

## Developed Market Rates

21 June 2011 | 12 pages

# Global Month-End Index Projections

## End-June 2011 EGBI and WGBI Projections

- **EGBI:** We expect a relatively small extension in the effective duration of EGBI at the end of June. The largest weighted-duration increases are projected mainly for the large liquid AAAs (France, Germany and the Netherlands) and also Belgium. Overall, the index changes should support the 2- and 10yr sectors of Europe.
- **Individual Euro country curves:** Projected index changes point to flattening pressure in the Netherlands and Austria. The changes should also support the 10yr sector in Germany, Finland and Belgium.
- **WGBI:** We also project index changes due to changes in composition for the US, UK and Japan components of the WGBI. The US and the UK should benefit from the index changes, though they are relatively neutral for the EMU.

### Aman Bansal

+91-22-4277-5021

aman1.bansal@citi.com

### Robert Crossley

+44-20-7986-9255

robert.crossley@citi.com

EGBI Effective Duration			Largest Duration changes over last year		
End May	End Jun(e)	Duration Change(e)	-ve	+ve	Average Absolute Change
6.26	6.30	0.04	(0.00)	0.14	0.06
EGBI excl. Portugal and Ireland	6.31	6.33	0.02		

Source: Citi Investment Research and Analysis

[See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.](#)

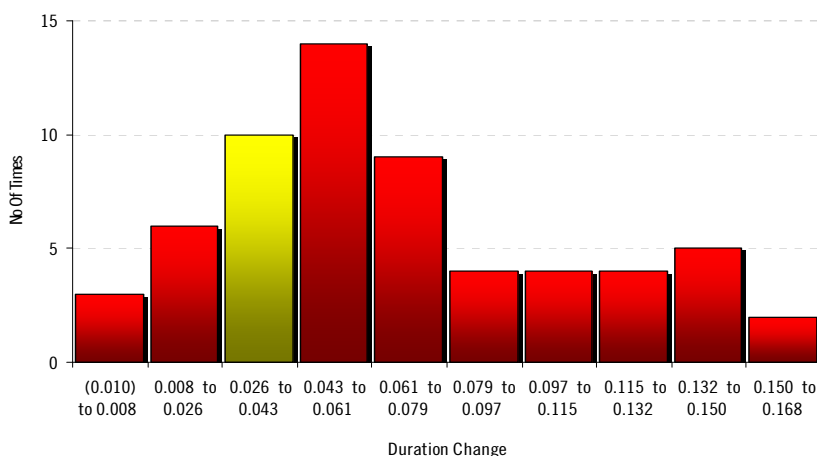
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## End-Jun EGBI Projections

### Below median change projected in the EGBI

The effective duration of the EGBI should extend by 0.04 at the end of Jun<sup>1</sup>. As the five-year frequency distribution of month-end changes shows (Figure 1), this change is below its median for the last 5 years.

**Figure 1. Five Year Distribution of Month-End EGBI Duration Changes (Jun Projection Highlighted)**



Source: Citi Investment Research and Analysis

The rating requirement for inclusion in the EGBI is investment grade by both Moody's (Baa3) and S&P (BBB-). For those investors not comfortable with Portugal and Ireland in their portfolio, the change in EGBI (excluding Portugal and Ireland) is expected to be 0.02.

