

Nordea

EUR rates

Wednesday morning call

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EUR rates: Bear steepening

Higher real rates, steeper curves, tighter financial conditions

Risk off! EUR curves have bear steepened with cues taken from the USD curves, continuous ECB speak about faster QT and issuance.

Higher longer-term real rates, in turn, tighten financial conditions. With increased downside risks to the economy from tighter financial conditions, credit spreads are widening, and the short-term trend has turned lower in equities.

In this scenario, steepeners and paid outright positions add near-term protection to broader portfolios. We prefer forward 5s30s and 10s30s steepeners.

Receiving 1y fwd 1s3s € to reduce curve risk or fade the recent steepening adds decent roll-to-vol and a negative loading to the curve risk factor to the portfolio.

It is a higher-for-longer trade – the logic being that more rate hikes being priced in, or rate cuts being priced out, would be negative for long-end steepeners. Risks being that some of the curve risk becomes curvature risk and that correlations may not be stable enough.

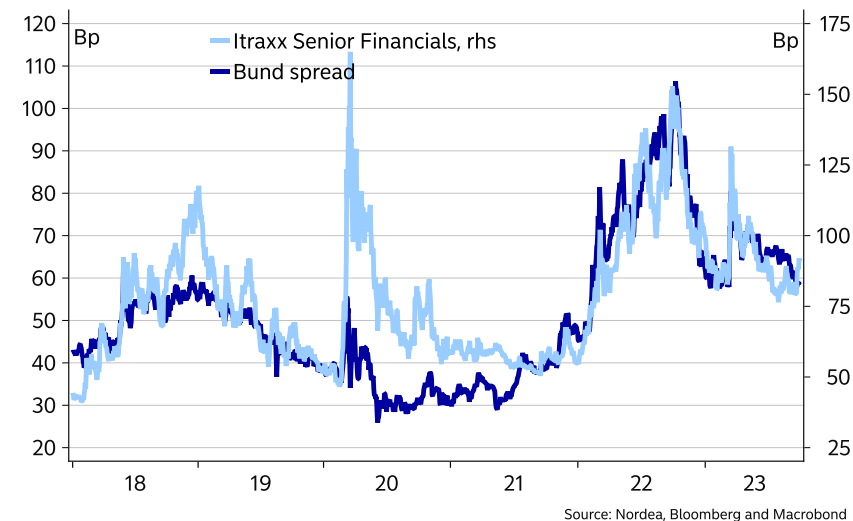
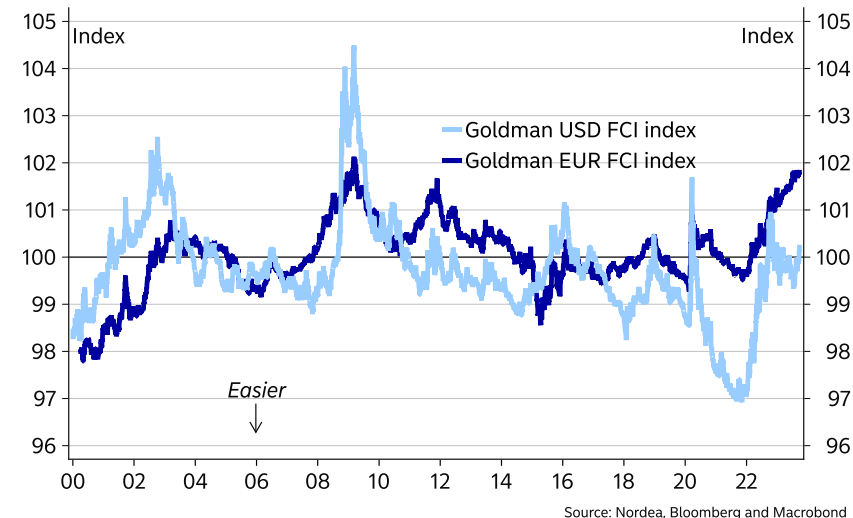
Widening credit spreads bode well for tenor basis wideners:

- The 30y €STR/6s is back in positive territory, but we still think it makes sense to shift receiving vs 6s to €STR.
- 5y €STR/BOR hasn't kept up with ITRAXX Sen Fin and should work well in a continued risk off.
- 10y5y 3s6s still looks like a good balance between entry level and carry/roll.

How long can bear steepening continue? At this point, steepening momentum is strong! Moreover, curves are likely to be steeper in the longer term as central banks reduce balance sheets and due to the Dutch pension reform.

