



## Bond Market Update

**ECB Bond Market Contact Group, prepared by MS Sales and Trading (Research reports used are clearly referenced)**

**September 2022**

**Harriet Hart-Fox, Head of Client Macro Advisory EMEA**

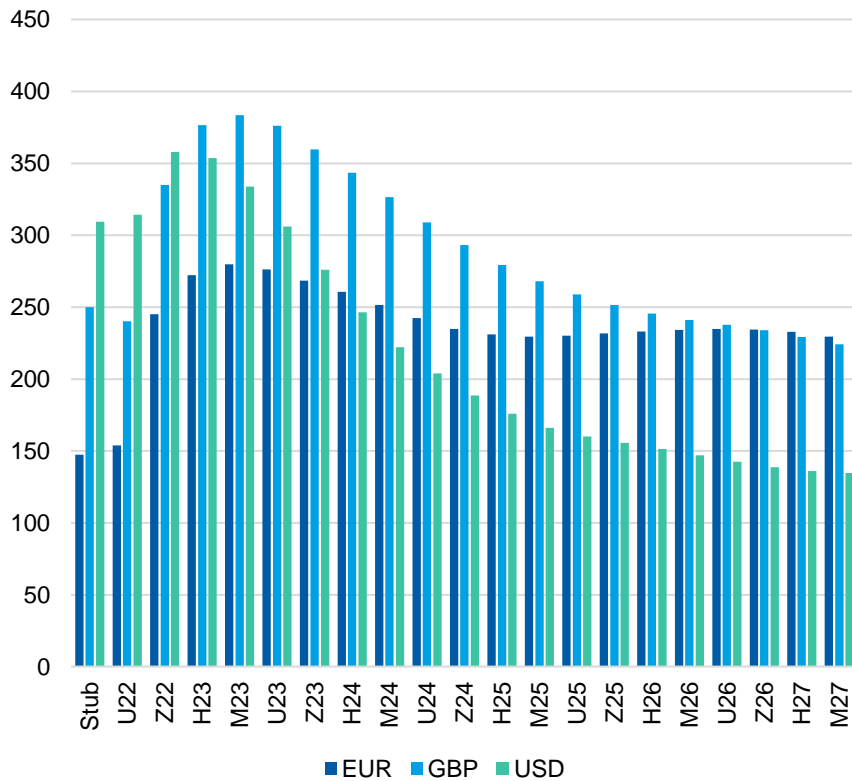
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# Front End Rates Remain in the Driving Seat

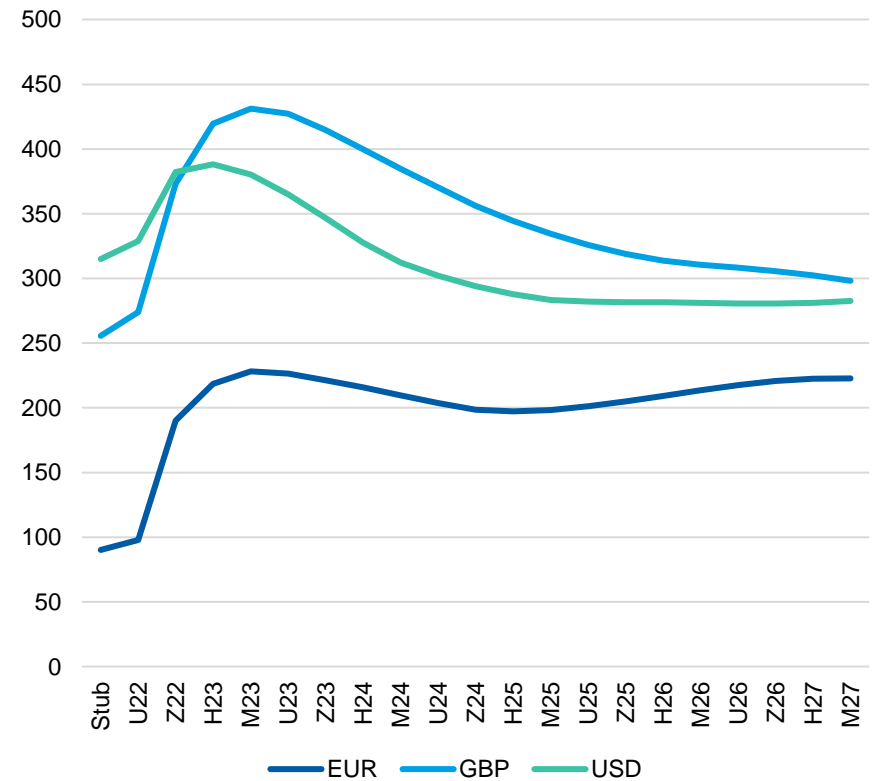
## Front End Rates Have Repriced Significantly This Year

