# ESMA Risk Dashboard

**No. 3, 2014**

3 September 2014|ESMA/2014/883

ESMA Risk Dashboard, No. 3, 2014

ESMA Economics and Financial Stability Unit

 The reporting period of this document is 01 April 2014 to 30 June 2014, unless indicated otherwise. Legal reference of this Report: Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC, Article 32 "Assessment of market developments", 1. "The Authority shall monitor and assess market developments in the area of its competence and, where necessary, inform the European Supervisory Authority (European Banking Authority), and the European Supervisory Authority (European Insurance and Occupational Pensions Authority), the ESRB and the European Parliament, the Council and the Commission about the relevant micro-prudential trends, potential risks and vulnerabilities. The Authority shall include in its assessments an economic analysis of the markets in which financial market participants operate, and an assessment of the impact of potential market developments on such financial market participants." The charts and analyses in this report are, fully or in parts, based on data not proprietary to ESMA, including data from commercial data providers and public authorities. ESMA uses these data in good faith and does not take responsibility for their accuracy or completeness. ESMA is committed to constantly improving its data sources and reserves the right to alter data sources at any time.

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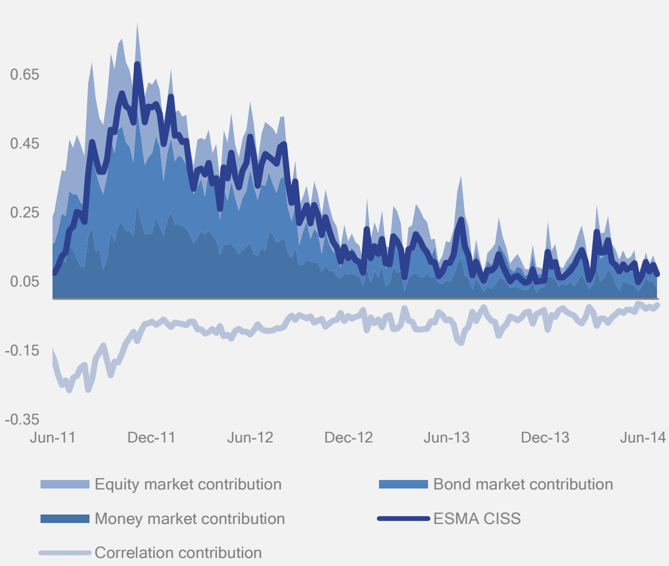
# ESMA Risk Dashboard

Systemic stress: Systemic stress low but volatile R.1




Note: ESMA version of the ECB-CISS indicator measuring systemic stress in securities markets. It focuses on three financial market segments: equity, bond and money markets, aggregated through standard portfolio theory. It is based on securities market indicators such as volatilities and risk spreads.
Sources: ECB, ESMA.

Main risks: Sources R.2

| Risk category | Systemic risk | Change since 1Q14 | Outlook for 3Q14 |
|---|---|---|---|
| Liquidity risk | ● (yellow) | ↗ | ↗ |
| Market risk | ● (yellow) | ↗ | ↗ |
| Contagion risk | ● (yellow) | → | → |
| Credit risk | ● (red) | ↘ | ↘ |

Note: Assessment of main risk categories for markets under ESMA's remit since last quarter and outlook for the following quarter. Systemic risk assessment based on categorisation of ESMA Systemic Risk Heat Map, green=low, yellow=moderate, orange=high, red=very high. Systemic Risk Heat Map measures current risk intensity. Upward arrows indicate a risk increase; downward arrows indicate a risk decrease.

Main risks: Categories R.3

| Economic environment | Change since 1Q14 |
|---|---|
| Macroeconomic conditions | → |
| Interest-rate environment | ↗ |
| Sovereign-bank nexus | → |
| **Securities markets conditions** | |
| Risks in EU sovereign debt markets | ↘ |
| Market clustering | → |
| Funding risk | → |
| Valuation risk | ↗ |
| Market functioning | ↗ |

Note: Assessment of main risk sources under ESMA's remit: change since the last assessment. Upward arrows indicate an increase in the contribution to risks, downward arrows indicate a decrease in the contribution to risks.

*In 2Q14, EU systemic stress indicators reverted to relatively low levels. The prevailing sanguine market sentiment was at odds with sluggish economic fundamentals and partially related to the ultra-low interest rate environment. Market and liquidity risk increased and look set to increase further, however, while credit risk fell but remained very high. The hunt for yield intensified and, in turn, sustained yield compression across risk classes, loaded new risks onto balance sheets, and drove valuation and market risks up. The risk of critical market corrections rose further. The systemic impact of any correction could be exacerbated by liquidity bottlenecks, such as might arise from thin dealer markets or rising collateral requirements. We maintain our overall systemic risk assessment for 2Q14, but expect a further deterioration in market and liquidity risks in the third quarter which may trigger a revision.*

**Systemic stress:** Following a more volatile 1Q14, systemic stress levels abated early 2Q14, with the focus remaining on external risks. The CISS systemic stress indicator dropped back to the low levels of early 1Q14, also in line with anticipation of continued monetary policy support. While this reduction was broad-based, equity markets led money and, to a lesser extent, bond markets. Market risk, especially for valuations, continued to grow: Prices of financial assets remained close to historic highs across various asset classes in several MS, as market participants appeared increasingly sanguine. Illiquidity could exacerbate dislocations that result from an interest rate snapback or market corrections triggered by other events. Depending on the degree to which high valuations are credit-fuelled, a change in real debt burdens could have significant implications. The gradual and fragile nature of the recovery, even if more balanced across MS, implies that convergence in the real economy and continued reduction of risks related to legacy assets will take time. Geopolitical risks remained elevated, notably in UA.