But what happens in-between the short term and the longer term is much more uncertain. Resilient economies to higher rates suggest rates need to be higher for longer to get central banks what they ordered, namely more balanced labour markets. However, once labour markets start weakening, curves may flatten until central banks are ready to cut interest rates.

- Curves could steepen until the first bad labour market releases!



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EUR rates: Central views

Bear steepening

• Outright Highs again!

- *Momentum:* Higher, especially in the longer end.
- *View:* Range. Paying adds near-term protection to broader portfolios.

• Curve Steeper

- *Momentum:* Steeper across the board on rising risk premia and anchored central banks. PEPP QT discussion adds pressure.
- *View:* steepening moving to 10s30s again. Curves could steepen until the first bad labour market release.

• Curvature bending over again after ECB

- *Momentum:* Lower belly. Still no life in 2s5s10s despite credit widening.
- *View:* 2s10s to steepen more/flatten less than 10s30s. Currently markets are doing the opposite. Consider paying the belly for risk-off protection.

• Tenor basis €STR/BOR bottoming out?

- *Momentum:* Flattening €STR/BOR has stopped. 30y €/6s back in black.
- *View:* Pay 5y €STR/BOR, 10y5y 3s6s, 30y €STR/6s.

• ECB Focus shifting to the duration of high rates

- *Momentum:* First full rate cut priced for July. Second for October.
- *View:* The ECB is now done until inflation really falls, or growth numbers become much worse. Focus on PEPP run-off

Outright

	Rate	50d range, -1w, last	Carry+roll	Cvx-adj (c+r)/v	+50d z-score	+PCA misprice
1y1y €	317.8		-81.8	-0.9	-0.7	-0.9
5y 6s	336.5		-24.8	-0.3	1.2	1.2
5y5y 6s	327.2		7.4	0.2	2.2	2.2
10y 6s	332.2		-9.0	-0.1	1.8	1.8
10y10y 6s	321.7		-7.4	-0.0	2.3	2.3
30y 6s	305.0		-7.7	-0.0	2.2	2.2

Curves

	Rate	50d range, -1w, last	Carry+roll	Cvx-adj (c+r)/v	+50d z-score	+PCA misprice
2s5s 6s	-42.7		33.7	1.2	2.2	2.3
5s10s 6s	-4.3		15.8	0.8	2.7	2.7
5s30s 6s	-31.5		17.1	0.5	2.8	2.8
10s30s 6s	-27.2		1.3	0.1	2.4	2.5

Flies/curvature

	Rate	50d range, -1w, last	Carry+roll	Cvx-adj (c+r)/v	+50d z-score	+PCA misprice
2s5s10s 6s	-38.4		17.9	0.8	-0.2	-0.0
10s15s20s 6s	11.8		3.2	0.7	0.8	0.4
10s20s30s 6s	18.4		0.1	0.0	1.6	1.5
5s10s30s 6s	22.9		14.4	0.7	-0.5	-0.7

Tenor basis

	Rate	50d range, -1w, last	Carry+roll	Cvx-adj (c+r)/v	+50d z-score	+PCA misprice
1y E/E	6.3		-11.1	-1.1	-1.2	-1.1
5y E/E	12.6		-16.9	-6.8	-6.1	-6.4
5y5y E/E	13.9		-0.0	-0.0	0.5	-0.7
10y E/E	13.2		-9.1	-2.9	-2.3	-2.9
5y5y 3s6s	-3.4		-2.5	-0.4	-2.0	-2.6
10y 3s6s	1.8		-2.6	-1.0	-2.7	-3.2
10y5y 3s6s	-15.6		-1.3	-0.3	-0.7	-1.0
30y 3s6s	1.8		-2.6	-1.0	-2.7	-3.2

Timestamp: 26Sep2023. Source: Nordea Markets

* Note: All structures are received positions. Carry and roll is annualised 3m for 3s, 6m for 6s and €STR. Vol is 50d rlzd.