OIS CoY (bps)



## Rate Forward Pricing

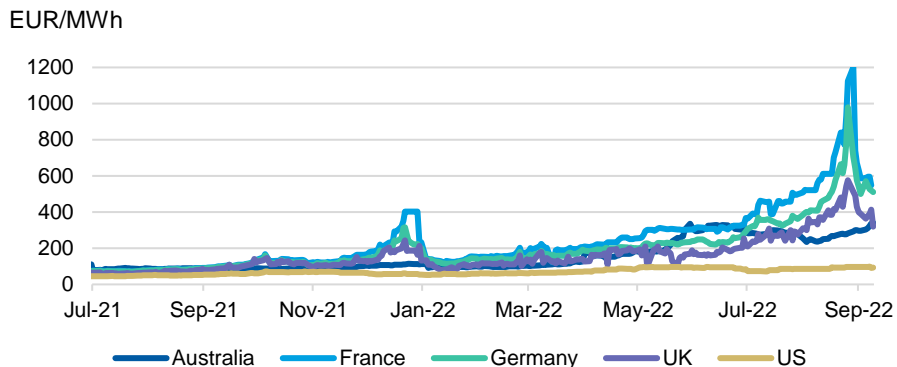
OIS (bps)



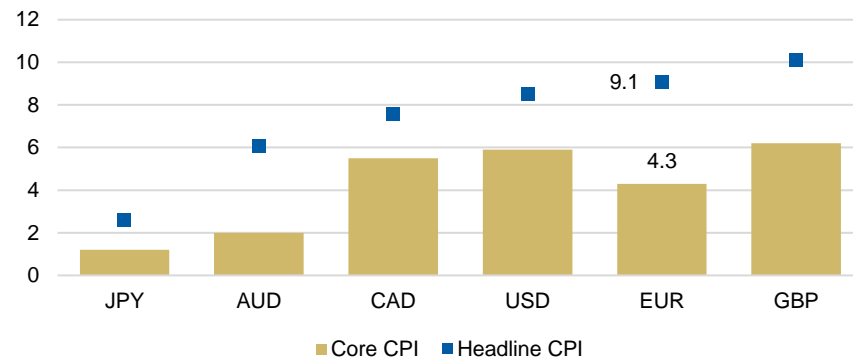
Source: MS Interest Rates Desk

# European Inflation Narrative... Still Driven By Gas/Energy

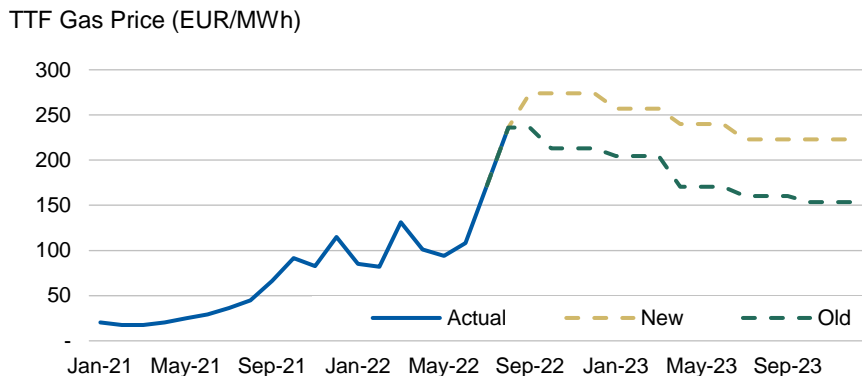
## Energy Prices Have Risen More Meaningfully in Europe than Elsewhere



