ROBECO

Peripheral Europe Update

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- **Higher fiscal deficit in Spain for 2018/19**
- **Ongoing conflicting messages from Italian officials**

Main market events
Over the past week, peripheral bond spreads have remained broadly flat. This could appear rather strange in the aftermath of the ECB initiative aiming at tackling non-performing loans in the Eurozone, by forcing banks to increase their provisions. In addition, the promise made by PM Conte to fully reimburse Italian savers that lost their money in the bail-in of local banks in 2016, could have damaged Italian spreads more. Italian bonds have returned -2.0% year-to-date, Spanish bonds 2.8%, Portuguese bonds 2.4% and Irish bonds 1.0%.

Spain
On Tuesday, Spanish Prime Minister Sanchez proposed a fiscal plan in Congress to reinforce the social cohesion by tackling the issue of inequality. The strategy that involves higher corporate taxes, more public spending and a higher fiscal deficit for 2018/19 is in sharp contrast with the rather conservative stance of the previous government. The additional EUR 16bn spending will be directed toward education, health, pensions and social services. To finance it, taxes on business, banks, financial transactions and polluting energy will be increased. In total, if these measures are passed in Congress, the deficit would then be lifted by 0.5 percentage point in 2018 and 2019. The more accommodative fiscal stance of this new government could be viewed in the context of a possible snap election in 2019.

Italy
Some Lega officials renewed their anti-euro rhetoric this week, calling for an euro exit. Their messages were counter-balanced by PM Conte who affirmed that the euro is irreversible. He furthermore stressed the principle of tax progressivity for any tax reform, a position contrasting with the flat tax supported by Salviani and Di Maio. BTP volatility has been further fueled by rumors that Finance Minister Tria could be pushed out by the leaders of the two populist parties, but this rumor has been refuted by Giovanni Tria himself. This does not bode well for a quiet summer until September 27, when the Draft Budget will be presented. With this budget plan, more insight will be provided into the real fiscal posture of the populist coalition. Meanwhile, PM Conte met savers who lost their money in the bankruptcy of Banca Monte dei Paschi and some smaller Venetian banks. He promised them that they will be fully reimbursed. This, if implemented, could fuel a negative dynamics between Sovereign BTP and bank spreads.

Robeco Euro Government Bonds
The positioning of the fund in periphery markets has remained unchanged in the past two weeks. Overall, our risk position in peripheral bonds is slightly higher than that of the index, mainly located in Spain and Ireland. We remain cautious towards Italy as markets are vulnerable to headline-risk. Currently the fund is 35% invested in peripheral bonds, less than the index level as expressed in market value. Year-to-date the fund's absolute return is 0.69%*.

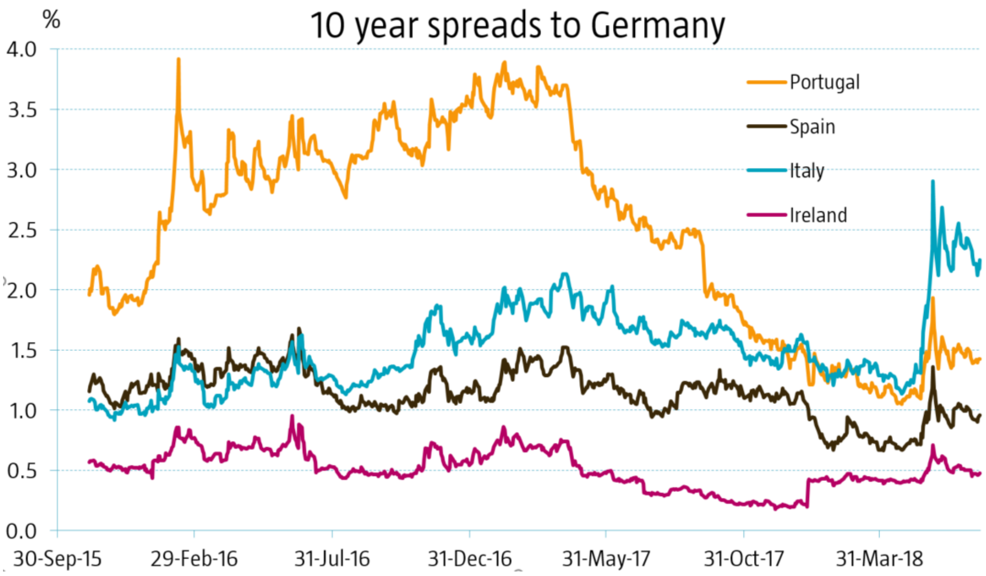
* Robeco Euro Government Bonds, gross of fees, based on Net Asset Value, 19 July, 2018. The value of your investments may fluctuate. Past results are no guarantee of future performance.

Current 10-yr spreads versus Germany

Maturity	German yields	Spreads France	Italy	Spain	Netherlands	Belgium	Austria	Greece	Ireland	Finland	Portugal
1	-0.66	0.11									
2	-0.63	0.19	1.27	0.34	-0.02	0.10	0.13	2.03	0.14	0.03	0.51
3	-0.57	0.28	1.61	0.45	0.05	0.07	0.15		0.13	0.03	0.51
4	-0.45	0.29	1.83	0.49	0.07	0.05	0.13		0.23	-0.02	0.69
5	-0.30	0.31	1.97	0.64	0.08	0.26	0.18	3.30	0.18	0.02	0.84
6	-0.14	0.20	2.10	0.68	0.07	0.20	0.17		0.25	0.05	0.87
7	-0.02	0.24	2.20	0.74	0.10	0.25	0.24		0.34	0.00	1.24
8	0.10	0.27	2.20	0.86	0.10	0.28	0.09			0.08	1.33
9	0.21	0.24	2.27	0.94	0.12	0.31	0.22			0.12	1.37
10	0.33	0.31	2.24	0.95	0.11	0.33	0.20	3.54	0.48	0.11	1.42
15	0.62	0.42	2.34	1.21		0.51	0.32	3.85	0.68	0.10	1.67
20	0.77	0.38	2.45			0.58	0.23	3.95			1.73
30	1.00	0.53	2.43	1.45	-0.02	0.59	0.32			0.13	1.79

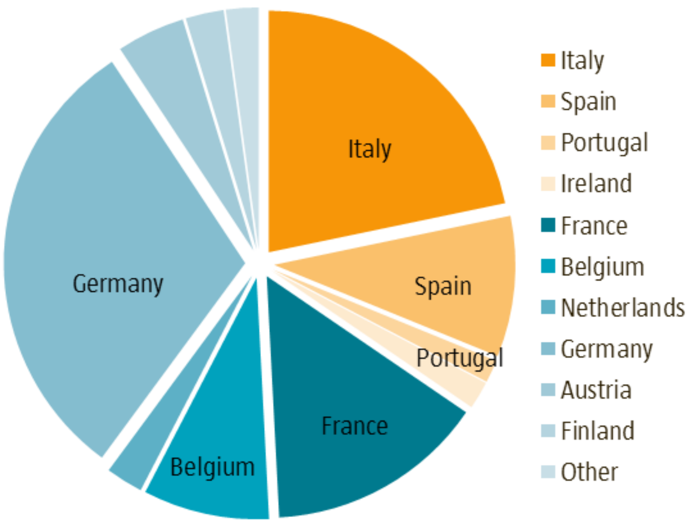
Source: Bloomberg

Movement over time



Source: Bloomberg.

Country allocation Robeco Euro Government Bonds (19 July, 2018)



Source: Robeco

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