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Irish Bonds Lead High-Deficit Nations' Slump as Crisis Deepens

2010-11-23 13:00:40.913 GMT

By Paul Dobson and Lukanyo Mnyanda

Nov. 23 (Bloomberg) -- Irish bonds led a slump in debt issued by the euro area's high-deficit nations amid speculation that rescue talks won't damp the region's escalating crisis.

Spanish and Portuguese securities slid on concern more countries will struggle to manage their obligations as borrowing costs surge. Irish Prime Minister Brian Cowen signaled yesterday he would call elections for early 2011, triggering concern any agreement on a bailout may not be upheld. German two-year yields dropped below 1 percent after North and South Korea exchanged fire, pushing investors to seek the safest assets.

"This political uncertainty won't let Ireland enjoy the upcoming benefits of an aid package," said Ioannis Sokos, an interest-rate strategist at BNP Paribas SA in London. "There's clearly a contagion effect from Ireland" for other euro-area nations, he said.

Irish 10-year bonds fell, sending the yield 24 basis points higher to 8.55 percent as of 12:47 p.m. in London. The extra yield investors demand to hold the securities instead of German bunds widened 25 basis points to 569 basis points.

Spanish 10-year bonds dropped a sixth day, with the yield 12 basis points higher at 4.87 percent. Portugal's 10-year yield rose seven basis points to 6.88 percent.

The yield on the 10-year bund declined four basis points, or 0.04 percentage point, to 2.61 percent. The 2.25 percent security maturing in September 2020 gained 0.33, or 3.30 euros per 1,000-euro ($1,354) face amount, fell to 96.93. Two-year yields fell five basis points to 0.99 percent and touched 0.98 percent, the lowest since Nov. 12, according to Bloomberg generic data.

Spanish Auction

Today's drop in Irish bonds reversed yesterday's advance, when a request by the government for financial aid from the European Union and International Monetary Fund initially buoyed the securities. The country's Green Party plans to pull out of the ruling coalition following a vote on the budget, saying Cowen misled voters in negotiating the bailout.

Spain sold 3.3 billion euros of Treasury bills today at higher yields than previous sales. The indicative range set for the offering was 3 billion euros to 4 billion euros.

"None of these countries look sustainable, and that means wider spreads" between benchmark bunds and peripheral-nation debt, said Mark Schofield, head of interest-rate strategy at Citigroup Inc. in London. "Korea is another bit of uncertainty at a time when the markets are very nervous."

North Korea fired dozens of artillery shells near the western border with South Korea, prompting the South to scramble jets and return fire. Equities fell, with the Stoxx Europe 600 Index 0.7 percent lower.

‘Internal Turbulence’

“The Korean headlines have had a negative impact on risky markets, and that’s added to the flight to quality we were seeing because of our own internal turbulence,” said David Schnautz, a fixed-income strategist at Commerzbank AG in London.
“We are confident of seeing bund yields heading lower.”

Bond yields in the so-called peripheral nations initially subsided after the EU and the IMF announced a backstop for ailing nations worth about $1 trillion on May 10. They’ve since risen, with the increase accelerating since European leaders agreed Oct. 29 to consider German Chancellor Angela Merkel’s proposal for a permanent rescue mechanism as of 2013 that would include losses for sovereign-debt holders.

“The markets currently have virtually zero confidence that the bailout in Ireland will solve the European crisis,” Charles Diebel and David Page, fixed-income strategists at Lloyds TSB Corporate Markets in London, wrote in a note today. “With markets effectively in a position to dictate policy, the risk is that the credibility crisis shifts to more sizeable EU countries and thereby poses a greater risk to the system as a whole.”

Greek Bonds

Greek bonds dropped after the EU and IMF said Greece must make an “extra effort” to cut its deficit to keep receiving aid. Spain missed its maximum target in a sale of debt today.

Greece’s pledge to trim its budget shortfall to 7.5 percent of gross domestic product next year has been complicated by slower-than-forecast revenue growth and a revision of economic data, EU and IMF officials reviewing Greece’s progress said at a press conference in Athens today. The 10-year yield rose four basis points to 12.01 percent.

“Buying Portuguese sovereign debt is a good investment,” Portuguese Prime Minister Jose Socrates said in an interview on television channel SIC Noticias. Portugal “doesn’t need aid. We will solve our own problems.”

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