FinanciaLounge

Italian BTPs (Italian Multi-Year State Treasury Bonds): a 120 billion euro bill for the next six months

by Giancarlo Salemi

That is the value of the debt the State has to refund on its treasury bonds from June to December. For market analysts, the pain threshold for our bonds is 400 basis points, and there will be new tensions with yields destined to rise

A big fat bill worth approximately 120 billion euro. This is the amount of debt that the State has to refund to those who placed their bets on our bonds. According to a Bloomberg projection, bonds worth 54 billion will mature in the next quarter from June to August, which will be added on to those maturing in the last four-month period from September to December for 66 billion euro. For this reason, the Treasury will have to resort to issuing new bonds and, for the analysts, the tense climate, which is mainly due to uncertainty on the Italian political front together with an international scenario with a slowing economy—with Brexit and the customs duty war between the United States and China—could raise the cost of the next bond issue.

2018 WAS VERY COSTLY FOR PUBLIC EXPENDITURE, AND THIS YEAR IT WILL BE EVEN WORSE - In 2018, the overall issue of bonds amounted to 390 billion euro, of which more than 61% is represented by medium- to long-term bonds and 39% by Italian BOTs (Italian Short-Term Treasury Bills). The average yearly cost upon issue is increasing going from 0.68% to 1.07%. According to estimates made by the Bank of Italy in its latest report on financial stability, the medium- to long-term bonds maturing this year amount to about 200 billion euro. Also taking into account the bonds with a shorter maturity and the need to cover the government's budget deficit, the gross value of bonds issued in 2019 will exceed 400 billion euro.

IN Q1, AN EXTRA COST FOR INTEREST OF ALMOST 1 BILLION EURO WAS PAID - The fact that the situation is not an easy one is demonstrated by Q1 data: 76 billion euro worth of medium- to long-term Treasury Bonds issued by the Treasury cost approximately 900 million euro more in interest than the bonds issued in the same period of last year. Unfortunately, this trend is destined to grow in the coming months. Tension and announcements feed speculation (which is then reflected above all in our bonds) and the yield spread between the Italian BTP and the German Bund ten-year curve rose suddenly from values close to 250 bps, as recorded up to a few days ago, and once again reach almost 300 points to settle subsequently at values around 280. This implies a shift in **BTP** yields, which reached 2.75% for the ten-year term. On the contrary, in other countries of the euro zone, the yield trend is falling, with **France** reaching 0.278% on the ten-year curve, the lowest since October 2016. Behind Italy, we find Cyprus at 1.3%, **Portugal** at 1.07%, while the rest are below 1%, with Germany even in the negative. Only Greece has yields higher than 3.45%.

THE "PAIN" THRESHOLD FOR BTPs IS 400 BASIS POINTS - "This is a photograph of what happened to date," explains **Vincenzo Longo**, market strategist of the Ig Group, "The threshold that would alarm operators is 400 basis points, and we are not too far off if we consider that, with 30 point leaps a day, if the situation gets out of control, we will reach this threshold in a week. In short, we must not lower our guard. Four hundred is an important threshold because, beyond that level, difficulties would be transferred to the financial institutions with the worst quality of assets, in this case, those with BTPs in their portfolios. And then, one must consider the conditions of credit deterioration that would impact families and companies for financing or mortgages. This could then push ratings agencies even to revise our rating, with a cascade of repercussions."

IF THE 400-POINT THRESHOLD IS EXCEEDED, IT IS POSSIBLE THAT THERE COULD BE A NEW GOVERNMENT OR TROIKA INTERVENTION - This analysis is also shared by **Angelo Meda**, head of equities at Banor Sim. "Even for us, the 400-basis-point threshold is the point of no return, he explained, "and the declarations of the last few days, which were certainly electoral propaganda material, to the effect that the government could push the **deficit / GDP ratio beyond 3%**, have scared some investors. It is a mistake to play with fire. The problem is that a yield spread at 270 or 290 for two to three years involves a significant slowdown of the economy, meaning that the State must pay more in interest instead of using these resources for economic development. If, in the end, the threshold of 400 is reached, then it means that a change is needed, and that we can't go on like this. It could lead to the fall of the government or even the intervention of the troika, scenarios that we hope will not materialise, but which the markets take into account".

Yield of the 10-year BTP from April 2018 to date (Source: AskBrokers)

A FALLING YIELD SPREAD SCENARIO IS DIFFICULT TO IMAGINE, AND THIS REMAINS THE REAL ITALIAN PROBLEM - For analysts, however, a reversal of the trend, possibly with a yield spread falling to around 200 basis points, is really not at all realistic. “We do not expect significant falls,” explained Longo, “because we are in a situation of fragile growth for Italy. The lowest threshold could be 230 basis points, which was the level reached in more conciliatory phases, but improvements beyond that level can be discounted”. “**Our country will have to fight against the yield spread for a long time**,” concluded Meda. “It does not have great prospects on the banking or financial market. We have to free ourselves of this ballast, the yield spread, which costs companies at least 20% to 30% more with respect to their European counterparts operating in the same sectors and with the same parameters”.

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