

It's not just Deutsche Bank and Commerzbank. Several major Eurozone Banks are now in Unstable Contraction.

During the Financial Crisis of 2008-2009, most large European banks went into 'Unstable Contraction' — indicative of anti-bubbles of panic selling. Now, with the Euro Stoxx® Banks Index down 26% in the past year, some major Eurozone banks have entered this danger zone again. Deutsche Bank¹ and Commerzbank have now been joined by ING and UniCredit, among others.

Unstable Contractions: Anti-Bubble Indicators.

Just as Unstable Expansion—unsustainable asset price increases—emerge during market booms, market busts can produce Unstable Contractions. These are leading indicators of anti-bubbles of panic selling.

Like Unstable Expansions, our Unstable Contraction Indicators also come with a predicted Correction Level. To a short seller who constantly reinvests his profits (compounding minus the daily return) the Unstable Contraction looks like an expanding bubble as the actual price falls. The Correction Level is the share price that returns this position to its breakeven value.

Unlike the case of Unstable Expansions which eventually correct as booms turn to busts, a share price in Unstable Contraction doesn't have to reach its Correction Level— the share price can go to zero. This is exactly what happened to Lehman Brothers which went into Unstable Contraction late in 2007.

Merging Anti Bubbles is a Bad Idea.

During the Financial Crisis of 2007-2009, most large European and U.S. banks went into Unstable Contraction. Some, like Barclays, Goldman Sachs and Morgan Stanley, survived by selling— they secured additional capital. Others, like Commerzbank, suffered devastating losses after merging with another bank that was also in Unstable Contraction.

From the point of view of a trader, an anti-bubble is something to sell, just as a bubble is something to buy, as long as he has an exit strategy.

In our October 2016² comment on the announcement that a merger of Banca Popolare di Milano and Banco

Popolare had obtained regulatory approval from the Banca d'Italia and the ECB we observed that both banks were in Unstable Contraction. The merged entity, Banco BPM, has dropped 52% from its 2017 peak and is now in Unstable Contraction. Over the same period the Euro Stoxx® Banks Index, which contains Banco BPM as well as Commerzbank and Deutsche Bank, has lost 'only' 41%.

More Accidents Avoided—for Now.

As we pointed out prior to Deutsche Bank's restructuring announcement¹, abandoning the Commerzbank merger at least avoided the Financial Crisis era mistake of combining two banks in Unstable Contraction. Buying shares in this 'anti-bubble' mode is the same as being short a bubble — a recipe for large losses.

In August 2008, Lehman Brothers had been in Unstable Contraction for months but its management turned down the price offered by the Korean Development Bank. Now, Deutsche Bank, still in Unstable Contraction and trading well below its Correction Level, has also decided claimed that it won't need to raise capital.

Once Commerzbank and Deutsche Bank abandoned their merger talks, UniCredit and ING both looked into a takeover of Commerzbank³. By mid June it was reported that ING had abandoned the takeover⁴ and days later the UniCredit plan was put 'on ice for now'⁵.

That's just as well because the shares of all three banks have been in Unstable Contraction for months and are trading below their Correction Levels⁶.

(continued)

¹ Accidents Waiting to Happen - Deutsche Bank 31 May 2019, <https://www.omegaanalysis.com/accidentswaitingtohappen>

² *Bank Mergers: Back to the mistakes of 2008? What Just Happened?* 18 October 2016, <https://www.omegaanalysis.com/bank-sector>

³ *ING, UniCredit Tap Advisors to Explore Commerzbank* Bloomberg 14 May 2019, <https://www.bloomberg.com/news/articles/2019-05-14/ing-unicredit-said-to-tap-advisers-to-explore-commerzbank-bid>

⁴ *ING will not pursue Commerzbank tie-up* Reuters 10 June 2019, <https://uk.reuters.com/article/us-commerzbank-m-a-ing-groep/ing-will-not-pursue-commerzbank-tie-up-handelsblatt-idUKKCN1TB10M>

⁵ *UniCredit Commerzbank on Ice* Reuters 24 June 2019, <https://uk.reuters.com/article/us-commerzbank-m-a-unicredit-exclusive/exclusive-italys-unicredit-puts-possible-commerzbank-bid-on-ice-for-now-sources-idUKKCN1TP1S0>

⁶ As are Intesa San Paolo and UBI Banca. For more information on anti-bubbles in Italian Banks contact Research@OmegaAnalysis.com.

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It Can Always Get Worse.

Christopher Fildes, who used to cover the City of London for the Evening Standard, frequently observed that there's no problem so bad it can't be made worse by a politician.

When Commerzbank announced its takeover of Dresdner Bank at the end of August 2008, it was reported that Dresdner management had turned down an offer of better terms (more money and fewer job cuts) from the China Development Bank, on grounds that the Government was wary of foreign investors, especially in strategic interests⁷. As of the close on Friday 2 August 2019, Commerzbank shareholders were down over 96% since that decision was announced.

After failing in its efforts to put Deutsche Bank and Commerzbank together, the German Government, which has a 15.5% stake in Commerzbank was reportedly in talks with Dutch finance ministry about an ING linkup⁸.

A Repeat of the Mistakes of 2008?

We now have the technology that would have alerted management, regulators and politicians of the dangers of encouraging floundering banks to cling to each other instead of the lifeguard in the 2008 crisis..

That technology is producing clear warning signals. Shareholders in Commerzbank, ING and UniCredit (and any other bank touted as a 'saviour' for Commerzbank) should listen..

⁷ Germany's Commerzbank Agrees to Buy Dresdner Deutsche Welle 31 August 2008,
<https://www.dw.com/en/germanys-commerzbank-agrees-to-buy-dresdner/a-3606354-0>

⁸ German Govt pursuing ING Commerzbank deal Bloomberg 6 June 2019,
<https://www.bloomberg.com/news/articles/2019-06-06/germany-said-to-explore-commerzbank-ing-deal-with-netherlands>

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