European Stability Mechanism

BOND MARKET CONTACT GROUP

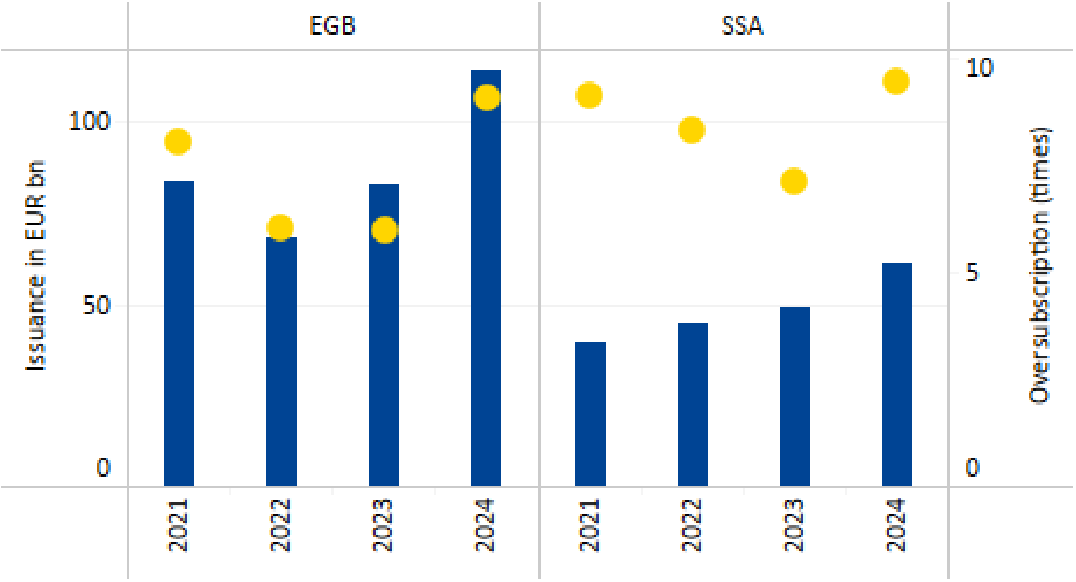
Market absorption update following a very active start to the year in bond issuance

12 March 2024

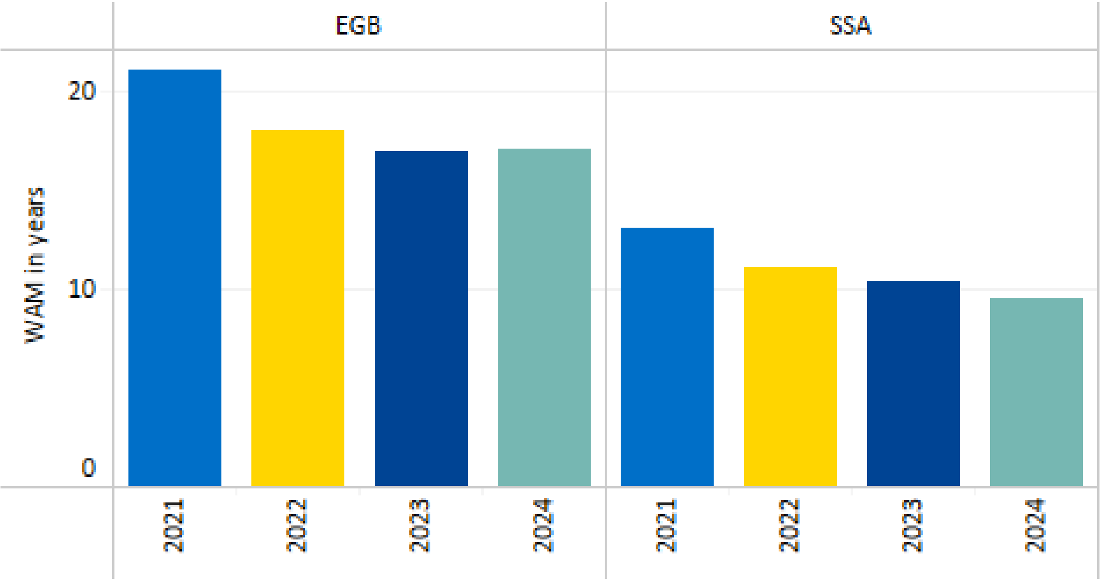
2021-2024 - ISSUANCE PARAMETERS

- **Issuance via syndications and oversubscription**: 2024 has the most prominent first 9 weeks vs the past 3 years in both EGB and SSA due to frontloading, with higher net issuance in view (QT)
- **Little changed WAM** compared to the previous 3 years (especially in EGB) as yield levels, yield curve shapes and expectations conditioned the sweet spot of demand
- QT, an established exercise, meeting still ample excess reserves bodes well for issuance conditions through **improved secondary market liquidity**
- Progressively **increased secondary market activity,** also assisted by **improved repo market conditions** in recent months, has been instrumental for price discovery and in defining "fair market value" around issuance

