Newsletter, 1st Quarter 2017

Trading the Bond Markets and Currency Spreads

Trading the yield curve and country to country cross rates

Introduction:

We can offer a few sophisticated Retail clients, of high net worth, the opportunity to trade, in a managed or Simi-managed account, right alongside our largest fully accredited Hedging and Portfolio Management Institutional Customers. We work with very serious Institutional Financial Managers, Treasures, CFOs and Corporate Chief Investment Officers.

See the following *News Item* as to how these spread trading opportunities dynamically develop and revel to *our analysts* very lucrative profit opportunities

News Item

European Credit Investors Face Uncertain Future After QE Unwind

Simon Ballard
February 27, 2017

- Credit markets in euros, dollars and pounds highly correlated
- BOE unwinding scenario key; Fed QE experience provides lessons

The moment of truth for debt markets beckons.

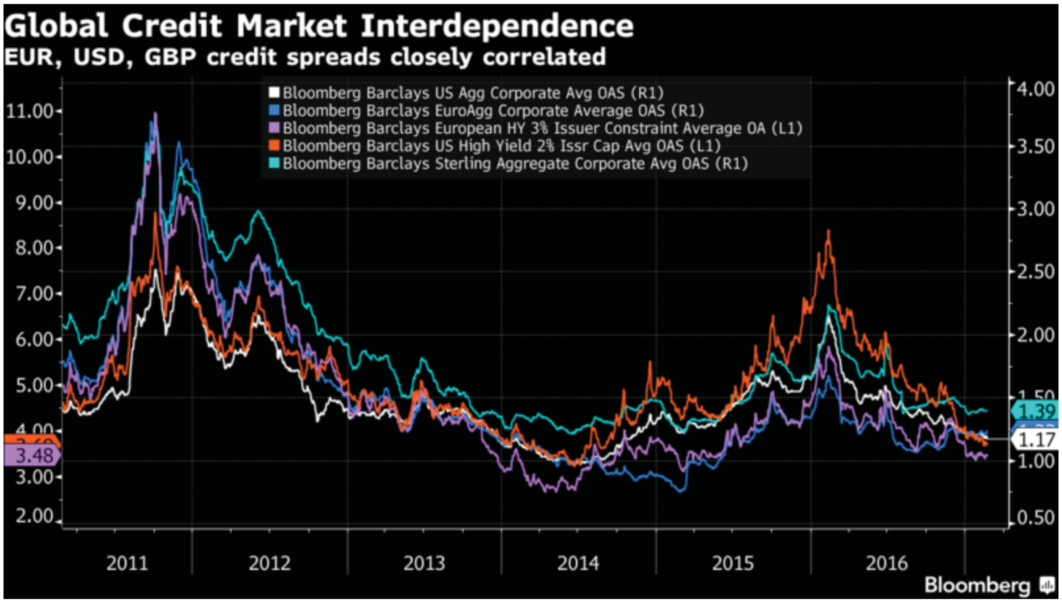
Given the extent to which monetary stimulus in Europe has helped to compress corporate bond spreads and flatten the credit curve, fears may grow over the coming months as to how investors will react to the end of the monetary backstop bid. That will depend on the speed of any reversal.

The Bank of England bought 7.4 billion pounds ($9.2 billion) of corporate bonds in the five months through Feb. 22. The monetary authority says its 18 month, 10 billion pound Corporate Bond Purchase Scheme may end ahead of schedule.

The ECB's Corporate Sector Purchase Program, meanwhile, may conclude at the end of the year at the earliest, although it's more likely that persistent economic weakness in the single-currency bloc could see it extended into 2018. The ECB has purchased around 67 billion euros ($71 billion) of corporate bonds under the scheme, it said in a Feb. 27 statement, implying average weekly purchases of 1.68 billion euros since the program began in June 2016.

The ramifications of diminishing monetary stimulus may be felt globally, since corporate credit markets in euros, dollars and pounds tend to move in lockstep.

