

11 March 2019 /// n°8-2019

The ECB's permanent easing

Key Points

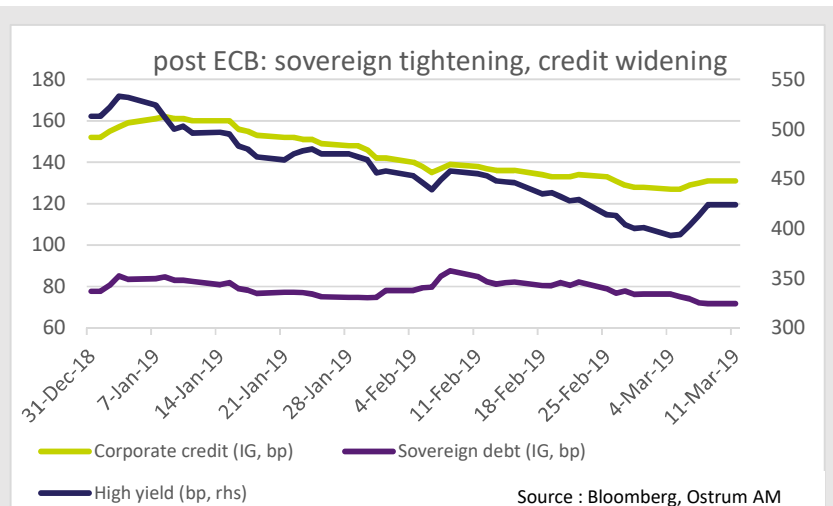
- Draghi cuts forecasts, keeps policy easy
- Bund yields under 0.10%, the euro falls further
- Euro area: sovereign debt outperforms credit
- US equities fell 2% last week as job data disappoints
- Brexit: postponement increasingly likely

The ECB revised down its forecasts and eased monetary policy. Euro area sovereign bonds benefited from the decision, so that bund yields now trade below the 0.10% mark. All sovereign spreads have narrowed. Italian BTPs trade within 250bp vs. Bunds. The impact of ECB easing was less favourable in credit space, in particular on financials. High yield widened noticeably (+23bp) and European stocks fell 1% despite support from a weaker euro. In the US, disappointing February job numbers have amplified the bid for safety. The yield on US 10-year note hovers about 2.65% ahead of the FOMC meeting scheduled next week. Equities have

undergone a 2% weekly pullback for the first time this year. The S&P index is still up some 9% in 2019. The dollar strengthened to the detriment of some asset classes including emerging bonds. The retracement of emerging spreads suggest profit-taking was overdue after a strong start of the year amid renewed protectionist threats.

A new round of Brexit-related votes in UK parliament is scheduled this week. This will be more of the same in all likelihood. Uncertainty does benefit Gilts which trade below the 1.20% mark.

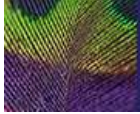
Chart of the week



Monetary easing announced by the ECB on Thursday 7 March has had differentiated impacts on asset classes.

After the ECB decision, sovereign spreads (-4bp) have outperformed to the detriment of euro IG credit (+2bp) and, even more so, equities and high yield (+23bp).

Furthermore, financials' bond spreads have widened more than the market overall. In turn, subordinated financials (junior and Tier 1) posted total returns of 1% last week.



Draghi reopens the tap

The ECB took account of the economic slowdown in the euro area that had transpired in a variety of surveys since last autumn. The return to potential growth after a strong year 2017 accelerated late last year due to protectionist measures limiting world trade and political uncertainty. The drop in oil prices (actually quite modest in euro terms) does not compensate for the underlying slowdown dynamics. Inflation may hover about 1.2%ya this year on ECB forecasts before a very slow upturn towards target. Furthermore, the ECB cut its GDP growth forecast from 1.7%ya to just 1.1%ya in 2019. The expected recovery thereafter appears dubious since fiscal policy remains unused in most euro area member countries. It is true that public spending avoided technical recession in Germany but it is by no means a coordinated policy aimed at raising output growth in the longer run. Debt reduction remains Germany's main objective. Instead, euro area countries where public finances are in worse shape, including France and Italy, are the ones pursuing fiscal expansion using inadequate demand policies to tackle supply-side issues. The lack of coordinated government policies remains one of the main impediments to growth in the euro area. On the monetary front, the ECB postponed potential rate increases to 2020, or even later. A new series of targeted LTRO will be launched next September. The ECB had no choice but to prolong long-term refinancing operations as most peripheral banks cannot access market funding at acceptable conditions at present. The maturity of TLTRO-III will be shorter than that of previous long-term loans (2 years instead of 4 years). The maximum amount lent by the ECB will be 30% of the participating bank's loan book. This may create a source of fragility in countries where bank credit has continued to shrink despite ECB targeted lending operations. Some Italian or Spanish banks may be unable to roll the total amount of existing ECB loans in this context.

