

June bond market cash: On the count of 3, let it fly

By Warren Lovely & Taylor Schleich

Back by popular demand is a detailed preview of Canada's outsized June bond market coupon/roll/maturity effects.

As you may already be aware, there are a few wrinkles to this June's cashflows. Not least of which is the day of the week when the particularly large cashflows are scheduled to arrive.

As a reminder, the rather acute concentration of maturities/coupon payments in Canada's domestic bond market have long made June 1st and June 2nd extraordinary cashflow days. While somewhat overshadowed by the 1st/2nd, a nice slug of cash typically lands on June 15th too. This year is no different. In fact, Index-related cashflows will be larger than ever this June.

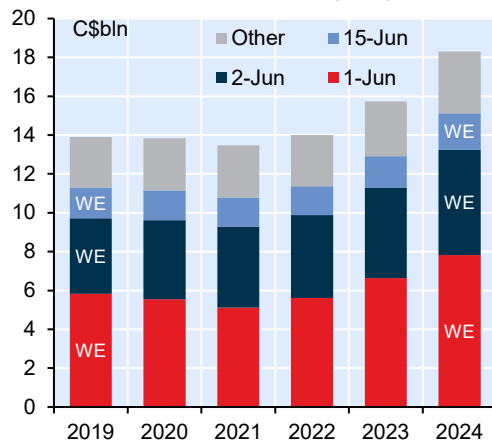
But glancing at a Gregorian calendar for 2024 you will see this: June 1st: Saturday. June 2nd: Sunday. June 15th: Saturday. Clearly part of what makes this year different is that all three of the largest cashflow

days fall on a weekend. It means super-concentrated cashflow/duration effects, which we've not yet had in the post-COVID period. So get ready for some fireworks.

Other wrinkles? Well, just like last year, we have a less-than-certain BoC policy rate decision coming just days after the biggest wave of cash. Mind you, the surprise in June 2023 ended up being a *hike*. This year, we're debating whether conditions are sufficient to warrant a *cut*. (We're not so sure.) Meanwhile, market location is unique, with yields, curves and differentials in many cases far removed from where things have traditionally stood in the lead up to June. And don't forget that bond issuers are presumably ready to respond to investor demand spurred by all that cash, this supply impulse another variable to control for. There's a fair bit to unpack then. What follows could be thought of as a first installment. We will have more to say as we move ever closer to what will be an extraordinary bond market event.

Chart 1: More cash flowing this June

Total Index cashflows: Jun-24 vs. prior years



Source: NBF, FTSE Russell | Note: WE denotes weekend

Table 1: June 1st/2nd fall on weekend

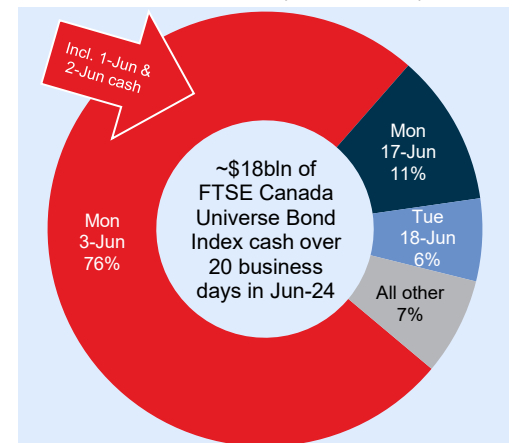
Day of week: Key June cashflows over the years

Year	June			
	1st	2nd	15th	18th
2024	Sat	Sun	Sat	Tue
2023	Thu	Fri	Thu	Sun
2022	Wed	Thu	Wed	Sat
2021	Tue	Wed	Tue	Fri
2020	Mon	Tue	Mon	Thu
2019	Sat	Sun	Sat	Tue
2018	Fri	Sat	Fri	Mon
2017	Thu	Fri	Thu	Sun
2016	Wed	Thu	Wed	Sat
2015	Mon	Tue	Mon	Thu
2014	Sun	Mon	Sun	Wed
2013	Sat	Sun	Sat	Tue
2012	Fri	Sat	Fri	Mon
2011	Wed	Thu	Wed	Sat
2010	Tue	Wed	Tue	Fri

Source: NBF

Chart 2: June 3rd a very big deal

Distribution of Index cash by business day: Jun-24

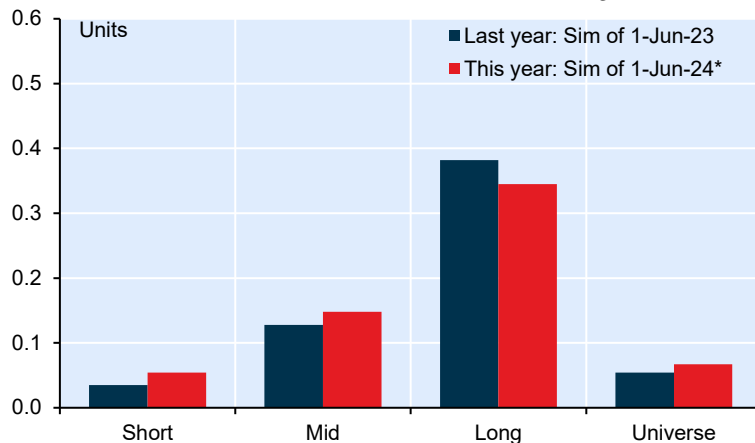


Source: NBF, FTSE Russell | Note: As of 1-May-24

As it stands, a record amount of FTSE Canada Universe Bond Index cash is set to flow this June (>\$18 billion for the month as a whole). Index-related cashflows are 16% higher than June 2023 and 30% north of June 2022. Note that all three of the largest cashflow days fall on a weekend this year, which concentrates the cash even more.

