

## Rates Spark: Index disappointment versus AAA squeeze

ICE has decided again not to include the EU bonds in its sovereign indices, sending EU spreads wider. In the broader context EU bonds are still part of a considerable smaller AAA-universe since the last US downgrade



With strong supply, rate markets are likely to remain volatile for a while

### ICE decides against EU's sovereign index inclusion, but EU is still part of a scarce AAA-resource

While EU bonds have traded well-supported over the summer, that picture saw a sudden dent as spreads widened out on the news that the index provider ICE has again decided against the inclusion of EU bonds into its sovereign indices. The notion of course has been, that such an inclusion would have created additional structural demand from investors tracking these indices. Spreads over swaps accordingly widened by more than 2bp on the back of the disappointing news, with prospects of the next EU auction being just around the corner next week perhaps playing into the mood.

The decision by ICE is also not entirely surprising since the tangible progress on fronts such as establishing the EU as a permanent issuer remains modest. The outstanding volume of EU bonds is still set to increase next year as remaining NGEU support is disbursed, but starting in 2028 the NGEU debt will be repaid. Offsetting that 18 countries have signed up for a total of €127bn from the EU's SAFE instrument to support European defence efforts, but it is also a one-off instrument.

Last month the EU Commission's 2028-2034 proposal for the EU long-term budget does call for the creation of a permanent EU crisis mechanism with a fire power of close to €400bn and a loan facility of €150bn called "Catalyst Europe" to help member states invest in EU objectives. Another large chunk that could be funded is the financial support of Ukraine. But especially with a view to the first two instruments, they are only proposals so far and may still face pushback. And the discussions around the next EU long-term budget will likely run through 2026.

That being said we also have to acknowledge that since the US was stripped of its last AAA rating ahead of summer, the global AAA-sovereign and supranational debt segment has slimmed down considerably to just below US\$10tr, of which more than half now is in EUR. Any investor explicitly seeking AAA-exposure will not get around the German debt market of €2.25tr, the most liquid AAA debt available, and the next largest AAA segment which is the EUR-denominated supranational issuer segment of around €1tn, which of course is dominated by the EU with an outstanding of €0.66tr.

## Wednesday's events and market views

The UK CPI numbers in the morning will be watched closely as gilt yields have risen more than peers over the past days. Consensus sees the services year-on-year number tick up from 4.7% to 4.8%, still too hot for the Bank of England's liking. From the US we'll receive the minutes from July's FOMC meeting. Given the fierce ongoing debate about rate cuts every word will be weighed. The question is whether it will contain anything new.

In terms of issuance we have a syndication from Finland for a new 7Y RFGB at an estimated €4bn. Germany will auction 21Y and 29Y Bunds totalling €2.5bn. From the US we will have a 20Y Bond auction for \$16bn.

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