“Eurobonds”

Elisa Ferreira

Assembleia da República

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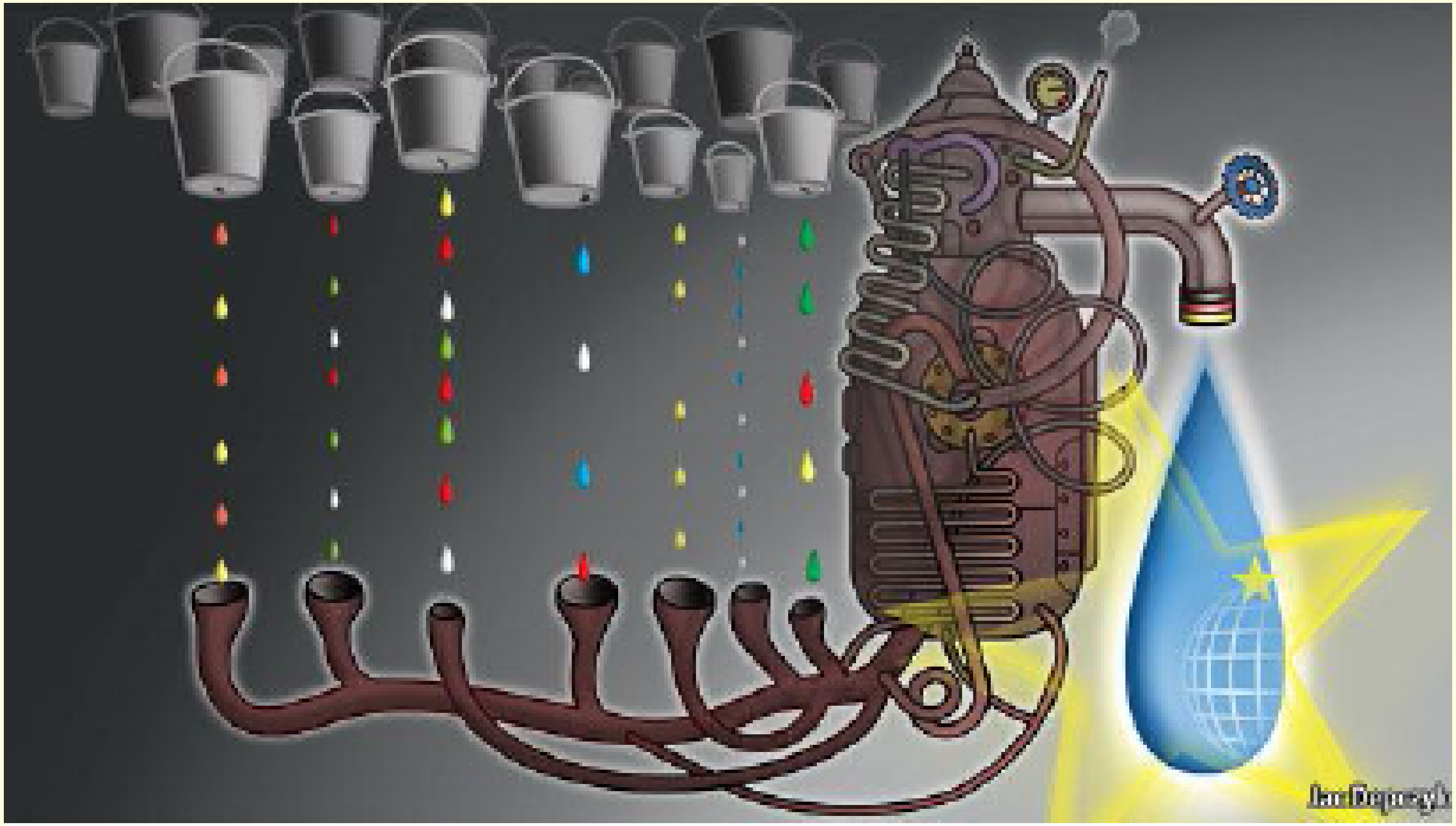


1. European Parliament

The European Parliament has been a strong voice calling for Eurobonds

- **In a report of 17.2.2009 on the European Economic Recovery Plan, Elisa Ferreira asked for the assessment of such introduction:**

