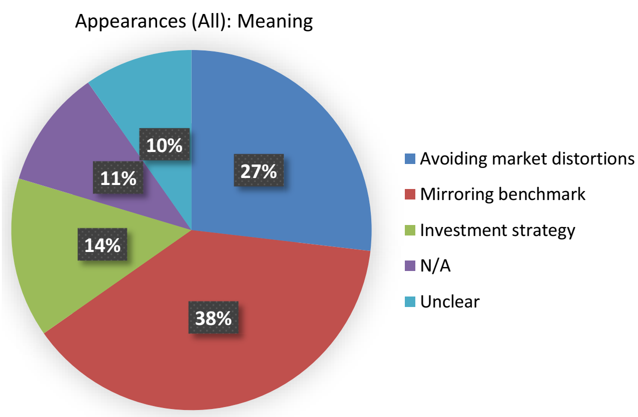


**Diagram 3.** The meanings of market neutrality in the euro area's monetary policy (All views).

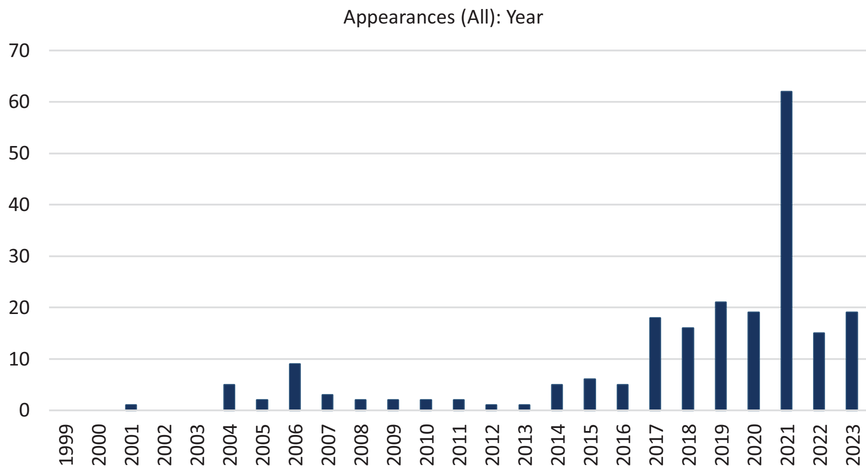


**Diagram 4.** The use of market neutrality and related terms over time in the euro area monetary policy (All views).

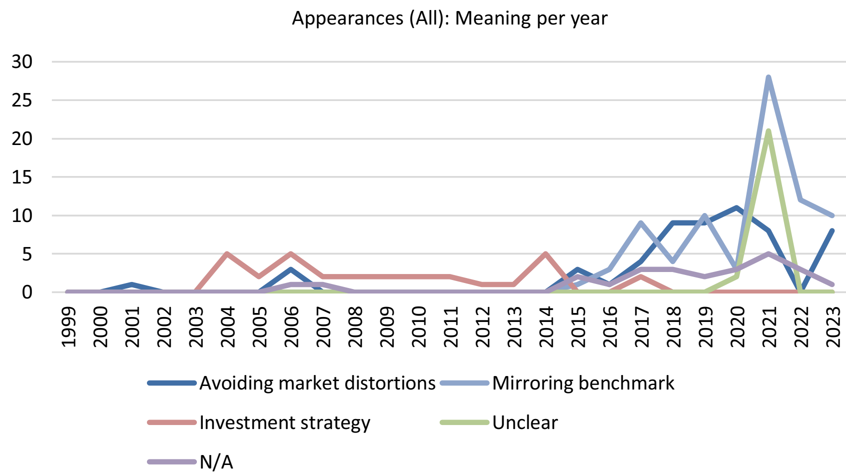


**Diagram 5.** The meanings of market neutrality in the euro area's monetary policy over time (All views).

Despite the regular presence of the second meaning of market neutrality (ie a particular investment strategy) until 2014, we will argue that this sense of market neutrality is irrelevant for the euro area monetary policy. When the ECB and its staff used market neutrality in this second sense, they did so to describe developments in the hedge fund industry and in contexts that were not directly relevant to the euro area's monetary policy.[87] In the context of the euro area monetary policy, the ECB and its staff only used market neutrality in its first (ie the avoidance of unnecessary distortions of market functioning) and third (ie the characteristic of a portfolio that mirrors the composition of a reference market) meanings.

[87] Out of the 31 appearances of market neutrality that we categorised under this second sense, 21 were in a Financial Stability Review. The remaining appearances were in the ECB Monthly Bulletin from January 2006 (3), in a Working Paper published in 2014 (5) and in an Occasional Paper published in 2017 (2), both of which were written by Other ECB staff. In all of these cases, market neutrality was used to describe the hedge funds' investment strategies.

This basic quantitative analysis also sheds light on the perceived lack of clarity in the use of market neutrality and related terms. As explained in Section 2.D.4, we categorised as 'Unclear' those appearances where, lacking an express articulation of the meaning of market neutrality, we were unable to infer the meaning from the context in which the relevant author used the term with different meanings in the same context albeit inconsistently. The fact that we categorised 10 per cent of appearances as 'Unclear' evidences the level of ambiguity of the term in the euro area's monetary policy. In practice, however, these appearances were concentrated in a small number of sources: 4 out of 100 that comprise our data sample.[88] They were also concentrated in time: save for two appearances in 2020, they all occurred in 2021.

Additionally, in 11 per cent of appearances we were unable to discern the meaning of the term market neutrality from the context in which it was used. We classified these appearances as 'N/A'. Unfortunately, a summative content analysis does not allow us to provide conclusive explanations of this phenomenon. This would require a different type of analysis, one that would allow us to investigate the context in which market neutrality and related terms were used beyond the textual data.[89] Nevertheless, we can provide some tentative explanations. One possible explanation is that the ECB and its staff did not consider it important to clarify the meaning of the term. This could be the case if they were unaware of the various senses in which the term was being used. An analysis of the use of each of the meanings of market neutrality over time presents another possible explanation. As Diagram 4 illustrates, the number of instances where the ECB and its staff were assuming the meaning of market neutrality increased in 2021 and remained relatively high thereafter. This was also the year when most of the debates around the ECB's review of its monetary policy strategy took place.[90] The review focused on market neutrality in the context of the ECB's evaluation of the impact of climate change on monetary policy.[91] At a time when market neutrality was being the object of so much debate, perhaps ECB staff did not feel the need to expressly articulate the sense in which they were using market neutrality, relying on the debate around the strategy review for implicit context.

We could use a similar logic to explain the relatively high frequency of appearances of market neutrality categorised as N/A *after* 2021: the debate around the review of the ECB's monetary policy strategy may have helped clarify the meaning of market neutrality in the context of the euro area's monetary policy so that the ECB and its staff did not feel the need to expressly articulate the meaning of the term. Indeed, Diagram 5 illustrates that 2021 marked a change in the prevailing understanding of the meaning of market neutrality within the ECB. Between 2015 and 2020, the frequency in the use of market neutrality in its first and third meanings was more or less the same, the first meaning clearly predominating in 2020. But in 2021 this trend reversed: the ECB and its staff used the term market neutrality in the third sense more than in the first sense; in fact, considerably more. Diagram 6 shows that similar trends can be observed when we narrow the scope of the dataset to views that can be attributed to the ECB.

In any event, although to this date the ECB and its staff continue to use market neutrality in the third sense (ie the characteristic of a portfolio that mirrors the composition of a reference market) more than in the first (ie the avoidance of unnecessary distortions of market functioning), we

[88]These sources were one Annual Report, two speeches from Ms Isabel Schnabel, and a Working Paper from other ECB staff.

[89]For example, interviews with relevant ECB staff.

[90]The ECB conducted a review of its monetary policy strategy between January 2020 and July 2021. See <https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200123~3b8d9fc08d.en.html> accessed 19 February 2024; <https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200402~942a1358ee.en.html> accessed 19 February 2024. This was only the second time the ECB reviewed its monetary policy strategy since it was first adopted in October 1998. The first time the ECB reviewed its monetary policy strategy was in 2003. See <https://www.bis.org/review/r030721c.pdf> accessed 19 February 2024.

[91]See eg Letter from the ECB President to Mr Markus Ferber, MEP (5 February 2021) available <https://www.ecb.europa.eu/pub/pdf/other/ecb.mepletter210205_Ferber~382cd05490.en.pdf?e7915a6f9a95415ad3c5142a605de1e8> accessed 19 February 2024.

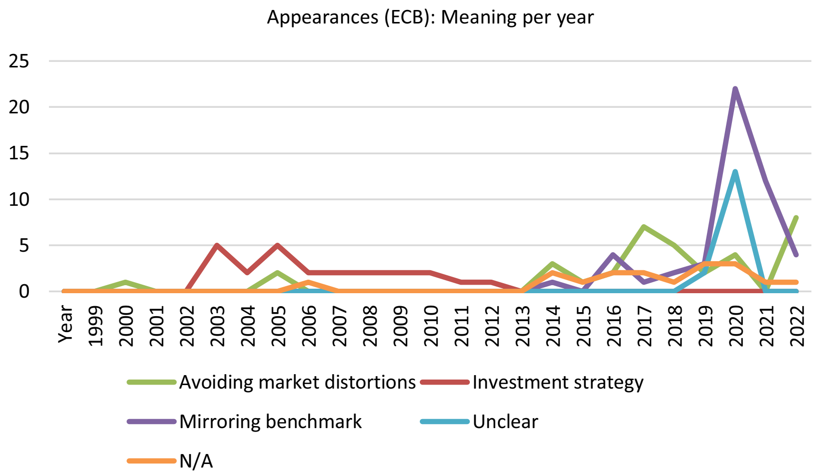


**Diagram 6.** The meanings of market neutrality in the euro area's monetary policy over time (ECB views).

should be wary of concluding from this simple fact that the third sense is the main sense. First, in spite of a sharp decline of the use of market neutrality in its first meaning in 2022, its use has rebounded in 2023 to the point where it almost matches the level of usage of market neutrality in its third meaning. Diagrams 5 and 6 evidence that such a rebound was observable both in views that can be attributed to the ECB and in views by all ECB staff. The fact that the ECB and its staff continue to use market neutrality in its first meaning even after the outcome of the monetary policy strategy review in July 2021 reinforces the argument that market neutrality is a polysemous term. Moreover, there are a few instances where the same member of staff or decision-making body has used the term market neutrality with the two different meanings at two different points in time, which suggests that the polysemy of market neutrality is evident both at the institutional level and the level of individual members of staff and decision-making bodies.[92] In some cases, the same person or decision-making body has even used the term market neutrality with two different meanings on the same occasion.[93]

