



Bond Market Outlook

Jon Ridgway

ECB BMCG meeting 1st July 2014

The impact of the June ECB package has been felt most in shorter dated periphery

Rates market has seen more notable moves since the June ECB meeting									
	Current	une (before الله ECB)	7 May (before May ECB)	Change vs 4 June	Change vs 7 May				
3m Euribor	0.21%	0.30%	0.34%	-9 bp	-13 bp				
3m EONIA	0.05%	0.09%	0.18%	-4 bp	-13 bp				
Overnight GC Germany	-0.02%	0.10%	0.13%	-12 bp	-15 bp				
Overnight GC Italy	0.03%	0.20%	0.23%	-17 bp	-20 bp				
Bobl yield	0.36%	0.48%	0.61%	-12 bp	-25 bp				
Bund yield	1.25%	1.43%	1.47%	-19 bp	-23 bp				
5y Italy - Germany spread	112 bp	131 bp	119 bp	-19 bp	-7 bp				
5y France - Germany spread	19 bp	25 bp	25 bp	-6 bp	-6 bp				
Itraxx Main	61 bp	64 bp	68 bp	-3 bp	-7 bp				
Itraxx Crossover	239 bp	251 bp	270 bp	-12 bp	-31bp				
Eurostoxx 50	3236	3238	3160	-2	76				
EURUSD	1.365	1.360	1.391	0.005	-0.026				

Source: Bloomberg, Barclays Research



ECB action has contributed to low volatility across asset classes





Equity and currency volatility also indicate very benign market conditions





Inflation expectations are also stabilising post the June ECB meeting

ECB has helped arrest the fall in inflation expectations, but the market remains below the ECB's projections





EUR short rate path is now largely contained



Liquidity surplus is likely to pick up post the TLTROs





Long bond yields have rallied globally, not just in EURs







Source: Bloomberg, Barclays Research

BARCLAYS

EGB demand: activity is stabilising



Jan10 Apr10 Jul10 Oct10 Jan11 Apr11 Jul11 Oct11 Jan12 Apr12 Jul12 Oct12 Jan13 Apr13 Jul13 Oct13 Jan14 Apr14



Jan10 Apr10 Jul10 Oct10 Jan11 Apr11 Jul11 Oct11 Jan12 Apr12 Jul12 Oct12 Jan13 Apr13 Jul13 Oct13 Jan14 Apr14

Source: Barclays Trading



Periphery spread curve remains steep



5y5y fwd rates in Italy and Spain are still not very low considering the levels in Germany





What is fair value for Italian and Spanish spreads?





Rating downgrades have bottomed but structural reform efforts have slowed

Euro area sovereign ratings are bottoming out; the dispersion of ratings already has started to fall



Gradual rating upgrades could see the return of foreign investors to the periphery especially by more conservative investor segments



Source: Bloomberg, Barclays Research



Issuance progress for Eurozone countries

						% of 2014							
Up to 26/ 06/ 14	2-3	5	7-10	15+	All Maturities	Net issuance YTD €bn	Estimated gross issuance	Difference vs 2013	Funding - '14				
Germany	27.0	27.0	29.0	8.0	91.0	33.0	53%	1%	17:				
rance (inc buybacks)	22.7	31.9	39.4	24.7	118.6	79.2	62%	2%	192				
taly	41.9	51.8	44.4	17.3	155.5	76.6	65%	13%	24				
pain	12.9	29.0	33.8	8.4	84.1	54.4	64%	4%	13				
Belgium	0.0	2.5	10.1	8.8	21.4	8.7	65%	-2%	3				
lolland	12.8	8.6	9.6	5.0	36.0	18.8	72%	2%	50				
ortugal	0.0	3.3	4.7	0.0	8.0	3.4	61%	NA	1:				
inland	0.0	0.0	5.0	0.5	5.5	5.3	42%	-6%	1:				
ustria	0.0	2.0	6.4	1.6	10.0	6.9	40%	-9%	2				
Greece	0.0	2.0	0.0	0.0	2.0	NA	NA	NA					
eland	0.0	0.0	6.5	0.0	6.5	-0.3	82%	82%					
ovakia	0.5	0.4	0.3	1.7	2.8	-0.9	40%	40%					
urozone Aggregates	117.8	158.4	189.3	75.9	541.3	285.8	61%	4%	88				
Percentages	22%	29%	35%	14%									
Difference vs. 2013	-15%	7%	4%	3%									



Revisions to long-term equilibrium rates and term premia caused us to lower our forecasts for long maturity yields

10y Govt. bond yields	US	Germany	UK	Japan	Euro government (Germany) bond yield						
Q3 14	2.9	1.55	3	0.65		Refi rate	3m Euribor	2у	5y	10y	30y
Q4 14	3.15	1.65	3.1	0.85	Q3 14	0.15	0.18	0.05	0.5	1.55	2.4
Q1 15	3.25	1.75	3.25	1.05	Q4 14	0.15	0.18	0.05	0.6	1.65	2.5
Q2 15	3.4	1.9	3.4	1.25	Q1 15	0.15	0.18	0.1	0.75	1.75	2.55
	1				Q2 15	0.15	0.18	0.15	0.85	1.9	2.65

- *DURATION:* We have a bearish bias toward global developed market rates in H2, especially in the US and UK. In both, the market is pricing in a much less aggressive hiking cycle than we forecast.
- *CURVE:* We are underweight the intermediate sector against both the very front end and the back end in the US and UK.
- CROSS-MARKET: We expect continued divergence between US/UK and euro area/Japan rates. We believe Treasury-bund spreads, particularly in 5s, will widen over the next year.
- EGB SPREADS: We are moving from a strategic to a tactical overweight on peripheral bonds as fundamental unexplained cheapness has largely disappeared.