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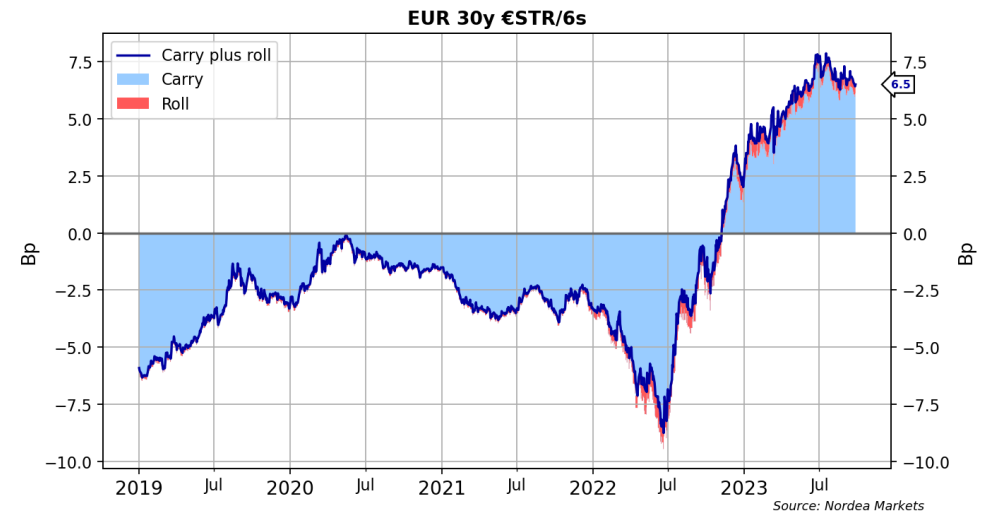
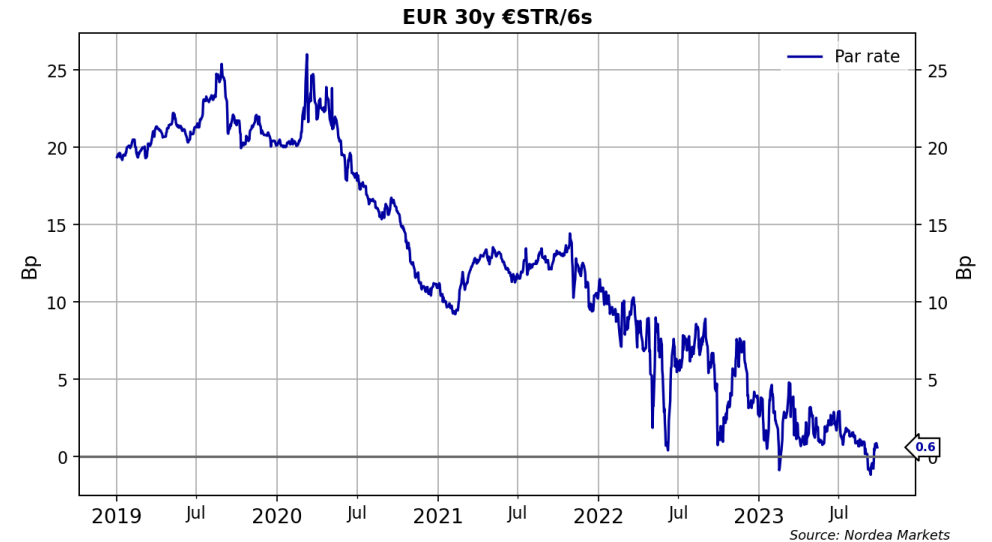
Shift long-end rec positions vs 6s to €STR

Text from 13 Sep – updated charts

30y €/6s trade in negative territory. Long forwards are even more negative:

1. The received fixed rate is almost the same, while the paid floating rate is 9bp lower in €STR in the current €STR/6s spot break.
2. However, given that the first 6m fixing on the Euribor swap is known, while the €STR fixings during the same period are only known at the end of the period, the shift requires a not too hawkish ECB.
3. Negative implied fixings from 12y out are unlikely to be realized.
4. 7bp carry + roll (6m annualised) weigh against the risks that long forwards become more negative before turning positive again. Long-end 3s6s have remained too low for a long time.

➤ Shift long-end received positions vs 6s to €STR or pay long-end €STR/6s as a standalone trade. The trade-off between paying spot or forward is that forwards are more deeply into negative territory but does not provide the same carry positive carry as long spot-starting.



