Inflation-linked Focus

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Inflation swaps & breakevens vs spreads widening

- **Inflation swaps and breakevens are overall driven by three factors: energy prices, realised inflation and market sentiment. Energy is currently a neutral-to-slightly-negative factor, while inflation is expected to rise further (headline above 4% YoY, core near 3% in Q127). The main concern to be long inflation, however, is deteriorating market sentiment driven by the ongoing Eurozone sovereign spread widening.**
- **Spread widening historically hurts inflation swaps and breakevens. Analysing 14 episodes since 2010 where the "Big 3 - Bund spread" (a weighted average of OAT, BTP and Bonos vs Bund) widened by 30bp or more, the 10Y HICPx inflation swap declined in 12 out of 14 cases after adjusting for the concurrent drop in crude oil prices that typically accompanies spread stress.**
- **The relationship is non-linear and hard to quantify precisely. The R^2 between spread widening and HICPx moves is close to zero, meaning the magnitude of the inflation sell-off is unpredictable. A rough estimate suggests that an additional 40bp of spread widening – itself a scenario implying severe further financial stress – would translate into only a 5-7bp decline in the 10Y HICPx, all else equal.**
- **Cash breakevens are more vulnerable than inflation swaps in a severe crisis. During the worst spread widening episode (November 2011), the 10Y OATei breakeven fell 45bp vs only 10bp for the 10Y HICPx swap, reflecting forced liquidation of inflation-linked bonds. Outside of a full-blown debt crisis, however, iotas (the inflation swap-breakeven spread) have historically shown very little sensitivity to spread widening – averaging just 1bp of widening across non-crisis episodes.**
- **Given the elevated risk of further spread widening over the next three months and its likely negative impact on inflation products, we closed this morning our 5Y HICPx and 3YF2Y HICPx forwards recommendation, posting a small loss.**
- **You can check out our Inflation swaps and breakevens, real yield SA, breakeven SA database and tools at Red Mount Analytics / My daily report / Eurozone & French inflation market monitor.**



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Inflation swaps and breakevens vs spreads widening

What if spreads continue to sell off?

Generally speaking, inflation swaps and breakevens benefit from (1) higher energy prices, (2) higher inflation numbers and (3) improving market sentiment. Conversely, inflation swaps and breakevens decline when these drivers go the opposite way.

1. **Energy** has been – to say the least – erratic in recent months. As usual, we do not forecast energy prices and rely on futures for our inflation forecasts. From this perspective, energy prices are a neutral (actually slightly negative) factor to being long inflation on a – say – six-month perspective.
2. We expect reported **inflation** to continue to rise in Q426 and Q127, with headline soon passing 4% YoY and core approaching 3% in Q127. Expecting this is one thing, seeing it is another. Higher realised core inflation should gradually push inflation forwards higher going into Q127 (**all else equal**), mirroring the situation of 2018-19, **when never-ending weak core inflation took the 5YF5Y from 1.6% to around 1.1%.**
3. **Market sentiment** is the focus of this inflation document, against the backdrop of the ongoing **sovereign spread sell-off in the Eurozone**. **Today we are trying to quantify how much inflation swaps and breakevens would suffer should spreads continue to sell off.**

Case 1: 10Y HICPx swap vs spread widening

We define the "Big 3 – Bund spread" as an arbitrary weighted average yield (40% 10Y OAT, 40% BTP, 20% Bonos) spread vs the 10Y Bund. The weights roughly mirror the size of the government debt for the big three issuers ex-Germany (France, Italy, Spain).

Since early 2010, this spread has evolved between 50bp and 375bp. The spread was at 50bp in January 2010 (before the great Eurozone debt crisis) and in early 2026 (thanks to the tightening of Spanish and Italian spreads). See Figure 1.

Fig 1. Big 3 – Bund spread, vs 10Y HICPx inflation swap



Source: Crédit Agricole CIB, Bloomberg

Between 2010 and today, we retain 14 episodes when the spread materially widened relatively quickly, ie, by 30bp or more within – generally – a couple of months. See Figure 2 for these samples. We did not retain the immediate aftermath of the Russian invasion of Ukraine, when natural gas prices were multiplied by almost five at some point. Of course we are aware that we may be comparing apples with oranges: the inflation regimes, the central bank cycles, the fiscal pictures were all different. We are only trying to find a more detailed argument than "inflation swaps and breakeven would likely suffer if there is more financial stress".

