



Market Update

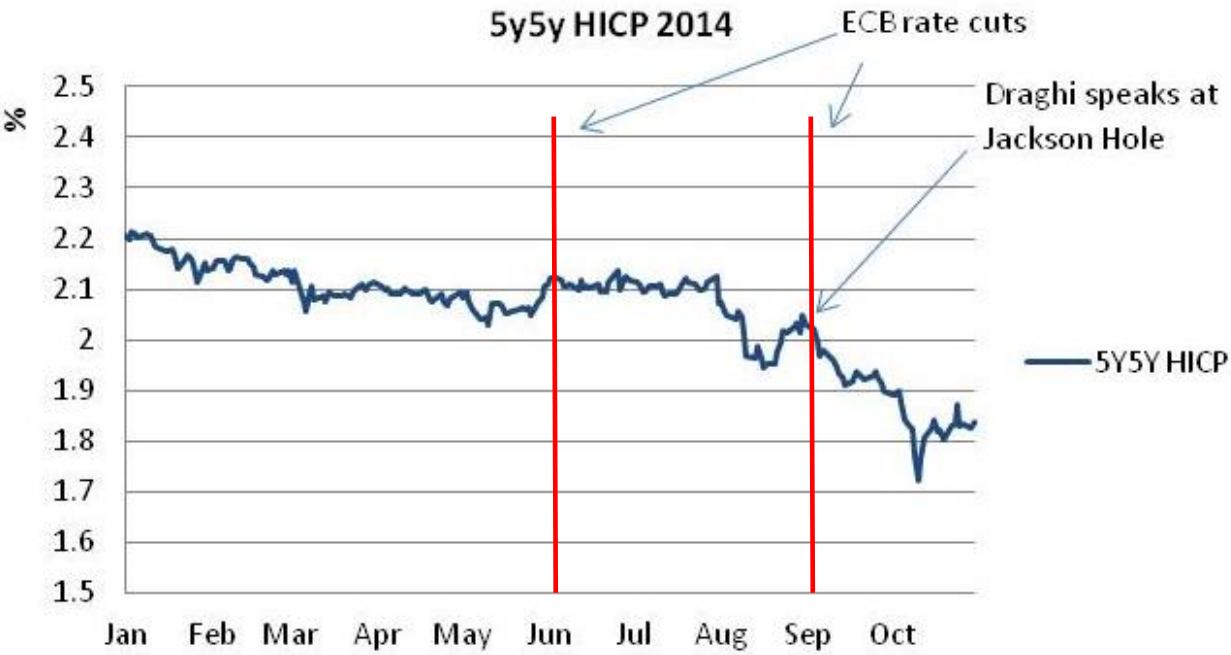
ECB Money Market Contact Group



21st November 2014

Sascha Weil, Head of Euro Liquidity Management

Inflation – Market Focus



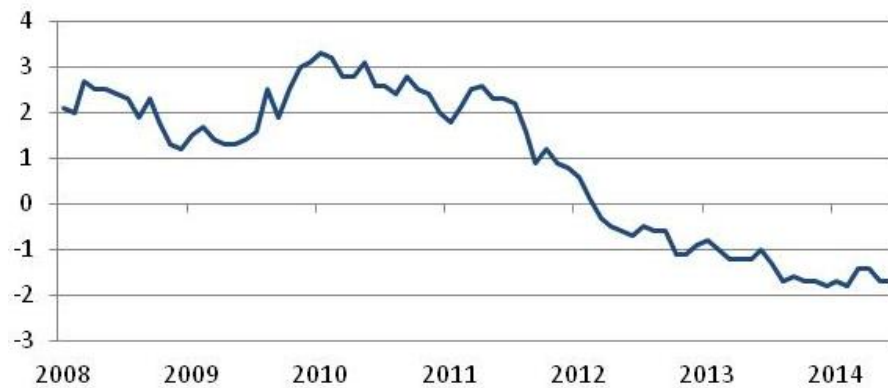
Goodhart's Law: *When a measure becomes a target, it can no longer be used as the measure.*

Since President Draghi noted that the 5Y5Y inflation curve was a key indicator for the ECB Governing Council the market has been focused upon it. The trend continues downward, prompting markets to speculate about further accommodative policies.

Source: Bloomberg.

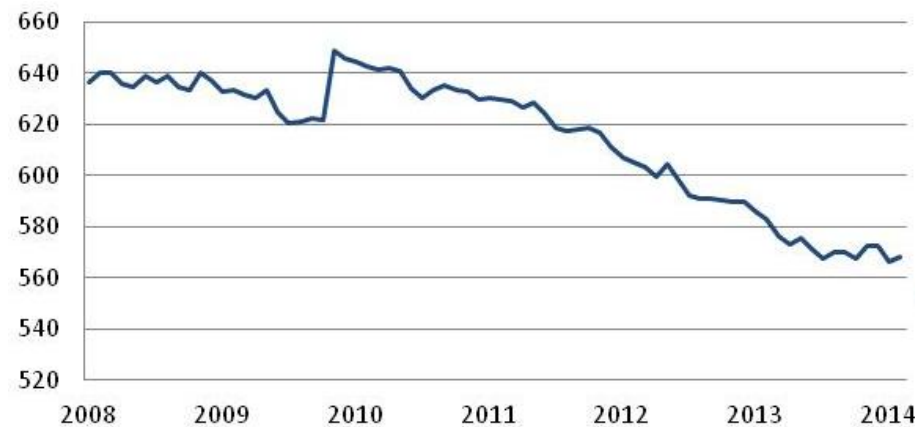
Credit in Decline

ECB Euro area MFI loans to households, annual growth rates %

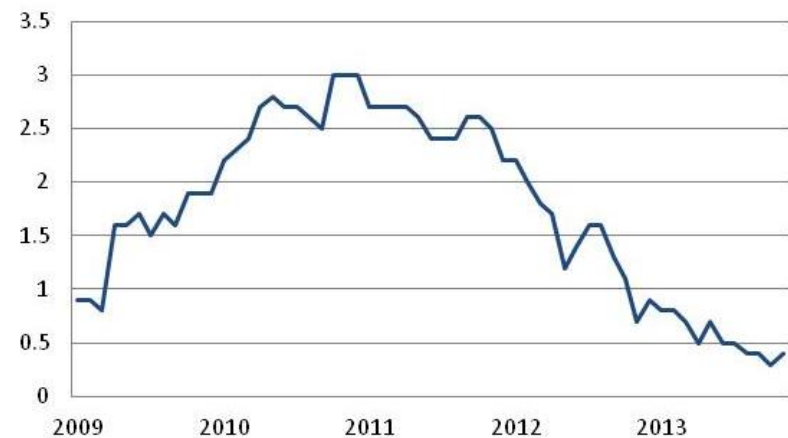


Credit supply remains constrained in the Euro Area. Demand for and supply of credit appear slack, with credit growth in negative territory.

