



Bond Market Update

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

September 2022

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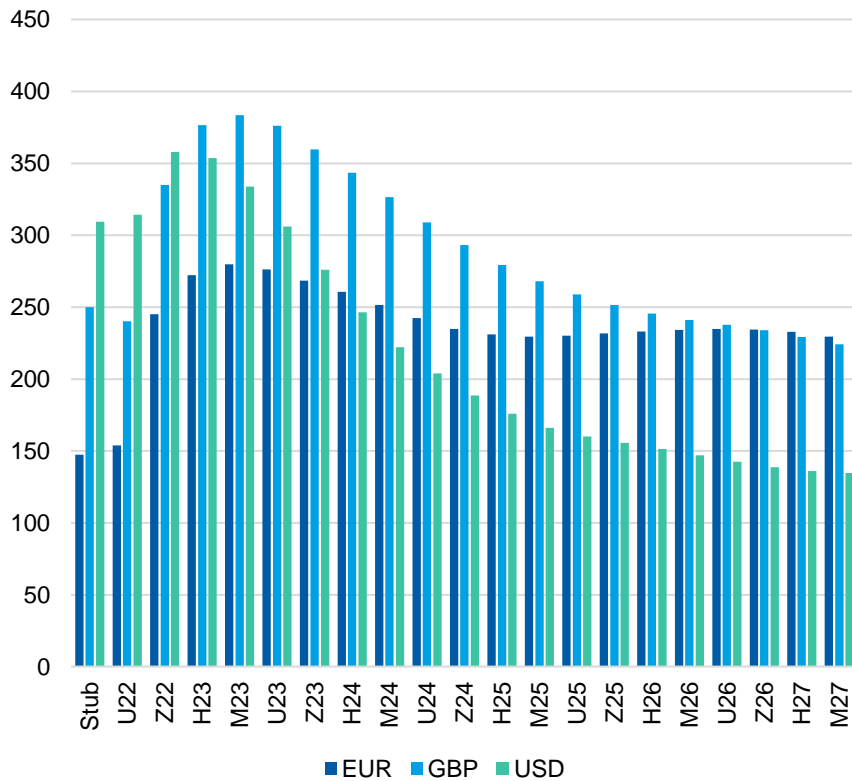
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Front End Rates Remain in the Driving Seat

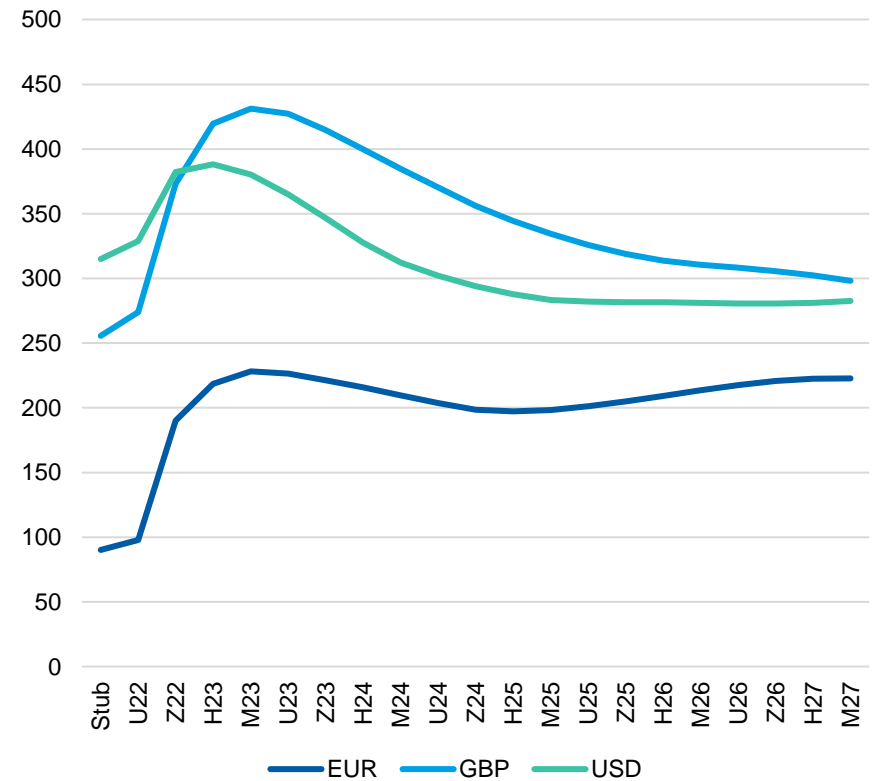
Front End Rates Have Repriced Significantly This Year

