

# CEPS – DEVELOPING A SAFE ASSET

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European Stability Mechanism

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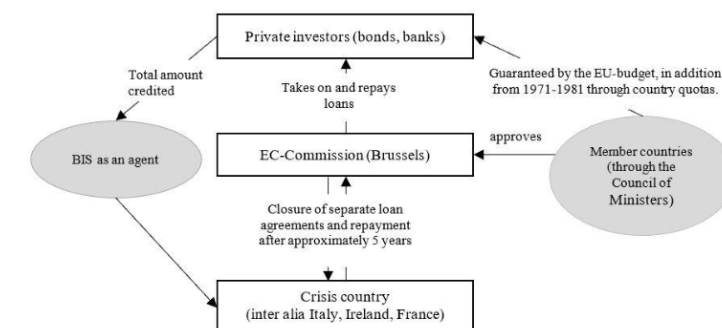


# DEVELOPING A EUROPEAN SAFE ASSET

- European Investment Bank bonds the first European safe asset
  - EIB issued its first ever bond in 1961 (in Dutch Guilder)\*
- European Commission
  - European Commission started borrowing in 1976\*\*: first European Community Bond, on-lent to Italy and Ireland
- European Financial Stability Facility
  - EFSF started issuing in 2011
  - Guarantees-based issuance – backed by 17 countries, over guarantee by 6 strongest-rated
- European Stability Mechanism
  - ESM started issuing in 2013
  - Backed by 20 countries of the euro area, Croatia joined in January



Figure 1 Design of the Community Loan Mechanism of 1975



Source: EEC Council (1975a), EEC Council (1975b), own illustration.

\*The EIB, 1958 -2008

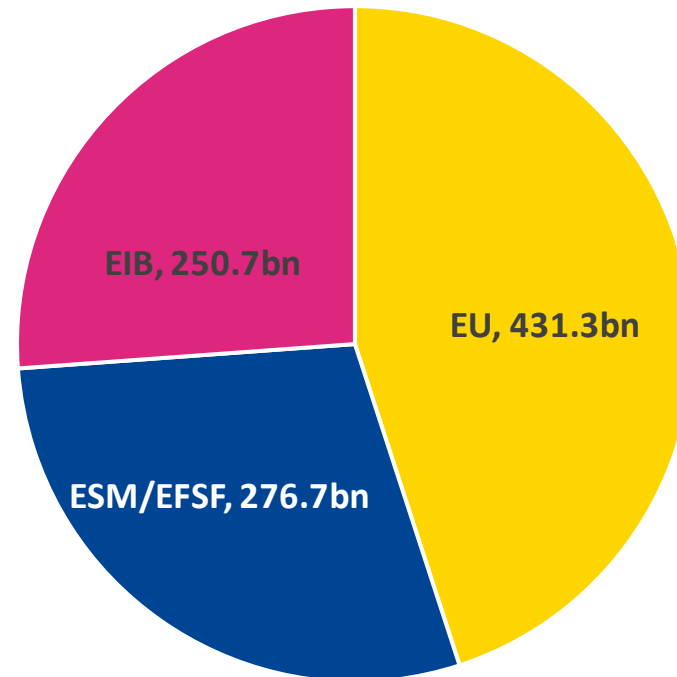
\*\* Coronabonds: The forgotten history of European Community debt | CEPR