The summative content analysis that we have developed illustrates that market neutrality is a polysemous term. To date, however, all of the academic analyses of the legal nature of market neutrality attribute a single meaning to this term: the third of the three meanings that we identified above, ie the characteristic of a portfolio that mirrors the composition of a reference market. In the next section, we develop an analysis of the legal nature of the first and third meanings of market neutrality identified in the summative content analysis, the only meanings that are relevant for the euro area monetary policy. We conclude that the legal nature of the term depends on the sense in

[92]Compare, for example, the statements made by Mario Draghi, a former President of the ECB, at the Monetary Dialogue of 21 June 2016 (<https://www.europarl.europa.eu/committees/en/econ/econ-policies/monetary-dialogue>) accessed 19 February 2024, where he used market neutrality in the first sense, and his statements in two letters dated as of 29 August 2017 <https://www.ecb.europa.eu/pub/pdf/other/ecb.mepletter170830_DeMasi.en.pdf?d28413c045c0d596415dd344009d2d57> accessed 19 February 2024; <https://www.ecb.europa.eu/pub/pdf/other/ecb.mepletter170830_TrebesiusStarbatty.en.pdf?169d60e9624eb161008425211e9e99e2>) accessed 19 February 2024, written in response to questions raised by MEPs, where he used market neutrality in the third sense.

[93]For example, in a speech delivered on 3 March 2021, Ms Isabel Schnabel defined market neutrality by citing Mr Benoît Cœuré's speech quoted above, where he had used market neutrality in its first sense, and immediately afterwards Ms Schnabel questioned whether, in the presence of market failures, market neutrality could be the 'appropriate benchmark'. See I Schnabel, 'From green neglect to green dominance?' (3 March 2021) available <https://www.ecb.europa.eu/press/key/date/2021/html/ecb.sp210303_1~f3df48854e.en.html> accessed 19 February 2024. See also the 2019 ECB Annual Report.

which the term is used. Our conclusion reveals the complexity of the legal nature of market neutrality and expands the contours of the existing academic debate.

## 3. The legal nature of market neutrality

### *A. In its first meaning, market neutrality is a principle of primary EU law*

#### *Dissection of the OME principle*

The Treaties mention the OME principle five times: twice in Article 119 TFEU, which opens Title VIII, dedicated to economic and monetary policy; once in Article 120 TFEU, which opens the specific chapter on economic policy; once in Article 127 TFEU, which, in turn, opens the chapter on monetary policy; and once in Article 2 of Protocol 4 on the European System of Central Banks and the ECB. Neither the Treaty of Maastricht, which introduced these four provisions, nor the working documents that led to its adoption define the content of the principle.

Unfortunately, the very few CJEU decisions that examine the OME principle do not examine its legal content. For example, in *Échirolles*, a reference for a preliminary ruling raised the question whether the provisions in the EC Treaty relating to the internal market precluded the fixing of book prices in France. In its ruling, the Court only examined the effect of the obligations that the principle imposes on Member States but it did not examine the content of those obligations.[94] In his Opinion in *Schindler*, Advocate General Gulmann provides a very succinct definition of an 'open market economy': 'In an open market economy it is market forces and not public regulation which should in principle determine what supply of certain goods or services there should be'.[95] Yet, while this definition provides some clarity about the meaning of the term 'open market economy' as a mechanism to allocate society's resources,[96] it does not shed much light on the legal content of the principle.[97] For example, an important question remains unanswered: under what conditions might public regulation substitute markets in the determination of the supply and demand of certain goods or services?

One of us has recently argued that the OME principle is comprised of four elements.[98] The first element is a 'market economy'. Neither the Treaty of Maastricht, which introduced the OME principle in the Treaties, nor the working documents that led to its adoption provide a definition of this term. An analysis of the working documents, however, suggests that the drafters of the Treaty of Maastricht used the term 'market economy' to describe the system through which society would

[94]The Court concluded that the principle lacks direct effect: no right is vested in any person to have markets work efficiently, or to have policies designed to make markets work efficiently. See Case C-9/99 *Échirolles Distribution SA v Association du Dauphiné and Others* (2000) ECR I-8207, para 25. After *Échirolles*, the Court has confirmed this interpretation in other decisions. See, eg, Case C-484/08 *Caja de Ahorros y Monte de Piedad de Madrid v Asociación de Usuarios de Servicios Bancarios (Ausbanc)* (2010) ERC I-4785, para 46.

[95]Case C-275/92, *Her Majesty's Customs and Excise v Gerhart Schindler and Jorg Schindler* (1994) ERC-I-1039, Opinion of AG Gulmann, para 41.

[96]This definition resonates with the use that the drafters of the Treaty of Maastricht made of the term 'market economy' to describe a system through which society would allocate its resources. See eg J Delors, *Report on Economic and Monetary Union in the European Community (1989)* paras. 27–9. Available <https://www.cvce.eu/obj/report_on_economic_and_monetary_union_in_the_european_community_12_april_1989-en-725f74fb-841b-4452-a428-39e7a703f35f.html> accessed 19 February 2024. The use of the terms '*système* de marchés' and '*système* économique de marché' in the proposed Arts 3A(1) and 102A, respectively (the precedents of current Arts 119(1) and 120 TFEU), by the European Council (1991) in its Draft Treaty on Union, also seems to support this view.

[97]The Opinion is part of a rather different legal culture which, used to juxtapose market rationality to legal regulation. For a refreshing approach which emphasises the hybrid nature of markets see K Pistor, *The Code of Capital* (Princeton University Press 2019).

[98]J Solana, 'Market Efficiency as a Directive Principle of EU Monetary Policy' in A Chadwick, E Lozano-Rodríguez, A Palacio-Lleras and J Solana (eds), *Markets, Constitutions, and Inequality* (Routledge 2022) ch 7.

allocate its resources.[99] For the purposes of this essay, we shall define a market economy as a system where resources are allocated through prices, which result from the interaction of different actors in markets, some seeking to buy goods or services and others looking to sell them.

The second element in the OME principle is the 'open' nature of the market economy. Just as the Treaties do not provide a definition of a 'market economy', they do not provide a definition of its open nature either. Nevertheless, the working documents leading to the adoption of the Treaty of Maastricht suggest that, in this context, the word 'open' describes the conditions under which economic actors can access markets.[100] In particular, an open market economy can be understood as one that is easy to access for economic actors within the internal market and outside of it.[101] Internally, an open market economy may be seen as the outcome of the four fundamental freedoms, especially the free movement of capital.[102] Externally, open markets can be understood as a declaration of intention to have the internal market connected to the global economy.[103]

The third element in the OME principle is 'free competition'. An analysis of Article 3(1)(g) of the Treaty Establishing the Economic Community ('EC Treaty') and the working documents that led to the adoption of the Treaty of Maastricht suggest that the reference to 'free competition' in the OME principle should be read as the avoidance of any distortion on competition by private or public economic actors.[104] The reference to an internal market where competition is not distorted was excised during the process of approval of the Lisbon Treaty (under the pressure of France)[105] and it was moved to Protocol 27 TFEU on Internal Market and Competition. Yet, the 'demotion' from the text of the Treaty to the Protocol does not seem to have affected the legal status of the principle of undistorted competition. As it has been recognised by the CJEU,[106] the Protocol contains a fundamental principle of the economic constitutional law of the EU.

The fourth and last element is the formula 'favouring an efficient allocation of resources'. The introduction of the efficiency formula serves an explanatory purpose: it identifies an efficient allocation of resources as the normal outcome of an open market economy. As we shall see in the next section, this explanatory purpose defines the relationship between the four elements of the OME principle.

In his dissection of the OME principle, one of us also examined the relationships between the four elements that comprise the principle: (i) a 'market economy' that is (ii) open, (iii) where actors can compete freely and that (iv) favours an efficient allocation of resources. He argued that the relationship between the first three elements, which are encapsulated in the wording 'an open

[99] See eg Delors, (n 96), paras. 27–9. The use of the terms '*système* de marchés' and '*système* économique de marché' in the proposed Arts 3A(1) and 102A, respectively (the precedents of current Articles 119(1) and 120 TFEU), by the European Council (1991) in its Draft Treaty on Union, also seems to support this view.

[100] Solana. Market Efficiency (n 98).

[101] See eg Case C-275/92 *Her Majesty's Customs and Excise v Gerhart Schindler and Jörg Schindler* (1994) ERC I-1039, Opinion of AG Gulmann, paras 117, 121.

[102] See eg Case C-452/01 *Margarethe Ospelt and Schlössle Weissenberg Familienstiftung* (2003) ERC I-09743, Opinion of AG Geelhoed, para 34.

[103] See eg Consolidated version of the Treaty on the Functioning of the European Union (TFEU) (2012) OJ C 326/47, art 206.

[104] In support of this view, see also T Tridimas, 'Community Agencies, Competition Law, and the ESCB Initiatives on Securities Clearing and Settlement' 29 (2009) Yearbook European Law 216, 274.

[105] The question became an issue when in the draft of the Constitutional Treaty 'undistorted competition' was elevated to an objective of the European Union.

