EUROBOND ISSUE ON INTERNATIONAL CAPITAL MARKET: PRINCIPILES AND CHALLENGES

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ABSTRACT. Many start-up issuers have either graduated or are about to graduate from low-income country status and transfer to the category of middle-income countries and, as a result, there are reductions in available multilateral concessional funds. Therefore, the growing financing needs for many start-up issuers, together with reduced access to concessional financing, relatively underdeveloped domestic markets and a favorable interest rate environment have made international bonds an attractive financing alternative. The issuance of global bonds allows these issuers to diversify their investor base and exploit fewer credit constraints in a more liquid global bond market. Moreover, by issuing bonds in any of the currencies with the lowest cost of capital, start-up issuers are able to reduce the costs of borrowing by not assuming a significant impairment of the currency over the maturity of the bond.

KEYWORDS: *EUROBOND, debt, international financing, interest rate*

Introduction

What is a Eurobond?

The term **"Eurobond"** applies to all international trade finance through bond issues. The term Eurobond generally refers to a bond that is listed, traded and settled in the European Union (in addition to the EU's domestic government bonds). For example, it may be listed in Luxembourg and issued in accordance with United Kingdom law. However, the Eurobond does not necessarily indicate that the currency of this bond is the euro. In fact, bonds can be denominated in any currency. [3]

A Eurobond is a debt instrument denominated in a currency other than the currency of the country or market in which it is issued. Eurobonds are often grouped according to the currency in which they are denominated, such as Eurodollar or Euro-yen bonds. Due to the fact that Eurobonds are issued in a foreign currency, they are often called external bonds. Eurobonds are important because they help organizations raise capital while having the flexibility to issue them in another currency. [4]

In the Republic of Moldova, the provisions of Law no. 419 of 22.12.2006 on public sector debt, state guarantees and state on-lending, explain the notion of **securities issued on the foreign market** as an instrument of state debt issued on the foreign market in the form of negotiable financial security. [5]

One of the main reasons why start-up issuers have exploited international capital markets has been to collect resources, which are not available in local markets, to finance infrastructure projects.

Given the lack of funding in local markets in the amount needed to cover the costs of large infrastructure projects, many countries have had to turn to international markets. This was the case for most African broadcasters, such as Zambia and Senegal, but also for some Latin Americans, such as Paraguay and Bolivia. [2]

Some start-up issuers have issued international bonds to help finance the budget deficit, repay arrears or create a benchmark for the corporate sector. Some countries intended to use at least part of the proceeds for budgetary purposes or, as in the case of Honduras, to cover arrears. International bonds have also been issued as part of the debt restructuring process, such as Seychelles (2010) and Gabon (2007). Others, such as Nigeria, wanted to create benchmarks for the corporate sector. Bolivia, for example, has explicitly acknowledged in its interaction with market participants that it intends to use the new international bond to attract the attention of international investors in the country. [2]

Methods applied. The achievement of the objectives of this analysis was possible due to the selection of the theoretical and empirical methods of research: the analysis and the synthesis, the content analysis, the comparative study. A comparative analysis of the financial aspects and costs of issuing an Eurobond on international financial market by a list of countries such as: Armenia, Albania, Georgia, Macedonia, Montenegro, Tadjikistan, Ukraine, Romania and Moldova, was made based on the examination of the data provided by *Bloomberg*. Their cognitive potential allowed to research and identify the process of a first-time possible EUROBOND issuing on international financial market by the Rep. of Moldova and in comparison with other countries such as: Tadjikistan and Montenegro, to explain the main principles, challenges, positive and negative results in this regard.

