

## Euro Rates Strategy

### Update on Short 10yr & 30yr Bund Spread Recommendations

- **Take profits on short 30yr Bund Spreads:** We recommend taking profits on our short 30yr Bund spread recommendation that was opened at -11bp in [The Morning Call - 30yr Bund ASW](#). The main reasons for this are: (1) technical levels - 30yr Bunds have broken the 2.10% level today and the momentum behind the rally may result in a breach of the 6month low of 2.06%, (2) we do not expect any 30yr issuance in core-EMU markets until June.

– **Trade details: Unwind short 30yr Bunds vs swaps (YYS) for a 4.5bp gain**

- **Revise stop on short 10yr Bund spreads trade to -27bp:** A couple of weeks ago we recommended selling 10yr Bund spreads at -31bp with a target of -20bp and a stop of -37bp ([Euro Rates Strategy - Derivative trades after recent moves](#)).

- With 10yr Bunds breaking 1.20% level today and only 2bps above the 1year low of 1.16% the scope for 10yr swaps to move down towards Bunds whilst Bunds were supported by technical levels may be waning.

- However, we do still expect Bund spreads to tighten over the next few weeks due to the non-supportive cash flow profile in May and the prospect of further reduction in the risk premium embedded in Bunds should peripheral yields rally further. We therefore recommend revising the stop on this trade to -27bp (currently 10yr Bund spreads are at -25bp) rather than taking profits.

- **Trade details: Revise stop on short 10yr Bunds vs Swaps (YYS) to -27bp**

– Current -25bp, Open -31bp. Target -20bp.

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**See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.**

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# Update on Bund Spread Recommendations

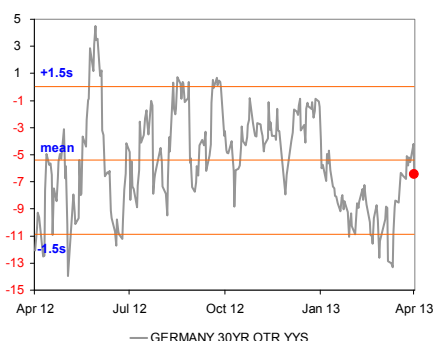
## (1) Take profits on short 30yr Bund Spreads

**Trade details: Unwind short 30yr Bunds vs swaps (YYS) for a 4.5bp gain**

**Open -11bp. Current -6.5bp. Stop -9bp (revised stop on 19 April 2013). Target -1bp**

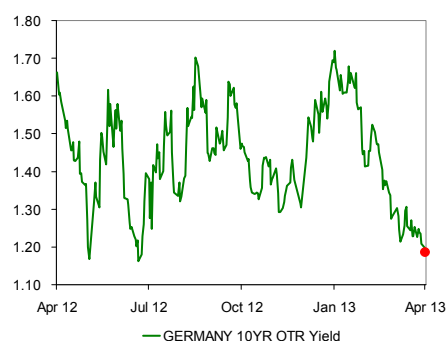
- We recommend taking profits on our short 30yr Bund spread recommendation that was opened at -11bp in [The Morning Call - 30yr Bund ASW](#). The main reasons for this are: (1) technical levels - 30yr Bunds have broken the 2.10% level today and the momentum behind the rally may result in a breach of the 6month low of 2.06%, (2) we do not expect any 30yr issuance in core-EMU markets until June.
- Further, we continue to expect 30yr Bund spreads to remain range bound but with spreads in the middle of their 1yr range (Figure 1) and potential headwinds for further spread tightening ahead we feel the risk-reward of holding short 30yr Bunds spreads at current levels is unattractive.

**Figure 1. 30yr Bund Spreads (YYS) have been range bound in the last year**



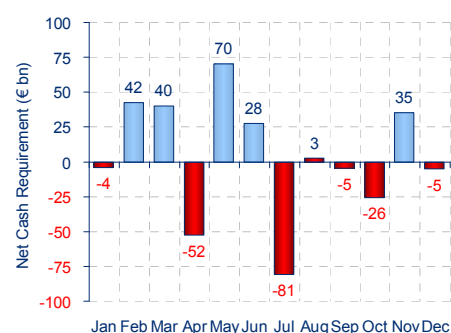
Source: Citi Research

**Figure 2. 10yr Bunds are fast approaching the one year low (yield, %)**



Source: Citi Research

**Figure 3. The EMU-10 NCR is strongly non-supportive for bonds in May as gross supply easily outweighs coupons & redemptions, (€bn)**



Source: Citi Research

## (2) Revise stop on short 10yr Bund spreads trade to -27bp

**Trade details: Revise stop on short 10yr Bunds vs Swaps (YYS) to -27bp**

**Open -31bp. Current -25bp. Stop -27bp. Target -20bp.**

- A few weeks ago we recommended selling 10yr Bund spreads at -31bp with a target of -20bp and a stop of -37bp ([Euro Rates Strategy - Derivative trades after recent moves](#)). The rationale for this recommendation was: the risk premium embedded in Bunds was too high relative to swaps and that the disconnect between Bund spreads vs peripheral yields, equities and money market rates was unlikely to persist.
- With 10yr Bunds breaking 1.20% level today and only 2bps above the 1year low of 1.16% (Figure 2) the scope for 10yr swaps to move down towards Bunds whilst Bunds were supported by technical levels may be waning. However, we do still expect Bund spreads to tighten over the next few weeks due to: (1) the non-supportive cash flow profile in May (€76bn of gross supply easily outweighs €6bn of coupons and zero redemptions, Figure 3 ) and (2) the prospect of further reduction in the risk premium embedded in Bunds should peripheral yields rally further.
- We therefore recommend revising the stop on this trade to -27bp (currently 10yr Bund spreads are -25bp) rather than taking profits. The revised stop on our trade will provide a 4bp gain should 10yr Bund spreads (YYS) move below -27bp.

## Appendix A-1

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