Outright

	Rate	50d range, -1w, last	Carry+roll	Cvx-adj (c+r)/v	+50d z-score	+PCA misprice
1y €	390.6		-11.7	-0.3	1.3	1.4
1y 3s	403.5		-17.5	-0.5	1.2	1.3
1y 6s	413.2		-17.3	-0.5	1.3	1.4
2y €	355.0		-33.2	-0.5	0.4	0.4
2y 3s	370.4		-49.8	-0.8	0.2	0.2
2y 6s	379.2		-58.4	-1.0	-0.0	-0.0
5y €	312.7		-4.6	-0.0	1.5	1.5
5y 3s	330.2		-21.1	-0.3	1.3	1.3
5y 6s	336.5		-24.8	-0.3	1.2	1.2
10y €	312.3		2.5	0.1	1.9	1.9
10y 3s	330.4		-6.3	-0.0	1.9	1.9
10y 6s	332.2		-9.0	-0.1	1.8	1.8
20y 6s	327.8		-8.3	-0.1	2.1	2.1
30y 6s	305.0		-7.7	-0.0	2.2	2.2
1y1y €	317.8		-81.8	-0.9	-0.7	-0.9
2y2y €	281.0		-9.6	-0.1	1.3	1.3
4y2y €	288.9		6.8	0.1	1.9	2.0
6y2y €	307.4		9.8	0.2	2.2	2.3
8y2y €	327.3		10.3	0.2	2.2	2.2
10y2y €	344.0		6.3	0.2	2.3	2.3
3y3y €	286.1		7.2	0.1	1.9	2.0
6y3y €	312.1		9.6	0.2	2.2	2.3
9y3y €	340.2		7.9	0.2	2.3	2.3
5y5y 6s	327.2		7.4	0.2	2.2	2.2
10y5y 6s	345.4		-2.3	0.1	2.2	2.1
15y5y 6s	293.9		-13.2	-0.1	2.3	2.3
20y5y 6s	245.3		-6.9	0.0	2.5	2.5
25y5y 6s	219.9		-3.0	0.1	2.5	2.5
10y10y 6s	321.7		-7.4	-0.0	2.3	2.3
20y10y 6s	233.4		-5.1	0.1	2.5	2.5

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Curves

	Rate	50d range, -1w, last	Carry+roll	Cvx-adj (c+r)/v	+50d z-score	+PCA misprice
1s2s €	-35.6		-21.4	-0.8	-2.4	-3.2
2s3s €	-23.7		12.8	1.1	1.3	1.4
2s5s €	-42.3		28.5	1.1	2.2	2.4
2s5s 6s	-42.7		33.7	1.2	2.2	2.3
5s10s €	-0.3		7.1	0.4	2.2	2.3
5s10s 6s	-4.3		15.8	0.8	2.7	2.7
2s10s €	-42.7		35.6	0.8	2.3	2.4
2s10s 6s	-47.0		49.5	1.1	2.6	2.6
5s20s 6s	-8.7		16.5	0.6	2.7	2.7
5s30s 6s	-31.5		17.1	0.5	2.8	2.8
10s20s 6s	-4.4		0.7	0.1	2.3	2.3
20s30s 6s	-22.8		0.6	0.1	2.3	2.4
10s30s 6s	-27.2		1.3	0.1	2.4	2.5
1y fwd 10s30s 6s	-26.5		0.1	0.0	2.3	2.4
1y1y/2y3y €	-35.6		76.8	1.8	3.3	3.9
2y2y/4y2y €	8.0		16.4	0.5	2.4	2.6
4y2y/6y2y €	18.5		3.0	0.1	2.2	2.1
6y2y/8y2y €	19.9		0.5	0.0	1.1	0.5
8y2y/10y2y 6s	10.4		-4.3	-0.2	-0.1	-0.2
7y3y/10y2y 6s	14.2		-4.2	-0.2	0.2	-0.0
3y3y/6y3y €	26.0		2.5	0.1	2.2	2.1
6y3y/9y3y €	28.1		-1.7	-0.1	0.6	0.1
4y4y/8y4y 6s	27.0		-0.9	-0.0	1.9	1.5
5y5y/10y5y 6s	18.1		-9.7	-0.4	1.0	0.9
10y2y/12y3y 6s	-6.6		-9.5	-0.8	0.6	1.1
12y3y/15y5y 6s	-48.6		-6.9	-0.4	1.5	1.9
10y5y/15y5y 6s	-51.4		-10.9	-0.6	1.3	1.7
15y5y/20y5y 6s	-48.6		6.3	0.3	0.9	0.7
20y5y/25y5y 6s	-25.4		3.9	0.3	-0.8	-0.9
10y10y/20y10y 6s	-88.4		2.3	0.1	1.2	1.3

