



Blame [Bank of] Canada

By Warren Lovely & Taylor Schleich

Maybe it's our latent inferiority complex, but Canadians love it when Americans pay attention to us. Consider the perverse pride many took from the satirical 'Blame Canada' movement popularized by the wholly fictional South Park series. Well, fair to say American bond traders have been paying attention to Canada in recent sessions.

The GoC bond market got a violent, central bank-induced jolt this week. It wasn't so much Wednesday's Bank of Canada's decision—a second straight 50 bp hike that had been fully expected—that rattled traders. Rather, it was the decidedly tough talk in the statement, as the Bank's shone a klieg light on faster-than-expected and yet-to-peak inflation. Follow-on remarks from BoC's Paul Beaudry have done little to settle nerves, as the DepGov kept a 75 bp hike on the table and raised the prospect of a >3% overnight rate. Whether you blame the Bank of Canada or not, the resulting sell-off snuffed out many seasonal trading dreams. We're talking about the much-hyped (although all-too-unpredictable) market tendencies in/around Canada's enormous June 1st/2nd cashflows.

It's only June 2nd and the bond market cash is still flowing. As we've [detailed](#), additional lumpy cashflows are teed up for mid-month too. In other words, some may be reluctant to throw in the towel on their technical/seasonal bets. Taken to the extreme, some might view the rates selloff and Canada underperformance as an opportunity to re-load and/or re-establish fresh longs. We're not necessarily sold on that strategy. We've always been hesitant to place blind faith in seasonals and this June 1st/2nd (complete with its hawkish BoC communiqués) may serve as a painful lesson to some, reinforcing a long-standing warning that 'all else is not always equal'.

Table 1: A qualitative take on how the June 1st seasonal trading strategy has gone so far (in some cases, not well at all)

June 1st/2nd seasonal/technical trading strategies: Null hypothesis vs. 2022 experience

| Category | Null hypothesis | 2022 experience* | Comment |
|--------------------------------|--------------------|------------------|--|
| GoC outright yield | Lower | No! | Canadas got smashed by the BoC on 1-Jun & Beaudry did no favours today; pressure has been most acute in 2s & 5s, where yields have jumped ~30 bps vs. T-5; so much for the rally often observed going into June cash (Chart 1) |
| GoC-UST yield differential | Relatively tighter | No! | Seasonal devotees prep for GoC outperformance vs. USTs, with historical success rates not terrible in the lead-up to 1-Jun (Chart 2); but as we've cautioned, having a BoC decision on 1-Jun was a massive wildcard; Canadas have puked vs. USTs, particularly in 2s & 5s, with index adjustments & related demand limiting damage in the long end |
| GoC yield curve | Flatter | Yes | A flattener was the a-priori bias & at least here recent moves jive with empirical tendencies; if anything, an already flat Canada curve has moved even flatter, 5s30s having joined 10s30s in inverted territory (Chart 3); 2s10s still has a bit of slope, but a more aggressive BoC raises risks a housing meltdown so beware! |
| GoC-UST box | Relatively flatter | Yes | Pick your box... we've observed a notable richening (i.e., out-flattening) of GoC vs. UST, a movement thrown into overdrive by BoC re-pricing; of note, the 10s30s box is sitting at the richest levels since last spring, with 20D to 50D Z-scores around -2½ SDs; looking for a June cashflow effect, start here |
| Provincial spread/credit curve | Tighter/flatter | Yes | Provi credit has done relatively well, Ontario 10s tightening a net 5 bps vs. T-5 levels & longs doing even better (i.e., flatter credit curve) (Chart 4); despite new issue supply, provis have outperformed corp credit benchmarks in recent sessions; eyes now shift to the Ontario general election (2-Jun), although a status quo result seems likely |

Source: NBF, Bloomberg

Table 2: Detailing this year's performance

Observed move (net) in GoC interest rates (yields, curves, butterflies, vs. UST) & provincial credit in days before/after 1-Jun-2022