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Fig 2. Past moves in the 10Y HICPx during spread widening episodes, adjusted for the sensitivity to crude oil

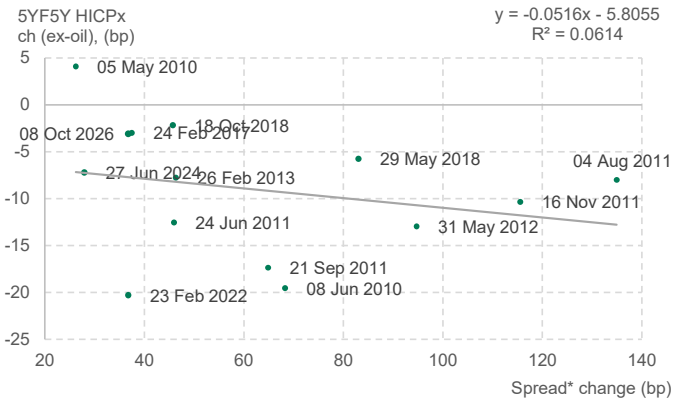
1	2	3	4	5	6	7	8	9	10	11	12	13
		Big 3 - Bund spread (bp)			10Y HICPx (bp)			Brent 3rd contract (USD/bl)			10Y HICPx (bp)	
start	end	start	end	change	start	end	change	start	end	change	Oil sensi 0.98 bp per USD	change ex-oil
14 Apr 2010	05 May 2010	60	86	26	217	215	-2	87	85	-3	-3	1
13 May 2010	08 Jun 2010	67	135	68	218	195	-23	82	74	-9	-9	-15
16 May 2011	24 Jun 2011	115	161	46	232	208	-24	110	106	-5	-5	-19
01 Jul 2011	04 Aug 2011	135	270	135	224	215	-9	112	107	-5	-4	-4
31 Aug 2011	21 Sep 2011	201	266	65	201	184	-18	114	108	-6	-5	-12
28 Oct 2011	16 Nov 2011	260	375	116	202	190	-12	109	111	2	2	-14
02 Apr 2012	31 May 2012	247	341	95	214	182	-32	124	101	-23	-23	-10
31 Jan 2013	26 Feb 2013	198	245	46	204	197	-7	114	111	-3	-3	-4
13 Jan 2017	24 Feb 2017	103	140	37	148	148	0	56	57	0	0	0
14 May 2018	29 May 2018	76	159	83	161	156	-6	78	75	-2	-2	-3
27 Sep 2018	18 Oct 2018	127	172	46	159	156	-3	81	79	-2	-2	-1
08 Nov 2021	23 Feb 2022	73	109	37	202	211	9	81	92	11	11	-2
31 May 2024	27 Jun 2024	86	114	28	227	222	-4	81	84	4	3	-8
08 Sep 2026	08 Oct 2026	76	113	37	229	229	0	91	98	7	7	-7

Source: Crédit Agricole CIB, Bloomberg

In those 14 episodes, the 10Y HICPx inflation swap declined 11 times (column 8 in Figure 2). The spread widening episode coincided with falling crude oil prices 9 out of 14 times (column 11). Considering the importance of crude oil to inflation products, we decided to also calculate the change in 10Y HICPx swap net of the effect of the decline in crude oil (columns 12 and 13). The HICPx swap – oil-adjusted – declined 12 out of 14 times in the spread widening episodes. See the third bullet point below for details on this oil adjustment. We plot the changes in the 10Y HICPx inflation swap (adjusted for the move in crude oil prices) vs the spread widening in Figure 3. Our remarks:

