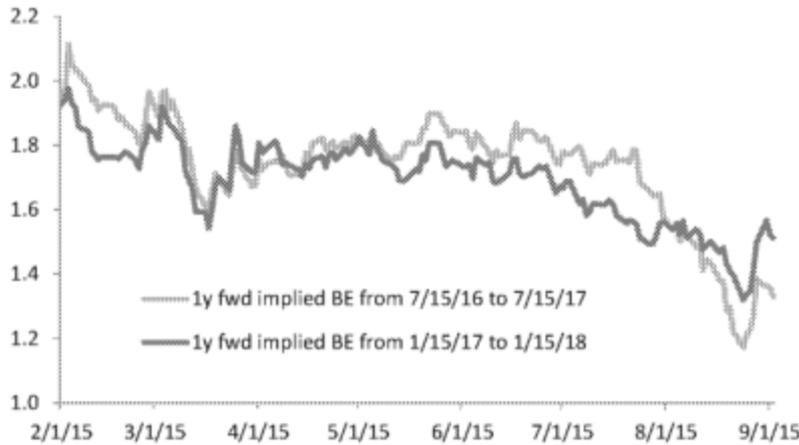




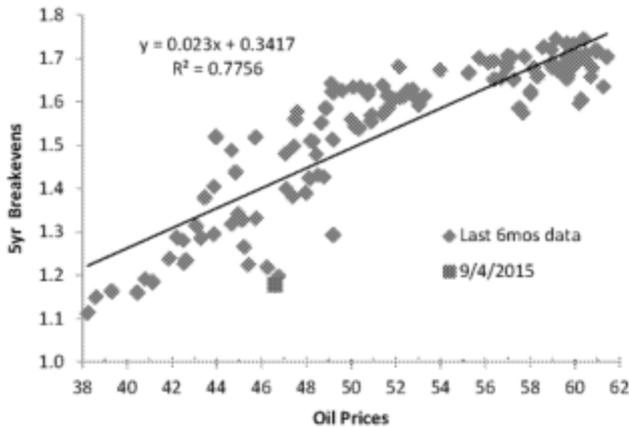
Long forward breakevens, either outright or hedged with energy futures



Source: Bloomberg Finance LP and Deutsche Bank

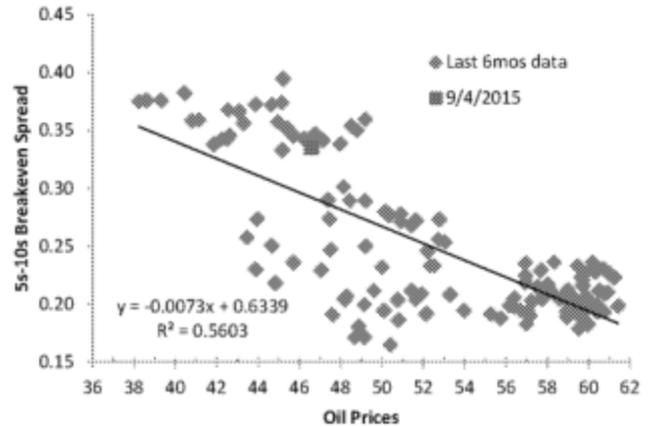
A simpler version of the implied front end forward breakevens is to be long front end breakevens outright. They have lagged oil prices. A regression of five-year TIPS breakevens against oil prices on past six months' data suggests breakevens are too low by 15bp to 20bp, given the current oil prices. Similarly, 5s/10s breakeven curve appears too steep and have room to flatten relative to oil prices. So the weakness in front end breakevens appears to be more than a function of energy prices. Dealer positions in TIPS maturing in less than or equal to 2 years are at a record high.

Front end TIPS breakevens have lagged oil prices



Source: Bloomberg and Deutsche Bank

5s/10s breakeven curve appears to have room to flatten



Source: Bloomberg and Deutsche Bank

5-year inflation basis has recovered, while 30-year inflation basis has done less well, and remains in the low end of the long term trading range. The 5-year inflation basis traded as low as +13bp in April and has bounced to about +25bp lately. The 30-year inflation basis currently trades about +25bp as well, having widened from about +18bp in late May. Over the past one year, the spread between the two basis spread has averaged around +6bp. Investors should consider inflation basis steepeners by being long 30-year inflation basis against 5-year inflation basis.