Analysis

ECB purchase programme expanded to include corporate bonds

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When the Governing Council of the ECB decided in March 2016 to increase monthly purchases under the expanded asset purchase programme (EAPP) from EUR 60 billion to EUR 80 billion, it also decided to add corporate sector bonds to the programme. Purchases under the corporate sector purchase programme (CSPP) began at the beginning of June and are intended to run – as is the whole APP – until the end of March 2017, or beyond, if necessary. The purchases are carried out by six national central banks, including the Bank of Finland, acting on behalf of the Eurosystem.



The basic principles of corporate bonds do not differ from government bonds that yield a coupon rate. Banks issue the bonds on behalf of companies, and they are also traded on the secondary markets, in the same manner as government bonds. The Eurosystem may purchase corporate bonds both on the primary and on the secondary markets.

Since the corporate bond markets are considerably smaller than the government bond markets, it requires special expertise to operate on them. For this reason, only certain Eurosystem central banks participate in implementation of the programme. In addition to the Bank of Finland, the national central banks of Germany, France, Spain, Belgium and Italy will purchase bonds of companies operating in their own country. The Bank of Finland will also purchase bonds issued by Irish, Austrian and Baltic corporations, while the Belgian central bank will operate on the Portuguese, Luxembourgian, Slovak, Slovenian, Cypriot, Maltese and Dutch markets. As many international businesses operating in different European countries issue bonds in the Netherlands, Dutch corporate bonds are allocated between the large national central banks under the CSPP mainly according to the actual location of the company.

In order to qualify for purchase under the CSPP, corporate bonds must comply with the programme's eligibility criteria, which are based on the Eurosystem's collateral framework for monetary policy operations. The bonds must be denominated in euro and have a credit assessment obtained from an external credit assessment agency of which at least one has provided the bonds an investment grade rating (equivalent to a rating of BBB-). The bonds must have a minimum remaining maturity of six months and a maximum remaining maturity of 30 years at the time of purchase.

The bond issuers must be companies operating in the euro area, but bonds of international corporations whose parent undertaking is located outside the euro area are also eligible for purchase under the CSPP. By contrast, banks and other credit institutions or companies whose parent undertaking is a credit institution are excluded from the programme. Public sector corporate bonds are also eligible for purchase under the CSPP. Limitations on these are more or less similar to those on the Eurosystem's public sector purchase programme.

The ECB Governing Council has decided that the Eurosystem may hold a maximum of 70% of bonds issued. Stricter limits apply if the undertaking is classified as a public sector corporation or a publicly owned company. In order to maintain market liquidity, national central banks participate in securities lending schemes in which corporate bonds are lent to market participants.

By September 2016, the Eurosystem's purchases of corporate bonds amounted to EUR 20.5 billion. Purchases have been targeted on a broad range of sectors and countries. However, they have been larger on the markets of countries with sizable issues, compared with countries with small corporate bond markets. Monthly purchase volumes vary, since there is monthly fluctuation in the volume of corporate bonds available on the secondary markets and because businesses do not issue bonds evenly throughout the year. Consequently, the Eurosystem's monthly purchases may be above average in months of sizable corporate bond issuance.

The CSPP complements the EAPP, which covers purchases of public sector debt securities, banks' covered bonds and asset-backed securities. The purpose of the programmes is to further enhance the transmission of monetary policy and ease borrowing conditions for businesses, contributing to a return of inflation rates to levels consistent with the objective of price stability. The announcement of the commencement of corporate sector bond purchases narrowed corporate bond spreads by 0.20 of a percentage point (Chart 1). When interest rates on corporate loans fall, companies' funding costs decrease, and thereby also their expectations of investment returns. For this reason, many solid European companies have issued bonds at negative interest rates. The CSPP is intended to encourage companies to seek market-based funding. This would stimulate euro area capital markets and offer an alternative funding channel to traditional bank financing.

Keywords

capital markets, corporate sector purchase programme (CSPP), expanded asset purchase programme (EAPP)