

Peripheral Europe Update

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- **ECB strikes downbeat tone, announces new TLTRO and extends forward guidance**
- **Italian spread tightens towards low end of trading range**

Main market events

The main market event this week was the ECB governing council meeting on Thursday. Consensus expectations were for the ECB to strike a dovish tone but not to already make any policy adjustments. President Draghi therefore seemed to live up to his dovish reputation and surprised the market seemingly on all fronts. Italian bonds have returned 1.5% year-to-date, Spanish bonds 2.4%, Portuguese bonds 3% and Irish bonds 2.0%

Italy

Italian bonds extended their rally this week. Markets found some comfort in Italian purchasing managers' indices stabilizing, possibly an indication that the Italian economy is finding some ground. Also the dovish ECB meeting supported the Italian bond market. Policy rates lower for longer should help keep a lid on government funding costs. The Italian spread over Germany declined to 240bp right after the ECB council meeting, the lowest level of the year. Hence a significant rally since reaching just under 290bp over Bunds halfway through February.

ECB

The ECB struck a very dovish tone Thursday, surprising markets. Both growth and inflation forecasts were downgraded significantly. The ECB also extended its forward guidance on policy rates into the start of 2020 and announced a new TLTRO3. Details, however, seem much less generous for banks than the previous TLTRO2. Both regarding the maturity (2 years now versus 4 years then) and the level of rates, which will be linked to the main refinancing rate rather than the deposit facility rate. Draghi quashed expectations that the new TLTRO could be used for peripheral bond carry plays, and reiterated that risks to the outlook for growth and inflation remained tilted to the downside. An indication that it will be very challenging for the ECB to hike rates at all this cycle. Mr. Draghi will be remembered as the first ECB president not to have hiked rates during his 8 year tenure.

Robeco Euro Government Bonds

The expected trading environment for Italian government bonds is muddle through, with asymmetric downside risks. As long as the current government remains in place, BTPs will be subject to lingering event risk. The post-May 2018 trading range over Bunds (230-320bp) will probably be difficult to break. So at the current 240bp over Germany, Italy is now at the low end of this range. We therefore used this level to add to the Italian underweight position. Next to the underweight in Italy we have a small overweight in Ireland and a small underweight in Spain. The fund's investments in peripheral bonds amount to circa 33%, about 7% below the level of the index. Year to date the absolute return of the fund is 1.70%*

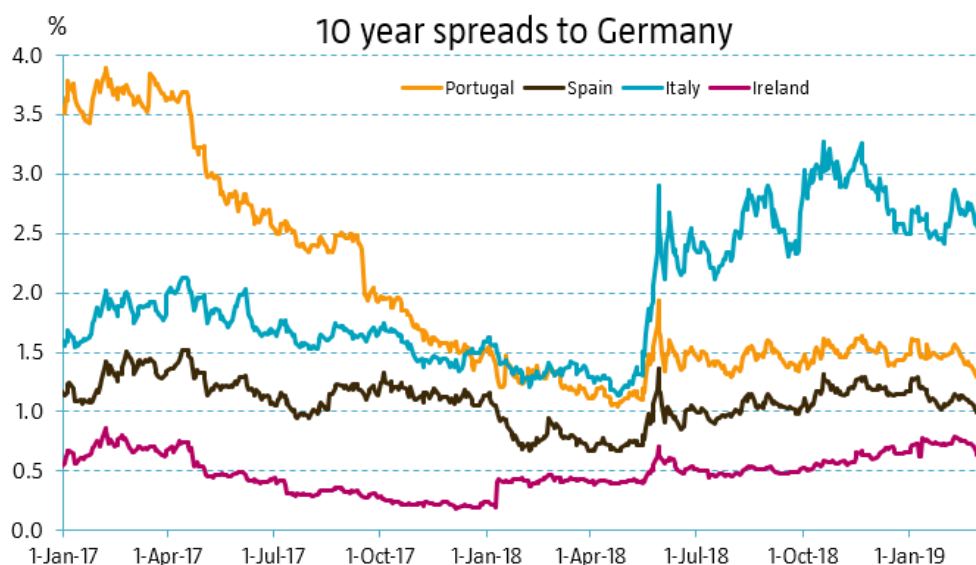
* Robeco Euro Government Bonds, gross of fees, based on Net Asset Value, 8th March, 2019. The value of your investments may fluctuate. Past results are no guarantee of future performance

Current 10-yr spreads versus Germany (%)

Maturity	German yields	Spreads	France	Italy	Spain	Netherlands	Belgium	Austria	Greece	Ireland	Finland	Portugal
1	-0.55	0.04										
2	-0.54	0.06	0.69	0.23	-0.01	0.09	0.06			0.10	0.06	0.27
3	-0.52	0.15	1.21	0.36	-0.02	0.15	0.18			0.31	0.07	0.41
4	-0.44	0.16	1.47	0.38	-0.01	0.23	0.18			0.24	0.09	0.53
5	-0.35	0.20	1.77	0.47	0.02	0.29	0.22		3.25	0.30	0.12	0.58
6	-0.31	0.19	2.04	0.67	0.06	0.32	0.28			0.41	0.13	0.94
7	-0.23	0.24	2.21	0.80	0.08	0.36	0.34			0.48	0.19	1.06
8	-0.14	0.29	2.18	0.89	0.09	0.43	0.32				0.19	1.15
9	-0.05	0.26	2.31	0.96	0.11	0.46	0.31					1.26
10	0.07	0.34	2.44	0.99	0.09	0.47	0.32		3.73	0.61	0.25	1.29
15	0.32	0.57	2.84	1.30		0.64	0.45		4.14	0.79	0.38	1.55
20	0.50	0.53	2.84			0.74	0.33		4.25			1.63
30	0.71	0.72	2.86	1.60	0.06	0.90	0.44				0.28	1.76

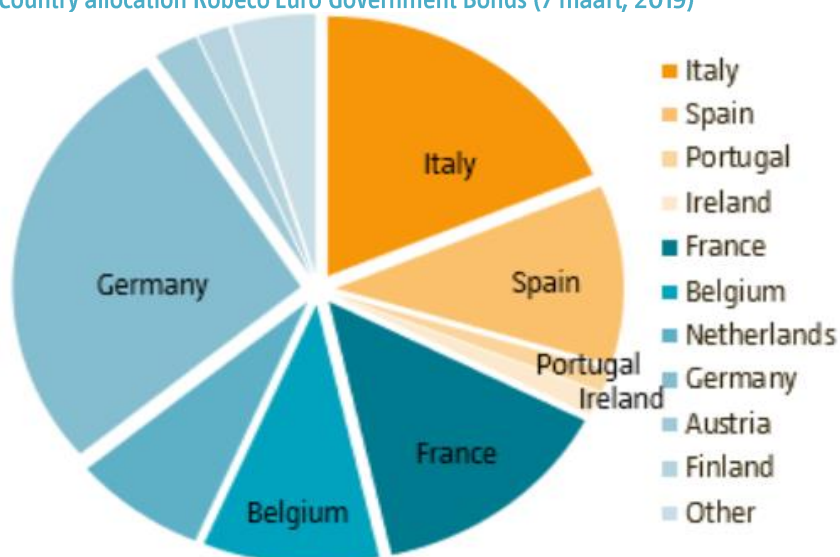
Source: Bloomberg

Movement over time



Source: Bloomberg.

Country allocation Robeco Euro Government Bonds (7 maart, 2019)



Source: Robeco

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