### Bonds dropping out of the EGBI at the end of Jun

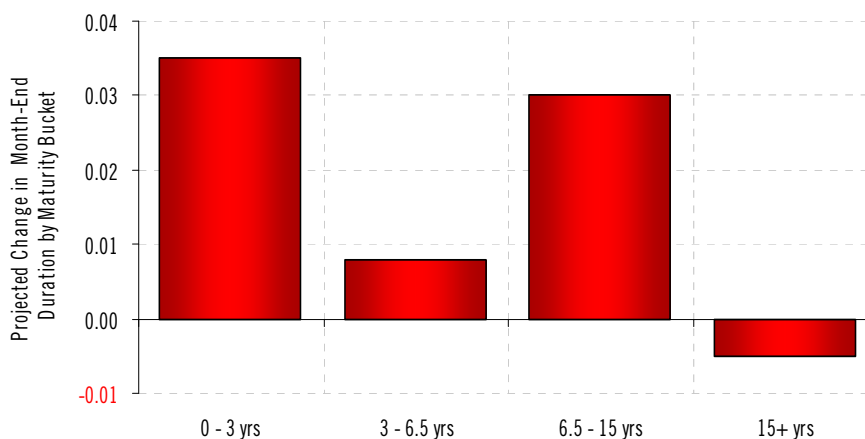
The bonds dropping out of the index will be Bund Jun12 (€19bn) and PTGV Jun12 (€8.5bn). In case of the latter, this is 7.6% of the total Portugal debt and would result in a reduction in Portugal's weight in the index. This might put selling pressure on the bond.

### Curve breakdown of end-Jun EGBI projection

The curve breakdown of the projected changes suggests significant extensions in the 2- and 10yr sectors (Figure 2). *Ceteris paribus*, this should put downward pressure on 2- and 10yr yields relative to other maturities as previously matched investors buy these sectors to rematch the index, and increase curvature.

<sup>1</sup> Please see the supply section of our weekly *International Interest Rate Strategist* for details of the estimated issuance on which this and related projections are based. Supply is the main driver of projections but other factors, e.g., yield level and curve shape, also affect the calculations and are subject to change.

Figure 2. End-Jun Projected Index Changes by Curve Sector (Unweighted Duration)

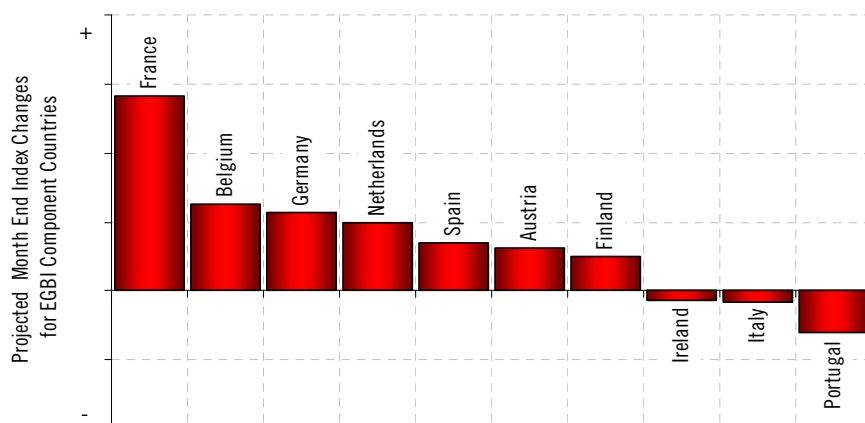


Source: Citi Investment Research and Analysis

### Country breakdown of end-Jun EGBI projection

Among the projected index changes at a country level, the weighted duration increase in France<sup>2</sup> stands out, followed by Belgium, Germany and the Netherlands. These changes should be supportive for the big AAA markets; however, the extensions in Belgium and Spain may be less supportive than they otherwise should be. Investors may be willing to be taken short/shorter by the extension.

Figure 3. End-Jun Projected Index Changes by Country (Weighted Duration)



Source: Citi Investment Research and Analysis

### Detailed breakdown of end-Jun EGBI projections

Figure 4 shows the detailed breakdown of projected end-Jun duration and index weight changes by country. The largest duration extension is for Portugal but because of the decline in its weight in the EGBI, its weighted duration decreases.

<sup>2</sup> it will increase for the tenth consecutive month.

