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## RBC European Rates & Economics Daily

- **Overnight news:** German parliament vote on fiscal package; UK welfare reform proposals; Israel airstrikes target Gaza; UK pay awards
- **Data and events:** ECB speakers; German ZEW survey; German parliament debt break vote; US industrial production; Canada CPI
- **Gilt market outlook:** UKT 4r28 auction preview

### Overnight news

**Germany's Parliament will vote today on the proposed fiscal package for defense and infrastructure** (summarised [here](#)). According to Bloomberg, the session is due to begin at 10am CET and end at 13:30pm CET. A final vote is expected at the end of the session after members of parliament have debated the proposals. Bavaria has agreed to support the changes to the debt brake - assuming approval today - when it comes before Germany's upper house, Bundesrat, on Friday.

In the UK, the **BBC reports that Work and Pensions Secretary Liz Kendall will set out reforms to the welfare system** aimed at making savings from mainly by tightening eligibility for ill-health related benefits in a speech today. We discussed the proposals in yesterday's [European Daily](#).

Region	GMT	Period	Data/Event	RBC	Consensus	Prior
Euro Area	09:00		ECB's Rehn & Escriva speak			
Germany	10:00	Mar	ZEW survey: current situation, expectation	-80.5, 50.3		-88.5, 26.0
Euro area	10:00	Mar	ZEW survey: expectations index			24.20
Euro Area	10:00	Jan	Trade balance sa (EURbn)	14.0		14.6
Germany	After 12		Vote on debt break in German Parliament			
Canada	12:30	Feb	CPI m/m, y/y (%)	0.6, 2.2		0.1, 1.9
US	12:30	Feb	Housing starts, building permits (k)	1381, 1450		1366, 1473
US	12:30	Feb	Import, export price index m/m (%)	-0.1, -0.2		0.3, 1.3
US	12:30	Mar	New York Fed Services Business Activity			-10.5
US	13:15	Feb	Industrial production m/m (%)	0.2		0.5

Sources: Bloomberg, Reuters, and RBC Capital Markets

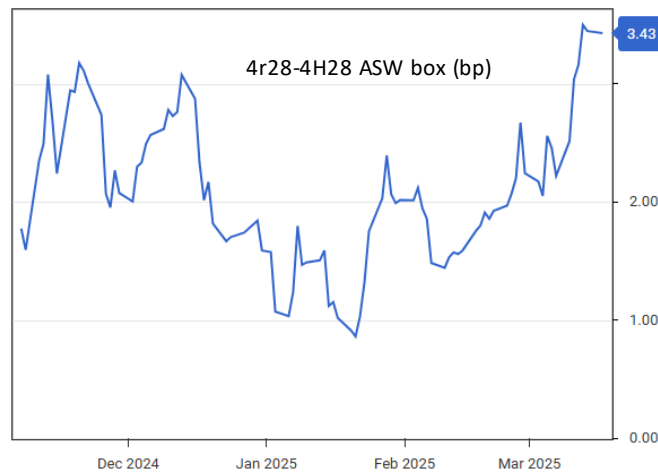
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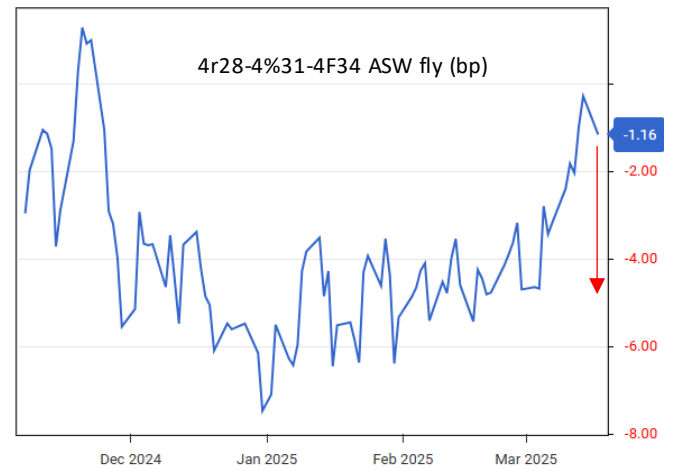
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**Exhibit 1: The 4r28s have cheapened nicely ahead of today's auction...**



