

8 June 2020 /// n°23-2020

## Short sellers capitulate

### Key Points

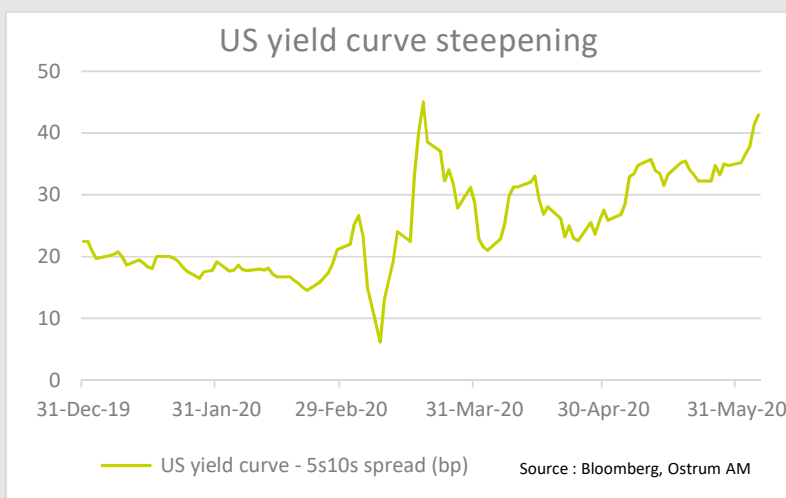
- **European equity markets post double-digit returns last week**
- **ECB adds 600mds € to PEPP**
- **Fed may opt for yield curve control**
- **Considerable tightening in spreads**

Equity short sellers seem to have capitulated. The S&P 500 index hovers about the 3200 mark amid short covering. Sentiment vis-à-vis European stock markets has considerably improved since the EU recovery plan proposal. The main European indices made gains in the vicinity of 10% last week. Cyclical value stocks and banks are being bought. This time round, bond yields have indeed risen sharply in response to the risk asset rally. The 10-year yield on Treasuries is now trading above 0.90%. A new round of ECB easing (600b increase in PEPP) slowed the rise in Bun yields and sparked a sharp narrowing in sovereign spreads. At \$1.13, the euro's rise

emphasizes investor confidence in the euro area. The dollar remains weak ahead of the FOMC decision. A yield curve policy may be debated this week.

Credit markets remain well oriented, buoyed by strong final demand and increased central bank support. Credit spreads narrowed by more than 20bp last week and more significantly in speculative-grade markets. Emerging debt denominated in US dollars also rallied with spreads well within 500bp vs. Treasuries.

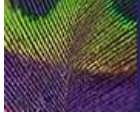
### Chart of the week



The FOMC will meet this week. A yield curve control may be debated this week.

This policy consists in targeting long-term rates in an attempt to anchor market expectations and ensure low-cost funding of deficits. Under this monetary regime, rate volatility will likely fall thanks to the conditional support of Central Banks.

The sharp widening in 5s10s spreads may indicate that markets expect the Fed policymakers to target 5-year bond yields.



## Short sellers capitulate

Is irrational exuberance reemerging in financial markets? Dollar depreciation is funding positions in risk assets including equities, energy commodities, credit or even CLO tranches. The 2009 carry trade may be repeating itself. Unprecedented liquidity provisioning by the Central Banks remains the main driver of the violent rise in risky asset prices since their low point in March. Excess asset demand induced by monetary easing is catching off guard the bearish consensus, which had built up as activity plunged. The speculative net short positioning in stocks on S&P futures diminished last week from extreme levels. Hence, pessimistic investors are capitulating. The unwinding of positions has sparked large swings in asset prices with no relation to underlying fundamentals. Yet, the latest economic releases suggest that April was indeed the low point in the cycle. Service activity has improved in China (55). Most European surveys have initiated a rebound linked to the gradual easing of lockdown measures in several countries. In the US, the employment situation turned out to be better than expected in May although the gap between the ADP estimate (2.7mn jobs lost in May) and the BLS non-farm payroll data of 3mn private jobs added, reflecting a sharp reduction in temporary unemployment.

## The ECB expands PEPP, the Fed may opt for yield curve control

The ECB raised the amount of asset purchases adding €600b to the PEPP scheme started in March. The asset purchase program now totaling €1.35T will run until June 2021. Reinvestments of PEPP bond proceeds are expected until the end of 2022. Excess liquidity will also increase after the new TLTRO-III. The transaction may add €800b to the financial system. On this note, the ECB did not alter the tiering system of bank reserves which exonerates banks from the negative deposit rates despite increased excess liquidity. Adjustment at a later date remains likely.