Figure 4. End-Jun EGBI Projections

17-Jun-11	End of May - Actual		End of Jun - Projected		Projected Change			Duration change range over last year		
	% weight in EGBI	Duration	% weight in Index	Duration	Weighted Dur Change X 100	Weight Change	Duration Change	-ve	+ve	Average Absolute Change
Germany	22.5	6.118	22.2	6.225	0.57	(0.30)	0.11	(0.08)	0.17	0.08
Italy	23.0	6.530	23.1	6.511	(0.08)	0.06	(0.02)	(0.02)	0.25	0.09
France	23.0	6.704	23.2	6.698	1.41	0.23	(0.01)	(0.06)	0.17	0.07
Spain	10.1	5.847	10.1	5.837	0.35	0.08	(0.01)	(0.03)	0.28	0.08
Portugal	1.9	4.569	1.7	5.096	(0.30)	(0.26)	0.53	(0.08)	0.53	0.05
Belgium	6.3	5.818	6.3	5.890	0.63	0.03	0.07	(0.02)	0.26	0.06
Netherlands	6.0	6.310	6.2	6.243	0.49	0.14	(0.07)	(0.07)	0.36	0.09
Ireland	1.4	5.049	1.4	5.049	(0.06)	(0.01)	0.00	(0.03)	0.37	0.07
Austria	4.3	6.269	4.3	6.334	0.31	0.00	0.06	(0.03)	0.07	0.03
Finland	1.5	5.219	1.5	5.298	0.24	0.02	0.08	(0.03)	0.23	0.05

Source: Citi Investment Research and Analysis

## Pressures on individual country curves

Figure 5 summarises the pressures on individual country curves from the projected index changes. Green arrows indicate support for prices and red arrows indicate downward pressure on prices, relative to the domestic curve. Double arrows indicate strong pressure on that part of the domestic curve relative to other maturities. The underlying detail is shown in Figure 6 to Figure 21.

Projected index changes imply flattening pressure in the Netherlands (Figure 15) and Austria (Figure 19). The changes should also support the 10yr sector in Germany (Figure 7), Finland (Figure 21) and Belgium (Figure 17)<sup>3</sup>.

Figure 5. Summary of Pressure on Prices of Individual Country Curve Sectors

	2yr	5yr	10yr	30yr	
Germany			↑↑		Germany
Italy				↓	Italy
France			↑	↓	France
Spain					Spain
Netherlands		↑	↓	↓	Netherlands
Belgium			↑		Belgium
Austria		↓	↑	↑↑	Austria
Finland		↓	↑↑		Finland
	2yr	5yr	10yr	30yr	

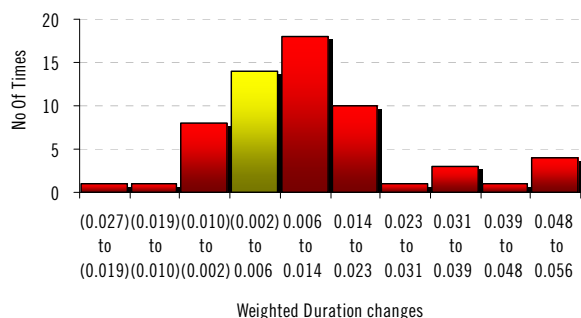
Source: Citi Investment Research and Analysis

<sup>3</sup> Note that all these changes are on the domestic curve only and should not be viewed as necessarily indicating cross-market opportunities.

## Putting projected country changes in perspective

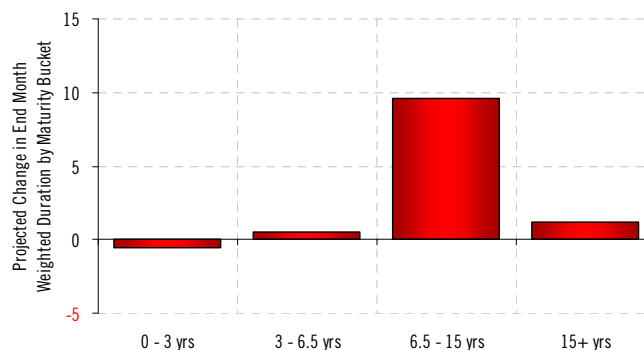
Below we show the distributions of weighted duration changes and the curve splits of the projected end-Jun changes.

