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Harr's View

Buoyant markets despite geopolitical uncertainty

Thomas Harr, PhD, Global Head of FI&C Research, +45 45 13 67 31, thhar@danskebank.com

Good evening all

Today, I discuss US/Iran tensions, syndicated debt issuance and implications for euro and Scandi markets. The US-Iran conflict escalated following US assassination of General Soleimani on 3 January, and Iran's largely symbolic retaliation early Wednesday. On Wednesday, we arranged a conference call with Heather A. Conley, who is an expert in geopolitics and international security at the Center for Strategic and International Studies in Washington. **Heather argued that we should expect a broader regional retaliation through proxy groups close to Tehran with the retaliation concentrated in the Middle East. She expects that retaliation is likely to take years, the intensity will increase, but both the US and Iran are keen to avoid a direct confrontation.** Despite the severe risk of human casualties, in my view US-Iran tensions will only influence financial markets if they have an impact on the economic outlook and the behaviour of market participants where the transmission channel would be through oil prices. (See e.g. *here* for my take on the link between political uncertainty and financial markets). **Most likely, heightened US-Iran tensions will not be a key driver of oil markets and thereby on overall market sentiment as long as oil supply, for example in Iraq, is not damaged.**

The perception that the global economy is recovering also supports the buoyant market sentiment. In my view, the global macro backdrop is indeed constructive, but nothing more than that. We expect a shallow global growth recovery led by large emerging market countries, which have eased monetary policy substantially. I expect the US to slow modestly as the impact from Trump's tax reform fades and private consumption moderates, but loose financial conditions will cushion the slowdown. The gradual pick-up in Asia led by China stimulus will spill over to the Eurozone, but German manufacturing remains remarkably weak. Continuing woes in the German auto-sector support our view that it is too early for EUR/USD to head substantially higher (see *here*).

The EUR syndicated debt market recorded its largest weekly issuance that we have tracked, according to our Chief Strategist on covered bonds and financials, Sverre Holbek. The issuance was split between financials (EUR20.3bn), SSAs (EUR17.8bn), corporates (EUR12.5bn), covered (EUR10.3bn) and sovereigns (EUR8.5bn). Markets absorbed the substantial supply very well with new issue premiums at low levels and secondary spreads only widening very marginally. The solid performance mirrors the sentiment among end-investors, where European debt funds witnessed modest inflows whereas equity funds experienced outflows for the week ending 8 January. **Spreads are very compressed across the credit spectrum, but I believe European equities may still head higher near-term, given the shallow upturn in the cycle and relative valuation. The positive equity sentiment may still provide some cushion for credit spreads.** Issuance is set to continue next week, albeit likely at slightly lower levels ahead of the silent period, which for many companies begins in the week starting 20 January. (Note that the silent period starts earlier for e.g. several European banks). The large issuance has led to a modest tightening in German ASW (i.e. lower swap rates relative to bond yields) as some issuers swap fixed rate debt to floating. Our Chief Fixed Income Analyst, Jens Peter Sørensen, argues that bund ASW should widen again due to the negative net supply of German government bonds in January on the back of redemptions and ECB buying. (See *here*).

In our Scandi markets, *we argue* that the minutes from the Riksbank meeting, where they hiked rates in December to 0%, revealed that the central bank was uncomfortable with the risk of negative rates being perceived as something permanent, which could have undesired effects on behaviour. Riksbank's concern resembles the ones raised by other central banks and official institutions (see *here* for a discussion). **Still, we interpret the minutes as slightly dovish, which supports our bearish view on the Swedish krona, as argued by our SEK strategist, Stefan Mellin.** In Norway, *we argue* that the market is too dovish on Norges Bank while heavy NOK issuance could tighten NOK-EUR rates spreads further. We believe that NOK could strengthen a bit further, but fading risk appetite is a risk. **In Denmark, we argue in our flagship *Reading the Markets Denmark* publication led by our head of Fixed Income Research, Jan Weber Østergaard, that 30Y 2% callable bonds should outperform short-dated non-callable bonds if yields rise slightly.** Note that going forward Reading the Markets Denmark will be a weekly publication where we will focus on the most topical themes across Danish FI and FX markets. Finally, I want to flag that our credit research team have provided an overview of potential Nordic corporate issuers in 2020 in EUR, SEK and NOK based on our estimate of their funding surplus in the coming year, publicly known strategies (e.g. ongoing changes in the capital structure) and upcoming redemptions. (See *here*).

On tomorrow's Macro Strategy View podcast, I will discuss the outlook for new syndicated debt issuance and the implications for government bonds, covered bonds, credit and bund ASW with Sverre Holbek and Jens Peter Sørensen. That is all for today's comment. On that note, I wish you a great Sunday night and coming week. Best regards, Thomas.

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