OIS CoY (bps)



Rate Forward Pricing

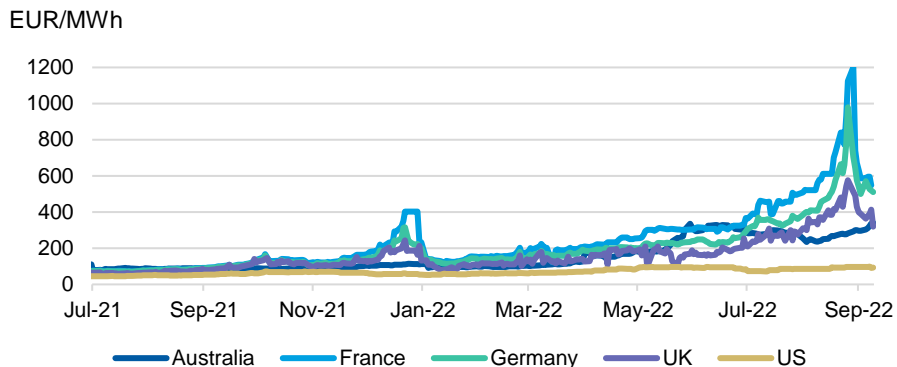
OIS (bps)



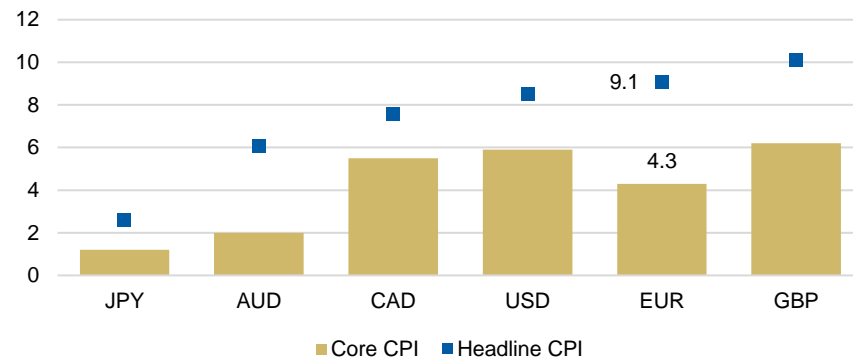
Source: MS Interest Rates Desk

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

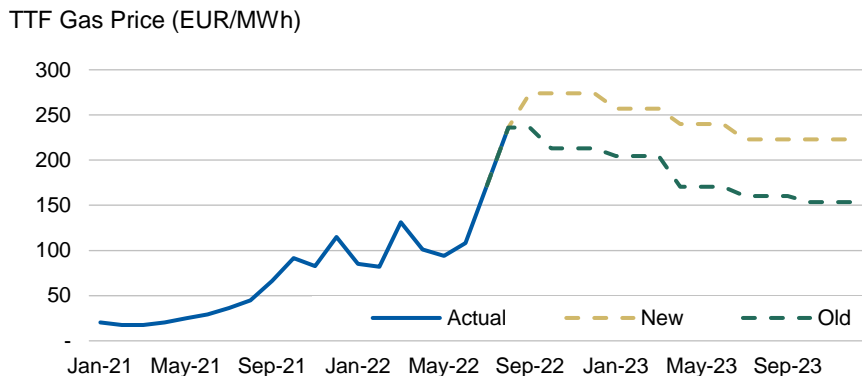
Energy Prices Have Risen More Meaningfully in Europe than Elsewhere



