BARCLAYS

Credit Research

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European Credit Alpha

Sovereign downgrade fire drill

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European credit has shrugged off another echo from last summer, this time in the form of a peripheral sovereign downgrade. While the market reaction to Italy's downgrade was muted, the follow on downgrades that we expect will weigh on the performance of affected credits over the long term. Though we remain constructive on the market and believe credit will continue to grind tighter, or at least stay range bound, structures with limited downside are starting to look more compelling than outright longs.

Large outflows from US HY funds garnered a significant amount of attention in June and raised concerns that European credit markets could also be affected by outflow-driven selling. These concerns appear exaggerated, but not unfounded. Fund flows in Europe continue to lag (rather than lead) performance and the negative total returns of recent months suggests that some retail money will exit credit over the summer. However, outflows are unlikely to have a significant impact on spreads, ex ante.

Sterling bonds have underperformed in the recent sell-off, even when measured on a like-for-like basis versus EUR- and USD-denominated equivalents. With the premium for GBP bonds back to January levels, we reinstate our preference for Sterling credit over Euro credit and screen for the most attractive cross-currency opportunities.

The European HY market has been firmer over the past few weeks, with CDS outperforming cash in the move tighter. This has been most apparent in the higher-quality parts of the market. We believe investors should look to put on negative basis packages on these names, or alternatively rotate long positions into cash. We highlight a selection of opportunities where the basis looks particularly attractive.

Post the FOMC headlines, European credit markets have taken on a very subdued tone with a steady grind in spreads, with neither higher-than-expected NFP numbers nor the Italy downgrade causing much volatility. Clients remain net short risk in Main and while Main is modestly tight vs. SX5E, we believe spreads could grind tighter, or at the very least stay range-bound. We recommend two option trades with August expiry to position for this.

OVERVIEW

Sovereign downgrade fire drill

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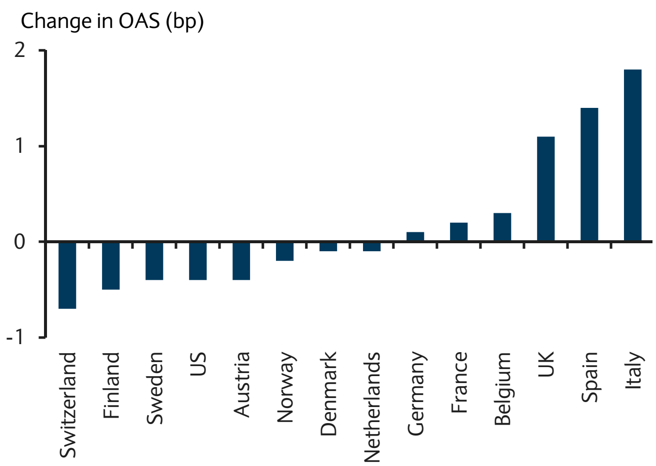
S&P's downgrade of the Italian sovereign to BBB/Neg from BBB+/Neg was somewhat out of the blue, though not entirely unexpected as the Negative outlook had been in place since January 2012. The initial response was muted, with spread widening concentrated in Italian credits and some limited spill-over into other peripheral names (Figure 1). This is similar to the reaction of markets around events in Cyprus and Portugal, and reinforces our theme of falling systemic risk perceptions in Europe.

While the market reaction is a further data point on this trend, more interesting (in our view) was the written opinion from S&P. There was not a single mention of the EU, of the ESM or of the EFSF (and only a single mention of funding pressure) in the six page report. The focus fell instead on the necessity of structural reforms that successfully lift the long-term growth potential of Italy and on the funding crunch being suffered by Italian SMEs. This reflects the sea-change in how European risk is perceived now versus a year ago. It also suggests that (in line with the view from our colleagues in economics and interest rates) we cannot assume that the downgrade of Italy is negative for the Spanish sovereign. S&P appears to be viewing them as stand-alone credits at this juncture.

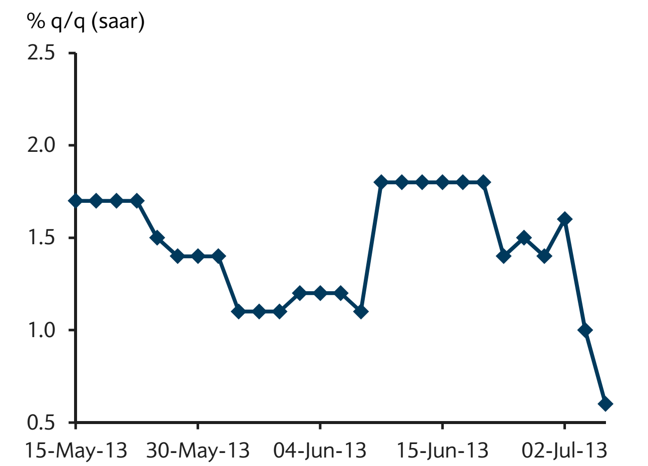
We can, however, assume that the sovereign downgrade will result in follow-on action for the majority of Italian credits that are currently rated above the Italian sovereign. Banks, in particular, look vulnerable to a one-notch downgrade – which should bring S&P's rating into line with Moody's – as do utilities. Our analysts also expect Atlantia to be downgraded as a result of the sovereign rating action (*Ratings risk set to return*, 10 July 2013). Downgrades are likely to create a performance drag for affected credits in the long term. That said, we do not expect any credits to fall to HY.

FIGURE 1
Reaction to Italy downgrade, one day OAS change



Note: Based on Euro Aggregate Corporate Index. Source: Barclays Research

FIGURE 2
Barclays US Q2 GDP tracking estimate



Source: Barclays Research

One Italian credit that did fall below investment grade this week was Banco Popolare di Milano (BPIM). Moody's has lowered the bank's senior unsecured rating three notches to Ba3/Negative, and gave a very negative opinion on the name – noting pressures on asset quality, profitability, and capitalisation. As a result, €2.3bn of BPIM bonds are expected to exit our benchmark IG indices at the end of July. The points raised by Moody's match those made by our bank team in their recent report on Italian banks (*Wait for the asset quality review*, 4 July 2013); particularly with respect to the deterioration of loan books and poor profitability relative to potential capital needs. Our analysts recommend waiting until after the ECB's asset quality review before adding exposure to Italian banks and we agree. We continue to like the ISPIM-BPIM pair trade recommended in *European Credit Alpha*, 21 June 2013.

On the positive side, bank capital instruments rallied sharply following the EBA's clarification that step-up T1 securities will remain "step-ups for life" with regards to capital treatment. Several bonds jumped in price following the announcement, which our bank team believe has significant implications across European bank capital instruments (*Purging the capital structure*, 10 July 2013). Other regulatory developments have been less positive, with the German government publically disagreeing with the EC over who should be in charge of winding up failed European banks under the Single Resolution Mechanism.

Overall, we remain constructive on credit. However, we also note that valuations have risen significantly over the past month, with iTraxx Main retracing from its year-to-date wides of 133bp to c.107bp today – slightly tighter than before the FOMC guided towards tapering of its asset purchases. While we expect spreads to grind tighter over the summer months, risk versus reward is less attractive now. In particular we note that, despite the strong payrolls report, our economists' tracking estimate for Q2 GDP has dropped sharply (Figure 2). A very low Q2 GDP print could re-ignite the question of whether the Fed is tapering too early, and create renewed market volatility. Therefore, we prefer structures where downside is capped over outright long positions, and highlight several attractive ways to do this in the CDS Relative Value section. It is too early to look at adding hedges/shorts, in our view.

FOCUS

Fund flows remain a lagging indicator

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Large outflows from US HY funds garnered a significant amount of attention in June and raised concerns that European credit markets could also be affected by outflow-driven selling. These concerns appear exaggerated, but not unfounded. Fund flows in Europe continue to lag (rather than lead) performance and the negative total returns of recent months suggests that some retail money will exit credit over the summer. However, outflows are unlikely to have a significant impact on spreads, ex ante.

Summer outflows from credit are likely…

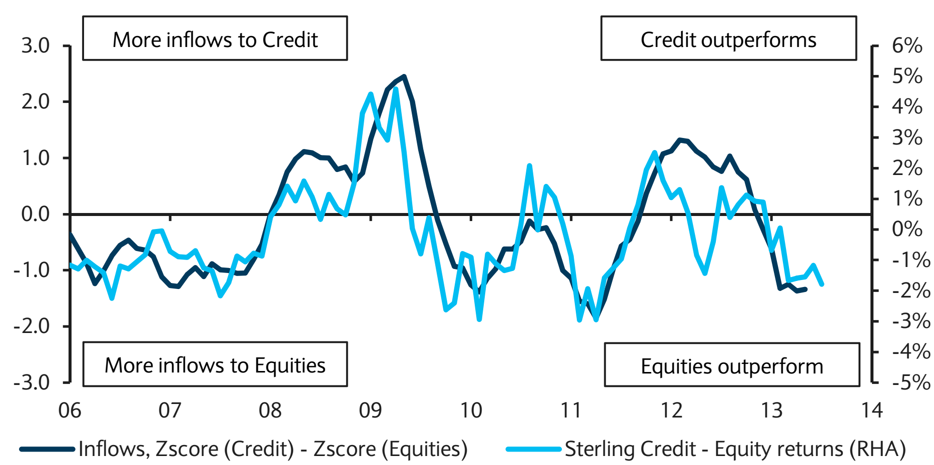
We have previously analysed the relationship between credit (total) returns and fund flows (*Retail fund flows and asset returns*, European Credit Alpha 22 February 2013). In particular, we noted that *relative* returns tend to lead *relative* inflows across asset classes. When credit underperforms equities retail investors buy more equity funds – and this may or may not be funded by selling their holdings in credit funds.

From February through May, our benchmark sterling credit index generated returns of +3.13% versus returns of +4.89% from the FTSE100. Over the same period, UK equity funds have seen net retail buying (inflows) of £1.69bn, versus outflows from IG corporate funds of -£0.20bn. In June, Sterling credit returned -4.21%, but this was actually ahead of equity returns for the month, with the FTSE100 down by -5.21%. Per Figure 1, inflows have continued to closely track the relative performance of the two asset classes.

Thus, concerns over the potential for outflows from credit in the coming months appear justified to us, though not because of deeply negative total returns in June (given that equity returns were even worse). Our analysis suggests that inflows lag returns by around two months; therefore, we expect continued weakness in retail fund flows through the summer. While our quantitative analysis is focused on sterling markets, we believe that a similar relationship will hold in the euro space. Over the last four months, our benchmark euro index generated returns of 0.04% versus returns of 1.43% from the Stoxx 600.

FIGURE 1

Relative inflows (credit – equities) versus relative total returns (credit – equities)



Note: Returns are the 6 month average total returns. Source: IMA, Bloomberg, Barclays Research

… but does it matter?

Based on our analysis, fears of outflows from credit funds are justified. But what does that mean for spread performance? When we add fund flow data to our macro model for credit spreads, it appears that inflows are most strongly positive when spreads look cheap versus our model (Figure 2), ie, after periods of underperformance. This seems to contradict our previous comments, but makes sense when we note that equity returns were more negative than credit returns during periods of major spread widening over the past five years. In line with our previous analysis (European Credit Alpha, 7 June 2013), there is little evidence that fund flows lead spread widening/underperformance.

Hence, the fact that we expect outflows does not, in itself, make us nervous about credit spreads. Of course, there is the risk that 'this time is different'; it is fair to highlight that there have not been any periods of sustained, heavy outflows in the post-crisis era and the liquidity of the market in those circumstances is untested. Then again, looking at our data there have never been any periods of sustained outflows from the credit product – the largest sequential outflows in the last 20 years of data totalled just £1.2bn (versus AUM of £31.6bn at the time). In that sense, very large redemptions are truly a 'known unknown'.

