OMFIF.ORG – 27 GENNAIO 2026

Why euro area bond markets are quietly repricing risk

di Edoardo Reviglio

Investors are facing the market with more confidence

Euro area government bond markets are delivering a signal that would have appeared unlikely only a few years ago. Yield spreads across major sovereign issuers are narrowing again, not because investors have become complacent, but because the institutional and economic framework of the monetary union has evolved.

Over the past year, Italian and Spanish bonds have outperformed much of the traditional core. Ten-year Italian yields have traded in a range of roughly 130–150 basis points above German Bunds, among the lowest levels seen since the introduction of the euro. Spanish yields have at times traded below those of France. These developments are not isolated technical movements. They reflect a broader reassessment of relative risk within the euro area.

The contrast with the post-2008 period is stark. During the 2012 sovereign debt crisis, markets amplified divergence, pricing fragmentation and redenomination risk with growing intensity. Today, those tail risks are far less prominent. The European Central Bank has been central to this shift. Through successive intervention frameworks, it has reshaped expectations about how far spreads can widen before policy reacts. Even in the absence of net asset purchases, the ECB's role as a backstop continues to influence market behaviour.

This renewed convergence is also taking place under very different financial conditions from those that prevailed before the crisis. Nominal yields are higher than in the years of ultra-low rates, but real borrowing costs remain compressed by historical standards. Longer debt maturities, a higher share of fixed-rate issuance and more anchored inflation expectations have reduced refinancing risk across much of the euro area.

Markets appear increasingly willing to look beyond headline debt ratios towards broader assessments of sustainability.

Investors are more willing to diversify

Germany remains the euro area's benchmark issuer. The Bund continues to function as the risk-free reference asset and a privileged form of collateral. There is no serious reassessment of German creditworthiness. Yet the behaviour of Bunds has changed. As macroeconomic uncertainty has eased, inflation expectations have become more stable and the ECB has moved away from an aggressively restrictive stance, demand for Bunds as the sole refuge has softened. Investors are showing greater willingness to diversify within the euro-area core.

This shift does not reflect a loss of confidence in Germany, but a more nuanced reading of its outlook. Weak growth, delays in public investment, domestic political fragmentation and the transition away from a rigid application of the constitutional debt brake have introduced uncertainty over Germany's future fiscal stance. An export-led and energy-dependent growth model, once a clear source of strength, has become harder to sustain in a more fragmented and volatile global economy.

These factors do not imply higher default risk, nor do they seriously challenge Germany's status as a safe asset. They do, however, marginally reduce the institutional premium that Bunds have traditionally enjoyed.

France faces a different set of pressures. Public debt remains above 110% of gross domestic product, fiscal deficits are persistent and political fragmentation has reduced visibility on consolidation and reform. These tensions have surfaced in bond markets. The assumption that French debt automatically belongs at the heart of the euro-area core is no longer unquestioned.

By contrast, Italy and Spain have benefitted from a period of relative stability. Italy's public debt remains high, but its trajectory has stabilised. Debt maturities are long, refinancing risks are contained and interest expenditure has remained manageable. Fiscal policy has been tighter than many investors once assumed. Spain's performance has been more striking still. Strong domestic demand, labour-market resilience and effective use of European Union recovery funds have underpinned growth that outpaces most large euro-area economies. Markets have responded accordingly.

EU issuance is growing

Alongside national issuers, the rise of EU bonds is adding a further layer to the market. EU issuance remains smaller than that of major sovereigns, but it is becoming more regular, more liquid and more familiar to global investors. As the supply of highly rated euro-denominated paper increases, the Bund's scarcity value naturally diminishes, even as it retains its role as the system's most liquid reference asset.

What is emerging is not a return to the pre-crisis world, nor a disappearance of spreads. Rather, it is a more differentiated and less fear-driven pricing of risk. Markets are responding not only to macroeconomic indicators, but also to institutional credibility and political stability. Italy and Spain are increasingly perceived as offering policy continuity within a strong European framework. France and Germany face more visible political and structural constraints.

The euro area has not eliminated risk. But it has learned to manage it more effectively. The current convergence in sovereign bond markets reflects greater confidence in the system's capacity to absorb shocks without fragmenting. For investors, the message is clear: spreads still matter, but they are being priced with greater discrimination – and less anxiety – than in the past.

Edoardo Reviglio is Professor of Economics at LUISS Guido Carli and Member of the OMFIF Advisory Council.