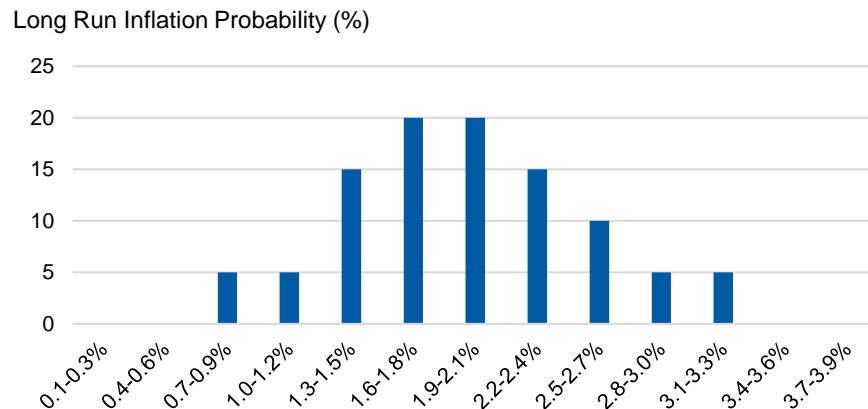
## Which Drives a Greater Divergence Between Core and Headline CPI



## MS Research Recently Revised Our TTF Forecasts Even Higher



## Skewing Long Run Inflation Probabilities Distribution to the Upside

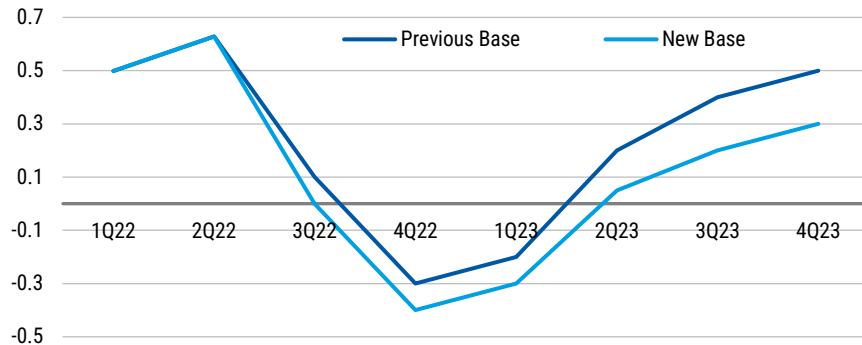


Source: Bloomberg, MS Research ([A Further Downgrade](#); [Elevator to Neutral](#))

# Against A Challenging Growth Outlook

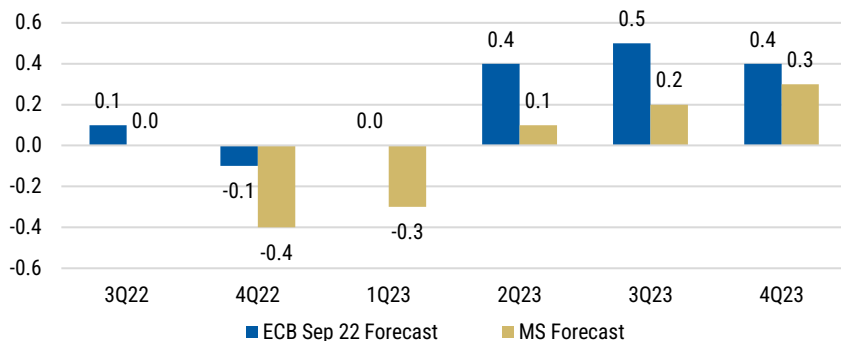
## MS Economics Revised Down EA Growth into Deeper Recession

GDP Growth (%Q)



