



# EMMEC EGB Repo Update

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## □ Global themes

- **Growing geopolitical uncertainty** with the ongoing **Iran war** (after Venezuela and Greenland) :
  - ✓ Iran regional retaliation + strait of Hormuz blockade were not expected
  - ✓ Non-linear effects depending on the blockade persistence = extreme volatility on the front-end
  - ✓ Fear of a stagflation scenario in Asia/Europe
  - ✓ **Global diversification move accelerates** (trade, supply chains, strategic autonomy)
- **Fiscal vs monetary dominance** / LT risk premia / supply-demand / stagflation / duration / bonds vigilantes ?

## □ Market context

- High frequency news flows **tested markets multiple times** = increasing resilience/fast digestion= **more complacency** ?
- **CBs reforms** have strengthened financial system frameworks: less tolerance to liquidity risk and volatility
- Before the Middle-East conflict:
  - ✓ **Low-vol** = strong risk appetite = **risk-off + volatility = opportunity**
  - ✓ **Large capacity**, confidence, FOMO?
  - ✓ Strong **fundamentals** + good flows **momentum** + **low realized volatility** = **carry roll down + mean reversion** vs tactical
- Since MAR26:
  - ✓ Extreme volatility = positions cleaning (Front-end, steepners, credit spreads) = **lower liquidity**
  - ✓ Reaction function of **Schatz spread** to risk-off **disappointed again**
  - ✓ **Bonds vigilantes** are back on fiscal and inflation risks (record on 30y yields across markets):
    - ✓ Political risk (driven by UK)
    - ✓ Expensive welfare policies / defense spending
    - ✓ CBs credibility / Inflation
    - ✓ Less appetite from pension funds for long term bonds + QT
    - ✓ Bond demand from Middle-East / China?
    - ✓ Issuance duration shifting to shorter maturities = refinancing risk

# New Regimes, New Opportunities for Europe?



## ❑ New ECB framework implementation

- I. Schnabel presentation (6nov25) clarified the direction of travel for the next months
  - ✓ Acknowledgement of the **demand-driven** system: FRFA + structural tools (LT repo + bond portfolio)
  - ✓ Liquidity excess reduction ongoing = repo rates will rise
  - ✓ Encourage banks to use repo facilities (ECB not a backstop but a « day-to-day liquidity counterparty) to remove any **stigma** (like BOE last year)
  - ✓ DFR/MRO spread already tight @ 15bps
- Securities Lending service now cleared (EUREX+LCH) @ DFR-20bps
- **Next review:** cleared MLF ?
- Conjonctural repo spikes (fwd YE) ? What is the (real) cap?

## ❑ EUR front-end

- **The ECB was in a « good place »**
- **But**, Middle-East situation changed everything
- **EGB repo rates « plateau »** since last year (around DFR) in line with DU invoice trading range [-7;-13]
- **Timing of repo rates resuming MRO convergence?**
- DMO cash
- Dealers scarce resources: balance sheet, NSFR, LCR

## ❑ Is there opportunities for Europe?

- **Recent US decisions triggered market volatility** (Tariffs, FED independence, military/defense )
  - ✓ (geo)political divergence, shifts in global trade, Inflation ...
  - ✓ Gold outperformance, FX hedging
- USD diversification? Reallocation or new money ?
  
- In this context, **EGBs might be seen offering more stability and visibility**
- **Europe challenges:** market fragmentation + liquidity comparison vs UST (bonds @ 13TRN vs 36 TRN, OI futures @ 6m vs 18m or repo @ 0.5 TRN vs 2.5 TRN)



## Asymmetrical risk on schatz spread

- ❑ DU invoice in tight range since 2025 + offering positive carry (3bps) = **cheap risk-off hedge**
- ❑ Currently **traders might overlook repo risks** (stable since last year), but **going into 2027** longs should reassess their rationale
- ❑ As (1) non-responsiveness is persistent + we see a potential convergence of (2) fundamentals, (3) positioning and (4) expected flows:

### 1. Non-responsiveness:

- **DU risk-off doesn't work** since « liberation day »: Bayrou, US regional banks, Greenland and very modestly to Iran war
- Political risk in Europe is idiosyncratic (since FR snap elections)
- Limited catalysts for DU invoice performance in current market conditions
- No clear bullish DU invoice drivers in our view

### 2. Fundamentals:

- Capped by funding rates / carry + repo-based derivatives flows
- **DU and repo correlated to liquidity excess since 22** before decoupling in 25
- Uncertainty on timing and linearity of repo rates convergence to MRO
- ESTR vs repo divergence may reflect temporary market dynamics

### 3. Positioning:

- Record high OI in DU futures (2.7m). Price action consistent with long positioning (invoice, steepners or vs BTS)
- Probably **no DU invoice shorts** :
  - ✓ negative carry + negative tail risk exposure
  - ✓ limited DU performance on risk-off (no short covering)

### 4. Expected flows (if repo rates move higher):

- Long carry positions may face pressure, potentially triggering unwinds
- New shorts to be build (signal + momentum)
- Convergence of unwinds + new trades
- MRO “backstop” (15bps higher)
- Potential new equilibrium for DU invoice estimated around -20bps

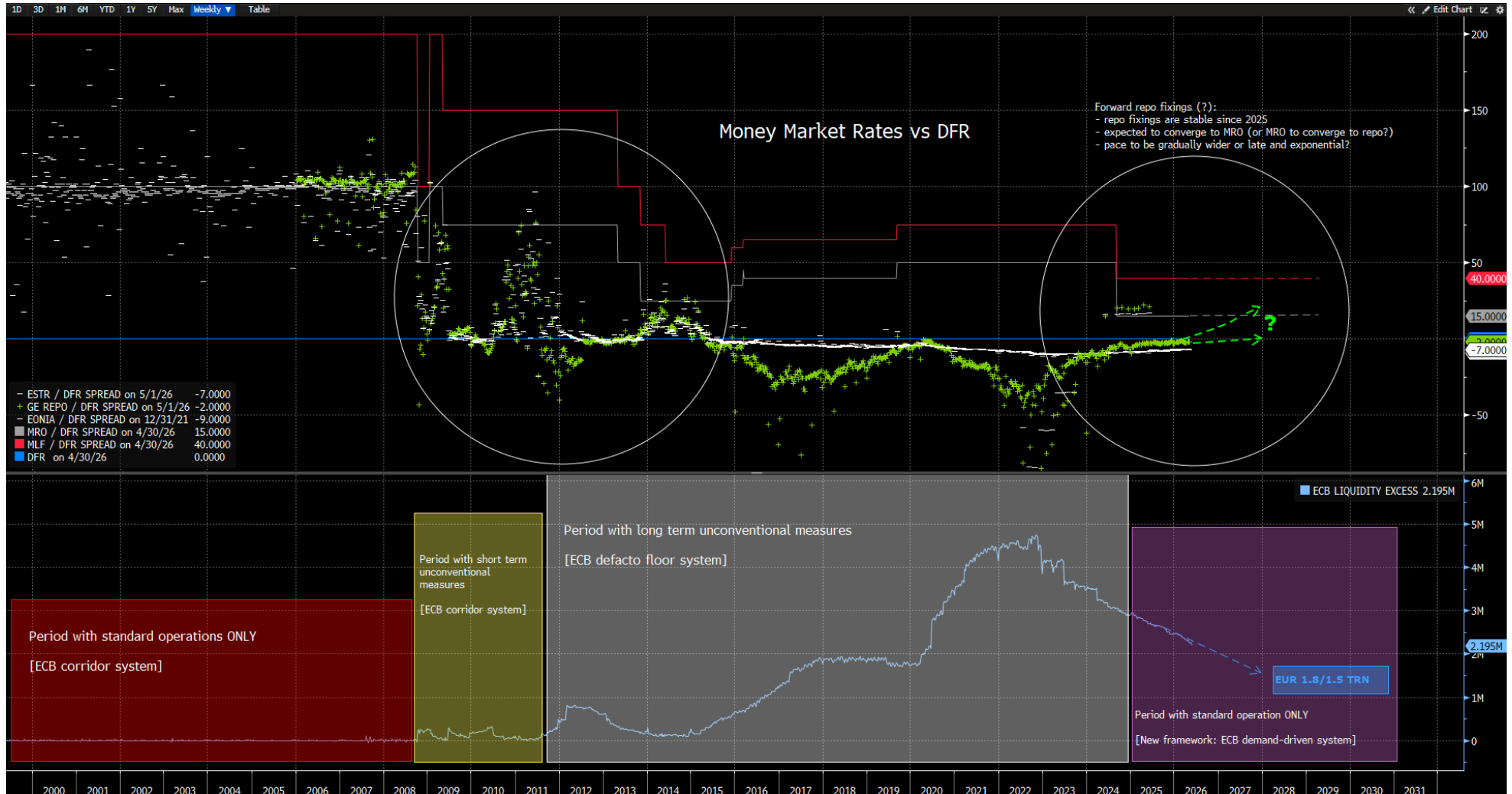
- ❑ Long GE ASW are doing well combining (marginal) expected value and risk-off protection, but **as we are moving everyday closer to the “inflexion point”, these positions might be at risk by next year** and expect to see gradual **long German ASW unwinds** (0-5y) or **switching OIS hedges** for bonds/futures