  *"Your draftswoman is of the view that, at the present moment, the instrument of **Eurobonds** can prove particularly relevant. Your draftswoman calls on the European Council to **assess the feasibility of such issuance**; extra finance for projects of common European interest, the reduction of financing costs to governments and the channelling of savings are some of the reasons that support such an initiative."*

- **In the regulation of the "Six-Pack" on** the effective enforcement of budgetary surveillance in the euro area, **that entered into force on 2011.12.13,** the European Parliament, imposed that:

  *"**Before the end of 2011** the **Commission shall present** a report to the European Parliament and to the Council on the possibility of introducing **euro-securities**."; the approval was accompanied by a **public written statement by the Commission** in the same sense.*

1. European Parliament

- **In the Resolution of the European Parliament (2012.02.02) on the European Council Resolution of the 30 January 2012, that led to the "Fiscal Compact " Intergovernmental Treaty, a specific demand was made for parallel decisions on Stability Bonds or Redemption Bonds.**

  "Reiterates its call for a rapid establishment of a redemption fund based on the proposal made by the German Council of Experts..."

  "Further to the series of measures to ensure fiscal stability.....calls for the establishment of project bonds, a roadmap for stability bonds and the introduction of an FTT at European level..."

- **In its last plenary session (2012.02.15) the European Parliament , in the follow up of its position on the "Six Pack", approved a Resolution on "the feasibility of introducing stability bonds", in which the EP *"calls on the Commission to come forward rapidly with proposals to address decisively the current sovereign debt crisis"* reinforcing the need for the common management of sovereign debt, but also states:**

  *"Notes in particular that the **US Treasury market** and the total **euro area sovereign bond market are comparable in size** but not in terms of **liquidity, diversity**, and **pricing**;*

1. European Parliament

*.....eurozone to develop a **common liquid and diversified bond market** together with a credibly established stability culture and as a result a **market of stability bonds** would offer a **viable alternative to the US dollar bond market** and establish the euro as a global 'safe haven'"*

- **In the Draft Report from the European Parliament** on: "**common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member Sates in the euro area", the "Two Pack"** the raporteur, Elisa Ferreira proposes that such regulation:

*"Shall be **accompanied,** upon its entry into force, by the publication of a **concrete roadmap** for the implementation of **stability bonds** along the Commission Green Paper* COM (2011) 818 ***and the immediate establishment of a Redemption Fund.***"

1. European Parliament

2. Commission Green Paper on Stability Bonds
COM (2011) 818 final 23.11.2011

Potential benefits, include:

- **the deepening of the internal market and rendering capital markets more efficient,**
- **increasing the stability and shock resilience of the financial sector and of government financing,**
- **raising the attractiveness of euro area financial markets and the euro at global level,**
- **reducing the impact of excessive market pessimism on sovereign borrowing costs.**

3 Options for common issuance of Stability Bonds :

- **N.1 : The full substitution of Stability Bond issuance for national issuance with joint and several guarantees**
  - Euro area government financing would be fully covered by the issuance of Stability Bonds with national issuance discontinued

2. Commission Green Paper on Stability Bonds

COM (2011) 818 final 23.11.2011

- ***would require***: *a single Euro Area Debt Agency that would distribute the process among the several MS; the pooling of credit risk , with implications for credit rating and yields accross MS*
- ***would produce:*** *full stability and maximum resilience in the euro-area, the broadest and most homogeneous bond market, full liquidity for sovereigns at the best price*
- ***But…***maximum risk of moral hazard and free-riding Member States. Would probably require far-reaching Treaty changes and the parallel strengthening of economic governance.*

- **N.2 - A partial substitution of Stability Bond issuance for national issuance with joint and several guarantees**
  - The Stability Bond issuance would be underpinned by joint and several guarantees , but would replace a limited portion of national issuance (Blue Bond/Red Bond)
- **N.3 - A partial substitution of Stability Bond issuance for national issuance under several guarantees.**
  - The Stability Bond would replace a limited portion of national issuance but MS would retain liability for their respective share of Stability Bond issuance as well as national issuance.