## Economic environment

**Macroeconomic conditions:** While EU macroeconomic conditions initially improved, the outlook of a sluggish and fragile recovery remained unchanged. Activity was uneven across MS, even if to a lesser extent than in previous years, as differences in developments among core economies became more apparent. Government and external current accounts broadly improved along with continued, if anaemic growth in the EA and stabilising dynamics in weaker MS. Yet, significant risks persist, including with respect to activity levels in several large MS. Questions also linger over the capacity to select and implement appropriate structural reform measures. Thus, several economies continued to exhibit weak growth and labour markets, with concerns over disinflationary trends important. These factors, where elevated, do not help reduce the burden associated with public and private debt. Risks of supply-side shocks remained elevated, especially in relation to external factors, including exchange rates and commodity prices as potential channels. Among these is uncertainty around EM, including China.

**Interest rate environment:** Interest rates remained near historic lows as leading central banks continued to provide monetary policy support and as yields continued to compress across sectors and risk categories. With its introduction of negative interest rates – lowering the deposit rate to -0.10% on 3 July 2014 – the ECB has entered unchartered territory, the effects of which on securities markets and investor

Main risks: Summary assessment R.4

| Risk category | Summary |
|---|---|
| Liquidity risk | Liquidity risk in 2Q14 increased and looks set to increase further. Aggregate liquidity appeared ample, though its distribution was uneven across markets. Both this unevenness as well as dependence on monetary policy support are important factors in determining liquidity risk. The risks related to a snapback and subsequently arising demands from asset reallocation increased. Liquidity measured in sovereign bond markets was stable. In equity markets, a brief deterioration early in the quarter highlighted the potential for disruption. Bond market volatility remained inversely related to maturities. Market data did not indicate hedge fund liquidity concerns. |
| Market risk | Market risk was high and rising in 2Q14, notably on account of upbeat financial market sentiment moving ahead of fundamentals and potentially overly reliant on continued policy support. Revaluation risk is thus increasingly of concern. Price and quantity adjustments that would accommodate a change in the low interest rate environment and resulting dislocations could meet with bottlenecks, which would raise liquidity risk. Though aggregate equity PE ratios remained below their average, considerable heterogeneity exists across markets and MS: Valuations in some markets exceeded historical highs while current yields on bonds simultaneously remained very low. Moreover, a hunt for yield continued to compress risk premia across asset classes. Corporates relied on market finance and spreads of lower-rated corporate bonds continued to decline while high-yield issuance was solid. Where prices are fuelled by short-term and cheap credit rather than expectations about economic recovery, valuation risk would further rise. |
| Contagion risk | EU contagion risk remained broadly stable at an elevated level, though its nature shifted somewhat. The situation of smaller, more vulnerable EA sovereigns broadly improved along with another programme exit. Their yields converged and continued to approach those of core countries. On the other hand, default insurance bought against a few larger, more vulnerable sovereigns increased. Developments in Ukraine started to cause unrest in relevant market segments. EM risks remained an important consideration, including due to prevailing geopolitical risks, macroeconomic uncertainty, and related potential for destabilising capital flow reversals. |
| Credit risk | Though credit risk remained very high, structural reforms continued to yield improvements. Notwithstanding difficult macroeconomic conditions and their interaction with quantity and quality of private and public indebtedness, important measures continued to be achieved in the EU to address related risks and their potential fallout. Noteworthy are the establishment of the banking union, accelerated repayments of LTRO balances and return of several sovereigns to capital markets. Further relief is expected to come from ongoing stress tests and asset quality review in the EU banking sector. Tempering this is the accumulation of new risks on balance sheets, with high-yield debt issuance particularly strong. |

Note: Qualitative summary of assessment of main risk categories in markets under ESMA's remit.

Market functioning: Risk summary R.5

| Risk | Summary |
|---|---|
| Bench-marks | Investigations into potential benchmark manipulations are ongoing. The silver fixes soon will be discontinued. Continuity of key interest rate benchmarks remains a concern: Euribor panel banks dropped to 26. IOSCO found that administrators of key interest reference rates made significant progress in enhancing governance and accountability of their benchmarks. Continuity of design reforms and data adequacy is needed. |
| Market infra-structures | During the current quarter, no major events threatening operational stability were observed. The market structure continues to evolve, including in response to regulation. Risks related to any potential interest rate snapback are carefully monitored, including with respect to resulting liquidity constraints and collateral scarcity. |
| Shadow banking | Shadow banking liabilities declined during 2H13 and stood at EUR 8tn (19% of EU banks liabilities) in 4Q13, down EUR 730bn from 2Q13. This was mainly due to smaller repo markets. Anecdotal evidence suggests increased reliance on non-bank lending, including through shadow banking activities. As this sector becomes larger its facilitating credit growth outside of the banking sector could raise financial stability risks. |

Note: Qualitative summary of assessment of main risks to the functioning of markets under ESMA's remit.

behaviour will need to be observed with caution. Cross-regional dynamics remained complex, however, as central banks' guidance differs according to relevant developments and expectations. It will be important that market participants make pertinent use of guidance and any financing provided, in particular with respect to maturity and risk transformation.

