

Market Comment | Bold ECB measures boost equity and credit markets

Global Financial Markets Unit 11 Mar 2016

 Bold ECB measures boost equity and credit markets. This week the focus was on the ECB's meeting and its new measures, which surprised markets positively, with sharp movements in the main financial variables. The ECB Governing Council decided: i) to cut the main policy rate by 5 bps to 0.0%, a historic low, the deposit facility rate by 10 bps to -0.40% and the marginal lending rate by 5 bps to 0.25%, ii) to expand the monthly purchases under the asset purchase program (APP) to EUR80 bn, iii) to broaden the scope of asset purchases (to now include investment-grade euro-denominated bonds issued by nonbank corporations) and iv) to introduce a new round of four-year TLTROs (see). The ECB announcement had a pronounced impact on the financial markets. The euro depreciated immediately after the announcement but turned higher after Mr. Draghi said that there is no reason to lower interest rate further, ending the week showing a strong appreciation against the main G10 currencies (USD 1,2%, JPY 1% BP 0.4%). With the ECB signalling that it does not intend to push interest rates deeper into negative territory, the 2Y German interest rate jumped (from -0.56% to -0.46%), narrowing its spread against the 2Y USD bond. The 10Y German Bund also increased (GER 10Y: +2 bps, France 10Y:+3 bps), while peripheral yields fell sharply (ITA 10Y:-14 bps SPA 10Y:-8 bps POR 10Y:-14 bps), narrowing European peripheral risk premiums (ITA 10Y:-16 bps SPA 10Y:-10 bps POR 10Y:-16bps). US bond rates also increased, underpinned by the advances in German rates, the rebound in oil prices (the IEA report said oil prices could rebound due to the current decline in oil production) and the recent upbeat US data, which boosted the probability of an interest rate hike at the FOMC June meeting (to 40% from 32%). Apart from this, the ECB's new TLTRO improves banks' funding, as borrowing conditions can be as low as the deposit facility, while the extension of the ECB asset purchase programme to non-bank euro corporate debt may also improve funding conditions for IG European corporates. Against this background, both European bank and corporate debt reacted positively after the announcement, with the synthetic CDS index narrowing, especially for the higher risks (iTraxx Europe -17 bps, iTraxx financial senior -17 bps, iTraxx financial subordinated -39 bps and x-crossover -51bps). Moreover, euro zone banks' stocks also surged, driving equity indices higher. European equity markets rose in the week with the exception of the DAX (Eurostoxx:+1.1% IBEX:+3.3% DAX:-0.1% CAC:+0.7%). Meanwhile, US equity indices remained almost unchanged (S&P:+0.7% Dow:+1.1%) waiting for next week's Fed meeting. Asian markets dropped led by China (Nikkei:-0.4%) dragged down by worse-than-expected trade data. The USD depreciated against other major currencies, especially against the euro, which rebounded during Mario Draghi's speech (EUR: 1.39% GBP:1.15%. EM currencies appreciated against the US dollar (RUB: +2.6% BRL:+3.8% PEN:+2.2% MXN: +0.4%) boosted by the oil price rally in the week (Brent:+3.4% Wtx:+6.3%) and underpinned by better-than-expected weekly inventories data and the IEA announcement.

FOMC preview

• The March FOMC meeting will hopefully provide some significant details on the future of Fed policy. While we do not expect another rate increase this month, we are likely to see some changes in the



FOMC's economic projections. In particular, the Committee is likely to revise down their projected path of interest rates - probably to just three instead of four rate increases in 2016. Furthermore, Chair Yellen's press conference will likely touch on the latest developments in global financial markets and how much the ongoing volatility has really impacted the Fed's outlook. She is also likely to clarify some other lingering concerns such as inflation and negative interest rates. Overall, we maintain our expectations for the next rate increase in June.

Update 17.30 CET 11 March, 2015 Table1



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Fuente: BBVA Research

*CDS, EMBI & MSCI indices with one day delay
**Credit spread (BAA) with two days delay
***S&P GSCI with one day delay

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