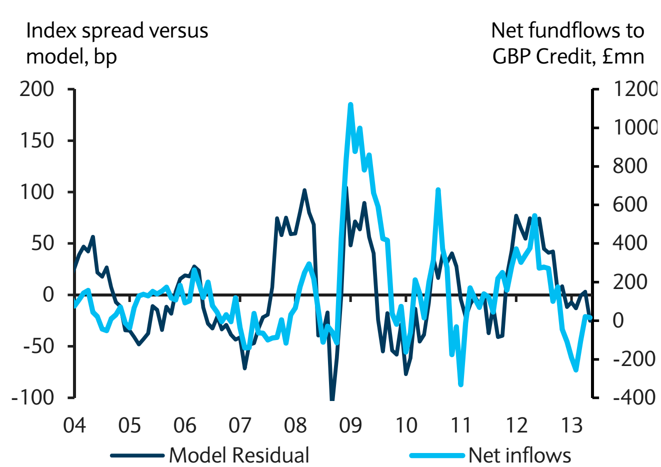
Negative net issuance should not be over looked when considering flows

Another technical that is often missed in discussions around outflows is the negative net issuance in Europe. When the investible universe of bonds is shrinking, money has to exit the asset class by definition (in aggregate). It would be unusual for all of the outflows to come solely from institutional investors, so while the negative issuance technical persists, outflows on the retail side are not only manageable, they are almost unavoidable.

Net issuance in Europe has been consistently negative over the past two and a half years. Year to date, we estimate that €126.2bn of bonds have been redeemed (Figure 2). Pro-rata, this would require c.€25bn of credit to be sold by retail funds over the year, which is orders of magnitude larger than any reasonable estimate of outflows in Europe. This is another reason that we are not concerned by the (small) outflows from credit that we expect over the coming months. Arguably, they are long overdue.

FIGURE 2

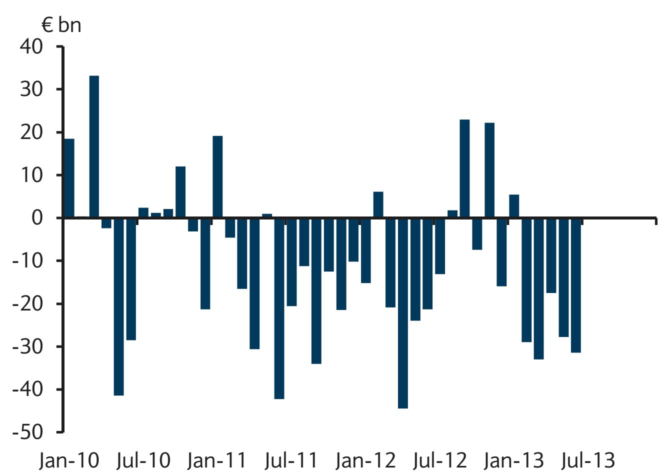
Macro model residual versus net fund inflows



Source: IMA, Bloomberg, Barclays Research

FIGURE 3

Net corporate issuance



Source: Dealogic, Barclays Research

Finally, we note that fixed income cash flows are an important buffer for fund managers when dealing with redemptions (outflows). Based on a 20% holding of our benchmark index, retail fund managers could fund €1bn per month of redemptions from coupon payments alone – and significantly more if they allow bonds to mature without reinvesting the principal proceeds. This would minimize the amount of 'forced selling'.

A different type of retail investor

It is worth putting the importance of retail fund flows into context. Based on our estimates of who holds European corporate credit, the retail investor holds a larger proportion of credit in Europe than in other markets (Figure 4). Retail holdings of EUR IG paper, in particular, are large relative to the UK and US. Notably, the reverse is true in HY, reflecting the less developed nature of the European HY market. The size of the retail investor base is unfortunate given the general lack of timely data with respect to fund flows in Europe.

FIGURE 4

Credit fund flow data – sources and coverage

		Index size (bn)	% of index held in retail funds	Data provider	AUM Covered (bn)	% of funds covered	% of index covered
EUR	IG	1,146	30%	LIPPER	109.6	31.9%	9.6%
	HY	166	20%	LIPPER	22.9	69.0%	13.8%
GBP	IG	497	20%	IMA	71.5	71.9%	14.4%
	HY	21	40%	IMA	6.9	83.5%	33.4%
USD	IG	4,100	15%	LIPPER	435	70.7%	10.6%
	HY	1,117	25%	EPFR	219	83.4%	19.6%

Note: Indices used are the US Aggregate Credit, Euro Aggregate Corporate, Pan European High Yield ex. Financials and Sterling Non-Gilt Indices. US IG AUM based on a 30% share of reported AUM for US IG bond funds (which can hold IG, MBS, UST), GBP HY AUM based on 80% of reported AUM, assuming 20% is in USD HY.
Source: EPFR, LIPPER, IMA, Barclays Research

Some other observations we make are that:

- **Fund flows coverage is much weaker in Europe**: Based on the data provided, Lipper only covers around 32% of EUR IG retail AUM (assets under management). Much of the remaining retail holdings are likely to be via non-IG specific funds, where it is difficult to disaggregate them. Coverage of the EUR HY space is better but still lags the GBP and USD data. Further, while EPFR offers daily data for the US, European data from Lipper is often only available monthly – and with significant lags.[1]

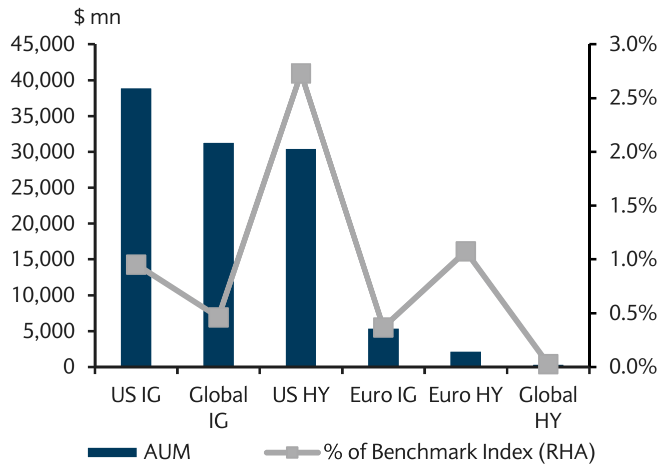
- **The fraction of index holdings covered is small:** Combining the coverage ratio with the retail holdings of credit, we note that European fund flow data captures only 10-15% of the investor base. In theory, we could pro-rata EUG IG fund flows higher (to reflect the low coverage ratio). However, it is not clear that the c.70% of IG retail holdings that are not covered by data providers are subject to the same flow dynamics, given the potential for selection bias.

- **Credit ETFs are smaller in Europe:** We think this is particularly relevant as there is less assumption that funds can/will provide instantaneous liquidity in Europe. Indeed, our impression, based on client interactions, is that much of the 'retail' money in Europe is comprised of assets managed for the benefit of high net worth individuals via wealth managers and private banks. This holding structure makes retail money less prone to being quickly re-allocated, in our view.

[1] EPFR also produces daily fund flow reports for Europe, but we have yet to fully analyze their data set and ascertain coverage rates.

FIGURE 5

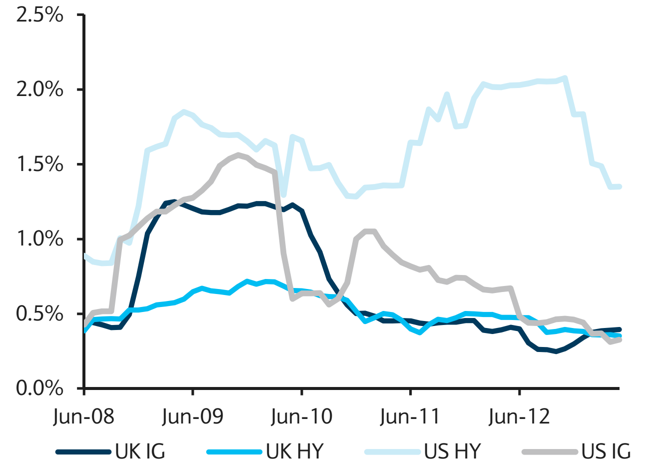
Credit ETF Assets under management (AUM)



Source: EPFR, Barclays Research

FIGURE 6

Volatility of retail fund flows



Note: Volatility defined as the 18-month standard deviation of 1 month fund flows, measured as a % of AUM. Source: EPFR, IMA, Barclays Research

On the last point, in Figure 5 we show the AUM of bond ETFs in Europe and the US. With c.€8bn of AUM (of which c.€5.5bn is IG focused), ETFs own c.0.6% of our benchmark Euro corporate index, making them considerably smaller in size (outright and as a % of the index) than US ETFs. In particular, US HY ETFs own 2.7% of the index which is far higher than any other asset class. This is also reflected in the volatility of flows into each credit class. European flows (both HY and IG) are much more stable (as a % of AUM) than those seen for US HY funds. We believe these two observations are related.

Data quality is limited

Our final argument for being relatively less focused on fund flows in Europe is data quality. As shown above, the coverage ratios are lower, data is released with a longer delay and with less regularity. Data providers are working to improve their coverage of European funds (and have made significant progress over the past two years), but this process has further to go.

Given the quality and timeliness of data, it appears to us that (for the time being) by the time we have hard evidence in Europe of outflows from the credit asset class it will be too late to act upon them. Thus, while we acknowledge the tail risk of a disorderly selling of credit by retail investors, in a context where institutional investors do not step in to facilitate risk transfer, we think it should be relatively low on the list of concerns for investors.

INVESTMENT GRADE CREDIT

Returning to overweight on Sterling credit

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Sterling bonds have underperformed in the recent sell-off, even when measured on a like-for-like basis versus EUR- and USD-denominated equivalents. With the premium for GBP bonds back to January levels, we reinstate our preference for Sterling credit over Euro credit and screen for the most attractive cross-currency opportunities.

In particular, we favour the following switches:

- Buy VOD £5.625 '25s, Sell VOD €5.375 '22s
- Buy UU £5.750 '22s, Sell UU €4.250 '20s
- Buy TDCDC £5.625 '23s, Sell TDCDC €3.750 '22s
- Buy EDF £6.875 '22s, Sell EDF $6.5 '19s

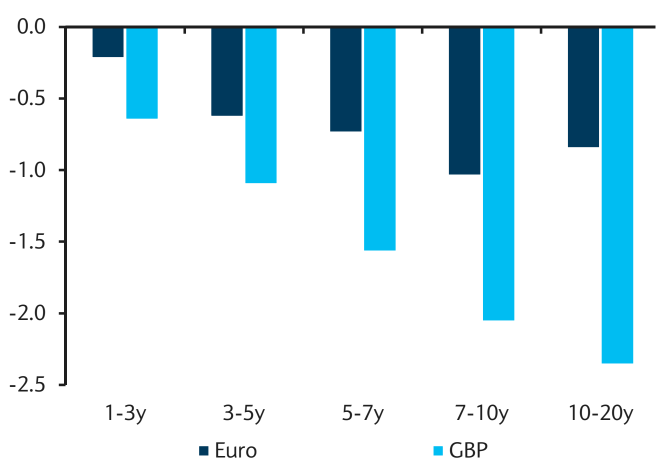
Time to oppose the cheapening

On 10 May, we noted the considerable outperformance of sterling credit in April, whether measured as index returns or as spread premium for GBP bonds over their EUR equivalents (*European Credit Alpha*, 10 May 2013). At that time, our opinion was that sterling credit no longer looked particularly attractive versus the euro market. Hence we stepped away from the overweight recommendation that we had held previously.

Since then, credit spreads have moved wider in Europe and globally. In this sell-off, Sterling credit has underperformed (Figure 1, Figure 2). In June, our benchmark Sterling credit index generated excess returns of -173bp, significantly worse than the -69bp from our Euro index. Part of this can be attributed to the longer duration of the Sterling index (OAD of 7.99 years versus 4.47 years for the Euro index), while spreads also underperformed with the index OAS moving 25bp wider to 179bp (versus the 21bp widening in the Euro index).