Chart 3: Theoretically, June 1st impact similar to last year...

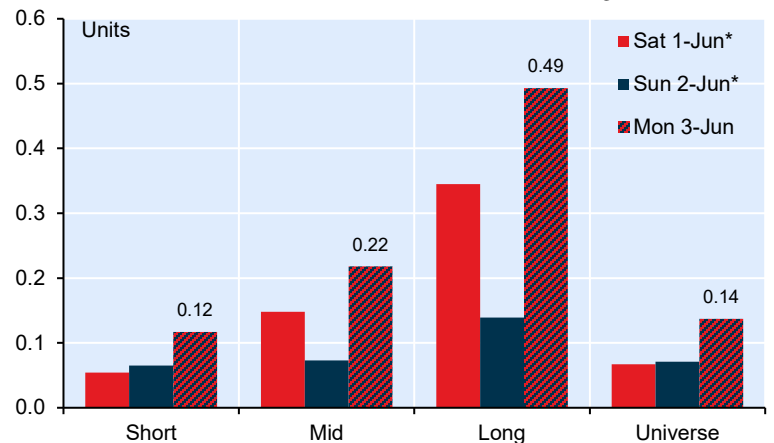
FTSE Canada Universe Bond Index: Simulated duration change on 1-Jun



Source: NBF, FTSE Russell | Note: 1-Jun-24 theoretical, as falls on weekend

Chart 4: ... but Jun 1st/2nd effect combined into June 3rd

FTSE Canada Universe Bond Index: Simulated duration change on 3-Jun-24

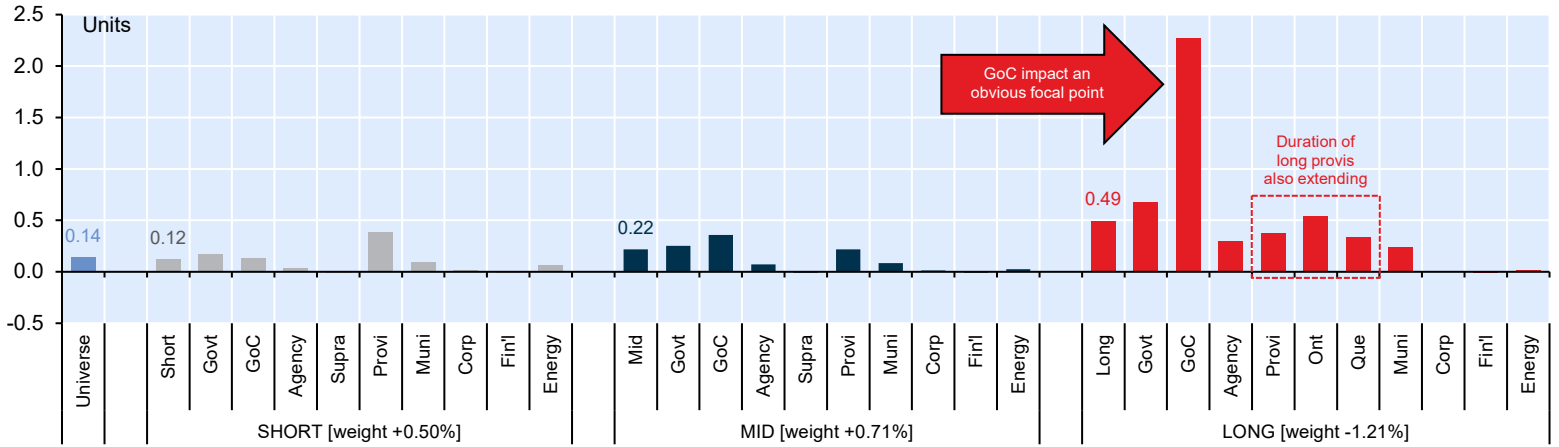


Source: NBF, FTSE Russell | Note: 1-Jun/2-Jun theoretical, as both fall on weekend

Theoretically isolating for the largest cashflow day—June 1st—you can find that Index duration impacts are significant, but not massively different than last year. But again, June 1st is not a good business day in 2024. Nor is June 2nd. So the cumulative/combined duration increase, to be captured on June 3rd, will be quite something.