ECB Euro area MFI loans to households, €bn



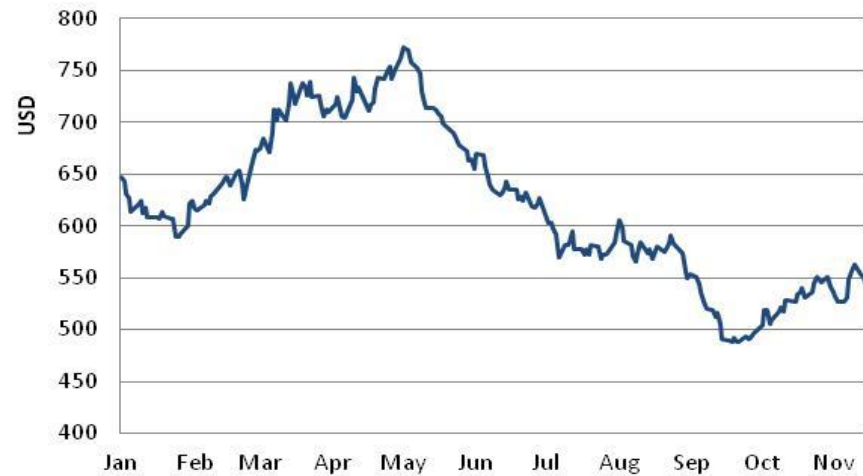
Eurostat Eurozone HICP (MUCIP YoY), %



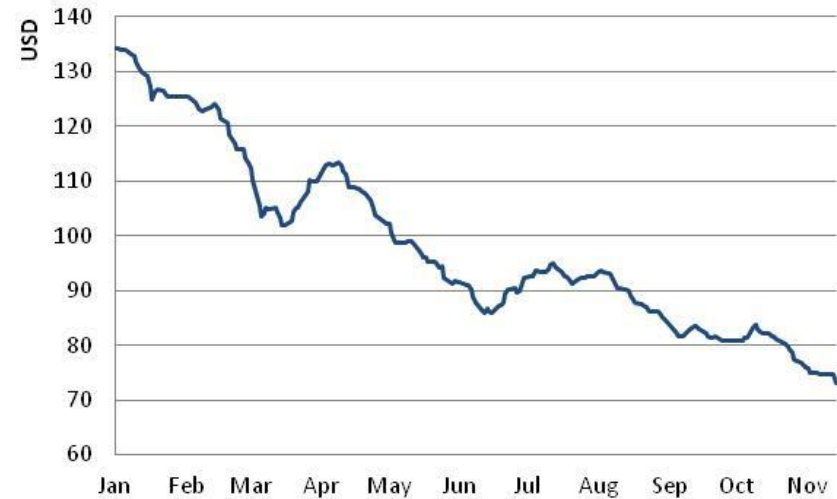
Source: Bloomberg.

Commodities: Continual Price Declines

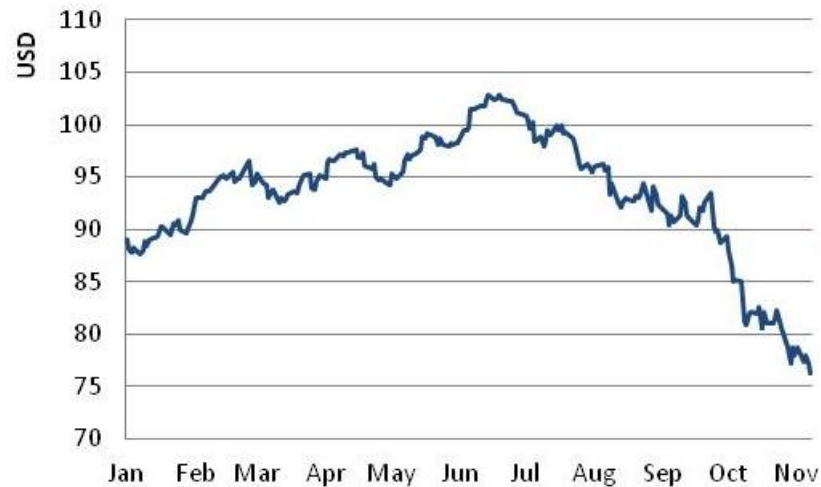
Wheat 2014



Iron Ore 2014



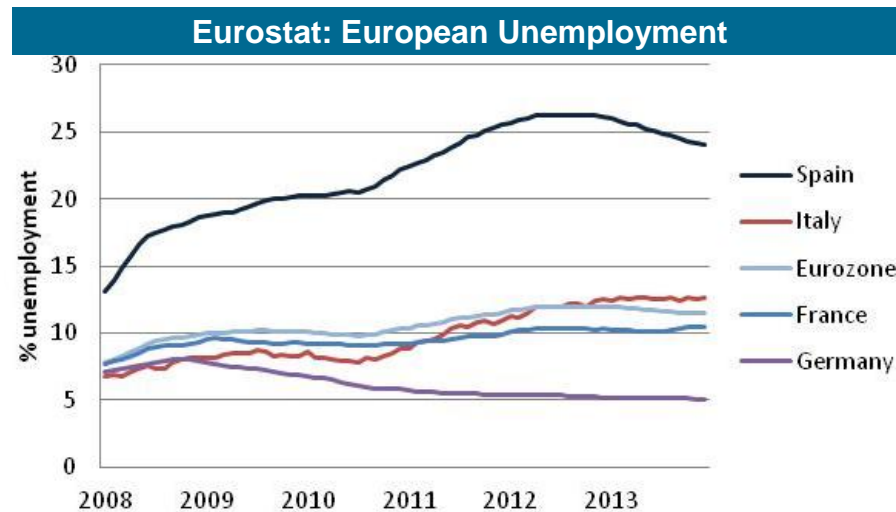
WTI crude 1st Future 2014



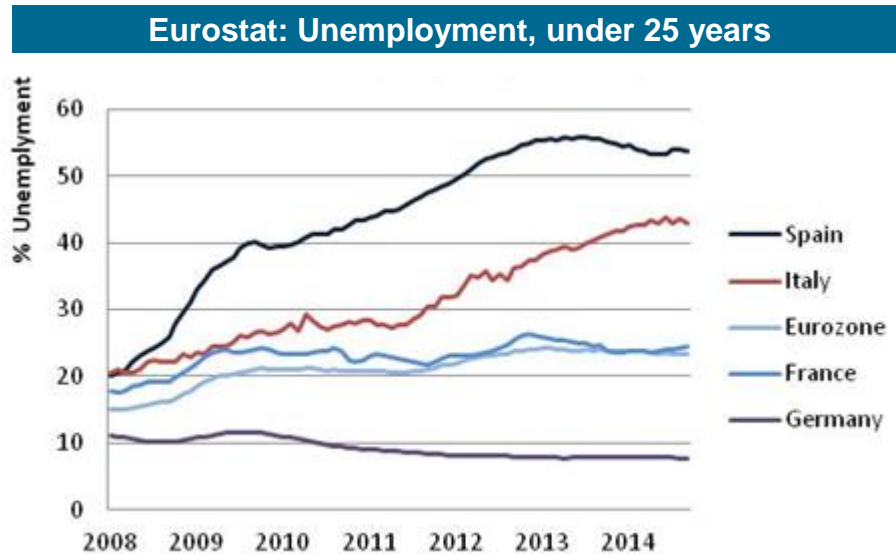
Commodity prices continue to decline, further adding to the disinflationary environment.

Source: Bloomberg.

Unemployment: Entrenched



Unemployment is slowly trending lower at a Eurozone level, however persistently elevated unemployment remains in Italy, France and Spain.

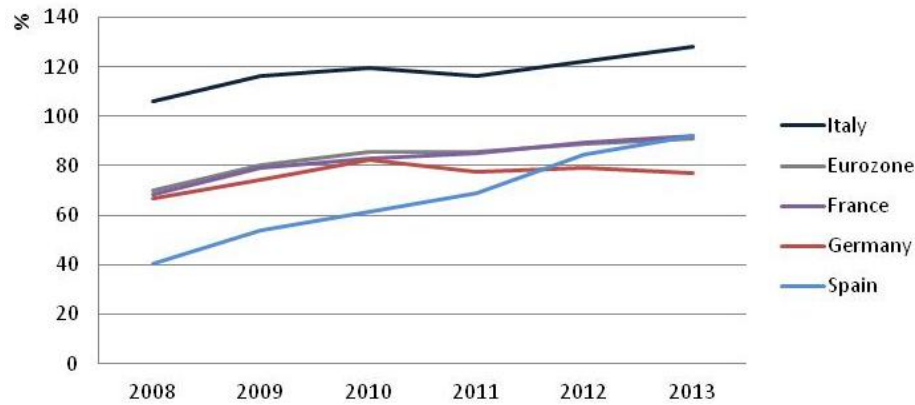


The unemployment of the under 25's across Europe is at chronic levels in Spain and Italy.

Source: Bloomberg, Eurostat.

