EUROPEAN CENTRAL BANK

EUROSYSTEM

ECB-PUBLIC

28 May 2019

Market consultation on a potential Eurosystem initiative regarding a European mechanism for the issuance and initial distribution of debt securities in the European Union

DISCLAIMER: *In line with its mandate, the Eurosystem will consider the feedback it receives in this consultation, with a view to determining any follow-up actions leading to a potential Eurosystem initiative in this area. In doing so, the Eurosystem will take into account all relevant legal, regulatory and statutory considerations*.

Responding to the market consultation

The European Central Bank (ECB) invites market participants to provide views on all matters described in this consultation and in particular on the specific questions at the end of each section. Comments are most helpful if they:

- are short and precise;
- contain a clear rationale and evidence, if possible;
- highlight the role/position of your institution in the debt issuance landscape; and
- describe any alternative that should be considered in the assessment.

Please indicate in which role(s) your institution expresses views in this consultation:

- issuer
- investor
- CSD
- custodian
- agent (issuing or paying)
- dealer
- other (please specify)

All comments received by **09 July 2019** will be considered**.**
Please provide your feedback by email to EDDI.Initiative@ecb.europa.eu.

Publication of responses

When sending your responses to the ECB, please fill in the box below as applicable:

		YES	NO
For institutions	***We agree with the publication of any related personal data included in the comments on the internet. We declare that we have obtained consent for the publication of such personal data from the involved persons.***	◯	◯
For individuals	***I agree with the publication of my personal data included in the comments on the internet.***	◯	◯

Next steps

The Eurosystem will consider the feedback it receives in this consultation, with a view to determining follow-up actions leading to a potential Eurosystem initiative regarding a European mechanism for the issuance and initial distribution of debt securities in the EU, in line with its mandate.

Contents

1. Introduction

In a truly integrated financial market, the issuance, trading, clearing and settlement of a financial instrument should neither be affected by the location of the instrument itself, nor by the location of the counterparties involved in a transaction in the instrument. This is a fundamental characteristic of a single financial market.

While several developments have taken place in the European Union (EU) in the area of financial market infrastructures regarding securities settlement, e.g. the CSD Regulation[1] and TARGET2-Securities (T2S)[2], there has not been similar progress at the issuance level towards fostering harmonisation and integration in Europe. At the current stage, there is no pan-European, neutral[3] and harmonised channel for the issuance and initial distribution of debt securities that covers the EU as a single "domestic" market. Instead, unlike the situation in other currency areas, issuers with a European perspective have to use a multiplicity of channels and procedures, either domestic or international, which are neither harmonised nor covering the EU and its investors as a single market.

The Eurosystem is therefore exploring the possibility to support a harmonised issuance and distribution of euro debt instruments in the EU. In order to analyse the underlying issue itself, as well as the potential business case for such a service, this Eurosystem market consultation invites responses from a wide audience of stakeholders, including issuers and investors.

[1] Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012.