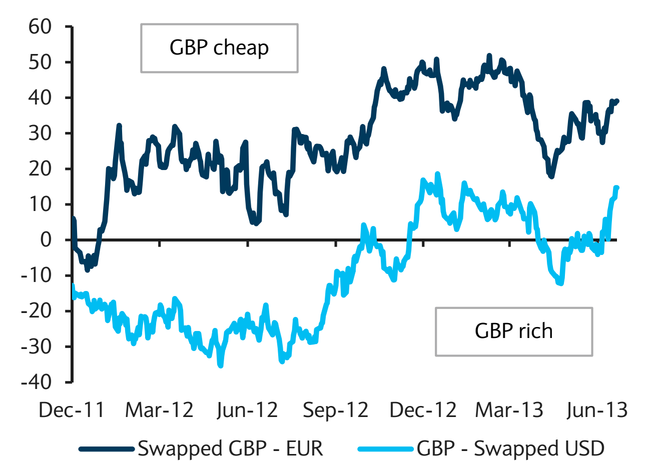
The recent move has pushed the 'sterling premium' back to its level at the start of the year, which we believe represents good value over the medium term. We do not expect the premium to collapse again in the near term, but do see room for it to compress.

FIGURE 1
Excess returns since 22 May (%)



Note: Measured to the 5th July. Source: Barclays Research

FIGURE 2
Non-financial cross-currency relative value (ASW, bp)



Source: Barclays Research

In part, the underperformance in sterling is likely to reflect the supply-demand dynamics of the two markets. Euro credit net-supply has remained deeply negative this year, given the continued de-leveraging by European banks, which is supportive for spreads. While sterling markets have seen very weak gross supply (we recently revised our CY13 forecasts down from £55bn to £37.5bn), net supply has been +£7bn year to date.

In addition, anecdotal evidence suggests that some large UK credit managers have been reducing risk over the past month, which may be related to de-risking from IG bond funds (see this week's focus for more detail). We do not have any particular insight as to how long this dynamic will persist, and acknowledge the potential for further underperformance in the near term. However, risk-reward in sterling appears attractive to us and, given tentative signs that fund de-risking and sterling underperformance are slowing, we are comfortable opposing the cheapness at these levels.

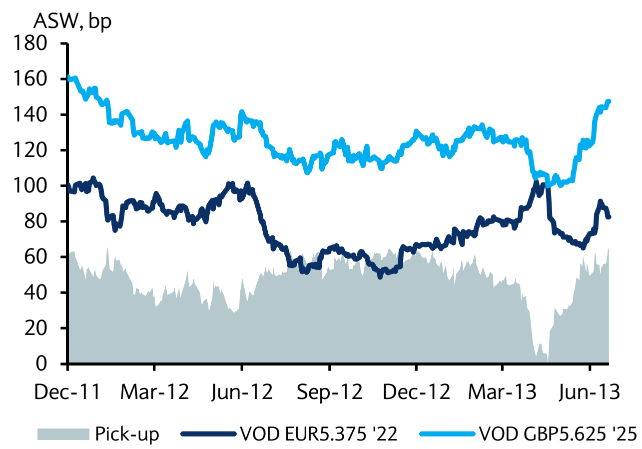
Best opportunities

In Figures 7 and 8, at the end of this section, we screen for the best opportunities to pick up spread by switching into GBP bonds from equivalent EUR and USD securities. Further, we highlight the following switches which we believe offer particularly compelling value:

- **Buy VOD £5.625 '25s, Sell VOD €5.375 '22s**. In Telcos, the VOD £25s offer a potential pick-up of 65bp versus the shorter-duration €22s (56bp after hedging, Figure 4).
- **Buy UU £5.750 '22, Sell UU €4.250 '20s**. The recent widening of the UU £22s means they now trade c.73bp back of the €20s (61bp after hedging) for an additional two more years (Figure 5). This is as the wide end of the 12-month range (20-67bp on a hedged basis).
- **Buy TDCDC £5.625 '23s, Sell TDCDC €3.750 '22s**. TDCDC £23s have underperformed significantly in June and now trade 79bp back of the €22s on ASW (69bp after hedging).
- **Buy EDF £6.875 '22s, Sell EDF $6.5 '19s.** The underperformance of GBP is also evident versus USD. In this space, we note that the EDF £19s offer a potential 39bp pick-up versus the $22s (59bp after accounting for the cost of hedging).

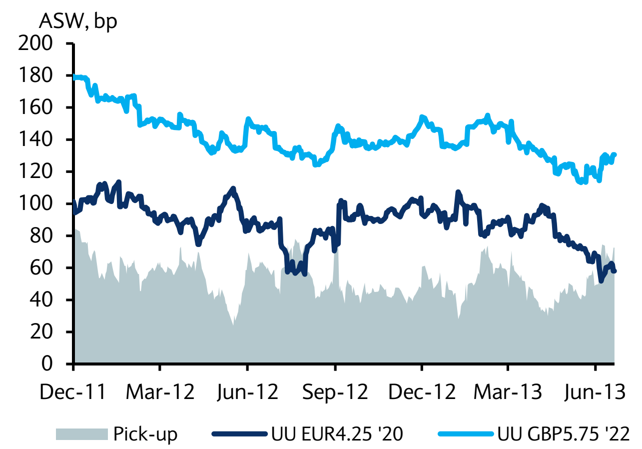
Details of the recommended trades are also shown in Figure 6.

FIGURE 4
VOD €5.375'22s vs. VOD £5.625 '25s



Source: Barclays Research

FIGURE 5
UU €4.250 '20s vs. UU £ 5.750 '22s



Source: Barclays Research

FIGURE 6
Top trade ideas

	EUR			GBP			GBP-EUR		
Ticker	Coupon	Maturity	ASW	Coupon	Maturity	ASW	GBP-EUR	Swapped GBP-EUR	Cash Price
UU	4.250	24/01/2020	58	5.750	25/03/2022	130	73	61	4.22
VOD	5.375	06/06/2022	83	5.625	04/12/2025	147	65	56	-5.79
TDCDC	3.750	02/03/2022	107	5.625	23/02/2023	185	79	69	4.66
	USD			GBP			GBP-USD		
Ticker	Coupon	Maturity	ASW	Coupon	Maturity	ASW	GBP-USD	Swapped USD-GBP	Cash Price
EDF	6.5	26/01/2019	120	6.875	12/12/2022	158	39	59	7.64

Source: Barclays Research

FIGURE 7
GBP/EUR top switches based on their 6-month range (Senior Non-financials)

	EUR			GBP							
Ticker	Coupon	Maturity	ASW	Coupon	Maturity	ASW	GBP-EUR	Swapped GBP-EUR	6m High	6m Low	Range
LINGR	3.125	12/12/2018	24	6.500	29/01/2016	57	34	10	10	-17	100%
TITIM	5.250	10/02/2022	330	5.875	19/05/2023	432	103	93	93	13	100%
ROLLS	2.125	18/06/2021	42	6.750	30/04/2019	79	37	18	18	7	99%
GSK	4.000	16/06/2025	42	5.250	19/12/2033	108	66	65	66	15	99%
VOD	5.375	06/06/2022	83	5.625	04/12/2025	147	65	56	57	-4	99%
TDCDC	3.750	02/03/2022	107	5.625	23/02/2023	185	79	69	70	22	98%
TELEFO	5.875	14/02/2033	278	5.445	08/10/2029	340	62	59	62	-9	95%
GFSLN	2.625	06/12/2018	161	7.750	13/05/2019	244	83	64	67	18	95%
NGGLN	5.000	02/07/2018	40	6.000	07/06/2017	75	35	12	13	-16	94%
GSZFP	5.950	16/03/2111	258	5.000	01/10/2060	177	-81	-91	-85	-172	94%

Source: Barclays Research

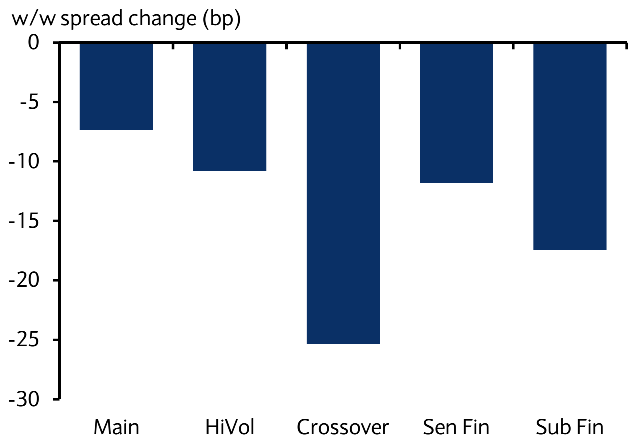
FIGURE 8
GBP/USD top switches based on their 6-month range (Senior Non -financials)

	USD			GBP							
Ticker	Coupon	Maturity	ASW	Coupon	Maturity	ASW	GBP-USD	Swapped GBP-USD	6m High	6m Low	Range
T	5.550	15/08/2041	168	7.000	30/04/2040	204	36	60	60	3	100%
EDF	5.600	27/01/2040	168	5.500	17/10/2041	196	28	51	51	-2	100%
PG	5.550	05/03/2037	93	5.250	19/01/2033	97	4	30	30	-2	100%
WMT	5.250	01/09/2035	115	5.625	27/03/2034	116	1	27	27	-5	100%
MCD	6.300	15/10/2037	115	5.875	23/04/2032	116	0	26	26	-25	100%
T	8.000	15/11/2031	164	5.500	15/03/2027	163	-2	25	25	-54	100%
EDF	6.950	26/01/2039	208	5.500	17/10/2041	196	-12	12	12	-42	100%
CMCSA	6.500	15/11/2035	165	5.500	23/11/2029	151	-14	12	12	-61	100%
VIEFP	6.750	01/06/2038	238	6.125	29/10/2037	218	-21	5	5	-57	100%
WMT	6.200	15/04/2038	133	4.875	19/01/2039	111	-22	4	4	-24	100%

Source: Barclays Research

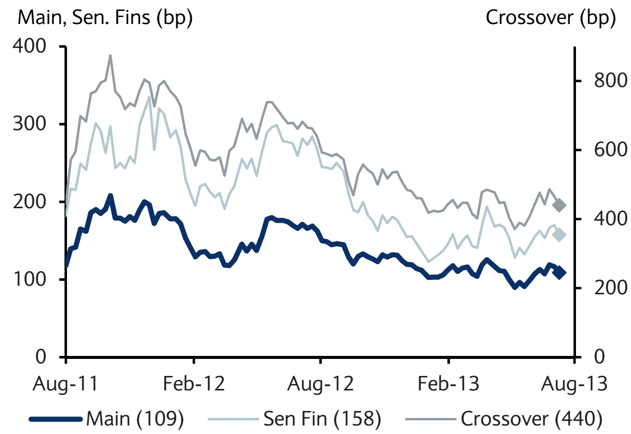
IG credit at a glance

FIGURE 9
Week-on-week change in iTraxx CDS indices



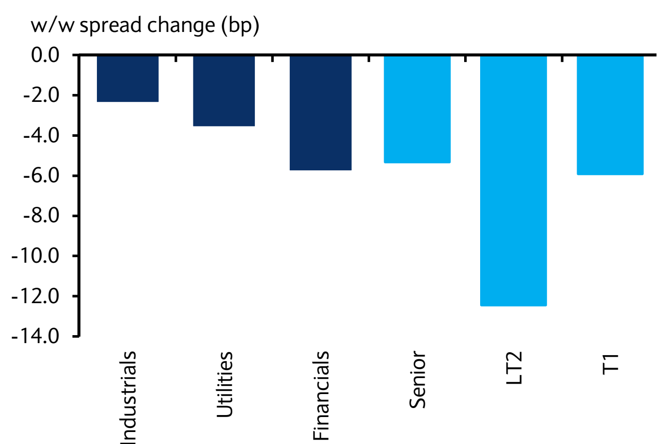
Note: Measured Wednesday to Wednesday. Source: MarkIt