Growth

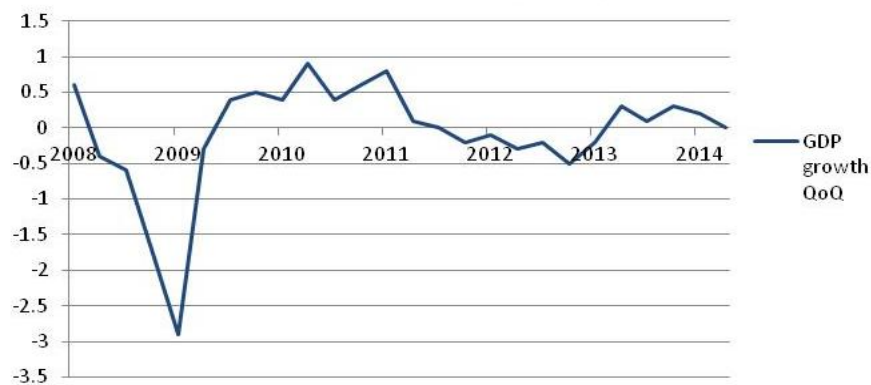
EURO Sovereign Debt: GDP Ratios



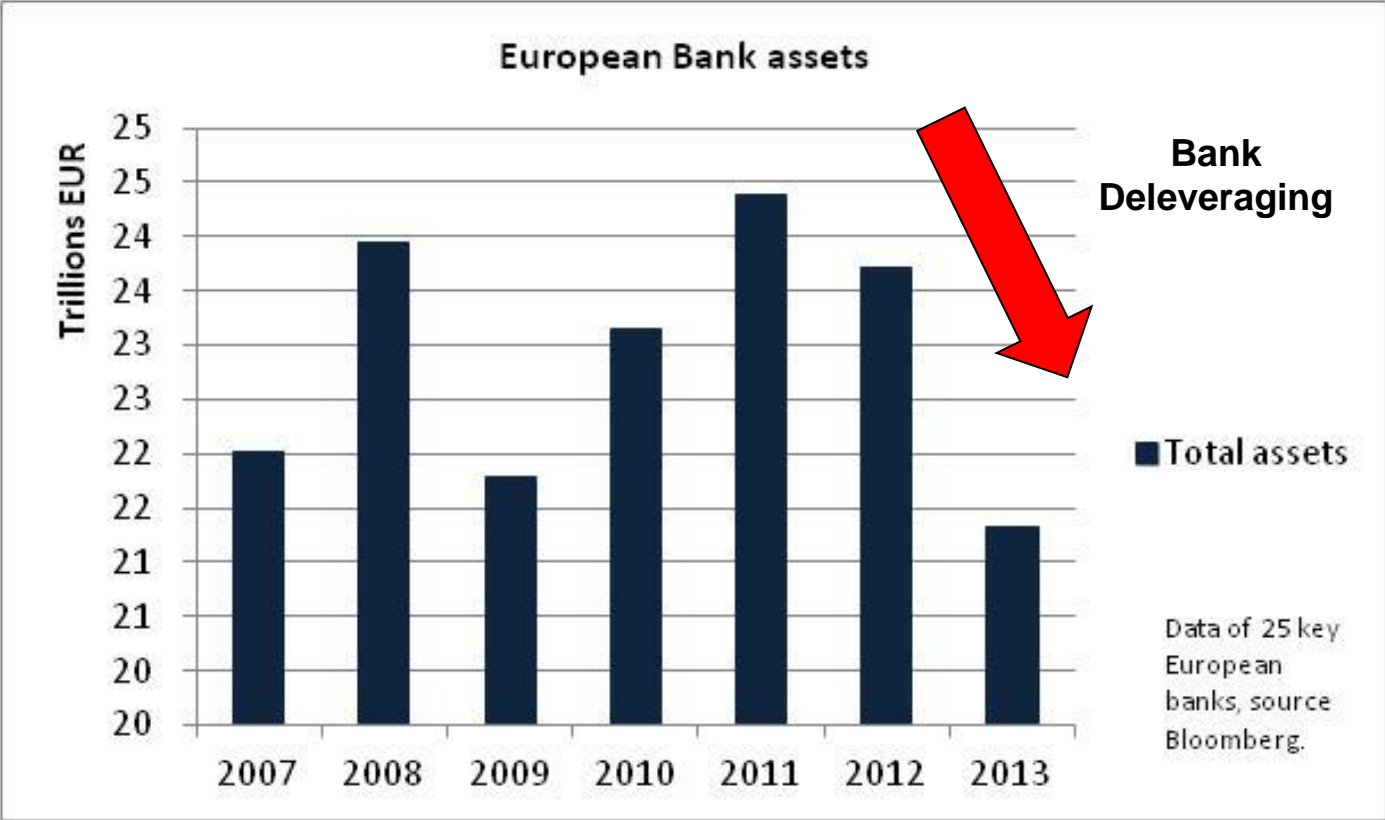
The rise of sovereign indebtedness poses a serious constraint to future growth. The Eurozone is trending towards non growth, while Debt: GDP ratios are rising in most European nations.

Note also 2015 Eurozone supply issuance is expected to increase by 220bn EUR vs 2014 (see slide 14)