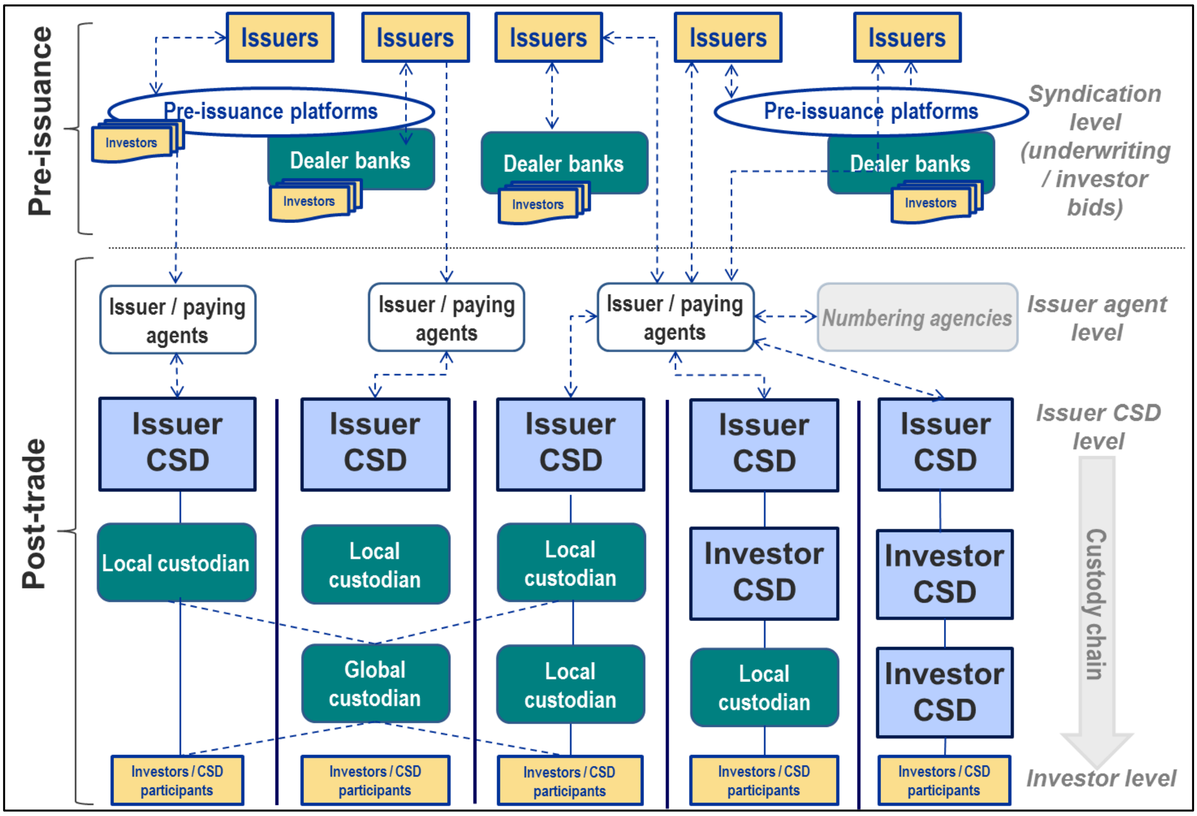
[2] https://www.ecb.europa.eu/paym/target/t2s/html/index.en.html.

[3] In this document, "neutrality" means that the desired market structure is such that it does not put the location of issuance (i.e. of the issuer CSD and its direct participants) in a privileged position over other intermediaries and end-users that wish to access the securities.

2. Current debt securities distribution ecosystem

The issuance process for debt securities in Europe consists of two main sequential phases: pre-issuance and post-trade[4]. The following paragraphs provide a high-level stylised description of these phases.

Chart 1: Schematic overview of the securities distribution ecosystem



Pre-issuance includes the preparation of issuance, choosing the modalities of the price discovery process (syndication, auctioning or private placement) and reaching agreement between the issuer and investors (mostly via dealer banks and the collection of bids) on the economic terms of the securities. In the pre-issuance phase, dealer banks and agents play a key role. They provide advice and market intelligence to issuers, underwrite the securities issuance, communicate with investors and collect their orders and take responsibility for certain elements of regulatory compliance (prospectuses, know-your-customer requirements, etc.).

To support the pre-issuance activities, issuers either rely on proprietary tools provided by the dealer banks or they can use the technical facilities of a pre-issuance platform provided by a third party. Investors, i.e. capital providers, on the other hand rely mostly on the dealer bank service for interacting with the issuers.

Post-trade processes take place after the pre-issuance phase and include the actual issuance of the debt security in central securities depositories (CSDs) and its delivery to investors via custodians and other intermediaries through multiple distribution channels. In the post-trade domain, issuers are usually represented by agent banks, which manage securities and cash accounts, arrange the issuance procedure and ensure collection and distribution of cash proceeds (e.g. interest payments) to the

[4] A more detailed description of the securities distribution landscape and the roles of different actors can be found in Annex 3 (pp. 21-41) of the report by the European Post Trade Forum (a group of experts set up by the European Commission in 2016).

investors during the lifespan of a security. Investors, i.e. individuals or legal entities holding the final investor balances, rely on a number of different channels or models for holding such balances. This can happen via global or local custodians or CSDs, or a combination thereof.