FIGURE 10
iTraxx Europe CDS indices, spread history



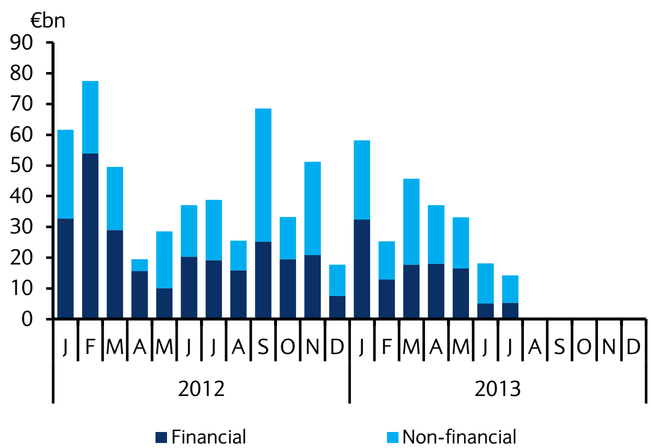
Note: Spreads taken at close of business Wednesday. Source: MarkIt

FIGURE 11
Week-on-week change in Euro Agg. Corporates



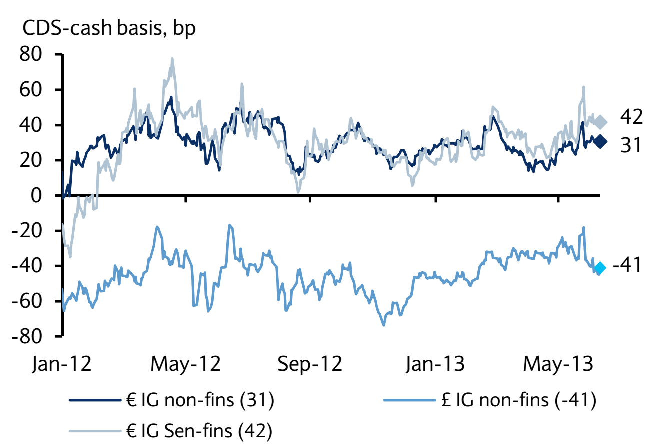
Note: Measured Wednesday-to-Wednesday. Source: Barclays Research

FIGURE 12
Investment grade €- and £-issuance, ex. covered



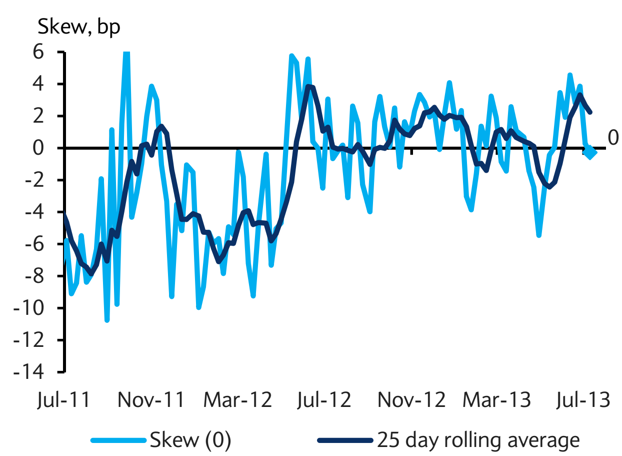
Source: Dealogic, Barclays Research

FIGURE 13
CDS-cash basis



Note: Spreads taken at close of business Wednesday.
Source: MarkIt, Barclays Research

FIGURE 14
iTraxx Europe, market – intrinsic



Note: Spreads taken at close of business Wednesday.
Source: MarkIt, Barclays Research

HIGH YIELD

BB-asis

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The European HY market has been firmer over the past few weeks, with CDS outperforming cash in the move tighter. This has been most apparent in the higher-quality parts of the market. We believe investors should look to put on negative basis packages on these names, or alternatively rotate long positions into cash. We highlight a selection of opportunities where the basis looks particularly attractive.

The European HY market was firmer this week, despite weak Chinese trade data and the Italian sovereign downgrade by S&P. As we saw with Portugal last week, price action was very much concentrated in the sovereign under question, with little spill over into the rest of the periphery (Figure 3). Elsewhere, primary market activity re-emerged this week amid the more stable environment. Issuance so far in July already looks like it will exceed June's total of €3.3bn equivalent.

BB-asis

Similar to the rest of the market, the basis in HY quickly moved positive after the sell-off began on 22 May. As Figure 4 shows, the aggregate CDS-cash basis moved from 25bp just prior to the sell-off to a peak of nearly 90bp on 24 June. Over the past few weeks, however, this has reversed meaningfully. Now, the aggregate basis is close to recent lows, and remains well below the 1-year average (Figure 4).

As we have highlighted previously, the higher-quality part of the cash market underperformed during the market weakness in May/June, and has yet to correct in the move tighter (Figure 5). Meanwhile, in CDS we have not seen this to the same extent. Given these dynamics, the basis in the higher-quality parts of the market looks particularly negative.

Furthermore, while aggregate basis is negative in the higher-quality parts of the market, there remains a meaningful amount of variation across individual credits. For example, PORTEL continues to trade with a more positive basis, particularly the longer dated issues while Auto names are trading with a negative basis.

FIGURE 1
Biggest movers – PE High Yield ex-fin Index (TR, %)

Select top performers	YTD 10 July	YTD 03 July	Weekly Total Return
Travelport	143.9	134.7	9.2
Schmolz + Bickenbach	31.9	27.7	4.2
Portugal Telecom	1.8	-1.8	3.6
Portucel	-0.9	-4.5	3.6
Brisa Finance Bv	0.5	-2.6	3.1
Select bottom performers			
Norske Skogindustrier	-17.4	-15.7	-1.7
Origin Energy	0.8	1.2	-0.4
Eircom	-5.5	-5.2	-0.3
Fmc Finance Vi Sa	0.7	1.0	-0.3
Softbank	2.0	2.3	-0.3

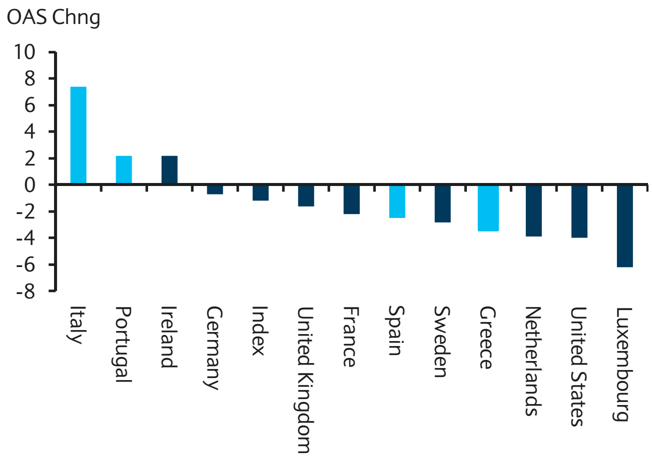
Note: Based on ticker level returns in EUR, Hedged. Source: Barclays Research

FIGURE 2
Biggest movers – iTraxx Crossover (bp)

Select top performers	Spread 10 July	Spread 03 July	Weekly spread change
Peugeot Sa	619	705	-86
Melia	671	748	-77
Hellenic Telecom	607	671	-64
Cerved Group	697	758	-61
Portugal Telecom	469	519	-50
Select bottom performers			
Codere Finance	12643	10620	+2024
Norske Skog	2394	2305	+89
Techem	377	377	0
Smurfit Kappa	355	356	0
Lafarge	280	282	-2

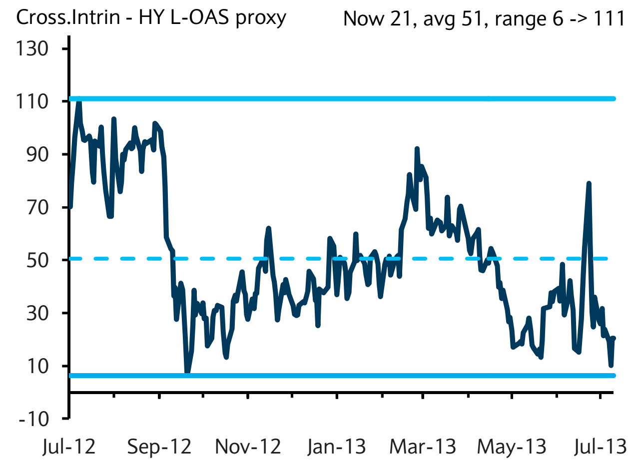
Source: Barclays Research

FIGURE 3
There was not a broad-based reaction to the Italian sovereign downgrade on the day of the downgrade



Source: Barclays Research

FIGURE 4
The aggregate HY CDS-Cash basis has corrected meaningfully



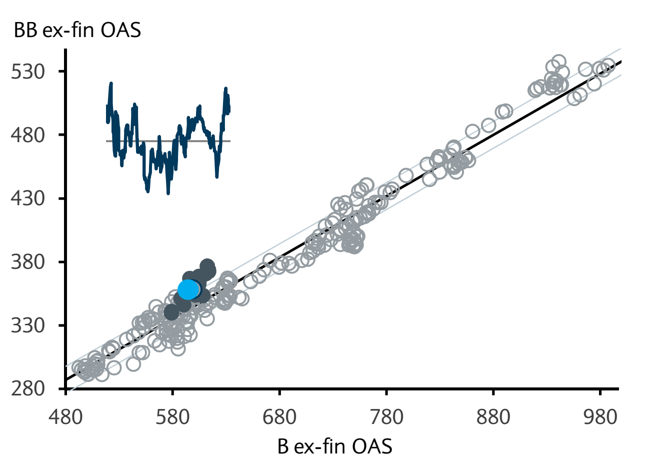
Source: Barclays Research

Overall, given our positive outlook on credit into year end, we believe that cash should catch up with CDS in the move tighter. The clear risk to this trade is if the market's recent aversion to duration were to persist or grow stronger, which could cause cash to further underperform CDS. Given the more dovish tone of recent Fed commentary and ECB/BoE forward guidance, we do not see this as likely. Indeed, fund flows in the US have recently been more constructive, and the same is true for high yield funds in Europe.

In order to screen for single-name opportunities, we applied the following filters:

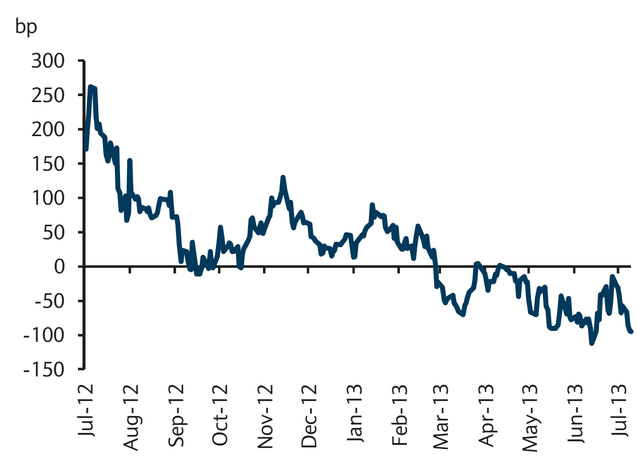
- bonds are bullets, to prevent large duration mismatches that can occur when bonds become call constrained;
- basis is negative and remains close to its 12m minimum (ie, most negative) value; and
- removing higher-priced cash bonds to mitigate recovery mismatches if investors where to put on the basis package.