Source: Bloomberg, RBC Capital Markets

**Exhibit 2: ...although our preferred micro-RV structure is being long the wings on the 4r28-4%31-4F34 ASW fly**



Source: Bloomberg, RBC Capital Markets

Israel launched airstrikes at targets across Gaza overnight. According to the Guardian newspaper, the Israel Defence Force (IDF) said the strikes would continue for as long as necessary and could extend beyond airstrikes. A statement from the Israeli Prime Minister's office, quoted by the BBC, said the strikes were in response to *"the repeated refusal to release our hostages, as well as its rejection of all of the proposals it has received from US Presidential Envoy Steve Witkoff and from the mediators"* and that *"Israel will, from now on, act against Hamas with increasing military strength"*. The BBC and other news outlets also report that the Hamas-run Gaza health ministry saying that "at least 330" were killed in the strikes.

Also in the UK the **country's largest supermarket chain Tesco which employs around 330k people, said that it had agreed a two-phase increase in pay worth 5.2%**. The UK's second largest supermarket chain, Sainsbury's already announced in January that it was raising pay by 5%. The Bank of England is expecting median pay gains to slow to around 4% this year.

In the overnight APAC session, equities gained led by Japan and Hong Kong. In Japan the Nikkei is up 1.2% and the Topix 1.3%. The Hang Seng is up by over 2% at the time of writing boosted by BYD cars after it unveiled a new battery and charging system that it said was capable of providing a range of 400km in 5 minutes. US S&P 500 futures are around 0.3% lower at the time of writing with Euro Stoxx futures up around 0.4%. In FX, DXY is up 0.2%. 10-year Treasury yields are at 4.29%. Oil (Brent crude) is up 0.55% to c.\$71.50 bbl.

## Data and events

- The **ECB's Rehn** is speaking at a livestreamed event. The **ECB's Escriva** is speaking at the opening speech at the 5th Finance Observatory. We have heard from both speakers recently, so it is unlikely we will get much new information. Both have been non-committal on whether they favour a cut at the April and/or June meetings. The **ECB's Villeroy** is speaking at a Euronext conference in Paris.
- In **Germany, the German parliament will vote on the debt break today**, likely sometime after 12pm UK time.
- **RBC economics expects US industrial production** to expand by 0.3% m/m, mainly driven by extended manufacturing hours that have boosted output across the sector.
- **RBC economics expects to see a rise in Canadian CPI y-o-y price growth to 2.5%** with the GST tax holiday that mechanically depressed prices in December and January, ending in mid-February. That would end a string of six straight readings at or below the Bank of Canada's 2% inflation target. Indeed, evidence was building that a faster-than-expected re-acceleration in Canadian growth late last year and into early 2025 was also putting a floor under inflation. The BoC's preferred "median" and "trim" core measures (which exclude the impact of changes in indirect taxes) picked up 2.7% year-over-year on average in January, and we expect it likely edged higher again in February. But, concerns that intensifying international trade risks will weigh on the economy are overshadowing stronger recent growth data. We continue to expect further BoC interest rate cuts down to 2.25% this summer.
- There is likely to be a strong pickup in the **German ZEW survey**, mirroring the strong improvement we saw in the euro area Sentix and another sign, we think, that the euro area economy is in an upswing. This is a small survey of German investors, although it is typically rarely watched since the Sentix survey is released earlier in the month and has a broader sample size.

## Gilt market outlook - UKT 4r28 auction preview

**Introduction:** Today, the DMO will re-open the UKT 4.375% Mar-28 (4r28s) conventional 3y gilt via auction, in which it will seek to sell £4.25bn nominal, taking the amount outstanding to £17.9bn and bringing around £1.2mn/bp of DV01 to the market. The bond was last tapped on 19<sup>th</sup> February and is not scheduled to be tapped before the 22<sup>nd</sup> April (as per the DMOs recently published early April auction calendar).

**On micro-RV we like being tactically long the 4r28s:** The 4r28s have cheapened well ahead of today's auction taking the 4r28s on the 4r28/4H28 ASW box to its historic cheap (Exhibit 1). Nevertheless, our favourite structure to be tactically long the 4r28s on is via buying the wings on the 4r28-4%31-4F34 ASW fly (Exhibit 2). The 4%31s have outperformed strongly of late given the bond has not been tapped since 4<sup>th</sup> December (given the DMO had launched a new 3y and 5y gilt since and hence has been concentrating its short-end gilt supply in those lines to bring them up to benchmark size). However, the 4%31s supply hiatus is set to end next Thursday when the bond is due to be tapped and hence we think the 4%31s can cheapen into that event. Within the 10y sector, the 4F34s have been a notable underperformer of late and hence we think some mean reversion (i.e. outperformance) is due in that also.