3. Technical Background:

3.1. Bruegel Blue Bond Proposal

Presented by Bruegel (Jacobson Weizsacker and Jackes Delpla)

the 6 May 2010

- How can the euro area's **return to fiscal sustainability** be organised in view of soaring debt levels and the sovereign debt crisis?
- How can we **finance our debts efficiently**, not least to **prevent debt crises in weaker countries** where high debt levels compounded by a hike in risk premiums on government bonds can create a debt trap?

" This looks like a classic dilemma. European solidarity with the ***most vulnerable European Union countries*** *runs the risk of further* ***weakening the incentives for individual countries to pursue fiscally sustainable policies.*** *"*

" While not a quick fix, our Blue Bond proposal charts an ***incentive-driven*** *and* ***durable way*** *out of this dilemma while helping* ***prepare the ground for the rise of the euro*** *as an important* ***reserve currency****, which could reduce borrowing costs for everybody involved. "*

3. Technical Background:

3.1. Bruegel Blue Bond Proposal

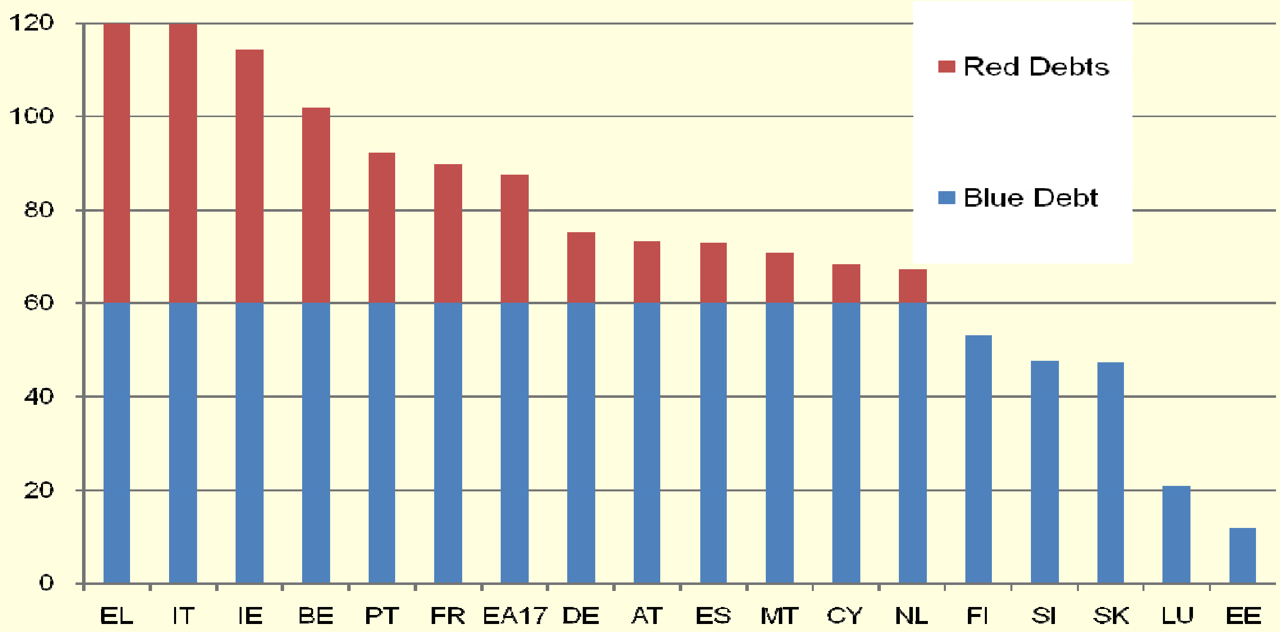
- **Blue bonds:** **up to 60 %GDP of national debt under joint and several liability as senior sovereign debt**, reducing the borrowing cost for that part of the debt.

- **Red bonds:** **any national debt beyond a country's Blue Bond allocation** should be issued as **national and junior debt with sound procedures for an orderly default**, (thus increasing the marginal cost of public borrowing and helping to enhance fiscal discipline).

- **Independent Stability Council (ISC):** will propose **Blue Bond allocations to MS** and voted on by National Parliaments in order to safeguard fiscal responsibility.