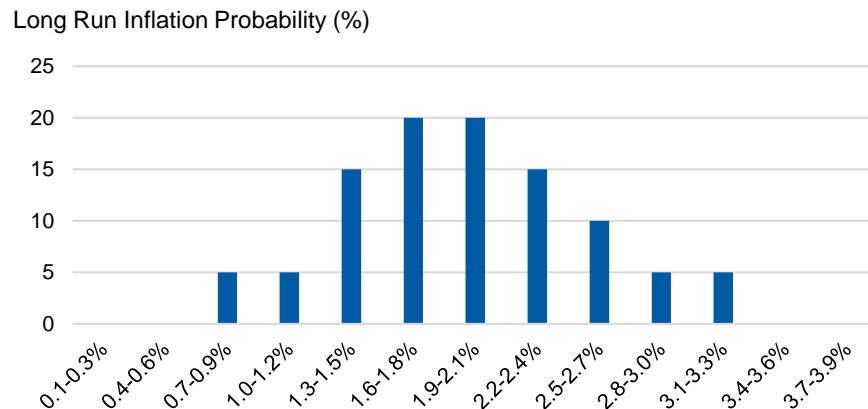
Which Drives a Greater Divergence Between Core and Headline CPI



MS Research Recently Revised Our TTF Forecasts Even Higher



Skewing Long Run Inflation Probabilities Distribution to the Upside

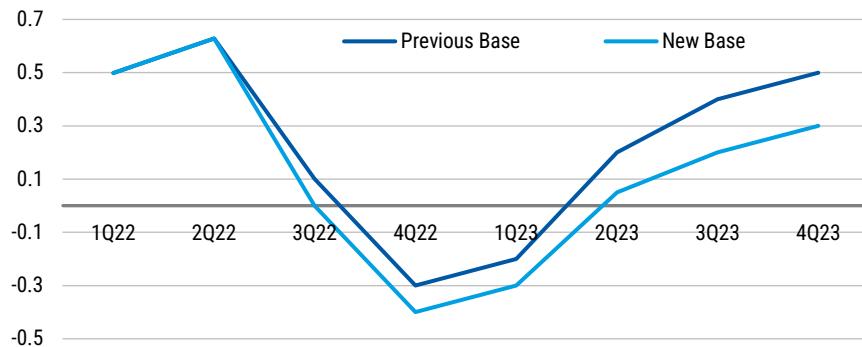


Source: Bloomberg, MS Research ([A Further Downgrade](#); [Elevator to Neutral](#))

Against A Challenging Growth Outlook

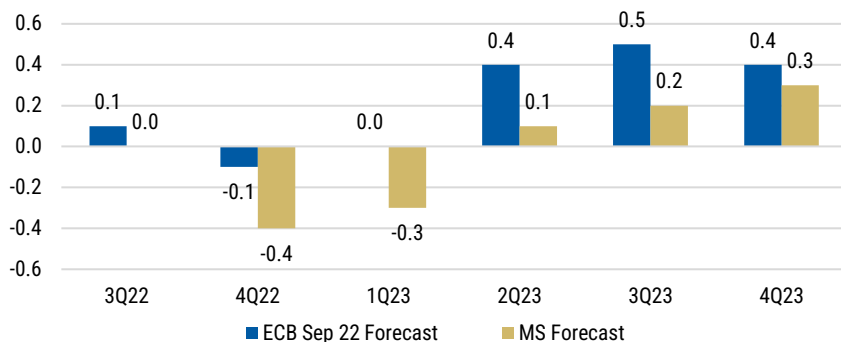
MS Economics Revised Down EA Growth into Deeper Recession

GDP Growth (%Q)