**On outright,** both from a technical and fundamental perspective, things are relatively murky to us in the near-term. We currently see the UK caught in between the opposing impulses coming from the US and Europe with gilts having moved largely sideways over the past 4 weeks, with no clear direction from the BoE either given their data dependent approach – which we don't anticipate will change at this Thursday's MPC meeting (read our review [here](#)). One could argue however that the bond bearish impulse from Europe (largely on the fiscal expansion narrative) has now been sharply priced into the market (with the actual real world effects of that to take time to feed through into the economy) and hence the marginal mover of the narrative going forward for global FI directionality is likely how the recession narrative, driven out of the US, continues to unfold. Hence, all eyes will be on the economic data and developments on the tariff front with the 2<sup>nd</sup> April reciprocal tariffs date fast approaching. Technically, 10y UST yields are still in somewhat of 'no man's land' and we look for either a break above 4.35% (as a bond bearish signal) or break below 4.13% (as bond bullish signal). Hence, we continue to remain patient on outright here.

**X-market,** we continue to favour being long Gilts vs Bunds and short Gilts vs USTs, a view we have held for the past 3 weeks or so and that has been performing well - although both spreads views have seen a small reversal in recent sessions.

**Continue to like curve steepeners (4r28-4%31 curve steepener):** We think SONIA Dec25-Dec26 (SFIZ5Z6) curve steepeners make a lot of sense here. If central banks (CBs) are at an inflection point in their rate cutting cycle (i.e. at the end of their rate cuts), then similar to what we've seen priced in of late in the ERZ5Z6 curve, we should see a bear steepening of the curve as the market prices in the possibility of rate hikes starting in 2026. However, if the recession risks continue to increase from here, driven out of the US, and particularly if we see risk assets reprice sharply lower, then the market pricing in a continuation of the rate cutting cycle from here would likely be via a front-loading of rate cuts – which should also lead to a steepening of the Z5Z6 curves.

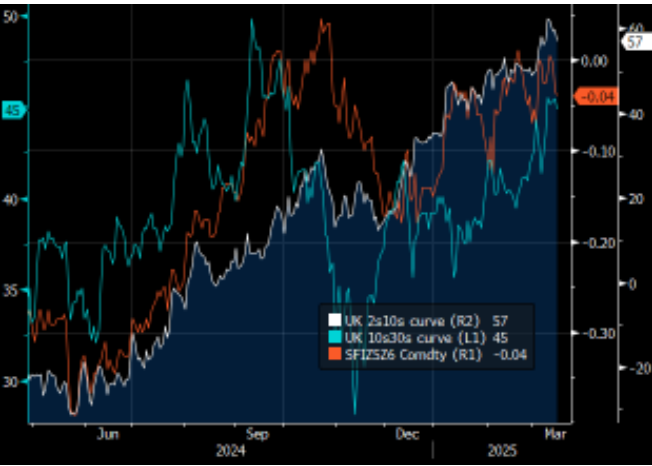
Given this view and the strong positive correlation between the SFIZ5Z6 curve and likes of 2s10s, 10s30s curves (Exhibit 3), we continue to hold our view of steeper curves – despite those gilt curves looking 'steep' on regressions vs the level of front-end rates when viewing it over recent history.

As we highlighted above, we think the 4%31s can cheapen into the auction next week (from current rich levels) and hence like the 4r28/4%31 curve steepener as an expression of this view in the near term – with the 4r28/4%31 switch looking 1-1.5bp flat relative to the broader 2s10s cash curve (Exhibit 4).

**On ASWs,** we don't have a strong view here on directionality over the next 3 months and see us largely in a sideways channel. In terms of risks, if recession risks can really start to increase and we see a risk-off move on the back of it, then ASWs could be bid near-term. Barring such outcome, then ASWs likely drift cheaper over the next few weeks/months as the elevated gilt supply outlook continues to slowly filter through the market. We note however that the 4r28 ASW is currently towards the YTD riches.