# ANNEXES: MONEY MARKETS

# ECB New 2024 Framework & German Repo vs DFR

(source: Bloomberg & CME)



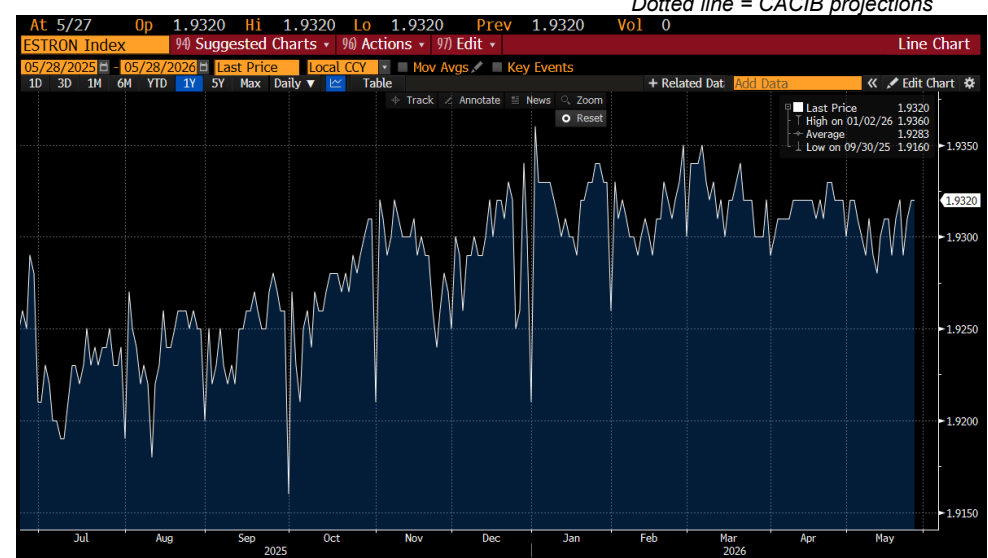
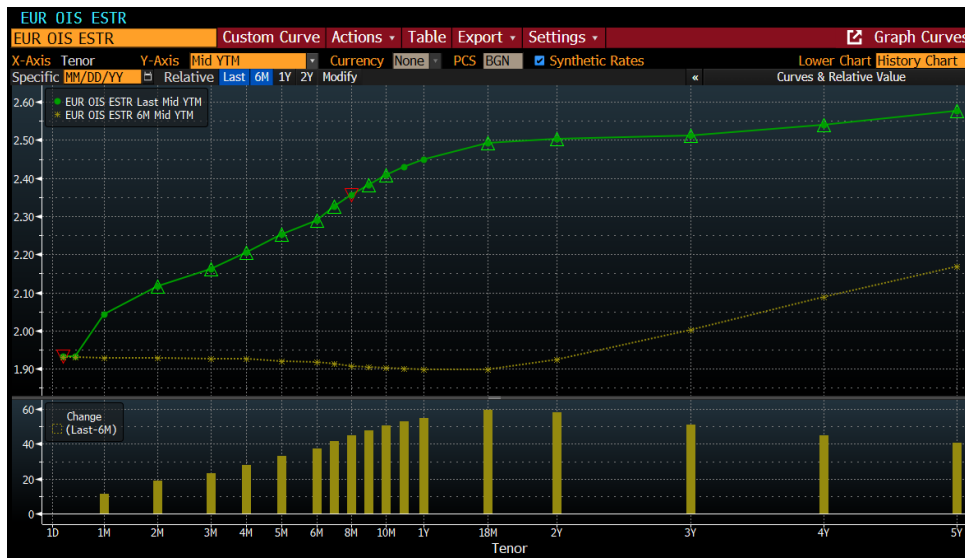
Dotted line = CACIB projections

