



United States

Rates
 Gov. Bonds & Swaps
 Credit
 Sovereigns

Steven Zeng, CFA
 Research Analyst



Agencies

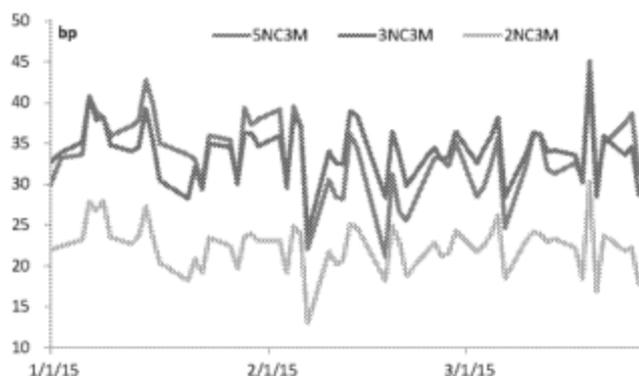
- As volatility has recently declined, yield picks for callables have also fallen. We find the 5yr+ maturities relatively protected with the smallest decrease in picks compared to the recent average.
- The additional yield for buying Berm vs. Euro call has increased. We like the 3NC3M Berm structure, which offers 10.7 bps over a 3NC3M Euro, the highest in a year.

Relative value in callables

Pick in yields for callable agencies over same-maturity bullets has fallen slightly over the past three months. For callable investors, we recommend extending out to 5yr maturities as the picks for various structures still look decent to their recent average. For example, a 5NC3M Berm has a new issue coupon of around 1.91%, a 31.4 bps pick over a par 5y agency. The pick is only about 2 bps lower than its 3m average, whereas for 2NC3M Berm and 3NC3M Berm, the picks are 4 bps and 5 bps lower, respectively.

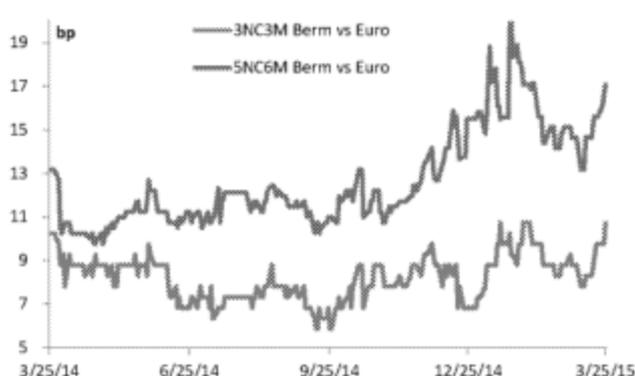
The best relative value play in callables seems to be in Euro vs. Berm switch. For a 3NC3M structure, buying the Berm vs. Euro offers the investor an additional 10.7 bps, the highest in a year. A 5NC6M structure also looks attractive on a 1m Z metric.

Yield picks for callables over same-maturity bullets



Source: Deutsche Bank

Berms vs. Euro calls history



Source: Deutsche Bank

The left table below shows new issue coupons, picks to bullet, and Berms vs. Euros, along with their respective 1m and 3m averages and z-scores. The table on the right shows the 3m z-score for the swaption implied volatility surface. The recent cheapening of vols was mostly concentrated in the upper left.