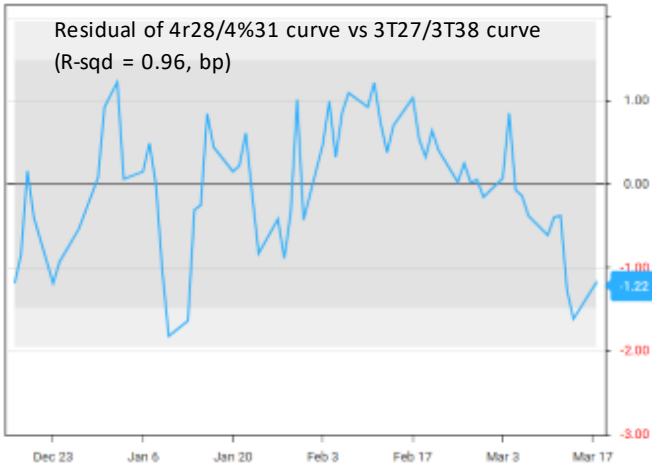
**In conclusion,** our favourite ways to hold the bond are on micro-RV, on the curve (2s5s, 2s10s steepeners) and x-market vs bunds. The bond does however trade towards the YTD riches on ASW which could be a small headwind for today's auction – although this could also explain why the concession has potentially come much more strongly through micro-RV and x-market. Hence, we continue to think the auction goes well.

Exhibit 3: We continue to favour curve steepeners here...



Source: Bloomberg, RBC Capital Markets

Exhibit 4: ...& a tactical 4r28/4%31 steepener expression



Source: Bloomberg, RBC Capital Markets

## Exhibit A: RBC growth and inflation forecasts

	2024				2025				Y/Y	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2024	2025
<b>US</b>										
Growth (q/q saar %)	1.6	3.0	3.1	2.4	0.0	1.5	1.9	1.8	2.9	1.6
Inflation (average %y/y)	3.2	3.2	2.6	2.7	2.4	2.2	2.3	2.1	4.1	2.9
<b>Euro area</b>										
Growth (q/q %)	0.3	0.2	0.4	0.4	0.3	0.4	0.5	0.5	0.8	1.4
Inflation (average %y/y)	2.6	2.5	2.2	2.2	2.4	2.6	2.7	2.6	2.4	2.6
<b>UK</b>										
Growth (q/q %)	0.7	0.5	0.0	0.1	0.1	0.3	0.4	0.4	0.9	0.8
Inflation (average %y/y)	3.5	2.1	2.1	2.5	2.6	2.4	2.5	2.3	2.6	2.5
<b>Canada</b>										
Growth (q/q saar %)	1.8	2.1	1.0	1.0	1.1	0.8	0.7	1.0	1.3	1.0
Inflation (average %y/y)	2.8	2.7	2.0	1.7	2.4	2.5	2.4	2.1	3.9	2.3
<b>Australia</b>										
Growth (q/q %)	0.2	0.2	0.5	0.4	0.7	0.6	0.7	0.7	2.0	1.2
Inflation (average %y/y)	3.6	3.8	2.8	3.0	2.2	1.9	2.4	2.9	5.6	3.3