**Sovereign-bank nexus**: Stabilising macroeconomic conditions, structural reform, and policy support contributed to improving both governments' and banks' positions. Further, the establishment of the banking union and banks' accelerated repayment of LTRO funds had a reassuring effect on markets. Improvements notwithstanding, uncertainty about banks' legacy assets remains a significant factor. Credible bank stress tests accompanied by an adequately calibrated asset quality review and suitable capital replenishment where needed are considered important next steps. In order to ensure that these broad improvements translate into a continued tempering of the risk of feedback loops, further risk diversification by investors will be valuable, including across assets and liabilities.

## Conditions in securities markets

**Risks in EU sovereign debt markets**: The broad reduction of EU sovereigns' bond yields continued, with spreads of smaller vulnerable sovereigns continuing to push multi-year lows. Important factors include the stabilising macroeconomic outlook, particularly for programme countries, accompanied by improved government deficits and external current accounts. Positive sentiment was reflected in the exit of another sovereign from its programme. Given high levels of indebtedness, structural issues, and the tepid and fragile recoveries, vulnerabilities remain significant, however.

**Market clustering:** Correlation among EU sovereign yields remained high, especially in the EA and including some newer MS. As vulnerable sovereigns clustered more closely together, the coherence with core economies increased.

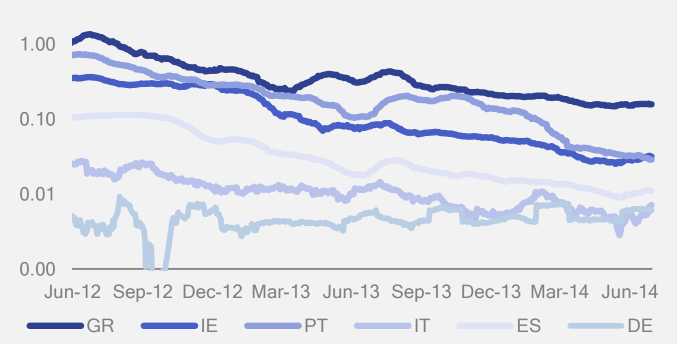
**Funding risk:** Funding risks appeared to have lessened in places, as LTRO repayments accelerated and debt maturities shortened marginally across sectors. Elevated high-yield issuance may point to future issues, however. Against a backdrop of deleveraging, with increased concentration of market making activities and increased reliance on institutional financing, a materialisation of an interest rate snapback could see bottlenecks arising with respect to asset reallocations resulting from related dislocations.

**Valuation risk:** Yields continued to compress across sectors and risk classes, as the low interest rate environment interacted with market sentiment and behaviour. These developments imply a heightened probability of a continued build-up of imbalances. The risk of a correction of valuations remains significant. For instance, asset prices are at highs, even in historical terms, across markets that would typically move in opposing directions, such as equity and bond markets. Intensified hunt-for-yield behaviour based on overly optimistic assumptions continues to be a concern and can lead to significant misallocation of capital.

**Market functioning:** Key structural issues that may become relevant to EU financial markets' stability relate to benchmarks, market infrastructures and shadow banking. For a summary risk assessment see textbox R.5.

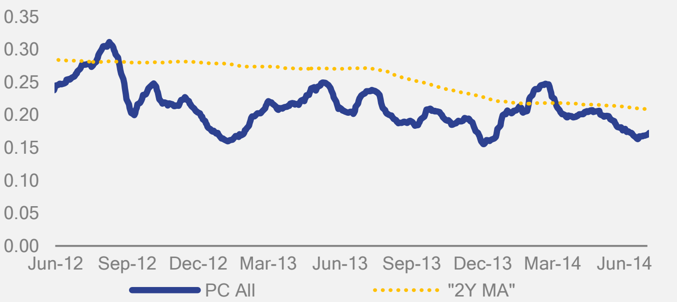
# Liquidity risk

Sovereign bid-ask spreads: Decline halted R.6



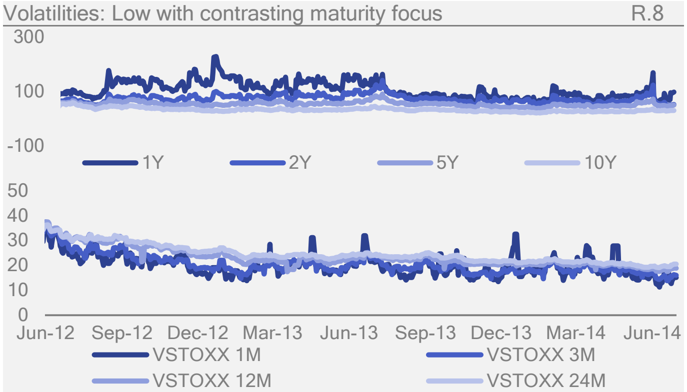

Note: 10Y EA sovereign bond bid-ask spread in percentage points; logarithmic scale, 30D moving average.
Sources: Thomson Reuters Eikon, ESMA.