Question 1: • **Please provide your views on the description of the European ecosystem for the issuance of debt instruments, in particular as regards whether you deem other actors, elements or processes relevant to complete the picture.**
Answer 1: *[please fill in]*

3. Issue at stake

From the perspective of a European or third-country entity interested in issuing debt in euro within a truly European market, the aforementioned securities distribution ecosystem might present a number of challenges. First, although large issuers can already reach a wide range of European and international investors[5], there is **no pan-European issuance mechanism**, and in particular one operating in central bank money[6], offering issuers the possibility to efficiently reach all European investors on an equal basis, and thereby fostering a single and deep European capital market. Second, in the existing, largely national, securities distribution channels, the location of issuance might put local actors in a preferential position compared with other investors and market actors in Europe. In today's practices, an issuer might choose primarily its own domestic market and CSD or rely on the services of an international CSD which serves its primarily international participants by settling in commercial bank money.

As shown in Chart 1, there are a variety of channels available in the market today to facilitate investor access. However, these solutions are neither neutral, nor pan-European by construction, i.e. they are based on a hierarchical model and they maintain a privilege for the initial issuance location and its participants. The position of the investors within the holding chain, including their location, may have an influence on the efficiency of and the costs associated with access to a given security. As a consequence, there may be an impact on the level playing field and hence on the equal access to European debt securities by investors. Thus, the number of intermediaries and the cost of holding the assets are determined by the location of the investor vis-à-vis the initial issuance location. Compared with other currency areas, e.g. the US, Japan or China where truly domestic issuance distribution channels exist, there seems to be a structural gap in the EU.

In the area of pre-issuance, European issuers and investors currently face a multiplicity of non-interoperable issuance platforms and proprietary procedures with a very low level of automation and digitalisation. This is due to the lack of **standardisation and harmonisation** between the different private initiatives, as well as the low level of automation of existing private initiatives. This lack of efficiency is recognised in an article in the third quarter 2018 Quarterly Report of the International Capital Market Association (ICMA),[7] which states the current challenges and opportunities, from the perspectives of the investors, issuers and syndicates. In addition, the report: (i) calls for the development of standards and further harmonisation in the primary bond markets' pre-issuance processes; and (ii) states that "*a scalable infrastructure utility, based on open source standards allowing for connectivity to multiple technology providers across asset classes, is strongly preferred to a monopolistic, commercial infrastructure*".

The European Post Trade Forum (EPTF) also notes in its report that: "*the actual issuance and holding procedures, as well as the type of services offered by different entities in the issuance process to issuers, vary considerably from country to country, depending on issuer preference, market practice and*

5 In relative terms, larger issues are normally more easily accessible to a wider set of investors, while smaller issues are much less accessible.

6 See the ECB glossary: https://www.ecb.europa.eu/home/glossary/html/glossc.en.html. *Central bank money: Liabilities of a central bank, in the form of either banknotes or bank deposits held at a central bank, which can be used for settlement purposes.*

7 See Callsen, G., "Electronification in primary bond markets" (available at https://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/Regulatory-Policy-Newsletter/Previous-versions/), pp. 26-27.

regulation".[8] The existing ecosystem results in considerable heterogeneity and complexity for market actors, including the end-investors. Some issuers have even argued that it entails inefficient and costly procedures that result in less favourable conditions for issuers which wish to reach a pan-European investor base.[9] The EPTF report recognises that this heterogeneity is the result of different national legal regimes in the EU in the area of securities and other financial law, which are outside the remit of the Eurosystem, but is also due to other barriers, including operational and technical standards, market conventions, etc. Furthermore, the current environment of structural fragmentation may not be conducive to a deep and liquid single European market for debt instruments.

Question 2a: • **Do you think that there is a structural issue in the current debt issuance and distribution in the EU, seen from the perspective of a single capital market? If so, what is your view regarding the underlying causes of this structural issue?**
Answer 2a: *[please fill in]*
Question 2b: • **Do you face problems or see problems for issuers when reaching out to a pan-European or international investor base? If so, please specify.**
Answer 2b: *[please fill in]*
Question 2c: • **What are the main considerations for issuers and/or their agents/dealers when choosing a place of issuance and a service provider?**
Answer 2c: *[please fill in]*
Question 2d: • **What is your view on the statement that there is a need to improve competition and level playing field conditions regarding the access of banks, investors and CSDs to debt securities?**
Answer 2d: *[please fill in]*
Question 2e: • **Would the improvement in the neutrality, harmonisation and pan-European reach support and develop further the issuance of debt in euro?**
Answer 2e: *[please fill in]*

8 https://ec.europa.eu/info/sites/info/files/170515-eptf-report-annex-3_en.pdf.