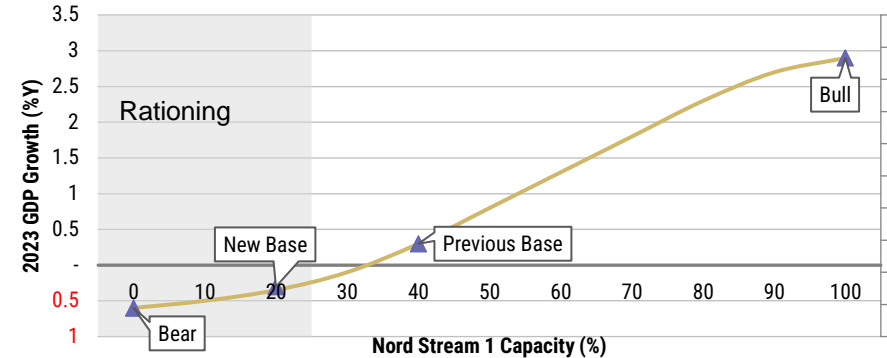
## Our Growth Forecasts See Further Downside to Even the ECB's Revised Projections

Euro Area Growth Forecast (%Q)



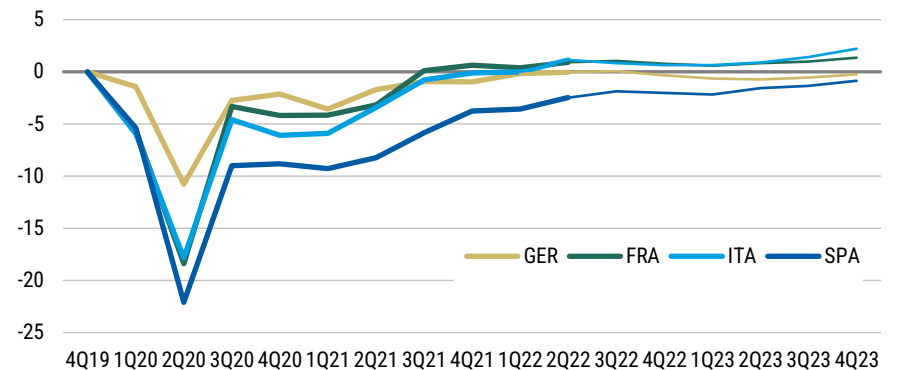
## New Base Case Also Sees a Drag on Economic Activity Driven by Power Rationing

2023 GDP forecasts and Nord Stream 1 Flows



## Growth Forecasts Diverge Across Countries

Euro Area GDP Forecasts (4Q19=0)



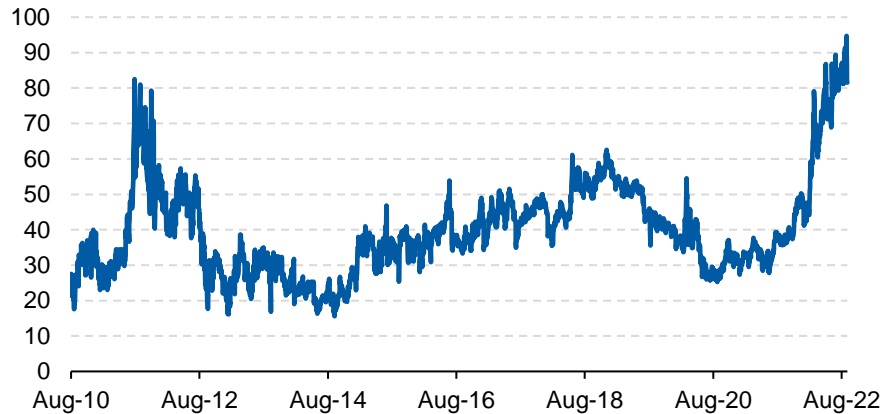
Source: Eurostat, MS Research ([A Further Downgrade](#); [Italy Economics and Strategy: At a Turning Point](#); [Elevator to Neutral](#))