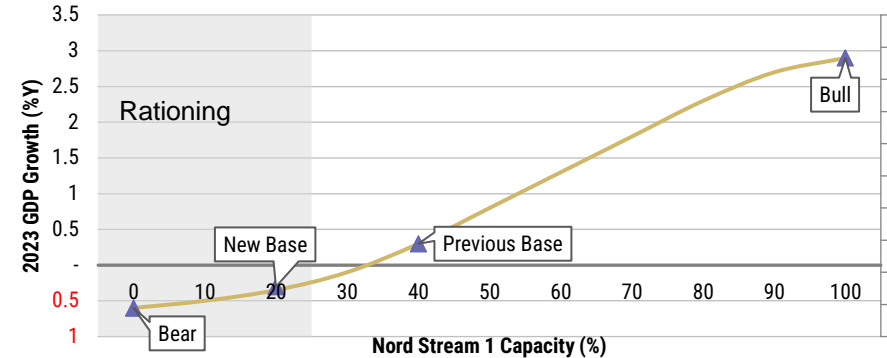
Our Growth Forecasts See Further Downside to Even the ECB's Revised Projections

Euro Area Growth Forecast (%Q)



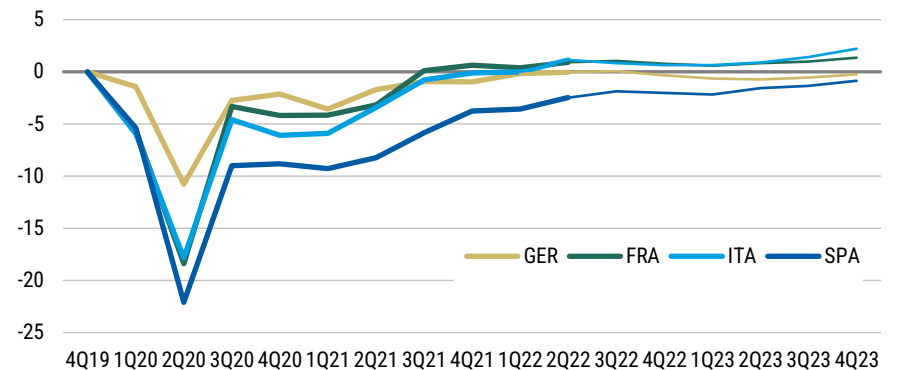
New Base Case Also Sees a Drag on Economic Activity Driven by Power Rationing

2023 GDP forecasts and Nord Stream 1 Flows



Growth Forecasts Diverge Across Countries

Euro Area GDP Forecasts (4Q19=0)



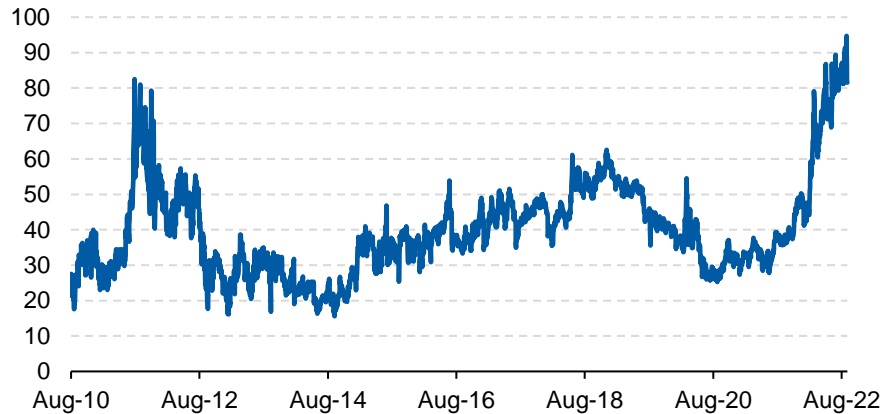
Source: Eurostat, MS Research ([A Further Downgrade](#); [Italy Economics and Strategy: At a Turning Point](#); [Elevator to Neutral](#))