Eurostat, Eurozone GDP Growth QoQ

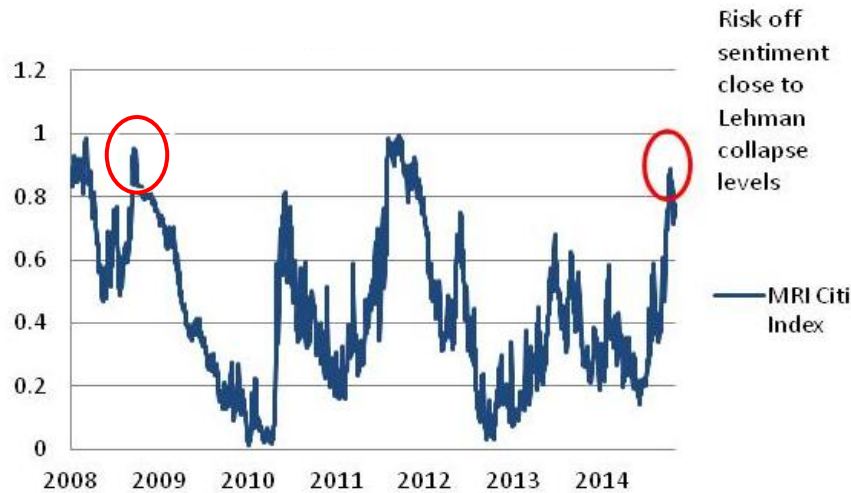


Bank Assets



Risk Indicators

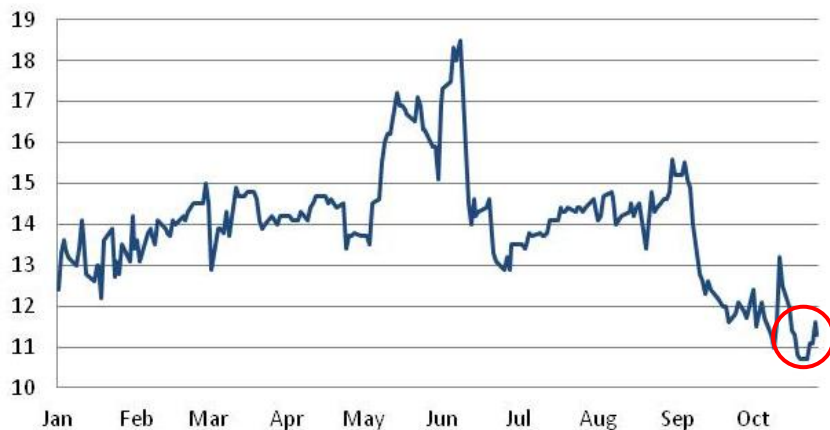
Risk Aversion / Macro Risk



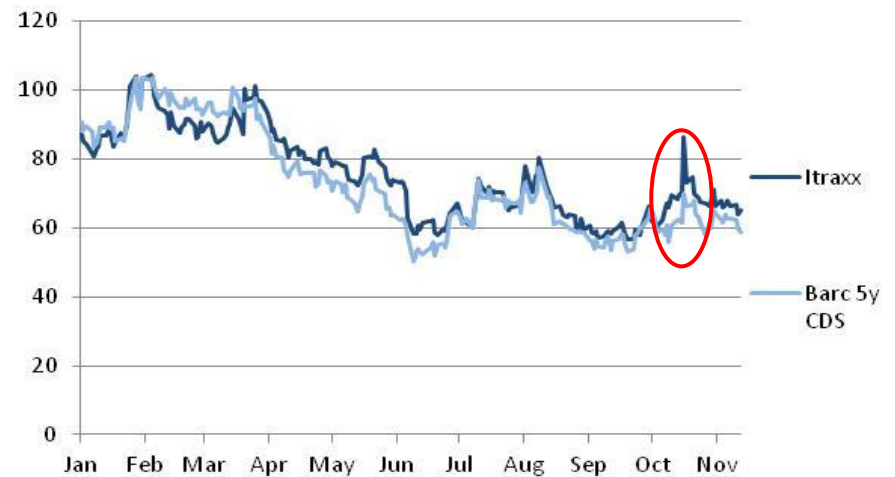
The Citi Index measure hit heights rarely seen since the collapse of Lehman Brothers in October 14, as a range of fears from Russia & ISIS to Ebola exacerbated a risk off move in Markets triggered by poor US retail sales.

In the context of banks deleveraging we are seeing outsized moves in risk.

IMM1 FRA-OIS Spread 2014



CDS Pricing 2014

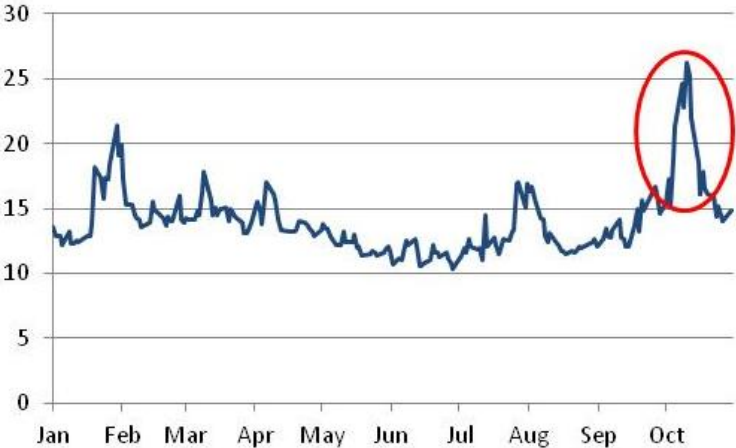


Source: Bloomberg.

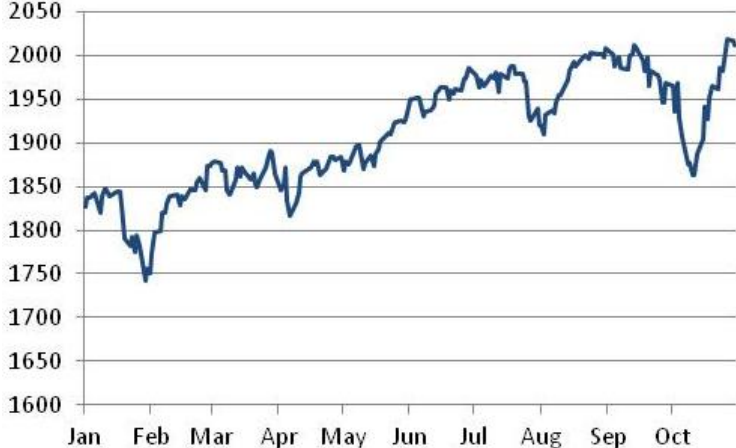
Equity Markets

Equity markets have been volatile in 2014

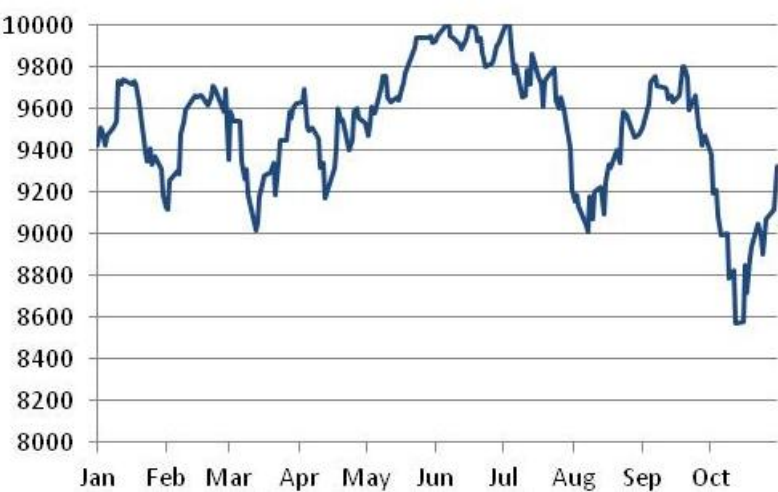
VIX 2014



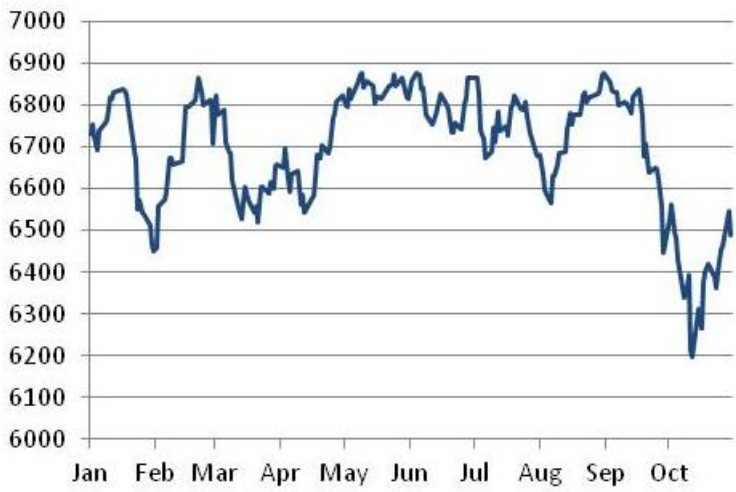
S&P 2014



DAX 2014



FTSE 100 2014

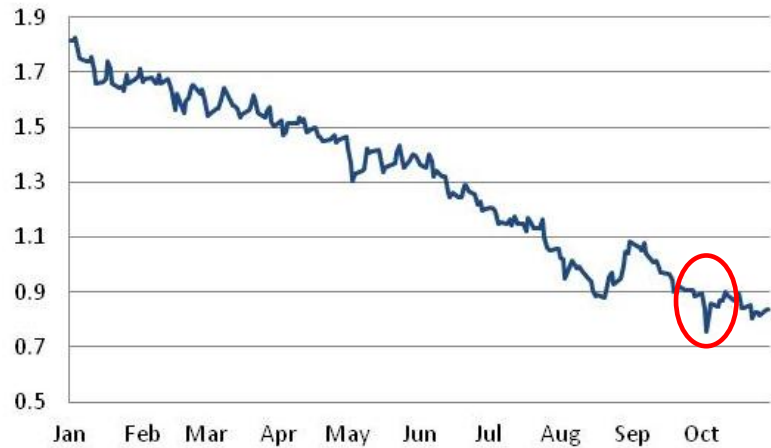


Source: Bloomberg.

Sovereign Credit

Interesting debt dynamics were noticeable during the recent market turbulence. As investors sought traditional safe havens, yields tumbled, but the German / France spread widened 10bps. Is the market perception of France as a core credit changing?

