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ECB BMCG Market Update

Christoph Rieger, 15 September 2021

Higher inflation – lower rates... at first!



Key developments since our last meeting:

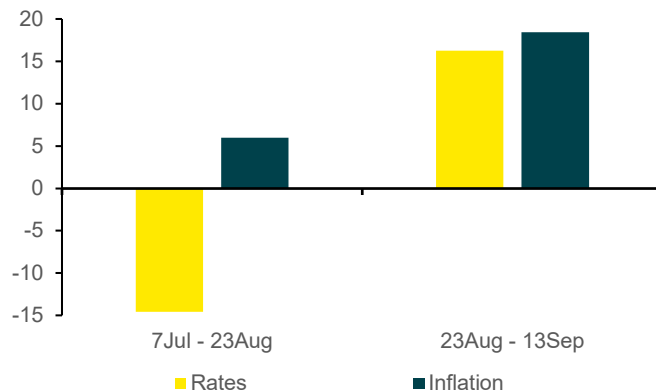
- 8 July: Results of **Strategy Review**
- 22 July: **New FG** on interest rates
- 24 August: **Lane** interview
- 31 August: **HICP** jumps to 3%
- 9 September: **PEPP** with “moderately lower pace”

What happened to the ECB members on their holidays? Date at which the first 10bp depo rate hike was fully priced in



Strategy review initially pushes back rate expectations despite higher inflation expectations...

Change in 3y3y €STR and ILS forward since strategy review and Lane interview, in bp

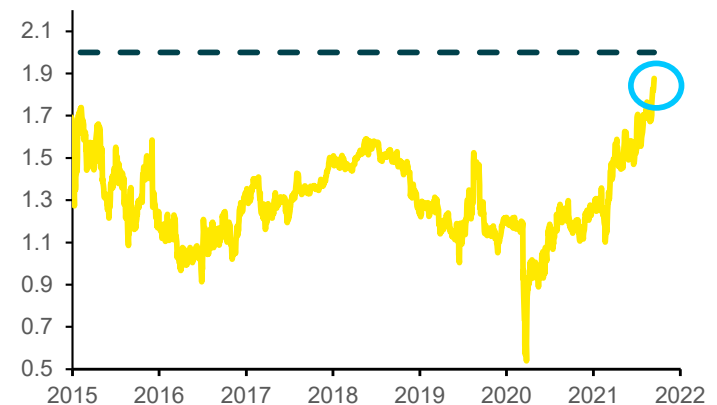


Source: Bloomberg, Commerzbank Research

20 September 2021

... but convergence is not yet complete!

2y1y forward/forward inflation at the time of lift-off (when first 10bp ECB depo rate hike was fully priced in), calculated from ILS adjusted for 8bp average ex-tobacco spread, in %



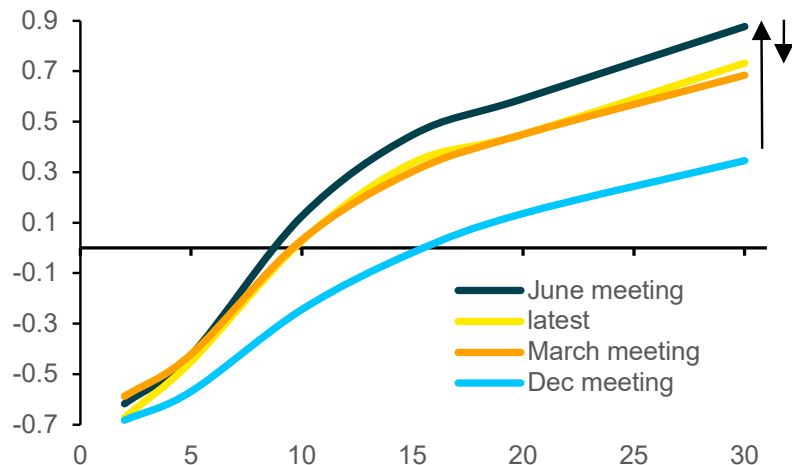
ECB stays in control!



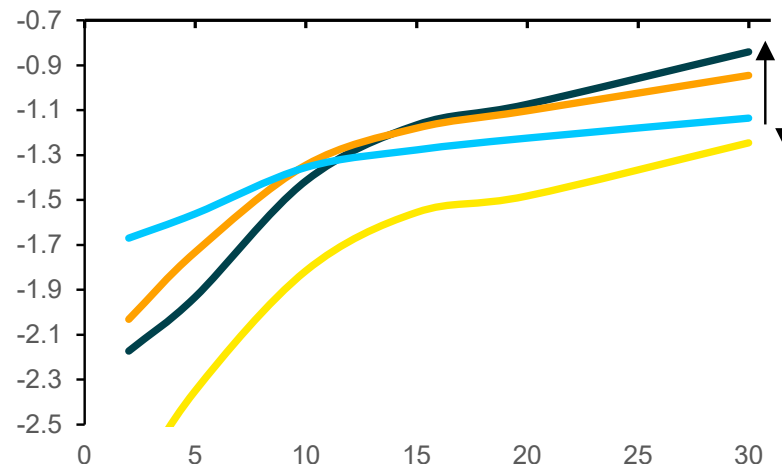
As ECB tries to cap nominal yields, real yields hit record lows!