# ECB Meetings, OIS Curve & ESTR

(sources: CACIB & Bloomberg)



MONETARY POLICY COMMITTEE (ECB)							
Meeting	Start	End	Days	Impl (bp)	Impl (rt)	Hikes/cut	ARM
Jun26	17Jun26	29Jul26	42	23.6	2.168		0.25
Jul26	29Jul26	16Sep26	49	32.1	2.253	34.1%	0.25
Sep26	16Sep26	04Nov26	49	48.0	2.412	63.8%	0.25
Nov26	04Nov26	23Dec26	49	53.7	2.469	22.7%	0.25
Dec26	23Dec26	10Feb27	49	61.9	2.551	32.8%	0.25
Feb27	10Feb27	24Mar27	42	64.3	2.575	9.4%	0.25
Mar27	24Mar27	05May27	42	66.2	2.594	7.6%	0.25
May27	05May27	16Jun27	42	67.0	2.602	3.3%	0.25
Jun27	16Jun27	28Jul27	42	66.0	2.592	-3.9%	0.25
Jul27	28Jul27	15Sep27	49	65.1	2.583	-3.7%	0.25
Sep27	15Sep27	03Nov27	49	62.4	2.556	-10.7%	0.25
Nov27	03Nov27	22Dec27	49	59.4	2.526	-12.0%	0.25
Dec27	22Dec27	09Feb28	49	56.8	2.500	-10.5%	0.25
Feb28	09Feb28	29Mar28	49	54.9	2.481	-7.6%	0.25
Mar28	29Mar28	10May28	42	54.2	2.474	-2.9%	0.25



# The ECB Expected Normalization Process Toward the New Framework

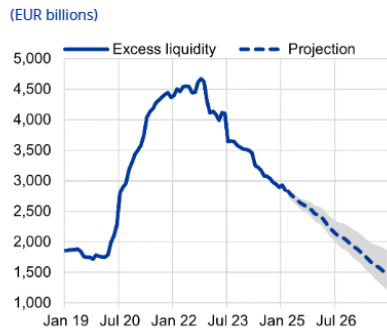
(source: ECB)



25 April 2025

**Chart 1**  
Liquidity position of euro area banks

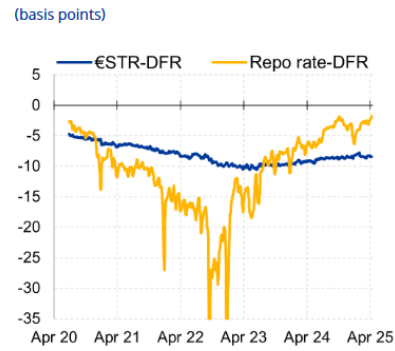
a) Path of excess liquidity



Sources: ECB (Supervisory statistics and MOPDB), ECB calculations.

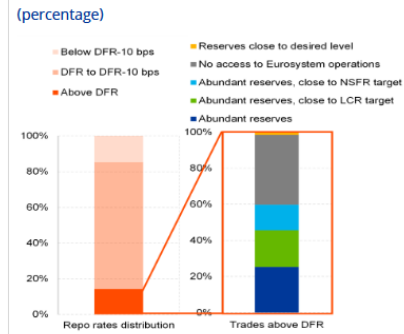
**Chart 2**  
Repo rates anchored at the DFR with no signs of reserve scarcity

a) Short-term rates-DFR spread



Sources: ECB (Supervisory statistics and MOPDB), ECB calculations.