9 "*A single system to distribute sovereign bonds would offer investors – especially international investors – more transparency and ease access for them.*" Speech by the ESM Managing Director on 26 November 2018 (https://www.esm.europa.eu/speeches-and-presentations/future-economic-and-monetary-union-and-role-esm-speech-klaus-regling).

4. Possible actions to address the issue at stake

In order to address the above structural challenges, different actions could be considered.

4.1 Harmonisation

It is widely acknowledged that harmonisation is an enabler of, if not a prerequisite for, market integration. Despite the remaining gaps, post-trade harmonisation has progressed substantially in the last decade, also thanks to the close collaboration between private entities and public authorities. In addition to the regulatory harmonisation (e.g. MiFID II, EMIR and the CSD Regulation),[10] it is widely acknowledged that the single most influential initiative has been the T2S[11] harmonisation agenda which is mostly attributable to the successful catalyst role of the Eurosystem in this area. The T2S harmonisation agenda focused on areas of core relevance for T2S (e.g. related to messages, accounts or corporate actions), but did not address any areas of pre-issuance.[12]

As reflected in the previous section, in the area of pre-issuance, the harmonisation efforts have not progressed equally despite efforts made by primary market practitioners. As targeted harmonisation areas, market actors usually refer, among other things, to those standards and market conventions relating to a standardised order book, the consistent usage of terminology in term sheets, rounding conventions, the corporate action information flow, timelines and processes, etc. Pursuing further the pre-issuance harmonisation agenda, in a coordinated and structured way, across the EU could tackle many of these topics.

Question 3a: • **Do you think that there is a need for further harmonisation and standardisation in the area of debt securities issuance?**
Answer 3a: *[please fill in]*
Question 3b: • **Should the work on harmonisation/standardisation cover the full transaction chain, i.e. from pre-issuance to post-trade?**
Answer 3b: *[please fill in]*
Question 3c: **What are your views regarding the pre-issuance harmonisation items/topics? Which processes should be looked at?**

[10] These EU laws mostly focused on aligning definitions, licensing regimes and prudential requirements and resolving conflicts in national laws in these fields, but did not cover pre-issuance procedures or all post-trade procedures.

[11] *T2S, One year of full operation*, December 2018 https://www.ecb.europa.eu/paym/intro/publications/pdf/ecb.targetsecspecial181219.en.pdf?91d587b5a441bbd11d3cc501138c0c79

[12] *9th T2S Harmonisation Progress Report,* October 2018 https://www.ecb.europa.eu/paym/intro/publications/pdf/ecb.targetsechpr181017.en.pdf?ae3a947ea50e4f19775c4c31d89d05f0

Answer 3c**:** *[please fill in]*
Question 3d: • **What would you consider the best way forward, for example in terms of methodology and governance, for fostering harmonisation in this area?**
Answer 3d: *[please fill in]*
Question 3e: • **Is there a need to reinforce and/or support with EU regulation any harmonisation efforts in the area of pre-issuance?**
Answer 3e: *[please fill in]*
Question 3f: • **Do you see any other efforts that could help resolve the current market fragmentation?**
Answer 3f: *[please fill in]*

4.2 Provision of a European market infrastructure service

In addition to harmonisation, the perceived lack of neutrality and pan-European reach could potentially be addressed by the establishment of a European market infrastructure service, which would be offered on a level playing field basis.

The objective of such a service would be to enable euro debt issuers to access the whole EU market as if it was a single domestic market, both in terms of a single issuance process and a streamlined, commoditised service layer. The service could be based on a multilateral governance arrangement, encompassing all interested stakeholders, e.g. issuers, banks, CSDs and potentially investors.

The provision of such a service does not need to be an alternative to the harmonisation work considered above. On the contrary, the delivery of a European service and the work on the pre-issuance harmonisation agenda could reinforce and support each other.