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

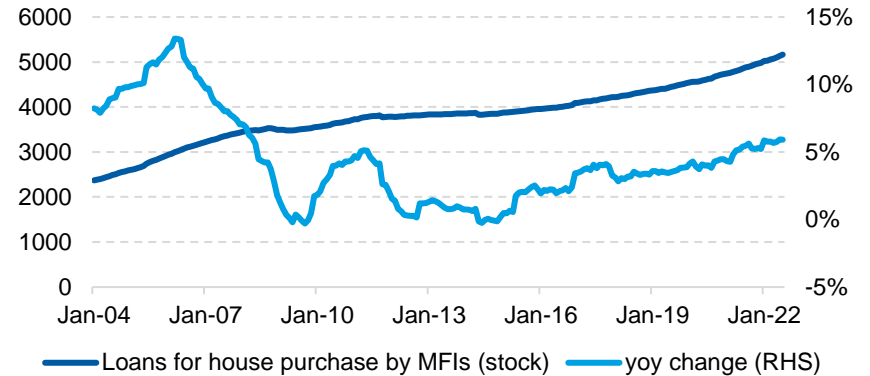
Swap minus Bund (bp)



- 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

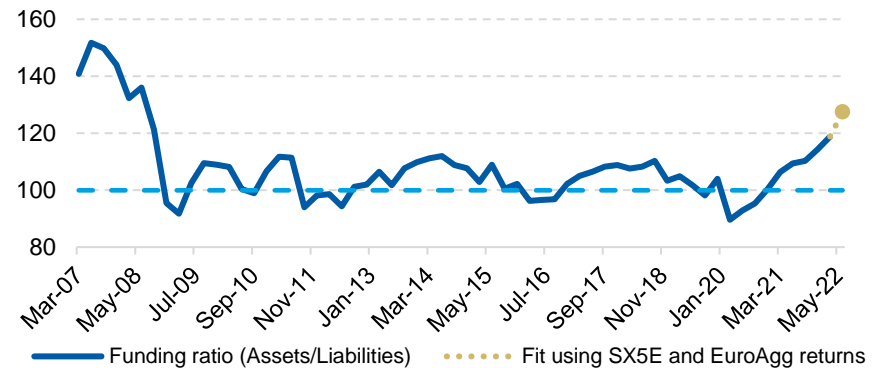
Rapid Mortgage Growth Has Led to Swap Paying

(EUR bn)



High PF Funding Ratios Suggest Receiving Needs Have Been Low

Dutch PF funding ratios (%)