Research results

Table no.1 Advantages / disadvantages of financing on the international capital market (Eurobond), maturity 5-15 years

Advantages	Disadvantages
Less dependence on internal funding sources	The discipline imposed by the international capital market may seem restrictive
Lack of conditionality	Currency risk, during the depreciation of the national currency, given the fact that the Eurobond is issued in a foreign currency
Signal of the "power of the country"	The risk of refinancing at maturity, given that Eurobond involves the repayment of the basic amount, usually in a single payment at the end of maturity
Reducing the risk of refinancing due to longer maturities	It involves long-term obligations. For the repayment of the first Eurobond there is a need to issue other international bonds
Large volume of financial resources in a single issue	Regular presentation of information to investors, monitoring of the international capital market
Execution of the show in a very fast time (2-3 months)	Additional fees related to the issue
Interest rate related to international issuance lower than interest rate related to domestic financing sources	The holding cost for Eurobonds issued in large volumes

Source: elaborated by the author [3]

The main benefit of issuing international bonds is to increase domestic savings. When a bond issue is undertaken in the context of a sustainable fiscal framework, it can significantly improve a country's available resources and therefore the sustainable prospects for growth and prosperity. Other benefits of issuing international bonds are: (i) the additional incentive to increase macroeconomic discipline and advance structural reforms as a result of intense control of the domestic economy by participants in the international market; (ii) establishing the sovereign's presence in international capital markets, which could also allow local corporations to access international markets in the future; and (iii) the substantial expansion of the country's investor base.

However, the issuance of international bonds also involves many risks. The key challenge for all sovereign bond issuers, including start-up issuers, is to maintain sound macroeconomic policies, in particular fiscal sustainability. This is necessary to ensure sovereign creditworthiness, as the confidence of international investors in many low- and middle-income countries is often fragile and quickly reversible. Other risks include the sovereign's exposure to foreign exchange risk as a result of the issuance of the international bond in a foreign currency, possible refinancing needs - especially during periods of strict international financial liquidity - and negative shocks to trading conditions. [1]

Although this financing alternative has the potential to allow countries to finance infrastructure and other urgent needs earlier, these risks stem mainly from the fact that such an issue represents an increase in external government debt and a higher share of GDP for many of these issuers and also a significant proportion for debt that is concentrated in a single instrument. These risks include concerns about debt sustainability, excessive exposure to currency risk and increased vulnerabilities in the debt redemption profile, given the repayment of a significant amount at a given time.

Some of the vulnerabilities have already manifested themselves during the crisis. For example, Seychelles matured a $230 million Eurobond in October 2008. Following a sharp decline in tourism revenues during the global financial crisis and years of excess government spending, the inability to repay the Eurobond at maturity. implicitly leading to debt restructuring and optimizing government spending.

Moreover, political instability in some countries poses an additional risk to debtors and creditors alike. [2]

Internally, most "start-up issuing" countries are to meet a number of preconditions considered necessary to attract investors in the first international issue before the issue. These preconditions have allowed most of them to obtain the best possible credit ratings, including:

- Creating a record of good economic performance in previous years, maintaining a positive medium-term outlook and demonstrating that the initial problems were part of their debt management framework and did not distort fiscal sustainability;
- Maintaining strong economic growth, keeping inflation under control and ensuring that the external current account deficit has been financed without difficulty;
- Adopt prudent fiscal policies and service existing public debt without any difficulty. In some countries, public debt has been reduced to sustainable levels as a result of substantial debt relief packages;
- Progress in data provision, transparency in the development of their macroeconomic policies and in the implementation of structural reforms; and
- Political situation to support and pursue appropriate economic policies. [1]

The country's macroeconomic bases, fiscal and external sustainability, financial depth and good institutions directly affect the performance of government bonds. Low inflation, coupled with prudent monetary policy and robust economic growth are expected to boost investor confidence and lower interest rates. A better fiscal policy (higher fiscal balances and lower debt-to-GDP levels) is expected to lower issuance costs.