# COMPARISON TABLE OF EUROPE'S SAFE ASSETS

	EFSF	ESM	EIB	EU
Ratings	Aaa/AA/AA-	Aaa/AAA/AAA	Aaa/AAA/AAA	Aaa/AA+/AAA
Ownership	Private company under Lux law owned by the 17 EA Member States at the time of EFSF creation	Inter-governmental under international law owned by the 20 EA Member States	Owned by 27 EU Member States	Owned by 27 EU Member States
Guarantee	Explicit	Implicit	Implicit	Implicit
Subscribed capital paid-in	€745mn	€81bn	€22bn	Non applicable
Subscribed capital unpaid	Non applicable	€624bn	€227bn	Non applicable
Risk Weighting	0%	0%	0%	0%
Liquidity Coverage Ratio	Level 1	Level 1	Level 1	Level 1
Purpose	Limited to rolling over maturing debt (outstanding loans €172.6bn - 76% GR, 14% PT, 10%IE)	Permanent institution, to enable countries of euro area to avoid/overcome financial crises	To Support investment in infrastructure projects, SME development and mitigate the effects of global warming	To support recovery from the Pandemic crisis and investments into a sustainable economy
PSPP eligible	Yes	Yes	Yes	Yes
2023e Funding	€20bn (liquid benchmark bonds, up to 2056, pp, N-bonds)	€8bn (liquid benchmark bonds EUR, USD, maturities 1 to 45y, pp, N-Bonds)	Up to €50bn (mainly EUR, USD, 3-5bn size, benchmarks 2-30y, green bonds)	€170bn borrowing authorization for the year (liquid bonds from 3y, 30% green format)

# THE FOUR MAIN EUROPEAN SUPRANATIONAL ISSUERS ACCOUNT FOR CLOSE TO €1TN

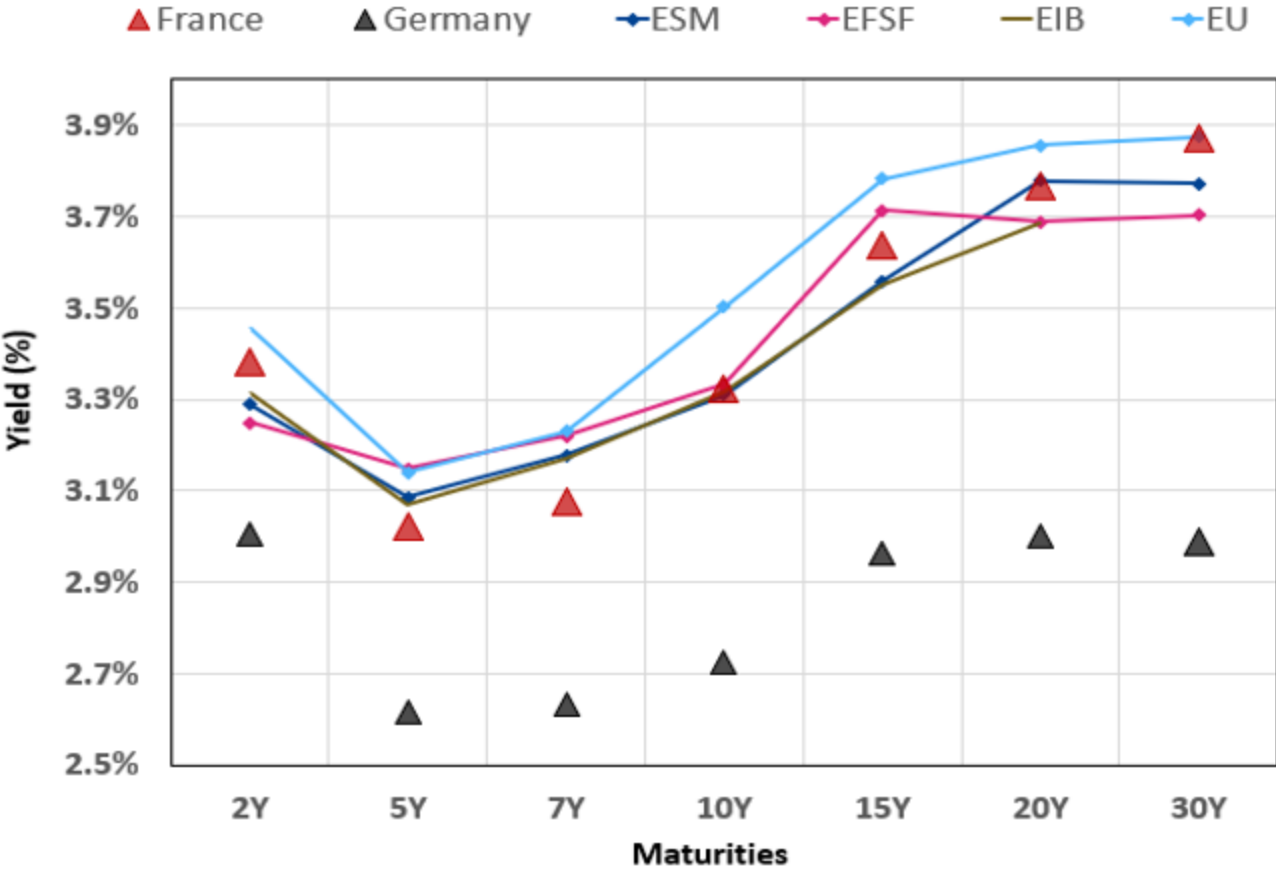
Euro denominated bonds and notes from the 4 European Supranational issuers (excluding bills and CPs)  
As of 6 November 2023