3. Technical Background:

3.1. Bruegel Blue Bond Proposal



3. Technical Background:

3.2. European Redemption Fund

Presented by the German Council of Economic Experts (GCEE) in their Annual Report 2011/12 published on the 9 Nov 2011

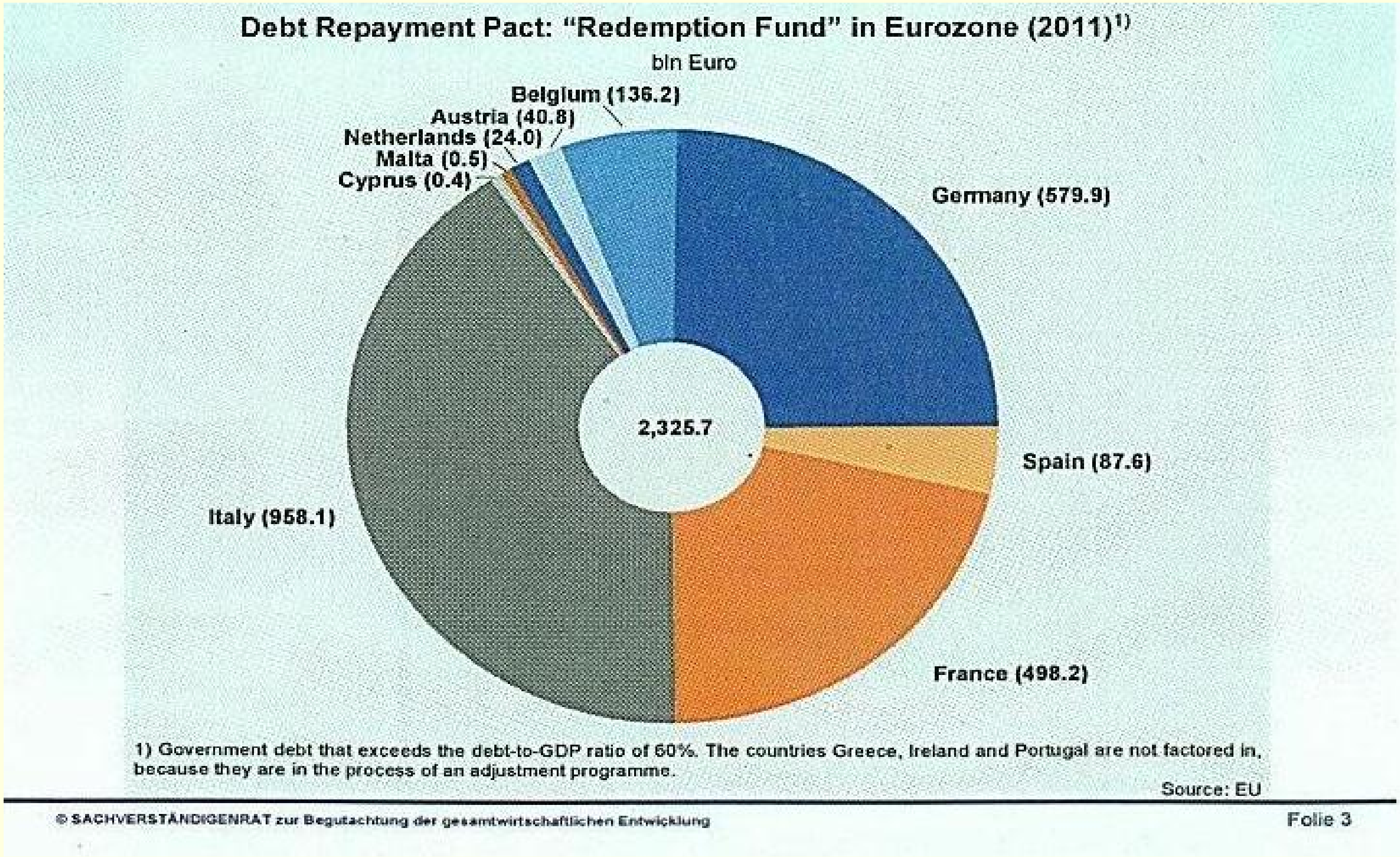
- **All EMU Member States' debt exceeding the 60 %** ceiling on a certain date to be **transferred into the European Redemption Fund (ERF)** for which the EMU members are **jointly and severally liable**.