[106] Case C-496/09 *Italy vs European Commission* ECLI:EU:C:2011:740. In paragraph 60, the Court makes clear that the Protocol is legally binding for the interpretation of Art. 3(3) TEU: 'As to the seriousness of the infringement, the vital nature of the Treaty rules on competition must be recalled, in particular those on State aid, which are the expression of one of the essential tasks with which the European Union is entrusted. At the time of the Court's assessment of the appropriateness and the amount of the present penalty payment, that vital nature is apparent from Article 3(3) TEU, namely the establishment of an internal market, and *from Protocol No 27 on the internal market and competition, which forms an integral part of the Treaties* in accordance with Article 51 TEU, and states that the internal market includes a system ensuring that competition is not distorted' (emphasis added)

market economy with free competition' used in Article 127(1) TFEU, and the fourth element (ie an efficient allocation of resources) is functional: 'an open market economy with free competition' is only justified *as long as* it leads to 'an efficient allocation of resources'.[107] This led him to conclude that interfering with the operation of an open market economy with free competition could be justified if such a market economy did not lead to an efficient allocation of resources.[108] The choice of a market economy and an efficient allocation of resources therefore go hand in hand.[109] Seen in this light, the OME principle is directive in nature. A directive principle is one that indicates to the interpreter a sense of finality with the aim of promoting certain activities, but that leaves plenty of room for the interpreter to choose and define how to pursue that finality.[110] In our reconstruction, market efficiency is the criterion that 'directs' the interpretation of the OME principle.[111]

The directive criterion of the OME principle would allow us to define the content of the principle by excluding, at least, certain forms of economic organisation (most notably, a form of economic organisation that is entirely run by the State): the OME principle imposes a floor upon which it is possible to elaborate an array of different economic options.[112] Importantly, however, this interpretation is based on a very specific economic theory (ie that which argues that markets allocate resources more efficiently than State-coordinated efforts), not on law: as much as the drafting of Title VIII of the TFEU on Economic and Monetary Policy may be driven or inspired by this particular economic theory, the Treaties do not enshrine this economic theory, they enshrine a very specific normative criterion (ie efficiency in the allocation of resources) as a directive principle of EU law. Therefore, we suggest that a formulation of the legal content of the OME principle that focuses on its directive criterion is more appropriate: when markets are able to allocate resources efficiently, an EU institution must minimise the distortion of market operation in order to favour the efficient allocation of resources; yet if the institution's technical assessment were to reveal that markets are failing to allocate resources efficiently and that such a failure might hinder the institution's ability to achieve its objectives, it must address that failure.

[107] See Solana, 'Market Efficiency' (n 98). In its resolution on the ECB's 2021 annual report, the European Parliament supports this interpretation: 'The European Parliament [ … ] Notes that, while the concept of market neutrality is related to the principle of "open market economy with free competition", the TFEU clearly stipulates that the ECB should pursue its mandate by favouring an efficient allocation of resources; invites the ECB, respecting its independence, to address market failures and ensure the efficient allocation of resources over a long-term horizon, while remaining as apolitical as possible; notes that the ECB has already deviated from market neutrality in several instances'. European Parliament, 'Resolution on the European Central Bank – Annual Report 2021' (16.02.2022), para 27, available <https://www.europarl.europa.eu/doceo/document/TA-9-2022-0029_EN.html> accessed 19 February 2024. For a different view on the relationship between market neutrality and market efficiency, see Dietz, Green Monetary Policy (n 16) 428–32.

[108] In a recent testimony before the European Parliament, President Lagarde shared a similar view:

> '[W]e have growing evidence that financial markets and banks are currently not fully pricing and managing the potential risks that may stem from climate change and the transition to a carbon-neutral economy. And as a result we might actually wonder whether this efficient allocation of resources is currently delivered upon, which would perfectly justify that we might deviate from this operationalisation, by way of market neutrality concept, of [the OME Principle]'.

See Lagarde's testimony (n 6) 6.

[109] Read in this way, the Treaty has taken a stance in the controversial realm of economic theories: an open market economy with free competition is more efficient than other ways of organising production and distribution. See C Hopman, 'Monetary Policy and the Principle of an Open Market Economy with Free Competition' (2018) ESCB Legal conference, at 40.

[110] Here, we follow the distinction between regulative and directive principles as introduced by L Ferrajoli, *La costruzione della democrazia* (Laterza 2021) 147; a similar distinction is also drawn by M Atienza, *El Derecho Como Argumentación* (Ariel 2012) 163–9.

[111] Cf Solana, 'Market Efficiency' (n 98). For a different interpretation of the role of market efficiency see Dietz, Green Monetary Policy (n 16) 407–9.

[112] Tridimas, Community Agencies (n 104) 273.

### *The first meaning of market neutrality is the definition of the OME principle in the euro area's monetary policy*

The CJEU has acknowledged that, as a general principle, '[the] application [of the OME principle] calls for complex economic assessments which are a matter for the legislature or the national administration'.[113] This interpretation is in line with other CJEU case law. For example, in *Gianni Bettati* the CJEU affirmed that 'general principles of the common market are to be applied in conjunction with the respective chapters of the Treaty devoted to their implementation'.[114] Following this line of reasoning, we can conclude that a general principle like the OME principle has to be interpreted in the specific context of the competences exercised by the Union. The ECB is the competent authority to design and implement monetary policy in the euro area.[115] That exclusive competence carries with it the normative power to define the application of the OME principle, as a general principle, in the specific context of the euro area's monetary policy.

We argue that the first meaning with which the ECB has used the term market neutrality defines the OME principle in the euro area's monetary policy.[116] It does so by focusing on the first three elements of the principle. Market neutrality identifies a legal obligation arising from the first element of the OME principle, a 'market economy': the ECB must refrain from distorting the operation of market forces that lead to price discovery. Moreover, market neutrality identifies a legal obligation arising from the second and third elements: the ECB must avoid any unnecessary distortion of competition by refraining from discriminating market participants, either positively or negatively. If the previous points are correct, then we can conclude that market neutrality is part of the ECB's definition of the OME principle in the euro area's monetary policy. Consequently, market neutrality being an integral part of the OME principle, the legal nature of market neutrality cannot be different from the legal nature of the OME principle: in its first meaning, market neutrality is primary EU law.

To date, the main academic analyses of the legal nature of market neutrality reach a different conclusion: that market neutrality is not primary law. Smits and Steinbach argue that market neutrality is not legally binding but they only regard market neutrality in its third meaning. Zilioli and Ioannidis acknowledge the first and third meanings of market neutrality that we identified in Section 2, but they base their analysis of the legal nature of the term only on the third meaning and conclude that '[it] is not a legal rule'.[117] For Dietz, the source of market neutrality's legal force goes beyond the OME principle: she points to the principle of non-discrimination,[118] the price stability objective and the central bank's independence.[119] Nevertheless, she rejects the argument that market neutrality is primary EU law.[120] Ultimately, according to Dietz, market neutrality may be better characterised either as a 'general functionality' of monetary policy and a reflection of the institutional set-up of the ECB, including its independence, or as 'a general principle requiring the

[113]C-9/99, *Échirolles Distribution SA v Association du Dauphiné* (2000) ECR I-8207, para 25.

[114]C-341/95 *Gianni Bettati and Safety Hi-Tech SRL* (1998) ECR I-4355, para 75.

[115]See Arts 3(1)(c) and 127(2) TFEU.

[116]According to Art 120 TFEU, the OME principle binds the Union and its Member States in the context of economic policy. It is not up to the ECB to define the principle in the context of economic policy. Other institutions will be responsible for that. In this sense, we can regard market neutrality as part of the OME principle: it only defines the OME principle in one of the two policy areas where the principle operates: monetary policy.

[117]Ioannidis and Zilioli, Climate Change (n 16) 389.

[118]See Dietz, Green Monetary Policy (n 16) 430.

[119]'[Market neutrality] is a general functionality of monetary policy and closely linked to the consequences of the institutional set-up of central banks as independent institutions. [ … ] [I]t is contrary to the foundations of monetary policy, with its primacy on price stability, to distinguish between market participants on the basis of any other policy criteria'. Dietz, Green Monetary Policy (n 16) 430.

[120]Dietz, Green Monetary Policy (n 16) 421. Interestingly, in her speech on market neutrality, Isabel Schnabel, a member of the Executive Board of the ECB, also used market neutrality in both the first and third senses identified in Section 2 and concluded that market neutrality was not primary law. See Schnabel, 'From market neutrality', n 71.

ECB to abstain from setting policy incentives other than those directly linked to price stability'.[121] Ramos, Cabrales and Sánchez also deny the status of primary law for market neutrality because they describe its nature as a social norm rather than a legal norm. In their reconstruction, market neutrality is the outcome of an environment where the main agents are economic and financial experts, and members of financial institutions. Market neutrality is formed through the convergence of opinions amongst these actors, but it does not create legal obligations.[122]

One could argue that the first meaning with which the ECB has used the term market neutrality cannot be primary law because it does not cover all of the elements in the OME principle; in particular, the fourth element of the OME principle, ie the efficiency formula. We reject that view. As it is formulated in the Treaties, the OME principle stands on the assumption that, under normal circumstances, the operation of markets will lead to an efficient allocation of resources. Hence, under normal circumstances, by minimising the impact of monetary policy on the operation of the price mechanism and on competition, ie by adhering to the ECB's first meaning of market neutrality, the ECB will be favouring an efficient allocation of resources. In other words, under normal circumstances, the normative element of the principle continues to direct the ECB's monetary policy, albeit latently. Only if a technical evaluation by the ECB were to reveal that the operation of markets could lead to an inefficient allocation of resources would the normative element of the OME principle become more patent.[123]

The legal obligations that the first meaning of market neutrality articulates for the ECB (ie to refrain from distorting the operation of market forces that lead to price discovery, including any distortion on competition) do not operationalise the OME principle; they are in need of operationalisation themselves. As we shall argue in the next section, the third meaning of market neutrality, ie the characteristic of portfolios that mirror the composition of a reference market, is one of the measures that the ECB uses to operationalise these obligations.

## B. In its third meaning, market neutrality is a rule of secondary EU law

### The third meaning of market neutrality is one of several measures to operationalise the OME principle

The following quote from Mr Mario Draghi's response to a letter from an MEP on 29 August 2017 indicates that the rationale for the third meaning of market neutrality, ie the Eurosystem mirroring the composition of a given market when allocating its purchases under the APP, was the need to comply with the Eurosystem's own definition of the OME principle:

> The universe of CSPP-eligible bonds is deliberately broad and its composition is primarily guided by monetary policy and risk management considerations. In pursuing its objective of maintaining price stability, the ECB is mandated to act in accordance with the principle of an open market economy with free competition, favouring an efficient allocation of resources. Consequently, the ECB aims for a market-neutral implementation of the APP and therefore CSPP purchases are conducted according to a benchmark that proportionally reflects the nominal value of eligible bonds in the CSPP-eligible universe.[124]

[121] See Dietz, 'Green Monetary Policy' (n 16) 430.

[122] Ramos, Cabrales, Sanchez, n 24.

[123] Whether the ECB conducted such a technical evaluation before the launch of the APP and during its implementation is an empirical question that falls beyond the scope of our paper. Nevertheless, we do not need to answer this empirical question to argue that, in theory, market neutrality could define the OME principle, its directive element being latent.