If we were to examine the Republic of Moldova from the perspective of issuing a Eurobond, we could refer to the Memorandum of Economic and Financial Policies approved in the first quarter of 2020 by the IMF, which certifies the following:

- Through the implementation of the reform program, supported by the IMF, the Republic of Moldova has managed to restore macro-financial stability, revive the pace of economic growth and improve governance in the financial sector. In this regard, decisive steps shall be taken to complete the reform agenda set out in this Memorandum for the remaining period of implementation of the current program. Despite the change of governments in 2019, the program continues to enjoy strong and comprehensive political support.
- Economic growth was better than expected.
- In 2019, the budget balance was below the limits set in the program and the reforms in the banking sector are fruitful. [8]

In the process of issuing a Eurobond, it is also necessary for the sovereign to examine and decide on the specific strategic considerations of an initial bond issue on the international capital market, including volume, maturity, choice of fixed interest rate or flexible and currency. In addition, managerial issues, including the choice of legal and financial advisers, underwriters and issuing capacities, were crucial in deciding on the first issue of an international bond on the international financial market. [1]

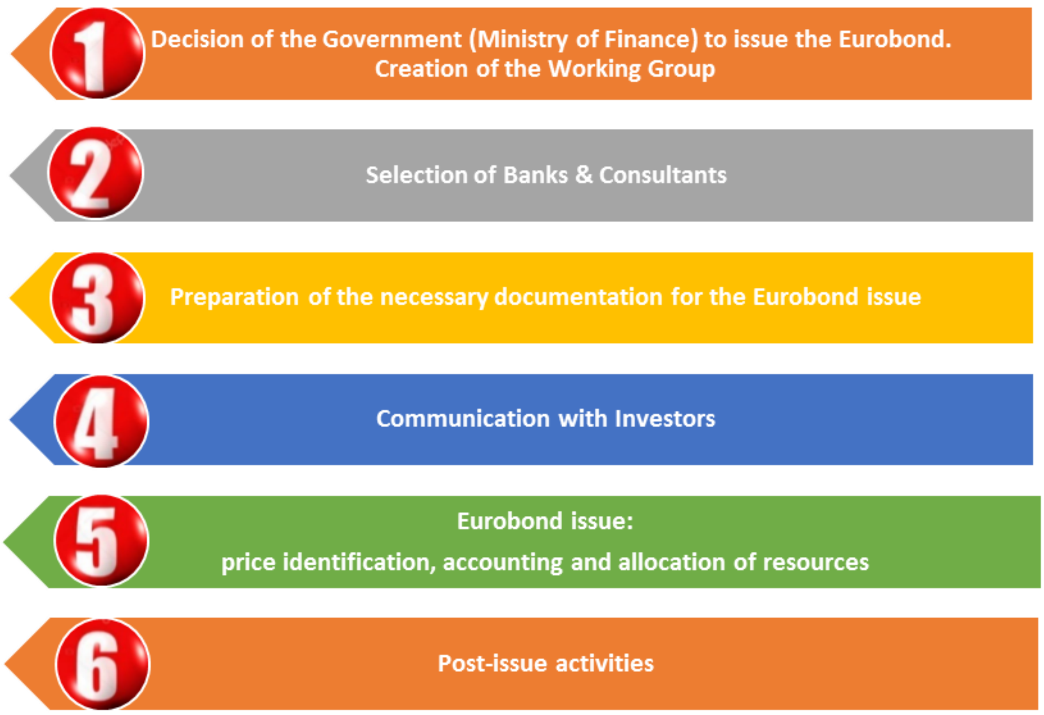

Figure 1 Stages of issuing a Eurobond on the international capital market

Source: elaborated by the author [3]

In order to successfully place debut bonds on international capital markets, sovereigns must pay due attention to the following considerations:

• **The volume of the debut bond**. The size should be determined when conducting the debt sustainability analysis (DSA) exercise for the country. Sovereigns should also not place larger volume bonds than required to cover liquidity shortfalls. Higher bond issues involve higher costs and higher foreign exchange and redemption risks.

• **Use of resources from the issue of debut bonds**. The purpose of the intended use of bond proceeds should be publicly announced, especially if the purpose of the bond issue is to finance infrastructure projects or to repurchase costly government debt. In general, investors tend to offer better conditions for such bond issues.

• **Maturity or repayment structure of the debut bond**. Maturity or maturity and repayment structure should be decided at the initial stage so that refinancing risks are kept to a minimum. Small countries and start-up issuers may also consider a bond amortization structure (multiple payments), rather than a bullet bond (single payment), to ensure a more refined debt repayment profile.