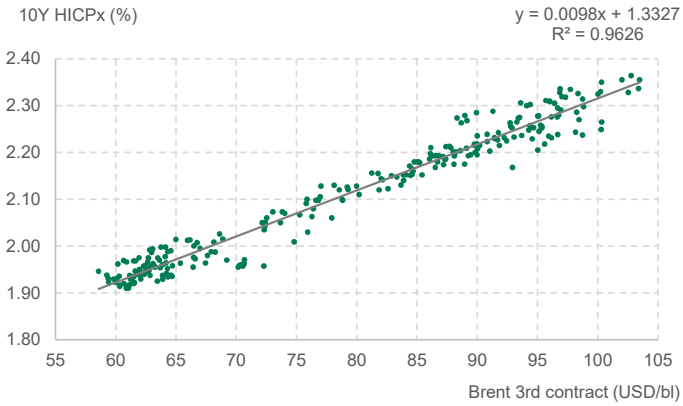
- Taking the example of the 8 September to 8 October 2026 spread widening, the 10Y HICPx was unchanged, but the oil move (+USD7/bl) would have suggested +7bp in the HICPx . **Hence, our estimated -7bp move in the oil-adjusted 10Y HICPx**. We did not adjust for the 3bp monthly roll in the 10Y HICPx, which occurred on 1 October.
- There was almost always a decline in the 10Y HICPx (Figure 2), confirming the general rule at the beginning of page 2.
- R^2 is close to zero, evidencing a non-linear relationship (we learned something today). For example from 1 July 2011 to 4 August 2011, there was a massive 135bp spread widening (3.6 x the one we experienced last month) which only led to a 4bp decline – once oil adjusted – in the 10Y inflation swap.
- When making the oil adjustment (columns 12-13), we assume a sensitivity of the 10Y HICPx vs of 0.98bp per USD1/bl change in crude oil price, based on the regression over the past year (Figure 4). A regression over 15 years would have made more sense as the sensitivity may have changed since 2010, but we opted for last year as this was one of the purest energy shocks in decades.

Fig 3. 10Y HICPx move vs the spread* change, adjusted for crude oil. The dates refer to the end of episodes



*Source: Crédit Agricole CIB. *spread is the Big 3 vs Bund spread defined in page 2*

Fig 4. 10Y HICPx: sensitivity vs crude oil price, calculated over the last 12 months



Source: Crédit Agricole CIB, Bloomberg

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Let's try to conclude. What could be the decline in the 10Y HICPx, should there be – say – 40bp more spread widening, in an unchanged crude oil price scenario? **We would expect around a 5-7bp decline** all-else equal considering (1) the weakness of the regression in Figure 3; and (2) what happened over the last month (10Y HICPx stability despite a theoretical +7bp effect from the rising crude oil price).

Bear in mind that around 40bp of additional spread widening (of our 40% BTP-Bund, 40% OAT-Bund, 20% Bonos-Bund average spread) **would be a very serious deepening of the current financial stress.**

Case 2: the 5YF5Y HICPx swap forward vs spread widening

We share the same tables and charts below:

Fig 5. Past moves in the 5YF5Y HICPx during spread widening episodes, adjusted for the sensitivity to crude oil

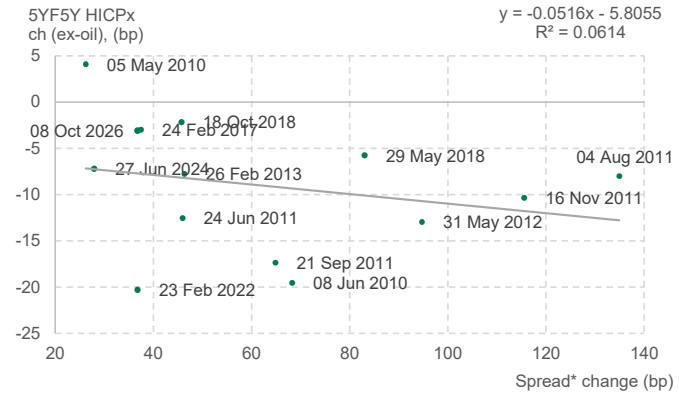
1	2	3	4	5	6	7	8	9	10	11	12	13
		Big 3 - Bund spread (bp)			5YF5Y HICPx (bp)			Brent 3rd contract (USD/bl)			5YF5Y HICPx (bp)	
start	end	start	end	change	start	end	change	start	end	change	Oil sensi 0.24 bp per USD	change ex-oil
14 Apr 2010	05 May 2010	60	86	26	241	245	3	87	85	-3	-1	4
13 May 2010	08 Jun 2010	67	135	68	252	230	-22	82	74	-9	-2	-20
16 May 2011	24 Jun 2011	115	161	46	243	229	-14	110	106	-5	-1	-13
01 Jul 2011	04 Aug 2011	135	270	135	245	236	-9	112	107	-5	-1	-8
31 Aug 2011	21 Sep 2011	201	266	65	220	202	-19	114	108	-6	-1	-17
28 Oct 2011	16 Nov 2011	260	375	116	215	205	-10	109	111	2	1	-10
02 Apr 2012	31 May 2012	247	341	95	234	215	-19	124	101	-23	-6	-13
31 Jan 2013	26 Feb 2013	198	245	46	234	226	-8	114	111	-3	-1	-8
13 Jan 2017	24 Feb 2017	103	140	37	174	171	-3	56	57	0	0	-3
14 May 2018	29 May 2018	76	159	83	173	166	-6	78	75	-2	-1	-6
27 Sep 2018	18 Oct 2018	127	172	46	171	168	-3	81	79	-2	-1	-2
08 Nov 2021	23 Feb 2022	73	109	37	198	180	-18	81	92	11	3	-20
31 May 2024	27 Jun 2024	86	114	28	236	230	-6	81	84	4	1	-7
08 Sep 2026	08 Oct 2026	76	113	37	217	215	-1	91	98	7	2	-3