[124] Letter from the ECB President to Ms Ulrike Trebesius and Mr Joachim Starbatty, MEPs (29 August 2017) available <https://www.ecb.europa.eu/pub/pdf/other/ecb.mepletter170830_TrebesiusStarbatty.en.pdf?169d60e9624eb161008425211e9e99e2> accessed 19 February 2024.

Indeed, when used with its third meaning, market neutrality is often associated with a 'benchmark'.[125] Interestingly, however, the market neutrality benchmark has referenced different parameters. For example, in the quote from Mr Draghi presented above, the benchmark reflects the nominal value of eligible bonds in the CSPP-eligible universe. In later uses of the term market neutrality in its third sense, however, the benchmark focuses on the market value of eligible bonds.[126] We shall refer to the former benchmark as the 'nominal value benchmark' and to the latter benchmark as the 'market capitalisation benchmark'.

Yet these two benchmarks were not the only operational measures that the Eurosystem introduced in order to implement its own definition of the OME principle, ie to minimise distortions on market functioning. For example, the Eurosystem introduced limits on how many assets from the same issue the relevant national central banks (NCBs) tasked with the implementation of the APP can buy.[127] For the private sector purchase programmes, the issue share limit was 70 per cent, with lower limits for the CSPP in specific cases.[128] In the PSPP, the issue share limit was originally 25 per cent per international securities identification number (ISIN) and was later reviewed.[129]

Similarly, the Eurosystem introduced limits on how many assets from the same issuer the relevant NCBs could buy. For example, under the PSPP, the Governing Council originally indicated an aggregate limit of 33 per cent of an issuer's outstanding securities to all eligible marketable debt securities.[130]

Additionally, the Eurosystem distributed asset purchases along the yield curve to buy assets with different maturities. For example, at the end of 2018, the remaining maturity of assets in the PSPP portfolio ranged from 1 year to 30 years whereas the remaining maturity of assets under the CSPP ranged from 6 months to 30 years. No maturity restrictions were defined for the CBPP3 or the ABSPP.[131]

Furthermore, the Eurosystem used a broad set of counterparties and adopted a wide range of transparency tools to minimise the informational advantages for eligible counterparties.[132] These measures allowed the Eurosystem to avoid persistent effects in the micro-structure of bond market segments and also fostered competition.[133]

[125]See eg speech by Schnabel available <https://www.ecb.europa.eu/press/key/date/2020/html/ecb.sp200717~1556b0f988.en.html> accessed 19 February 2024. See also this other speech by Schnabel <https://www.ecb.europa.eu/press/key/date/2020/html/ecb.sp200928_1~268b0b672f.en.html> accessed 19 February 2024.

[126]See eg Schnabel, 'From Market neutrality' (n 71). In the context of the CBPP3, see <https://www.ecb.europa.eu/mopo/implement/app/html/ecb.faq_cbpp3.en.html> accessed 19 February 2024.

[127]The implementation of the APP was decentralised. For detail of the various NCBs responsible for the implementation of each of the programmes under the APP, see F Hammermann, K Leonard, S Nardelli and J von Landersberger, 'Taking Stock of the Eurosystem's Assets Purchase Programme After the End of the Net Asset Purchases' 2 (2019) Economic Bulletin at 76, available <https://www.ecb.europa.eu/pub/pdf/ecbu/eb201902~a070c3a338.en.pdf> accessed 19 February 2024.

[128]See Decision (EU) 2016/948 of the European Central Bank of 1 June 2016 on the implementation of the corporate sector purchase programme (ECB/2016/16), Art 4(1). See Hammermann et al (n 127) at 74.

[129]See Decision (EU) 2015/774 on a secondary markets public sector asset purchase programme (ECB/2015/33), Art 5(1). In November 2015, the Governing Council raised the issue share limit to 33 per cent subject to case-by-case verification that it would not lead to the Eurosystem having a blocking majority for the purpose of collective action clauses (in which case it was set at 25 per cent). See Decision (EU) 2015/2101 of the European Central Bank of 5 November 2015 amending Decision (EU) 2015/774 on a secondary markets public sector asset purchase programme (ECB/2015/33). In April 2016, the Governing Council introduced different issue share limits for different types of securities. For example, the issue share limit for eligible marketable debt securities issued by eligible international organisations and multilateral development banks was later set at 50 per cent per ISIN. See Decision (EU) 2016/702 of the European Central Bank of 18 April 2016 amending Decision (EU) 2015/774 on a secondary markets public sector asset purchase programme (ECB/2016/8), Art 1(2).

[130]See ECB Decision (EU) 2015/774, Art 5(3). The issuer limit was raised to 50 per cent of the outstanding securities of an issuer which is an eligible international organisation or a multilateral development bank. See ECB Decision (EU) 2016/702, Art 1(2).

[131]See Hammermann et al (n 127) at 74.

[132]Ibid., at 78.

[133]Ibid.

Lastly, in order to avoid temporary market dominance, the Eurosystem aimed to maintain a continuous market presence throughout the day.[134] When instructing the NCBs tasked with implementing asset purchases, the Governing Council set average monthly targets, which included monthly purchase guidance for each programme.[135] In all months, the purchase guidance was expressed in monthly totals, rather than strict daily volumes, providing flexibility in the day-to-day execution of purchases.[136] When setting these monthly targets, the Governing Council took into account 'seasonal patterns in fixed income market activity, such as the decline in market liquidity from mid-July to late August and in December'.[137] Purchase activity was front and back-loaded around these periods to minimise market distortions.[138]

The Eurosystem also introduced other operational measures in the various programmes under the APP that were not aimed at minimising distortions on market functioning. Most notably, in the PSPP, the Eurosystem distributed asset purchases across jurisdictions in a way that would bring 'the share of the PSPP portfolio into closer alignment with the respective national central bank's subscription to the ECB's capital key'.[139] Unlike the market value benchmark, this capital key benchmark did not aim to operationalise the Eurosystem's own definition of the OME principle. Rather, it tried to maintain a connection between Member States' responsibility for their own public finances and the expectations of participants in State bonds' markets. This is to say that while the ECB accepted, for the PSPP, that there could be a distortion in the formation of State bonds' prices, it still maintained the Member States' ultimate responsibility with the reference to capital keys in case of poor performances of their bonds.[140] Moreover, the Eurosystem introduced certain eligibility requirements to ensure that the programmes would target the right parts of the real economy and/or the financial sector. For example, the Eurosystem excluded securities issued by credit institutions from the CSPP[141] and securities from bad banks from the PSPP.[142] Other eligibility criteria aimed to manage the Eurosystem's financial risk. For example, eligible assets under the APP were subject to certain credit quality requirements in line with the Eurosystem's collateral framework.[143] As we shall see in Section 4, the Eurosystem has now introduced a new set of operational measures to address the carbon bias of the CSPP.

### *The relationship between market neutrality and relevant legal principles: rationales, not definitions; legal grounds, not legal nature*

When using market neutrality in its third meaning, particularly in the context of the APP, the ECB and its staff have justified the need for asset purchases to mirror the composition of a relevant market on various grounds: an open market economy, discrimination and economic policy considerations. In Section 2.D.3, we argued that these considerations did not define new meanings

[134] Ibid., at 75.

[135] Ibid.

[136] Hammermann et al provide an example of this flexibility in the context of the PSPP: 'Depending on a central bank's operational modalities, flexibility can relate inter alia to the selection of securities to purchase, the timing of operations and the overall purchase amount for the day. [ … ] As an example of this flexibility, the share of regional government purchases as a proportion of total PSPP purchases fluctuated significantly in 2018'. See Hammermann et al (n 127) at 75.

[137] Ibid., at 73.

[138] See Hammermann et al (n 127) at 73. See also 2019 ECB Annual Report, at 34.

[139] See FAQs website update on 22 February 2023, available <https://www.ecb.europa.eu/mopo/implement/app/html/ecb.faq_pspp.en.html> accessed 19 February 2024.

[140] In order to avoid any misunderstanding, we have to specify that when issuing a new Decision, the Governing Council would still be bound by the OME principle. It is also not possible to speculate, at this stage, about the consequences of the suspension of market neutrality for the future interpretative moves of the German Constitutional Court after its decision on the PSPP.

[141] See ECB Decision (EU) 2016/948, Art 2(1).

[142] See Hammermann et al (n 127) at 74.

[143] See eg ECB Decision (EU) 2015/774, Art 3(2).

of market neutrality but rather illustrated different rationales for the ECB to mirror the composition of a given market with its asset purchases, ie what we classified as the third meaning of market neutrality. In this section, we will argue that, as rationales, these considerations do not define the principles that they invoke. As rationales, these principles provide the legal grounds for the third meaning of market neutrality, but these legal grounds should not be conflated with the legal nature of market neutrality.

The legal nature of market neutrality is determined by the relationship of the term with the principles which serve as the term's legal grounds. In our analysis of the legal nature of the first meaning of market neutrality, presented in the previous section, we identified this relationship as one of definition: in its first meaning, market neutrality defines the OME principle in the specific context of the euro area's monetary policy. With regard to the third meaning of market neutrality, we argue that the relationship between market neutrality and the principles which serve as the legal grounds for market neutrality is one of implementation.

As illustrated in the preceding section, in its third meaning, market neutrality refers to a characteristic of portfolios that mirror the composition of a reference market. Typically, the Eurosystem has used a market capitalisation benchmark to ensure that its purchases under the relevant monetary policy programmes are market neutral in this third sense, but this benchmark is only one of many tools that the Governing Council has used to operationalise various legal principles, including the OME principle. As an operational measure, in its third meaning, market neutrality is related to the OME principle, but it is not the legal principle itself. The same conclusion extends to the other relevant legal principles, eg the principle of non-discrimination.

If market neutrality, in its third meaning, and the principles it seeks to implement are different elements, the legal nature of the former cannot be contained in the latter. As an operational measure, the legal nature of market neutrality cannot be that of the principles it seeks to implement. Consequently, market neutrality, in its third sense, cannot be primary law.