• **The currency of the bond issued**. In recent years, US dollar bond issues have been placed more easily, as US dollar fixed income markets are the deepest and most liquid.

• **Implications for the management of assets and liabilities** as a result of the issuance of the debut bond. An international bond issue should be valued in terms of its implications for the country's balance sheet assets and liabilities and should generally be in line with the country's asset and liability management objectives.

• **The jurisdiction and legal framework** that will govern the obligation to start. The issuer is to decide on the legal jurisdiction in which the bond obligation will be issued mainly on the basis of the investor's target base and currency.

• Sovereigns should pay particular attention to establishing **strong investor relations and creating demand** in the international capital market long before the issue. This may involve the appropriate introduction of the country to international investors through pre-transaction programs ("road-shows") and obtaining a credit rating, preferably from several rating agencies.

• **Selection of financial and legal advisers.** In designing and executing debut issues, sovereigns must hire financial and legal advisers from the earliest stages. Financial advisers help sovereigns obtain a credit rating and prepare economic and financial reports, while legal advisers help them with legal issues (e.g., the laws that will govern the bond, the type of bond (e.g., global bonds, or Eurobond) and the necessary documentation in this regard, reputation and experience should matter most for their selection.

• **Hiring a manager/expert (or managers)**. Issuing managers should be selected independently of financial advisors and should primarily assist start-up sovereign issuers. In principle, senior managers should be hired after decisions have been made on the level of debt and the core issuance strategy. Lead managers should also be chosen competitively on the basis of the services they will provide to the issuer, for example, the marketing and distribution of start-up bonds and the commitment to provide post-issue market support. [1]

Table no. 2 Estimated costs per category related to the issuance of a Eurobond (eg volume 750.0 million US dollars, maturity 10 years)

Eurobond	Amount (US dollars)
Issue price (6.15% yield)	**748 612 500**
Fees and charges:	
Leaders managers	1 125 000
Independent expert	150 000
Legal consultant	250 000
Eurobond rating assessment	750 000
Rating evaluation consultant	40 000
Placement on the international capital market	35 000
Total Commissions and expenses	**2 350 000**

Source: elaborated by the author [3]

In international capital markets, there are three key categories of participants in an international bond issue transaction (Eurobond): **issuers, intermediaries (banks, unions) and investors**. [3]

The structure of the bond refers to the characteristics and format of the bond documentation (eg, currency, maturity (the most popular maturity being 7-15 years), the type of interest rate (floating, fixed, indexed) and redemption (bullet or amortization)). In addition, the size of the issue is crucial. [3]

Table no.3 Yield, margin, coupon and issue price

Eurobond Maturity (10 years)	Quotes
US treasury bond 10 years	2,85%
Swap margin	10 p.p.
Swap yield (a)	2,95%
Margin for the country (b)	320 p.p.
Offer yield (c%=a+b/100)	6,15%
Semi-annual coupon	6 1/8%
Issue price	99,815

Source: elaborated by the author [3]

Although the volume of initial bonds varies widely for start-up issuers, other features of debut bonds tend to be similar. Most sovereigns in middle-income countries have issued international bonds of at least US $ 500 million, the minimum volume for a bond to be included in a bond index (eg JP Morgan EMBI Global). [1]

Access to international markets depends on perceived credit risk, often measured by a country's credit rating. An international rating of B- is generally considered the minimum for issuance on international capital markets. [3] Most of the bonds were bullet-type securities with a fixed coupon, in US dollars, with a maturity of between 5 and 10 years and a "sub-investment" country rating. While governments have more control over the structure of their domestic debt, the characteristics of instruments issued in the external market are largely defined by the practices established by the international financial centers. Debt issued on the external market tends to be medium or long term, with a fixed rate and expressed in foreign currencies (USD or EUR). [2]

Moody's			
Aaa			
Aa1			
Aa2			
Aa3			
A1			
A2			
A3			
Baa1			
Baa2			
Baa3	ROMANIA		
Ba1			
Ba2	GEORGIA		
Ba3	ARMENIA	MACEDONIA	UZBEKISTAN
B1	ALBANIA	MONTENEGRU	
B2	UKRAINE		
B3	TADJIKISTAN	MOLDOVA	
Caa			
Ca			