## Exhibit B: RBC yield forecasts

USD	17-Mar	Q1 25	Q2 25	Q3 25	Q4 25
Fed Funds Mid	4.375	4.375	4.375	4.375	4.375
3m T-bill	4.28	4.26	4.21	4.23	4.28
2y TSY	4.01	3.90	3.70	3.90	4.15
5y TSY	4.07	3.95	3.65	3.80	4.00
10y TSY	4.29	4.20	3.90	4.05	4.20
30y TSY	4.59	4.55	4.30	4.40	4.50
CAD	17-Mar	Q1 25	Q2 25	Q3 25	Q4 25
BoC rate	2.75	2.75	2.25	2.00	2.00
3m CTB	2.65	2.55	2.20	2.00	2.00
2y CAN	2.57	2.60	2.30	2.20	2.10
5y CAN	2.73	2.75	2.65	2.55	2.45
10y CAN	3.07	2.95	2.90	2.80	2.80
30y CAN	3.31	3.05	3.00	3.00	3.00
EUR	17-Mar	Q1 25	Q2 25	Q3 25	Q4 25
ECB Depo rate	2.50	2.50	2.25	2.25	2.25
3m ESTR	2.32	2.35	2.15	2.15	2.15
2y Schatz	2.18	2.20	2.25	2.30	2.40
5y OBL	2.47	2.55	2.75	2.85	2.95
10y Bund	2.83	2.90	3.05	3.15	3.25
30y Bund	3.13	3.20	3.40	3.55	3.70
2y ASW	12	20	25	25	30
5y ASW	3	15	20	20	25
10y ASW	-12	5	5	10	10
30y ASW	-49	-45	-50	-50	-55
GBP	17-Mar	Q1 25	Q2 25	Q3 25	Q4 25
BoE rate	4.50	4.50	4.25	4.00	3.75
3m SONIA	4.39	4.43	4.18	3.93	3.68
2y Gilts	4.19	4.50	4.25	4.30	4.40
5y Gilts	4.30	4.60	4.40	4.50	4.60
10y Gilt	4.66	5.00	4.75	4.80	4.90
30y Gilt	5.26	5.50	5.35	5.40	5.55
2y SONIA ASW	-13	-10	-10	-15	-25
5y SONIA ASW	-29	-25	-25	-30	-40
10y SONIA ASW	-52	-40	-40	-45	-55
30y SONIA ASW	-89	-80	-90	-95	-100
AUD	17-Mar	Q1 25	Q2 25	Q3 25	Q4 25
RBA Rate	4.10	3.85	3.60	3.60	3.60
2y TSY	3.75	3.80	3.75	3.85	3.90
10y TSY	4.41	4.15	4.15	4.20	4.15
NZ	17-Mar	Q1 25	Q2 25	Q3 25	Q4 25
RBNZ Rate	3.75	3.75	3.25	3.25	3.25
2y Swap	3.50	3.30	3.25	3.50	3.75
10y Swap	4.19	4.10	4.30	4.70	4.75