As an operational measure, we will argue that market neutrality is the result of the Eurosystem's discretion as to how best to implement a directive principle such as the OME principle, a discretion that includes the choice of tool with which to implement the measure.[144] In the Decision that established the CSPP, the Governing Council did not make an express reference to market neutrality or related terms, but it did make an implicit reference to the third meaning of market neutrality. When describing the limits to purchases under the CSPP, the Governing Council indicated in Article 4(3) that 'The Eurosystem shall define additional purchase limits for issuer groups *based on a benchmark allocation related to an issuer group's market capitalisation* to ensure a diversified allocation of purchases across issuers and issuer groups.'[145] In our opinion, such an implicit reference indicates that market neutrality, in its third meaning, is a rule of secondary EU law.

Such characterisation of the legal nature of market neutrality in its third meaning is a result of the institutional design of the CSPP. The implementation of the CSPP is decentralised: the ECB coordinates the outright purchases of eligible assets in order to safeguard the singleness of the Eurosystem monetary policy, but the actual purchases are executed by a number of participating NCBs.[146] The responsibility to coordinate the programme is split between the Governing Council and the Executive Board. The Governing Council defines the monetary policy of the euro area through the issuance of Guidelines and Decisions.[147] The Executive Board implements that

[144]As we shall see in Section 4 (climate change action plan in new strategy), the market capitalisation benchmark is only one of several benchmarks available to the Eurosystem.

[145]ECB Decision (EU) 2016/948, Art 4(3). (Emphasis added.)

[146]Ibid., para (9).

[147]See Statute of the ESCB and the ECB, Art 12(1). We use the term 'Decision', with a capital letter, to refer to the specific legal act that the Governing Council of the ECB may adopt in accordance with Art 17(4) of the Decision of the European Central Bank of 19 February 2004 adopting the Rules of Procedure of the European Central Bank (ECB/2004/2) (2004/257/EC) (as amended) (hereinafter, 'ECB Rules of Procedure'). We use the term 'decision', with a lowercase, to refer to the more general meaning of the term.

monetary policy in accordance with the relevant Guidelines and Decisions of the Governing Council.[148] To perform this task, the Executive Board has the power to give NCBs any necessary Instructions.[149] Article 4(3) of the CSPP Decision defines the conditions under which the Eurosystem will implement the CSPP: the Executive Board must instruct participating NCBs to impose limits on the amounts of eligible securities that they buy from a given issuer group under the CSPP on the basis of the issuer group's market capitalisation. The CSPP Decision is a legal act of secondary EU law that is binding on participating NCBs and on the Governing Council itself, at least as long as the Governing Council does not decide to change it with another decision.[150]

Our view of the legal nature of market neutrality in its third meaning contradicts the prevailing interpretation of the ECB and its staff, which does not regard market neutrality as a source of legal obligations.[151] As already noted, this is also the prevailing view among academic commentators. Smits, Steinbach, and Zilioli and Ioannidis all focus (exclusively) on the third meaning of market neutrality and expressly conclude that it is not legally binding.[152] Dietz also understands market neutrality in this third meaning, describing it as an 'allocation framework'.[153] While she does not reach a clear conclusion about what the legal nature of market neutrality actually is, the non-binding nature of market neutrality seems like the only possible conclusion for her analysis.

Aware of the intricacies and lack of express definition, we respectfully disagree with the view that market neutrality, in its third meaning, is not legally binding. Market neutrality, in its third meaning, is a rule of secondary EU law contained in a Decision of the Governing Council and, as such, it is legally binding on participating NCBs. For example, if one of the participating NCBs tasked with the implementation of the CSPP were to execute outright purchases in breach of the issuer limit indicated in Article 4(3) of the CSPP Decision, it would be in breach of secondary EU law. Moreover, market neutrality, in its third meaning, is also legally binding on the ECB itself. If the ECB wanted to change the conditions of the implementation of the CSPP as defined in Article 4(3) of the CSPP Decision, it would not be able to do so through an Instruction of the Executive Board, for example.[154] The relevant Instruction of the Executive Board requiring that NCBs take into account an issuer's market capitalisation to calculate issuer purchase limits under

[148]See Statute of the ESCB and the ECB, Art 12(1).

[149]We use the term 'Instruction', with a capital letter, to refer to the specific legal act that the Executive Board of the ECB may adopt in accordance with Art 17(6) of the ECB Rules of Procedure. We use the term 'instruction', with a lowercase, to refer to the more general meaning of the term.

[150]In the literature, a distinction between decisions with addressees and without addressees has been thematised and it is also mentioned in the ECB's website in the context of banking supervision (see: <https://www.ecb.europa.eu/pub/economic-bulletin/articles/2019/html/ecb.ebart201906_02~3e2f0e4f63.en.html>) accessed 19 February 2024. This distinction is echoed in Ioannidis, n 33, ch. 14. Ioannidis puts the accent on two types of decisions: one, based on art. 34 of Protocol 4, which he calls 'formal legal instruments', the other, based on art. 12 of Protocol 4, which he calls 'internal decisions'. The former is an example of a standard ECB legal act and it is directly applicable while the latter is an instrument of internal governance of the Eurosystem (eg, Rules of procedures), and although binding, they are not directly applicable. We believe that the CSPP Decision is a decision that belongs to legal acts of the ECB according to art. 34 of the Statute. But even if this were not the case and the CSPP decision were to be considered a decision of the second type, market neutrality would still be legally binding.

[151]The following quote from President Lagarde illustrates this position: 'Regarding your first question, the corporate bond purchase limits continue to be based primarily on the market capitalisation of the issuer group in question to ensure a diversified allocation of purchases across issuers. *Market neutrality is an operational tool, not a legal requirement.* Generally, it helps to safeguard that the Eurosystem's interventions in the market comply with the [OME principle]' (emphasis added): C Lagarde, 'Letter from the ECB President to Mr Markus Ferber, MEP' (11 November 2022) available <https://www.ecb.europa.eu/pub/pdf/other/ecb.mepletter221111_ferber_1~1feffc15f9.en.pdf?30f53ff43764ad3cb8f28492b0d3abf0>, at 1 accessed 19 February 2024.

[152]See eg Smits (n 16), Steinbach (n 16), Zilioli and Ioannidis (n16), at 38.

[153]She frames her analysis of market neutrality in the context of the ECB's climate change action plan and refers to market neutrality as an 'allocation framework' that guides asset purchases. See eg Dietz (n 16) at 409.

[154]According to Art 14(3) of the Statue of the ESCB and the ECB, '[NCBs] are an integral part of the ESCB and shall act in accordance with the guidelines and instructions of the ECB'. Art 12(1) of the Statute specifies that the Executive Board shall give NCBs the necessary Instructions to implement monetary policy in accordance with the guidelines and decisions laid down by the Governing Council. This makes NCBs the 'operating arm' of the Eurosystem. See Ioannidis, The European Central

the CSPP is not a result of the Executive Board's discretion: it is grounded in the conditions defined by the Governing Council in the CSPP Decision. Consequently, any modification of the Executive Board's instructions to participating NCBs regarding the use of the market capitalisation benchmark to calculate issuer limits to purchases under the CSPP would require a new Decision of the Governing Council. Under this interpretation, the recent decision of the ECB to require the Eurosystem to take into account climate change considerations in addition to an issuer's market capitalisation when calculating issuer limits[155] was legally valid.[156]

The analysis presented in this section illustrates that the polysemy of market neutrality is central to the analysis of the legal nature of the term. So much so that the legal nature of market neutrality varies depending on the meaning of market neutrality that we adopt. In its first sense, ie the need to minimise distortions on market functioning, market neutrality defines an important part of the content of the OME principle in the specific context of the euro area's monetary policy and it is therefore primary EU law. In its third meaning, ie the characteristic of portfolios that mirror the composition of a reference market, market neutrality is an operational measure used to implement the OME principle and other legal principles of primary EU law that is binding on the Eurosystem. As a rule of secondary EU law, its normative power is particularly clear in relation to the NCBs tasked with the execution of asset purchases under the CSPP.

## 4. The new monetary policy strategy

### *A. The integration of climate change considerations*

On 23 January 2020, the Governing Council of the ECB announced the launch of a review of its monetary policy strategy.[157] The strategy, which had been adopted in 1998, had only been reviewed in 2003 to clarify some of its elements, so the scope of the 2020–2021 strategy review was very significant. Although the Governing Council did not expressly identify market neutrality as one of the aspects to be reviewed, the Governing Council did undertake to explore how to take climate change into account in its monetary policy, the very issue that has exposed market neutrality to considerable scrutiny for the past six years.

The new monetary policy strategy was announced on 8 July 2021.[158] Alongside the publication of the new strategy, the Governing Council approved 'an ambitious climate-related action plan' and a detailed timeline for the implementation of different climate change-related actions.[159] These proposed actions spanned several areas of the ECB's work, including monetary policy, banking supervision, financial stability, economic analysis, statistical data and corporate

Bank (n 33) para 14.14. It is the responsibility of the Governing Council to ensure compliance with those Instructions, however. See Statute of the ESCB and the ECB, Art 14(3).

[155]The Governing Council adopted this new instruction in Decision (EU) 2022/1613 of the European Central Bank of 9 September 2022 amending Decision (EU) 2016/948 on the implementation of the corporate sector purchase programme (ECB/2016/16) (ECB/2022/29), Art 1.

[156]At least in relation to the respect for the legal nature of market neutrality in its third meaning. We briefly reflect on other validity considerations in Section 5.

[157]The original strategy had been adopted in 1998 and had only been reviewed in 2003 to clarify some of its elements. See <https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200123~3b8d9fc08d.en.html> accessed 19 February 2024.

[158]Originally, the Governing Council expected to conclude the strategy review by the end of 2020, but on 2 April 2020 it announced a six-month extension of the timeline for the completion of the strategy review due to the outbreak of the coronavirus pandemic. See <https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200402~942a1358ee.en.html> accessed 19 February 2024. The monetary policy strategy statement can be found here: <https://www.ecb.europa.eu/home/search/review/html/ecb.strategyreview_monpol_strategy_statement.en.html> accessed 19 February 2024.