Source: Bloomberg

# THE FOUR MAIN EUROPEAN SUPRANATIONAL ISSUERS PRICE CLOSE TO FRANCE

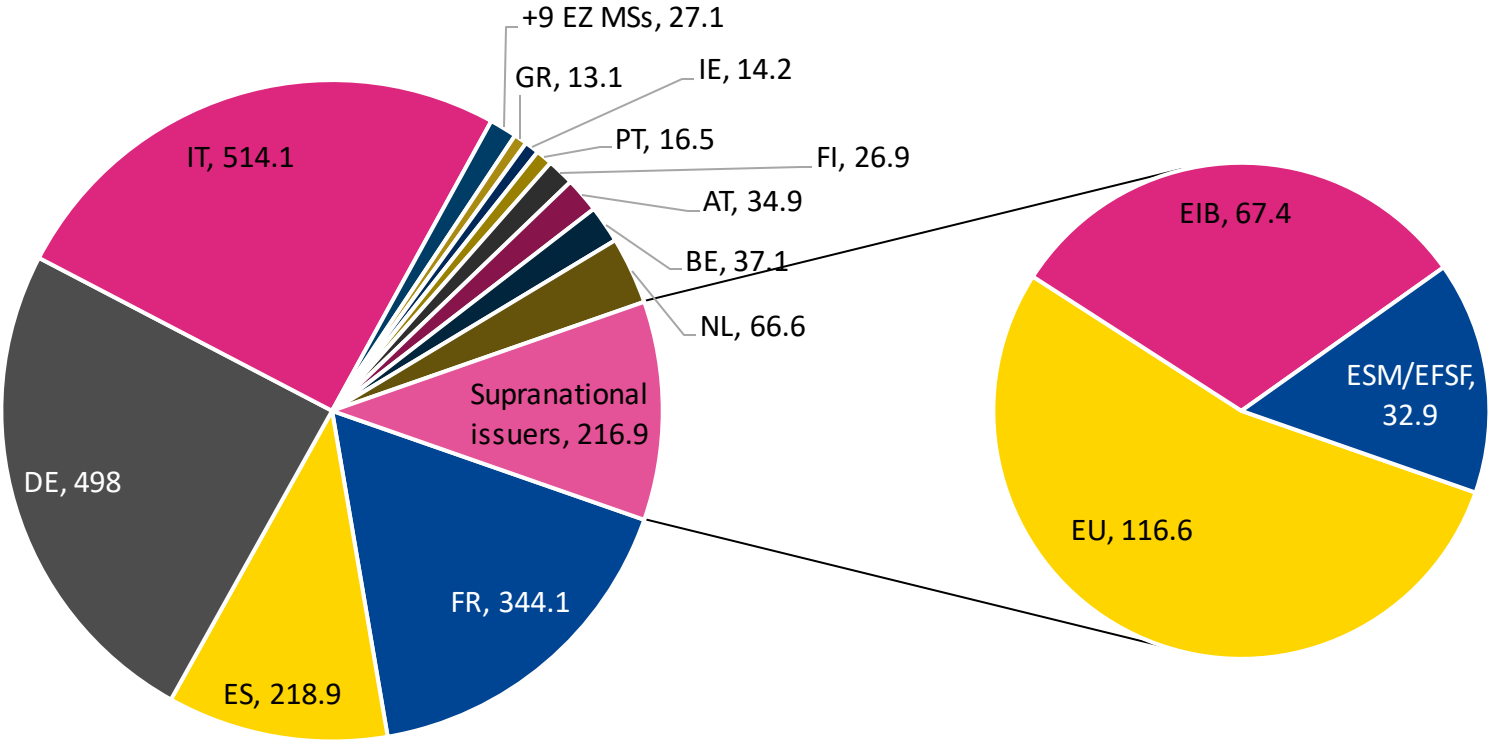
Yield curve of the 4 European Supranational issuers versus Germany and France – As of 6 November 2023