Source: Crédit Agricole CIB, Bloomberg

The conclusion is relatively similar:

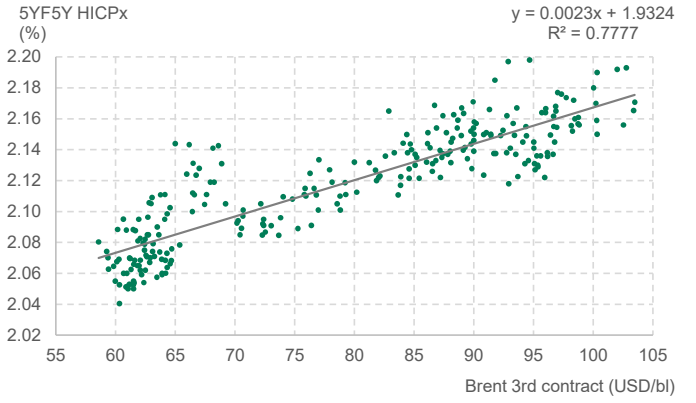
- In the 14 episodes, 13 declines in the 5YF5Y HICPx (whether adjusted for oil or not).
- A very low R^2 in the relationship between spread widening and 5YF5Y HICPx decline.

Fig 6. 5YF5Y HICPx move vs the spread* change, adjusted for crude oil



*Source: Crédit Agricole CIB. *spread is the Big 3 vs Bund spread defined in page 2*

Fig 7. 5YF5Y HICPx: sensitivity vs crude oil price, calculated over last 12 months



Source: Crédit Agricole CIB, Bloomberg

In the current spread widening episode, the decline of the 5YF5Y HICPx (adjusted for Brent crude oil) has been fairly limited: so far -3bp.

Case 3: the 10Y OATei breakeven SA vs spread widening

In our last case, we apply the same framework to our 10Y constant maturity OATei breakeven SA which we already used in the past in our fast-moving fair-value model. See results below:

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Fig 8. Past moves in the 10Y OATei breakeven SA during spread widening episodes, adjusted for the sensitivity to crude oil

1	2	3	4	5	6	7	8	9	10	11	12	13
		Big 3 - Bund spread (bp)			10Y OATei B/E SA (bp)			Brent 3rd contract (USD/bl)			10Y OATei B/E SA (bp)	
		start	end	change	start	end	change	start	end	change	Oil sensi 1.01 bp per USD	change ex-oil
14 Apr 2010	05 May 2010	60	86	26	#N/A	#N/A	#N/A	87	85	-3	-3	#N/A
13 May 2010	08 Jun 2010	67	135	68	#N/A	#N/A	#N/A	82	74	-9	-9	#N/A
16 May 2011	24 Jun 2011	115	161	46	220	197	-23	110	106	-5	-5	-18
01 Jul 2011	04 Aug 2011	135	270	135	215	205	-10	112	107	-5	-5	-5
31 Aug 2011	21 Sep 2011	201	266	65	183	165	-18	114	108	-6	-6	-12
28 Oct 2011	16 Nov 2011	260	375	116	188	145	-42	109	111	2	2	-45
02 Apr 2012	31 May 2012	247	341	95	180	142	-38	124	101	-23	-23	-14
31 Jan 2013	26 Feb 2013	198	245	46	190	177	-12	114	111	-3	-3	-10
13 Jan 2017	24 Feb 2017	103	140	37	134	134	0	56	57	0	0	0
14 May 2018	29 May 2018	76	159	83	149	144	-5	78	75	-2	-2	-3
27 Sep 2018	18 Oct 2018	127	172	46	148	147	-1	81	79	-2	-2	1
08 Nov 2021	23 Feb 2022	73	109	37	184	188	4	81	92	11	11	-7
31 May 2024	27 Jun 2024	86	114	28	219	218	-1	81	84	4	4	-5
08 Sep 2026	08 Oct 2026	76	113	37	228	225	-3	91	98	7	7	-10