FOMC to clarify balance sheet policy next week

Activity in the US is still stronger than in the rest of the world. Yet, retail sales disappointed over the December-January period and employment rose only 20k in February. That prompted some (over-)reaction from market participants although growth is still likely to come in above potential of 1.7% on Fed estimates even as the economy operates at full employment. In any case, the Fed is very unlikely to roll back the dovish language. Priority for Fed policymakers is to set a timetable for the expected end of balance sheet shrinkage. The recent change of tone by the Fed played a key role in propping up asset prices. Jerome Powell will take no risk to reignite an equity correction

all the more so that potential dollar appreciation would be detrimental to the US trade balance, which already shows an outsized deficit.

In the UK, Gilts remain a function of political shenanigans around the Brexit process. A new round of votes is scheduled with much the same issues on the table: deal/no-deal, procrastination and postponement of effective Brexit date.

Neutrality on rates

In terms of strategy, the major bond markets exhibit the same bullish backdrop. The decline in bond yields continues in the wake of ECB easing. Bund yields trade within 0.10% helping to lower spreads across the board in both core and non-core sovereign markets. The spread on French OATs indeed came in within 40bp. Recent success at Spanish bond syndication is a sign of great investor interest for long-dated sovereign securities. Spain's Bonos indeed trade within 110bp. Besides Mario Draghi's dovish turn, the possibility of early elections and somewhat reassuring survey data ignited a bout of optimism in Italian bond markets. We are still cautious on Italian bonds and prefer holding other peripheral bonds. In the US, the Fed's change of heart maintains 10-year yields way under their fair value of 3.10% at present. At 2.65%, US bond yields are near the upper end of their forecasted range for year-end print (2-2.75%) assuming no more hikes and ending of balance-sheet run-off.

In equity space, the dollar's rise proved detrimental to US indices. It is also likely that a number of investors chose to take profits after double-digit returns year-to-date. The widespread rally in stocks provides a favourable backdrop for profit-taking. Utilities and telecommunication services have been safe havens whilst cyclical stocks took a beating. The energy sector lost fully 4% last week. In Europe, the drop was cushioned by the euro's depreciation under \$1.13 as ECB pushed out rate hikes. Banks suffer from less favourable terms for the new TLTRO-III series whilst cyclicals (automobiles and basic resources) resume outperforming. The move into utilities was also quite pronounced in European markets.

Euro Investment grade bond markets, pulled down by financials, did underperform sovereign bond indices in the past week. The average spread on the asset class increased by 3bp. Flows also reversed in European high yield and emerging bond markets where spreads had shrunk considerably since the start of the year. It also hints at profit-taking considering outsized capital gains so far this year. Speculative-grade corporate bond spreads widened by as much as 23bp in five trading sessions. The average spread in emerging markets (USD global diversified) is up some 20bp from a week ago to 357bp.

