Swapnote® futures are designed to reflect the interbank swap curve, and can be traded against German Government Bond futures to gain exposure to changing market views on the relative credit pricing in the interbank and sovereign debt markets. For a given maturity date this relative credit pricing will be expressed in the yield spread between the interbank and sovereign curves.

For example, the yield spread is 0.6524%. An investor believes that this yield spread will narrow as interbank credit improves relative to German Sovereign credit. By entering into a position which profits from a rise in the lower (German Sovereign) yields and / or a fall in the higher (interbank) yields, the investor is able to express his view on relative credit pricing. This can be achieved through selling Euro Bund futures whilst simultaneously buying 10 Year € Swapnote® futures, with the proportional number of futures traded determined by their relative basis point values.

When the investor enters the trade, market values are as follows:

- 10 Year € Swapnote® price: 136.48
- 10 Year € Swapnote® bond equivalent YTM: 1.950%
- 10 Year € Swapnote® BPV: €109.17 per lot
- Bund future price: 141.83
- Bund future implied YTM: 1.307%
- Bund future BPV: €113.50 per lot

The Bund futures yield to maturity (YTM) and basis point value are derived using the cheapest to deliver (CTD) bond. In an upward sloping yield curve environment, the CTD bond typically has a shorter maturity; in the case of Bund futures shorter than ten years from the delivery date, therefore there is also an element of curve trading in this example strategy.
Here, the yield spread is \(1.950\% - 1.307\% = 0.643\%\)

The proportional number of futures to trade is \(109.17 : 113.50 = 0.96185\)

Therefore for each 100 contracts of 10 Year € Swapnote® purchased, 96 Bund futures should be sold. In practice, given the closeness of the basis point values, these trades are often transacted on a 1 for 1 basis for simplicity.

A week later, market values are as follows:

- 10 Year € Swapnote® price: 137.07
- 10 Year € Swapnote® bond equivalent YTM: 1.895%
- Bund future price: 141.52
- Bund future implied YTM: 1.354%

Here, the yield spread is \(1.895\% - 1.354\% = 0.541\%\), narrowing as predicted, as interbank yields have fallen whilst sovereign yields increased.

The return on this trade is:

- \(\text{Return} = \text{Swapnote® return} - \text{Bund return}\)
- \(\text{Return} = (100 \times (137.07 - 136.48) \times €10 / 0.01) - (96 \times (141.52 - 141.83) \times €10 / 0.01)\)
- \(\text{Return} = €88,760\)

© 2014 Intercontinental Exchange, Inc. The information and materials contained in this document—including text, graphics, links or other items—are provided "as is" and "as available." ICE and its subsidiaries do not warrant the accuracy, adequacy or completeness of this information and materials and expressly disclaim liability for errors or omissions in this information and materials. This document is provided for information purposes only and in no way constitutes investment advice or a solicitation to purchase investments or market data or otherwise engage in any investment activity. No warranty of any kind, implied, express or statutory, is given in connection with the information and materials. The information in this document is subject to change and ICE undertakes no duty to update such information. You should not rely on any information contained in this document without first checking that it is correct and up to date. The content of this document is proprietary to ICE in every respect and is protected by copyright. No part of this material may be copied, photocopied or duplicated in any form by any means or redistributed without the prior written consent of ICE. All third-party trademarks are owned by their respective owners and are used with permission.

Swapnote® is a registered trademark of ICAP plc and has been licensed for use by LIFFE. The Swapnote® contract design and algorithm are protected by patent (GB 537,946), and is exclusively licensed to LIFFE worldwide by ICAP plc. LCSD® and ICSD® are registered trademarks of LCSD S.A., a company wholly owned by ICAP plc.

Euribor® and Eonia® are registered trademarks of Euribor-FBE.

ISDA® and ISDAFIX® are registered trademarks of the International Swaps and Derivatives Association, Inc.

Trademarks of ICE and its affiliates include Intercontinental Exchange, ICE, ICE Block design, NYSE, New York Stock Exchange and LIFFE. Information regarding additional trademarks and intellectual property rights of Intercontinental Exchange, Inc. and its affiliates is located at https://www.intercontinentalexchange.com/terms-of-use

Further Information

Interest Rate Derivatives
+44 (0)20 7429 4640
rates@theice.com
theice.com/products/futures-&-options/financials/interest-rates