Markets will pay attention to the Fed meeting which may opt for long-run Treasury yield targeting. The policy will aim at preventing a disorderly yield increase. The targeted yield may be a 5- or 10-year rate. The objective is also limit balance sheet growth at a time when Fed total assets surpass \$7T.

## Constructive sentiment on euro area

In terms of strategy, the sharp rise in equity markets was fueled by short covering. The capitulation of pessimistic investors resulted in a 10% weekly on the French CAC 40 for instance. Investor sentiment towards European equities has greatly improved so that non-resident accounts are again accumulating

holdings in euro area stocks. The euro exchange rate is up to 1.13\$. The other new element pertains to asset allocation flows. Until recently, rising equity markets has not weighed on bond yields. Bond funds are now experiencing outflows which fund inflows into risky assets. In the US, Treasury bond ETFs recorded their first week of outflows last week since the outbreak of the crisis.

In fixed income markets, bund yields notably rose in the wake of the US Treasury market. The yield on German benchmark bond hit -0.28%. The recovery fund proposed by the European Commission, which remains to be validated, will require large issuance of EU bonds which will compete with Bunds. This may have added upward pressure on German bond yields. The ECB's decision to ease policy still helped bunds outperform US 10-year notes (+12bp vs. +26bp). Besides employment numbers, the market may be testing the Fed's commitment to keep yields low even as negative Fed Funds rates appear off the table. The Fed will take no chance on market volatility. This situation argues for a long stance on US Treasuries as 10-year note yields hover about 0.90%. Curve steepening continues, and 30-year yields may increase further. Gilts performed in line with Bunds. It is worth keeping in mind that the BoE does not rule out negative rates. In Japan, whilst 10-year yields oscillate about 0%, the 10s30s spread has room to widen out in keeping with the US backend.

Sovereign spreads have continued to narrow after the European Commission launched its proposal for a recovery fund. The spread on Italy is now around 170bp on 10-year maturities. The syndication of 2030 BTP drew investor demand in excess of a €100b. Positioning surveys point to significant final investor over-exposure to peripheral sovereign bond markets. In turn Portugal and Spain bonds are trading within 90bp.

Credit markets are benefitting from the risk-on environment. Spreads on investment grade corporate bonds narrowed by 36bp (spreads vs. Bunds) with financials outperforming slightly. In the US, the average IG spread has now shrunk to 146bp from over 375bp at the height of the financial stress. The rally in spreads accelerated in the past two weeks as the Fed started credit bond purchases as announced back in March. The high yield market also performed very well. Yield premiums have adjusted lower, including in synthetic markets. The iTraxx Crossover index is now trading within 350bp. Lastly emerging bonds participates to the broad-based rally in risky assets. The depreciation in US dollar does facilitate the implementation in carry strategies on external debt and emerging market fund inflows have indeed picked up of late.

