

Peripheral Europe Update

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- **Nascent signs of divergence within the Italian populist coalition**
- **EU summit dominated by the migrants issue**

Main market events

Peripheral spreads were modestly wider in the past week. Italy and Spain suffered from a general risk off sentiment in the beginning of the week, while spreads tightened back a bit thereafter. The advances of the EU summit this week were relatively limited. On the economic integration front, they only managed to agree on strengthening the European bailout fund, which will serve as a backstop for failed banks. All the other expected measures were postponed until December this year, while the migrants deal remained relatively vague. Greek bonds rallied, following the agreement on debt relief last Friday. Italian bonds have returned -3.6% year-to-date, Spanish bonds 2.0%, Portuguese bonds 1.7% and Irish bonds 0.8%.

Italy

According to the Repubblica, the Italian government has already started to negotiate with the European Commission the fiscal leeway for the 2019 budget and is reported to target “only” 0.5% of GDP. This means that the flat tax and the universal minimum income measures will not be implemented next year. If confirmed, this would suggest a more pragmatic and market-friendly approach of the 5 Star and Lega coalition than is generally perceived. But to the extent that Italy already committed to seek fiscal tightening of 0.5% of GDP for 2019 and 2020, it is not obvious whether the European Commission will agree on such slippage. Another sign of continuity with the previous government given by the Finance Minister Tria has been his blockage of the “Dignity Decree” proposed by 5 star, which intended to penalize companies delocalizing abroad and using temporary contracts. This is the first sign of diverging interests among the two populist parties.

Spain

This week, the two main trade unions agreed on a maximum 3% annual wage hike by 2020. The deal consists of a 2% fixed part and 1% which will depend on productivity gains. Furthermore, the employers’ associations accepted an increase in the minimum annual wage to EUR 14k for the next three years. This acceleration in negotiated pay growth has been taking place amid ongoing improvement in the labor market over the past five years. Meanwhile, the Bank of Spain confirmed the relative slowdown of the economy in Q2, forecasting only 0.7% GDP growth QoQ. It did not change its estimate of 2.7% for 2018 growth, but revised up its inflation forecast to 1.9%, from 1.3% three months ago, due to higher oil prices.

Robeco Euro Government Bonds

The positioning of the fund in periphery markets has remained unchanged in the past week. 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 long as markets are vulnerable to headline-risk. Currently the fund is 34.5% invested in peripheral bonds, less than the index level as expressed in market value. Year-to-date the fund’s absolute return is -0.04%*.

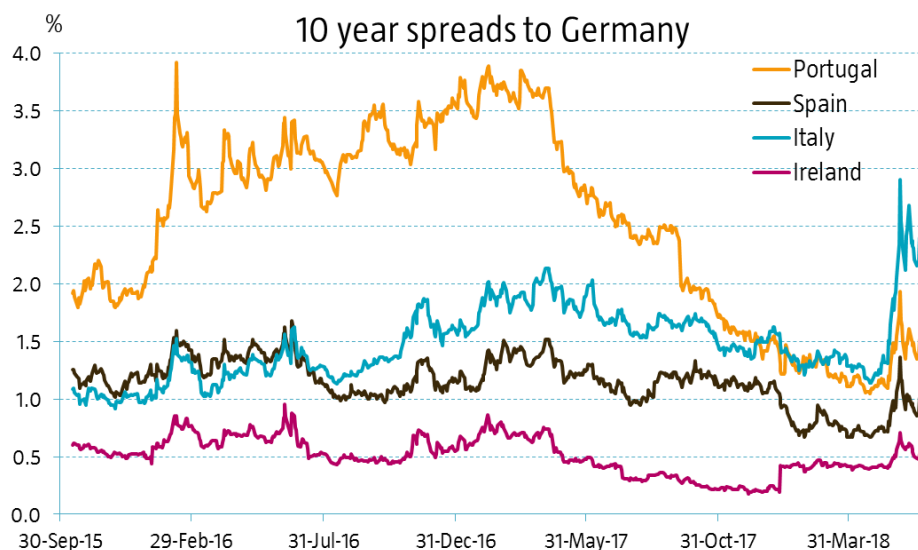
* Robeco Euro Government Bonds, gross of fees, based on Net Asset Value, 28 June, 2018. The value of your investments may fluctuate. Past results are no guarantee of future performance.

Current 10-yr spreads versus Germany

Maturity	German yields	Spreads										
		France	Italy	Spain	Netherlands	Belgium	Austria	Greece	Ireland	Finland	Portugal	
1	-0.64	0.09										
2	-0.66	0.20	1.38	0.43	0.00	0.13	0.11	2.07	0.11	0.03	0.55	
3	-0.59	0.28	1.66	0.53	0.05	0.06	0.10		0.15	0.03	0.66	
4	-0.47	0.31	1.93	0.57	0.07	0.01	0.12		0.23	-0.02	0.84	
5	-0.30	0.32	2.05	0.71	0.07	0.25	0.19	3.41	0.17	0.00	0.94	
6	-0.19	0.28	2.29	0.79	0.14	0.25	0.26		0.30	0.10	0.99	
7	-0.06	0.30	2.36	0.83	0.16	0.30	0.30		0.37	0.04	1.31	
8	0.06	0.34	2.34	0.95	0.17	0.34	0.14			0.16	1.40	
9	0.19	0.30	2.42	1.01	0.17	0.38	0.28			0.15	1.44	
10	0.31	0.36	2.39	1.02	0.16	0.39	0.28	3.65	0.51	0.18	1.49	
15	0.45	0.62	2.57	1.44		0.69	0.56	4.09	0.85	0.35	1.88	
20	0.73	0.45	2.50			0.63	0.36	3.98			1.82	
30	1.03	0.53	2.45	1.49	-0.02	0.59	0.38			0.18	1.84	

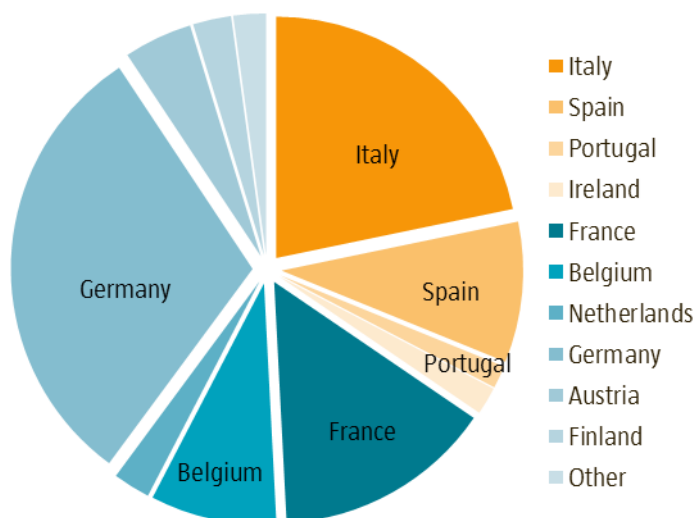
Source: Bloomberg

Movement over time



Source: Bloomberg.

Country allocation Robeco Euro Government Bonds (28 June, 2018)



Source: Robeco

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