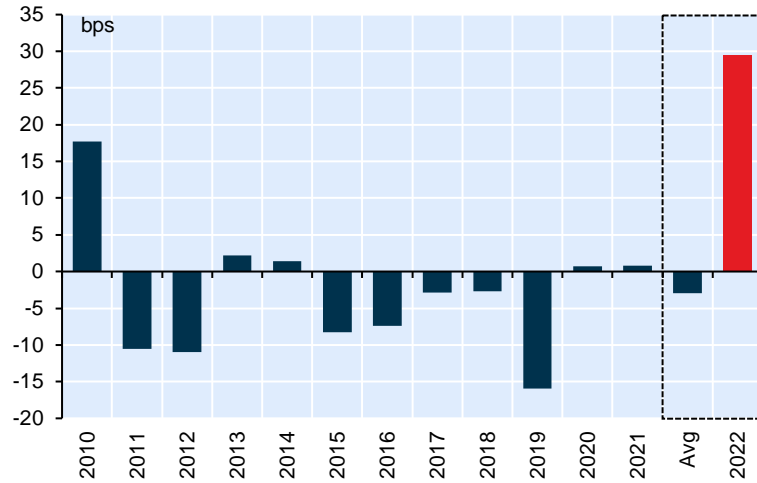
| | | Canada Outright | | | | Canada Curves | | | | | | Canada Flies | | | |
|----------------|-----|-----------------|--------|---------|---------|---------------------|--------|--------|--------|--------|---------|-------------------|-----------|------------|------------|
| | | 2-year | 5-year | 10-year | 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 |
| Days vs. 1-Jun | -20 | 17.4 | 10.5 | 5.4 | 0.1 | -6.9 | -12.0 | -17.3 | -5.1 | -10.4 | -5.3 | -1.8 | 3.5 | -6.7 | 0.2 |
| | -10 | 3.5 | 3.2 | 3.1 | -4.1 | -0.3 | -0.4 | -7.6 | -0.1 | -7.3 | -7.2 | -0.2 | 7.0 | 6.8 | 7.1 |
| | -5 | 24.9 | 23.7 | 20.2 | 10.0 | -1.2 | -4.7 | -14.9 | -3.5 | -13.7 | -10.2 | 2.3 | 12.5 | 5.5 | 6.7 |
| | -3 | 23.9 | 23.3 | 18.7 | 8.6 | -0.6 | -5.2 | -15.3 | -4.6 | -14.7 | -10.1 | 4.0 | 14.1 | 4.9 | 5.5 |
| | -1 | 12.9 | 12.9 | 8.5 | 2.7 | 0.0 | -4.4 | -10.2 | -4.4 | -10.2 | -5.8 | 4.4 | 10.2 | 1.4 | 1.4 |
| | +1 | 4.6 | 6.2 | 4.7 | 2.7 | 1.6 | 0.1 | -1.9 | -1.5 | -3.5 | -2.0 | 3.1 | 5.1 | 2.1 | 0.5 |
| Test | | Lower yield | | | | Flatter yield curve | | | | | | Belly performance | | | |

| | | Canada-US Differential | | | | Canada-US Boxes | | | | | | Ontario spread/credit curves* | | | |
|----------------|-----|---------------------------------|--------|---------|---------|---------------------------------------|--------|--------|--------|--------|---------|--|---------|---------|---------|
| | | 2-year | 5-year | 10-year | 30-year | 2s-5s | 2s-10s | 2s-30s | 5s-10s | 5s-30s | 10s-30s | 5-year | 10-year | 30-year | 10s-30s |
| Days vs. 1-Jun | -20 | 17.3 | 10.2 | 8.2 | -2.1 | -7.1 | -9.1 | -19.4 | -2.0 | -12.3 | -10.3 | 1.0 | 0.0 | -0.5 | -0.5 |
| | -10 | 6.0 | 0.8 | 0.9 | -3.4 | -5.2 | -5.1 | -9.4 | 0.1 | -4.2 | -4.3 | 0.0 | -1.5 | -2.0 | -0.5 |
| | -5 | 9.8 | 4.1 | 4.0 | 1.2 | -5.7 | -5.8 | -8.6 | -0.1 | -2.9 | -2.8 | -3.5 | -4.5 | -5.0 | -0.5 |
| | -3 | 7.1 | 3.4 | 1.8 | -0.7 | -3.7 | -5.3 | -7.8 | -1.6 | -4.1 | -2.5 | -1.5 | -1.0 | -1.5 | -0.5 |
| | -1 | 4.2 | 3.2 | 2.3 | 1.5 | -1.0 | -1.9 | -2.7 | -0.9 | -1.7 | -0.8 | -0.5 | -0.5 | -1.0 | -0.5 |
| | +1 | 4.3 | 5.9 | 3.5 | -0.1 | 1.6 | -0.8 | -4.4 | -2.4 | -6.0 | -3.6 | -0.5 | -0.5 | -1.0 | -0.5 |
| Test | | Relatively tighter yield vs. US | | | | Relatively flatter yield curve vs. US | | | | | | Tigher credit spread, flatter credit curve | | | |

Source: NBF, Bloomberg | Note: Net changes are relative to 1-Jun closes; changes up to 1-Jun are actuals, whereas T+1 rate/yield changes are as of 2-Jun @ 12:30 ET; Ontario spread/credit curves are based on NBF's constant maturity spreads vs. GoC curve

