Bond Market Update

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

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Front End Rates Have Repriced Significantly This Year

Source: MS Interest Rates Desk

Rate Forward Pricing

Source: MS Interest Rates Desk

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European Inflation Narrative… Still Driven By Gas/Energy

Energy Prices Have Risen More Meaningfully in Europe than Elsewhere
EUR/MWh

Which Drives a Greater Divergence Between Core and Headline CPI

MS Research Recently Revised Our TTF Forecasts Even Higher

TTF Gas Price (EUR/MWh)

Skewing Long Run Inflation Probabilities Distribution to the Upside
Long Run Inflation Probability (%)
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)

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

**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

- 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

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

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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-Schatz Futures (DU)

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

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

(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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