Timestamp: 26Sep2023. Source: Nordea Markets

Flies/curvature

	Rate	50d range, -1w, last	Carry+roll	Cvx-adj (c+r)/v	+50d z-score	+PCA misprice
1s2s3s €	-11.9		-34.2	-1.7	-3.3	-4.6
2s3s4s €	-11.6		1.4	0.1	-2.4	-3.1
3s4s5s €	-5.6		7.0	1.2	2.4	2.8
2s5s10s €	-42.0		21.4	1.1	0.0	0.3
2s5s10s 6s	-38.4		17.9	0.8	-0.2	-0.0
1y fwd 2s5s10s 6s	-19.1		20.6	1.0	2.1	3.2
2y fwd 2s5s10s 6s	-9.2		7.1	0.6	1.7	2.5
5s10s15s 6s	-8.0		13.8	0.9	2.6	2.6
10s12s15s 6s	1.1		1.7	0.7	-0.6	-1.1
5s10s20s 6s	0.1		15.1	0.9	1.3	1.2
10s20s30s 6s	18.4		0.1	0.0	1.6	1.5
5s10s30s 6s	22.9		14.4	0.7	-0.5	-0.7
2s10s30s 6s	-19.8		48.1	1.1	1.3	1.2
10s15s20s 6s	11.8		3.2	0.7	0.8	0.4
12s15s20s 6s	9.4		1.4	0.4	-1.7	-2.1
15s20s25s 6s	3.8		-1.4	-0.4	1.7	1.9
20s25s30s 6s	-1.0		-0.4	-0.2	2.6	2.8
1y1y/2y1y/3y1y €	-35.6		20.9	0.6	-1.6	-1.5
1y1y/2y3y/5y5y €	-65.3		62.1	1.8	2.1	3.0
2y2y/4y2y/6y2y €	-10.5		13.4	0.3	1.2	1.8
4y2y/6y2y/8y2y €	-1.4		2.5	0.1	2.0	2.3
6y2y/8y2y/10y2y €	3.2		4.4	0.2	0.8	0.2
8y2y/10y2y/12y3y 6s	17.0		5.2	0.2	-0.9	-1.7
10y2y/12y3y/15y5y 6s	42.1		-2.5	-0.1	-1.5	-1.7
3y3y/6y3y/9y3y €	-2.0		4.2	0.1	2.0	2.1
6y3y/9y3y/12y3y 6s	23.6		8.9	0.4	-0.2	-1.2
9y3y/12y8y/25y5y 6s	60.5		-22.8	-0.9	0.9	1.6
5y5y/10y5y/15y5y 6s	69.6		1.3	0.1	-0.9	-1.5
10y5y/15y5y/20y5y 6s	-2.8		-17.3	-0.8	1.4	2.1
15y5y/20y5y/25y5y 6s	-23.3		2.4	0.1	1.7	1.5

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Tenor basis

	Rate	50d range, -1w, last	Carry+roll	Cvx-adj (c+r)/v	+50d z-score	+PCA misprice
1y E/E	6.3		-11.1	-1.1	-1.2	-1.1
2y E/E	9.8		-18.2	-3.4	-3.4	-3.4
3y E/E	11.5		-18.8	-5.5	-5.1	-5.2
4y E/E	12.2		-19.4	-6.4	-5.8	-6.0
5y E/E	12.6		-16.9	-6.8	-6.1	-6.4
10y E/E	13.2		-9.1	-2.9	-2.3	-2.9
15y E/E	12.5		-6.2	-1.9	-1.8	-2.7
20y E/E	11.0		-5.3	-1.6	-1.4	-2.2
30y E/E	8.9		-5.0	-1.4	-0.9	-1.2
5y5y E/E	13.9		-0.0	-0.0	0.5	-0.7
10y5y E/E	10.7		-1.9	-0.3	-0.9	-2.7
15y5y E/E	4.8		-0.6	-0.1	0.1	-0.1
2s10s E/E	3.4		9.1	1.6	2.1	1.2
10s30s E/E	-4.3		4.1	1.9	1.2	1.9

Timestamp: 26Sep2023. Source: Nordea Markets

	Rate	50d range, -1w, last	Carry+roll	Cvx-adj (c+r)/v	+50d z-score	+PCA misprice
1y 3s6s	9.7		0.2	0.0	-0.1	0.1
2y 3s6s	8.8		-8.7	-1.1	-1.5	-1.4
5y 3s6s	6.4		-3.7	-1.4	-2.9	-3.2
10y 3s6s	1.8		-2.6	-1.0	-2.7	-3.2
15y 3s6s	-3.0		-2.2	-1.3	-2.8	-3.2
20y 3s6s	-6.0		-1.7	-0.9	-2.2	-2.6
30y 3s6s	-8.3		-1.4	-0.6	-1.3	-1.6
5y5y 3s6s	-3.4		-2.5	-0.4	-2.0	-2.6
10y5y 3s6s	-15.6		-1.3	-0.3	-0.7	-1.0
15y5y 3s6s	-18.3		0.3	0.1	0.0	-0.2
20y5y 3s6s	-15.4		0.7	0.2	-0.1	-0.3
25y5y 3s6s	-15.4		0.7	0.2	-0.1	-0.3
2s10s 3s6s	-6.9		6.0	0.8	0.3	-0.4
10s30s 3s6s	-10.1		1.2	0.7	2.2	2.5

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