[159]See new strategy, para 10. Details of the climate change action plan can be found here: <https://www.ecb.europa.eu/press/pr/date/2021/html/ecb.pr210708_1~f104919225.en.html> accessed 19 February 2024. A detailed timeline for the implementation of different climate change-related actions can be found here: <https://www.ecb.europa.eu/press/pr/date/2021/html/ecb.pr210708_1_annex~f84ab35968.en.pdf> accessed 19 February 2024.

sustainability. The implementation of the climate change action plan begun immediately after the conclusion of the monetary policy strategy review.[160]

On 4 July 2022, the Governing Council decided to take further steps to include climate change considerations in the Eurosystem's monetary policy framework and announced the introduction of several concrete measures.[161] First, it decided to 'tilt [corporate bond] holdings towards issuers with better climate performance through the reinvestment of the sizeable redemptions expected over the coming years'.[162] At the time of the Governing Council's decision, the ECB expected this measure to apply from October 2022 and committed to providing additional details on the methodology that they will use to calculate an issuer's climate performance shortly before then.[163] Relatedly, the ECB also committed to start publishing climate-related information on its corporate bond holdings regularly as of the first quarter of 2023.[164]

Second, the Governing Council decided to 'limit the share of assets issued by entities with a high carbon footprint that can be pledged as collateral by individual counterparties when borrowing from the Eurosystem'.[165] The scope of these limits will increase progressively: they will first apply to marketable debt instruments issued by non-financial corporations and, as climate-related data improves, the limits may also apply to additional asset classes. At the time of the Governing Council's decision, the ECB expected this measure to apply 'before the end of 2024 provided that the necessary technical preconditions are in place'. Relatedly, the Governing Council also committed to start 'consider[ing] climate change risks when reviewing haircuts applied to corporate bonds used as collateral' in 2022.[166]

Third, the Governing Council decided that 'The Eurosystem will only accept marketable assets and credit claims from companies and debtors that comply with the Corporate Sustainability Reporting Directive (CSRD) as collateral in Eurosystem credit operations (once the directive is fully implemented)'.[167] This requirement will apply to all companies within the scope of the CSRD.[168] At the time of the Governing Council's decision, the ECB expected these new eligibility criteria to apply as of 2026.[169]

[160]The ECB provided a first update on its progress with the implementation of the climate change action plan on the occasion of the 2021 United Nations Climate Change Conference (COP 26). See <https://www.ecb.europa.eu/pub/pdf/other/ecb.pledge_climate_change_action211103~6af74636d8.en.pdf?8b1bc8a34bc3780cd41ff9802343d01e> accessed 19 February 2024.

[161]See ECB Press Release of July 4, 2022, available at the following address: <https://www.ecb.europa.eu/press/pr/date/2022/html/ecb.pr220704~4f48a72462.en.html> accessed 19 February 2024. The ECB's Climate Agenda, which was published concurrently with the Governing Council's decision, provided an overview of ongoing actions and updated the climate change action plan that had been announced on 8 July 2021. See <https://www.ecb.europa.eu/press/pr/date/2022/html/ecb.pr220704_annex~cb39c2dcbb.en.pdf> accessed 19 February 2024.

[162]See n 161.

[163]The ECB published further details on issuer's climate scores and the methodology that the ECB will use to calculate them on 19 September 2022. See <https://www.ecb.europa.eu/press/pr/date/2022/html/ecb.pr220919~fae53c59bd.en.html> accessed 19 February 2024.

[164]On 24 March 2023, the ECB published the first climate-related financial disclosures of the Eurosystem's corporate sector holdings under its monetary policy portfolios and non-monetary policy portfolios. See <https://www.ecb.europa.eu/pub/pdf/other/ecb.climate_related_financial_disclosures_eurosystem_corporate_sector_holdings_monetary_policy_purposes2023~9eae8df8d9.en.pdf?44e1ca0d64e12148df58cb8acaed6f4a> accessed 19 February 2024 and <https://www.ecb.europa.eu/pub/pdf/other/ecb.climate_related_financial_disclosures_ECB_non_monetary_policy_portfolios2023~9199143410.en.pdf?cac4e583bdd600149bb5025e3b180f54> accessed 19 February 2024.

[165]See n 161.

[166]Ibid. Haircuts are reductions applied to the value of collateral assets to reflect their risk.

[167]Ibid.

[168]A significant proportion of the assets that can be pledged as collateral in Eurosystem credit operations, such as asset-backed securities and covered bonds, do not fall under the CSRD, however. To ensure a proper assessment of climate-related financial risks for those assets, the ECB committed to engaging closely with the relevant authorities. See eg the Joint ESAs-ECB Statement on disclosure on climate change for structured finance products, available <https://www.ecb.europa.eu/pub/pdf/other/ecb.ESA_ECB_joint_statement~c1f96d353b.en.pdf?02fb3e782ccd745be3f3505071bf6d97> accessed 19 February 2024.

[169]Mainly as a result of the delayed implementation of the CSRD.

Lastly, the Governing Council decided to 'further enhance [the Eurosystem's] risk assessment tools and capabilities to better include climate-related risks'.[170] To improve the external assessment of these risks by rating agencies, the ECB committed to 'urge rating agencies to be more transparent about how they incorporate climate risks into their ratings and to be more ambitious in their disclosure requirements on climate risks'.[171] Moreover, 'the Eurosystem agreed on a set of common minimum standards for how national central banks' in-house credit assessment systems should include climate-related risks in their ratings'.[172] At the time of the Governing Council's decision, the ECB expected these standards to enter into force by the end of 2024.[173]

At its meeting in December 2022, the Governing Council decided that it would begin to unwind the APP from the beginning of March 2022 by refraining from reinvesting all of the principal payments from maturing securities.[174] Between March and June 2023, only redemptions in excess of €15 billion per month will be reinvested. On 2 February 2023, the Governing Council announced further details of these partial reinvestments. As a general rule, for the private sector programmes (ABSPP, CBPP3 and CSPP) the Eurosystem's market presence during the period of partial reinvestment will only focus on secondary market purchases, but the Governing Council introduced an exception for non-bank corporate issuers with a better climate performance and green corporate bonds, which will continue to be purchased in the primary market.[175] Moreover, the Governing Council also announced that, for the Eurosystem's corporate bond purchases, the remaining reinvestments will be tilted more strongly towards issuers with a better climate performance.

### *B. Market neutrality under the new monetary policy strategy*

The main rationale behind the measures that the Governing Council included in the ECB's climate change action plan was the need to manage risk more effectively, in particular, climate-related financial risks.[176] Moreover, the Governing Council made clear that these measures were necessary for the Eurosystem to achieve its primary objective of price stability.[177] It also invoked, for the first time, the Eurosystem's secondary objective, in particular, the need to support the green transition of the economy in line with the EU's climate neutrality objectives.[178]

Some of the documents that accompanied the Governing Council's decision to adopt a climate change action plan as part of the new monetary policy strategy indicate that market efficiency was an important rationale of the overall plan.[179] For example, in the press release that announced the Governing Council's adoption of a climate change action in the context of the monetary policy strategy review, the ECB affirmed that 'The design of these measures [contained in the climate change action plan] will be consistent with the price stability objective and should take into

[170]See n 161.

[171]Ibid.

[172]Ibid.

[173]For further details on these common minimum standards, see this paper <https://www.ecb.europa.eu/home/search/html/climate_change.en.html> accessed 19 February 2024.

[174]See the press release of the Governing Council's monetary policy decisions on December 15, 2022, available here: <https://www.ecb.europa.eu/press/pr/date/2022/html/ecb.mp221215~f3461d7b6e.en.html> accessed 19 February 2024.

[175]See press release of the ECB's decision on detailed modalities for reducing APP holdings (February 2, 2023), available at this address: <https://www.ecb.europa.eu/press/pr/date/2023/html/ecb.pr230202~1a4ecbe398.en.html> accessed 19 February 2024.

[176]See eg the press release at n 161.

[177]Ibid.

[178]Ibid.

[179]Somewhat surprisingly, there is no evidence of market efficiency considerations in the decisions of the Governing Council that detail the new measures that aim to integrate climate change considerations. All of the evidence is contained in publications relating to the monetary policy strategy review.

account the implications of climate change for an efficient allocation of resources'.[180] Moreover, in the detailed roadmap of the climate change action plan, the Governing Council expressly indicated its intention to '[a]ssess potential biases in the market allocation amid market inefficiencies and the pros/cons of alternative allocations'.[181] and, based on that assessment, to '[m]ake concrete proposals for alternative benchmarks, in particular for the [CSPP]' throughout 2022.[182]

The ECB has not indicated the legal grounds for using market efficiency as a rationale for some of the measures included in its climate change action plan. Under the framework that we present in Section 3.A, market efficiency is one of the four elements that comprise the OME principle, and it gives the principle its directive nature. We could therefore argue that the ECB's decision to use market efficiency as a rationale for some of the measures that are included in its climate change action plan is grounded in the OME principle; in particular, in the ECB's definition of that principle in the specific context of the euro area's monetary policy.

In the quote from the detailed roadmap of the climate change action plan presented above, the Governing Council's characterisation of benchmarks that better address market inefficiencies as an 'alternative' to benchmarks that simply mirror the composition of a given market (ie the third meaning of market neutrality) could lead us to think that market neutrality, in its third meaning, and market efficiency are mutually exclusive. This seems to be the framing through which policy discussions have taken place within the ECB.[183] Framing market neutrality and market efficiency as mutually exclusive could lead us to think that, following the strategy review, market neutrality is no longer relevant in the euro area's monetary policy. We believe that this is not the case.

Some of the measures that aim to better integrate climate change into the Eurosystem's new monetary policy strategy do mark a departure from market neutrality in its third meaning. In particular, the decision to tilt corporate bond purchases by increasing the share of assets on the Eurosystem's balance sheet issued by companies with a better climate performance compared to the share of assets issued by companies with a poorer climate performance will make the composition of the portfolio deviate from the composition of the reference market. But this measure only applies to certain programmes under the APP; mainly, the private sector purchases programmes, and more specifically the CSPP. Market neutrality, in its third meaning, remains active as an operational measure in other programmes.[184] The coexistence of 'market-neutral' benchmarks and alternative benchmarks under the APP refutes the idea that market neutrality, in its third meaning, and market efficiency cannot coexist.

The same conclusion holds true for market efficiency and the first meaning of market neutrality, ie the need to minimise distortions of market functioning. In Section 3.A, we argued that, in its first meaning, market neutrality defined the OME principle by focusing on the first three elements of the principle: (i) a 'market economy' that is (ii) open and (iii) where actors can compete freely. In that section, we also argued that the fourth element of the principle, ie the efficiency formula, gave the principle its directive nature and that, as a result, under normal circumstances, market neutrality could contribute to the efficient allocation of resources. Seen in this light, the relationship between market efficiency and the first meaning of market neutrality is

[180]See the press release on the ECB's plan to include climate change considerations in its monetary policy strategy (July 8, 2021), available at this address: <https://www.ecb.europa.eu/press/pr/date/2021/html/ecb.pr210708_1~f104919225.en.html> accessed 19 February 2024.