- At the time of the proposal, the total amount of the ERF would be close to **2.3 trillion Euros of bonds**, estimated to be rated top quality.

- In return, **participating countries would enter into payment obligations toward the ERF** that are calculated such that each country would repay its transferred debts within a total of some **25 years**.

3. Technical Background:

3.2. European Redemption Fund

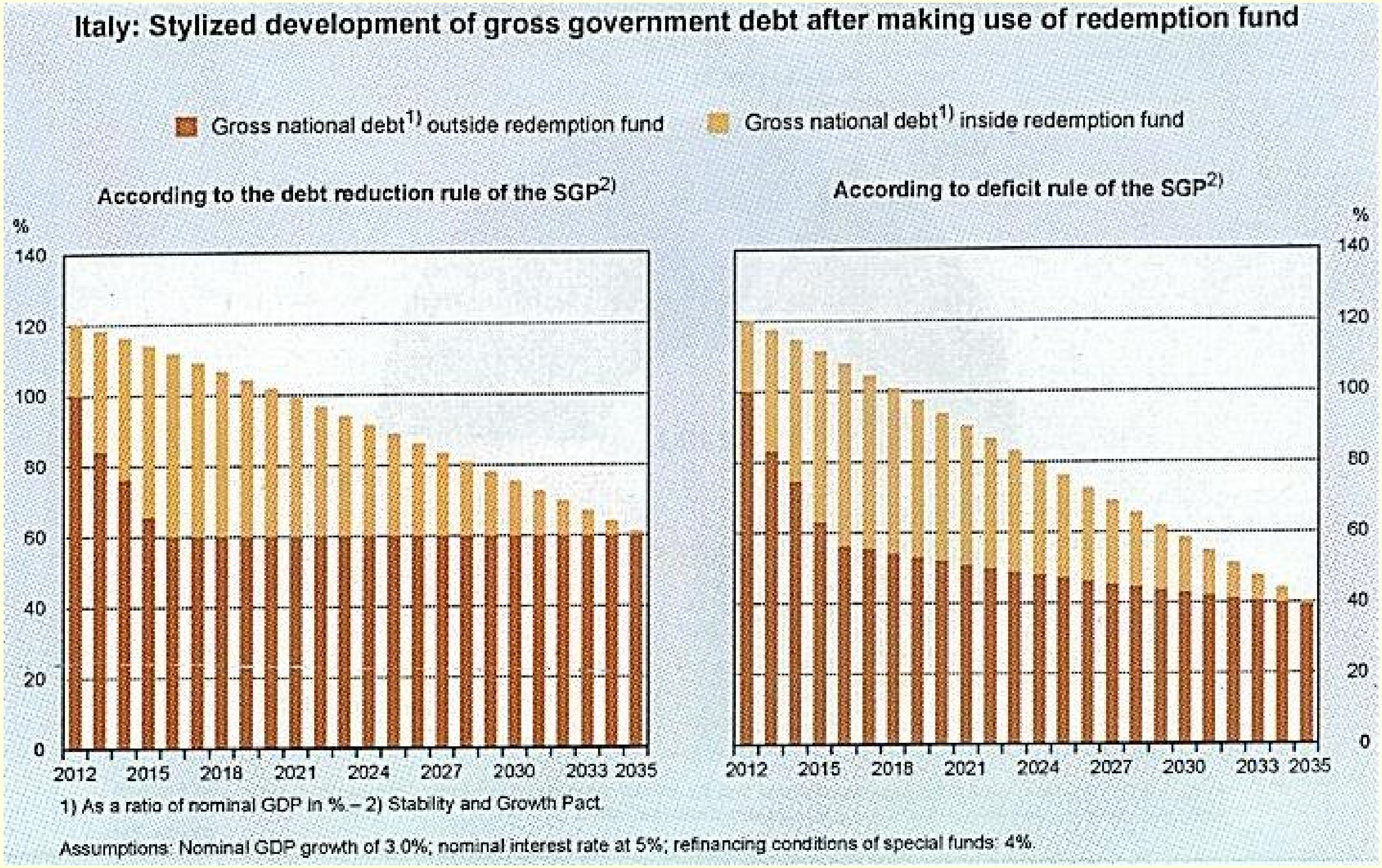


Elisa Ferreira

3. Technical Background:

3.2. European Redemption Fund