Chart 5: Dissecting prospective duration adjustments on June 3rd, with long end & GoC obvious focal points

Projected change in modified duration of FTSE Canada Universe Bond Index by term & sector/issuer: Friday 31-May-24 to Monday 3-Jun-24 (i.e., 3D impact)

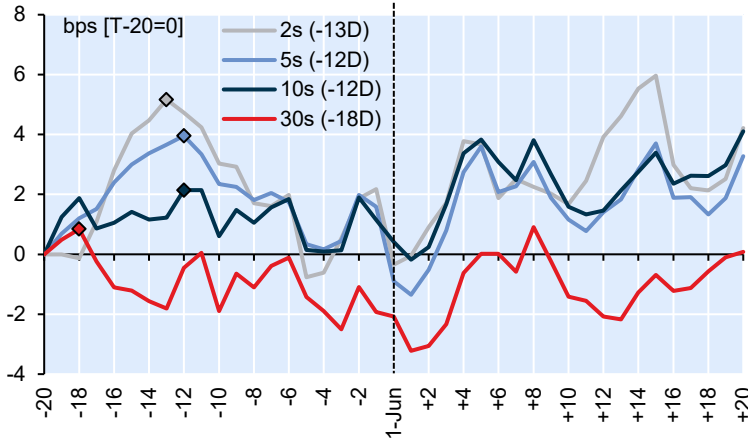


Source: NBF, FTSE Russell | Note: As with Charts 3-4, duration change based on NBF simulations using 1-May-24 closing values/constituents; assumes no change in yield curve

Given the nature of FTSE Canada Universe Bond Index rolls and coupons, the very biggest duration impacts are expected in the Long bucket. Without minimizing the simulated increase in Long Provi sub-index, it's in the long(er) end of the GoC market where things could get particularly spicy.

Chart 6: Optimal entry vs. UST 12-18 days prior (so get ready)

Cumulative change in GoC-UST yield differentials prior to/after 1-Jun

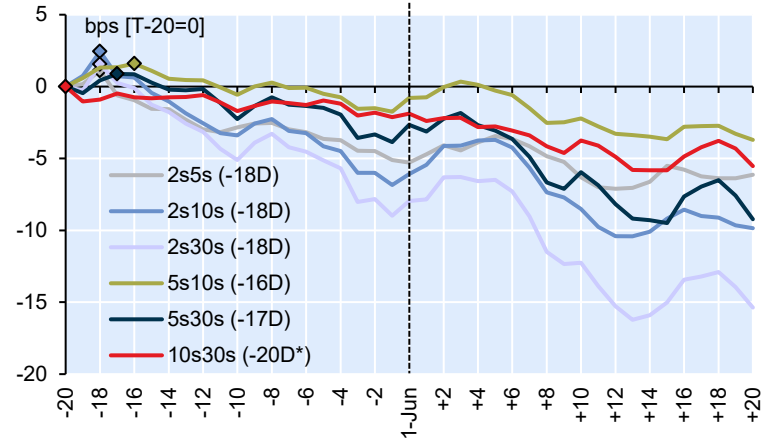


Source: NBF, BBG | Note: Value in (:) denotes optimal entry vs. 1-Jun (14Y sample)

The 'early June effect', if you want to call it that, isn't new. We've tested/analyzed it for ages. Investor awareness has grown. In the most general of terms, the 'a priori' assumption is for lower yields, flatter curves and outperformance vs. USTs (where bond maturities are less concentrated). As for entry, early May is usually a good bet.

Chart 7: Historically, paid to get curve flattener on early

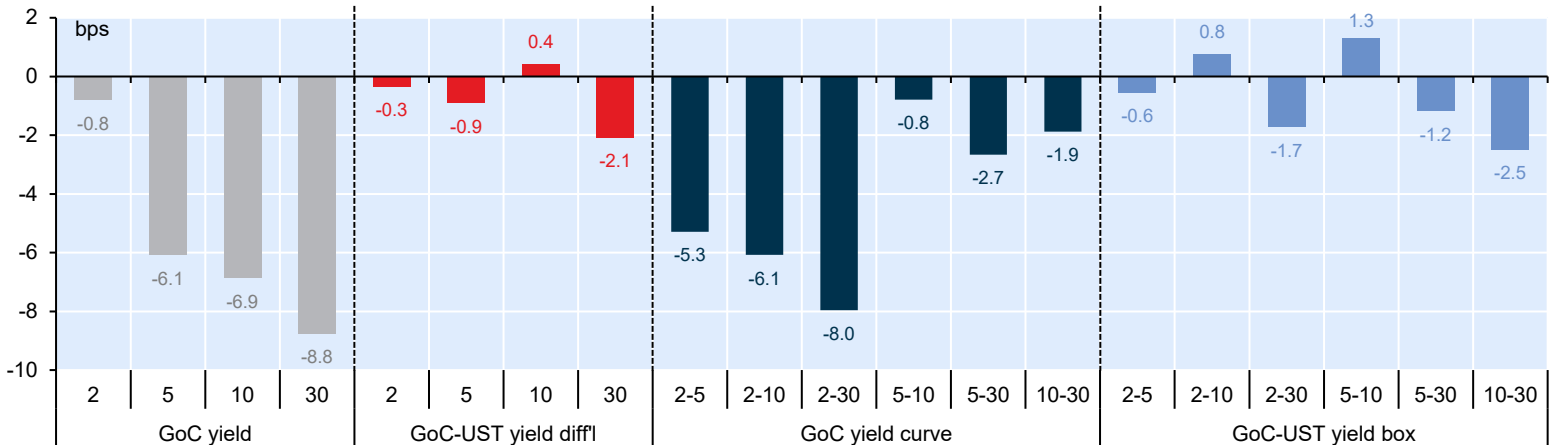
Cumulative change in GoC yield curves prior to/after 1-Jun