Source: Bloomberg, ESM

# THE FOUR MAIN EUROPEAN SUPRANATIONAL BENEFIT FROM STRONG LIQUIDITY

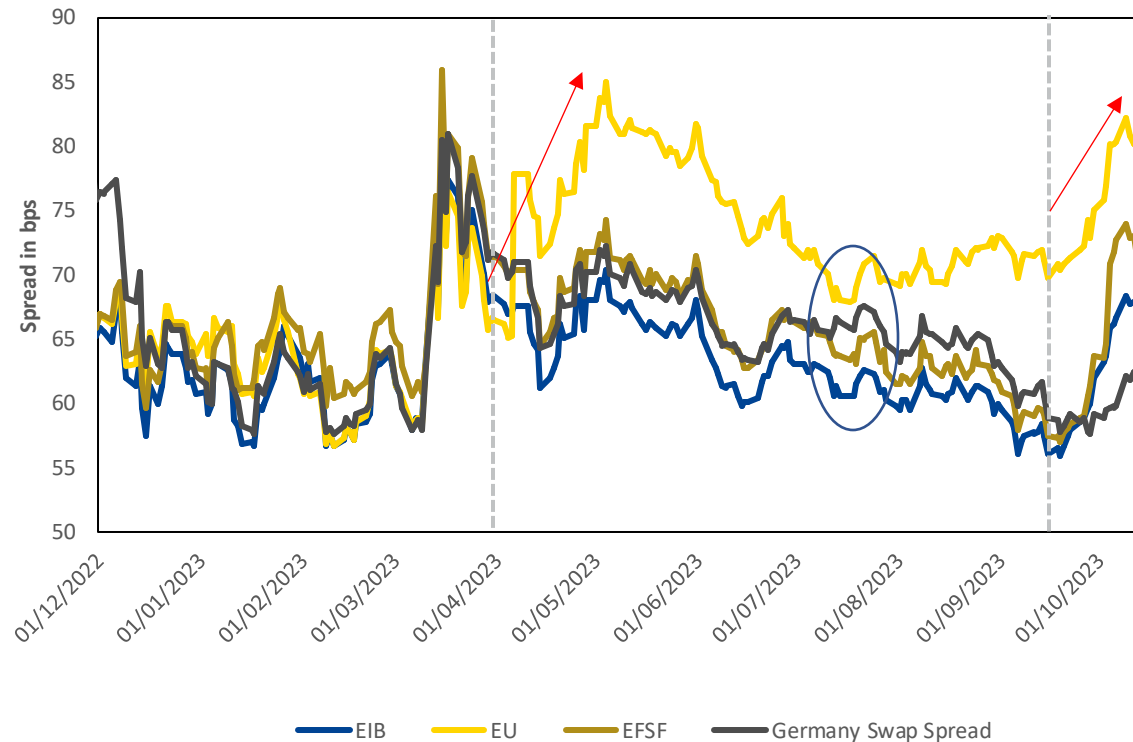
Daily average traded volumes for the main government and European supranational bonds (€bn)



Source: AFME, Finbourn (Oct 2022)