Nominal Issuance and Oversubscription in the first 9 weeks of year



WAM of Issuance in the first 9 weeks of year

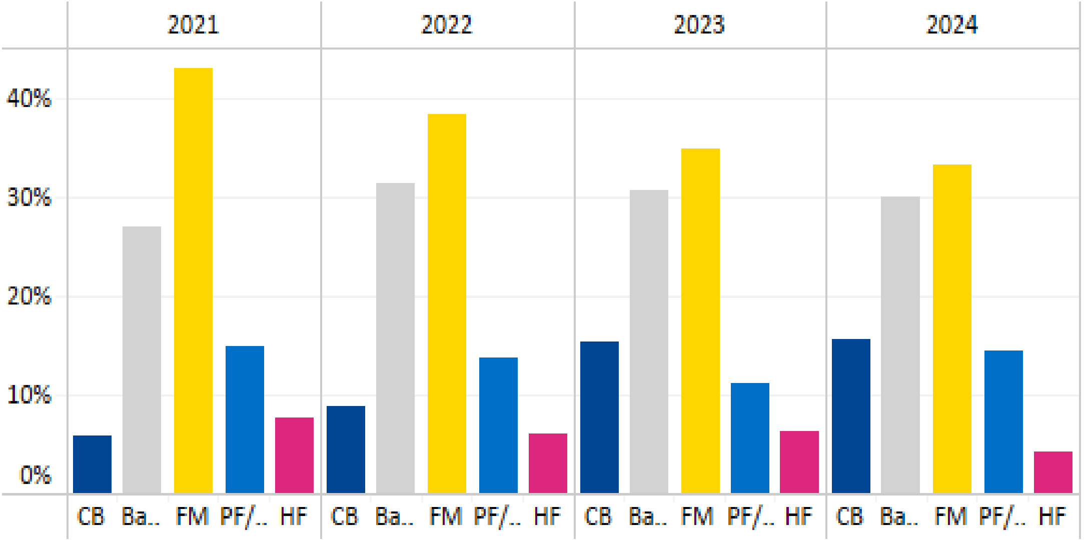


Source: ESM / bank data

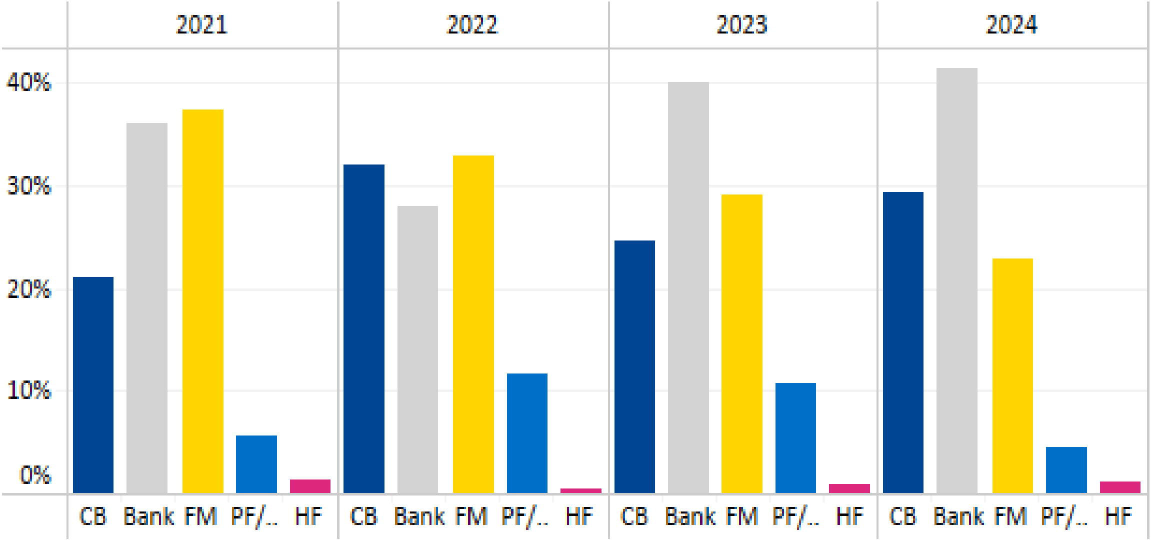
2021-2024 - INVESTOR TYPE ALLOCATIONS

- **Increasing Central Bank and Official Institutions presence** at the expense of fund managers (EGBs and SSAs)
- **Bank Treasuries presence remains strong** in EGB and dominant in SSA on wider spreads vs swaps
- **Higher share of Pension Funds and Insurance Companies** on higher WAM in EGBs compared to SSAs
- Any **investors cautiousness**, likely associated with absolute rates and swap spread developments, has been **limited so far,** as **moves** have been mostly of an **orderly** type and markets still expect lower funding costs later in 2024