Source: NBF, BBG | Note: Value in (:) denotes optimal entry vs. 1-Jun (14Y sample)

Chart 8: June's wall of cash has tended to leave mark on Canadian rates (although average moves to be treated with caution)

Average change (net) in GoC interest rates (yields, curves, butterflies, vs. UST) in 20D prior to 1-Jun (14Y sample, 2010-23)

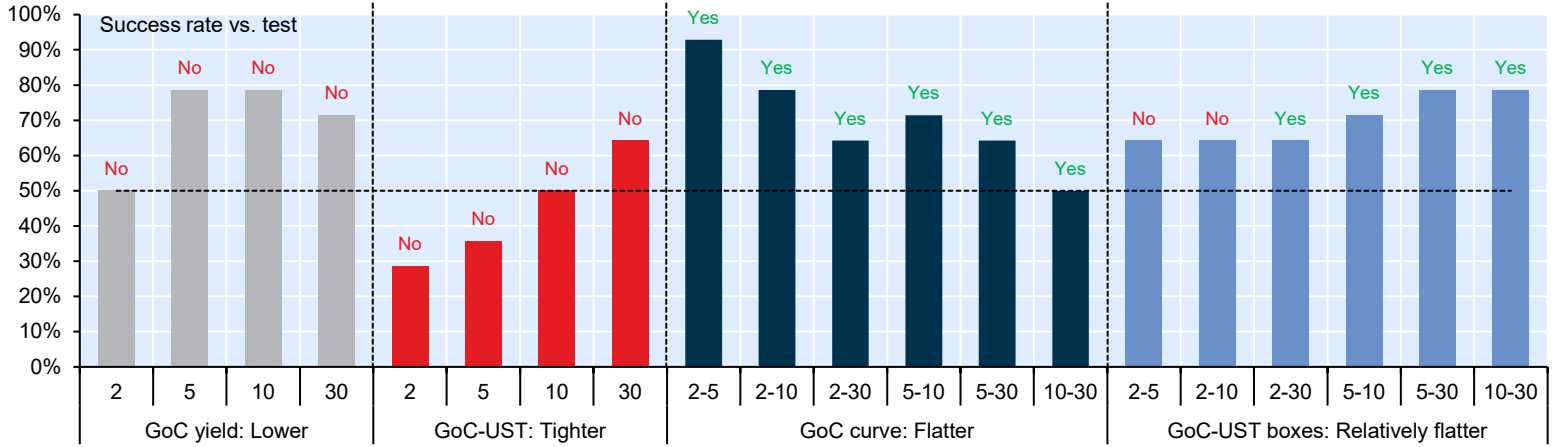


Source: NBF, BBG

We're mindful that simple averages—even when generated over a good number of years—don't necessarily paint a perfect picture. But tallying up actual performance going into June 1st, the intuitive direction of trade seems to have held. On average, absolute and relative performance of Canada's long end has been pretty solid.

Chart 9: Searching for consistently profitable trades going into the June cash deluge

Past success rates vs. expected direction in GoC interest rates (yields, curves, butterflies, vs. UST) in 20D prior to 1-Jun (14Y sample, 2010-23)

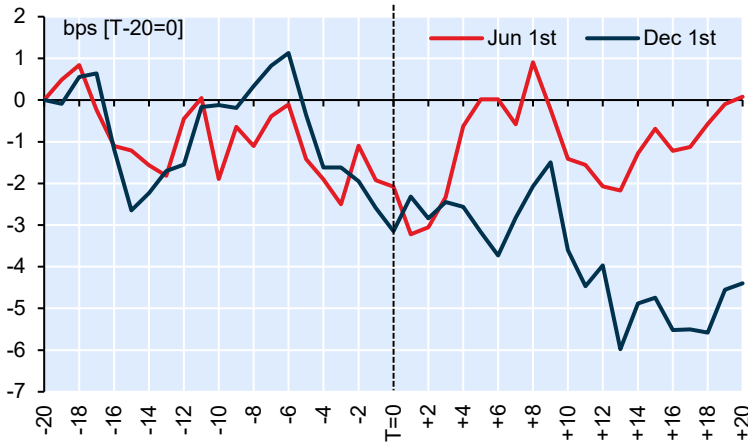


Source: NBF, BBG | Note: Success based on actual move vs. expected direction in lead up to 1-Jun for 14Y post-GFC sample; 'Yes' or 'No' refers to last year's success (i.e., 2023)

Further to Chart 8 (pg. 2), we've observed some past success going into June cashflows. Mind you, past performance is no guarantee of future success. Nor will you find 100% success rates in any particular element. Moreover, as we'll explore below, 2023 offered a clear reminder that things don't always follow the traditional path.