**Figure 6. Germany: Distribution of Month-End Duration Changes Over The Last Five Years (Weighted Duration)**



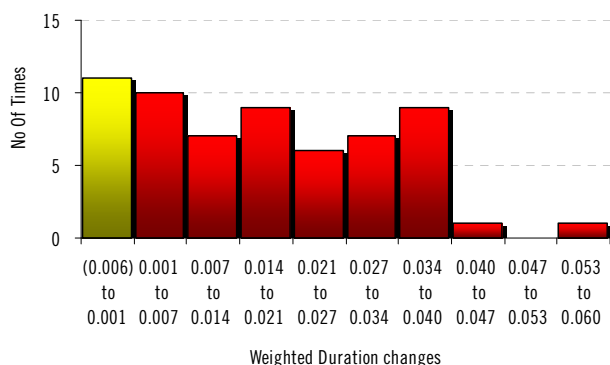
Source: Citi Investment Research and Analysis

**Figure 7. Germany: End-Jun Projected Index Change by Maturity (Weighted Duration)**



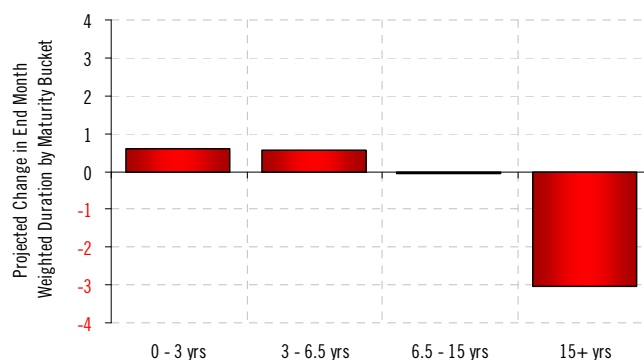
Source: Citi Investment Research and Analysis

**Figure 8. Italy: Distribution of Month-End Duration Changes Over The Last Five Years (Weighted Duration)**



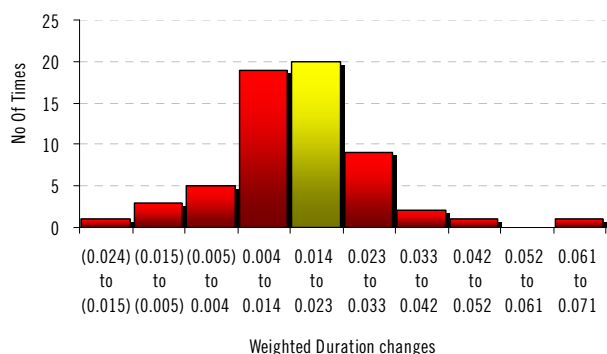
Source: Citi Investment Research and Analysis

**Figure 9. Italy: End-Jun Projected Index Change by Maturity (Weighted Duration)**



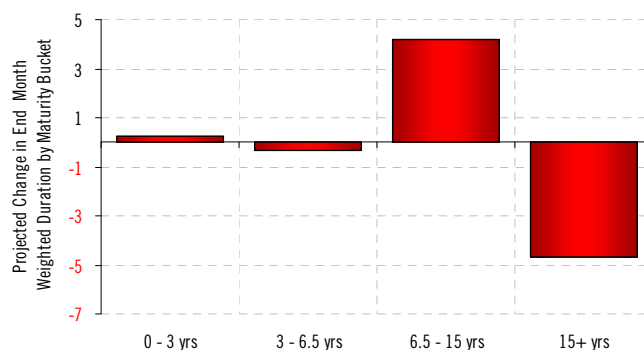
Source: Citi Investment Research and Analysis