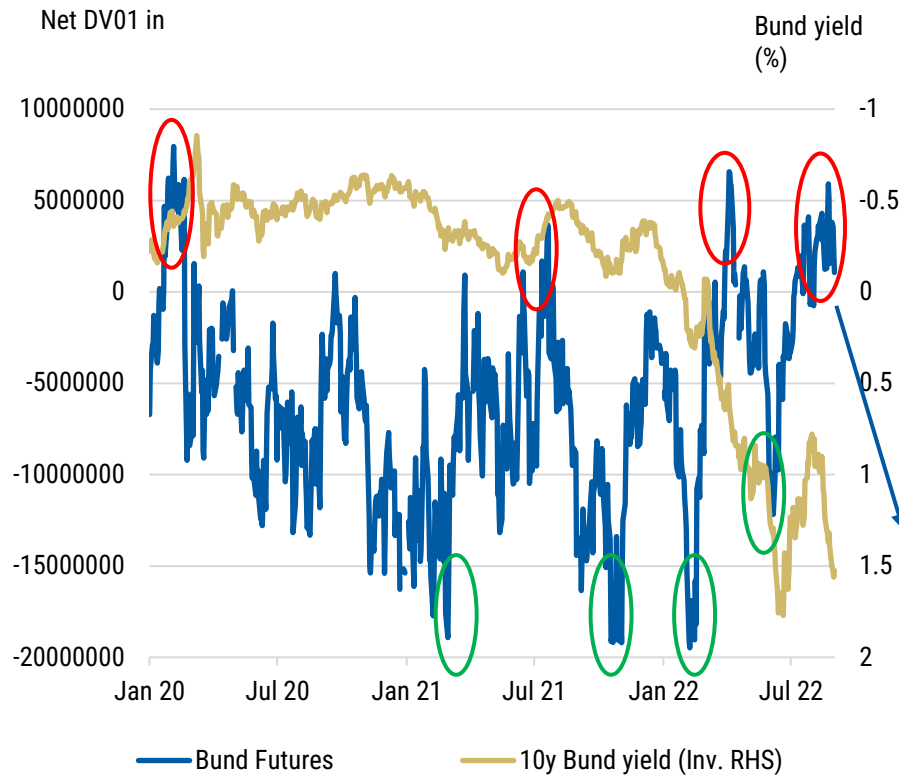


Source: ECB, DNB, Bloomberg, MS Interest Rates Desk

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

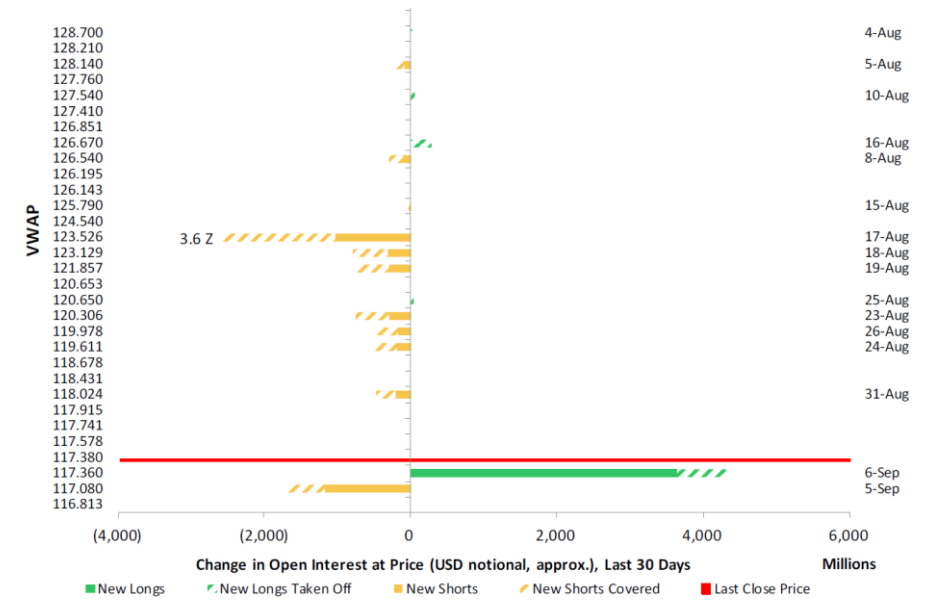
Flows & Positioning – Interest Rate Futures

Investors' Net Positioning in Bund Futures is Still Long



Significant Attention Around BTP Positioning

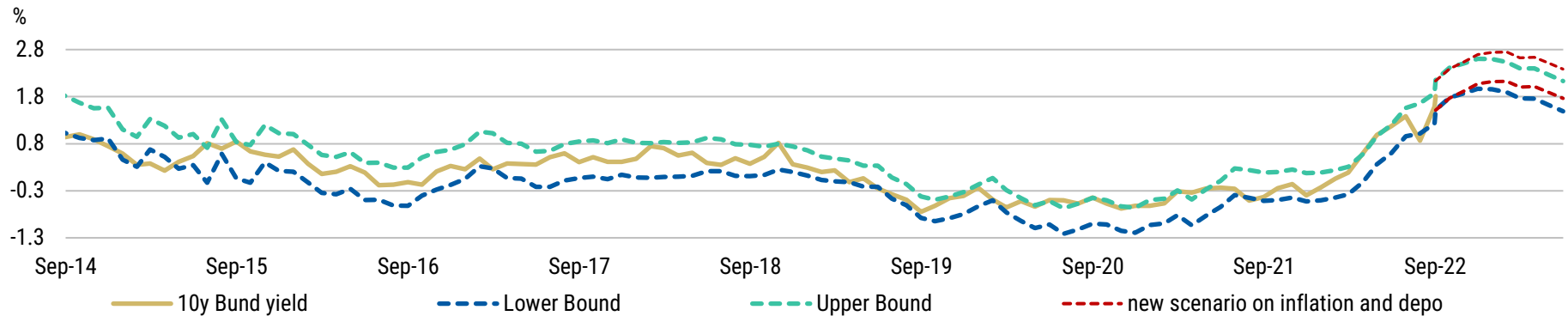
Eurex Euro-BTP Futures (IK)