Chart 10: Versus USTs, less-lasting impact than Dec 1st...

Cumulative change in GoC-UST 30s prior to/after 1-Jun & 1-Dec

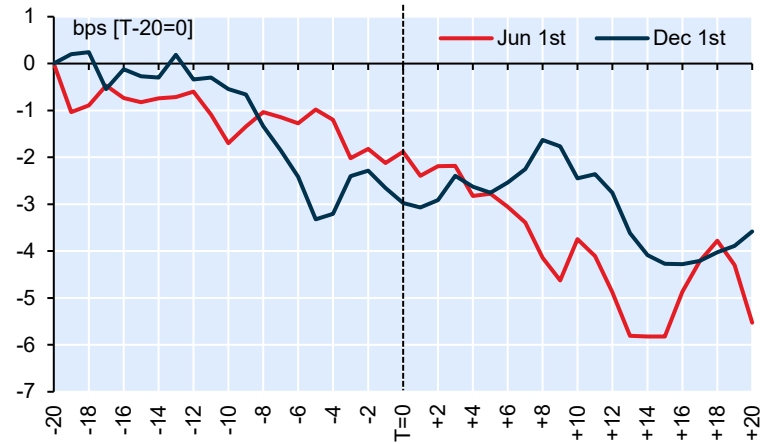


Source: NBF, BBG | Note: Weekdays relative to 1-Jun or 1-Dec (14Y sample)

Notwithstanding the apparent support for the long end, Canada's performance vs. Treasuries can fade post June 1st. Looking through daily oscillations, GoC-UST 30-year differentials have, on average, been no tighter at the end of June than they were at the dawn of May. Curve flatteners, however, appear to be longer lasting.

Chart 11: ... although flatterer often has legs

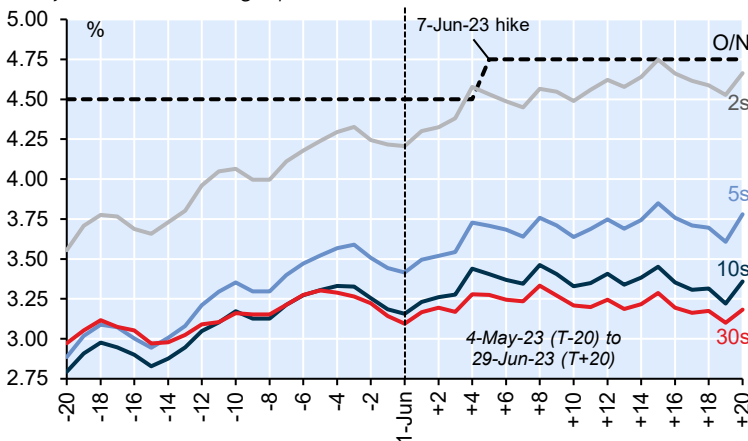
Cumulative change in GoC 10s30s curve prior to/after 1-Jun & 1-Dec



Source: NBF, BBG | Note: Weekdays relative to 1-Jun or 1-Dec (14Y sample)

Chart 12: Last year's less-than-fully-priced hike left mark

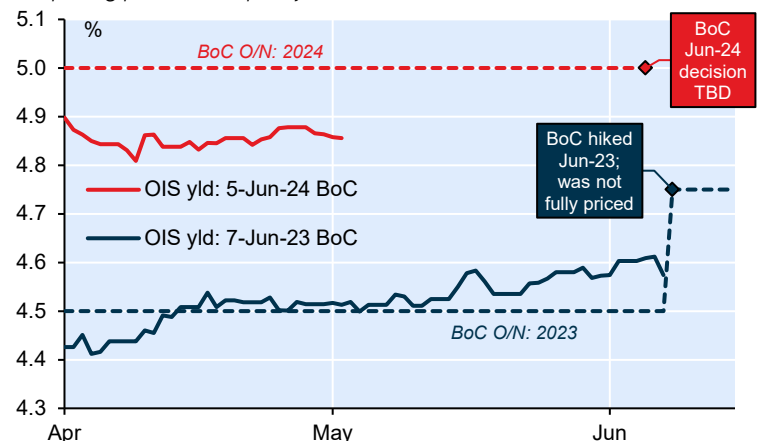
GoC yields & BoC overnight prior to/after 1-Jun-23



Source: NBF, BBG | Note: Weekdays relative to 1-Jun-23

Chart 13: Coming BoC rate decision a wild card (just like last year)