Low volatility environment is a concern and risks exist from different angles

- Any significant rise in volatility from extremely low levels in rates, FX and equity space
- Continuation of downside misses to Eurozone inflation prints
- Exit from Fed & BoE ultra accommodative policies: risks in both directions
- European politics heading into next year's elections in Finland, UK, Portugal and Spain
- Scottish referendum and potential Catalunya referendum
- Geopolitics and oil market implications



Topics for discussion

- What will be the medium to long term economic impact of the ECB's latest set of actions?
- Is the ECB closer or further away from EGB QE after its latest announcements?
- Are developed market central banks pushing volatility too low?
- Do low global real yields represent a new "bond market conundrum"?



Disclaimer

This document has been prepared by Barclays Bank PLC, acting through its investment bank ("Barclays"), for information purposes only. This document is an indicative summary of the terms and conditions of the securities/transaction described herein and may be amended, superseded or replaced by subsequent summaries. The final terms and conditions of the transaction and any related security will be set out in full in the applicable transaction confirmation, offering document(s), pricing supplement or binding transaction document(s).

This document shall not constitute an underwriting commitment, an offer of financing, an offer to buy or sell, or the solicitation of an offer to buy or sell any securities described herein, which shall be subject to Barclays' internal approvals. No transaction or service related thereto is contemplated without Barclays' subsequent formal agreement.

Barclays is acting solely as principal and not as advisor or fiduciary. Barclays does not provide, and has not provided, any investment advice or recommendation to you in relation to the transaction and/or any related securities described herein and is not responsible for providing or arranging for the provision of any general financial, strategic or specialist advice, including legal, regulatory, accounting, model auditing or taxation advice or services or any other services in relation to the transaction and/or any related securities described herein. Accordingly Barclays is under no obligation to, and shall not, determine the suitability for you of the transaction described herein. You must determine, on your own behalf or through independent professional advice, the merits, terms conditions and risks of the transaction described herein. You must also satisfy yourself that you are capable of assuming, and assume the risks of any such transaction. Neither Barclays nor any of its subsidiaries, affiliates or ultimate holding company, nor any of the subsidiaries or affiliates of such holding company (the" Barclays Group"), nor any of their respective directors, officers, employees, representatives or agents, accepts any liability whatsoever for any direct, indirect or consequential losses (in contract, tort or otherwise) arising from the use of this document or its contents or reliance on the information contained herein.

Barclays does not guarantee the accuracy or completeness of information which is contained in this document and which is stated to have been obtained from or is based upon trade and statistical services or other third party sources. Any data on past performance, modelling, scenario analysis or back-testing contained herein is no indication as to future performance. No representation is made as to the reasonableness of the assumptions made within or the accuracy or completeness of any modelling, scenario analysis or back-testing. All opinions and estimates are given as of the date hereof and are subject to change. The value of any investment may fluctuate as a result of market changes. The information in this document is not intended to predict actual results and no assurances are given with respect thereto.

Barclays is a full service securities firm engaged in a wide range of businesses and from time to time, in the ordinary course of its business, Barclays and/or other parts of the Barclays Group may hold long or short positions and trade or otherwise effect transactions for their own account or the account of their customers in the securities referred to herein and/or the debt or equity securities, assets or loans (or any derivatives thereof) of the companies referred to herein. Additionally, Barclays and/or other parts of the Barclays Group may have investment and commercial banking, lending, asset management and other relationships with parties which are or may become involved in the transactions referred to herein and/or which may have interests which could potentially conflict with the interests of the recipient hereof. Barclays and/or other parts of the Barclays Group have in place policies and procedures to restrict the flow of information and to identify, consider and manage such potential conflicts of interest. Accordingly, you acknowledge and agree that no part of the Barclays Group is required to restrict its activities as a result of the provision of this document, and that all parts of the Barclays Group may undertake any activities without further consultation with or notification to you. Barclays shall not be required to account to you for any revenue or profits obtained in connection with any activities of the Barclays Group as referred to herein.

Barclays' research analysts and research departments are independent from Barclays' investment banking division and are subject to certain regulations and internal policies. Barclays' research analysts may hold and make statements or investment recommendations and/or publish research reports with respect to any company referred to herein, the transactions contemplated herein or any person involved therein or related thereto that differ from or are inconsistent with the views or advice communicated by Barclays' investment banking division.

Barclays offers premier investment banking products and services to its clients through Barclays Bank PLC. Barclays Bank PLC is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority and is a member of the London Stock Exchange. Barclays Bank PLC is registered in England No. 1026167 with its registered office at 1 Churchill Place, London E14 5HP. Copyright Barclays Bank PLC, 2014 (all rights reserved).

This document is confidential, and no part of it may be reproduced, distributed or transmitted without the prior written permission of Barclays.

BARCLAYS