FIGURE 5
BBs have underperformed lower quality in Cash



Source: Barclays Research

FIGURE 6
Example of BB basis opportunity (FIAT 7 17s)



Source: Barclays Research

We highlight some of the opportunities from our screen in Figure 7. The negative basis tends to be most pronounced for the shorter-dated bonds, which is intuitive given the relative steepness of cash vs. CDS curves. Further, many of the autos currently trade with negative basis, which is interesting given they have traditionally traded with a more positive (Figure 6) basis in part due to a strong domestic bid for bonds. For investors that are disinclined or unable to implement basis packages, we suggest that investors at a minimum rotate longs into cash as opposed to CDS for any of these credits

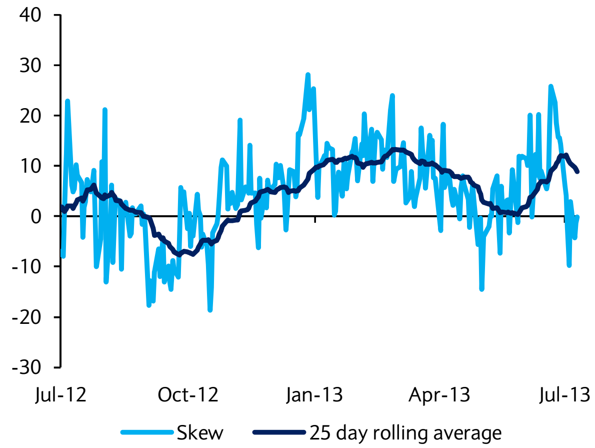
FIGURE 7
Selected negative basis opportunities

				Basis		
Bond	**Z-Spread**	**Maturity Matched CDS***	**Basis**	**2 Week Change in basis**	**12m Min**	**12m Max**
STENA 6.125 17	425	307	-119	-92	-131	150
FIAT 6.375 16	419	304	-115	-16	-148	136
FIAT 7 17	487	393	-95	-65	-112	194
MWDP 4.875 15	206	114	-92	-15	-121	43
MWDP 4.875 16	237	149	-88	-42	-104	91
RENAUL 4.625 16	219	149	-70	-49	-101	117
FIAT 5.25 16	417	365	-52	-47	-93	230
FIAT 6.625 18	509	473	-36	-80	-41	79
CLNVX 3.25 19	191	157	-34	-32	-39	96
TKAGR 4.375 15	148	117	-31	-32	-77	133
MWDP 4.375 17	265	234	-31	-44	-50	107

Note levels indicative only as of Tuesday 10th July 2013 *Based on an interpolated CDS spread between the 3, 5 and 10y marks Source: Barclays Research

European High Yield credit at a glance

FIGURE 8
Crossover skew (bp)

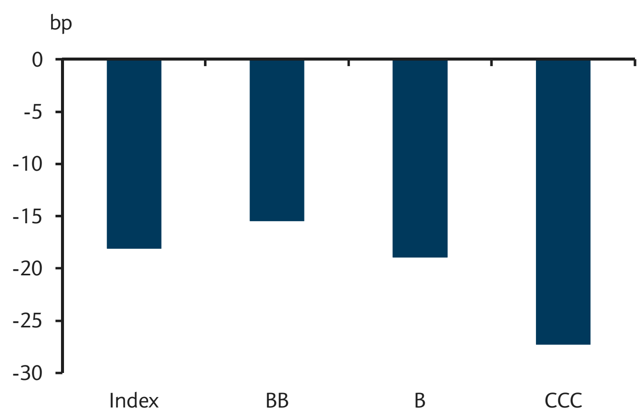


Note: Crossover not roll-adjusted. Source: Barclays Research

FIGURE 9
HY secured vs. unsecured yield difference (%)

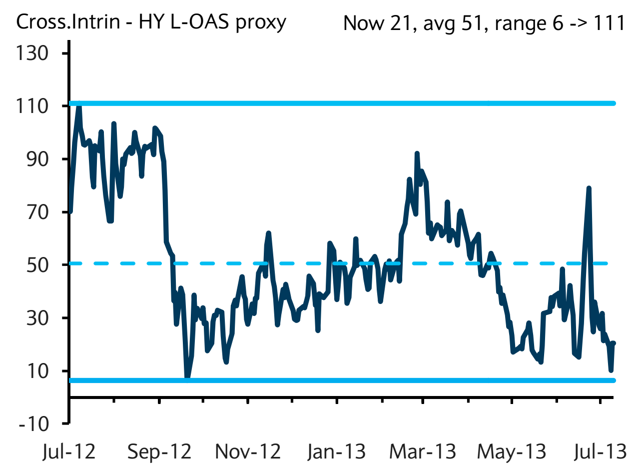
Source: Barclays Research

FIGURE 10
W/w OAS change PEHY ex financials (bp)



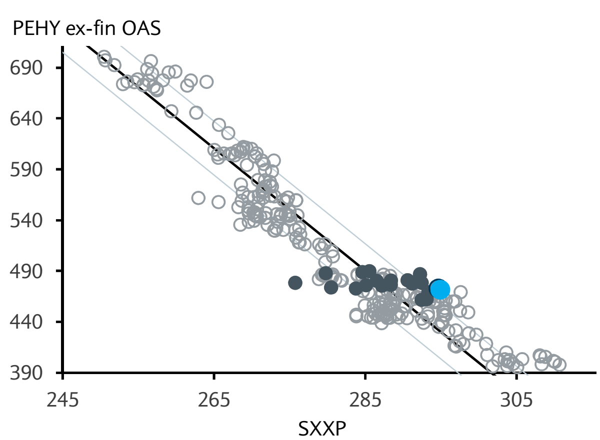
Note: Wednesday-to-Wednesday. Source: Barclays Research

FIGURE 11
Crossover and PEHY ex-fins CDS-cash basis (bp)



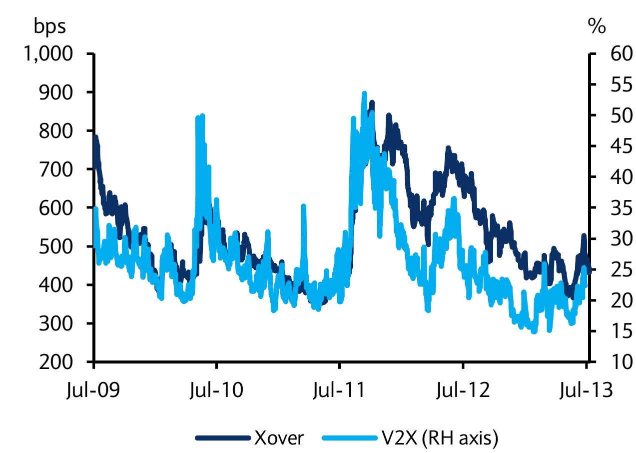
Note: Crossover roll-adjusted. Source: Barclays Research

FIGURE 12
High Yield cash vs. equities



Source: Barclays Research

FIGURE 13
V2X Index vs. iTraxx Crossover



Source: Barclays Research

CDS RELATIVE VALUE

Summer grind is finally here (?)

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Post the FOMC headlines, European credit markets have taken on a very subdued tone with a steady grind in spreads, with neither higher-than-expected NFP numbers nor the Italy downgrade causing much volatility. Clients remain net short risk in Main and while Main is modestly tight vs SX5E, we believe spreads could grind tighter, or at the very least stay range-bound. We recommend two option trades with August expiry to position for this.

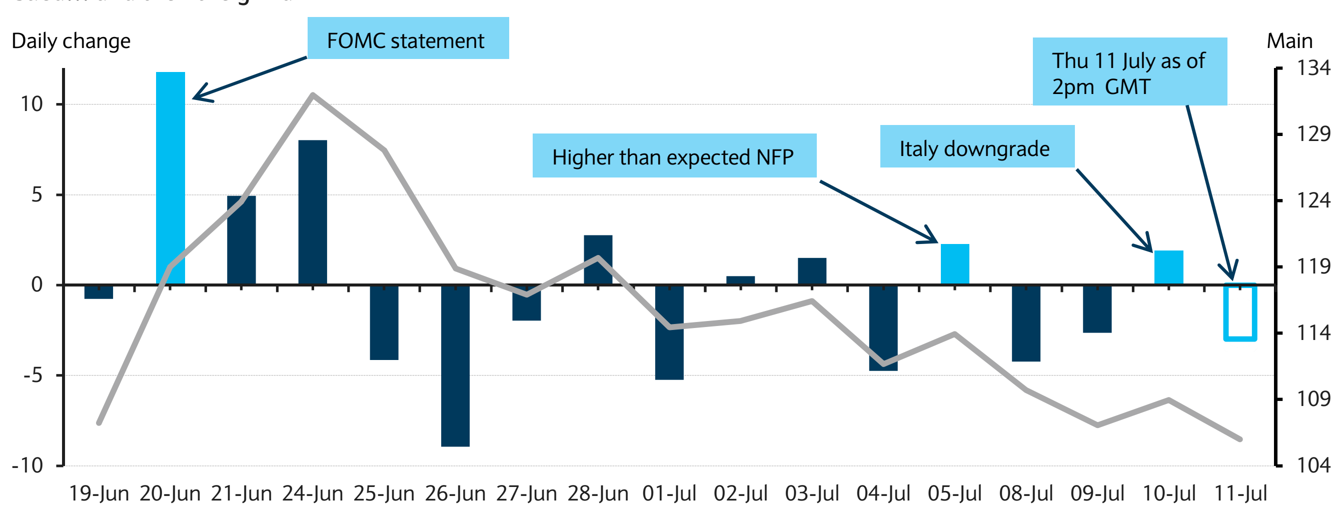
Option trades recommended, August expiry:

- *1x2 receiver spread*: Buy 1x strike 110 receiver, Sell 2x strike 100 receiver; and
- *Receiver financed by selling a payer spread*: Buy strike 100 receiver, Sell strike 120-140 payer spread.

Market backdrop – the grind

Markets have taken on a distinct "grind-y" feel following the burst of volatility after the FOMC statement (Figure 1). The day before the FOMC statement, 19 June, iTraxx Main closed at 107bp, 3bp wider than current levels; in the past two weeks, spreads have been much more stable, in general only tightening. Even the higher-than-expected NFP numbers on 5 July, and the Italian S&P downgrade, resulted in only a modest widening in spreads.

FIGURE 1
iTraxx Main daily changes: After the FOMC-induced volatility in June, a short spurt of volatility in sympathy with UST volatility ensued… and then the grind

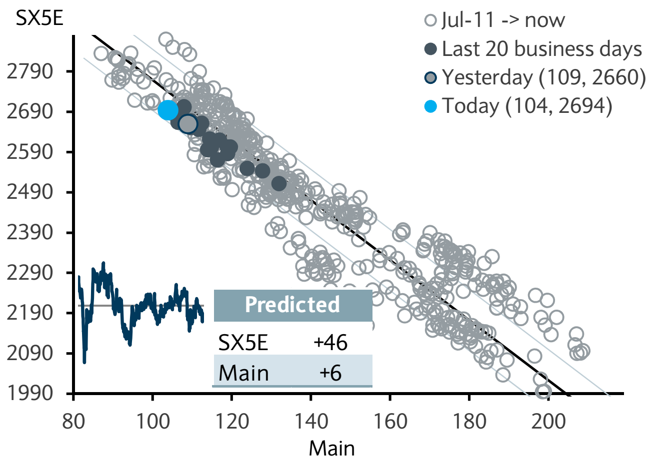


Source: Markit, Barclays Research

Main has outperformed SX5E (Figure 2), for the first time since the BoJ/Abenomics announcements in early April, highlighting to us, the "grind-y" feel of the market. Currently, Main trades 6bp tight vs SX5E on a 24-month regression basis, but we are reluctant to recommend a reversal at this stage. Going into the holidays (summer and winter), there has been a tendency for Main to outperform in a slow grind, and we are disinclined to position against it at this stage. The degree of outperformance vs historical data is not yet extreme and in principle could have more to go: for comparison, iTraxx Main has traded 16bp tight on mid-April vs the 6bp currently.

