

Peripheral Europe Update

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- **Italy: populist coalition government increasingly likely**
- **Catalan regional election in the coming days**

Main market events

Peripheral spreads have continued to widen this week. Italian bonds underperformed significantly as the scenario of a coalition government between the two populist parties is becoming increasingly likely. Italian bonds have returned 1.76% year-to-date, Spanish bonds 2.56%, Portuguese bonds 2.26% and Irish bonds 0.07%.

ECB

Governing Council member Lane mentioned this week that it is too early to assess whether the economic slowdown in the Eurozone was driven by a lack of demand or by capacity constraints. While a demand shortfall would possibly require an accommodative monetary stance for longer, a supply issue would by contrast strengthen inflationary pressures.

Italy

This week, coming as a last minute surprise, the two populist parties have agreed to form a government alliance. This was possible as Forza Italia gave its green light, assuring that it will abstain in the confidence votes of the new government. The announcement of such agreement came only two days after President Mattarella proposed to form a temporary technocratic government and called for new elections. Against this backdrop, several unknowns remain, especially the choice of the PM and the scope of policy reforms that both parties could agree upon. Among the area of convergence are: the reversal of the 2011 pension reform which would lead to a lower retirement age, a flat tax possible as low as 15%, a citizen income programme helping the distressed taxpayers and the fight against illegal immigration. All these measures, if implemented, would increase the fiscal deficit and the public debt. That said, if the new government is constrained in its ability to deliver radical changes, it could be positive for spreads given the current punitive carry.

Spain

Catalonian separatist parties intend to elect their regional president next week. Quim Torra is set to be the candidate of the separatists for the election on Saturday. To the extent that he is unlikely to be elected in the first round, a second round on Monday appears probable, when he will be able to be elected by a slender majority. On the economic front, the slowdown in Q1 is set to be temporary, given the sharp rebound in industrial production in March and the improvement in the industrial confidence surveys in April.

Robeco Euro Government Bonds

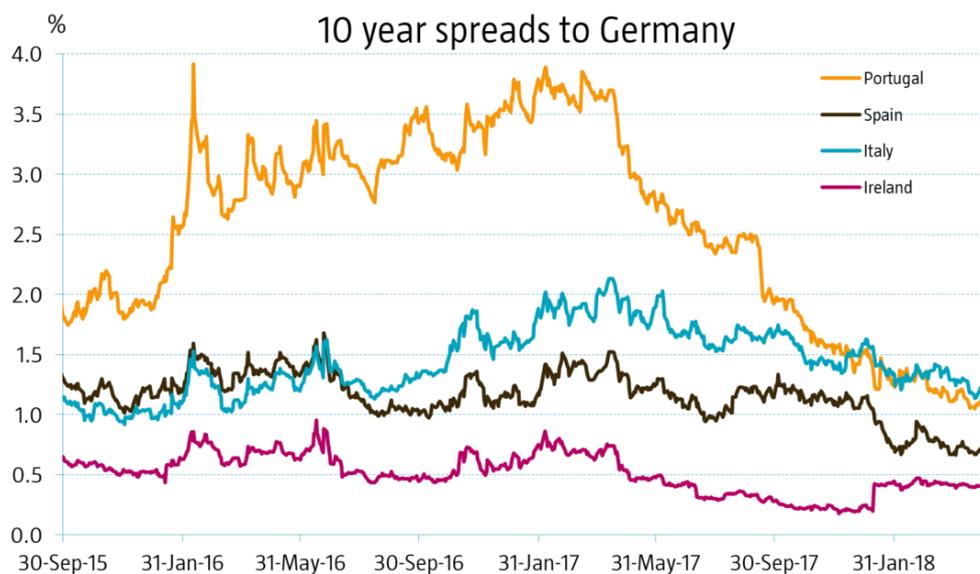
We increased exposure to short-dated bonds in Spain and Italy against France, while we reduced exposure to long-dated Italian bonds. The fund is now overweight 5-10 year Italian bonds and 10-year and longer-dated Spanish and Portuguese bonds. Currently the fund is 54% invested in peripheral bonds, well above index level. Year-to-date the fund's absolute return is 1.01%*.

* Robeco Euro Government Bonds, gross of fees, based on Net Asset Value, 10 May, 2018.
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Current spreads and the movement over time

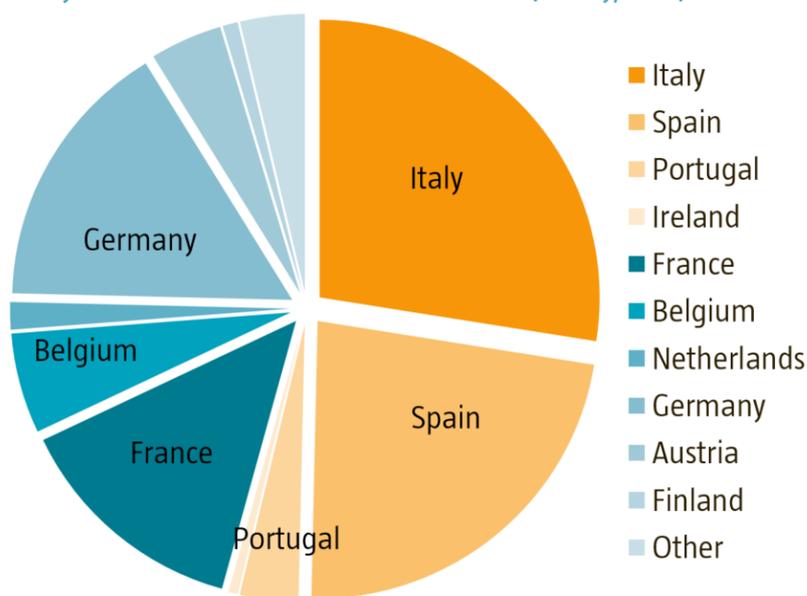
Maturity	German yields	Spreads									
		France	Italy	Spain	Netherlands	Belgium	Austria	Greece	Ireland	Finland	Portugal
1	-0.63	0.07									
2	-0.59	0.08	0.32	0.25	-0.04	0.08	0.14	1.99	0.14	0.01	0.41
3	-0.44	0.13	0.41	0.30	-0.10	0.00	0.16		-0.01	0.01	0.39
4	-0.26	0.14	0.69	0.17	-0.11	-0.03	0.12		0.17	-0.07	0.56
5	-0.07	0.11	0.78	0.26	-0.17	0.20	0.16	3.12	0.12	-0.03	0.62
6	0.05	0.16	0.82	0.49	0.13	0.20	0.23		0.23	0.06	0.66
7	0.19	0.18	1.03	0.56	0.15	0.24	0.26		0.28	0.01	0.96
8	0.30	0.21	1.17	0.67	0.16	0.26	0.12			0.10	1.03
9	0.42	0.24	1.21	0.72	0.16	0.28	0.23			-0.09	1.08
10	0.55	0.23	1.33	0.73	0.14	0.27	0.20	3.47	0.41	0.11	1.13
15	0.69	0.50	1.70	1.12		0.54	0.45	3.88	0.68	0.26	1.55
20	0.97	0.33	1.73			0.45	0.22	3.81			1.43
30	1.24	0.42	1.75	1.17	-0.02	0.40	0.25			0.10	1.44

Source: Bloomberg



Source: Bloomberg. Note: the jump in Irish yields is due to the issuance of a new 10-year bond.

Country allocation Robeco Euro Government Bonds (10 May, 2018)



Source: Robeco

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