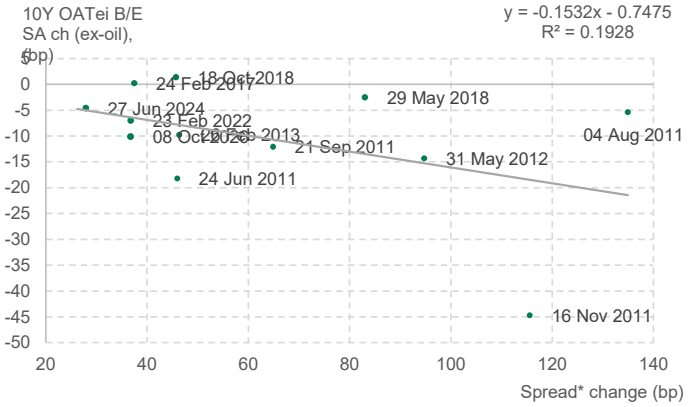
Source: Crédit Agricole CIB, Bloomberg

The results are not very different from the 10Y HICPx analysis, with one notable exception.

In the 28 October to 16 November 2011 episode, which was **the worst from a spread widening perspective**, the 10Y OATei breakeven SA dived by 42bp, and even 45bp adjusting for the slightly increasing oil price.

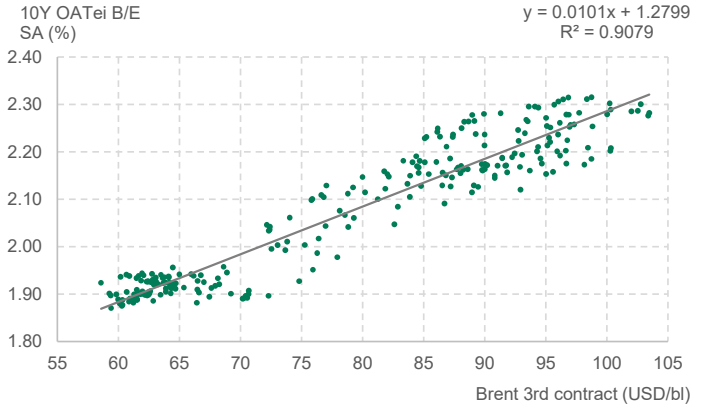
This has to be compared with the 'only' 10bp decline in the 10Y HICPx at the time. Simply put, the OATei (and other cash breakevens) suffered from liquidation at the time, hence the 30bp or so underperformance vs inflation swaps.

Fig 9. 10Y OATei breakeven SA move vs the spread* change, adjusted for crude oil



*Source: Crédit Agricole CIB. *spread is the Big 3 vs Bund spread defined in page 2*

Fig 10. 10Y OATei breakeven SA: sensitivity vs crude oil price, calculated over the last 12 months



Source: Crédit Agricole CIB, Bloomberg

The difference between an inflation swap and a seasonally adjusted breakeven (of an inflation-linked bond of similar maturity) is a DeltaZspread (also called iota). **Should there be a similar debt crisis as in November 2011, most iotas – ie, OATei, BTPei, Bonosei, even Bundei – would likely suffer.**

Since you may be wondering, here is the table for the 10Y OATei (constant maturity) iota. We actually use the simplified iota proxy, ie, the difference between 10Y inflation swap and 10Y SA constant maturity OATei breakeven.