- **ITALY as an example:**



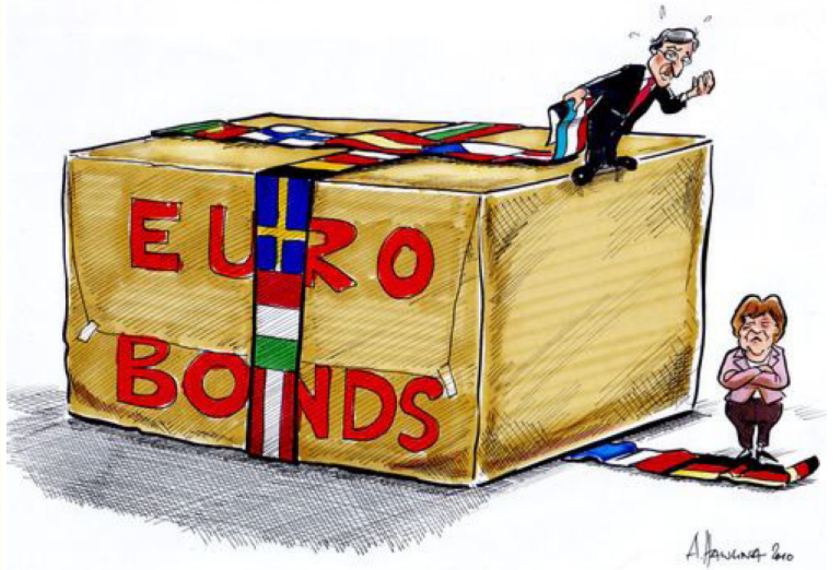
3. Technical Background:

3.2. European Redemption Fund

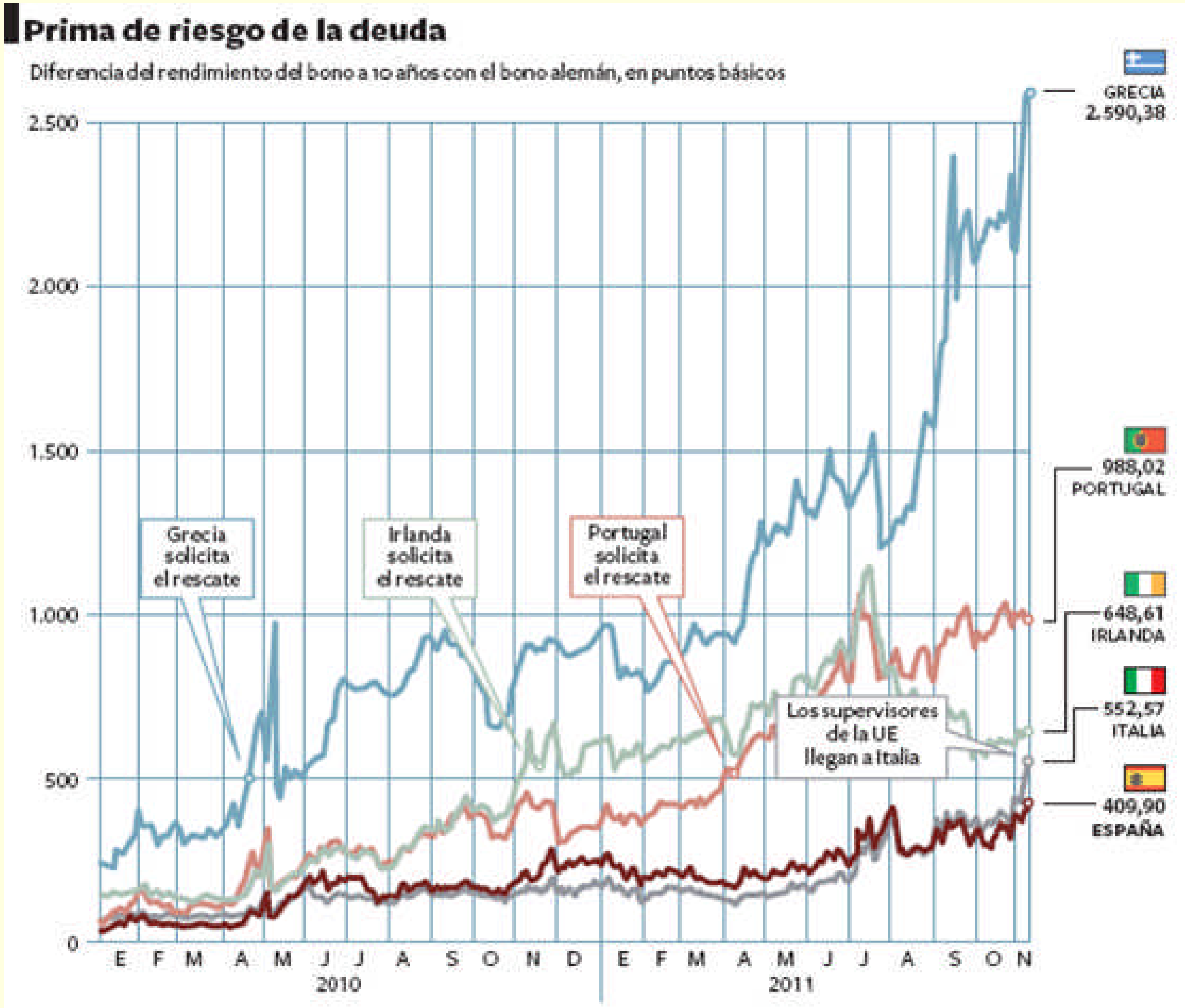
- **Strict conditionality**:
  - **Earmarking/devoting a part of the tax revenue** to payment obligations
  - Depositing **collaterals**
  - Strong commitment to **consolidation and structural reforms**
  - **Debt brakes** in all participating countries based on the German and Swiss models.
  - Sanction for **non compliance** include **being expelled** from the system.