Main Market Indicators

G4 Government Bonds	11-Mar-19	-1w k (bp)	-1m (bp)	Ytd (bp)
EUR Bunds 2y	-0.54 %	-3	+3	+7
EUR Bunds 10y	0.06%	-10	-6	-18
EUR Bunds 2s10s	60 bp	-7	-9	-25
USD Treasuries 2y	2.47 %	-7	-1	-1
USD Treasuries 10y	2.64 %	-8	-1	-4
USD Treasuries 2s10s	17 bp	-1	0	-3
GBP Gilt 10y	1.17 %	-11	-1	-11
JPY JGB 10y	-0.03 %	-4	0	-4
€ Sovereign Spreads (10y)	11-Mar-19	-1w k (bp)	-1m (bp)	Ytd (bp)
France	34 bp	-6	-10	-13
Italy	250 bp	-8	-28	0
Spain	109 bp	+8	-3	-8
Inflation Break-evens (10y)	11-Mar-19	-1w k (bp)	-1m (bp)	Ytd (bp)
EUR OATi	96 bp	-3	+5	-4
USD TIPS	191 bp	-3	+9	+20
GBP Gilt Index-Linked	315 bp	+7	-3	-2
EUR Credit Indices	11-Mar-19	-1w k (bp)	-1m (bp)	Ytd (bp)
EUR Corporate Credit OAS	131 bp	+3	-8	-21
EUR Agencies OAS	55 bp	-2	-7	-5
EUR Securitized - Covered OAS	53 bp	-3	-9	-10
EUR Pan-European High Yield OAS	424 bp	+23	-34	-89
EUR/USD CDS Indices 5y	11-Mar-19	-1w k (bp)	-1m (bp)	Ytd (bp)
iTraxx IG	63 bp	+1	-10	-26
iTraxx Crossover	285 bp	+7	-31	-69
CDX IG	62 bp	+1	-6	-26
CDX High Yield	356 bp	+8	-7	-94
Emerging Markets	11-Mar-19	-1w k (bp)	-1m (bp)	Ytd (bp)
JPM EMBI Global Div. Spread	357 bp	+20	-3	-58
Currencies	11-Mar-19	-1w k (%)	-1m (%)	Ytd (%)
EUR/USD	\$1.123	-0.89	-0.35	-1.93
GBP/USD	\$1.310	-0.63	+1.93	+2.77
USD/JPY	¥111.24	+0.43	-0.71	-1.42
Commodity Futures	11-Mar-19	-1w k (\$)	-1m (\$)	Ytd (\$)
Crude Brent	\$66.6	\$0.9	\$5.0	\$12.3
Gold	\$1 292.3	\$5.7	-\$15.1	\$10.8
Equity Market Indices	11-Mar-19	-1w k (%)	-1m (%)	Ytd (%)
S&P 500	2 775	-0.63	2.42	10.71
EuroStoxx 50	3 306	-0.34	4.43	10.14
CAC 40	5 268	-0.36	5.05	11.35
Nikkei 225	21 125	-3.19	1.25	5.55
Shanghai Composite	3 027	-0.02	13.29	21.38
VIX - Implied Volatility Index	14.63	0.00	-8.39	-42.45

Source: Bloomberg, Ostrum Asset Management

Writing



AXEL BOTTE
STRATEGIST
axel.botte@ostrum.com

Legal information

This document is intended for professional clients in accordance with MiFID. It may not be used for any purpose other than that for which it was conceived and may not be copied, distributed or communicated to third parties, in part or in whole, without the prior written authorization of Ostrum Asset Management.

None of the information contained in this document should be interpreted as having any contractual value. This document is prepared purely for the purposes of providing indicative information. This document consists of a presentation created and prepared by Ostrum Asset Management based on sources it considers to be reliable. Ostrum Asset Management reserves the right to modify the information presented in this document at any time without notice, and in particular anything relating to the description of the investment process, which under no circumstances constitutes a commitment from Ostrum Asset Management.

Ostrum Asset Management will not be held responsible for any decision taken or not taken on the basis of the information contained in this document, nor in the use that a third party might make of the information.

Figures mentioned refer to previous years. Past performance does not guarantee future results. Any reference to a ranking, a rating or an award provides no guarantee for future performance and is not constant over time. Reference to a ranking and/or an award does not indicate the future performance of the UCITS/AIF or the fund manager.

Under Ostrum Asset Management's social responsibility policy, and in accordance with the treaties signed by the French government, the funds directly managed by Ostrum Asset Management do not invest in any company that manufactures, sells or stocks anti-personnel mines and cluster bombs.

This material has been provided for information purposes only to investment service providers or other Professional Clients, Qualified or Institutional Investors and, when required by local regulation, only at their written request. This material must not be used with Retail Investors.