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Fig 11. Past moves in the 10Y OATei iota, during spread widening episodes

		Big 3 - Bund spread (bp)			10Y OATei iota (bp)		
		start	end	change	start	end	change
15 Apr 2010	06 May 2010	60	106	46	#N/A	#N/A	#N/A
13 May 2010	08 Jun 2010	67	135	68	#N/A	#N/A	#N/A
16 May 2011	24 Jun 2011	115	161	46	12	11	-1
01 Jul 2011	04 Aug 2011	135	270	135	9	10	1
31 Aug 2011	21 Sep 2011	201	266	65	19	19	0
28 Oct 2011	16 Nov 2011	260	375	116	14	44	30
02 Apr 2012	31 May 2012	247	341	95	35	40	5
31 Jan 2013	26 Feb 2013	198	245	46	14	19	5
13 Jan 2017	24 Feb 2017	103	140	37	14	14	0
14 May 2018	29 May 2018	76	159	83	12	11	-1
27 Sep 2018	18 Oct 2018	127	172	46	11	9	-2
08 Nov 2021	23 Feb 2022	73	109	37	18	23	5
31 May 2024	27 Jun 2024	86	114	28	8	4	-4
08 Sep 2026	08 Oct 2026	76	113	37	1	3	3

Source: Crédit Agricole CIB

As mentioned above, the November 2011 episode – when the Italian and Spanish spread approached 500bp with the French one close to 200bp – led to around 30bp of widening in the iota. However, the other spread widening episodes did not lead to a material iota widening: 1bp on average. Before conducting this analysis, we had not expected such a muted effect.

Bottom line, unless we assume a full debt crisis 2.0, there may not be that much juice in shorting iotas… if history is any guide.

Practical conclusions

On our end, we were long 5Y HICPx and long 3YF2Y HICPx forward. Considering the significant risk of spread widening within the coming three months (with likely negative consequence on market sentiment and in turn on inflation swaps), we preferred closing these trade recommendations earlier today, in turn booking a small loss.

Fig 12. Our inflation trade recommendations so far this year

	Opening	time (CET)	Inflation trade idea	Entry (bp)	Current (bp)	Carry (bp) *	P&L (bp) **	Target (bp) ***	Stop (bp) ***	Open/ closed	Closing	Author
X - curve	15-Sep-26	09:50	Sell 5YF5Y HICPx vs 5YF5Y FRCPIx (Livret A) Probably higher Livret A rate and ceiling from early 2027	2.9	7.4	-0.4	4.1	15	-8	Open	-	Perrin / Loise
EUR RV	01-Jun-26	10:44	Sell OATei Jul-47 breakeven vs BTPei Feb-46 BTPei breakeven cheapness vs OATei no longer justified, less BTPei Feb-46 supply ahead	25.9	23.6	2.7	5.0	10	-6	Open	-	Perrin / Loise
Directional	11-Sep-26	15:08	Buy 3YF2Y HICPx	211.5	209.5	-2.9	-4.9	12	-8	Closed	09-Oct-26	Perrin / Loise
Directional	25-Aug-26	09:30	Buy 5Y HICPx	224.0	240.3	-15.9	0.4	20	-12	Closed	09-Oct-26	Perrin / Loise
Curve	15-May-26	10:45	Sell 5YF5Y HICPx vs buy 10YF20Y	21.7	26.6	0.7	5.6	10	-6	Closed	14-Sep-26	Perrin / Loise
EUR RV	22-Jun-26	11:46	Sell OATei Jul-36 (RY) vs BPTei	19.4	8.0	1.3	12.7	12	-8	Closed	19-Aug-26	Perrin / Loise
X - curve	11-May-26	16:16	Sell 5YF5Y FRCPIx vs buy HICPx	5.0	-0.2	0.6	5.8	8	-6	Closed	17-Jun-26	Perrin / Loise
EUR RV	08-Apr-26	09:40	Sell BTPei May-30 vs BTPei Aug-31	21.5	15.5	-10.9	-4.9	12	-8	Closed	09-Jun-26	Perrin / Loise
Fixings	09-Apr-26	10:34	Buy FRCPIx May-26 fixing with oil hedge	198.0	261.0	-33.0	30.0	20	-10	Closed	30-Apr-26	Perrin / Loise
Directional	13-Mar-26	11:56	Buy 5Y HICPx with oil hedge	232.6	223.3	6.7	-2.6	20	-15	Closed	08-Apr-26	Perrin / Loise
Directional	05-Feb-26	16:24	Sell 3YF2Y FRCPIx	175.2	193.9	8.7	-10.0	20	-10	Closed	09-Mar-26	Perrin / Loise
X - curve	17-Jun-25	11:34	Sell OATi Mar-36 vs OATei Jul-36	-1.3	-28.9	6.2	33.8	40	20	Closed	09-Mar-26	Perrin / Loise
Directional	28-Jan-26	14:25	Sell 2Y HICPx	181.6	201.0	9.4	-10.0	15	-10	Closed	03-Mar-26	Perrin / Loise
Directional	27-Nov-25	15:31	Buy BTPei May-36 breakeven	174.1	185.5	-6.2	5.2	15	-10	Closed	28-Jan-26	Perrin / Loise
EUR RV	13-Oct-25	15:26	Sell 10Y OATei (RY) vs Bonosei and BTPei	-3.4	5.6	0.0	9.0	12	-8	Closed	19-Jan-26	Perrin / Loise