Question 4a: • **Do you think that the establishment of a European market infrastructure service could potentially address the lack of neutrality and pan-European reach in the current debt securities market? If not, what other solution would you propose?**
Answer 4a: *[please fill in]*
Question 4b: • **Do you think that this service, as described above, exists today in the EU? If not, should it**

be offered by a private entity or a public entity, and why?
Answer 4b: *[please fill in]*
Question 4c: • **Is there a need to combine both approaches, i.e. a Europe-wide harmonisation initiative and the provision of a European market infrastructure service, and why?**
Answer 4c: *[please fill in]*
Question 4d: • **Do you see a need for the Eurosystem to support those actions? If so, how?**
Answer 4d: *[please fill in]*

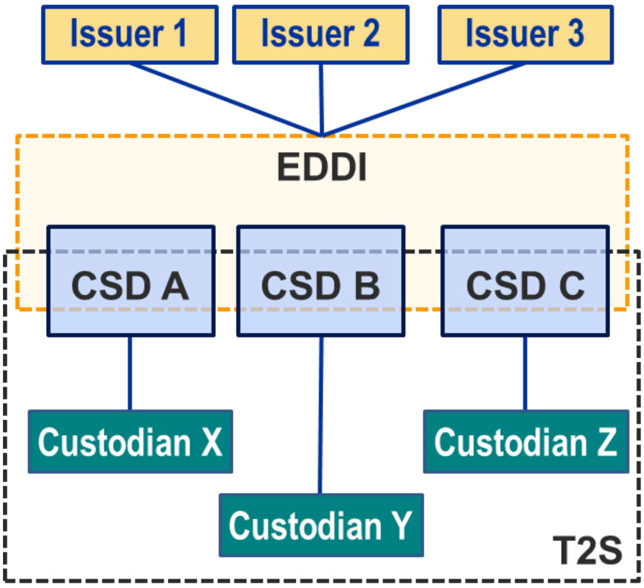
5. EDDI: high-level description of the scope

If the Eurosystem were to take a role in establishing a European service for the issuance and initial distribution of debt securities in the EU, the initiative would need to cover both ends of the transaction chain. Connecting the pre-issuance and the post-trade domains would foster a seamless standardised link between the two.

In addition, by covering both ends of the transaction chain, and based on the ECB's catalyst role, this service, with the working title "European Distribution of Debt Instruments (EDDI)", could potentially strengthen the momentum towards the establishment of a European debt instrument technical standard.[13]

As shown in Chart 2, EDDI could be envisaged as a centralised service interlinking issuers and CSDs to facilitate the pre-issuance and initial distribution of debt securities in the EU.

Chart 2: A high-level model of EDDI



EDDI would have two business components and would be based on a modular approach, i.e. leaving full freedom to its users as to which (if any) they want to use (see Charts 3 and 4).

The pre-issuance component would be a technical toolkit available for issuers (or their issuer agents and/or dealer banks upon authorisation) offering them functionalities which support the definition and communication of an upcoming debt issue, the creation of the order book, the collection of orders from investors and the allocation of the debt instrument issuance to these orders.[14]

The post-trade component would receive the final allocation from the pre-issuance component (and potentially from private pre-issuance tools). On that basis it would facilitate the creation and the

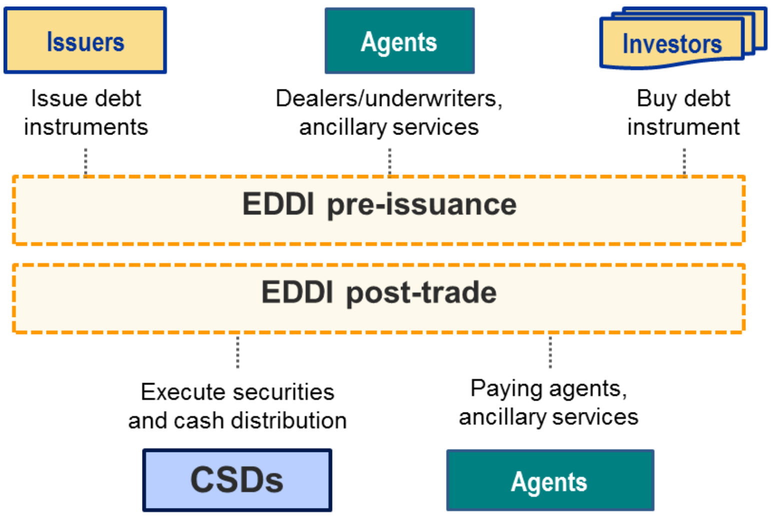
[13] The establishment of a European debt instrument technical standard could cover certain technical and operational rules and procedures and business conventions which could facilitate a harmonised and standardised issuance of debt in euro central bank money.