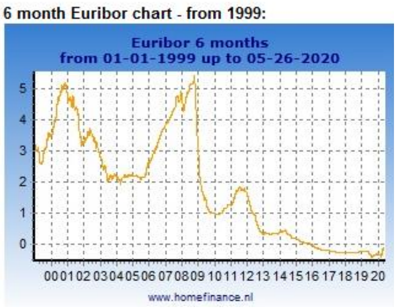

Figure 2. Rating given by the international company "Moody`s", evolution of Euribor6M, Libor6M quotes

Source: [bloomberg[6], www.homefinance.nl[7]]

According to the figure 2, it is concluded that the Republic of Moldova is in the same country risk category in which Tajikistan or Ukraine is found, and close to the country risk category in which Albania and Montenegro are found. Given that country risk is included in the costs of issuing government bonds on the foreign market through the "margin" of this instrument, it is possible to estimate the potential margin and interest rate (coupon) of a potential „Eurobond " issued by the Republic of Moldova. It is assumed that for the Republic of Moldova, the margin and interest rate (coupon) related to a "Eurobond" would be approximately the same quotations related to the bond issued on the foreign market by the government of Tajikistan or Ukraine, or higher in the case of Albania or Montenegro. Respectively, obtaining a better country rating is imperative in this regard for assessing and reducing the costs of issuing and servicing a Eurobond issued by the Republic of Moldova on the foreign market.

Table no. 4 Number of active bonds (Eurobond)

Maturity	Albania	Armenia	Georgia	Macedonia	Moldova	Montenegro	Tadjikistan	Ukraine	Uzbekistan
Total	**2**	**4**	**2**	**4**	**0**	**4**	**2**	**34**	**4**
2040								2	
2039									
2038									
2037									
2036									
2035									
2034									
2033									
2032								2	
2031									
2030								2	
2029		2				2			2
2028								2	
2027							2	2	
2026								4	
2025	2	2		2		2		3	
2024								4	2
2023								3	
2022								2	
2021			2	2				3	
2020								5	

Source: bloomberg [6]

According to the table presented (no.6), we attest an active performance of Ukraine's current presence on the foreign financial market. Moldova is being the country with approx. the same country rating as Ukraine, close geographical and economic view. Respectively, for an assessment of the current situation, Ukraine is a good example for the Republic of Moldova to examine. At the same time, the quotations of Eurobond issued by Tajikistan, Albania and Montenegro, which are equally active on the international capital market, are also to be taken into account.

Table no.5 Characteristics of the last Eurobonds issued by other countries

	Year of issue	Maturity	Volume (mln)	Currency	Price	Coupon rate (%, annual)	Moody's
Albania	2018	2025	500	EUR	99.695	3.50	B1
Armenia	2019	2029	500	USD	97.976	3.95	Ba3
Georgia	2011	2021	500	USD	98.233	6.88	Ba2
Macedonia	2018	2025	500	EUR	98.442	2.75	Ba3
Montenegro	2019	2029	500	EUR	97.846	2.55	B1
Romania	2020	2050	1600	EUR	99.702	3.38	Baa3
Tadjikistan	2017	2027	500	USD	100	7.13	B3
Ukraine	2017	2032	3000	USD	100	7.38	B2
Uzbekistan	2019	2024	500	USD	100	4.75	Ba3

Source: bloomberg[6]

Considering the group of countries assessed above as being the closest to the Republic of Moldova, the following notes may be observed. In 2017, Tajikistan issued a Eurobond in the amount of 500.0 million US dollars, with a maturity of 10 years, at a price of 100, with a fixed coupon (annual interest rate) of 7.13%. Ukraine issued a Eurobond in the same year in the amount of 3 000.0 million US dollars, with a maturity of 15 years, at a price of 100, with a fixed coupon (annual interest rate) of 7.38%. In 2018, Albania issued a Eurobond in the amount of 500.0 million euros, with a maturity of 7 years, at a price of 99.7, with a fixed coupon (annual interest rate) of 3.5%. Likewise, Montenegro, in 2019, issued a Eurobond in the amount of EUR 500.0 million, with a maturity of 10 years, at a price of 97.8, with a fixed coupon (annual interest rate) of 2.55%. In this sense, it is pointed out that the bonds issued by Albania and Montenegro are at a lower coupon (lower annual interest rate) compared to those issued by Tajikistan and Ukraine, have different maturities, a better country rating, a lower issue price, and are issued in euro, EURIBOR quotations on the international market being negative (see figure no.2).