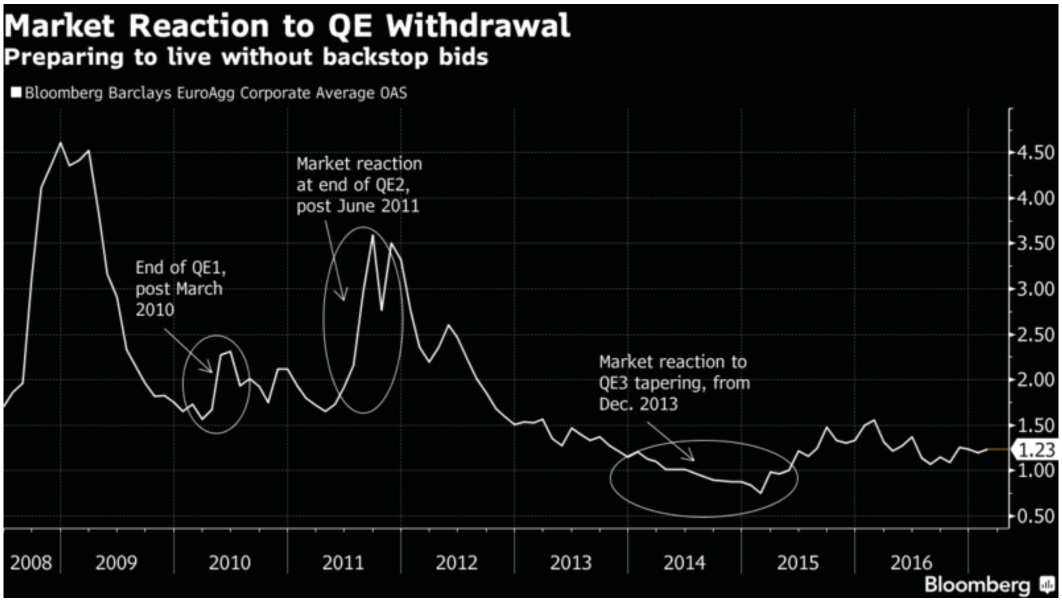
Between January 2011 and February this year, for example, the positive correlation coefficient between investment-grade credit indexes in euros, dollars and pounds ranged from 0.87 to 0.98, according to data compiled by Bloomberg.



The unwinding of quantitative easing (QE) will be historic -- no central bank has tapered corporate bonds before. The Federal Reserve's QE program focused on Treasuries and mortgage bonds, but its ending may provide clues to how credit markets will react to shifts in monetary policies in Europe.

After the U.S. central bank terminated QE1 in March 2010, for example, the option-adjusted spread for the Bloomberg Barclays EuroAgg Corporate Index jumped 70 basis points in April and May. When the Fed finished QE2 in June 2011, the spread more than doubled to 3.59 percent by the end of September that year from 1.65 percent on April 29, as valuations faltered without the implicit monetary backstop.

Muted credit market reaction to the tapering of QE3, when U.S. officials announced they would unwind the purchasing program in a gradual manner, may provide food for thought for Europe's central banks as they look to deliver market stability while fading out stimulus packages.



In the case of the Bank of England, there are at least three strategies it might adopt when it reaches its 10 billion-pound target:

- It could simply stop its weekly purchases and hold the portfolio until the accumulated bonds mature. In this scenario, spreads may ease wider on the official removal of the backstop bid, but that may be accompanied by muted market reaction thereafter.
- The bank could halt weekly purchases and then indicate its intention to sell down its holdings. This would likely trigger the most negative knee-jerk reaction in credit markets given the prospect of increased supply.
- If the macro backdrop remains negative after the triggering of Article 50 -- the formal mechanism by which the U.K. government leaves the European Union -- the central bank could decide to extend the program. Declaring a new target of, say, 15 billion pounds in total would be the best solution for the market, fueling a fillip for risk appetite and further spread tightening across the asset class.

Contact your Alliance FX Capital, Ltd. Professional Senior Account Manager to express your level of interest in our trading ideas:

Email: info@alliancefx.capital