OIS pricing prior to BoC policy rate decisions: 7-Jun-23 & 5-Jun-24

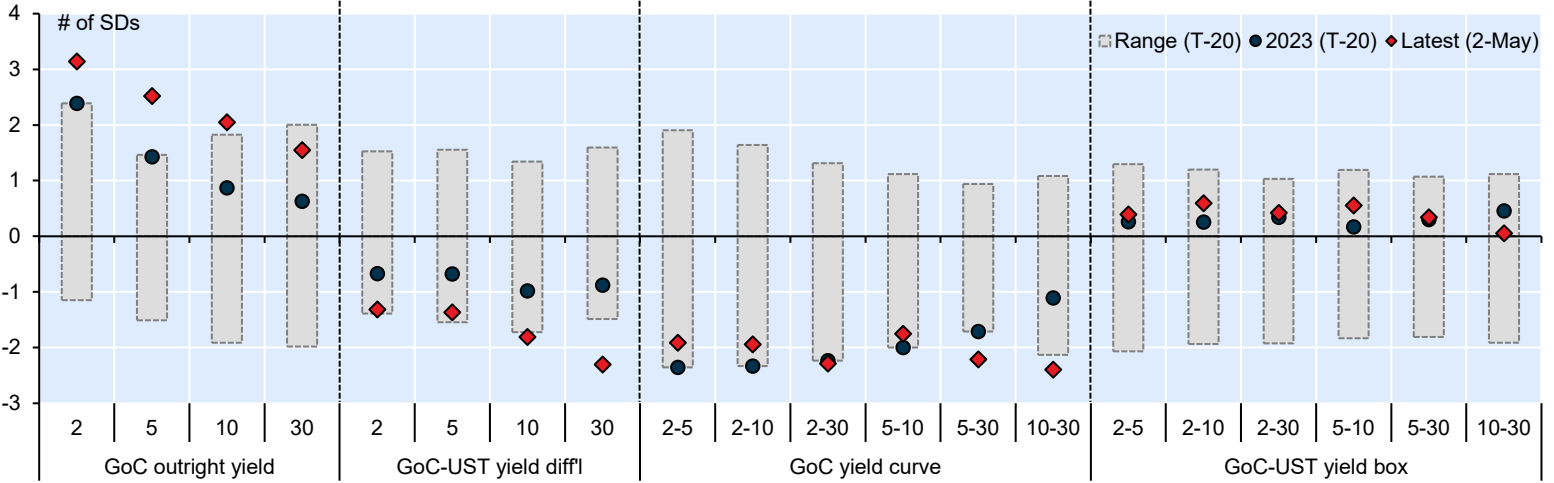


Source: NBF, BBG | Note: OIS pricing of 5-Jun-24 BoC decision up to 2-May-24

Empirical analysis comes with a caveat: all else equal. But as we saw last year, events can transpire to throw the market off its traditional path. Last June it was a less-than-fully-priced BoC rate hike. The BoC will once more be in the spotlight this June, where the prospect of a rate cut is being heavily debated. Some will be surprised.

Chart 14: Cross-market levels tighter and curves flatter than where things have traditionally stood

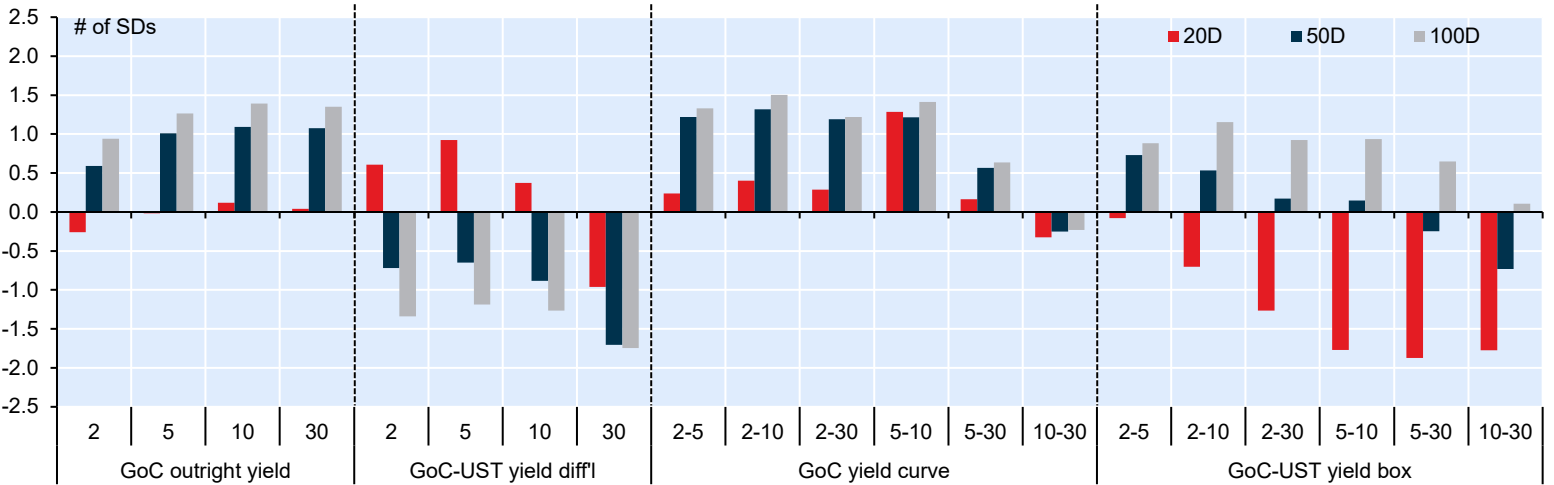
Valuation snapshot: Relative deviation of current GoC interest rates from historical average observed 20D prior to 1-Jun (14Y sample, 2010-23)