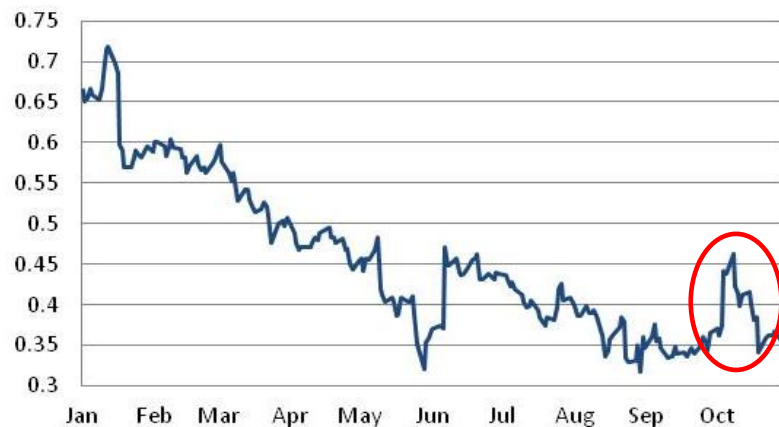
German 10yr Benchmarks 2014, %



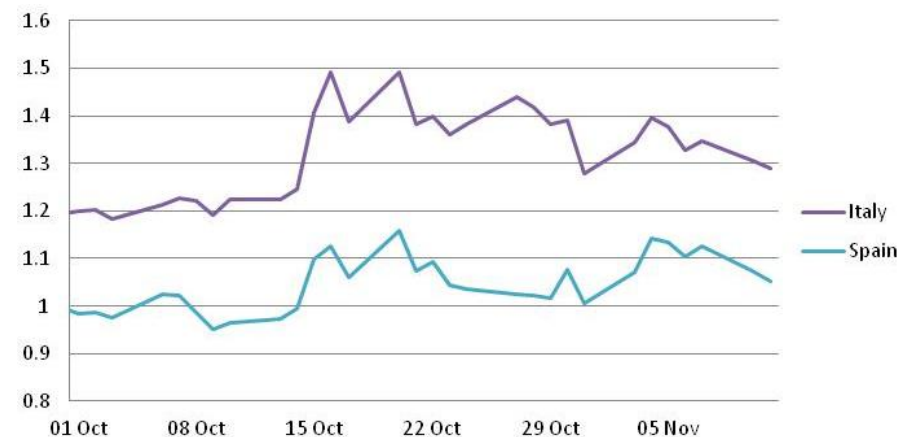
European 10yr Benchmarks on Asset Swaps, %



German French 10 yr Spread 2014, %



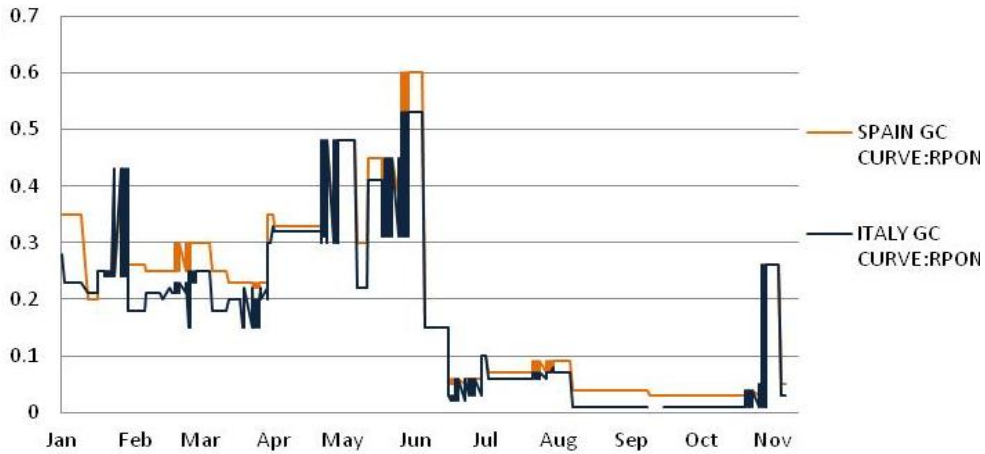
European 10yr Benchmarks on Asset Swaps, %



Source: Bloomberg.

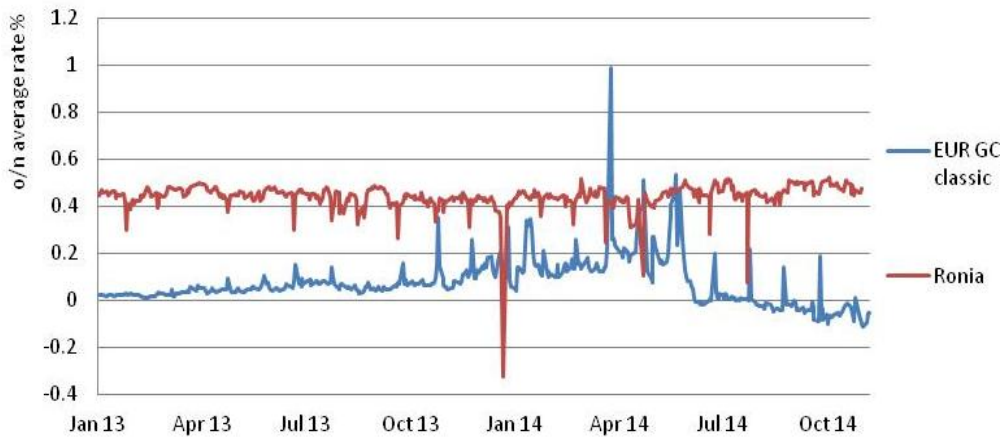
Repo Markets

Repo GC Levels 2014, %

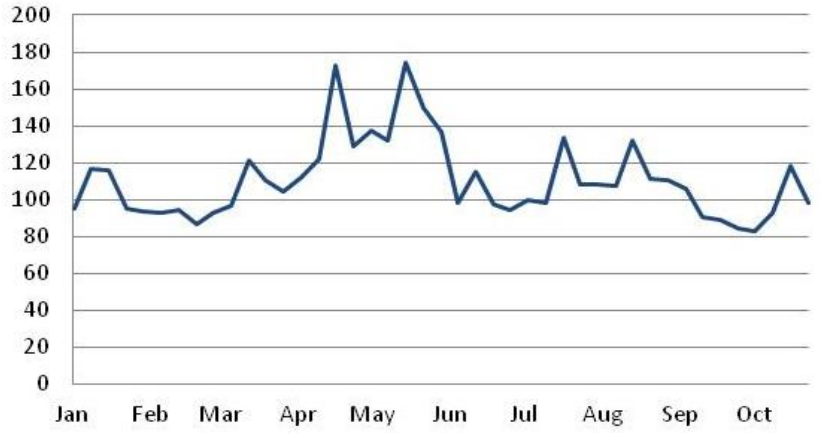


European repo market behaviour is notably different to UK repo market behaviour at month end, as balance sheet focus distorts pricing. The decline in the magnitude of month end spikes would tend to indicate a strengthening of bank balance sheets.