**Figure 10. France: Distribution of Month-End Duration Changes Over The Last Five Years (Weighted Duration)**



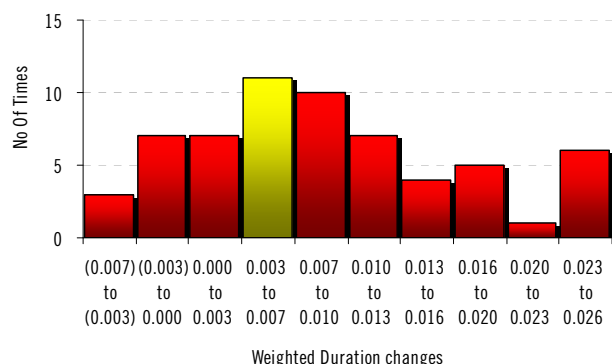
Source: Citi Investment Research and Analysis

**Figure 11. France: End-Jun Projected Index Change by Maturity (Weighted Duration)**



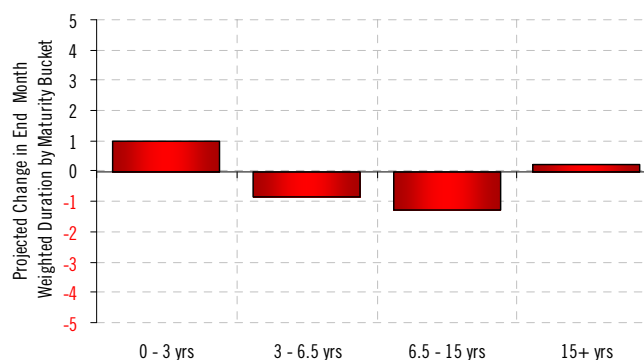
Source: Citi Investment Research and Analysis

**Figure 12. Spain: Distribution of Month-End Duration Changes Over The Last Five Years**



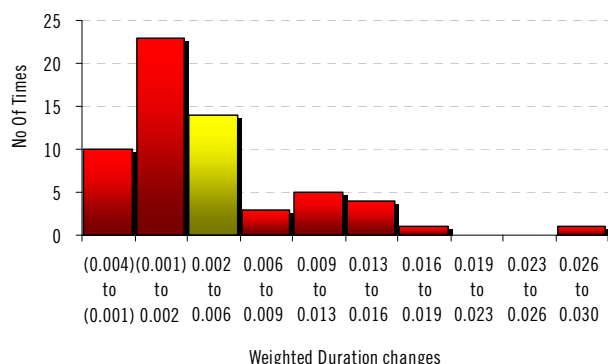
Source: Citi Investment Research and Analysis

**Figure 13. Spain: End-Jun Projected Index Change by Maturity (Weighted Duration)**



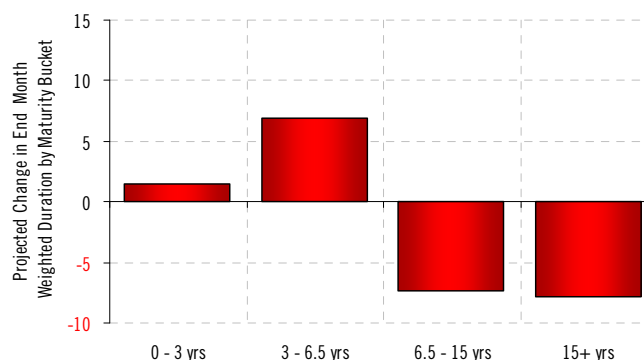
Source: Citi Investment Research and Analysis