[181]See detailed roadmap available here: <https://www.ecb.europa.eu/press/pr/date/2021/html/ecb.pr210708_1_annex~f84ab35968.en.pdf> accessed 19 February 2024.

[182]Ibid.

[183]See eg Schnabel, 'From market neutrality', n 71.

[184]See eg Letter from the ECB President to Mr Markus Ferber, MEP (10 February 2023) available <https://www.ecb.europa.eu/pub/pdf/other/ecb.mepletter230210_Ferber~c0323ef6b5.en.pdf> accessed 19 February 2024. The Eurosystem did not use the market value benchmark to guide its purchases under the PSPP, it used (and continues to use) the capital key as its benchmark. See Section 3.B.1.

not one of opposition but one of *functional dependence*: the ECB should adhere to market neutrality *because* markets can allocate resources efficiently. The fact that, as we described in the previous paragraph, under certain programmes the ECB considers that allocating resources efficiently does not require new operational tools and that it can continue to use 'market-neutral' benchmarks reinforces the value of our analysis of the OME principle: the idea that efficiency considerations may be latent in the definition of the OME principle allows the ECB to accommodate different efficiency assessments under different programmes of the APP.

Diagram 5 illustrates the use of market neutrality over time and confirms that market neutrality continues to be relevant event today.[185] Yet the salience of market efficiency considerations in the ECB's new monetary policy strategy raises important questions about the implementation of the ECB's monetary policy prior to the strategy review. For example, has the ECB always held this definition of the OME principle or did the definition change as a result of the review of the ECB's monetary policy strategy? Moreover, do the technical assessments that the ECB will use to evaluate market efficiency pre-date the strategy review or are they a new measure that the ECB has introduced to implement its new monetary policy strategy? And how exactly does the ECB evaluate the ability of markets to allocate resources efficiently? These are important questions that could help examine the validity of the ECB's monetary policy measures and assess its litigation risk.[186] Unfortunately, the scope of this Article prevents us from examining these issues on this occasion.

## 5. Market neutrality and the legitimacy of the ECB's interventions

The Treaties make the legitimacy of the ECB rest on two essential grounds: its independence from political institutions (art. 130 TFEU)[187] and a narrow definition of its competences with a clear primary objective (ie the pursuance of price stability). As long as there is a clear mandate over the main objective, independence allows a certain level of technical discretion (legitimated on the basis of expertise) in choosing how to pursue it.[188] In this section, we reflect on how a clearer understanding of the legal nature of market neutrality might help us understand the risks to the ECB's legitimacy when implementing unconventional measures of monetary policy.

We begin our analysis with an examination of the relationship between market neutrality and the ECB's independence. In her paper, Dietz focuses her analysis on the third meaning of market neutrality and describes its relationship with central bank independence in terms of causality:

> [T]he principle of market neutrality is [ . . . ] closely linked to the consequences of the institutional set-up of central banks as independent institutions, and the explanation for the 'link' is that '[w]hile it is for governments and their fiscal policies to set policy incentives with

[185] As illustrated in Diagram 5, the use of market neutrality declined significantly in 2022. Such a sharp decline could suggest that the strategy review led to the ECB reneging from market neutrality, but Diagram 5 also shows a slight increase in 2023. (The data collected for 2023 is incomplete so any interpretations of this year's data should be taken as preliminary.) That the ECB continues to use the term market neutrality indicates that it is too early to declare its time over.

[186] For example, whether the ECB's definition of the OME principle in the euro area's monetary policy, on which the ECB grounds measures that rely both on market value benchmarks and alternative benchmarks, such as the tilted benchmark under the CSPP, is compatible with the Treaties.

[187] For a helpful and synthetic analysis see M. Ioannidis, 'The European Central Bank' (n 33) at 14.IV.

[188] As it has been remarked in the previous section with the Strategy Review, the ECB has also the duty to pursue a secondary objective, but these have not been defined and only recently have come again under public scrutiny. This vacuum in the definition not only of the content, but also of the scope and strength of its secondary objective, has generated a wider margin of manoeuvre for the ECB. Cf, for a recent analysis, J van 'T Klooster and N de Boer, 'What to Do with the ECB's Secondary Mandate' 61 (2023) Journal of Common Market Studies 730–46. For a general assessment of the ECB's broad discretion when conducting unconventional monetary policy on the ECB's independence, see C Zilioli, 'The ECB's Powers and Institutional Role in the Financial Crisis: A confirmation from the Court of Justice of the European Union' 23 (2016) Maastricht Journal of European and Comparative Law 171–84.

> financial instruments and take distributive decisions, it is contrary to the foundations of monetary policy, with its primacy on price stability, to distinguish between market participants on the basis of any other policy criteria [ . . . ]' The aim of monetary policy is price stability, not treating certain market participants better than others due to non-monetary related reasons.[189]

According to this understanding, market neutrality (at least in its third meaning) is a consequence of the ECB's political independence because, in principle, it excludes non-monetary considerations from ECB's interventions.[190] Furthermore, it does not discriminate between market participants on the basis of non-monetary policies. In this light, market neutrality protects the ECB from the accusation of acting according to political instruction or discriminating arbitrarily among market participants.

Although this is a plausible reconstruction, we disagree with Dietz on the relevance of central bank independence to describe the legal nature of market neutrality. In our opinion, in the design and implementation of the APP, the main purpose of market neutrality is to allow the ECB to follow market inputs rather than to fence off political instructions. The ECB's primary objective makes prices the main input for ECB decision-making. The ECB needs markets to form prices in order to achieve its primary objective. This is particularly important for market neutrality in its first meaning: minimising the distortions of monetary policy on market functioning allows markets to support price formation. In short, in its first meaning, market neutrality is more about the ECB's commitment to a functioning and efficient market economy than about the ECB's political independence.[191] Additionally, even if central bank independence could be regarded as a rationale for market neutrality, it is not the only one. In Section 3.B.2, we present at least three other possible legal rationales: the OME principle, risk management and the principle of non-discrimination. Moreover, none of the documents that we have examined provide any indication of the ECB and its staff regarding central bank independence as a rationale for market neutrality in either sense of the term.

However, the potential impact of market neutrality on the interpretation of the ECB's mandate can raise concerns about the ECB's legitimacy. In our opinion, the salience of market efficiency as a rationale to deviate from the third meaning of market neutrality under the CSPP is particularly relevant. Market efficiency, with its potential for shaping financial markets with selective interventions,[192] might expand the space for discretion in monetary policies to questionable levels for two reasons. First, scrutinising the ECB's assessment of the efficiency can be difficult. If the ECB is to exercise its discretion to assess whether relevant markets are allocating resources efficiently but there is no public metric of efficiency against which the ECB's assessment can be compared to, it is difficult to imagine how the ECB's assessment of efficiency could ever be scrutinised. If such a metric existed, eg in the form of technical assessments conducted by political institutions, a broad interpretation of the ECB's independence would prevent that such assessments by political institutions are used to scrutinise the ECB's own assessments. In our opinion, if the ECB were to rely on those assessments that would not violate its independence. According to its secondary objective, the ECB is expected to contribute to the general economic

[189]Dietz (n 16) 430.

[190]Yves Mersch, during his term as a member of the Executive Board of the ECB, also pointed to this argument in 2018. See Section 2.D.3.

[191]Under this interpretation, an analysis of the potential implications of market neutrality for the constitutional position of the ECB should focus on the ECB's relationship to financial markets rather than on its relationship with political institutions.

[192]The argument that unconventional monetary policies even before the emergence of market efficiency were part of a transformation of the ECB into a market-maker of last resort is not new. See, for an analysis applied to contemporary central banking (and not only the ECB), J Verstergaard, D Gabor, 'Central Banks Caught between Market Liquidity and Fiscal Discipline' (2021) Working Papers Institute for New Economic Thinking (available at <https://www.ineteconomics.org/research/research-papers/central-banks-caught-between-market-liquidity-and-fiscal-disciplining-a-money-view-perspective-on-collateral-policy>) accessed 19 February 2024.

policies of the Union. It is unreasonable to expect the ECB to develop its own expertise in every single area of economic policy to which it might be able to contribute. Independence should not prevent the ECB from relying on the technical assessments made by political institutions when such assessments are necessary for the ECB to comply with its secondary objective. The ECB's Climate Change Action Plan that resulted from its Strategy Review is a case in point: rather than developing its own standard of climate due diligence, the ECB has expressly relied on the CSRD.

Second, efficiency considerations are at the heart of economic policy so the potential for non-monetary considerations to creep in the ECB's assessment of efficiency becomes conspicuously higher. The latter point might also affect the principle of independence, but only if that principle were to be interpreted in a bi-directional sense, ie not only as a (negative) prohibition to follow political instructions, but as a prescription for the ECB to pursue monetary policies with no impact on the political determination of economic policies by European institutions. But, as known, the CJEU has rejected this interpretation in *Gauweiler*.[193] Consequently, we think that, according to current law, this second issue concerns only the question of the ECB's competence and not that of its independence.