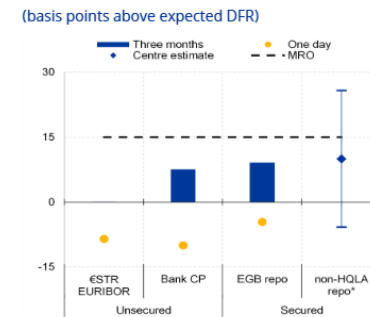
b) Share of repo trading above the DFR



Sources: ECB (Supervisory statistics and MOPDB), ECB calculations.

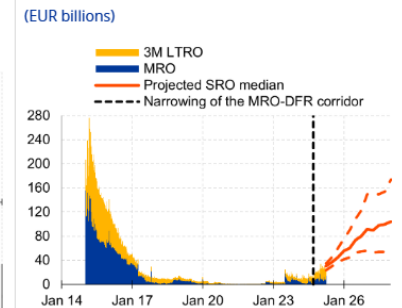
**Chart 3**  
Banks tap markets to satisfy liquidity demand as market funding is economically attractive

a) Relative market pricing of borrowing in money markets vs the expected DFR



Sources: ECB (Supervisory statistics and MOPDB), ECB calculations.

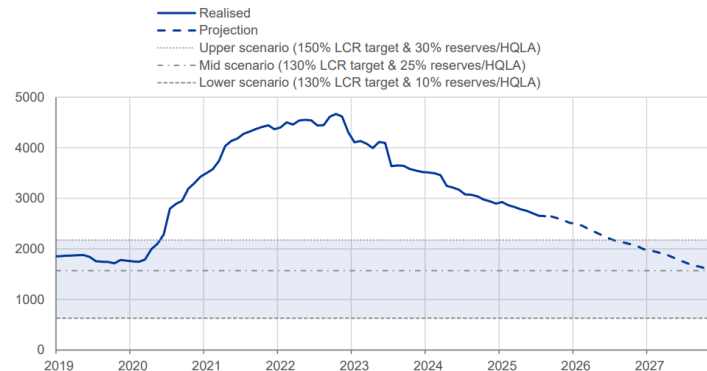
b) Use of Eurosystem standard refinancing operations



Sources: ECB (Supervisory statistics and MOPDB), ECB calculations.

6 November 2025

**Excess reserves and bank reserve demand scenarios**  
(EUR bn)



Sources: ECB (Supervisory statistics and MOPDB), ECB calculations.

# I. Schnabel Views On What Is Coming Next: Steering via DFR or MRO?

(source: ECB)



## 6 November 2025

As QN proceeds, there will come a point when the level of outstanding reserves is no longer sufficient to meet the aggregate demand from the banking sector, meaning that it will not be possible to satisfy liquidity demands via the redistribution of reserves.

At that point, overnight and term repo rates could rise more meaningfully, and take-up of our operations will increase. However, this would not be a signal of looming stress but rather a sign of a functioning system that endogenously steers banks towards our refinancing operations.

## 26 May 2026

**How do we know liquidity is “less ample”? Will there be greater volatility in the €STR? Rising take-up of main refinancing operations (MROs)?**

“Less ample” will show up in the form of greater access to our operations. This is a clear signal that banks have a demand for reserves that they cannot satisfy in the market at more favourable rates. Therefore they will start accessing our operations.

In this transition, I wouldn't exclude a bit more volatility in money market rates. We've also seen this in the United States and the United Kingdom. I don't think that's something to be overly worried about. It's the normal transition that we are expecting. And rates will have to move up to make this happen.

