

Flash Note 06/08/2018

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Eurozone - Two sides of the same coin

Sustainability

- German government debt falls below \$2T, reinforcing its reputation for good housekeeping and fiscal discipline, as a combination of surging fiscal revenues and low interest spending pushed its total government debt below €2T. German debt fell last year by 2.1% or €42.1B, to €1.97T (statistics office), and it was the first time, since the current method of calculation was introduced in 2010, that the debt level had dipped below the €2T threshold.
- Meanwhile, Italian bond yields & risk premium rose sharply in the last two days, with yields on the 10-year benchmark moving above 3% for the first time since early June. This shift came as a result of a key meeting today on the 2019 budget with focus on the new government's plan for fiscal expansion. Ahead of the meeting Deputy PM Salvini said the budget would include tax cuts and changes in Renzi's pension reform (which means higher deficit). Both of moves will likely increase Italy's large public debt, since the government has so far not detailed spending cuts yet.
- For his part, the IMF says Greece's longer term debt prospects remain uncertain. In its annual report on Greece, it highlighted that while it has successfully eliminated its extraordinarily high fiscal and current account deficits, the official sector debt will gradually be replaced by more expensive market debt, so Greece's ability to service its debt will gradually become more challenging.

Politic - Too much diachrony to have a moment of calm

- Germany - Support for Merkel's bloc hits record low while populist AfD is now at new high: The latest opinion showed support for Chancellor Merkel's conservative bloc has slumped to a record low, with support for the far-right Alternative for Germany (AfD) hitting a record high. The ARD DeutschlandTrend survey put support for Merkel's conservative alliance at 29% percent, down one point from the beginning of July. AfD gained one point to 17%.
- French Government survived two no confidence votes this week. Politico reported that the Benalla scandal, which has rocked French President Macron, took center-stage in parliament Tuesday as lawmakers debated two votes of no-confidence in the government. The first, brought by Macron's opponents on the right, was easily defeated. It won the support of 143 MPs, far short of the 289 needed. The second, a proposal from the left, received even less support, just 74 votes.

- Spain – Socialist leader Sanchez could call elections in the fall (El Confidencial). The report noted that for now Sanchez has dismissed the possibility of an election, but the polls signal a rise in support for the party and it underpins the view of some in his party, who think a vote in the fall could be positive. According to a poll by the Sociological Research Centre, Spain’s Socialists would easily win a general election if a vote were held, taking 29.9% of the vote.

Financial market’s Assessment & outlook

- European Equity market (Stoxx Europe 600): Positive (year end target for the index at 411. Currently at 388)
- 10Year German Government Bond: Negative (Entry point at 0.80%. Currently at 0.42%)
- 10Year Spanish Government Bond: Negative (Entry point at 1.60%. Currently at 1.4%)
- 10Year Italian Government Bond: Positive (Entry point at 2.70%. Currently at 3%)
- EUR/USD: Short-Term Neutral (target at 1.15); Long-Term view Negative (on EUR)

Best