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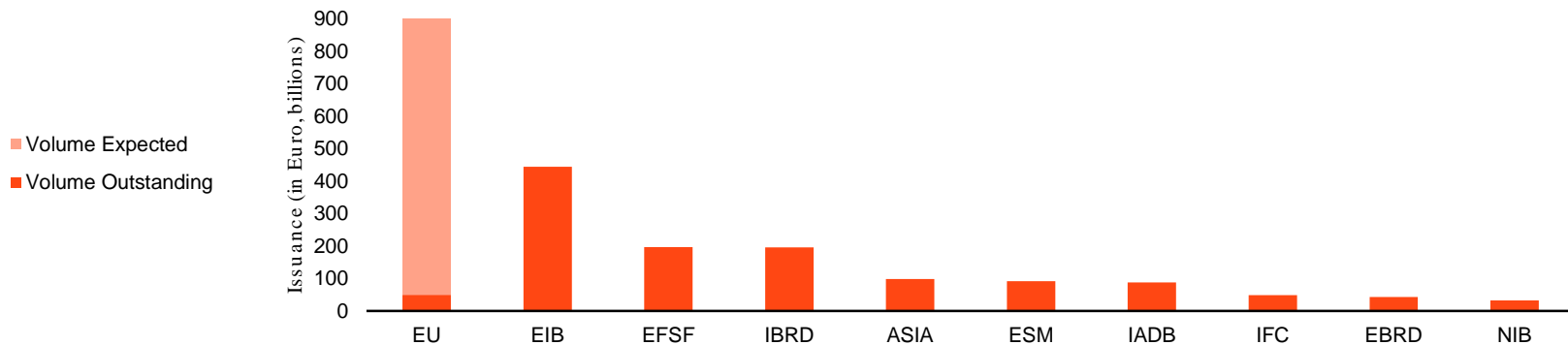
**BlackRock**<sup>®</sup>

# The implications of EU bond issuance

# The EU is poised to become one of the largest single issuers in the Euro area

- The planned EU issuance for SURE and NGEU over the next coming years will be **orders of magnitude larger than the past**
- The EU will become not only the **largest Supranational issuer in Europe and the world** but also one of the **largest pan-European issuing entities** . It will also become **the largest global issuer of green bonds**
- The relatively fast pace of new debt issuance and the resulting stock create **separate opportunities and challenges**
- **EU will benefit from a strong credit position** having de facto recourse to the EU budget

Expected volume of EU bonds relative to current outstanding of select Supranational bonds (in Euro, billions)

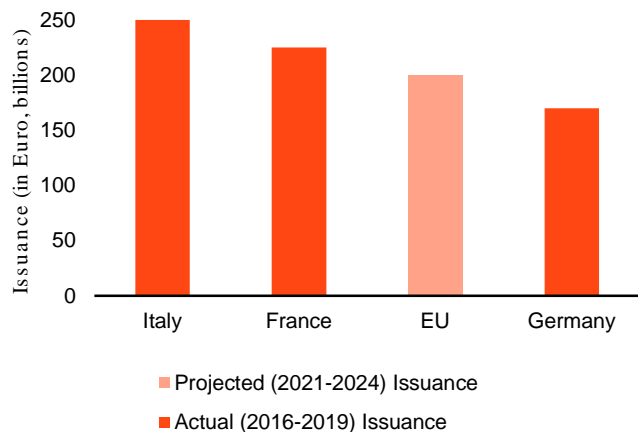


Sources: EU, Bloomberg, Commerzbank Research as of 20.08.2020.

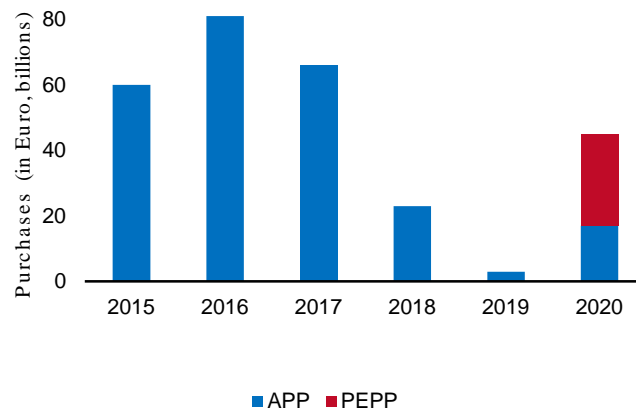
# EU issuance relative to EGBs<sup>1</sup> and ECB support via asset purchases

- With respect to the **annual issuance volume**, the EU is likely to **rank alongside the four largest EGB issuers** (Italy, France, Germany, and Spain) in the coming years
- On average, the EU is expected to issue **€150 bn - €200 bn per year**, this is in line with gross issuance in the main sovereigns which has averaged €125bn - €250bn per year in recent years
- Historical levels of supranational purchases by the ECB demonstrates support in the asset class

