

European Central Bank initiative to promote a new mechanism for issuing and distributing debt securities (EDDI) in the European Union. October 2019.

The European Central Bank (ECB) is studying the possibility of developing a new system for the issuance and distribution of debt securities in euros (EDDI, or European Distribution of Debt Instruments) in the European Union, which would be part of the Eurosystem. To this end, the ECB held a public consultation in May 2019 to ascertain the opinion of market participants and the general public about this initiative. The basis of the proposal is that in order to achieve a truly integrated financial market, the issue, negotiation and liquidation of a financial instrument should not be affected by the location of that financial instrument or of the investors that carry out the transactions on the same.

Therefore, it points out in the aforementioned document that although several initiatives have been developed in the European Union related to the liquidation of securities (among which Regulation (EU) 909/2014 on “improving securities settlement in the European Union and on central securities depositories” and the development of the TARGET2-SECURITIES settlement system), there has been no similar progress in the field of issuance and distribution of financial instruments, which in practice has resulted in the lack of harmonisation and integration of debt markets in the European Union. Consequently, according to the ECB there is currently no integrated and harmonised channel that facilitates the initial issuance and distribution of debt securities throughout this territory. On the contrary, in their opinion the issuers are forced to use different channels and procedures, whether national or international, which are neither homogeneous nor cover the European Union as a single market.

The European Securities and Markets Authority (ESMA), as reflected in the summary of conclusions¹ of the meeting of its Board of Supervisors held in July 2019, has reported on the concern of its members in this regard, of the referral of a letter on the matter to the ECB and of the assignment to ESMA’s Post-Trading Standing Committee (PTSC) to monitor developments in this area. **Analysis of the current situation**

In the ECB’s opinion, for a European entity or a third country, the current system of initial debt issuance and distribution presents several problems.

First, since there is no single issuance mechanism for the entire European market, different issuers may find it difficult, depending on their size and profile, to reach all investors in the same way. Although large issuers usually have no problem positioning themselves against all kinds of European and international investors, smaller issuers tend to have more difficulties, which puts them at a disadvantage.

Second, the current national debt distribution systems tend to favour, in their opinion, local issuers and investors over foreigners. In practice, issuers must choose between focusing on their own market through a central securities depository in their country or using the services of a central international securities depository to primarily target international investors.

Additionally, the ECB states in the consultation that, from the point of view of debt investors in euros, various factors (including their geographical location) are usually decisive in determining the efficiency and cost related to the acquisition of a certain value, which has resulted in conditions of access to different European

debt markets for investors. As a result, the ECB believes that, compared to other monetary zones in which there is an integrated issuance and distribution mechanism, such as the United States, Japan or China, the situation in the European Union seems to be at a structural disadvantage.

On the other hand, it also stands out in this document that the existence of various independent technology platforms for debt issuance, with a low level of automation and among which it is not possible to operate, is an additional problem for the creation of a genuine single market. In addition, this European institution considers that all the aforementioned factors contribute to the fragmentation of the European debt market and, therefore, affect its liquidity.

As a result of the deficiencies detected by the ECB in the euro debt market of the European Union, in the consultation it proposes several strategies to overcome them.

One of them would be to increase the levels of harmonisation of the different mechanisms for issuing and distributing debt in the European Union. The development of harmonisation initiatives similar to those of the Financial Instruments Markets Directive (MIFID II), the Market Infrastructure Regulation (EMIR) or Regulation (EU) 909/2014 mentioned above in the field of issuance and distribution of debt instruments could be a very important step towards the integration of the European debt market.

The second would be the creation of a single platform for the initial issuance and distribution of European debt. The objective of such a platform would be to provide euro issuers with access to the entire European Union market as if it were a single market, both from the point of view of the issuance of the financial instrument and the processes associated to it.

It should be noted that the initiative promoted by the ECB for the creation in the European Union of a new mechanism for issuing and distributing debt securities considers these two strategies as both complementary and necessary to overcome the deficiencies that it claims to have detected.

Possible impact of EDDI on the market

As previously mentioned, the new EDDI mechanism would consist of a centralised service that would be offered through the Eurosystem and that would cover the areas of initial issuance and distribution of euro debt in the European Union. In the ECB's opinion, since it is a new service, the introduction of EDDI could have certain consequences for the market and its members, which are briefly listed below:

- The interaction between the different market members would be facilitated

Being a centralised service, EDDI would facilitate interaction between issuers, investors, central securities depositories, agents, etc. In addition, through the centralisation of the service, it would be easier to define harmonisation standards and, above all, to ensure compliance.

- Disintermediation is not one of the objectives of EDDI

Existing intermediaries, such as issuer agents, dealer banks and custodians, could combine their own procedures with the new EDDI mechanism. For example, existing emission and distribution platforms could be connected to the EDDI component dedicated to post-trade, provided they met certain technical requirements.

- EDDI could affect the business model of central securities depositories

The issuance and distribution of securities through EDDI would only be possible through close collaboration with the central securities depositories. Currently, the business model of central securities depositories is determined by their position in the custody chain, that is, if they are positioned in it as an "issuing" or "investing" central securities depository. With EDDI, the determining differentiating factor would become the quality of the service and the price level of each of the central securities depositories. In addition, central

securities depositories would lose exclusivity over the initial registration in the registry, which until now depended on the place of issue of the security. On the other hand, with EDDI all central securities depositories would enjoy equal conditions to access the securities issued, that is, the current inequalities derived from the location of the issues would be eliminated.

- Issuers would have full choice in deciding how they prefer to use the EDDI service

Issuers would have the ability to decide certain parameters, such as issuing debt securities without specifying the place of issuance, which could contribute to increasing the attractiveness of debt issuance denominated in euros. This could in turn increase the liquidity of the securities, with the consequent benefits in terms of the credit rating of the issues and a greater ease in placing them among investors. On the other hand, since EDDI is an optional service, it is possible that some issuers are still interested in issuing securities through existing platforms. These decisions would allow issuers to have greater flexibility to adjust their strategies to their particular interests.

- Investors could benefit from the existence of a standardised communication channel

Compared to the multiplicity of platforms and communication channels that currently exist, EDDI would offer a single point of communication for all participants in the new system. On the other hand, it would no longer be necessary to connect to several central securities depositories to have access to the same value, so that investors could thus optimise the custody of their securities.

Once the responses to the public consultation carried out by the ECB have been received, the Eurosystem will evaluate the comments received and decide on the possible actions to be taken in relation to this initiative.

¹ See the main conclusions of the ESMA Board of Supervisors meeting of July 2019 on EDDI at the following link:

https://www.esma.europa.eu/sites/default/files/library/esma22-106-1895_soc_july_2019_board_of_supervisors.pdf

[Link of interest: European Central Bank's Market Consultation regarding the possible creation of a new mechanism for the issuance and distribution of debt securities \(EDDI\) in the European Union](#)