

ECB QE

How much will the ECB have to buy below depo in Germany in 2017?

- As of 2 January, it has been possible for the ECB to undertake QE purchases below the level of the deposit rate 'to the extent needed'. In this note, we estimate how much buying below depo will be required in German government bonds in order not to breach the 33% issue limit under different rate scenarios for 2017.
- We estimate that 15% of the QE purchases in German government bonds will have to be below the deposit level in our base scenario, with unchanged yields on German bonds throughout 2017. If purchases 'below depo' are postponed as long as possible, ECB purchases could continue 'unchanged' until November before QE would be forced 'below depo' in German government bonds. Admittedly, these estimates are very sensitive to the rate level, the fraction of government bonds versus agency/regionals in QE purchases and to some extent, the historical purchases pattern on the German curve.
- The estimate is in particular sensitive to the development in yields in the 1-6Y segment on the German curve. In a scenario where the yield on German bonds increases 25bp across the curve, the ECB could avoid 'buying below depo' in 2017 and wait until March 2018 before being 'forced' below depo (assuming QE at EUR60bn per month continues beyond December 2017). On the other hand, if yields decrease 25bp, the 'QE fraction below depo' would increase to 40% of 2017 QE, and buying below depo would be forced to commence in August.
- There has been no guidance on how 'QE below depo' will be implemented; hence, whether buying will be proportional or skewed towards higher yielding (closer to depo).
- These insights have interesting implications for a possible extension of QE into 2018. As QE holdings will have hit the issue limit, all QE purchases will have to be done below the 'depo level' aside from the 33% new issuance (equivalent to EUR30-40bn in purchases above depo). An alternative to substantial purchases 'below depo' could be a deviation from the capital key. In our view, this is still a likely scenario as we approach the end of the 'QE era', where in particular the periphery is likely to be in need of sustained support in order to avoid material spread widening.
- See also *Guide to Q1 issuance and thoughts on supply vs QE in 2017*, 1 January 2017.

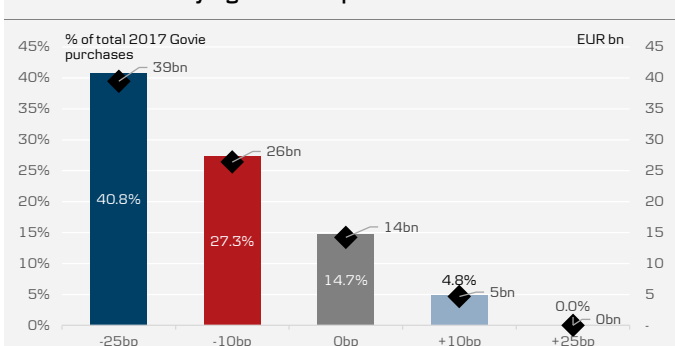
Chief Analyst

Anders Møller Lumholtz
+45 45 14 69 98
andjrg@danskebank.dk

Analyst

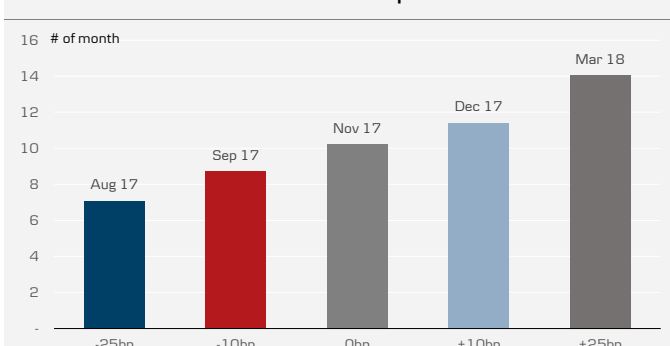
Thomas Hoppe Rosenlund
+45 45 14 32 85
thros@danskebank.dk

Fraction of QE buying 'below depo' in Ger. – diff. rate scenarios



Source: ECB, Danske Bank Markets

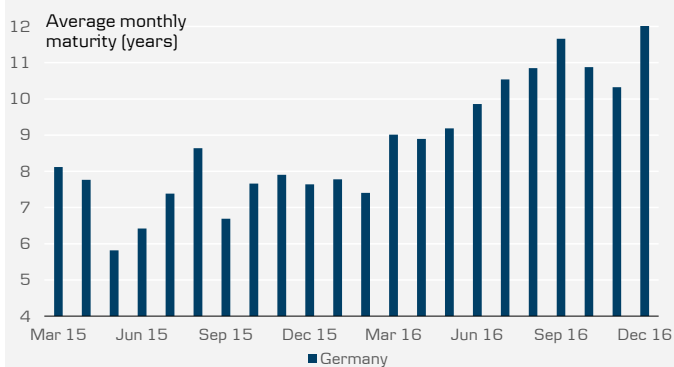
Month where QE is 'forced' below depo – diff. rate scenarios