Chart 1: Now that's a sell off

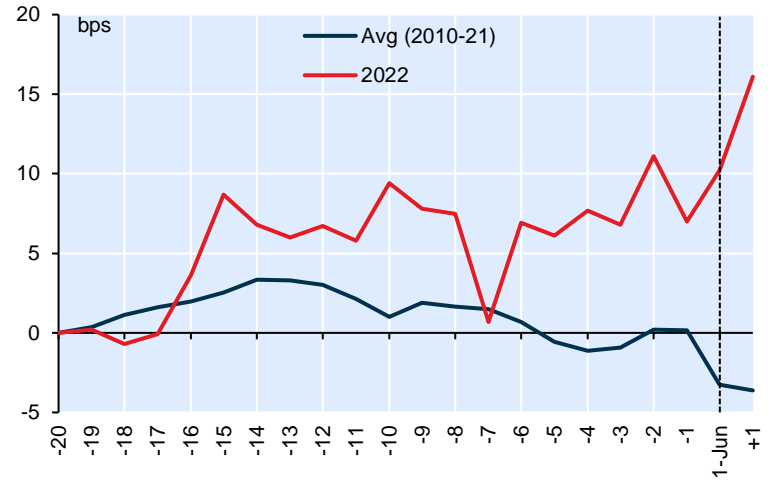
Net change in GoC 2Y yields: 6D to 2-Jun



Source: NBF, Bloomberg | Note: T-5 to T+1 vs. 1-Jun; 2022 as at 2-Jun @ 12:30 ET

Chart 2: Canada outperformance? Sorry, not this year

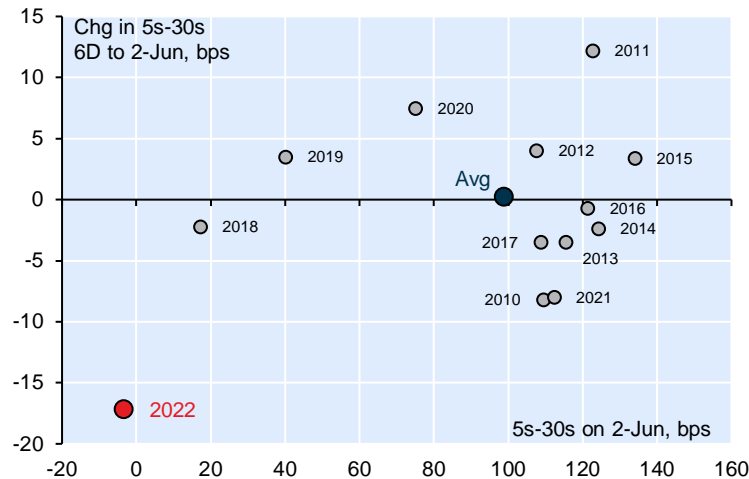
Cumulative change in GoC-UST 5Y differential relative to 20D prior to 1-Jun



Source: NBF, Bloomberg | Note: 2022 as at 2-Jun @ 12:30 ET

Chart 3: A flat curve gets flatter still

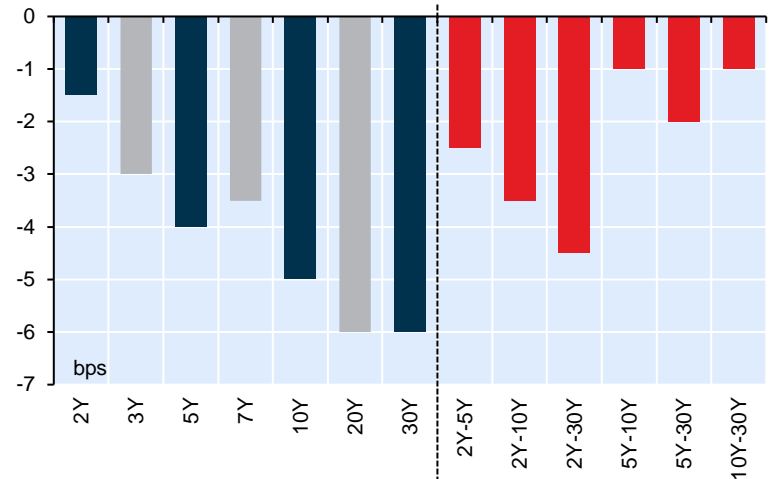
Net change & prevailing level for GoC 5s-30s yield curve to 2-Jun



Source: NBF, Bloomberg | Note: T-5 to T+1 vs. 1-Jun; 2022 as at 2-Jun @ 12:30 ET

Chart 4: Provi credit snugs up (recovering some earlier weakness)

Net change in Ontario spreads & credit curves: 6D to 2-Jun



Source: NBF | Note: Based on constant maturity indications; T-5 to T+1 vs. 1-Jun



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