# Bond Yields are at Historically Low Levels vs Swaps

Paying Flows in EUR Swaps Have Likely Led to Widening of the Spread

## Bund Asset Swaps are at Highest Levels of the Past Decade

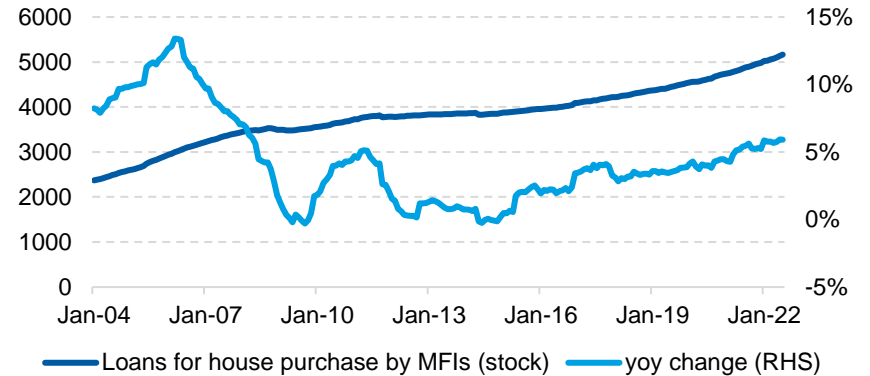
Swap minus Bund (bp)



- ASWs have widened aggressively this year despite ECB stopping asset purchases and potential for higher issuance on larger deficits going forward
- Paying flows, from sources such as mortgage hedging, have likely been behind this
- Moreover, receiving needs from ALM hedgers have been low
- Positioning for higher rates through bond/bond forwards has attractive levels on a relative basis

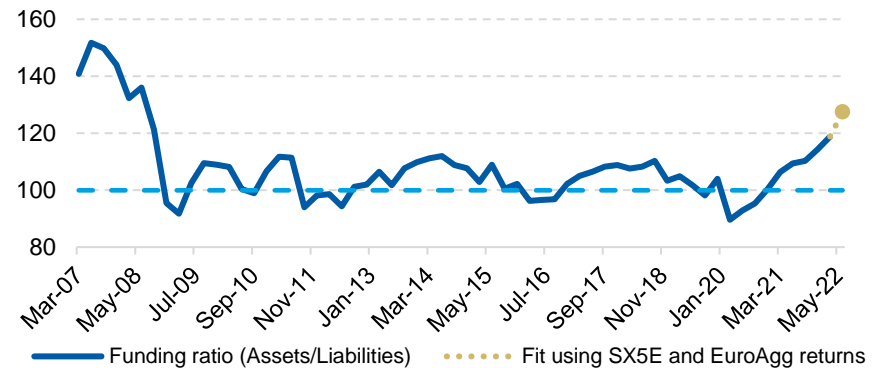
## Rapid Mortgage Growth Has Led to Swap Paying

(EUR bn)



## High PF Funding Ratios Suggest Receiving Needs Have Been Low

Dutch PF funding ratios (%)