## Main Market Indicators

| <b>G4 Government Bonds</b>         | <b>08-Jun-20</b> | <b>-1wk (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
|------------------------------------|------------------|------------------|-----------------|-----------------|
| EUR Bunds 2y                       | -0.62 %          | +4               | +16             | -1              |
| EUR Bunds 10y                      | -0.32%           | +9               | +22             | -13             |
| <b>EUR Bunds 2s10s</b>             | <b>30 bp</b>     | <b>+5</b>        | <b>+6</b>       | <b>-12</b>      |
| USD Treasuries 2y                  | 0.21 %           | +6               | +6              | -136            |
| USD Treasuries 10y                 | 0.87 %           | +21              | +19             | -105            |
| <b>USD Treasuries 2s10s</b>        | <b>66 bp</b>     | <b>+16</b>       | <b>+13</b>      | <b>+31</b>      |
| GBP Gilt 10y                       | 0.33 %           | +10              | +10             | -49             |
| JPY JGB 10y                        | 0.05 %           | +4               | +5              | +6              |
| <b>€ Sovereign Spreads (10y)</b>   | <b>08-Jun-20</b> | <b>-1wk (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
| France                             | 37 bp            | -1               | -13             | +7              |
| Italy                              | 172 bp           | -17              | -67             | +12             |
| Spain                              | 87 bp            | -11              | -47             | +21             |
| <b>Inflation Break-evens (10y)</b> | <b>08-Jun-20</b> | <b>-1wk (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
| EUR OATi (9y)                      | 51 bp            | +9               | +21             | -               |
| USD TIPS                           | 126 bp           | +7               | +14             | -53             |
| GBP Gilt Index-Linked              | 293 bp           | -1               | +12             | -18             |
| <b>EUR Credit Indices</b>          | <b>08-Jun-20</b> | <b>-1wk (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
| EUR Corporate Credit OAS           | 132 bp           | -36              | -58             | +39             |
| EUR Agencies OAS                   | 51 bp            | -9               | -23             | +7              |
| EUR Securitized - Covered OAS      | 41 bp            | -7               | -27             | 0               |
| EUR Pan-European High Yield OAS    | 496 bp           | -79              | -180            | +192            |
| <b>EUR/USD CDS Indices 5y</b>      | <b>08-Jun-20</b> | <b>-1wk (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
| iTraxx IG                          | 60 bp            | -10              | -24             | +16             |
| iTraxx Crossover                   | 338 bp           | -77              | -174            | +131            |
| CDX IG                             | 66 bp            | -12              | -25             | +21             |
| CDX High Yield                     | 438 bp           | -80              | -199            | +158            |
| <b>Emerging Markets</b>            | <b>08-Jun-20</b> | <b>-1wk (bp)</b> | <b>-1m (bp)</b> | <b>YTD (bp)</b> |
| JPM EMBI Global Div. Spread        | 460 bp           | -55              | -135            | +170            |
| <b>Currencies</b>                  | <b>08-Jun-20</b> | <b>-1wk (%)</b>  | <b>-1m (%)</b>  | <b>YTD (%)</b>  |
| EUR/USD                            | \$1.129          | +1.46            | +4.19           | +0.57           |
| GBP/USD                            | \$1.268          | +1.76            | +2.21           | -4.37           |
| USD/JPY                            | ¥108.61          | -0.95            | -1.8            | -0.03           |
| <b>Commodity Futures</b>           | <b>08-Jun-20</b> | <b>-1wk (\$)</b> | <b>-1m (\$)</b> | <b>YTD (\$)</b> |
| Crude Brent                        | \$41.0           | \$2.7            | \$8.9           | -\$22.0         |
| Gold                               | \$1 691.8        | -\$47.1          | -\$10.9         | \$169.0         |
| <b>Equity Market Indices</b>       | <b>08-Jun-20</b> | <b>-1wk (%)</b>  | <b>-1m (%)</b>  | <b>YTD (%)</b>  |
| S&P 500                            | 3 208            | 5.09             | 9.61            | -0.60           |
| EuroStoxx 50                       | 3 366            | 9.48             | 15.87           | -10.02          |
| CAC 40                             | 5 183            | 8.83             | 13.93           | -13.30          |
| Nikkei 225                         | 23 178           | 5.06             | 14.86           | -2.02           |
| Shanghai Composite                 | 2 938            | 0.77             | 1.47            | -3.68           |
| VIX - Implied Volatility Index     | 25.11            | -11.23           | -10.44          | 81.86           |

Source: Bloomberg, Ostrum Asset Management

## Writing



**AXEL BOTTE**  
STRATEGIST  
axel.botte@ostrum.com

## Legal information

This document is intended for professional clients in accordance with MiFID. It may not be used for any purpose other than that for which it was conceived and may not be copied, distributed or communicated to third parties, in part or in whole, without the prior written authorization of Ostrum Asset Management. None of the information contained in this document should be interpreted as having any contractual value. This document is prepared purely for the purposes of providing indicative information. This document consists of a presentation created and prepared by Ostrum Asset Management based on sources it considers to be reliable. Ostrum Asset Management reserves the right to modify the information presented in this document at any time without notice, and in particular anything relating to the description of the investment process, which under no circumstances constitutes a commitment from Ostrum Asset Management.

Ostrum Asset Management will not be held responsible for any decision taken or not taken on the basis of the information contained in this document, nor in the use that a third party might make of the information.

Figures mentioned refer to previous years. Past performance does not guarantee future results. Any reference to a ranking, a rating or an award provides no guarantee for future performance and is not constant over time. Reference to a ranking and/or an award does not indicate the future performance of the UCITS/AIF or the fund manager.

Under Ostrum Asset Management's social responsibility policy, and in accordance with the treaties signed by the French government, the funds directly managed by Ostrum Asset Management do not invest in any company that manufactures, sells or stocks anti-personnel mines and cluster bombs.