FIGURE 2

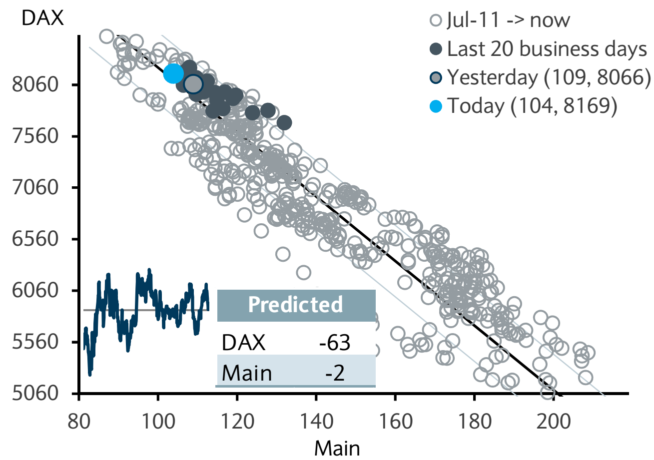
Main outperforms SX5E in the grind – seen before going into holidays – does not feel like the time to position against that move



Note: The embedded chart is the time series of the z-score of the regression.
Source: Bloomberg, Markit, Barclays Research

FIGURE 3

Main underperformance vs DAX during the sell-off has completely corrected



Note: The embedded chart is the time series of the z-score of the regression.
Source: Bloomberg, Markit, Barclays Research

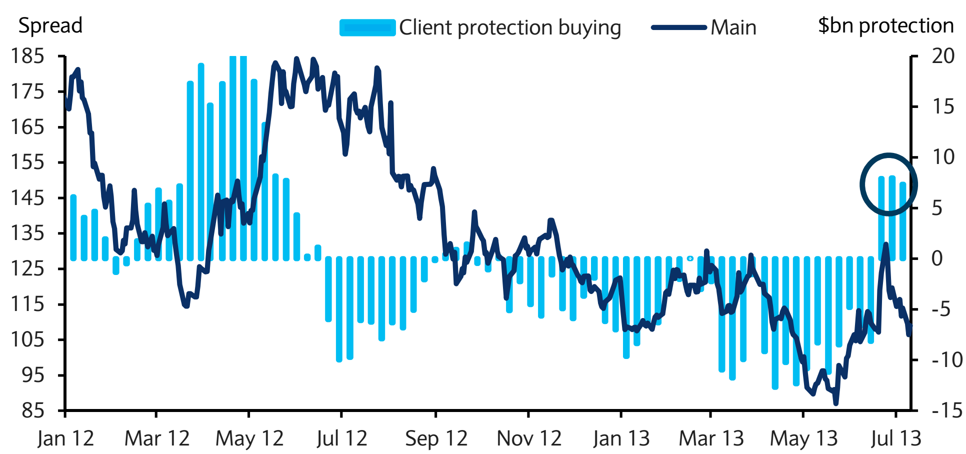
Main has also outperformed DAX (Figure 3), correcting the significant underperformance we highlighted last week, although Main is just now in line based on 24 months of history, as opposed to the relationship vs SX5E, where Main trades tight.

The grind is likely to continue, assuming no headlines in July/August. We would expect Main to grind tighter, predicated on continued low UST volatility (or Bunds' continued ability to show a reduced correlation to UST) and no new sovereign or Asia-related headlines. In addition, HY fund outflows in the US appear to have stopped, and even turning into small inflows. A continuation of this will, in our view, hinge on continued low UST volatility, but it does removes one more driver of spread widening in the near term.

This view is supported by client positioning in Main (Figure 4). Despite the post FOMC/NFP rally, clients (on balance) appear to have held onto the large short base that was built in the week of the FOMC meeting, with clients remaining short $8bn, even though spreads have tightened. To us, this is important for two reasons: 1) dealers on balance are long risk, making them happy to trade Main tighter in the absence of major flows; and 2) on balance clients are short, which could prove painful in a market with (probably) little news to take us materially wider.

FIGURE 4

Positioning in Main – Clients remain net short despite the tightening



Source: DTCC, Markit, Barclays Research

How low can we go in the summer grind? The "fair value" of Main, given current economic data is around 100bp, on our estimates. With uncertainties, among others, regarding the political agenda after the German elections in September creeping into investors' minds, we would be buyers of protection if Main is in the low 90s by the end of the summer (in the absence of any other material headlines).

Trades for the grind

To position for a grind tighter over the summer, while having limited exposure if spreads widen, we like the following two trades, all with an August expiry, ref 105. The P&L profiles of the two trades are shown in Figure 5 and Figure 6.

1x2 receiver spread:

- Buy €100mn strike 110 Receiver @ 46.8; and
- Sell €200mn strike 100 Receiver @ 19.8;
- Net cost of 7c.

Receiver financed by selling a payer spread:

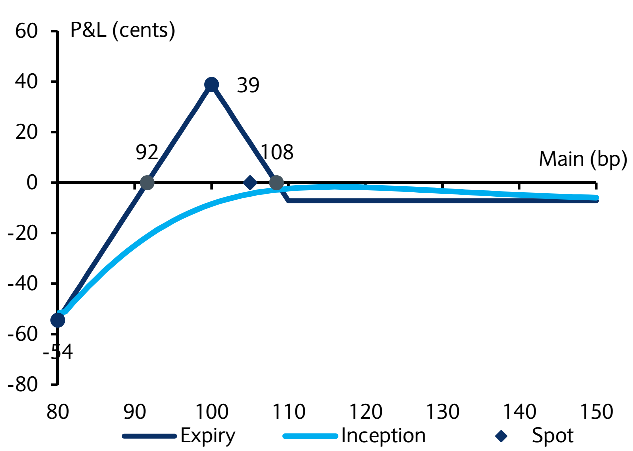
- Buy €100mn strike 100 Receiver @ 22.8;
- Sell €100mn strike 120 Payer @ 19.7; and
- Buy €100mn strike 140 Payer @ 9.8;
- Net cost of 13c.

The 1x2 receiver has a breakeven range of 92-108bp, which appears to be a likely range for spreads in late August, in our view. Furthermore, via the sold receivers, the investor would be automatically exercised into being a buyer of protection at low spreads, in line with our tactical view discussed above.

The more bullish long receiver financed by a payer spread has full upside if a rally below 100bp emerges, and starts to lose money only for spreads wider than 120bp, with losses capped at 1pct for Main above 140bp.

FIGURE 5

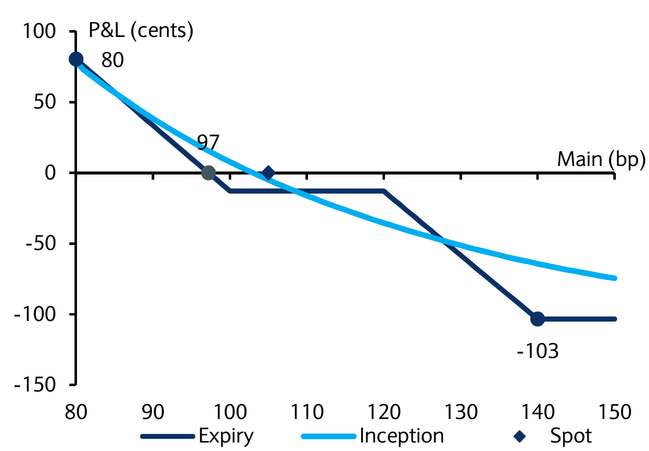
1x2 receiver spread – payoff at expiry and inception



Source: Barclays Research.

FIGURE 6

Receiver financed by selling a payer spread – payoff at expiry and inception



Source: Barclays Research.

ANALYST RATINGS SUMMARY

HIGH GRADE CREDIT RESEARCH

Sectors	Overweight	Underweight
	Insurance	Autos and Auto Parts, Building Materials, Chemicals, Diversified Manufacturing, Pharmaceuticals, Oil & Gas, Retail and Services, Utilities
Autos		Volkswagen, Daimler, Scania, MAN, Volvo, Michelin, Bosch
Banks	BBVA, Santander, Societe Generale	Commerzbank, Intesa, Unicredit
Consumer & Retail	Ahold, BAT, Experian, Tate & Lyle	Adecco, Carrefour, Carlsberg, Diageo, Henkel, Kingfisher, Metro, Suedzucker
General Industrial	CRH, Heathrow Funding, HIT Finance, Linde, SCA	ABB, Akzo Nobel, Alstom, Bayer, Bouygues, EADS, Lanxess, Saint Gobain, Syngenta
Insurance	Allianz, AXA, Hannover Re, Munich Re, Swiss Re, Zurich	
Oil & Gas	BP	BG, Repsol YPF, OMV
Pharmaceuticals	Merck KGaA, Roche	AstraZeneca, GlaxoSmithKline, Sanofi-Aventis
TMT	BskyB, TeliaSonera, Telenor, UBM	France Telecom, KPN, Vodafone, Ericsson, Reed, Pearson, Wolters Kluwer
Transport	National Express	Go-Ahead
Utilities	ESB, Edison	Dong Energy, Enel, ENBW, Fortum, Gas Natural, Red Electrica, RWE, SSE, Suez Environnement, UU plc, Vattenfall

High Grade CDS trade ideas (at current levels)

Buy Protection: Akzo Nobel, AstraZeneca, Atlantia, Bayer, Bouygues, BT Group, Carrefour, Carlsberg, Diageo, KPN, IMT, Metro, Next, Suedzucker, Pearson, Rexam, RWE, Saint Gobain, Tate & Lyle, UU plc, Wolters Kluwer, Gas Natural

Sell Protection: Casino, ITV, Heathrow, Kingfisher, Merck, Pernod, PostNL, Roche, SCA, SocGen, TeliaSonera, Veolia, GDF Suez, Iberdrola