Actual average issuance (in Euro, billions)



Historical ECB purchases of eligible supranational debt (in Euro, billions)



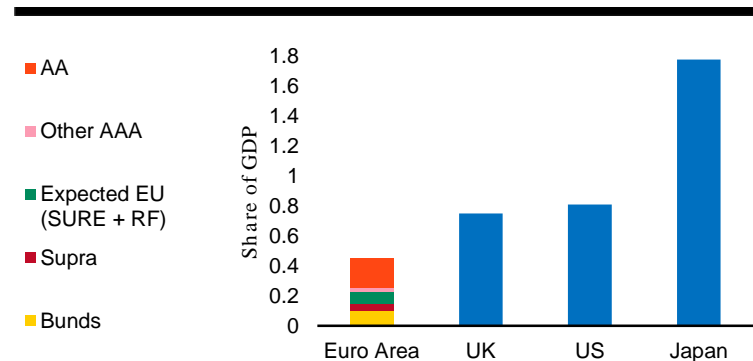
Sources: Haver Analytics, Goldman Sachs, as of 20.08.2020. (chart 1); ECB, as of 31.07.2020. APP stands for Asset Purchase Programm (chart 2)

<sup>1</sup> European Government Bonds

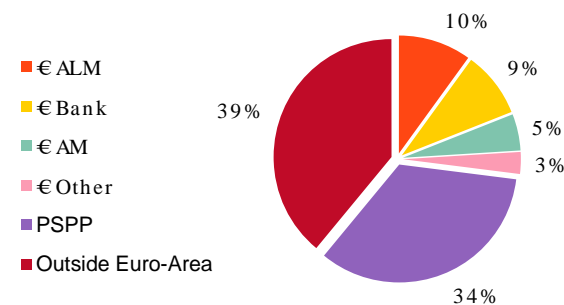
# Demand dynamics for EU bonds

- The upcoming EU issuance will add **a substantial amount to the current supply of low-risk assets in the Euro Area**. This is a welcome development for the region which will likely attract flows from a wide investor base
- An additional dynamic might be the **potential substitution effect away from “semi-core” bonds into the newly issued EU bonds**
- Euro Suprationals already benefit of a **high foreign investor involvement**
- The establishment of a benchmark curve for EU will further support that trend
- A number of practical challenges are hindering the development of liquidity towards that more common in sovereign: e.g. EU bonds are not eligible initial margin under derivatives contracts; there is no futures contract on EU bonds
- With **1/3 of total EU issuance**<sup>1</sup> to be in **green bonds** should further support demand from a wide range of investors

Size of safe assets relative to GDP (G10 economies)



Estimated investor breakdown in Euro denominated Suprationals



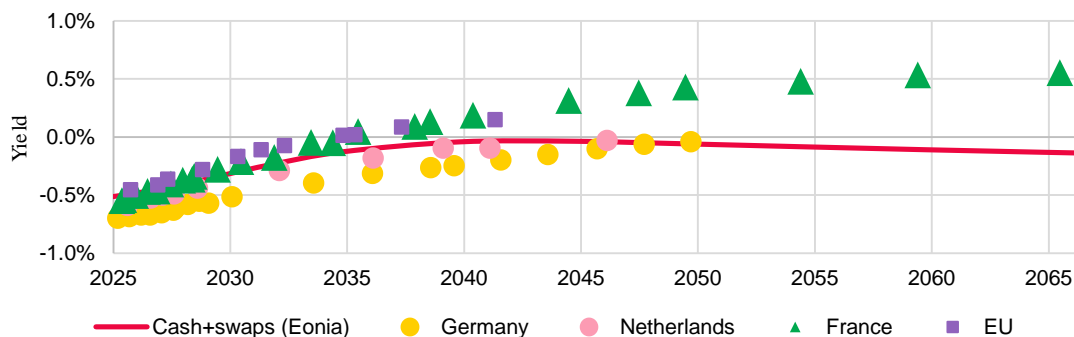
Sources: BlackRock, Commerzbank, as of 20.08.2020 (chart 1), BlackRock, Bloomberg, as of 20.08.2020 (chart 2)