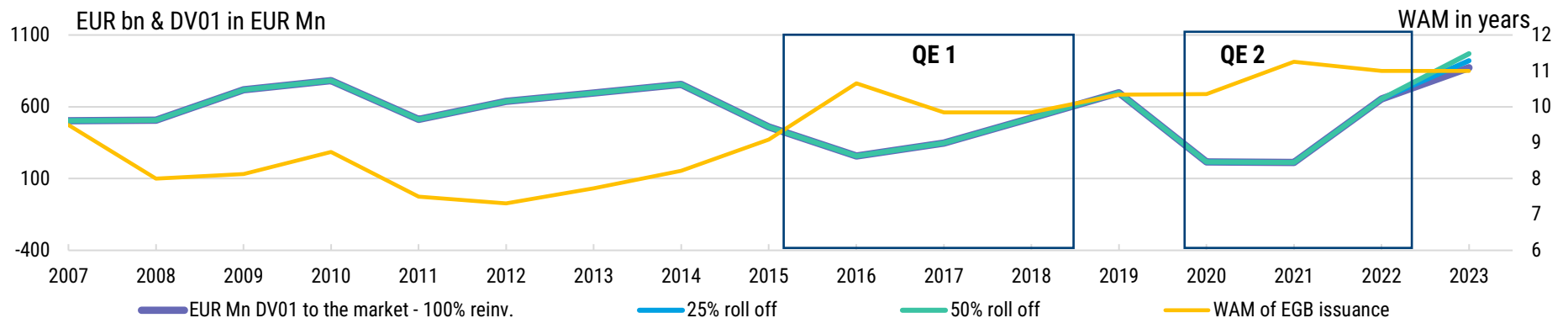
Source: Bloomberg, MS Research ([European Rates](#)); MS Futures Desk

Path Forward for 10Y Bund Yield and APP Reinvestments

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



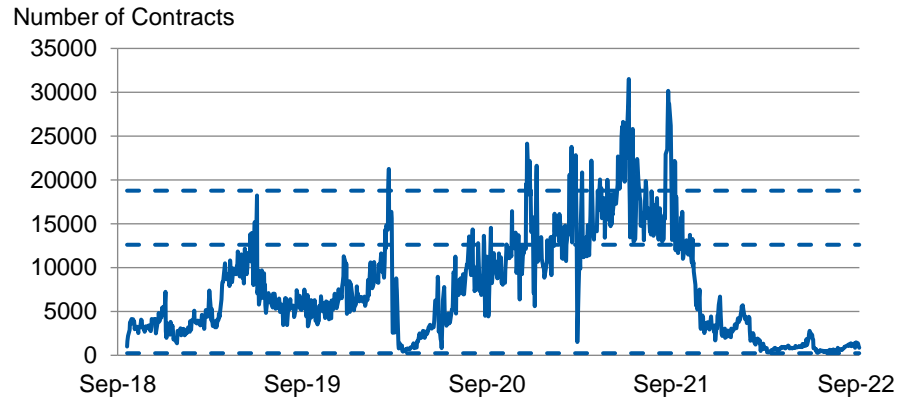
EGB DV01 Going into the Market under Full or Partial APP Reinvestments in 2023