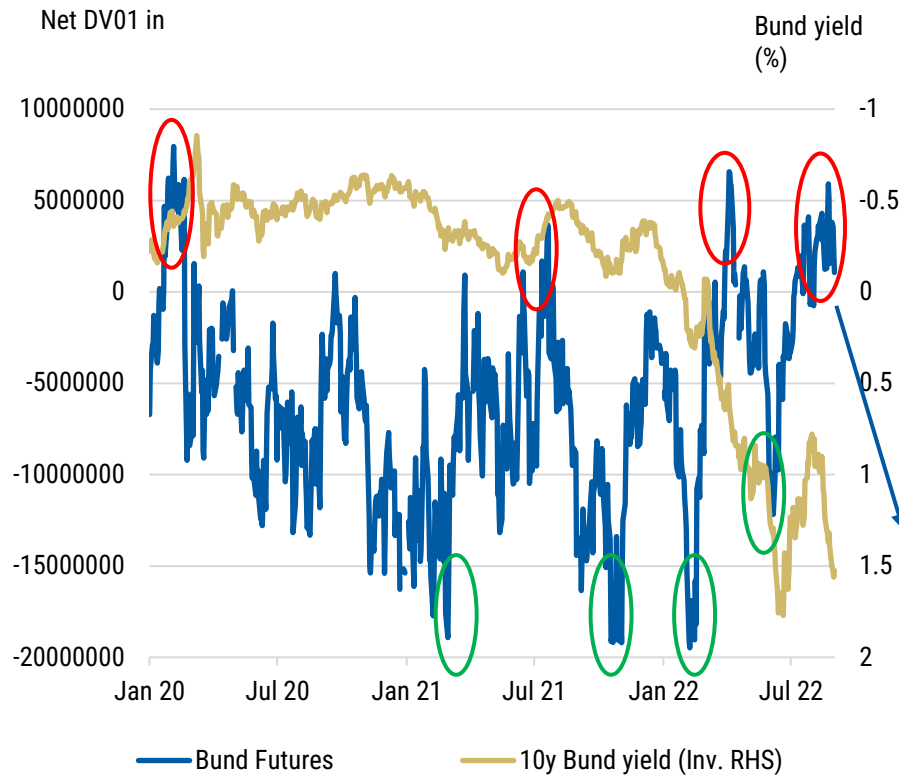


Source: ECB, DNB, Bloomberg, MS Interest Rates Desk

Please see additional important information and qualifications at the end of this material.

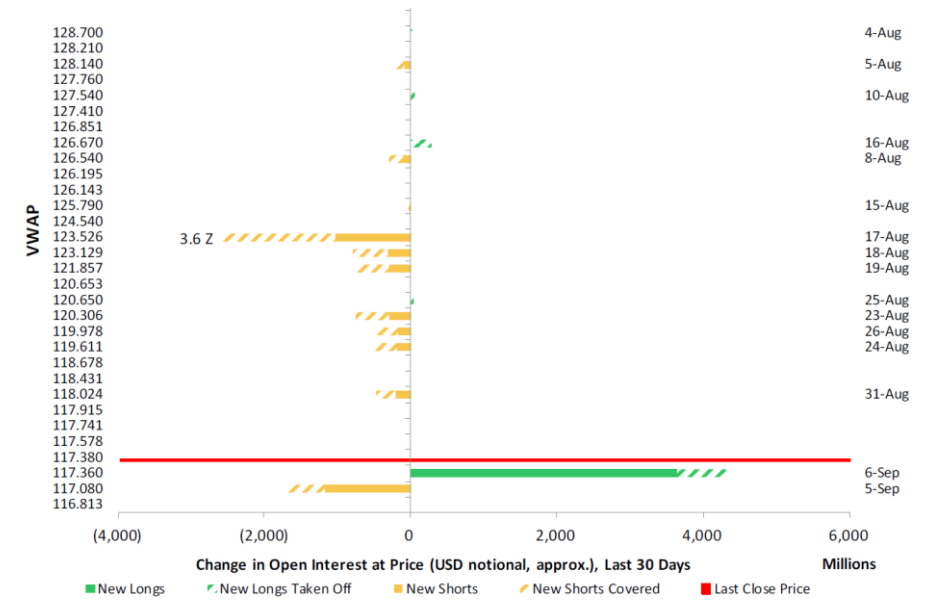
# Flows & Positioning – Interest Rate Futures

## Investors' Net Positioning in Bund Futures is Still Long



## Significant Attention Around BTP Positioning

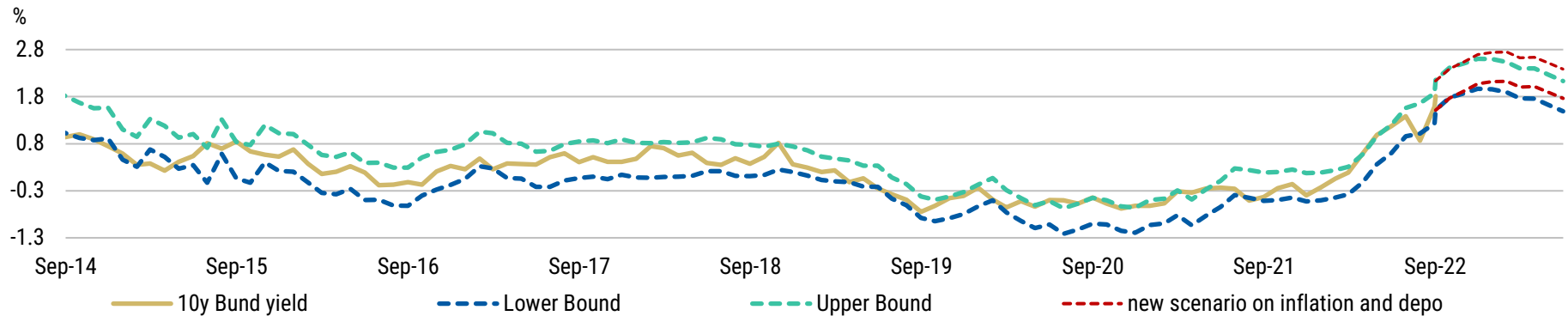
Eurex Euro-BTP Futures (IK)