Market values as at 09/10/2026 13:41 CET

*Carry = inflation & interest rates carry + roll down (swaps) + oil hedge
** P&L = Current level vs entry + carry
*** Targets and stops refer to the P&L of the trade, not levels

	Number of trades	Hit ratio	P&L
2026:	15	67%	79
2025:	16	81%	254
2024 (H2):	8	63%	70
2022 (H1):	11	82%	165
2021:	25	68%	219
2020:	28	82%	219
2019:	21	76%	182

Source: Crédit Agricole CIB

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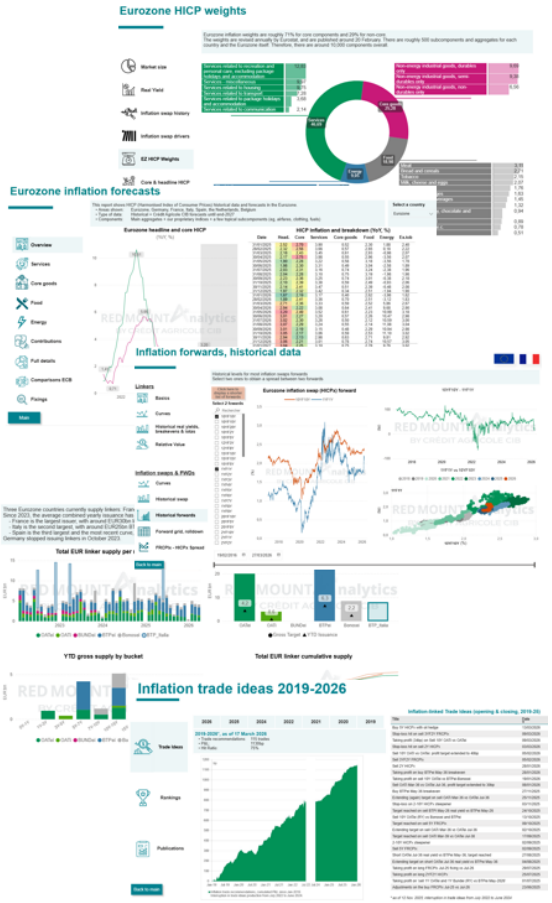
1 - Fundamentals
The basics of inflation: cash market size and mechanics, inflation swaps conventions, CPI weights and inflation drivers

2 - Forecasts
The one shop-stop for inflation forecasts: our projections up to two-year ahead combined with historical data, contributions charts, proprietary indices, comparing with fixings etc. Granularity of our models? 65 components for the US, 1000 components for the Eurozone. Unique in the market and weekly updated. Enjoy

3 – Market monitor
Eurozone linkers: proprietary data (SA breakevens and real yields, deltaZspread), RV analytics. Inflation swaps & forwards: curves, historical, forwards grids, rolldown, FR vs Eurozone inflation swaps and forwards. Hundreds of possible combinations. 3YF2Y France vs Eurozone? We have it. Soon coming? US TIPS & inflation swaps

4 – Flows and technicals
EUR linker supply: supply since 2009, linker by linker, tap by tap. Supplied vs target for the year.
US TIPS: auctions statistics since 2009

5 – Trade ideas
Don't miss this one. Our inflation trade ideas since 2019. Around 115 trades, 1130bp P&L, 75% average hit ratio over seven years. With the links to the trade recommendations, of course.
Also sharing the rankings (Bloomberg) of our short-term inflation forecasts since 2020



Source: RMA by Crédit Agricole CIB

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