# IN 2023, WE HAVE SEEN EU WIDENING FROM EFSF AND EIB

Spread 10Yr SSA vs 10Yr Germany and 10Yr Germany Swap Spread



Source: Bloomberg, ESM

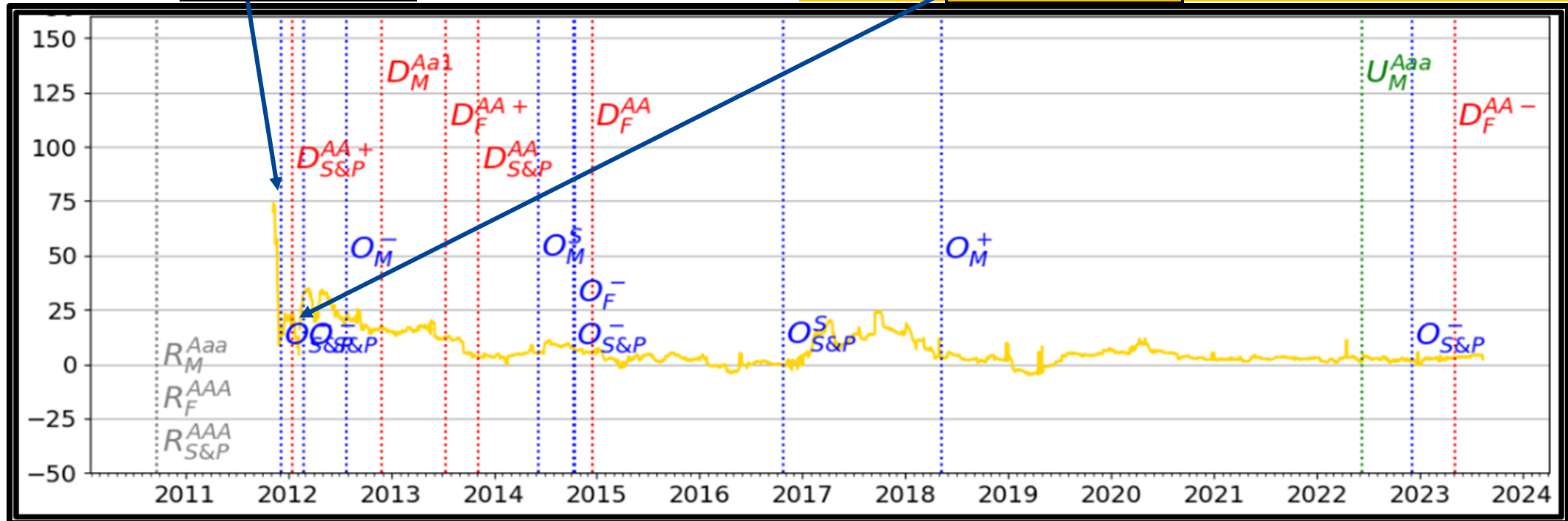
- Over the past six months **EU also widened vs other E-names...**
- ...**initially on** the introduction of the March **APP QT...**
- ...before **briefly converging** during summer **on** communicating a **reduced 2023 funding plan.**
- The subsequent **EU rewidening** on elevated 2024 net issuance projections **strongly conditioned the spreads of other E-names.**

# DEVELOPING A SAFE ASSET: EFSF CONVERGED TO EIB

10Yr EFSF spread vs EIB – similar despite different ratings, mandates and capital structures