# The first year of the Eurosystem's new operational framework

(source: ECB)



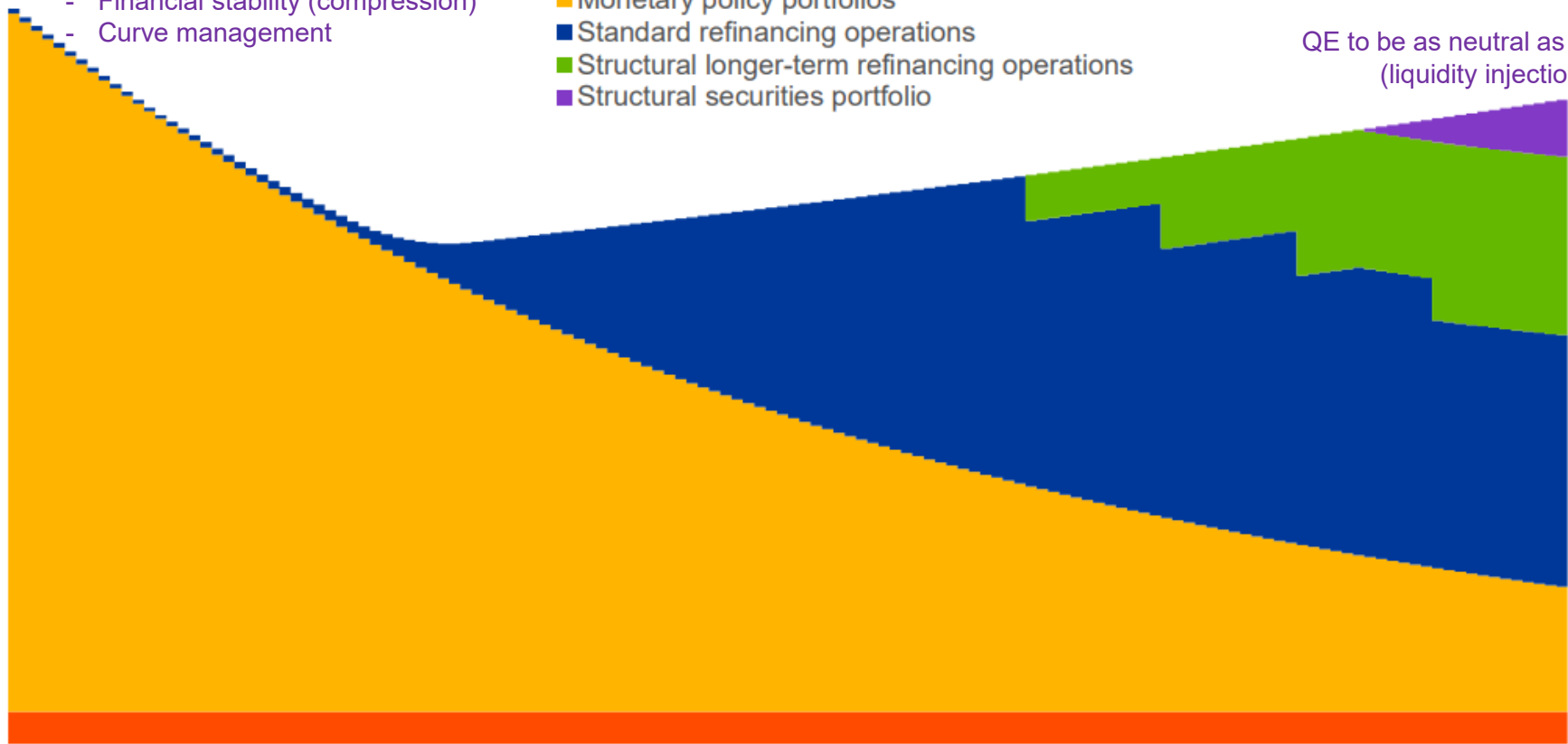
## Stylised evolution of the Eurosystem liquidity supply in the new operational framework

Various QE type:

- Liquidity injection
- Financial stability (compression)
- Curve management

- Net financial assets
- Monetary policy portfolios
- Standard refinancing operations
- Structural longer-term refinancing operations
- Structural securities portfolio

QE to be as neutral as possible  
(liquidity injection)