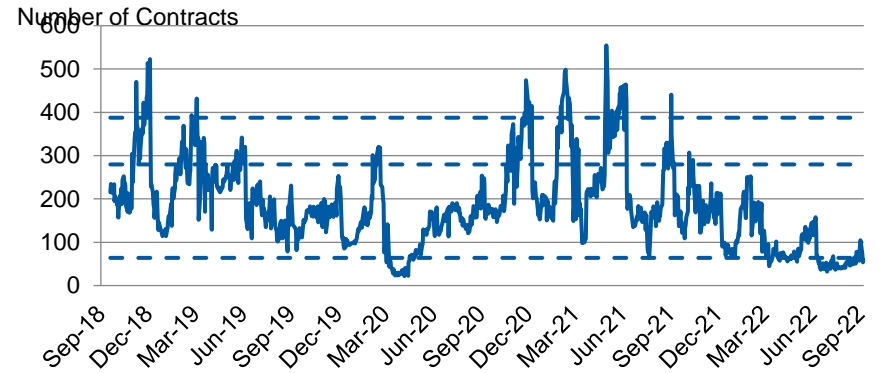
Source: Bloomberg, MS Research ([European Rates](#))

Average Available Size

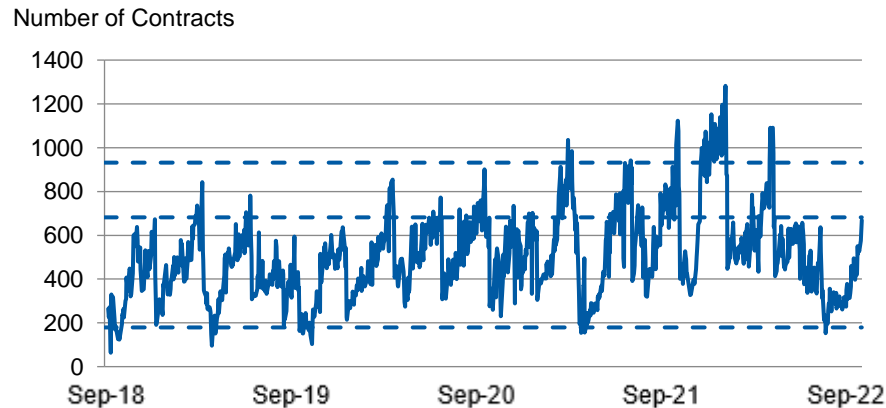
(Volume-Weighted) Average Available Size (ex-listed spreads)
Eurex Euro-Schat Futures (DU)



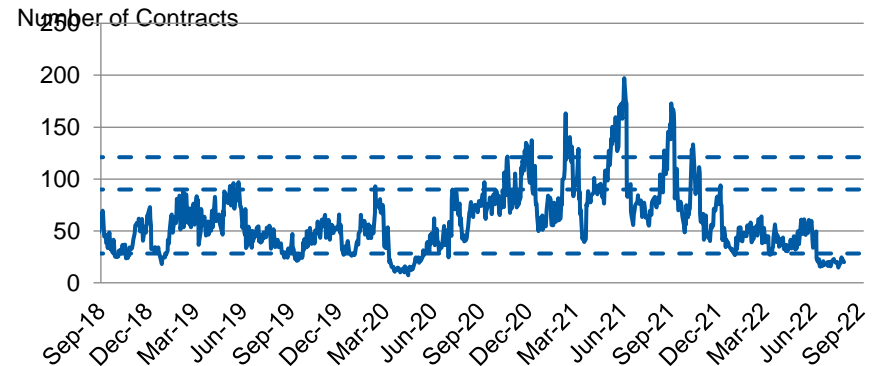
(Volume-Weighted) Average Available Size (ex-listed spreads)
Eurex Euro-Bobl Futures (OAT)



(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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