**EFSF-EIB 10-year Spread (in bps)**

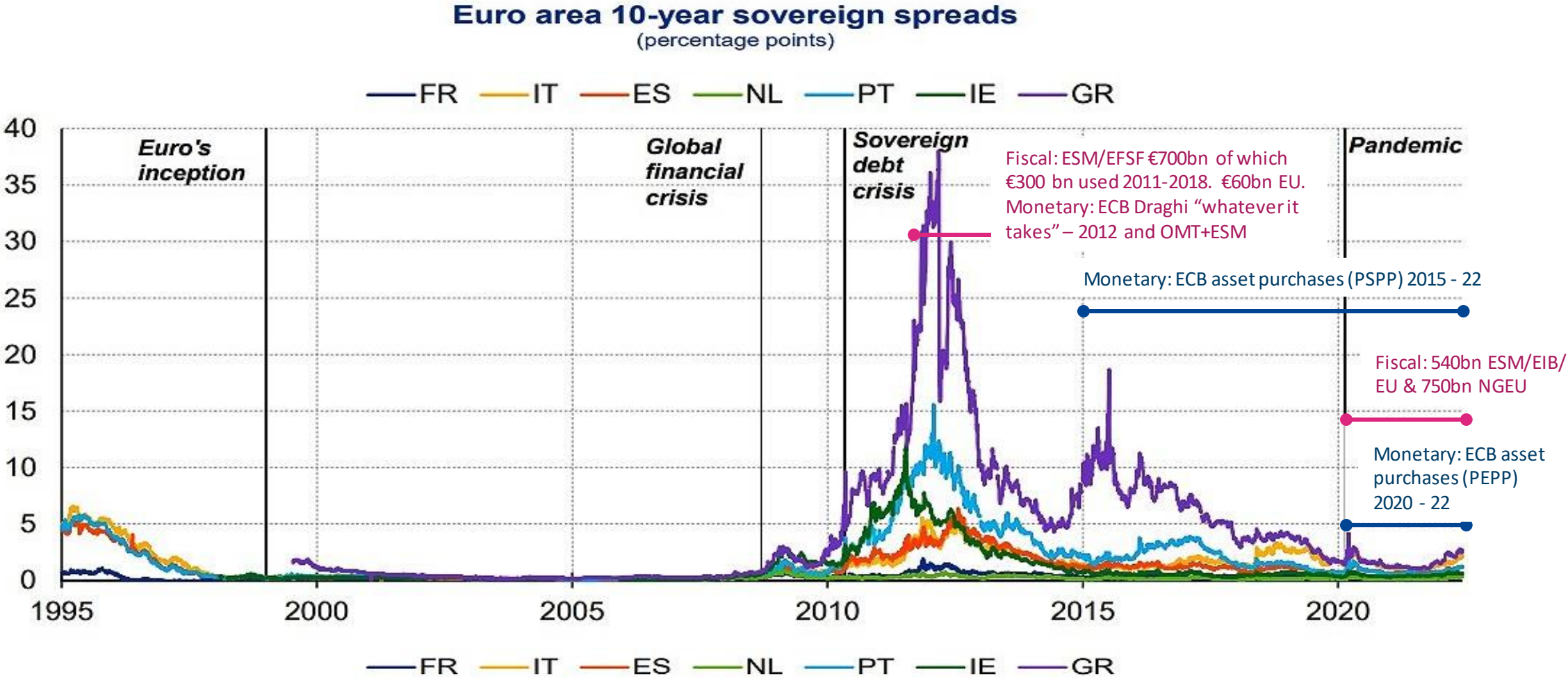
EIB	S&P	07 December 2011	AAA	Negative	Changed outlook to negative	EIB	S&P	17 January 2012	AAA	Stable	Changed outlook to stable
EIB	Fitch	19 December 2011	AAA	Negative	Changed outlook to negative	EIB	Fitch	25 September 2012	AAA	Stable	Changed outlook to stable



Source:  
Bloomberg,  
ESM  
calculations



# UNITED FISCAL AND MONETARY RESPONSE MADE EURO AREA STRONGER AND CALMED MARKETS



Source: ECB and ESM

## A CFO VIEW

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- Market appreciates Europe's safe assets
- The variety allows for diversification and trading
- It allows for hedging vs sovereigns – taking blended risk
- Spread pick up allows banks to buy more European safe assets
- ESM as investor and issuer supports the Commission
  - Staff contribution
  - Investor
  - Technical support

# FUTURE CONSIDERATIONS

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- European Commission NGEU has been a market success
- Europe's safe assets are performing well
- EIB and ESM are capital-based, balance sheet institutions
- EU market comments:
  - Temporary nature – 2026 end of new loans
  - Indirect taxation vs direct taxation
- Political concerns:
  - Transfer union – beyond once off for Covid19?
  - Fear of federalism through backdoor