- The **debt cap** shall ensure that, following a transition period, the **structural deficit does not exceed 0.5 % of GDP.**

4. Conclusion



4. Conclusion



4. Conclusion

- The call for Eurobonds is not new (among others):
  - **1977: MacDougall Report** on the future role of public finance in European integration
  - **1993: Jacques Delors** on the "White Paper on Growth Competitiveness and Employment", bonds to be funded by project revenues
  - **1997: Giovannini Group** on public finance presents a range of possible options for co-ordinating the issuance of euro-area public debt
  - **2008: European Primary Dealers Association** (EPDA) published a paper on "A Common European Government Bond"
  - **2009: EMU @10 Report**

4. Conclusion

- The issue became an priority, when:
  - The **2007/8 crisis** in the financial markets ended in a crisis of the **public finances** of Eurozone Member States (30% GDP involved in rescuing the financial sector).
  - The **lack of instruments** within the Eurozone to: develop anti-cyclical policies, to safeguard the € from speculative attacks and to prevent contagion became obvious (Ad-hoc support to Greece, EFSF,ESM, etc.)
  - With the crisis, the principle of "**no default, no bail out and no exit**" of the Eurozone melted; public declarations by **Merkel on Private Sector Involvement PSI** (10/6/2010) made the default of an Eurozone country a real possibility; markets behaved accordingly.

4. Conclusion

4. Conclusion

- Eurobonds are not a “silver bullet”; they must be accompanied by a multi-pillar approach including:

  - A concrete **agenda for convergent growth and employment** (a “Marshall Plan” involving the EIB?)
  - The pursue of **adequate financial market regulation** including the **management of crises in the banking sector**
  - Reinforcing the **ESM under the “community method”,** preferably anchored in EU budget resources
  - Reinforcement of the **EU budget** through **new own resources (a share of FTT)**
  - Reinforcement of the **Economic Governance in the EU and Eurozone** in particular

4. Conclusion

- For the moment, the two "moving" areas with concrete proposals for action are:
  - Financial market regulation <u>without</u> the **management of crises in the banking sector**
  - Reinforcement of the **Economic Governance in the EU and Eurozone** in particular, where: **Euro + Pact + 6 Pack+2 Pack + Fiscal Compact**

- Risking to deliver a **completely unbalanced outcome if not accompanied by** adequate supporting measures, among which, **EUROBONDS**, although in need of definition of:
  - Their concrete **SHAPE**
  - Their **economic and political "PRICE" (including sovereignty)**

4. Conclusion

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