Equity illiquidity index: Mild temporary deterioration R.7



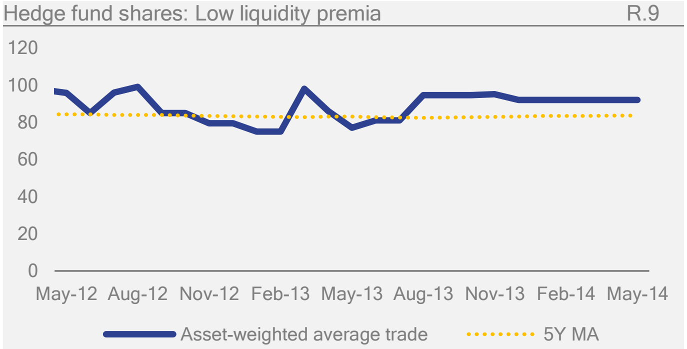

Note: Composite indicator of liquidity in the equity market for the Eurostoxx50 constituents, computed by applying the principal component methodology to six input liquidity measures (Amihud illiquidity coefficient; bid-ask spread, Hui-Heubel ratio, turnover value, inverse turnover ratio, MEC. The indicator range is between 0 (higher liquidity) and 1 (lower liquidity).
Sources: Datastream, ESMA.

Volatilities: Low with contrasting maturity focus R.8




Note: On top are 3M forward Euro-Euribor swaptions implied volatilities; below are Eurostoxx50 implied volatilities measured as indices; %.
Sources: Thomson Reuters Datastream, ESMA.

Hedge fund shares: Low liquidity premia R.9




Note: Monthly price index for HF shares traded on secondary markets. Computed as the asset-weighted average market value as a share of NAV, in %. 5Y MA plotted alongside.
Sources: Hedgebay, ESMA.

*Liquidity risk in 2Q14 increased and looks set to increase further. Aggregate liquidity appeared ample, though its distribution was uneven across markets. Both this unevenness as well as dependence on monetary policy support are important factors in determining liquidity risk. The risks related to a snapback and subsequently arising demands from asset reallocation increased. Liquidity measured in sovereign bond markets was stable. In equity markets, a brief deterioration early in the quarter highlighted the potential for disruption. Bond market volatility remained inversely related to maturities. Market data did not indicate hedge fund liquidity concerns.*

**Sovereign bond bid-ask spreads:** Bid-ask spreads were broadly stable across the EA. A degree of convergence continued, however, with those of the three largest EA sovereigns reverting back to end-2013 levels. A downward movement was particularly noticeable for one sovereign exiting an adjustment programme. Anticipation about possible policy responses to continued disinflationary trends may also have augmented liquidity. At the high-liquidity end, however, some increased volatility was recorded.

**Equity illiquidity index:** Liquidity conditions of large EU equities appeared favourable in 2Q14. The quarter commenced with the illiquidity indicator briefly breaching its two-year average, reflecting a slight tightening of conditions. This brief tightening of liquidity was similar to levels witnessed in 1H13, when concerns around potential bailout requirements in the EA were heightened. It is important to bear in mind that the indicator relates to typically highly liquid equities.

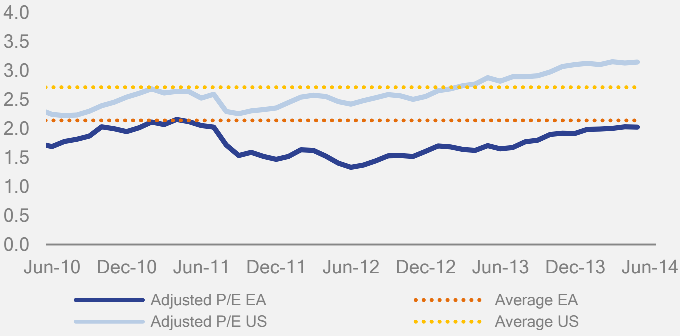
**Bond volatility:** Implied bond volatility remained fanned out evenly across the maturity spectrum, with a brief exception in June, and at levels similar to 1Q14. Volatility was considerably less settled at the shorter end of the curve, even breaching 1H13 levels early-June, around the time of monetary policy announcements. Overall, this fanned out distribution continued from end-October, signifying some heightened risk, with sensitivity particularly marked around early June.

**Equity volatility:** Implied equity volatility remained around its four-year average, trending down slightly at the longer end of the spectrum while implied volatility at the shorter end tended to oscillate just below, breaching the longer-term volatility mid-April. In June, volatilities fell markedly around the time of monetary policy announcements. Overall, this picture is consistent with a view that liquidity in equity markets currently is adequate, though reversal risk lingers.