Overnight Repo Trends 2013/2014



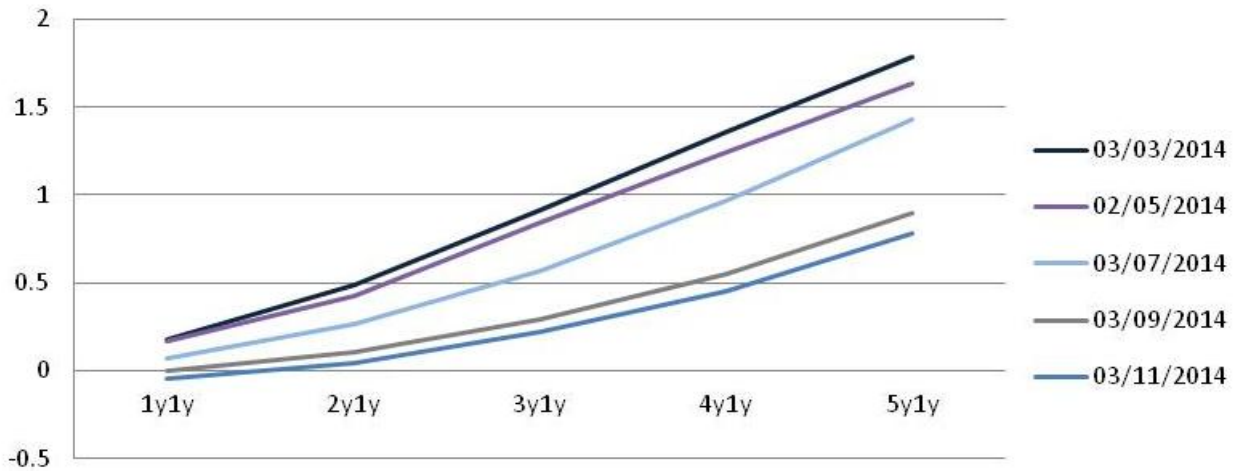
MRO Borrowing, €m



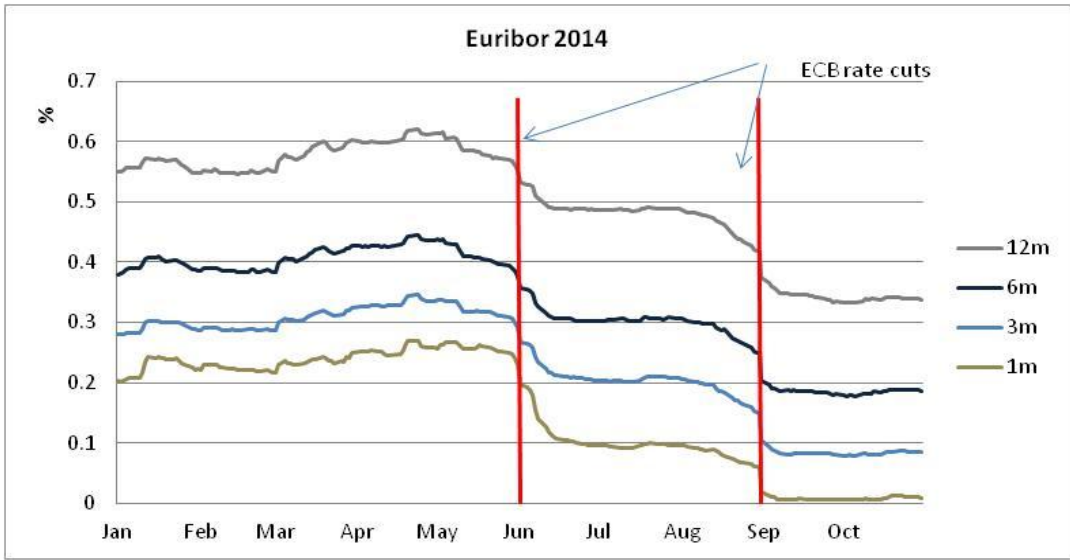
Source: Bloomberg.

ECB Measures: Forward Guidance is working

Forward Eonia 2014, %



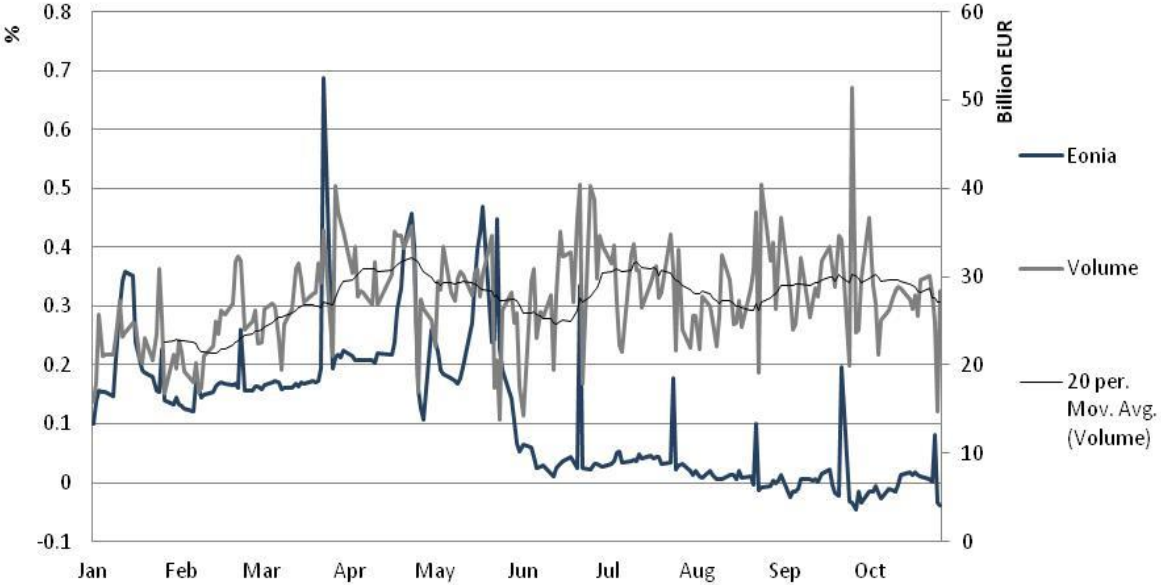
Euribor 2014, %



Source: Bloomberg.

Eonia Volumes

Eonia vs. Volume 2014



In spite of ECB Open Market Operations, notably the LTRO's, the volume in the Eonia market has not picked up markedly, suggesting interbank market participants are still unwilling to increase lending.

Source: Bloomberg.

Central Bank Balance Sheets

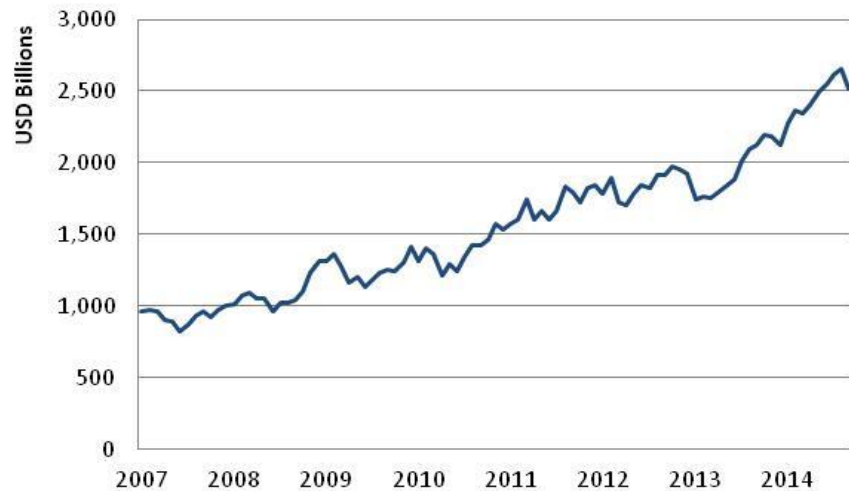
ECB Balance Sheet



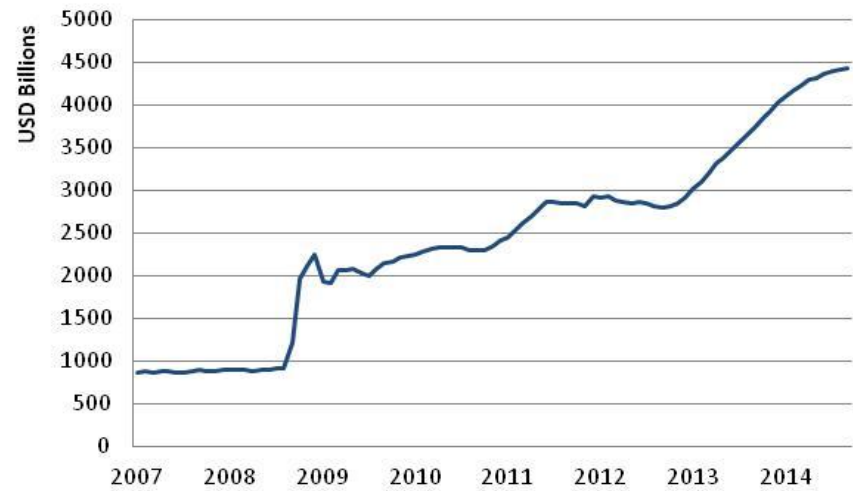
Both the FED and the BOJ have aggressively increased their balance sheets via QE programmes.