HIGH YIELD CREDIT RESEARCH

Sectors	Overweight	Underweight
	Chemicals, Gaming, Retailers, Utilities-Electric, Wireless	Airlines, Automotives, Diversified Manufacturing, Metals & Mining, Paper
Autos & Airlines	Jaguar Land Rover £ 8.125% 2018s, Jaguar Land Rover $ 7.75% 2018s, Jaguar Land Rover £ 8.25% 2020s, Jaguar Land Rover $ 8.125% 2021s, FIAT (7.75% 16s, 7% 17s)	Air France 2014s, 2016s, Conti 6.5% €16s, Conti 7.125% €18s, Conti 4.5% $ 19s, FIAT (6.375% '16, 5.625% '17, CHF 5% 15s, CHF 5.25% 16s), Faurecia (9.375% 2016, 8.75% 2019), Lufthansa, PSA 6.875% 16s, PSA 5% '16, PSA 6% '33, PSA 6.875% '16, Renault (6% 14s, 6.625%, 15s, 4.625% 16s, 5.625% 17s, 4.625% 17s), Schaeffler 6.75% 17s, 8.75% 19s
Basic Industry/ Healthcare	Albea 8.75% 19s, Albea 8.375% 19s, Ardagh 8.750% '20s, Ardagh 7.125% '17s, Ardagh 9.250% '20s, Ardagh 9.125% '20s, Ardagh 11.125% '18s (€+$), Clariant €'17s, HeidelbergCement (all rated issues), Kerling 10.625% '17s, Lecta €+262.5bp '14s, 8.875% '19s, M-Real 8.875% '13s, Reynolds 9.5% 17s, Sappi 6.625% '18s , UPM $18s, £'17s,	ArcelorMittal, Ardagh 9.25% '16s, Ardagh 7.375% €17s, Ardagh 7.375% €17s, Ardagh 7.375% $17s, Ardagh 7.375% $17s, Clondalkin €+200bp '13s, Kinove 10.000% '18s, Kinove 9.625% '18s, Lafarge, Metsa Board 8.75% '13s, Norske Skog 7.000% '17s, Norske Skog 11.750% 16s, Norske Skog 6.125% 15s, Norske Skog 7.125% 33s, Oxea € 9.625% '17, Reynolds 8.0% '16s, Sappi 6.625% '21s, Smurfit Kappa 5.125% 18s, Smurfit Kappa 4.875% 18s, Smurfit Kappa 7.25% 17s, Smurfit Kappa 7.75% 19s, Smurfit Kappa €+350 20s, Stora Enso €14s, Stora Enso €19s, Stora Enso $16s
General Industrial/Chemicals	Taylor Wimpey 10.375% '15s, Securitas Direct 8.875% 18s, Securitas Direct 8.875% 18s, Ciech 9.5% 19s	ATUGRP 11% 14s, Grohe FRNs (Sep-17), Styrolution 7.625% 16s, ISS 8.875% 16s
Consumer & Retail & Gaming	Boparan 9.875% 2018, Boparan 9.75% 2018, Cirsa 8.750% '18s, Codere 8.250% '15s, Codere 9.250% '19s, DFS FRN '18s, DFS 7.625% '18s, Dixons 6.125% '12s, Edcon €+325bp '14s, Edcon €+550bp '15s, Foodcorp 8.750% '18s, Gala 11.5% 15s, House of Fraser 8.875% '18s, Ontex 9.000% '19, Ontex 0 '18s, Phones4u 9.500% '18s, Peermont 7.750% '14s, Matalan 8.875% '16s	Agrokor 10% 16s, Campofrio 8.25% '16s, Odeon 9.000% '18s, Odeon €+500bp '18s, Picard 9.000% '18s
TMT	CETV 9.000% '17s, CETV 11.625% '16s, Kabel BW 7.500% '19s, Kabel BW 7.500% 19s, Matterhorn 7.750% 20s, Unity Media 8.125% '17s, Unity Media 8.125% '17s, Unity 9.625% 19s, Unity 9.500% '21s, Unity 5.5% 22s, Virgin Media £6.000% '21s, Virgin Media £7.000% '23s, Wind 6.500% '20, Wind 7.250% '18s, Wind 7.375% '18s, Ziggo 8.000% '18s, UPC 6.375% '22s	Numericable €+787.5 18s, Numericable 12.375% 19s, Numericable 8.75% 19s, ONO 11.125% 19s, ONO 10.875% 19s, Sunrise 7% 17s, Telenet 6.375%, Telenet 6.625% '21s, Telenet €+378bp '21s, Telenet 6.25% 22s.,Virgin Media 7.000% '18s, Virgin Media 6.500% '18s, Virgin Media $8.375% 19s, Ziggo 6.125% 17s
Transportation	**AVAN €9.5 '19s, AVAN €7.5 '18s**	Europcar 9.75 '17s Hapag-Lloyd €9 '15s, Stena 6.125% '17s, Stena 5.875% '19s, Stena 7.875% '20s
Utilities	EDP €3.25 '15s, EDP €3.75 '15, EDP €5.875 '16s, EDP €4.625 '16s, EDP €4.75 '16s, EDP £6.625 '17s	

High Yield CDS trade ideas (at current levels)

Buy Protection: ArcelorMittal, GKN, Lafarge, Lufthansa, Dixons (2y/5y steepener)

Sell Protection: British Airways, Clariant, HeidelbergCement, ELEPOR

Note: Bold text represents rating(s) change this week. Source: Barclays Research

RECENT RATING CHANGE				
Sector	**Issuer/Security**	**From**	**To**	**Date**
Transportation	AVAN €9.5 '19s, AVAN €7.5 '18s	Initiate	Overweight	10/07/2013

KEY CREDIT MARKET INDICATORS AS OF WEDNESDAY, 10 JUL 2013

	current		diff changes				3-month range			
Investment Grade	**OAS**	**yield**	**daily**	**WTD**	**MTD**	**YTD**	**OAS**		**yield**	
Corporates	145	2.2	0	-2	-2	-5	123	153	1.7	2.5
Industrials	123	1.9	0	-1	0	-5	103	127	1.5	2.2
Financials	162	2.3	0	-3	-3	-5	138	172	1.9	2.7
Basic industry	118	1.9	0	-1	-1	1	94	123	1.5	2.1
Capital goods	124	1.9	0	-1	2	-12	102	127	1.5	2.1
Communications	156	2.4	1	-2	-1	4	129	163	1.9	2.7
Consumer cyclical	99	1.5	0	-1	0	-22	84	106	1.2	1.7
Consumer non-cyclical	93	1.6	0	-1	-1	-4	77	96	1.2	1.8
Energy	124	2.0	1	1	4	11	98	128	1.4	2.2
Technology	100	2.1	0	0	-1	-33	94	129	1.6	2.2
Transportation	161	2.4	1	-1	-4	-24	129	175	1.9	2.7
Utilities	163	2.4	1	-1	0	-6	137	175	2.0	2.7
Banking senior	129	1.8	-1	-4	-4	-3	110	139	1.4	2.1
AAA	57	1.6	0	-1	-2	-10	54	72	1.1	1.9
AA	81	1.5	0	-1	0	2	72	86	1.2	1.7
A	112	1.8	0	-2	-1	-3	95	117	1.4	2.0
BBB	202	2.8	0	-3	-1	-14	169	211	2.3	3.1
AA-AAA	24		0	0	2	12	11	26		
A-AA	31		0	-1	-2	-5	23	31		
BBB-A	90		0	-1	0	-11	75	95		
IG Excess return										
Corporates			-0.02	0.11	0.21	1.23				
Industrials			-0.01	0.07	0.15	0.86				
Financials			-0.01	0.15	0.27	1.40				
AAA			0.04	0.05	0.21	0.32				
AA			0.01	0.06	0.08	0.44				
A			0.00	0.10	0.21	0.87				
BBB			-0.04	0.13	0.25	1.93				
Markit Indices										
iTraxx Main	109		3	-5	-11	-17	87	132		
iTraxx Senior Financials	158		4	-8	-10	4	126	190		
CDX IG	82		0	-5	-6	-23	69	98		
Index-Intrinsic skew										
iTraxx Main skew	0		0	-2	-5	-7	-5	6		
iTraxx SenFin skew	-1		-1	-1	-3	-6	-3	5		
CDX IG skew	-3		0	-2	-1	-2	-6	4		
Cash-CDS Basis										
iTraxx Main - Industrials	29		3	-1	-3	1	19	46		
	current		**diff changes**				**3-month range**			
Index pairs	**diff**	**ratio**	**daily**	**WTD**	**MTD**	**YTD**	**diff**		**ratio**	
CDX IG - iTraxx Main	-27	0.7x	-3	0	5	-5	-36	-16	0.7x	0.8x
iTraxx SenFin - Main	49	1.4x	1	-3	0	21	38	61	1.4x	1.5x
iTraxx SenFin - SovX	61	1.6x	3	-7	-13	17	39	93	1.4x	2.0x
iTraxx Main - SovX	12	1.1x	2	-4	-14	-4	1	35	1.0x	1.4x

	current		diff changes				3-month range			
High Yield	**OAS**	**yield**	**daily**	**WTD**	**MTD**	**YTD**	**OAS**		**yield**	
Corporates	477	6.6	-1	-10	-2	-12	408	495	5.7	6.9
Industrials	475	5.9	-1	-9	-5	-16	398	493	5.1	6.2
Financials	490	8.5	-2	-12	3	-5	434	510	7.2	9.1
Basic industry	506	6.0	-1	-11	-8	-25	429	519	5.3	6.3
Capital goods	377	5.0	-1	-8	-13	29	295	407	4.1	5.2
Communications	519	6.7	-2	-19	-21	-67	433	554	6.0	7.1
Consumer cyclical	461	5.6	0	-5	9	-3	401	477	4.9	5.9
Consumer non-cyclical	552	6.8	-2	-5	10	-11	446	560	5.8	6.9
Energy	582	6.5	-3	17	29	-11	430	585	4.7	6.5
Technology	497	6.1	-3	-16	-30	29	497	551	5.8	6.5
Transportation	577	6.7	-2	-2	2	23	476	591	5.7	7.0
Utilities	423	5.1	2	-3	4	-3	349	452	4.2	5.5
BB	377	5.3	-2	-9	-7	-7	323	396	4.5	5.7
B	585	7.4	-4	-12	-1	-46	489	606	6.8	7.8
CCC	801	9.5	-8	-22	-7	-142	711	843	8.8	10.2
BB-BBB	176		-2	-7	-5	7	153	189		
B-BB	208		-3	-2	6	-38	160	219		
CCC-B	216		-4	-10	-6	-96	205	312		
HY Total return										
Corporates			0.01	0.56	0.65	2.24				
Industrials			0.04	0.48	0.66	1.80				
Financials			-0.07	0.81	0.69	3.46				
BB			-0.04	0.49	0.67	2.17				
B			0.12	0.70	0.60	2.02				
CCC			0.04	0.67	0.49	3.44				
Markit Indices										
iTraxx XO	440		8	-15	-37	-109	367	528		
CDX HY	360		-2	-33	-38	-129	300	436		
Index-Intrinsic skew										
iTraxx XO skew	0		1	-3	-14	-25	-15	26		
CDX HY skew	7		0	-14	-19	-7	-6	31		
Cash-CDS Basis										
iTraxx XO - HY Industrials	10		14	2	-12	-58	-4	66		
	current		**diff changes**				**3-month range**			
Index pairs	**diff**	**ratio**	**daily**	**WTD**	**MTD**	**YTD**	**diff**		**ratio**	
iTraxx XO - Main	331	4.0x	6	-10	-26	-91	280	396	4.0x	4.2x
CDX HY - iTraxx XO	-81	0.8x	-10	-18	-2	-20	-102	-45	0.8x	0.9x
CDX HY - CDX IG	278	4.4x	-2	-28	-32	-106	231	339	4.3x	4.6x

Source: Bloomberg, Barclays Research

KEY NON-CORPORATE INDICATORS AS OF WEDNESDAY, 10 JUL 2013

	current	diff changes				3-month range	
Benchmark Yields		daily	WTD	MTD	YTD		
2Y Germany	0.10	0.02	-0.01	-0.08	0.13	-0.03	0.27
5Y Germany	0.60	0.04	-0.03	-0.13	0.31	0.28	0.86
10Y Germany	1.66	0.00	-0.06	-0.07	0.34	1.17	1.81
30Y Germany	2.46	0.00	-0.04	-0.02	0.29	2.06	2.53
2Y US	0.35	-0.02	-0.04	0.00	0.10	0.20	0.41
5Y US	1.46	-0.03	-0.16	0.06	0.73	0.65	1.61
10Y US	2.63	-0.01	-0.12	0.14	0.87	1.63	2.74
30Y US	3.65	0.00	-0.06	0.15	0.70	2.82	3.71
Sovereign Risk							
10Y France - Germany	0.59	0.00	0.01	-0.03	-0.09	0.47	0.65
10Y Greece - Germany	9.19	0.06	-0.22	0.12	-1.17	6.62	10.12
10Y Ireland - Germany	2.74	0.00	0.06	0.07	-0.47	2.59	3.24
10Y Italy - Germany	2.79	0.03	0.09	-0.02	-0.39	2.48	3.09
10Y Portugal - Germany	5.01	0.03	-0.29	0.35	-0.56	3.78	5.68
10Y Spain - Germany	3.14	0.07	0.21	0.11	-0.78	2.74	3.48
Rates							
3M £ LIBOR	0.51	0.00	0.00	0.00	-0.01	0.50	0.51
3M Euribor	0.22	0.00	0.00	0.00	0.03	0.20	0.23
2Y € swap	0.51	0.05	-0.01	-0.09	0.14	0.34	0.70
5Y € swap	1.13	0.06	-0.04	-0.11	0.36	0.71	1.39
10Y € swap	1.97	0.04	-0.06	-0.05	0.40	1.44	2.12
30Y € swap	2.52	0.01	-0.04	0.01	0.29	2.14	2.57
S&P 500 Sector Performance							
Consumer Discretionary	464	0.1%	1.4%	3.8%	23.5%	417	464
Consumer Staples	421	0.1%	1.9%	2.8%	16.7%	402	434
Energy	597	-0.6%	1.2%	3.1%	11.9%	549	610
Financials	270	-0.6%	1.0%	2.9%	21.9%	240	271
Healthcare	567	0.7%	1.5%	2.9%	22.5%	543	573
Industrials	382	-0.1%	1.7%	3.1%	16.0%	349	383
Information Tech	503	0.5%	0.7%	2.8%	8.4%	460	512
Materials	249	-0.1%	2.1%	3.1%	4.9%	235	259
Telecom	159	-0.4%	-1.0%	0.4%	8.5%	153	169
Utilities	193	0.5%	2.7%	0.6%	8.4%	183	210