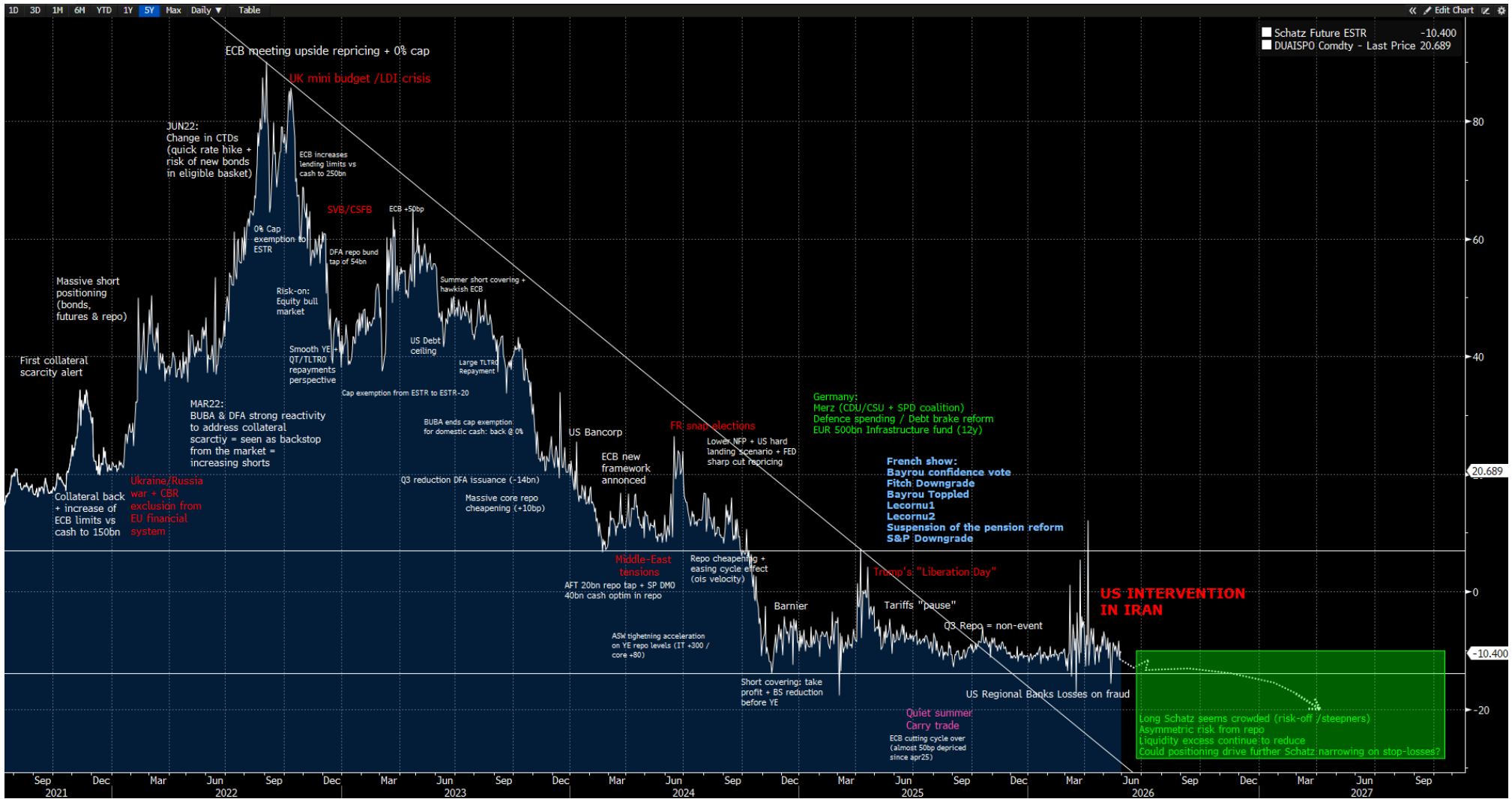
Source. ECB.



# ANNEXES: SCHATZ

# Main Markets Events & Schatz ESTR

(source: Bloomberg)



Dotted line = CACIB projections

# Is EGB Repo Lagging?

(source: Bloomberg & CME)



# Is Schatz ESTR Lagging?

(source: Bloomberg)



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