GDP-weighted € sovereign yield curve, nominal and real yields (average nominal yield minus inflation swap), in %

nominal yields



real yields

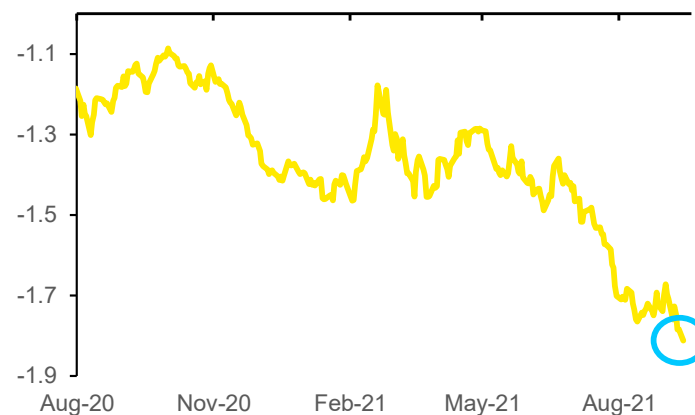


Joint assessment of financing conditions and inflation outlook:

Favourable financing conditions “can be maintained with a moderately lower pace of net asset purchases” under the PEPP than in the previous two quarters.

(ECB decision on 9 September)

€ 10y real swap rate, in %



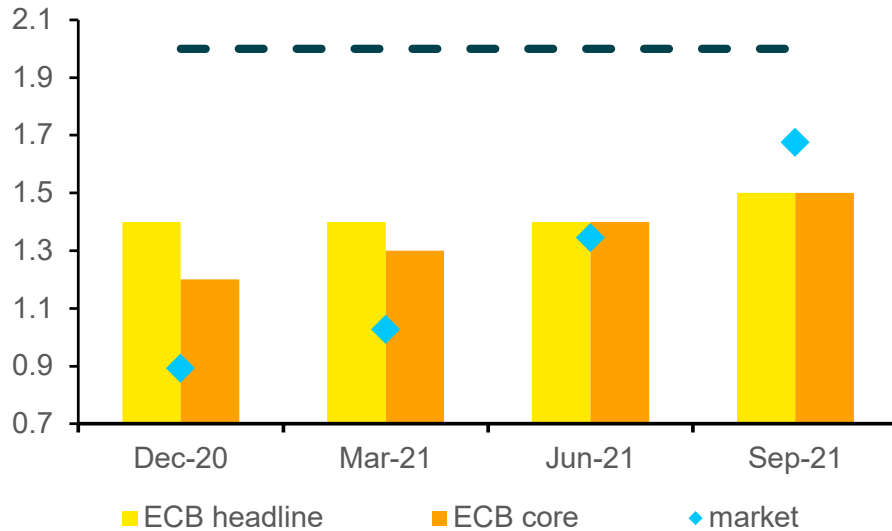
Source: ECB, Bloomberg, Commerzbank Research

Projections hold the key!



Right direction, but still missing the target!

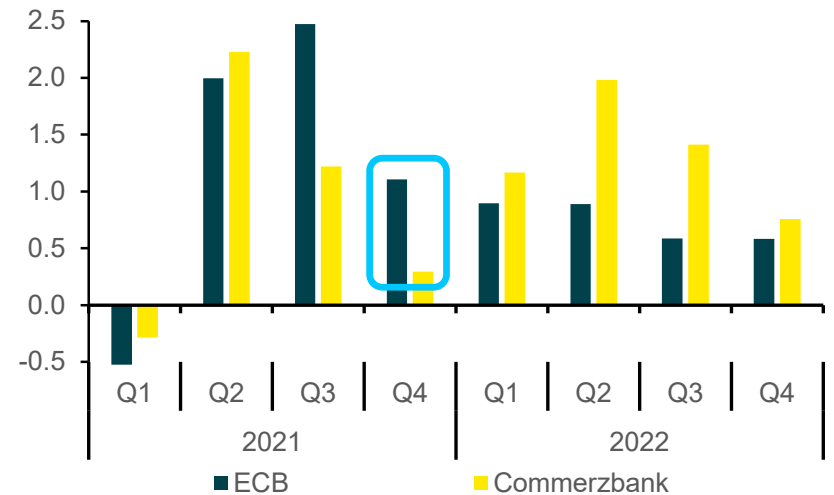
2023 ECB inflation projections and market forwards*, in %



*) using ILS on headline HICPx, adjusted for 8bp ex-tobacco difference and 3m lag in reference index. Forwards are calculated at cut-off date of ECB projections

ECB could be too optimistic on Q4 GDP!

ECB projections for euro area real GDP, Sep-21, q/q in %



Source: ECB, Bloomberg, Commerzbank Research

Discussion points:



- How would the market react to a wind-down of the PEPP until the end of March 2022?
- Are spreads exposed if the APP cannot inherit flexibility from the PEPP?
- Would it enhance transparency if the ECB communicates the intended monthly purchase pace of the PEPP?
- What will be the impact on issuance and spreads from the ECB climate change action plan?
- Should TLTROs become a permanent feature?
- How should the TLTRO and tiering parameters be recalibrated?

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I) Recommendations versus benchmarks:

Overweight (OW)	We expect outperformance versus the benchmark in spread and/or total return terms
Marketweight (MW)	We expect performance in line with the benchmark in spread and/or total return terms
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Benchmark:	Unless stated otherwise, the benchmark is the iBoxx € Corporate for IG-rated names/instruments, and the iBoxx € High Yield core cum crossover LC for HY-rated names/instruments

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Buy	We suggest entering / expanding positions in the relevant names/instruments
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Marketweight	44%	25%
Underweight	20%	18%

Source: Commerzbank Research

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Neutral	29%	0%
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Source: Commerzbank Research

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