	current	diff changes				3-month range	
Equities		daily	WTD	MTD	YTD		
Euro Stoxx 50	2,660	-0.2%	2.4%	2.1%	0.9%	2,512	2,836
FTSE 100	6,505	-0.1%	2.0%	4.5%	9.3%	6,029	6,840
CAC 40	3,841	-0.1%	2.3%	2.6%	5.2%	3,596	4,051
DAX 30	8,066	0.1%	3.2%	1.3%	5.6%	7,460	8,531
S&P 500	1,653	0.0%	1.3%	2.8%	13.7%	1,542	1,669
NIKKEI	14,417	-0.4%	0.7%	5.1%	27.9%	12,445	15,627
VIX	14	-0.1	-0.7	-2.7	-3.8	12	20
VSTOXX	20	-0.3	-2.2	-1.4	-1.0	16	25
Commodities							
Gold	1,260	8	37	25	-416	1,201	1,561
Copper	309	3	3	3	-59	303	347
Oil	109	1	1	6	-3	98	109
Gas	3.68	0.02	0.06	0.12	0.33	3.57	4.41
Corn	522	0	30	11	-78	491	571
Foreign Exchange							
EUR/USD	1.30	0.02	0.01	0.00	-0.02	1.28	1.34
EUR/JPY	129	0	0	0	15	126	133
EUR/GBP	0.86	0.00	0.00	0.01	0.05	0.84	0.86
EUR/CHF	1.24	0.00	0.01	0.01	0.04	1.21	1.26
EUR/SEK	8.71	0.02	-0.02	-0.01	0.13	8.32	8.87
EUR/NOK	7.90	0.00	-0.12	0.00	0.56	7.47	8.05
S&P Euro 350 Sector Performance							
Consumer Discretionary	1,411	0.4%	2.8%	5.2%	11.2%	1,244	1,444
Consumer Staples	2,541	0.0%	1.6%	2.8%	7.4%	2,393	2,699
Energy	1,258	0.6%	2.8%	3.0%	-2.3%	1,197	1,331
Financials	668	-0.2%	2.3%	4.6%	6.2%	619	714
Healthcare	1,684	0.3%	2.0%	2.7%	16.4%	1,560	1,757
Industrials	1,424	0.0%	2.6%	4.0%	7.8%	1,328	1,479
Information Tech	946	0.1%	2.7%	4.0%	10.4%	872	988
Materials	2,001	-0.5%	2.7%	1.0%	-12.9%	1,948	2,239
Telecom	1,027	-0.4%	1.4%	2.3%	5.9%	959	1,090
Utilities	1,101	-0.2%	1.6%	0.8%	-2.5%	1,060	1,200

Notes: Equity index/sector returns are price returns only (ex-dividends).
Source: Bloomberg, Barclays Research

REPORTING CALENDAR NEXT WEEK

Date	Company	Release/event	Economic data	Other events
Mon, 15 July	Citigroup	Q2 13	CH: **Q2 GDP**, **IP**, Retail Sales US: Retail Sales, Empire Manf, Business Inventories	
Tue, 16 July	Accor Swedbank AB Goldman Sachs	Q2 revenues Q2 13 Q2 13	EZ: CPI ("Final"), Car Registrations, ZEW Survey, Trade Balance UK: PPI, **CPI**, RPI GE: ZEW Survey US: CPI, IP	Spain T-Bills
Wed, 17 July	Nordea Novartis Telia Svenska Handel Bank of America	Q2 13 H1 Q2 13 Q2 13 Q2 13	UK: Unemployment Report US: Housing Starts	BoE Minutes Fed Beige Book
Thu, 18 July	AkzoNobel Carrefour Ericsson Nokia Norske Skog Ziggo Morgan Stanley	H1 Q2 sales Q2 13 Q2 13 Q2 13 Q2 13 Q2 13	EZ: Current Account UK: **Retail Sales** US: Jolbess Claims, Philadephia Fed, Leading Indicators	Spain Bond Auction
Fri, 19 July	Assa Abloy Fortum Scania Stora Enso Vodafone GE	H1 H1 H1 H1 Q2 13 Q2 13	UK: Public Finance GE: Producer Prices	

Note: Items in bold we consider to be more important to markets.
Source: Bloomberg, company reports, Barclays Research

THE WEEK AFTER

Date	Company	Release/event	Economic data	Other events
Mon, 22 July			US: Existing Home Sales, Chicago Fed	
Tue, 23 July	Edison	Q2 13	EZ: Consumer Confidence	Spain T-Bills
	Gas Natural	Q2 13	US: Richmond Fed Manf., HPI	
	KPN	Q2 13		
	Telenor	Q2 13		
	Vattenfall	Q2 13		
	Apple	Q2 13		
	AT&T	Q2 13		
Wed, 24 July	Compass	Q3 13	EZ: **PMIs ("Flash")**	
	Daimler	Q2 13	GE: **PMIs ("Flash")**, Import Price Index	
	Edenred	H1 13	US: New Home Sales	
	GSK	H1 13		
	Heathrow	H1 13		
	Iberdrola	Q2 13		
	Kingfisher	Q2 13		
	OMV	Trading		
	Ono	Q2 13		
	Puma	H1 13		
	St-Gobain	H1 13		
	Syngenta	H1 13		
	Tate & Lyle	Q1 13		
	Volvo	Q2 13		
	Boeing	Q2 13		
Thu, 25 July	ABB	Q2 13	EZ: M3	
	Areva	Q2 13	UK: **Q2 GDP ("First")**	
	BASF	Q2 13	GE: IFOs	
	BT	Q2 13	US: Jobless Claims, **Durable Goods**, Kansas City Fed Manf.	
	Casino	H1 13		
	Cemex	Q2 13		
	Credit Suisse	Q2 13		
	CWC	Q2 13		
	Faurecia	Q2 13		
	FT	Q2 13		
	Luxottica	H1 13		
	Michelin	Q2 13		
	PPR	H1 13		
	Reed Elsevier	Q2 13		
	Repsol	H1 13		
	SSE	IMS		
	Statoil	H1 13		
	Telefonica	Q2 13		
	Telenet	Q2 13		
	Terna	H1 13		
	Unilever	H1 13		
	GM	Q2 13		

Date	Company	Release/event	Economic data	Other events
Fri, 26 July	Air France	Q2 13	US: U. of Michigan Conf.	Italy Bond Auction
	Anglo	Q2 13		
	Banco Populare	Q2 13		
	BG Group	H1 13		
	BSkyB	Q2 13		
	Lafrage	Q2 13		
	Pearson	Q2 13		
	Rallye	Q2 13		
	Renault	Q2 13		
	SES	Q2 13		
	Total	H1 13		
	UU	IMS		

Note: Items in bold we consider to be more important to markets.
Source: Bloomberg, company reports, Barclays Research

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Analyst Certification

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Explanation of the Barclays Research High Grade Sector Weighting System

Overweight: Expected six-month excess return of the sector exceeds the six-month expected excess return of the Barclays U.S. Credit Index, the Pan-European Credit Index, or the EM Asia USD High Grade Credit Index, as applicable.

Market Weight: Expected six-month excess return of the sector is in line with the six-month expected excess return of the Barclays U.S. Credit Index, the Pan-European Credit Index, or the EM Asia USD High Grade Credit Index, as applicable.

Underweight: Expected six-month excess return of the sector is below the six-month expected excess return of the Barclays U.S. Credit Index, the Pan-European Credit Index, or the EM Asia USD High Grade Credit Index, as applicable.

Explanation of the Barclays Research High Grade Credit Rating System

The High Grade Credit rating system is based on the analyst's view of the expected excess returns over a six-month period of the issuer's index-eligible corporate debt securities relative to the Barclays U.S. Credit Index, the Pan-European Credit Index or the EM Asia USD High Grade Credit Index, as applicable.

Overweight: The analyst expects the issuer's index-eligible corporate bonds to provide positive excess returns relative to the Barclays U.S. Credit Index, the Pan-European Credit Index, or the EM Asia USD High Grade Credit Index over the next six months.

Market Weight: The analyst expects the issuer's index-eligible corporate bonds to provide excess returns in line with the Barclays U.S. Credit Index, the Pan-European Credit Index, or the EM Asia USD High Grade Credit Index over the next six months.

Underweight: The analyst expects the issuer's index-eligible corporate bonds to provide negative excess returns relative to the Barclays U.S. Credit Index, the Pan-European Credit Index, or the EM Asia USD High Grade Credit Index over the next six months.

Rating Suspended (RS): The rating has been suspended temporarily due to market events that make coverage impracticable or to comply with applicable regulations and/or firm policies in certain circumstances including where the Corporate and Investment Banking division of Barclays is acting in an advisory capacity in a merger or strategic transaction involving the company.

Coverage Suspended (CS): Coverage of this issuer has been temporarily suspended.

Not Rated (NR): An issuer which has not been assigned a formal rating.

For Australia issuers, the ratings are relative to the Barclays U.S. Credit Index or Pan-European Credit Index, as applicable.

Explanation of the Barclays Research High Yield Sector Weighting System

Overweight: Expected six-month total return of the sector exceeds the six-month expected total return of the Barclays U.S. High Yield 2% Issuer Capped Credit Index, the Pan-European High Yield 3% Issuer Capped Credit Index excluding Financials, or the EM Asia USD High Yield Corporate Credit Index, as applicable.

Market Weight: Expected six-month total return of the sector is in line with the six-month expected total return of the Barclays U.S. High Yield 2% Issuer Capped Credit Index, the Pan-European High Yield 3% Issuer Capped Credit Index excluding Financials, or the EM Asia USD High Yield Corporate Credit Index, as applicable.

Underweight: Expected six-month total return of the sector is below the six-month expected total return of the Barclays U.S. High Yield 2% Issuer Capped Credit Index, the Pan-European High Yield 3% Issuer Capped Credit Index excluding Financials, or the EM Asia USD High Yield Corporate Credit Index, as applicable.

Explanation of the Barclays Research High Yield Credit Rating System

The High Yield Credit Research team employs a relative return based rating system that, depending on the company under analysis, may be applied to either some or all of the company's debt securities, bank loans, or other instruments. Please review the latest report on a company to ascertain the application of the rating system to that company.

Overweight: The analyst expects the six-month total return of the rated debt security or instrument to exceed the six-month expected total return of the Barclays U.S. 2% Issuer Capped High Yield Credit Index, the Pan-European High Yield 3% Issuer Capped Credit Index excluding Financials, or the EM Asia

USD High Yield Corporate Credit Index, as applicable.

Market Weight: The analyst expects the six-month total return of the rated debt security or instrument to be in line with the six-month expected total return of the Barclays U.S. 2% Issuer Capped High Yield Credit Index, the Pan-European High Yield 3% Issuer Capped Credit Index excluding Financials, or the EM Asia USD High Yield Corporate Credit Index, as applicable.

Underweight: The analyst expects the six-month total return of the rated debt security or instrument to be below the six-month expected total return of the Barclays U.S. 2% Issuer Capped High Yield Credit Index, the Pan-European High Yield 3% Issuer Capped Credit Index excluding Financials, or the EM Asia USD High Yield Corporate Credit Index, as applicable.

Rating Suspended (RS): The rating has been suspended temporarily due to market events that make coverage impracticable or to comply with applicable regulations and/or firm policies in certain circumstances including where the Corporate and Investment Banking division of Barclays is acting in an advisory capacity in a merger or strategic transaction involving the company.

Coverage Suspended (CS): Coverage of this issuer has been temporarily suspended.

Not Rated (NR): An issuer which has not been assigned a formal rating.