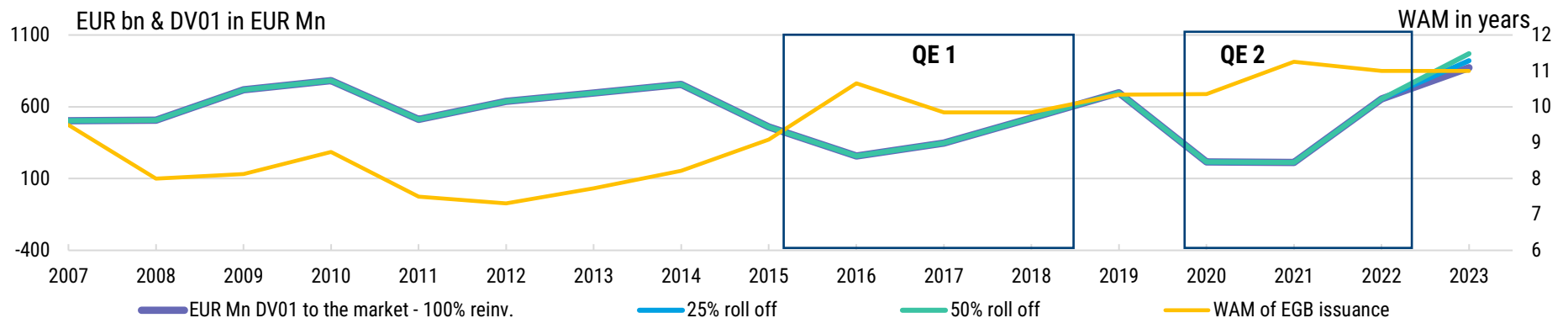
Source: Bloomberg, MS Research ([European Rates](#)); MS Futures Desk

# Path Forward for 10Y Bund Yield and APP Reinvestments

## Previous and New Forward Theoretical Path on the 10-year Bund Yield



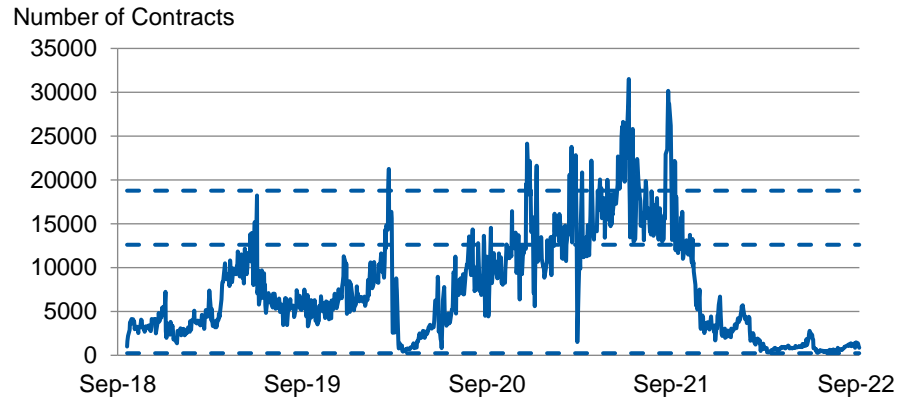
## EGB DV01 Going into the Market under Full or Partial APP Reinvestments in 2023