**Hedge fund shares' liquidity premia:** The discount of hedge funds' book value to their valuation in the secondary market remained stable, consistent with relatively low liquidity concerns in this area. With average secondary market transactions trading at 92% of NAV, the discount remained marginally higher than the averages recorded since August 2013. Overall, a low discount points to somewhat lower liquidity concerns vis-à-vis hedge funds, as it signifies that traders on the secondary market require less of a liquidation premium.

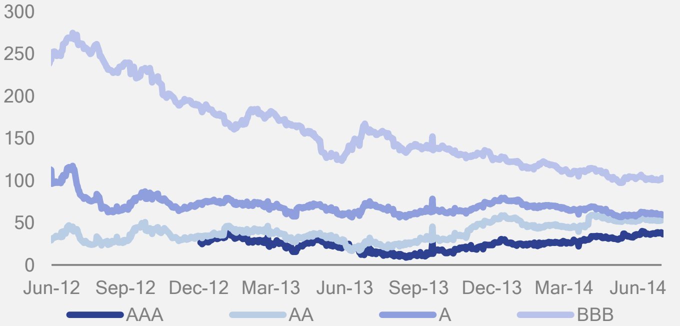
# Market risk

Adjusted equity PE ratios: EU valuations approaching average R.10



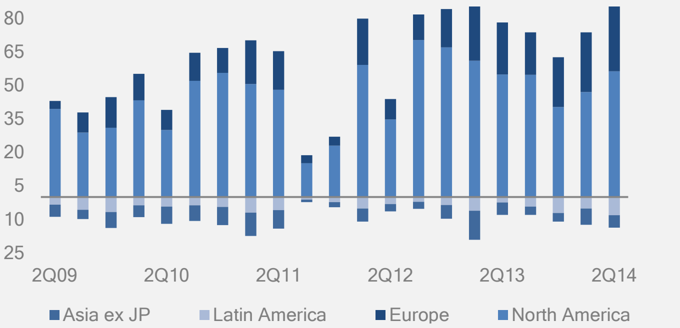

Note: Monthly earnings adjusted for trends and cyclical factors via Kalman filter methodology based on OECD leading indicators; units of standard deviation; averages computed from 8Y.
Sources: Thomson Reuters Datastream, ESMA.

Corporate bond spreads: Yield compression afoot R.11



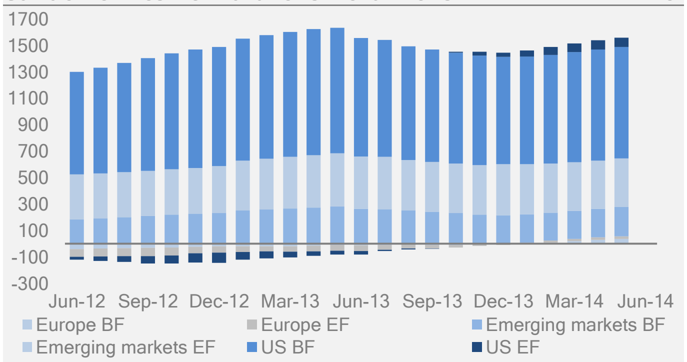

Note: Non-financial corporate bond spreads by rating grades between iBoxx non-financial corporate yields and ICAP euro euribor swap rates at maturities 5-7 years; EA, basis points. AAA-rated bonds data available since December 2012.
Sources: Thomson Reuters Datastream, ESMA.

HY issuance: Considerable activity R.12




Note: Quarterly data on high-yield corporate bond issuance by region of issue; EUR bn.
Sources: Dealogic, ESMA.

Cumulative investment fund flows: Bond inflows R.13




Note: Cumulative net flows into bond and equity funds (BF and EF) over time since 2004 by regional investment focus; USD bn. Data available until May 2014.
Sources: Thomson Reuters Lipper, ESMA

*Market risk was high and rising in 2Q14, notably on account of upbeat financial market sentiment moving ahead of fundamentals and potentially overly reliant on continued policy support. Revaluation risk is thus increasingly of concern. Price and quantity adjustments that would accommodate a change in the low interest rate environment and resulting dislocations could meet with bottlenecks, which would raise liquidity risk. Though aggregate equity PE ratios remained below their average, considerable heterogeneity exists across markets and MS: Valuations in some markets exceeded historical highs while current yields on bonds simultaneously remained very low. Moreover, a hunt for yield continued to compress risk premia across asset classes. Corporates relied on market finance and spreads of lower-rated corporate bonds continued to decline while high-yield issuance was solid. Where prices are fuelled by short-term and cheap credit rather than expectations about economic recovery, valuation risk would further rise.*

**Adjusted equity PE ratios:** Among robust corporate earnings, PE ratios in the EA continued to edge up towards their eight-year average, especially towards the end of the quarter. Valuation risks in the EU remained an important concern, however, as market confidence may be ahead of economic fundamentals and overly reliant on low interest rates. Further, differences across markets were considerable. Thus, valuation risk is more of a concern where crisis-related price corrections are no longer in evidence.