[14] Although the primary focus of EDDI is high-quality euro debt securities issued by issuers with a European funding perspective, the EDDI pre-issuance model would be able to handle any currency denominations.

centralised distribution of the EDDI-issued debt instruments via the EDDI-participating CSDs. The issuance and initial distribution function could be provided by EDDI only in close collaboration with the CSDs connected to EDDI. This function would also include the notary service (i.e. ensuring the integrity of the global amount issued) and support the relevant corporate actions (e.g. information flows, interest payments) throughout the life cycle of the securities. The EDDI post-trade component would rely on T2S in order to provide the necessary real-time realignment between CSDs in order to enable secondary market cross-CSD transactions across the EU. EDDI's objective is not to replace existing commercial arrangements, but rather to support the participants in the pre-issuance and initial distribution end-to-end process with standardised interactions and information flows.

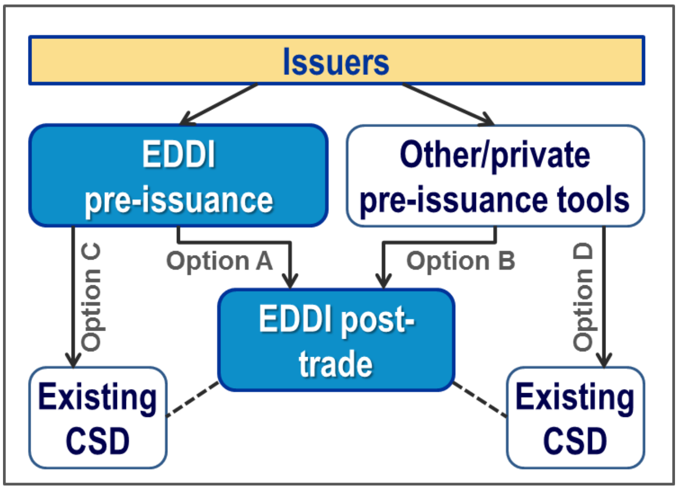
To achieve a high degree of synergies with existing market infrastructures, EDDI could be developed within the framework of the existing TARGET Services. This implies, inter alia, that EDDI would rely, via the EDDI-participating CSDs, on the state-of-the-art T2S settlement functionalities, e.g. real-time central bank money settlement or the central liquidity management functionalities (auto-collateralisation) commonly shared, or under development, across the TARGET Services.

Chart 3: Overview of the roles performed in EDDI pre-issuance and post-trade



EDDI would follow a modular approach, thus allowing users of the service to voluntarily adapt their usage of EDDI to best suit their issuance models and business needs. In practical terms, this translates into four possibilities available to the relevant stakeholders: (a) full use of both EDDI components, i.e. pre-issuance and post-trade; (b) use of only the post-trade EDDI component; (c) use of only the EDDI pre-issuance component; or (d) not using the EDDI service at all.

Chart 4: EDDI as an optional end-to-end service for the securities market



Question 5a: • **What is your view regarding the inclusion of the pre-issuance and post-trade functions in a potential EDDI initiative?**
Answer 5a: *[please fill in]*
Question 5b: • **What is your view regarding the concept of the optional and voluntary usage of the two EDDI components for all relevant EDDI stakeholders/users?**
Answer 5b: *[please fill in]*
Question 5c: • **What do you think are the relevant debt issuers that could benefit from, or would be interested in, issuing via EDDI and why?**
Answer 5c: *[please fill in]*
Question 5d: • **Should access to EDDI be restricted to certain classes of issuers? If so, why?**
Answer 5d: *[please fill in]*
Question 5e: • **How would the benefits of EDDI change if access to EDDI were restricted to certain classes of issuers, e.g. public or supranational, sub-sovereign and agency (SSA) issuers?**
Answer 5e: *[please fill in]*
Question 5f:

• **Should access to EDDI be restricted to certain CSDs?**
Answer 5f: *[please fill in]*
Question 5g: • **In your view, which criteria should an EDDI service meet in order to be attractive for your institution?**
Answer 5g: *[please fill in]*

6. EDDI's potential impact on the market

As presented above, EDDI could be a central European service covering the pre-issuance and initial distribution process, to be offered by the Eurosystem to the market. Since this would be a totally new service, currently not available in the market, it would have some influence on how the different stakeholders are currently organised.