**Figure 14. Netherlands: Distribution of Month-End Duration Changes Over The Last Five Years (Weighted Duration)**



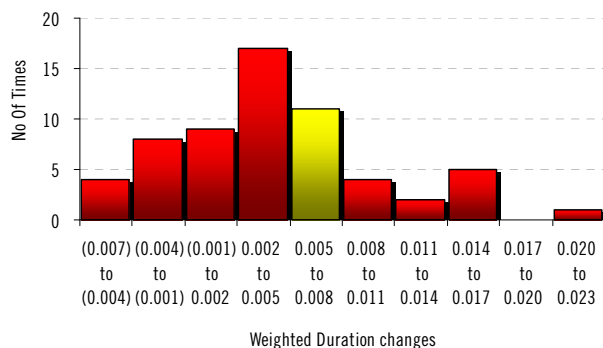
Source: Citi Investment Research and Analysis

**Figure 15. Netherlands: End-Jun Projected Index Change by Maturity (Weighted Duration)**



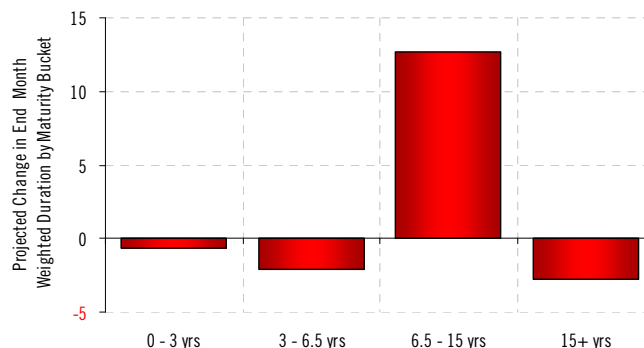
Source: Citi Investment Research and Analysis

**Figure 16. Belgium: Distribution of Month-End Duration Changes Over The Last Five Years**



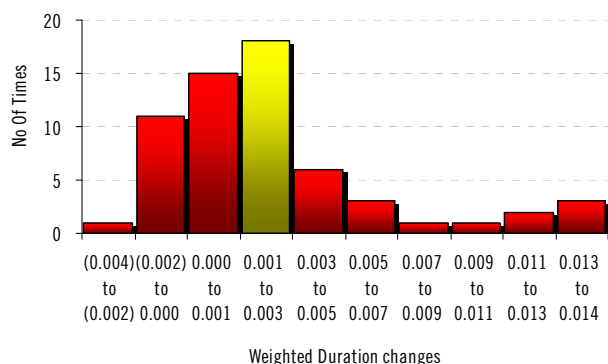
Source: Citi Investment Research and Analysis

**Figure 17. Belgium: End-Jun Projected Index Change by Maturity (Weighted Duration)**



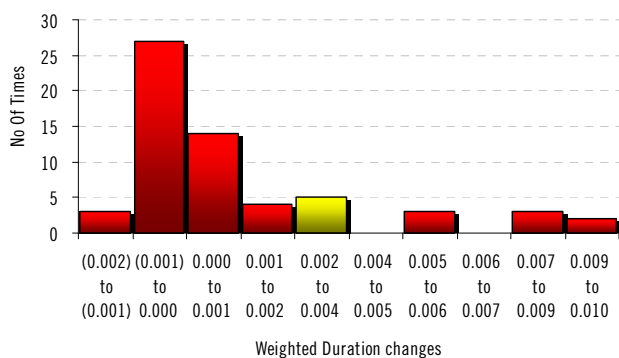
Source: Citi Investment Research and Analysis

**Figure 18. Austria: Distribution of Month-End Duration Changes Over The Last Five Years**



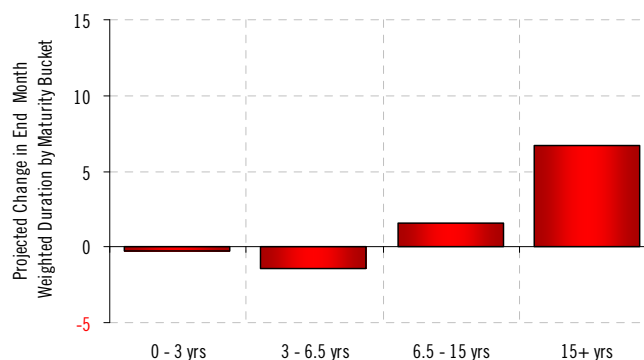
Source: Citi Investment Research and Analysis