There has been lots of discussion about the ECB's balance sheet target, with the launch of CBPP3 and ABS expected shortly. Looking at 2015 supply (overleaf) Sovereign QE remains a possibility.

BOJ Balance Sheet

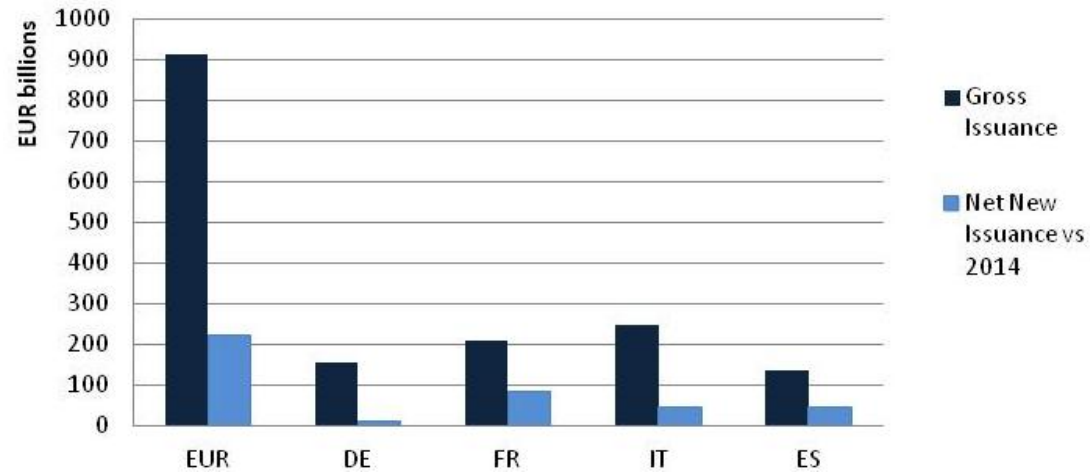


FED Balance Sheet



2015 Supply Outlook

European Debt Issuance 2015



Net new issuance of 221 bn EUR anticipated next year.

Scope if required for a meaningful Sovereign QE programme.

Source: Barclays Research.

Currencies

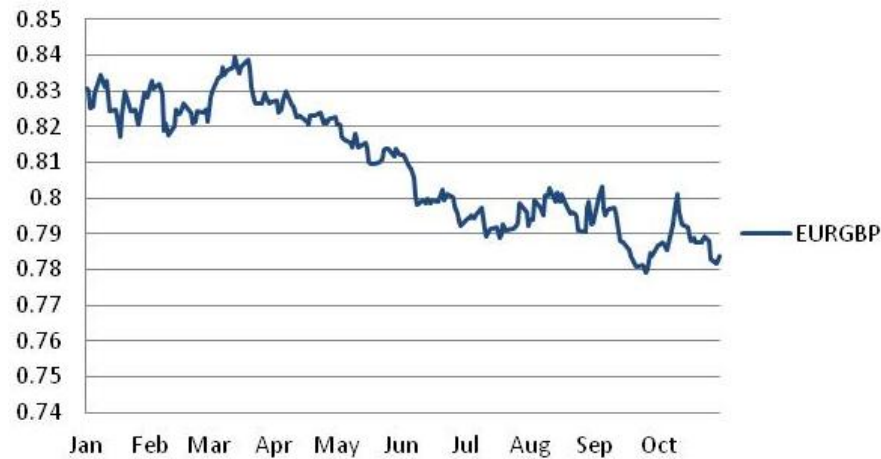
EURJPY 2014



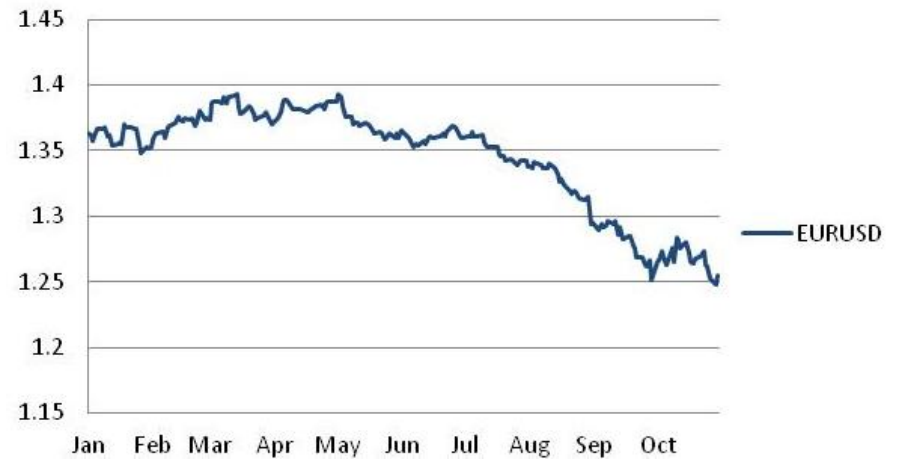
5y Cross Currency Basis, Key Currency Pairs



EURGBP 2014



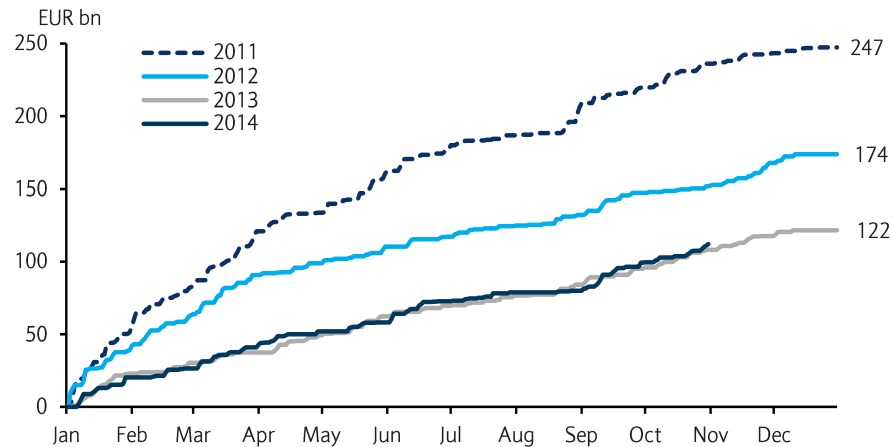
EURUSD 2014



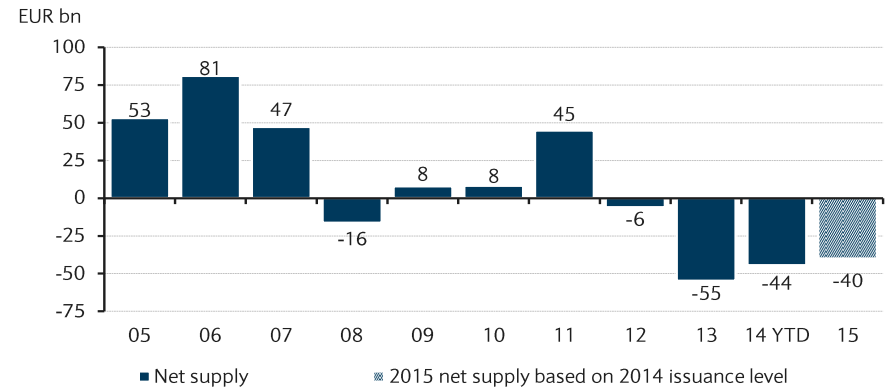
Source: Bloomberg.