The question of the legality of unconventional monetary policies after the Strategy Review is made more controversial by the attribution by the ECB of a legal weight to the secondary objective of contributing to the achievement of the objectives of the Union as laid down in Article 3 TEU, including a high level of protection and improvement of the quality of the environment. This sensibly increases the institution's discretion because the ECB has to proceed to a balancing act between its primary and secondary objectives in the absence of any instruction contained in primary and secondary law. This might expose the ECB to the accusation of acting politically, meaning that certain decisions would not be motivated only by monetary considerations,[194] and therefore to the risk of acting outside its competences. Whether those decisions are valid and legitimate would need to be examined against the facts of the specific case. An analysis of the proportionality of the decisions will be central to this exercise.[195]

We cannot speculate about what those facts will be, but the analysis of the legal nature of market neutrality that we have developed in this paper presents important insights that could inform such an analysis. First, the first meaning of market neutrality, ie the avoidance of unnecessary distortions of market functioning, is a principle of primary EU law. As such, it does not dictate any objectives of monetary policy. Second, any deviation from market neutrality in its third meaning, ie the characteristic of a portfolio that mirrors the composition of a reference market, will need to be grounded in a valid definition of the relevant principles of EU law that give this meaning of market neutrality a rationale, ie the OME principle, risk management and the principle of non-discrimination. In our opinion, an argument that stands on central bank independence as a rationale for market neutrality will be less persuasive. Third, market neutrality will only be relevant if the ECB relies on market neutrality to inform its interpretation of its primary or secondary objectives; for example, if the ECB were to rely on the first meaning of

[193]In *Gauweiler*, the CJEU examined one of the most debated aspects of unconventional monetary policies and established that even if these policies were to generate an economic impact as a side-effect, they would remain within the competences of the ECB, at least as long as they were functional to the pursuance of price stability. *Gauweiler*, at 60 (which makes explicit reference to acting in a 'wholly independent manner'). This is the formulation given by the CJEU: 'Thus, Article 130 TFEU is, in essence, intended to shield the ESCB from all political pressure in order to enable it effectively to pursue the objectives attributed to its tasks, through the independent exercise of the specific powers conferred on it for that purpose by primary law' (*Gauweiler*, n 33, at §40).

[194]For an analysis of the lack of parliamentary oversight for this balancing exercise and a set of recommendations on how to redress this issue see S Grünewald and J van't Klooster, 'New Strategy, New Accountability? The European Central Bank and the European Parliament after the Strategy Review' 60 (2023) Common Market Law Review 959–98.

[195]We reckon that this would require, at the very least, an analysis of the principle of proportionality as understood by the ECB. See, for an introduction to the topic, the papers in the 'Symposium on proportionality' from the ECB legal conference 2021 (April 2022).

market neutrality to justify the relevant measures of monetary policy. In fact, policy measures that deviate from that first meaning of market neutrality, eg to address concerns with the inability of relevant markets to allocate resources efficiently, will probably give rise to greater concerns about their proportionality than those measures that seek to adhere to market neutrality. In the former case, a deviation from the first meaning of market neutrality may be legitimised if, and only if, it is deemed necessary for the ECB to achieve its objectives, be they primary or secondary.

## 6. Conclusions

It is time to take stock and highlight the main findings of this Article. We have taken the question of the meaning and legal nature of market neutrality in the euro area's monetary policies seriously. In the absence of any reference to the term in the Treaties, we have developed a summative content analysis in order to identify the contextual meaning of the term as used by the ECB and its staff. We have identified three different meanings and have singled out the first and the third meanings as those most relevant for the analysis of the legal nature of market neutrality in the euro area's monetary policy and, in particular, in the context of the APP.

Clarification of the different meanings is an essential precondition for an assessment of the legal nature of market neutrality. Too often, ECB staff and scholars have tended to conflate or mix different meanings of market neutrality while they were actually 'using' these different meanings. This may be one of the reasons why the ECB, its staff and most academic commentators all come to the conclusion that market neutrality has no legal relevance. Under these views, market neutrality is just either a policy tool or a social norm internalised by ECB staff. By unpacking the different meanings of market neutrality, we have shown that, even if the emergence of market neutrality were the outcome of a social norm, ECB staff have used it, at least in the first meaning of the term (ie the avoidance of unnecessary distortions of market functioning), as an essential part of the content of the OME principle. Being an essential part of the OME principle, the legal nature of market neutrality cannot be different from the legal nature of the OME principle: in its first meaning, market neutrality is primary EU law. Market neutrality is not an absolute principle, however: the OME principle is not exhausted by market neutrality because it includes a directive criterion of efficiency. The content of the OME principle is guided by that directive criterion. As we explain in Section 3.A, the efficiency element of the OME principle is often latent; we can expect it to gain prominence in crisis times. When that happens, market neutrality, in its first meaning, can be suspended until the functioning of the price mechanism in markets is restored.

Our summative content analysis also reveals another meaning of market neutrality that is relevant for the euro area's monetary policy: the characteristic of a portfolio that mirrors the composition of a reference market. We have referred to this as the 'third meaning' of market neutrality. The ECB, its staff and the majority of academic commentators characterise this third meaning of market neutrality as an operational tool that is not legally binding. We respectfully disagree. In this third meaning, we have argued that market neutrality is a rule of secondary EU law that is disciplined by decisions of the Governing Council.

This polysemy of market neutrality paints a more complex picture of the legal nature of the term than what transpires from the policy debates and academic literature on this topic. Most evidently, we argue that the legal nature of market neutrality will vary depending on the meaning of market neutrality. In our view, market neutrality is legally binding on the ECB, albeit its legal force is different depending on the meaning: in its first meaning, market neutrality is a directive principle of EU law; in its third meaning, it is a rule of secondary EU law. This stands in stark contrast with the prevailing view in the ECB and in academic scholarship, which rejects the possibility of market neutrality being a source of legal obligations.

Furthermore, the analysis of the ECB strategy review has revealed that concerns related to the efficient allocation of resources and distorted pricing led the ECB to tilt the composition of the

CSPP towards bond issuers that are better able to manage climate-related financial risks. This decision shows that market neutrality, as instantiated in its third meaning, is legally relevant but less strong than the ECB's primary objective, its duty to manage risk effectively, and its secondary objective of contributing to the achievement of the objectives of the Union as laid down in Article 3 TEU, including a high level of protection and improvement of the quality of the environment. Moreover, the recognition that efficiency bears a weight in the ECB's decision-making process might impact the ECB's relations with other EU and Member States' institutions. In Section 5, we examined the relationship between market neutrality and the ECB's independence. We argue that the ECB's independence is not as clear nor as strong a rationale for market neutrality as other principles of EU law, particularly the OME principle. Nevertheless, the ECB's unconventional monetary policies might raise concerns with the ECB's legitimacy in other respects. In particular, the ECB's assessment of the ability of relevant markets to allocate resources efficiently and the consideration of its secondary objective as part of its mandate will lead the ECB to take into account an increasing number of non-monetary policy considerations. We anticipate that this will expose the ECB to greater legal and political scrutiny. A clear understanding of the legal nature of market neutrality can help inform the proportionality of the ECB's decisions.

**Data availability statement.** The data required to produce the above findings are available to download from the EUR-lex database, the ECON's website, and the website of the European Central Bank. The resulting dataset can be shared with any interested parties upon request by contacting Dr Javier Solana.

**Competing interests.** The authors have no conflicts of interest to declare.

## Annex 1

### *Additional search terms in the ECB's website search engine*

| Search terms | Type of source | Database | Number of results (as of 15 May 2023) |
|---|---|---|---|
| 'market neutral* introductory statement press' | Press conferences | ECB website | 209 |
| 'market neutral* your letter' | MEP Letters | ECB website | 106 |
| 'market neutral* blog' | Posts on ECB blog by:<br>• The President of the ECB<br>• Members of the Executive Board | ECB website | 118 |
| 'market neutral* interview*' | Interviews by:<br>• The President of the ECB<br>• Members of the Executive Board | ECB website | 222 |
| 'market neutral* This paper should not be reported as representing the views of the European Central Bank' | Working Papers<br>Occasional Papers<br>Discussion Papers<br>Legal Working Papers | ECB website | 633 |

## Annex 2

### *Number of appearances of market neutrality and related terms in each source*

| | Number of appearances | | | | | | |
|---|---|---|---|---|---|---|---|
| Type of source | 1 | 2 | 3 | 4 | 5 | 5+ | Total |
| FSR | 17 | | | | 1 | | 18 |
| Speech | 8 | 4 | 1 | | | 2 | 15 |
| Occasional papers | 3 | 4 | 2 | | 1 | 1 | 11 |
| Working papers | 4 | 2 | | | 1 | 4 | 11 |
| MEP Letters | 6 | 2 | 1 | 1 | | | 10 |
| ECB Annual Report | 3 | 3 | | 1 | | | 7 |
| Accounts | 6 | | | | | | 6 |
| Economic Bulletin | 3 | 1 | | | 1 | | 5 |
| Monetary Dialogue | 1 | 2 | | | | 1 | 4 |
| Monthly Bulletin | 2 | 1 | 1 | | | | 4 |
| Website | 2 | 1 | | | | 1 | 4 |
| Blog post | | 1 | 1 | | | | 2 |
| Guideline | 1 | | | | | | 1 |
| Interview | 1 | | | | | | 1 |
| Other reports | 1 | | | | | | 1 |
| Total | 58 | 21 | 6 | 2 | 4 | 9 | 100 |

## Annex 3

### *List of codes and categories*

CATEGORY (Conceptual) nature – as opposed to legal nature:

CODE: Benchmark
CODE: Concept
CODE: Index
CODE: Idea
CODE: Notion
CODE: Tool
CODE: Principle

CATEGORY: Hedge funds

CODE: Arbitrage
CODE: Leverage
CODE: Investment strategy

CATEGORY Impact on:

CODE: Balanced market presence
CODE: Collateral availability
CODE: Competition
CODE: Counterparty range
CODE: Efficiency
CODE: Liquidity
CODE: Market failures
CODE: Normal market functioning
CODE: Prices
CODE: Price discovery
CODE: Scarcity
CODE: Supply-demand
CODE: Volatility

CATEGORY Market mirroring:

CODE: Across jurisdictions
CODE: Across maturity spectrum
CODE: Capital key
CODE: Carbon bias
CODE: Composition
CODE: Deviation (from market neutrality)
CODE: Eligible asset universe
CODE: Green bonds
CODE: Issue limit
CODE: Issuer limit
CODE: Level of issuance
CODE: Market value/capitalisation
CODE: Negative yield
CODE: Nominal value
CODE: Paris alignment
CODE: Proportional
CODE: Reinvestment
CODE: Sovereign bonds
CODE: Tilting
CODE: Total outstanding

## CATEGORY: Portfolios

CODE: APP
CODE: CSPP
CODE: FX reserves
CODE: NMPP (Non-monetary policy portfolios)
CODE: PEPP
CODE: PSPP

## CATEGORY Rationales:

CODE: Discrimination
CODE: Diversification
CODE: Economic policy
CODE: Litigation risk
CODE: Mandate
CODE: Normative judgements
CODE: OME
CODE: Operationalisation
CODE: Preferential treatment
CODE: Regular and balanced market presence
CODE: Risk management

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