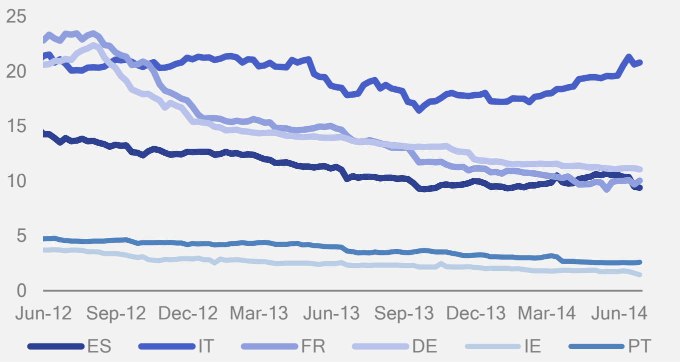
**Corporate bond spreads:** In 2Q14, non-financial corporate bond spreads continued to compress across risk categories. Yields of AAA-rated bonds increased, especially toward end-2Q14. For bonds rated below AAA, an initial reduction in yields halted in June. On the whole, yields on BBB-rated bonds fell slightly, however. Overall, these movements are consistent with a degree of convergence across risk classes. This continued a trend of broad-based yield compression since mid-2013. (The discrete jump for AA-rated related to a duration increase in the underlying basket.)

**High-yield corporate bond issuance:** In 2Q14, HY corporate bond issuance increased noticeably in the EU while being moderate in the US. In 2Q14, HY issuance was significantly higher than in the previous quarter: EUR 56.8bn compared to EUR 26.7bn in 1Q14. The level of issuance remained subdued for EM, increasing slightly in Latin America while decreasing in Asia. Such dynamics may be partly associated with a reduced risk perception. The combination of stabilised but sluggish economic environment together with the sustained low interest rate environment, however, would also incentivise investors to hunt for higher yields in order to maintain or improve their portfolio returns.

**Investment fund flows:** For all regions, flows from bond funds (BF) were positive at the beginning of 2Q14. In the EU, BF inflows continued to increase, amounting to USD 7.23bn for April and May 2014. For equity funds (EF) on the other hand, flows were negative compared to the first two months of 2014: USD -3.1bn, for April and May, versus USD 2.75bn earlier in the year. The US exhibited a similar trend with EF outflows of USD -6.8bn. For EM, the outflows through end-2013 reversed, as significant inflows were recorded especially for BF (USD 10.3bn for April and May 2014).

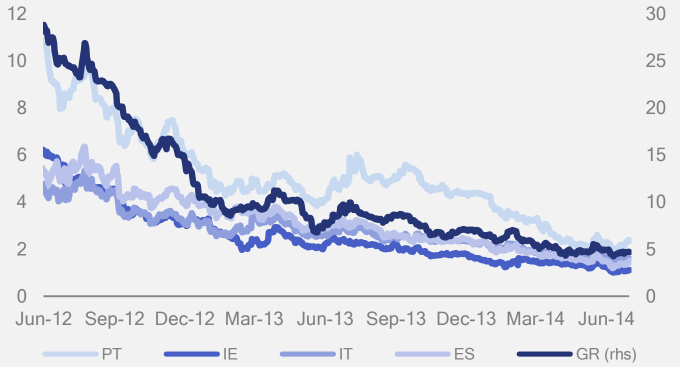
# Contagion risk

Outstanding EU sovereign CDS: Focus on large vulnerable MS R.14



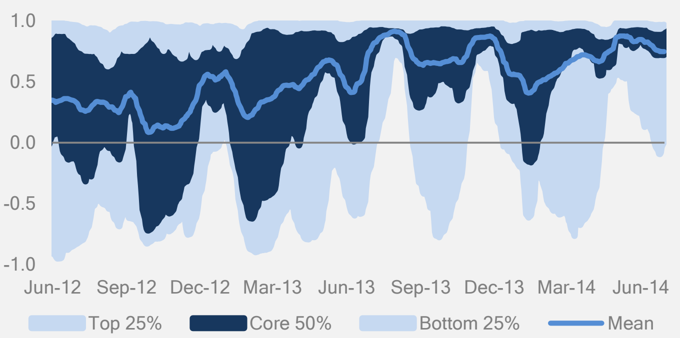

Note: Value of outstanding net notional sovereign CDS for selected countries; USD bn.
Sources: Thomson Reuters Eikon, ESMA.

Sovereign spreads: Uptick after convergence to new lows R.15



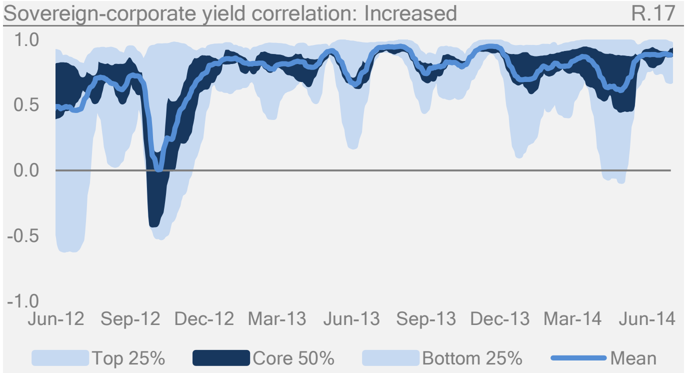

Note: Selected 10Y EA sovereign bond risk premia (vs. DE Bunds); percentage points.
Sources: Thomson Reuters Datastream, ESMA.