EGB Investor Type Allocations in the first 9 weeks of year



SSA Investor Type Allocations in the first 9 weeks of year

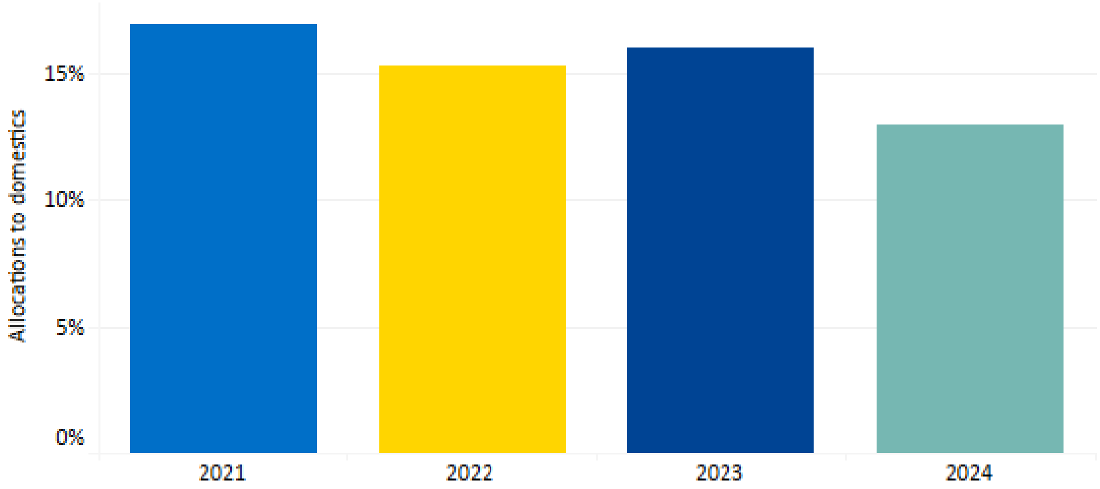


Source: ESM / data

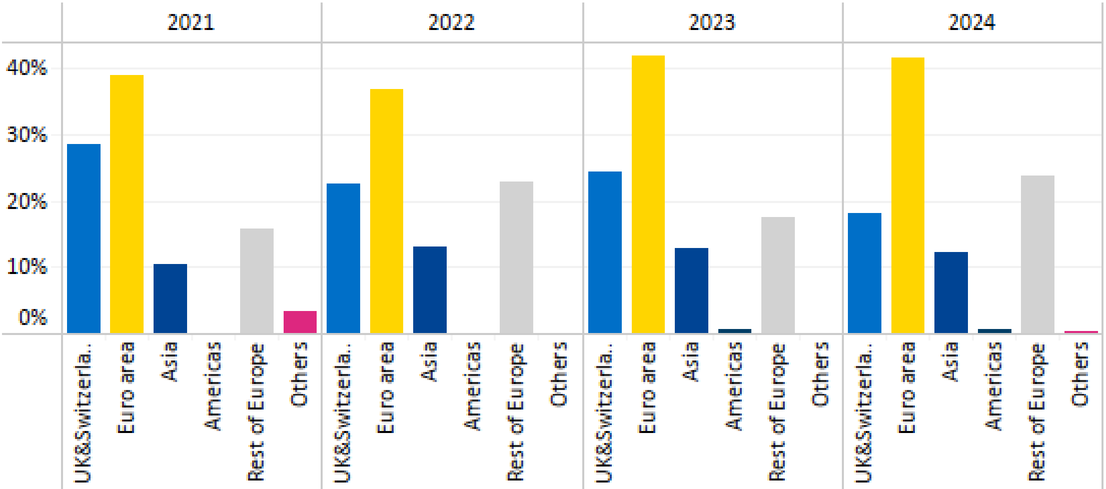
2021-2024 - GEOGRAPHICAL ALLOCATIONS

- **In EGBs, the share of allocations to domestics decreased in 2024** a general downtrend on rates normalisation and benign market conditions
- **In SSAs**, allocations are flowing out of the UK & Switzerland into Asia (continuing the trend observed in Q4 2023) and rest of Europe
- Improved secondary market liquidity helped **investor base diversification**

EGB - Share of Allocations to Domestics in the first 9 weeks of year



SSA - Geographical Allocation in the first 9 weeks of the year



Source: ESM / bank data

DISCUSSION POINTS

At the start of 2024, primary market issuance has benefited from an orderly rates and swap spreads repricing, seen as a positive and not as an impediment to final investor demand.

- How would developments (monetary and fiscal policy, or politics-wise) in other jurisdictions impact fixed income markets in an unfolding QT environment?

- What would then be the markets' reaction in case inflation expectations get repriced higher? How would market participants' expectations be reshaped on Central Banks' reactions to such a possibility and how these will impact demand appetite for EA bonds?

- The ECB will soon publish their new operational framework. What would be the impact on secondary and, consequently, primary fixed income markets? How could this impact different investor types' demand for EA bonds?

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