



EUROPEAN CENTRAL BANK

EUROSYSTEM

MONTHLY REPORT ON THE EUROSYSTEM'S COVERED BOND PURCHASE PROGRAMME

MAY 2010

From 1 May to 31 May 2010, the Eurosystem purchased eligible covered bonds with a total nominal value of €4,284 million under its covered bond purchase programme (CBPP).¹ Of this total, €294 million was accounted for by purchases in the primary market and the remaining €3,990 million by purchases in the secondary market.² The total nominal value of all covered bonds purchased by the Eurosystem since the programme was first started stood at €54,400 million on 31 May 2010.³

In comparison with the previous month, activity in the covered bond market contracted further in May, with both primary and secondary market activity strongly affected by volatile euro area sovereign debt markets.

In May activity in the primary market was limited to only three new issues and one tap issue, resulting in a total volume of new CBPP-eligible covered bonds of around €2.3 billion, with issuance activity in most euro area countries and non-euro area countries coming to a halt. The few new issues – from Germany and France – were mainly placed with domestic investors and were priced as initially foreseen. While, in previous years, May had usually been a strong month in terms of gross covered bond supply, this year activity in May was disrupted by the high degree of volatility in sovereign debt markets. The current pause in primary market activity, as well as the increase in volumes of maturing covered bonds, which will peak in June and July, may result in greater issuance activity over the next several months, depending on market conditions.

Activity in the secondary market also remained subdued in May, due to developments in the euro area government bond markets. Following

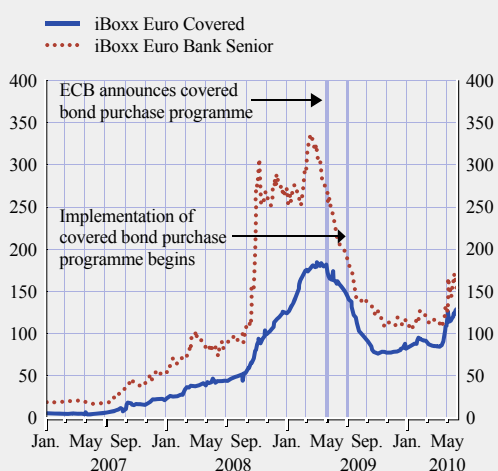
the announcement of the European financial stabilisation mechanism and the decision of the Governing Council of the European Central Bank (ECB) to conduct interventions in the euro area public and private debt securities markets (under the Securities Markets Programme), in order to ensure depth and liquidity in market segments that are dysfunctional, national covered bond markets that had been most affected by sovereign credit concerns benefited from significant spread tightening, although this lagged movements in the respective sovereign bonds. However, much of this contraction in spreads has since been reversed, and spreads of covered bonds from some jurisdictions remain above the levels that were observed at the beginning of the year, reflecting the general deterioration in euro area sovereign debt markets. Bid-offer spreads widened in May across all covered bond jurisdictions – albeit to differing degrees – with trading flows being concentrated in market segments that have remained more or less stable over time.

Overall, spreads of euro area covered bonds and senior unsecured bonds against swap rates increased significantly in May, compared with those recorded at the end of April (see the chart below), with covered bonds outperforming senior unsecured bonds.

- 1 Decision of the European Central Bank of 2 July 2009 on the implementation of the covered bond purchase programme (ECB/2009/16), available at http://www.ecb.europa.eu/ecb/legal/pdf/l_17520090704en00180019.pdf.
- 2 These figures include transactions concluded but not yet settled during the period from 1 May to 31 May 2010. The total amount of purchases settled on or before 31 May 2010 provided €4,527 million of liquidity in the money market, according to the ECB's liquidity analysis.
- 3 Over the last three months the Eurosystem has also lent some of the covered bonds held in its CBPP portfolio, responding to demand from Eurosystem counterparties wishing to borrow such covered bonds.

iBoxx spreads against swaps

(basis points)



Source: Markit.

Following its decisions of 7 May 2009 and 4 June 2009 to purchase euro-denominated covered bonds issued in the euro area, the Governing Council of the ECB confirmed today that, until further notice, all purchased covered bonds within the CBPP portfolio will be held until maturity.

GLOSSARY OF TECHNICAL TERMS AND EXPRESSIONS

Bid-offer spread: the difference between the price or yield at which a market-maker is willing to buy a given asset and that at which he is willing to sell it.

Covered bond spread: the spread between the yield of a covered bond and the rate quoted for a euro interest rate swap contract with a similar maturity date.

Cover pool: a set of collateral on which the investor in a covered bond has a prior claim in the event of the failure of the issuer of the covered bond.

Eligible covered bond: a covered bond that fulfils the conditions specified in the Decision of the European Central Bank of 2 July 2009 on the implementation of the covered bond purchase programme (ECB/2009/16).

iBoxx indices: commonly used indices that track the movement of spreads in several bond markets versus interest swap rates. They are compiled by a subsidiary of the financial information services company Markit. The iBoxx Euro Covered index is an indicator of the difference in the yield on a basket of euro-denominated covered bonds and interest rate swaps with a similar maturity, while the iBoxx Euro Bank Senior index is an indicator of the difference in the yield on a basket of senior unsecured bank bonds and interest rate swaps with a similar maturity. The iBoxx Euro Other Sub-Sovereigns Guaranteed Financials index is an indicator of the difference between the yield on a basket of euro-denominated bank bonds with a government guarantee and interest rate swaps with a similar maturity.

Inaugural covered bond: the first covered bond ever to be issued by an institution.

Interest rate swap: a contract between two parties to exchange one stream of interest payments for another, over a set period of time. The most commonly traded and most

liquid interest rate swaps are contracts under which parties exchange fixed-rate payments for floating-rate payments based on the LIBOR or EURIBOR, the interest rate at which a prime bank is willing to lend short-term funds to another prime bank.

Senior unsecured bank bond: a bond that is issued by a bank, is not secured by a cover pool, but represents a claim on the issuer's assets and income that is prior or superior to the junior bonds issued by the same entity.

Tap: the reopening of an existing bond that allows the issue size to be increased, thereby potentially improving the secondary market liquidity on that bond.

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