Futures invoice spread

Invoice spread transactions allow investors to express an opinion on the perceived credit risk of two financial debt instruments (for example, a sovereign government bond and an interest rate swap). A widening invoice spread reflects a perceived increase of credit risk. A narrowing invoice spread reflects a perceived diminishing of credit risk.

The futures invoice spread strategy is based on the forward-starting interest rate swap that begins on the last delivery date of the futures contract and ends at the maturity date of the underlying cash bond (the cheapest-to-deliver bond or CTD). The spread represents the difference between the fixed rate of the swap for the same maturity and the yield of the bond futures' CTD. Futures invoice spreads can be traded on-exchange through an Exchange for Risk (EFR) facility.

Government bond asset swap spread exposure can be achieved cost efficiently using interest rate futures instead of cash bonds. To initiate a long/short position in the bond futures market, only an initial margin is required. Bond futures, such as the CGB contract, also have a narrower bid/ask spread than that of the underlying cash bond market. Furthermore, bond futures contracts are a great alternative to investors who cannot short bonds or foreign investors that don't have easy access to the Canadian government bond market. Futures contracts also eliminate the need to do any financing transactions in the repo/reverse repo market.

Invoice spread analysis – two strategy examples

Hedging a forward interest rate swap with CGB contracts

Bloomberg's futures invoice spread analysis (IVSP) function calculates the forward bond futures yield against a corresponding forward-starting interest rate swap so that investors can evaluate potential invoice spread transactions. The IVSP analytics function can also be used to determine the number of CGB contracts required to hedge a notional amount of $10 million of forward interest rate swaps. In this analysis, we used the CGB June 2012 contract and the CTD reference bond is the Can 3½% June 1, 2020 bond.

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