Source: ECB, Danske Bank Markets

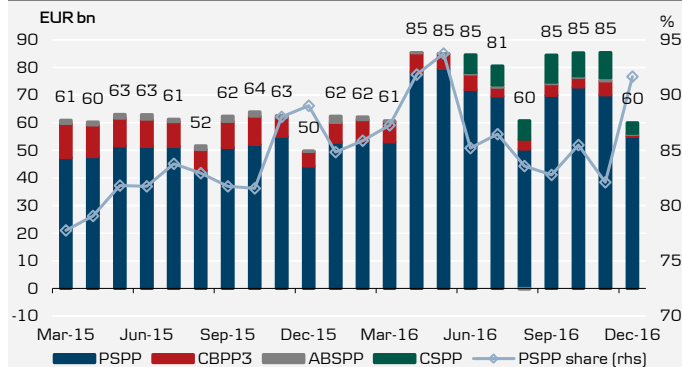
Note: estimates are based on a number of assumptions including: (1) purchases are made proportional on the curve when eligible historically (above depo and in eligible mat. segment); (2) purchases in agencies/regionals are assumed to represent the outstanding weight in the PSPP universe – historically and going forward; (3) other Eurosystem holdings of German government bonds aside from PSPP are not included (*ECB A.7.2 amounts to EUR320bn* or around 5% of EGBs, but are most likely mainly in short maturities); (4) we estimate EUR95bn QE in German government bonds in 2017.

Ave. maturity of German purchases is steadily increasing



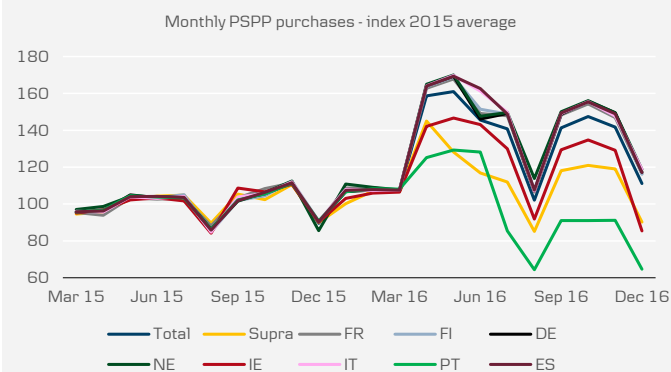
Source: ECB, Danske Bank Markets

Distribution of QE purchases



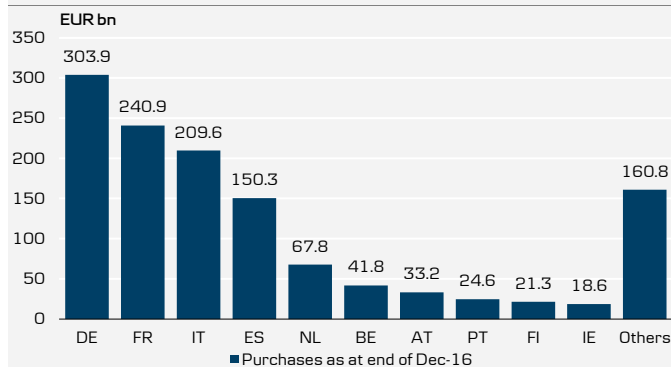
Source: ECB, Danske Bank Markets

Already capital key deviation in countries hitting restrictions



Source: ECB, Danske Bank Markets

Total PSPP purchases across countries



Source: ECB, Danske Bank Markets

Disclosure

This research report has been prepared by Danske Bank Markets, a division of Danske Bank A/S ('Danske Bank'). The authors of the research report are Anders Møller Lumholtz, Chief Analyst, and Thomas Hoppe Rosenlund, Analyst.

Analyst certification

Each research analyst responsible for the content of this research report certifies that the views expressed in the research report accurately reflect the research analyst's personal view about the financial instruments and issuers covered by the research report. Each responsible research analyst further certifies that no part of the compensation of the research analyst was, is or will be, directly or indirectly, related to the specific recommendations expressed in the research report.

