

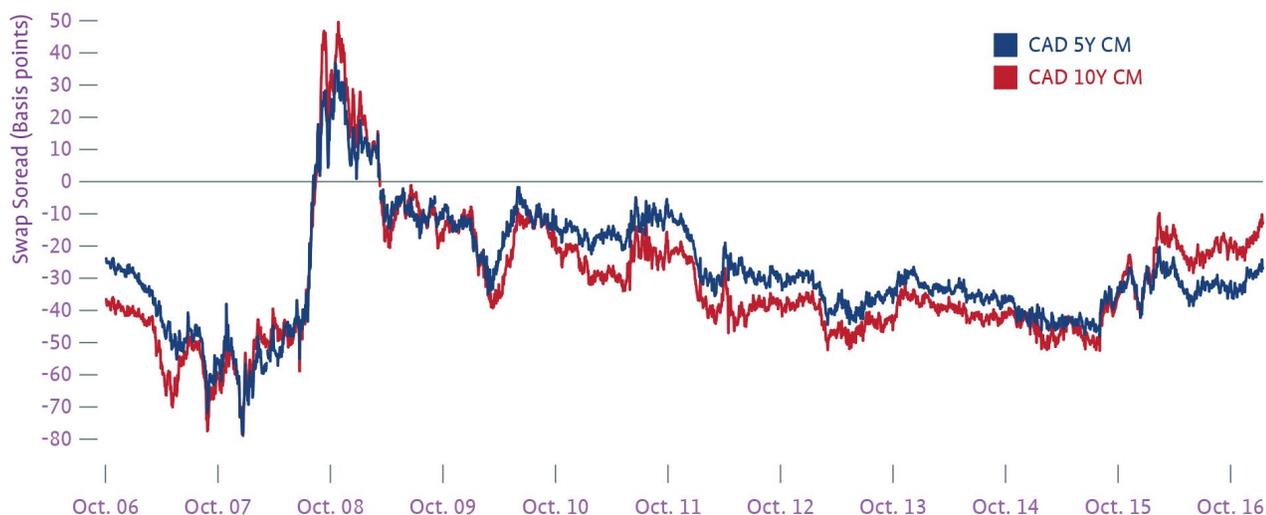
MONTRÉAL EXCHANGE

Canada Swap Spreads

Recent Tightening

Since reaching a wide point in mid-summer 2015, Canadian swap spreads have tightened (bonds cheapened relative to swaps) to levels not seen for around a year in the 5y segment and are approaching levels not seen in over half a decade in the 10y segment.

FIGURE 1
5Y and 10Y Constant maturity Swap Spreads, 10 year History



Source: BMO Capital Markets' Fixed Income Sapphire database

Invoice Spread² Constructions

An investor can create speculative swap spread widening positions without the need to conduct repo operations to fund the bond purchase by using futures contracts which, additionally, trade a little cheap to bonds currently. Some sample constructions are shown below in both the 5-year segment of the yield curve and the 10-year segment of the curve, using CGFH17 and CGBH17 contracts respectively.

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2 For a short discussion of Invoice Spreads, including some of the drivers of swap spreads, refer to the January 2017 update of the CGF Invoice Spread.

FIGURE 2**CGF Spread Widener Example**

CGFH17 INVOICE SPREAD WIDENER	
Futures Position	Buy 180 contracts CGFH17. (CTD bond = 0.75% sep1/21)
Swap Position	Pay fixed, \$23.45 million notional from Mar31/17 to Sep1/21
Futures DV01	0.0556
Swap DV01	0.0426
Futures Forward Yield	1.165%
Forward Swap Rate	1.456%
Interest Rate (DV01) Exposure	DV01 futures = +\$10,000 DV01 swap = -\$10,000 Net DV01 = \$0
Invoice Spread Level	29.1 bps

FIGURE 3**CGB Spread Widener Example**

CGBH17 INVOICE SPREAD WIDENER	
Futures Position	Buy 95 contracts CGBH17. (CTD bond = 2.25% Jun1/25)
Swap Position	Pay fixed, \$13.23 million notional from Mar31/17 to Jun1/25
Futures DV01	0.1050
Swap DV01	0.0756
Futures Forward Yield	1.685%
Forward Swap Rate	1.836%
Interest Rate (DV01) Exposure	DV01 futures = +\$10,000 DV01 swap = -\$10,000 Net DV01 = \$0
Invoice Spread Level	15.1 bps

For more information

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