

## European Rates Alpha

## Sell 3m Sonia vs. 3m. Euribor futures using December 2024 contracts

**We favour fading 2024 BoE Bank rate cuts vs. ECB**

UK front-end curve steepening since late September does not appear to be fully warranted by economic developments and stands in contrast to our Bank of England (BoE) rate call for 2024-2025. We have more confidence in fading Bank rate cuts in 2024 than in positioning for more cuts getting priced in for 2025. We sell 3m. Sonia vs. 3m. Euribor futures using Dec 2024 contracts to express this view.

**Market pricing of BoE rate cuts contrasts with our call ...**

The market has taken out around 10bp of terminal rate pricing since the September MPC (Exhibit 1), now implying relatively limited probability of more BoE hikes (cumulative 11bp by Feb 2024 – Exhibit 2). This is broadly in line with our view that the BoE will stay on hold at 5.25%. On the curve, the market has priced out around 8bp of cuts from 2024 and 20bp from 2025, now pricing around 50bp and 40bp of cuts for these years, respectively. In contrast, we expect no cuts in 2024 and 100bp in 2025.

**... and is not fully warranted by economic developments**

Front-end curve steepening in a rates selloff – the modus operandi at the front-end since late September (Exhibit 3) – makes sense if the move higher in rates is driven by upside surprises in data. But inflation and growth have been weaker relative to the BoE's expectations, and the wage growth surprise was not larger than in September. At least to some extent the selloff has been US-led: our EUR rates team highlighted last week that the Bund selloff of the week prior was all in US hours, with Bunds rallying in London mornings (see [Hi 5s, 20 Oct](#) report).

**Sell 3m Sonia Dec'24 futures vs. 3m. Euribor futures**

The front-end curve in the UK is now the most mispriced relative to our base case in the UK, Europe and US (Exhibit 4), in our view. In the UK, we have more confidence in fading Bank rate cuts in 2024 than in positioning for more cuts being priced in for 2025. Pre-election fiscal stimulus measures in the Spring Statement could be one reason for pricing out rate cuts in 2024. "Higher for longer" implies the possibility of fewer Bank rate cuts than the 100bp we expect in 2025, if they begin later than we anticipate. We sell 3m Sonia Dec'24 (SFIZ4) vs. 3m. Euribor Dec'24 (ERZ4) futures to express this view. Entry: 1.53%. Target: 2.00%. Stop: 1.25%. Risk to the trade is Euribor-Estr spread widening.

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[See Team Page for List of Analysts](#)**Exhibit 1: Terminal rate (Sonia), %**

Some 10bp lower since September MPC



Source: Bloomberg, BofA Global Research  
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For a list of our open and closed trade over the last 12 months, please see the latest [Global Rates Weekly](#) (20 Oct).

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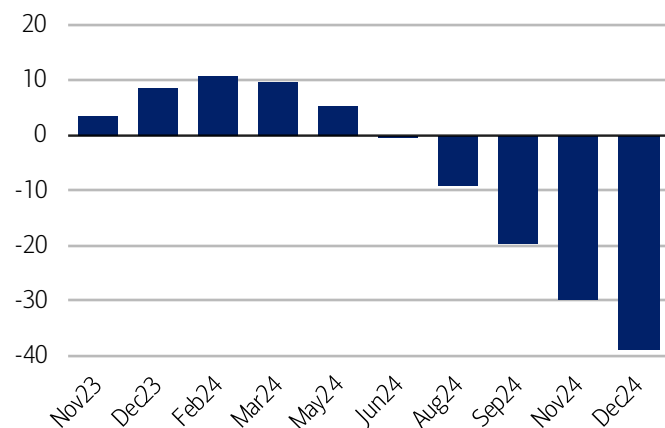
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Timestamp: 27 October 2023 01:00AM EDT

**Exhibit 2: MPC-dated Sonia Bank Rate hike expectation, bp**

Cumulative 11bp of hikes priced in ahead

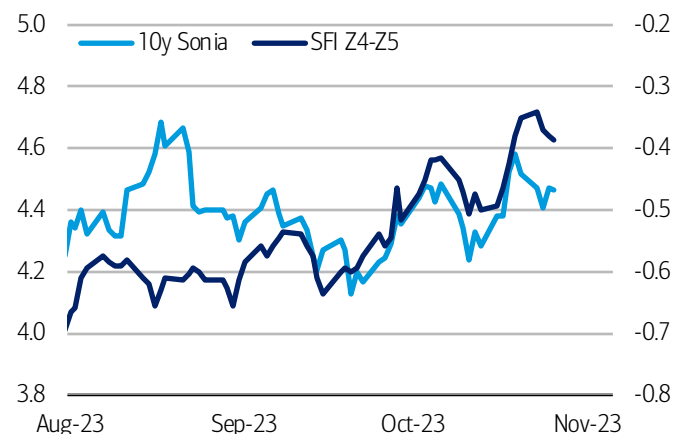


Source: Bloomberg, BofA Global Research

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**Exhibit 3: Sonia futures curve vs. 10y Sonia, %**

3m Dec'24/Dec'25 curve steepening in a rate selloff



Source: Bloomberg, BofA Global Research

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**Exhibit 4: BofA Bank rate cut expectation vs. futures pricing, bp**

Sonia futures pricing most out of line versus our expectation

BofA (bp)	Q4 2024	Q4 2025
Fed (upper)	-75	-100
ECB depo	-75	-100
BoE	0	-100
<b>Futures (bp)</b>	<b>Z4</b>	<b>Z5</b>
SFR	-80	-39
ER	-73	-34
SFI	-52	-39
<b>BofA vs. futs</b>	<b>2024</b>	<b>2025</b>
Fed	5	-61
ECB	-2	-66
BoE	52	-61

Source: Bloomberg, BofA Global Research. Numbers updated as of 26 October.

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