Regulation

Danske Bank is authorised and subject to regulation by the Danish Financial Supervisory Authority and is subject to the rules and regulation of the relevant regulators in all other jurisdictions where it conducts business. Danske Bank is subject to limited regulation by the Financial Conduct Authority and the Prudential Regulation Authority (UK). Details on the extent of the regulation by the Financial Conduct Authority and the Prudential Regulation Authority are available from Danske Bank on request.

Danske Bank's research reports are prepared in accordance with the recommendations of the Danish Securities Dealers Association.

Danske Bank is not registered as a Credit Rating Agency pursuant to the CRA Regulation (Regulation (EC) no. 1060/2009); hence, Danske Bank does not comply with nor seek to comply with the requirements applicable to Credit Rating Agencies.

Conflicts of interest

Danske Bank has established procedures to prevent conflicts of interest and to ensure the provision of high-quality research based on research objectivity and independence. These procedures are documented in Danske Bank's research policies. Employees within Danske Bank's Research Departments have been instructed that any request that might impair the objectivity and independence of research shall be referred to Research Management and the Compliance Department. Danske Bank's Research Departments are organised independently from and do not report to other business areas within Danske Bank.

Research analysts are remunerated in part based on the overall profitability of Danske Bank, which includes investment banking revenues, but do not receive bonuses or other remuneration linked to specific corporate finance or debt capital transactions.

Danske Bank is a market maker and may hold positions in the financial instruments mentioned in this research report.

Danske Bank, its affiliates and subsidiaries are engaged in commercial banking, securities underwriting, dealing, trading, brokerage, investment management, investment banking, custody and other financial services activities, may be a lender to the companies mentioned in this publication and have whatever rights are available to a creditor under applicable law and the applicable loan and credit agreements. At any time, Danske Bank, its affiliates and subsidiaries may have credit or other information regarding the companies mentioned in this publication that is not available to or may not be used by the personnel responsible for the preparation of this report, which might affect the analysis and opinions expressed in this research report.

See <http://www-2.danskebank.com/Link/researchdisclaimer> for further disclosures and information.

General disclaimer

This research has been prepared by Danske Bank Markets (a division of Danske Bank A/S). It is provided for informational purposes only. It does not constitute or form part of, and shall under no circumstances be considered as, an offer to sell or a solicitation of an offer to purchase or sell any relevant financial instruments (i.e. financial instruments mentioned herein or other financial instruments of any issuer mentioned herein and/or options, warrants, rights or other interests with respect to any such financial instruments) ('Relevant Financial Instruments').

The research report has been prepared independently and solely on the basis of publicly available information that Danske Bank considers to be reliable. While reasonable care has been taken to ensure that its contents are not untrue or misleading, no representation is made as to its accuracy or completeness and Danske Bank, its affiliates and subsidiaries accept no liability whatsoever for any direct or consequential loss, including without limitation any loss of profits, arising from reliance on this research report.

The opinions expressed herein are the opinions of the research analysts responsible for the research report and reflect their judgement as of the date hereof. These opinions are subject to change, and Danske Bank does not undertake to notify any recipient of this research report of any such change nor of any other changes related to the information provided in this research report.

This research report is not intended for, and may not be redistributed to, retail customers in the United Kingdom or the United States.

This research report is protected by copyright and is intended solely for the designated addressee. It may not be reproduced or distributed, in whole or in part, by any recipient for any purpose without Danske Bank's prior written consent.

Disclaimer related to distribution in the United States

This research report was created by Danske Bank A/S and is distributed in the United States by Danske Markets Inc., a U.S. registered broker-dealer and subsidiary of Danske Bank A/S, pursuant to SEC Rule 15a-6 and related interpretations issued by the U.S. Securities and Exchange Commission. The research report is intended for distribution in the United States solely to 'U.S. institutional investors' as defined in SEC Rule 15a-6. Danske Markets Inc. accepts responsibility for this research report in connection with distribution in the United States solely to 'U.S. institutional investors'.

Danske Bank is not subject to U.S. rules with regard to the preparation of research reports and the independence of research analysts. In addition, the research analysts of Danske Bank who have prepared this research report are not registered or qualified as research analysts with the NYSE or FINRA but satisfy the applicable requirements of a non-U.S. jurisdiction.

Any U.S. investor recipient of this research report who wishes to purchase or sell any Relevant Financial Instrument may do so only by contacting Danske Markets Inc. directly and should be aware that investing in non-U.S. financial instruments may entail certain risks. Financial instruments of non-U.S. issuers may not be registered with the U.S. Securities and Exchange Commission and may not be subject to the reporting and auditing standards of the U.S. Securities and Exchange Commission.