Sovereign yield correlation: Slight divergence outlier-driven R.16




Note: Dispersion of correlations between 10Y DE Bunds and other EU countries' sovereign bond redemption yields over 60D rolling windows.
Sources: Thomson Reuters Datastream, ESMA.

Sovereign-corporate yield correlation: Increased R.17




Note: Dispersion of correlation between Barclays Aggregate for corporate and 10Y sovereign bond redemption yields for BE, FI, FR, IT, NL.
Sources: Thomson Reuters Datastream, ESMA.

*EU contagion risk remained broadly stable at an elevated level, though its nature shifted somewhat. The situation of smaller, more vulnerable EA sovereigns broadly improved along with another programme exit. Their yields converged and continued to approach those of core countries. On the other hand, default insurance bought against a few larger, more vulnerable sovereigns increased. Developments in Ukraine started to cause unrest in relevant market segments. EM risks remained an important consideration, including due to prevailing geopolitical risks, macroeconomic uncertainty, and related potential for destabilising capital flow reversals.*

**Outstanding EU sovereign CDS**: Net volumes were stable for most MS in 2Q14, with a slight uptick registered for some in early June. While a continued increase for two larger and more vulnerable sovereigns formed part of a recent trend, in June their paths diverged. An increased amount of insurance sought against large, vulnerable MS may point to potential risks forming on the horizon, including due to macroeconomic conditions. The accelerated drop in CDS outstanding that accompanied successful exit from adjustment programmes by smaller MS slowed.

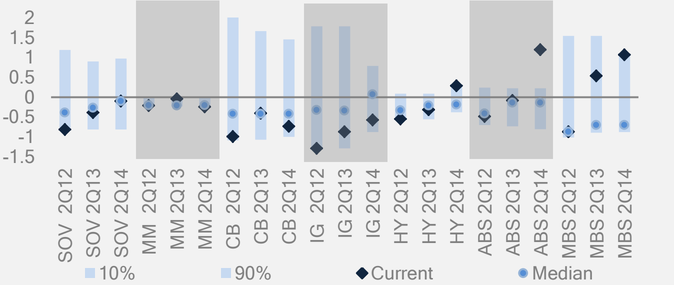
**Sovereign spreads**: Spreads of vulnerable EU sovereigns' 10Y bonds relative to Bunds generally fell, with lows recorded in early June. Within this development three movements are relevant. First, DE yields trended downward. Second, there was a degree of convergence among some smaller sovereigns as their trend decline continued. Against a background of continued international policy support, this is consistent with both a perception that reform efforts are beginning to bear fruit, thus reducing credit risk, as well as with a growing appetite for risk in a low interest rate environment. Third, spreads ticked up in June for a few larger and more vulnerable MS.

**Sovereign yield correlation**: The cohesion of movement of European sovereigns' 10Y bond yields relative to Bunds reverted back to 4Q13 highs mid-quarter, though this was partially reversed. As in June 2013, the convergence represented a wider development. An important qualitative shift was that negative correlation with rising DE 10Y yields was driven by improvements for several vulnerable sovereigns, including of several countries to the East as well as several EA sovereigns that returned to markets. Overall, this indicates that financial markets in the EA continued to stabilize. In particular, economic rebalancing achieved in MS that were buffeted by the crisis is being achieved and may even hint at some positive contagion from successful programme completion. Further, the acuteness of Ukraine crisis-related stresses abated, after having flared up in 1Q14 and having affected Central and Eastern European MS.

**Sovereign-corporate yield correlation**: Correlation between corporate bond yields and those of the sovereign of localisation stabilised at a high level. Initially they dropped to mid-2013 levels, thereafter recovering to approach end-2013 levels. Against the background of broadly declining sovereign yields, this remains consistent with risk differentiation among sovereigns and corporates.