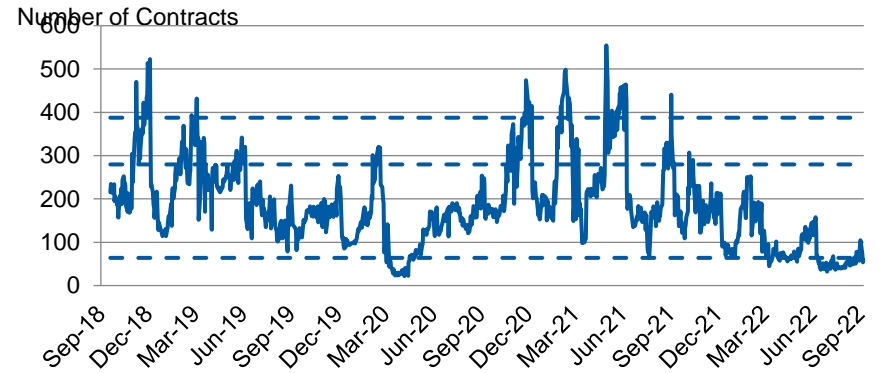
Source: Bloomberg, MS Research ([European Rates](#))

# Average Available Size

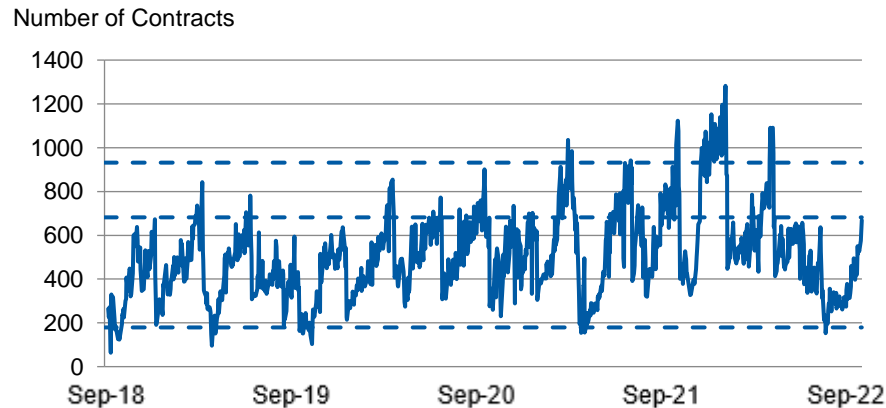
**(Volume-Weighted) Average Available Size (ex-listed spreads)**  
**Eurex Euro-Schat Futures (DU)**



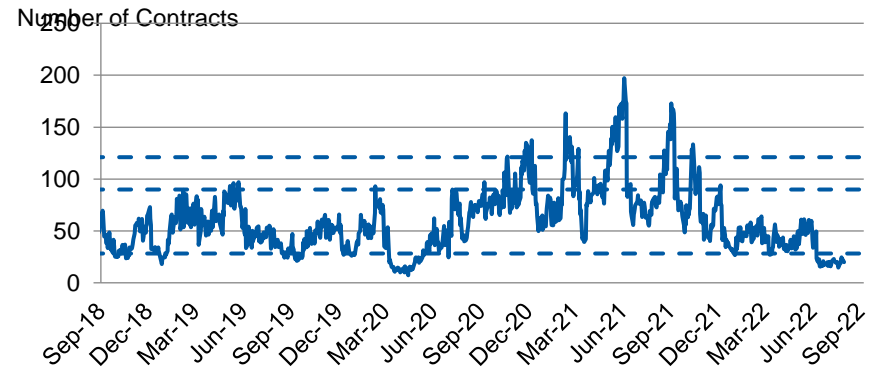
**(Volume-Weighted) Average Available Size (ex-listed spreads)**  
**Eurex Euro-Bobl Futures (OAT)**



**(Volume-Weighted) Average Available Size (ex-listed spreads)**  
**Eurex Euro-Bund Futures (RX)**



**(Volume-Weighted) Average Available Size (ex-listed spreads)**  
**Eurex Euro-Buxl Futures (IK)**



Source: Bloomberg, MS Futures Desk



## Points For Discussion

- **Market Expectations Beyond the Change in Official Rate**
- **Liquidity & Leverage In a World of Central Bank Balance Sheet Withdrawal**
- **Politics In Europe – How the Current Political Landscape May Shape Government Policy Going Forward**

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