Table no.6 Eurobond issued by Tajikistan and Montenegro, maturity - 10 years

Scenario	Volume (mln)	Currency	Price	Coupon rate (%, annual)	Type	Debt service expenditure, (annual, mln)*	Debt service expenditure, (annual, mln, MDL)**
Montenegro	500	EUR	97.846	2.55%	fixed	11.6	222.7
Tadjikistan	500	USD	100	7.13%	fixed	35.7	625.6
			Difference				-402.9
Montenegro	500	EUR	100	2.80%	fixed	12.7	244.6
			Difference				-381.1

* For Montenegro, an USD equivalent was used

** NBM exchange rate at 11.02.2020

Source: elaborated by the author

According to the table no.6, the attention is drawn to the fact that Tajikistan issued the Eurobond at a price of 100.0 (par value), while Montenegro - at a price of 97,846 (at a discount). Therefore, using the formula for calculating the price of a bond, we may estimate that if Montenegro had issued the same Eurobond at the price of 100.0 (par value), then the coupon (fixed interest rate) would have been higher and would have constituted approx. 2.80% per annum. At the same time, it is assumed that the fixed coupon (annual interest rate) would have been higher if Montenegro had been assessed with the same country rating as Tajikistan, which is included in the risk margin (component of the interest rate). In both cases, we could find that the bonds issued on the international financial market in US dollar are currently more expensive in terms of their service than those issued in euro, the cause being the negative quotations of EURIBOR in that period.

Taking into account the aspects mentioned above (volume, maturity, country rating, issue price, macroeconomic situation) it is estimated that if the Republic of Moldova issued a Eurobond on the international market in the amount of 500.0 million in euro, with a maturity of 10 years, at a price close to par value, the fixed coupon (fixed annual interest rate) (debt service expenses) would be in the current financial conditions in the range of 4.0-4.5% annually.

Conclusions

• In the light of recent experience, countries considering an international bond issue should carefully consider the associated benefits and risks and prepare well before attempting to raise funds in international markets.

• Governments should plan their actions over a period of time that extends beyond the market access stage and consider bond issuance in a broader, medium-term debt sustainability framework.

• In addition, if the start-up issuer wants to establish its presence on international markets or create a sovereign benchmark, it should opt for the issuance of a bond with features that ensure a large investor base, liquidity in the secondary market and, if possibly including at least one of the major bond indices used by investors and asset managers. [1]

• International issuance needs to be placed in a broader debt management/DSA context. Countries should avoid exploiting international markets on the basis of opportunistic views.

• Countries need to start preparing in advance for the redemption of these instruments. Refinancing risks occur at maturity, when the first bonds begin to mature and could end up in an environment with much higher interest rates.

• Finally, countries must pay attention to the best principles in the operational stages of issuing debut bonds. These operational steps (managers, experts, consultants, existing procedures) are important to avoid excessive costs. [2]

Regarding the Republic of Moldova, the following is concluded:

• In the current conditions, the Republic of Moldova has managed to restore macro-financial stability, revive the pace of economic growth and improve governance in the financial sector.

• the bonds issued on the foreign financial market in US dollar currency are currently more expensive in terms of their service than those issued in euro, due to the negative quotations of EURIBOR in that period.

• if the Republic of Moldova initiated the issuance of a Eurobond on the international capital market in a volume of approx. 500.0 million euros, maturity - 10 years, at an issue price close to par value, the fixed coupon (annual interest rate) would be estimated in the quotation range 4.0-4.5% annually.

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