CBPP3 – Will Add to Current Supply/Demand Imbalance

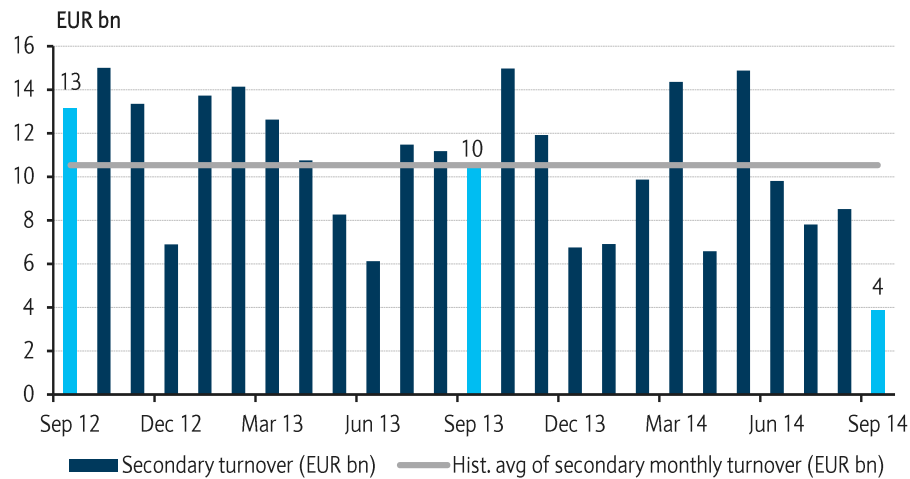
Global gross supply (benchmark covered bonds, major currencies)



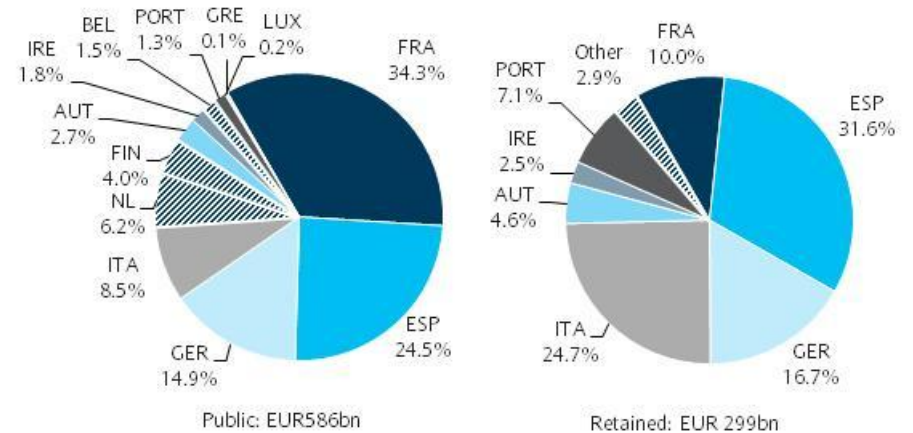
Euro area net supply of EUR benchmark covered bonds



Monthly secondary turnover (EUR)



Universe of CBPP3-eligible covered bonds

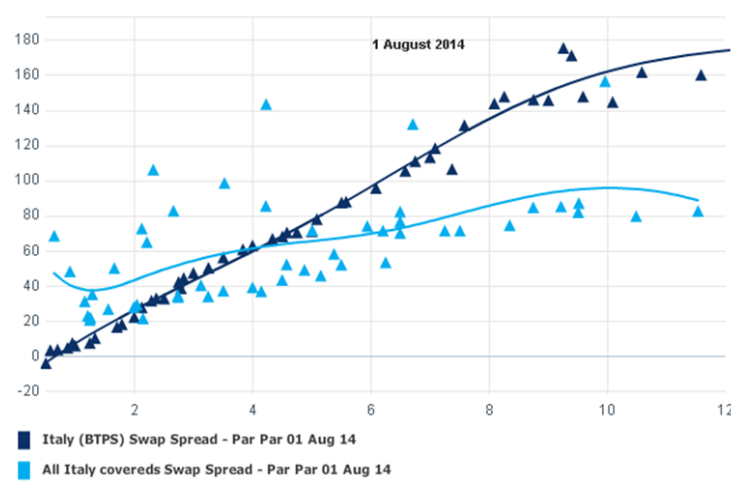
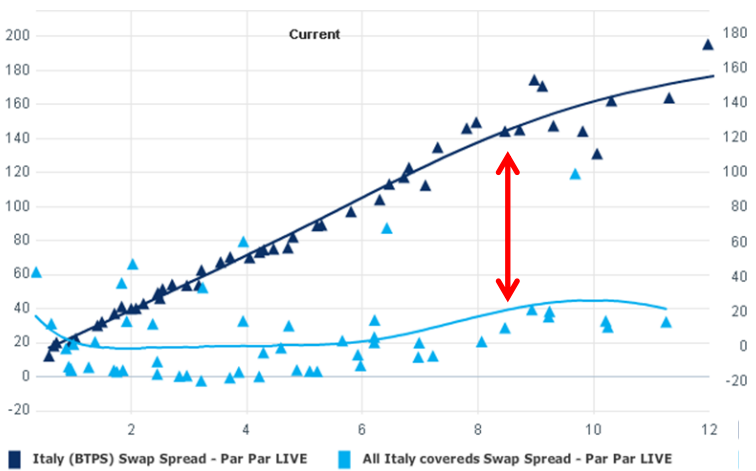
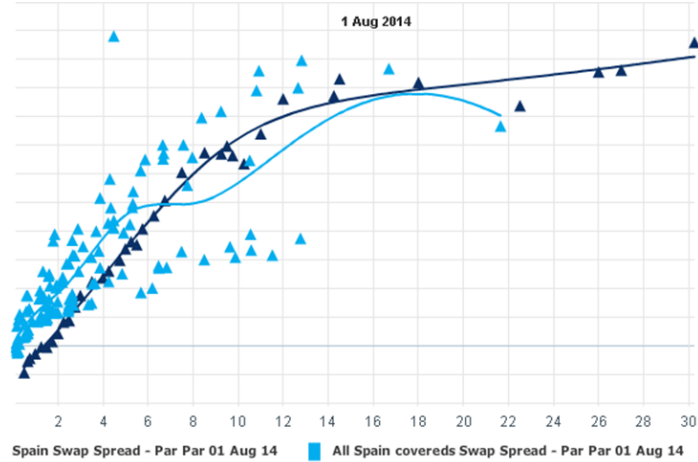
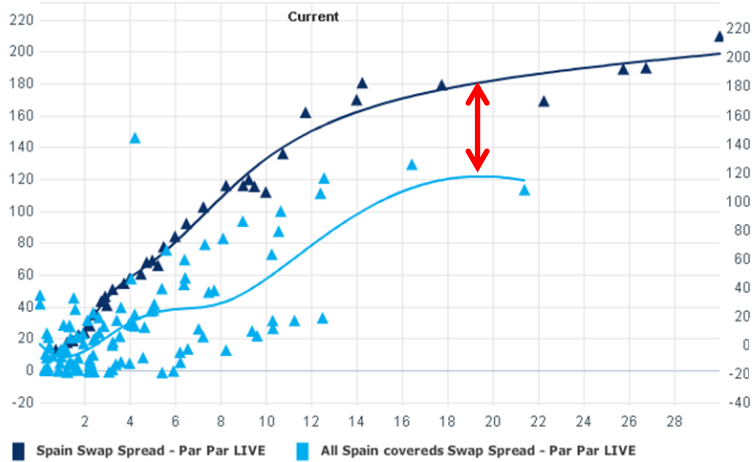


Source: Barclays Research.

CBPP3 – Pronounced Impact on Covered Bond Spreads

Current

1 August 2014



Source: Barclays Live.

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