This material has been provided for information purposes only to investment service providers or other Professional Clients, Qualified or Institutional Investors and, when required by local regulation, only at their written request. This material must not be used with Retail Investors.

In the E.U. (outside of the UK and France): Provided by Natixis Investment Managers S.A. or one of its branch offices listed below. Natixis Investment Managers S.A. is a Luxembourg management company that is authorized by the Commission de Surveillance du Secteur Financier and is incorporated under Luxembourg laws and registered under n. B 115843. Registered office of Natixis Investment Managers S.A.: 2, rue Jean Monnet, L-2180 Luxembourg, Grand Duchy of Luxembourg. Italy: Natixis Investment Managers S.A., Succursale Italiana (Bank of Italy Register of Italian Asset Management Companies no. 23458.3). Registered office: Via Larga, 2 - 20122, Milan, Italy. Germany: Natixis Investment Managers S.A., Zweigniederlassung Deutschland (Registration number: HRB 88541). Registered office: Im Trutz Frankfurt 55, Westend Carrée, 7. Floor, Frankfurt am Main 60322, Germany. Netherlands: Natixis Investment Managers, Nederlanden (Registration number 50774670). Registered office: Stadsplateau 7, 3521AZ Utrecht, the Netherlands. Sweden: Natixis Investment Managers, Nordics Filial (Registration number 516405-9601 - Swedish Companies Registration Office). Registered office: Kungsgatan 48 5tr, Stockholm 111 35, Sweden. Spain: Natixis Investment Managers, Sucursal en España, Serrano nº90, 8th Floor, 28006, Madrid, Spain.

In France: Provided by Natixis Investment Managers International – a portfolio management company authorized by the Autorité des Marchés Financiers (French Financial Markets Authority - AMF) under no. GP 90-009, and a public limited company (société anonyme) registered in the Paris Trade and Companies Register under no. 329 450 738. Registered office: 43 avenue Pierre Mendès France, 75013 Paris. In Switzerland: Provided for information purposes only by Natixis Investment Managers, Switzerland SARL, Rue du Vieux Collège 10, 1204 Geneva, Switzerland or its representative office in Zurich, Schweizergasse 6, 8001 Zurich.

In the U.K.: Provided by Natixis Investment Managers UK Limited which is authorised and regulated by the UK Financial Conduct Authority (register no. 190258). This material is intended to be communicated to and/or directed at persons (1) in the United Kingdom, and should not to be regarded as an offer to buy or sell, or the solicitation of any offer to buy or sell securities in any other jurisdiction than the United Kingdom; and (2) who are authorised under the Financial Services and Markets Act 2000 (FSMA 2000); or are high net worth businesses with called up share capital or net assets of at least £5 million or in the case of a trust assets of at least £10 million; or any other person to whom the material may otherwise lawfully be distributed in accordance with the FSMA 2000 (Financial Promotion) Order 2005 or the FSMA 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 (the "Intended Recipients"). The fund, services or opinions referred to in this material are only available to the Intended Recipients and this material must not be relied nor acted upon by any other persons. Registered Office: Natixis Investment Managers UK Limited, One Carter Lane, London, EC4V 5ER.

In the DIFC: Provided in and from the DIFC financial district by Natixis Investment Managers Middle East (DIFC Branch) which is regulated by the DFSA. Related financial products or services are only available to persons who have sufficient financial experience and understanding to participate in financial markets within the DIFC, and qualify as Professional Clients or Market Counterparties as defined by the DFSA. No other person should act upon this material. Registered office: Office 603 - Level 6, Currency House Tower 2, PO Box 118257, DIFC, Dubai, United Arab Emirates.

In Japan: Provided by Natixis Investment Managers Japan Co., Ltd., Registration No.: Director-General of the Kanto Local Financial Bureau (kinsho) No. 425. Content of Business: The Company conducts discretionary asset management business and investment advisory and agency business as a Financial Instruments Business Operator. Registered address: 1-4-5, Roppongi, Minato-ku, Tokyo.

In Taiwan: Provided by Natixis Investment Managers Securities Investment Consulting (Taipei) Co., Ltd., a Securities Investment Consulting Enterprise regulated by the Financial Supervisory Commission of the R.O.C. Registered address: 34F., No. 68, Sec. 5, Zhongxiao East Road, Xinyi Dist., Taipei City 11065, Taiwan (R.O.C.), license number 2018 FSC SICE No. 024, Tel. +886 2 8789 2788.