In the E.U. (outside of the UK and France): Provided by Natixis Investment Managers S.A. or one of its branch offices listed below. Natixis Investment Managers S.A. is a Luxembourg management company that is authorized by the Commission de Surveillance du Secteur Financier and is incorporated under Luxembourg laws and registered under n. B 115843. Registered office of Natixis Investment Managers S.A.: 2, rue Jean Monnet, L-2180 Luxembourg, Grand Duchy of Luxembourg. Italy: Natixis Investment Managers S.A., Succursale Italiana (Bank of Italy Register of Italian Asset Management Companies no. 23458.3). Registered office: Via Larga, 2 - 20122, Milan, Italy. Germany: Natixis Investment Managers S.A., Zweigniederlassung Deutschland (Registration number: HRB 88541). Registered office: Im Trutz Frankfurt 55, Westend Carrée, 7. Floor, Frankfurt am Main 60322, Germany. Netherlands: Natixis Investment Managers, Netherlands (Registration number 50774670). Registered office: Stadsplateau 7, 3521AZ Utrecht, the Netherlands. Sweden: Natixis Investment Managers, Nordics Filial (Registration number: 516405-9501 - Swedish Companies Registration Office). Registered office: Kungsgatan 48 5tr, Stockholm 111 35, Sweden. Spain: Natixis Investment Managers, Sucursal en España, Serrano nº90, 8th Floor, 28006, Madrid, Spain.

In France: Provided by Natixis Investment Managers International – a portfolio management company authorized by the Autorité des Marchés Financiers (French Financial Markets Authority - AMF) under no. GP 90-009, and a public limited company (société anonyme) registered in the Paris Trade and Companies Register under no. 329 450 738. Registered office: 43 avenue Pierre Mendès France, 75013 Paris.

In Switzerland: Provided for information purposes only by Natixis Investment Managers, Switzerland SArl, Rue du Vieux Collège 10, 1204 Geneva, Switzerland or its representative office in Zurich, Schweizergasse 6, 8001 Zürich.

In the U.K.: Provided by Natixis Investment Managers UK Limited which is authorised and regulated by the UK Financial Conduct Authority (register no. 190258). This material is intended to be communicated to and/or directed at persons (1) in the United Kingdom, and should not to be regarded as an offer to buy or sell, or the solicitation of any offer to buy or sell securities in any other jurisdiction than the United Kingdom; and (2) who are authorised under the Financial Services and Markets Act 2000 (FSMA 2000); or are high net worth businesses with called up share capital or net assets of at least £5 million or in the case of a trust assets of at least £10 million; or any other person to whom the material may otherwise lawfully be distributed in accordance with the FSMA 2000 (Financial Promotion) Order 2005 or the FSMA 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 (the "Intended Recipients"). The Fund, services or opinions referred to in this material are only available to the Intended Recipients and this material must not be relied nor acted upon by any other persons. Registered Office: Natixis Investment Managers UK Limited, One Carter Lane, London, EC4V 5ER.

In the DIFC: Provided in and from the DIFC financial district by Natixis Investment Managers Middle East (DIFC Branch) which is regulated by the DFSA. Related financial products or services are only available to persons who have sufficient financial experience and understanding to participate in financial markets within the DIFC, and qualify as Professional Clients or Market Counterparties as defined by the DFSA. No other person should act upon this material. Registered office: Office 603 - Level 6, Currency House Tower 2, PO Box 118257, DIFC, Dubai, United Arab Emirates.

In Japan: Provided by Natixis Investment Managers Japan Co., Ltd., Registration No.: Director-General of the Kanto Local Financial Bureau (kinsho) No. 425. Content of Business: The Company conducts discretionary asset management business and investment advisory and agency business as a Financial Instruments Business Operator. Registered address: 1-4-5, Roppongi, Minato-ku, Tokyo.

In Taiwan: Provided by Natixis Investment Managers Securities Investment Consulting (Taipei) Co., Ltd., a Securities Investment Consulting Enterprise regulated by the Financial Supervisory Commission of the R.O.C. Registered address: 34F., No. 68, Sec. 5, Zhongxiao East Road, Xinyi Dist., Taipei City 11065, Taiwan (R.O.C.), license number 2018 FSC SICE No. 024, Tel. +886 2 8789 2788.