<sup>1</sup> Quote from Commission President Ursula von der Leyen on 16.09.2020

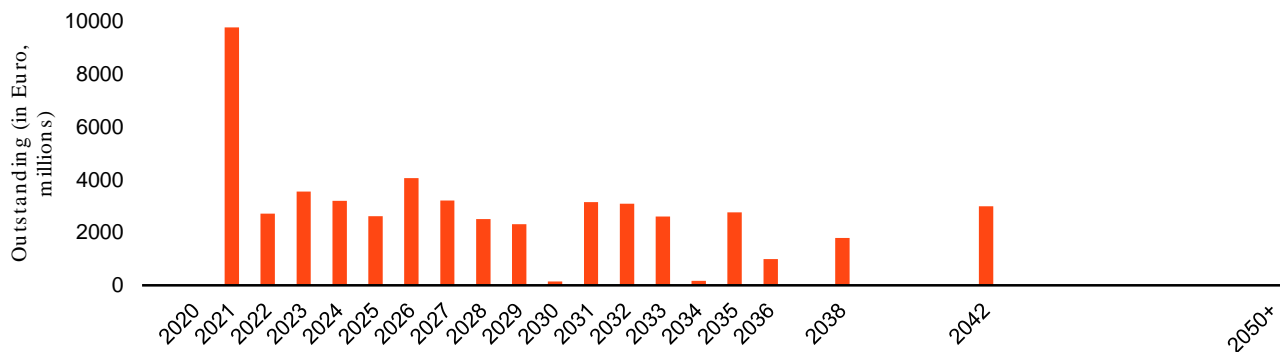
# Secondary market valuations of EU bonds

- EU yield curve is set to extend on the back of the planned SURE and NGEU issuance
- Investors will likely focus on relative value dynamics between EU bonds, other European Supranationals and similarly rated Government bonds

## Select Euro area yield curves



## Current EU bond curve by amount outstanding



Sources: BlackRock, Bloomberg, as of 29.07.2020 (chart 1), BlackRock, Bloomberg, as of 16.09.2020 (chart 2)

# BLK Survey of Sell-Side expectations regarding EU issuance

## Summary of results :

- **All respondents expect new investors to enter the SSA market** when the EU issuance gets underway
- Regarding trading desks, **60% of banks will continue to trade EU bonds from the SSA desk**, 30% will move the issuer to the EGB desk and 10% is yet to decide
- **Most expect issuance in the form of multi-tranche syndications with pre-set windows**, similarly to ESM and EFSF. Regarding **auctions**, 70% expect the issuer to make use of auctions over time but with syndications remaining the biggest tool for issuance
- As for **EU futures**, there is a **strong majority** of 80% which sees **no prospect for a EU bond future**
- With regards to **zero coupon bonds**, 100% respondents believe this is not a viable strategy

QUESTIONS	ANSWERS
Do you expect new investors to join the market for EU bonds?	100% yes
With the upcoming sizeable change in EU outstanding are you planning to:	
Move the issuer to EGB desk	30%
Keep at SSA desk but allocate significantly more balance sheet/ risk limits	60%
Other (pls specify)	10% TBD
What is your 2020/2021/2022 expectation for gross issuance for EU (EUR billions)?	30/180/175
Do you expect the issuer to move towards multi-tranche vs. single-tranche issuance?	70% multi-tranche, 20% single-tranche, 10% TBD
Would you expect issuance windows to be communicated in advance (e.g. ESM/ EFSF) or more ad-hoc issuance?	60% windows, 40% no pre-set windows but presence in market every 2 weeks
Are you expecting to see significant shift from syndications to auctions over coming years?	70% yes (with syndication proportion still higher), 20% no, 10% TBC
Do you see potential and/or demand for a EU bond future?	80% no, 10% yes, 10% TBC
Do you think there would be a benefit in EU issuing only zero coupon bonds?	100% no

Sourcesurvey carried out amongst 11 participants with responses collected on 16 Sept 2020

# Q&A session

## Technical questions

1. Which desk should this be traded from on bank side (SSA or govie)?
2. How can the liquidity of the bonds be enhanced?
3. Should EU have primary dealers?
4. Should EU migrate from swap product to benchmark spread product over time?
5. Issuance of zero coupon bonds rather than bullet bonds?
6. Will the issuer move towards multi-tranche (less frequent issuance) vs single tranche (more frequent issuance) issuance?
7. Should issuance windows be communicated in advance (e.g. ESM/ EFSF) or more ad-hoc issuance?
8. Will a repo and/or futures market on EU bonds develop?

## Broader questions

1. Will the EU issuance unlock demand from new investors, specifically overseas?
2. Will the agreed support package be ratified by all relevant institutions?
3. Will enough requests be made by Member States to fully use the available budget?
4. How will the ECB's bond purchase programmes evolve in the face of the upcoming EU issuance?
5. Will Dutch regulator De Nederlandsche Bank (DNB) change the VEV rules to give EU bonds a zero risk weighting for Dutch pension schemes to determine required capital buffers?
6. Will EU bonds become eligible as collateral for bilateral derivative transactions?