Sources: Bloomberg, RBC Capital Markets

Exhibit C: US policy rate forecasts

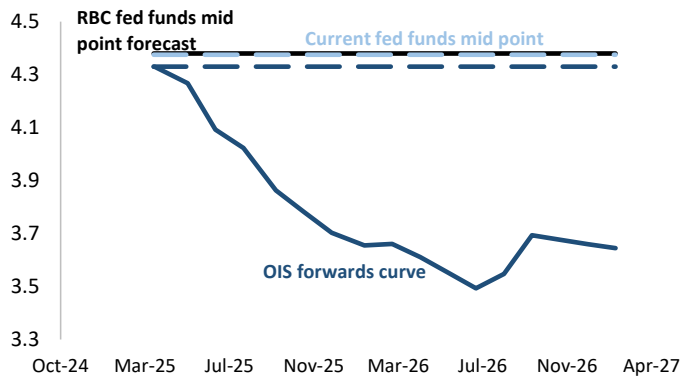


Exhibit D: Euro area policy rate forecasts

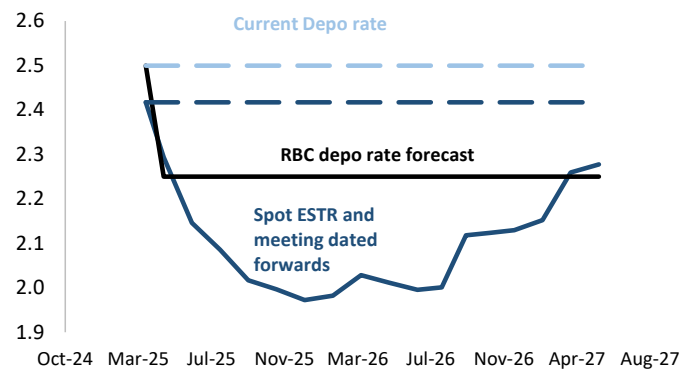


Exhibit E: UK policy rate forecasts

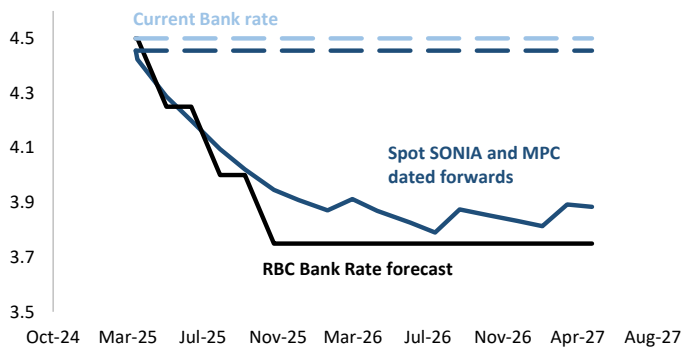
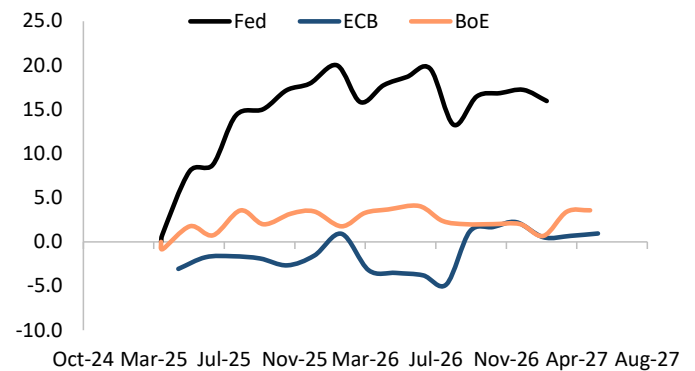
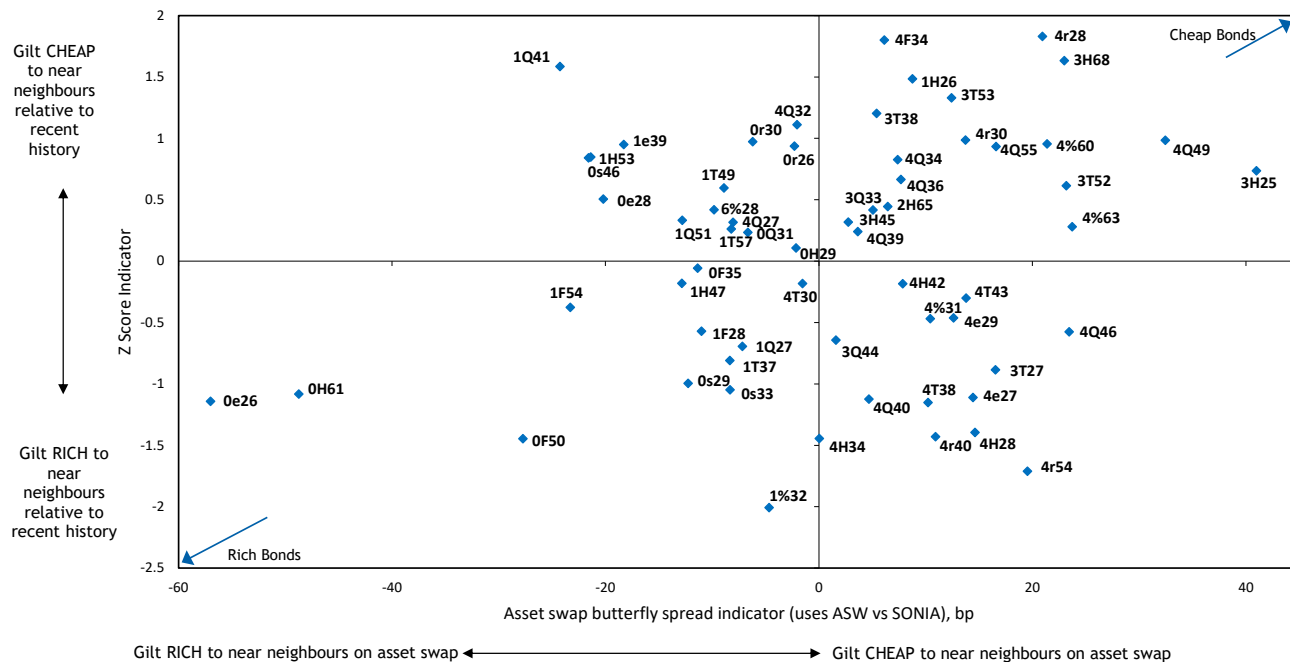


Exhibit F: 5-day change in meeting dated OIS forwards



## RBC RV Quadrant

Exhibit G: RV quadrant chart, 30d yield butterfly z-score, with asset swap butterfly indicator, bp \*





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