- **Market-wide interaction would be facilitated**. With the EDDI service, the Eurosystem would provide issuers and the relevant market actors (e.g. issuer agents, investors, CSDs) with a central, standardised and neutral platform in order to facilitate their interaction. Apart from the immediate standardisation gains due to a single centralised system, such interaction could facilitate, in the medium to long run, the definition and endorsement of and compliance with harmonisation standards, in particular in the area of pre-issuance. The EDDI harmonisation agenda, and in particular the potential establishment of a European debt instrument technical standard, would be expected to have a positive impact also when the issuance and distribution are processed outside EDDI.[15]

- **Disintermediation is not an objective of EDDI.** Existing intermediaries, including issuer agents, dealer banks and custodians, would be able to use any combination of the two EDDI components and their own proprietary procedures depending on the issuer's choice of pre-issuance and post-trade solutions. Existing or new private pre-issuance platforms could link up with the EDDI post-trade component (subject to establishing technical access to EDDI's standardised interface). At the same time, the EDDI pre-issuance component could be used to support post-trade services outside EDDI (i.e. by feeding into a single issuer CSD outside EDDI).

- **EDDI could influence the business models of CSDs**. As mentioned above, the EDDI issuance and initial distribution service could only be delivered in close collaboration with the CSDs. For the securities issued via EDDI, the business model of the EDDI-participating CSDs would no longer be determined by their ranking in the custody chain, i.e. whether they act as "issuer" or "investor" CSD for a specific security. Instead, the differentiation between the CSDs would be based on the service and prices they would offered to the market participants. As a consequence, these CSDs will, for securities issued via EDDI, forgo the exclusivity over the primary deposit which has so far been established by the location of issuance. On the other hand, any EDDI-participating CSDs would be in a position to benefit from access to new securities issued via EDDI, which would be made equally available to all EDDI-participating CSDs on a level playing field, i.e. with no location exclusivity attached to the issuance and distribution process.

- **Issuers would have full choice in deciding how they want to use the EDDI service**. EDDI would offer eligible issuers a choice that they do not have today, namely the possibility to issue European

[15] This could be achieved via a long-term conversion of certain national conventions towards the EDDI European debt instrument technical standard.

securities without having to select a specific location of issuance. Combined with an EDDI-related harmonisation agenda, EDDI could increase, for both European and international institutions, the efficiency and attractiveness of the issuance of debt denominated in euro. As a consequence, EDDI could potentially increase the liquidity of the assets issued through its service, and thus provide benefits for issuers with highly rated debt instruments in achieving a truly pan-European reach when collecting funds. However, as EDDI would be an optional service offered to debt issuers with a European perspective and would not be able to cover all issuers and securities, some issuers would continue using the existing issuance and distribution channels and some securities would continue to be issued outside EDDI. Such choices would reflect their specific fund-raising interests and/or their wider market strategies, as well as the scope of EDDI. As shown in Chart 4, EDDI would be based on a modular approach providing its users with optionality regarding the usage of its service components. In any case, issuers of all sizes, also outside EDDI, should in principle benefit from the positive externalities of the EDDI harmonisation agenda.

- **Investors could benefit from a standardised communication channel.** Compared with a multiplicity of non-automated communication channels and interfaces, institutional investors could benefit from a single communication channel for all instruments issued through EDDI in their interactions with issuers and their agents in the context of EDDI. As mentioned above, EDDI's objective is not to replace existing commercial arrangements, but rather to support the participants in the pre-issuance and initial distribution end-to-end process with standardised interactions and information flows. Investors could optimise their interactions within the custody chain. On the custody side, investors/custodians would be able to choose their CSDs on the basis of the level of the service and its cost. There would no longer be a need to connect to a multiplicity of European issuer CSDs for the securities issued in EDDI. This could offer investors/custodians the opportunity to streamline and optimise the custody of their holdings.

Question 6a: • **What are your views on the expected impact of EDDI on the market in general and on your institution in particular?**
Answer 6a: *[please fill in]*
Question 6b: • **Which other elements do you consider relevant regarding the potential impact of EDDI, beyond what is described above?**
Answer 6b: *[please fill in]*