

# Peripheral Europe Update

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- **Strong start for peripheral bonds**
- **Italian confidence remains strong ahead of the March election**

## Main market events

Peripheral bonds performed very well this week. This is worth noting as the ECB has started to reduce the magnitude of its sovereign bond purchases and several ECB Governing Council members have recently reinforced the message that the QE could possibly end at the end of September. The weak Eurozone inflation figure recorded this Friday is likely to push back market expectations about the future normalization of monetary policy by the ECB. This could support peripheral bonds. Italian bonds have returned 1.68% in the first three days of this year, Spanish bonds 1.33%, Portuguese bonds 1.81% and Irish bonds 1.21%.

## Italy

The good economic momentum continues, with the PMIs remaining particularly strong. Business confidence is apparently not hampered by political uncertainty ahead of the 4 March elections. The centre-right bloc still appears the most likely to win. Its leader Salvini this week rejected the idea of collaborating to a government led by the anti-establishment party M5S, but instead confirmed his intention to join forces with Forza Italia. A deal between Lega Nord and Forza Italia ahead of the election could well dampen the rather extreme anti-euro position currently taken by Salvini. That said, the M5S party remains the first single party in polls. Were the centre-right coalition to fail, M5S could well be in charge of forming a government. Such a scenario is not negligible and could affect negatively Italian spreads in the next couple of months.

## Spain

Increasing pressures from the Basque Party are currently put on PM Rajoy to revoke the Article 155 in Catalonia and end the direct rule in the region as early as in January. This is set as a condition by this pro-secessionist party that provided support to the ruling PP-led minority government to re-engage negotiations over the 2018 Budget. The new Catalan parliament will reconvene on 17 January with the aim to form a new regional government. The fact that 8 elected PMs are still in exile or in detention since November will complicate the task of the parliament – unless some kind of amnesty is granted by the Supreme Court. It is set to decide this Friday whether or not to release the leaders of the pro-independence Catalan parties. The overall climate has improved in Spain and the de-escalation of the conflict between Madrid and Catalonia appears a credible scenario. A new general election in Spain is then unlikely, while it seems possible that the Article 155 ends after the formation of a new government in Catalonia.

## Robeco Euro Government Bonds

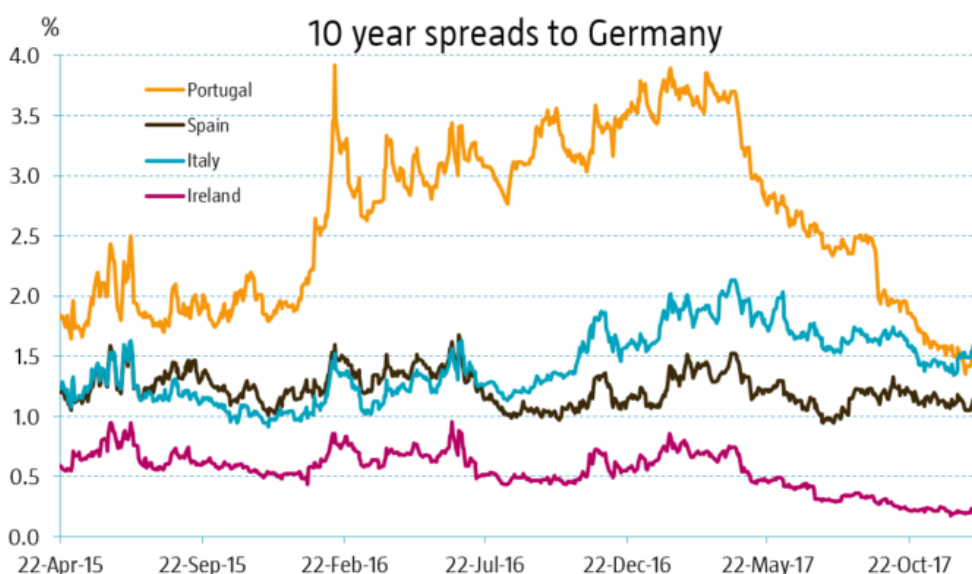
We have an overweight position in Spanish government bonds and a small underweight position in Italian bonds. We are positive on Spanish fundamentals, while we remain wary of the political risks in Italy. We hold no Irish bonds as their spreads over France do not compensate for the potential risks stemming from Brexit, international tax reform and the volatility inherent to Ireland's size. Currently the fund is 40% invested in peripheral bonds, in line with the index. Year-to-date the fund's absolute return is 0.02%\*.

\* Robeco Euro Government Bonds, gross of fees, based on Net Asset Value, January 4, 2018.  
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Current spreads and the movement over time

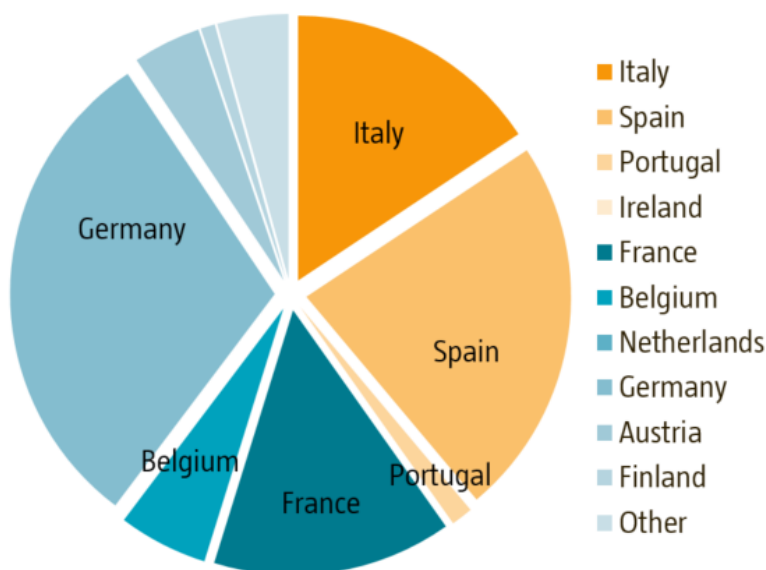
maturity	German yields	Spreads									
		France	Italy	Spain	Netherlands	Belgium	Austria	Greece	Ireland	Finland	Portugal
1	-0.61	0.03									
2	-0.61	0.14	0.27	0.23	-0.04	0.09	0.08	2.18	0.12	0.03	0.51
3	-0.53	0.23	0.53	0.48	0.01	0.10	0.07		0.09	0.09	0.50
4	-0.38	0.23	0.63	0.40	-0.02	0.06	0.04		0.28	0.05	0.44
5	-0.21	0.21	0.86	0.54	-0.06	0.06	0.08	3.50	0.26	0.07	0.66
6	-0.09	0.23	0.94	0.64	0.04	0.15	0.11		0.18	0.14	0.87
7	0.04	0.26	1.19	0.74	0.06	0.19	0.12		0.22	0.09	0.94
8	0.16	0.30	1.37	0.91	0.09	0.18	0.16			0.15	1.32
9	0.29	0.34	1.47	0.98	0.08	0.19	0.19			0.04	1.40
10	0.43	0.35	1.55	1.07	0.10	0.21	0.16	3.34	0.21	0.17	1.48
15	0.65	0.39	1.96	1.51		0.36	0.40	3.55	0.45	0.23	1.69
20	0.94	0.41	1.85			0.17	0.17	3.35			1.87
30	1.25	0.48	1.95	1.51	-0.01	0.42	0.20			0.08	1.90

Source: Bloomberg



Source: Bloomberg

Country allocation Robeco Euro Government Bonds (January 04, 2018)



Source: Robeco

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