Source: NBF, BBG | Note: Latest levels refer to 2-May-24; shaded range refers to max/min recorded T-20D for 2010-23 period; 2023 valuations included for more timely reference

Chart 15: A shorter-term assessment of curves and relative yield differentials (again taking Z-score approach)

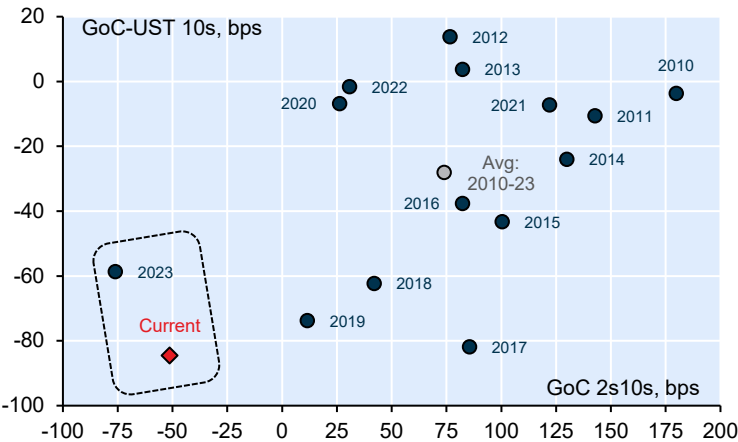
Valuation snapshot: Relative deviation of current GoC interest rates from recent averages (20D, 50D, 100D)



Source: NBF, BBG | Note: Latest levels refer to 2-May-24

Chart 16: Flatter and richer than average

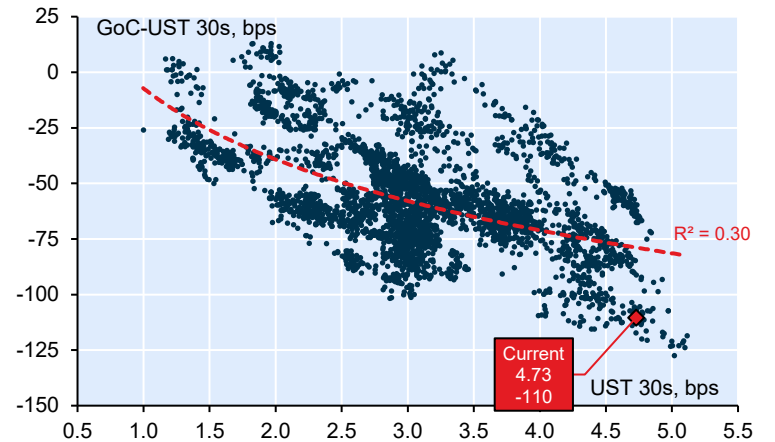
GoC 2s10s curve & GoC-UST 10s: Current vs. prior years (prior to 1-Jun)



Source: NBF, BBG | Note: Current refers to 2-May-24; prior years are 20D prior to 1-Jun

Chart 17: Further perspective on Canada-US longs

GoC-UST 30s vs. UST outright yield



Source: NBF, BBG | Note: Current refers to 2-May-24; daily levels from Jan-20 onwards

Spare a thought for current market valuation/location, which is anything but 'normal'. As powerful/significant as June cashflow can be, Canadas already trade at a material premium to USTs, while individual curves tend to the flatter side of average. That's true when lining things up vs. years' gone by or more recent levels. We offer this as context, being mindful that economic, financial, policy rate and geopolitical outlooks remain fluid. Much could change before the bond market cash flows.

Table 2: A closer examination of average historical performance in/around Jun 1st

Average move (net) & success rates in GoC interest rates (yields, curves, butterflies, vs. UST) & provincial credit in days before/after 1-Jun (14Y sample, 2010-23)

