

Silke Weiss in interview with *Börsen-Zeitung* (January 2023)

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Interviews

ESM



Interview with Silke Weiss, ESM Head of Funding and Investor Relations

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Interviewer: Kai Johannsen

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Börsen-Zeitung: Ms Weiss, there was a significant rise in yields on the bond markets in 2022, which also affected ESM/EFSF bonds. How did you

as an issuer cope with this rise in yields?

Silke Weiss: That is right. The two rescue funds and all other issuers were confronted with a volatile market situation and rising interest rates last year. At the beginning of 2022, we issued a 30-year bond with a coupon of only 0.7%, while the ESM bills were priced at minus 67 basis points. The EFSF was able to secure favourable long-term conditions for its borrowing countries. In volatile markets, it is important to be able to act flexibly, i.e., to have different instruments and issuance formats available. As usual, we used the auction system, together with syndications for our refinancing. Auctions were used exclusively for bills and syndications for our long-term refinancing. We had already raised the entire long-term refinancing requirement for 2022 by October, earlier than usual.

What has been the response of investors in the primary market in this market environment?

Despite the exceptional market volatility, our order books were significantly oversubscribed, and our bonds enjoyed strong demand from investors worldwide. Last year, we saw a strong increase in demand in the euro area: more than half of our bonds went to investors in the euro area, our domestic buyer base. This is remarkable given our well-diversified network of around 1,700 investors. In addition, due to the normalisation of the ECB's interest rate policy coupled with the uncertainty regarding growth and inflation in the euro area, we noticed an increased interest among investors in securities with shorter maturities.

What is the status of the social bond framework and what are your plans for this year?

We introduced a social bond framework about three years ago. This framework is related to our credit line that we introduced at the beginning of the pandemic. This credit line was available until the end of last year in case euro countries needed support to finance health-related costs. As is often the case with precautionary credit lines, it was not drawn. Therefore, we did not issue any social bonds. However, the credit line, along with the actions of the European Investment Bank and the European Commission, proved very effective in calming the markets and showing unity after the pandemic outbreak. The ESM is a major issuer and investor, and we see it as extremely important to be represented in various bodies and working groups and to contribute to the development and promotion for best practices in

greening the financial system.

What impact do you see the Covid-19 pandemic, which is currently gaining momentum again in China, and the Ukraine war are having on green and sustainable finance and thus also on social bonds?

The market for sustainable bonds in Europe has developed very dynamically in recent years, also recently due to the pandemic: in 2021, around 51% of issuers were from Europe, almost half (45%) of the bonds were denominated in euros, compared to around a third (29%) in US dollars. Luxembourg has become the global centre for sustainable bonds. From an issuer perspective, green label bonds had a cost advantage over conventional bonds. However, we also saw that in the changed interest rate environment this so-called “greenium” seems to disappear. If this cost advantage disappears from the issuers' perspective, the segment could falter; this is something to watch. The ESM has been investing in green and sustainable bonds since 2014 and signed the United Nations Principles for Responsible Investment about three years ago. This year, the first ESM signatory report will be published.

Let's move on to your funding outlook for 2023. What are the funding volumes for ESM and EFSF in detail, and how does that compare with 2022?

The funding programme for this year is €28 billion, of which €20 billion for the EFSF and €8 billion for the ESM. Compared to 2022, this is very stable. We will continue to add to outstanding bonds, issue new bonds in euros and US dollars, and maintain our bill programme with 3- and 6-month maturities. Our main objective will be to smoothly cover funding needs, using a wide range of maturities and financial products.

How has the year started for you so far?

Our first EFSF issue took place on 9 January and was a promising start in the year, with a high oversubscription rate. As usual, there are a lot of issuers in the market at the same time in January and the coordination of primary transactions is very important, especially when transactions take place at the same maturity and yield level. This coordination went very well with the euro area debt management offices and the issuers in Luxembourg. Since the beginning of the year, our bond issues and bill auctions have all been oversubscribed several times and we are pleased with the strong and broad support from our investors.

How high is the current outstanding bond volume of the two entities ESM and EFSF, and how many bonds are there now?

The outstanding volume for the EFSF is €199.2 billion, distributed over 50 bonds and €99.5 billion for the ESM with 25 bonds. On the credit side, the ESM reached an important milestone in December 2022: after several unscheduled repayments by Spain, there was the first scheduled repayment of €3.6 billion. The Spanish government had previously transferred [repaid] funds (€17.6 billion out of a total of €441.3 billion) from the bank recapitalisation programme several times before the deadline. Scheduled repayments mean that we have now fully left the euro crisis behind us.

In 2022, as in 2021, you were able to close your funding very early, i.e., already in October. How was it possible to close the funding again so early despite the rise in yields and tense market conditions at the beginning of the year due to the Ukraine war?

In fact, we successfully closed our annual funding needs for both rescue funds already in October. To be more precise, the last EFSF transaction was on 4 October and the ESM transaction on 17 October 2022. Last year, we focused exclusively on the euro market and did not – as in previous years – execute a US dollar transaction, which might have taken place a little later in the year. We also benefited from our communication strategy. Not announcing the issuance windows and thus gaining flexibility has allowed us to choose the timing of our transactions more flexibly. We were thus able to better respond to investor demand and avoid “volatile” times for our executions. This has benefited us as an issuer but also our investors.

How did the dollar curve continue to build and what is planned for this year? Do you intend to tackle other currencies?

Since 2017, the dollar market has given us access to US dollar funding with maturities of up to 5 years. Until 2021, we issued one dollar-denominated ESM bond every year. In total, there are five benchmarks with two- and five-year maturities and the total outstanding volume of \$7 billion. Given the higher interest rates and greater interest in the short end of the euro curve, investor demand for euro bonds has been particularly strong. Therefore, we did not issue any bonds in US dollars last year. However, our dollar activities continue to be an important complement to our funding strategy. They will remain an important, strategic instrument in the future.

The ESM has the possibility to refinance in currencies other than the euro and the dollar. However, the euro remains our priority, allowing us to offer our investors a regular supply of euro bonds.

What is the status of the registered bond programme and what are your plans for 2023?

It is very important for the ESM and EFSF to have a variety of refinancing instruments at our disposal. We need to be able to use different products in case of increased ESM funding needs. Just like the dollar-denominated bonds, the privately placed registered bonds (N-bonds) that can be issued for the rescue funds are an instrument of our diversified funding strategy. If there is a corresponding demand, investors can contact us at any time via a member bank of our market group and express their interest in such securities. The outstanding N-bond volume is currently €2 billion and has enabled us to secure favourable long-term refinancing costs for all five programme countries.

Are you planning to use other new instruments this year?

The new Managing Director is currently travelling to all 20 euro area countries and discussing with the finance ministers how to make the ESM even better prepared for crises and meaningful. We will then see what the result is.

Author



[Silke Weiss](#)

Head, Funding and Investor Relations

Contacts



[Cédric Crelo](#)

Head of Communications and Chief Spokesperson

+352 260 962 205

c.crelo@esm.europa.eu



[Anabela Reis](#)

Deputy Head of Communications and Deputy Chief Spokesperson

+352 260 962 551

a.reis@esm.europa.eu



[Juliana Dahl](#)

Principal Speechwriter and Principal Spokesperson

+352 260 962 654

j.dahl@esm.europa.eu