In Singapore: Provided by Natixis Investment Managers Singapore (name registration no. 53102724D) to distributors and institutional investors for informational purposes only. Natixis Investment Managers Singapore is a division of Ostrum Asset Management Asia Limited (company registration no. 199801044D). Registered address of Natixis Investment Managers Singapore: 5 Shenton Way, #22-05 UIC Building, Singapore 068806.

In Hong Kong: Provided by Natixis Investment Managers Hong Kong Limited to institutional/ corporate professional investors only.

In Australia: Provided by Natixis Investment Managers Australia Pty Limited (ABN 60 088 786 289) (AFSL No. 246830) and is intended for the general information of financial advisers and wholesale clients only.

In New Zealand: This document is intended for the general information of New Zealand wholesale investors only and does not constitute financial advice. This is not a regulated offer for the purposes of the Financial Markets Conduct Act 2013 (FMCA) and is only available to New Zealand investors who have certified that they meet the requirements in the FMCA for wholesale investors. Natixis Investment Managers Australia Pty Limited is not a registered financial service provider in New Zealand.

In Latin America: Provided by Natixis Investment Managers S.A.

In Uruguay: Provided by Natixis Investment Managers Uruguay S.A., a duly registered investment advisor, authorised and supervised by the Central Bank of Uruguay. Office: San Lucar 1491, oficina 102B, Montevideo, Uruguay, CP 11500. The sale or offer of any units of a fund qualifies as a private placement pursuant to section 2 of Uruguayan law 18.627.

In Colombia: Provided by Natixis Investment Managers S.A. Oficina de Representación (Colombia) to professional clients for informational purposes only as permitted under Decree 2555 of 2010. Any products, services or investments referred to herein are rendered exclusively outside of Colombia. This material does not constitute a public offering in Colombia and is addressed to less than 100 specifically identified investors.

In Mexico: Provided by Natixis IM Mexico, S. de R.L. de C.V., which is not a regulated financial entity or an investment manager in terms of the Mexican Securities Market Law (Ley del Mercado de Valores) and is not registered with the Comisión Nacional Bancaria y de Valores (CNBV) or any other Mexican authority. Any products, services or investments referred to herein that require authorization or license are rendered exclusively outside of Mexico. Natixis Investment Managers is an entity organized under the laws of France and is not authorized by or registered with the CNBV or any other Mexican authority to operate within Mexico as an investment manager in terms of the Mexican Securities Market Law (Ley del Mercado de Valores). Any use of the expression or reference contained herein to "Investment Managers" is made to Natixis Investment Managers and/or any of the investment management subsidiaries of Natixis Investment Managers, which are also not authorized by or registered with the CNBV or any other Mexican authority to operate within Mexico as investment managers.

The above referenced entities are business development units of Natixis Investment Managers, the holding company of a diverse line-up of specialised investment management and distribution entities worldwide. The investment management subsidiaries of Natixis Investment Managers conduct any regulated activities only in and from the jurisdictions in which they are licensed or authorized. Their services and the products they manage are not available to all investors in all jurisdictions. It is the responsibility of each investment service provider to ensure that the offering or sale of fund shares or third party investment services to its clients complies with the relevant national law.

The provision of this material and/or reference to specific securities, sectors, or markets within this material does not constitute investment advice, or a recommendation or an offer to buy or to sell any security, or an offer of any regulated financial activity. Investors should consider the investment objectives, risks and expenses of any investment carefully before investing. The analyses, opinions, and certain of the investment themes and processes referenced herein represent the views of the portfolio manager(s) as of the date indicated. These, as well as the portfolio holdings and characteristics shown, are subject to change. There can be no assurance that developments will transpire as may be forecasted in this material. Past performance information presented is not indicative of future performance.

Although Natixis Investment Managers believes the information provided in this material to be reliable, including that from third party sources, it does not guarantee the accuracy, adequacy, or completeness of such information. This material may not be distributed, published, or reproduced, in whole or in part.

All amounts shown are expressed in USD unless otherwise indicated.



www.ostrum.com

Ostrum Asset Management

Asset management company regulated by AMF under n° GP-18000014 – Limited company with a share capital of 27 772 359 euros

Trade register n°525 192 753 Paris – VAT: FR 93 525 192 753 – Registered Office: 43, avenue Pierre Mendès-France, 75013 Paris – www.ostrum.com

Tél. : 01 58 19 09 80