In Singapore: Provided by Natixis Investment Managers Singapore (name registration no. 53102724D) to distributors and institutional investors for informational purposes only. Natixis Investment Managers Singapore is a division of Ostrum Asset Management Asia Limited (company registration no. 199801044D). Registered address of Natixis Investment Managers Singapore: 5 Shenton Way, #22-05 UIC Building, Singapore 068906.

In Hong Kong: Provided by Natixis Investment Managers Hong Kong Limited to institutional/ corporate professional investors only.

In Australia: Provided by Natixis Investment Managers Australia Pty Limited (ABN 60 088 786 289) (AFSL No. 246830) and is intended for the general information of financial advisers and wholesale clients only.

In New Zealand: This document is intended for the general information of New Zealand wholesale investors only and does not constitute financial advice. This is not a regulated offer for the purposes of the Financial Markets Conduct Act 2013 (FMCA) and is only available to New Zealand investors who have certified that they meet the requirements in the FMCA for wholesale investors. Natixis Investment Managers Australia Pty Limited is not a registered financial service provider in New Zealand.

In Latin America: Provided by Natixis Investment Managers S.A.

In Uruguay: Provided by Natixis Investment Managers Uruguay S.A., a duly registered investment advisor, authorised and supervised by the Central Bank of Uruguay. Office: San Lucar 1491, oficina 102B, Montevideo, Uruguay, CP 11500. The sale or offer of any units of a fund qualifies as a private placement pursuant to section 2 of Uruguayan law 18.627.

In Colombia: Provided by Natixis Investment Managers S.A. Oficina de Representación (Colombia) to professional clients for informational purposes only as permitted under Decree 2555 of 2010. Any products, services or investments referred to herein are rendered exclusively outside of Colombia. This material does not constitute a public offering in Colombia and is addressed to less than 100 specifically identified investors.

In Mexico: Provided by Natixis IM Mexico, S. de R.L. de C.V., which is not a regulated financial entity or an investment manager in terms of the Mexican Securities Market Law (Ley del Mercado de Valores) and is not registered with the Comisión Nacional Bancaria y de Valores (CNBV) or any other Mexican authority. Any products, services or investments referred to herein that require authorization or license are rendered exclusively outside of Mexico. Natixis Investment Managers is an entity organized under the laws of France and is not authorized by or registered with the CNBV or any other Mexican authority to operate within Mexico as an investment manager in terms of the Mexican Securities Market Law (Ley del Mercado de Valores). Any use of the expression or reference contained herein to "Investment Managers" is made to Natixis Investment Managers and/or any of the investment management subsidiaries of Natixis Investment Managers, which are also not authorized by or registered with the CNBV or any other Mexican authority to operate within Mexico as investment managers.

The above referenced entities are business development units of Natixis Investment Managers, the holding company of a diverse line-up of specialised investment management and distribution entities worldwide. The investment management subsidiaries of Natixis Investment Managers conduct any regulated activities only in and from the jurisdictions in which they are licensed or authorized. Their services and the products they manage are not available to all investors in all jurisdictions. It is the responsibility of each investment service provider to ensure that the offering or sale of fund shares or third party investment services to its clients complies with the relevant national law.

The provision of this material and/or reference to specific securities, sectors, or markets within this material does not constitute investment advice, or a recommendation or an offer to buy or to sell any security, or an offer of any regulated financial activity. Investors should consider the investment objectives, risks and expenses of any investment carefully before investing. The analyses, opinions, and certain of the investment themes and processes referenced herein represent the views of the portfolio manager(s) as of the date indicated. These, as well as the portfolio holdings and characteristics shown, are subject to change. There can be no assurance that developments will transpire as may be forecasted in this material. Past performance information presented is not indicative of future performance.

Although Natixis Investment Managers believes the information provided in this material to be reliable, including that from third party sources, it does not guarantee the accuracy, adequacy, or completeness of such information. This material may not be distributed, published, or reproduced, in whole or in part.

All amounts shown are expressed in USD unless otherwise indicated.



[www.ostrum.com](http://www.ostrum.com)

Ostrum Asset Management

Asset management company regulated by AMF under n° GP-18000014 – Limited company with a share capital of 27 772 359 euros

Trade register n°525 192 753 Paris – VAT: FR 93 525 192 753 – Registered Office: 43, avenue Pierre Mendès-France, 75013 Paris – [www.ostrum.com](http://www.ostrum.com)

Tél. : 01 58 19 09 80