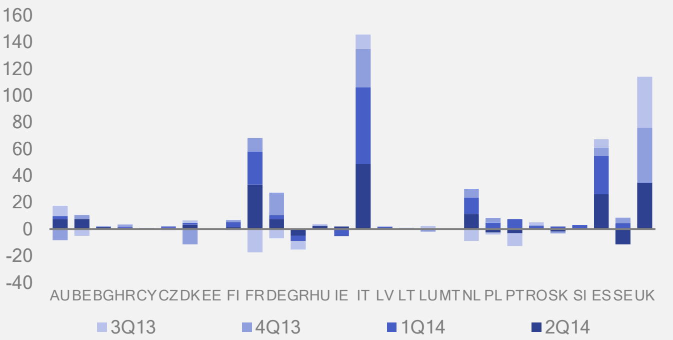
# Credit risk

Debt issuance: HY again solid as securitisation rebounded R.18



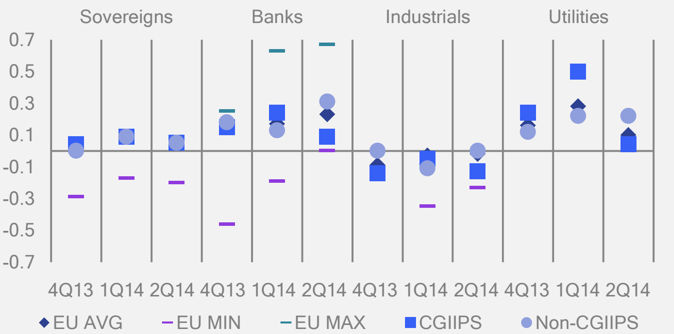

Note: Growth rates of issuance volume in per cent normalised by standard deviation for the following bond classes: sovereign (Sov); money market (MM); covered bonds (CB); investment grade (IG); high-yield (HY); asset backed securities (ABS); mortgage backed securities (MBS). Percentiles computed from 11Q rolling window. All data include securities with a maturity higher than 18M. Bars denote the range of values between the 10th and 90th percentiles.
Sources: Dealogic, ESMA.

Net sovereign debt issuance: Uneven across EU R.19



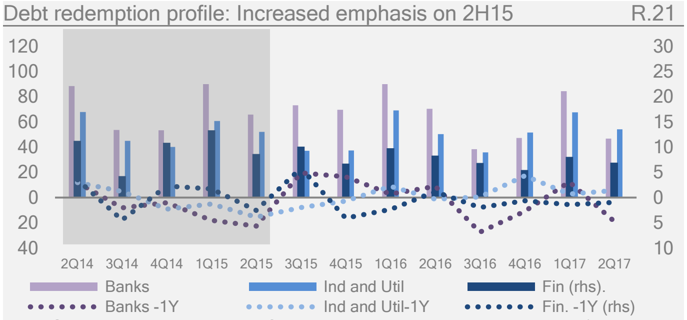

Note: Quartely net issuance of EU sovereign debt by country, EUR bn. Net issuance calculated as the difference between new issuance over the quarter and outstanding debt maturing over the quarter.
Sources: Dealogic, ESMA.

Debt maturity: Lengthening at slower pace R.20




Note: Quarterly change in maturity of outstanding debt by sector and country groups. EU, years. CGIIPS include CY, GR, IT, IE, PT and ES. Min and Max may not be displayed where they are of the scale provided in the graph.
Sources: Dealogic, ESMA.

Debt redemption profile: Increased emphasis on 2H15 R.21




Note: Quarterly redemptions over a 3Y-horizon by European private corporates (banks, non-bank financials, and industrials and utilities), current and change over 1Y, EUR bn. Excluding bank redemptions to central banks. Grey-shaded area relates to the ECB's LTRO, which expires in March 2015, and reflects additional financing needs for banks of about EUR 474.3bn.
Sources: Dealogic, ESMA.

*Though credit risk remained very high, structural reforms continued to yield improvements. Notwithstanding difficult macroeconomic conditions and their interaction with quantity and quality of private and public indebtedness, important measures continued to be achieved in the EU to address related risks and their potential fallout. Noteworthy are the establishment of the banking union, accelerated repayments of LTRO balances and return of several sovereigns to capital markets. Further relief is expected to come from ongoing stress tests and asset quality review in the EU banking sector. Tempering this is the accumulation of new risks on balance sheets, with high-yield debt issuance particularly strong.*

**Debt issuance:** In 2014, EU bond issuance decreased for covered bonds and investment grade bonds, while it was flat for sovereigns. High-yield issuance, on the other hand, continued apace. Securitisation issuance picked up strongly both for ABS and MBS, albeit from low levels. ABS issuance stood at EUR 11bn, EUR 6bn above the previous quarter. MBS issuance reached almost EUR 10bn, EUR 5bn more than in 1Q14, and was concentrated in some larger MS.

**Net sovereign debt issuance:** In 2Q14, issuance was broadly positive with some heterogeneity across sovereigns. A further stabilisation of the economic outlook across the EU together with upbeat investor sentiment continued to accommodate market access for more vulnerable sovereigns: issuance was positive, particularly for one large MS. During 1H14, three sovereigns returned to capital markets that effectively had been shut out.

**Debt maturity:** At the aggregate EU level, maturity profiles continued to lengthen across most sectors and country groupings, albeit at a slowing pace when compared with the previous quarter. This lengthening was especially pronounced for the group of more vulnerable countries. This lengthening of maturity profiles was the case for banks, sovereigns and utilities. Maturity profiles for industrials were stable for core countries and declining elsewhere. In terms of country groupings, the lengthening of maturity profiles slowed most for more vulnerable countries. In the previous quarter, the lengthening of maturity had been more even across peripheral and core countries.

**Debt redemption profile:** Corporate redemption activity remained cyclically high across sectors during 2Q14, especially for industrials and utilities. The redemption profile for banks was relatively high in 2Q14 even before considering LTRO repayments. These repayments are accelerated and in April 2014 already stood above 1Q14 repayments. As of end-June, the outstanding LTRO balance stood at EUR 490.6bn. Looking at a three-year horizon, profiles are shallower when compared to last year. This is especially so for banks, with a slight emphasis on 2H15 after the scheduled closing of the LTRO window. The profile is also shallower for industrials and utilities, though to a lesser extent. The three-year profile for financials is focused on the coming eighteen months and relatively unchanged from the previous quarter in the period thereafter.

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