		GoC outright yield				GoC yield curve						GoC butterfly			
Wk days		2-year	5-year	10-year	30-year	2s-5s	2s-10s	2s-30s	5s-10s	5s-30s	10s-30s	2s-5s-10s	2s-5s-30s	2s-10s-30s	5s-10s-30s
Before 1-Jun	-20	-0.8	-6.1	-6.9	-8.8	-5.3	-6.1	-8.0	-0.8	-2.7	-1.9	-4.5	-2.6	-4.2	1.1
	-10	-5.9	-8.4	-8.6	-8.8	-2.5	-2.7	-2.9	-0.2	-0.4	-0.2	-2.2	-2.1	-2.5	0.0
	-5	-2.5	-4.2	-4.5	-5.4	-1.6	-1.9	-2.8	-0.3	-1.2	-0.9	-1.4	-0.5	-1.0	0.6
	-3	-3.7	-4.5	-3.8	-3.6	-0.8	-0.1	0.1	0.8	0.9	0.1	-1.6	-1.7	-0.2	0.6
After 1-Jun	-1	-2.4	-2.6	-1.7	-1.4	-0.2	0.8	1.0	1.0	1.2	0.2	-1.1	-1.4	0.5	0.7
	+1	2.6	3.2	3.3	2.7	0.6	0.6	0.1	0.0	-0.5	-0.5	0.5	1.1	1.1	0.6
	+3	3.6	4.5	5.6	5.3	0.8	2.0	1.7	1.1	0.8	-0.3	-0.3	0.0	2.3	1.4
	+5	6.9	8.8	9.3	8.4	1.9	2.4	1.5	0.5	-0.4	-0.9	1.4	2.3	3.3	1.4
	+10	8.5	7.5	6.1	4.2	-1.0	-2.4	-4.3	-1.4	-3.3	-1.9	0.4	2.3	-0.6	0.4
Success rate (%)	+20	10.7	9.9	7.0	3.3	-0.8	-3.8	-7.4	-2.9	-6.6	-3.7	2.1	5.7	-0.1	0.7
	-20	50%	79%	79%	71%	93%	79%	64%	71%	64%	50%	57%	64%	79%	57%
	-10	57%	57%	79%	79%	79%	86%	64%	57%	64%	57%	79%	57%	57%	57%
	-5	57%	64%	64%	71%	71%	57%	71%	57%	57%	57%	50%	50%	79%	57%
	+5	21%	36%	21%	21%	29%	36%	50%	50%	50%	64%	50%	36%	36%	29%
Test >	+10	29%	36%	36%	43%	57%	64%	64%	64%	71%	79%	57%	43%	43%	36%
	+20	36%	36%	43%	50%	64%	79%	71%	57%	64%	57%	43%	43%	64%	57%
	Lower yield				Flatter yield curve						Belly performance				

		GoC-UST yield differential				GoC-UST yield box						Ontario spread/credit curves			
Wk days		2-year	5-year	10-year	30-year	2s-5s	2s-10s	2s-30s	5s-10s	5s-30s	10s-30s	10-year	30-year	9s-10s	10s-30s
Before 1-Jun	-20	-0.3	-0.9	0.4	-2.1	-0.6	0.8	-1.7	1.3	-1.2	-2.5	1.6	0.4	0.1	-1.2
	-10	-3.4	-3.3	-0.2	-0.2	0.1	3.2	3.2	3.1	3.1	0.0	0.4	-0.7	0.0	-1.0
	-5	0.4	-1.2	0.3	-0.7	-1.7	-0.2	-1.1	1.5	0.6	-0.9	-0.3	-0.7	0.0	-0.4
	-3	-0.9	-1.3	0.3	0.4	-0.5	1.2	1.3	1.6	1.8	0.1	0.2	-0.2	0.1	-0.4
After 1-Jun	-1	-2.5	-2.5	-0.7	-0.2	0.0	1.8	2.4	1.7	2.3	0.6	-0.3	-0.3	0.1	-0.1
	+1	0.3	-0.5	-0.6	-1.1	-0.7	-0.9	-1.4	-0.1	-0.7	-0.6	-0.7	-0.3	0.0	0.4
	+3	2.1	1.7	1.3	-0.3	-0.4	-0.8	-2.3	-0.4	-1.9	-1.5	-0.8	-0.2	0.1	0.5
	+5	4.0	4.5	3.4	2.1	0.5	-0.6	-1.9	-1.1	-2.4	-1.3	-1.3	-0.5	0.1	0.7
	+10	2.0	2.1	1.2	0.7	0.0	-0.9	-1.4	-0.9	-1.4	-0.5	-0.3	0.5	0.1	0.8
Success rate (%)	+20	4.6	4.2	3.7	2.2	-0.4	-0.9	-2.4	-0.5	-2.0	-1.5	-1.2	0.0	0.2	1.3
	-20	29%	36%	50%	64%	64%	64%	64%	71%	79%	79%	36%	43%	29%	93%
	-10	57%	64%	50%	50%	57%	50%	50%	43%	43%	43%	43%	57%	29%	93%
	-5	57%	43%	50%	57%	57%	57%	57%	57%	57%	50%	36%	36%	50%	57%
	+5	43%	29%	29%	50%	50%	71%	64%	57%	64%	64%	50%	50%	50%	36%
Test >	+10	43%	43%	43%	50%	50%	64%	64%	57%	57%	50%	43%	29%	36%	21%
	+20	36%	57%	43%	50%	64%	57%	57%	36%	43%	57%	50%	43%	50%	21%
	Relatively tighter yield vs. US				Relatively flatter yield curve vs. US						Tighter credit spread, flatter credit curve				

Source: NBF, BBG | Note: Based on weekdays; success rates calculated over 14Y period covering 2010-23; success rates reflect the percentage of time the expected direction of trade held in pre- & post-cash period; examples of the 'a priori' direction of trade include: Canada outright = lower yield; Canada curve = flatter; Canada-US yield differential = tighter/narrower; refer to "Test" for expected direction



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