**Figure 20. Finland: Distribution of Month-End Duration Changes Over The Last Five Years**



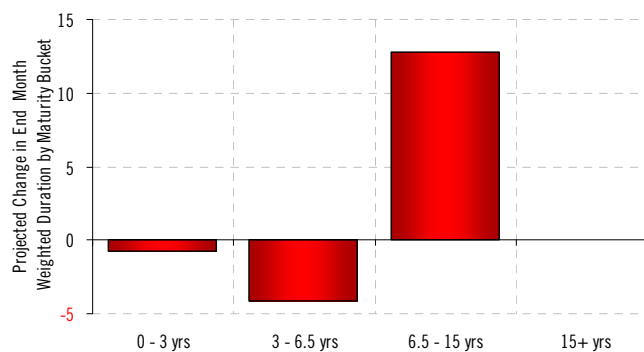
Source: Citi Investment Research and Analysis

**Figure 19. Austria: End-Jun Projected Index Change by Maturity (Weighted Duration)**



Source: Citi Investment Research and Analysis

**Figure 21. Finland: End-Jun Projected Index Change by Maturity (Weighted Duration)**

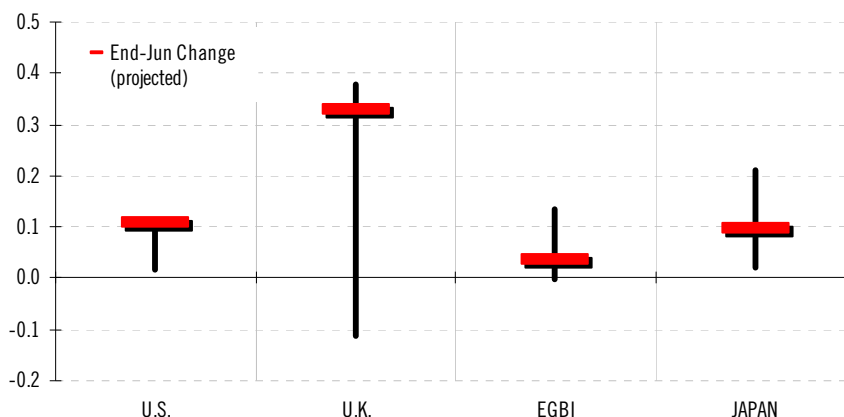


Source: Citi Investment Research and Analysis

## End-Jun WGBI component projections

Figure 22 shows the projected end-Jun index changes for the EGBI, Japan, UK and US components of the WGBI, and places them in the context of their respective 12-month ranges. It highlights the change in the US expected at top of its 1yr range, while the extension in the EGBI should be more subdued. The UK stands at 91 percentile of its 1yr range, though if we look at longer history, it is 2.04 standard deviations above its 5yr mean.

Figure 22. Projected Duration Changes for WGBI Components and 12-Month Range



Source: Citi Investment Research and Analysis

Figure 23 shows the details of these changes.

Figure 23. End Jun Projected Duration Changes for the Main Components of the WGBI

17-Jun-11	End of May - Actual		End of Jun - Projected		Projected Change		Duration change range over last year		
	% weight in WGBI	Duration	% weight in Index	Duration	Weight Change	Duration Change	-ve	+ve	Average Absolute
EGBI	30.2	6.261	30.5	6.296	0.23	0.04	(0.00)	0.14	0.06
JAPAN	31.6	7.434	31.6	7.625	(0.07)	0.19	0.02	0.21	0.10
U.S.	26.1	5.373	26.3	5.482	0.24	0.11	0.02	0.11	0.06
U.K.	5.6	9.477	5.5	9.805	(0.15)	0.33	(0.11)	0.38	0.09

Source: Citi Investment Research and Analysis



## Appendix A-1

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