STRATEGY

CRA Three-Month CORRA Futures

MONTRÉAL EXCHANGE

Yield Curve Strategy - Calendar Spread

Situation

An investor anticipates a steepening of the short-term yield curve.

Objective

The investor would like to profit from a possible change in the yield curve in the next month.

Strategy

Market conditions on July 2nd

	June Contract	September Contract
CRA	95.285	95.495

Given that the investor expects a normalization of the yield curve (an increase in long-term versus short-term rates), he will buy the nearest month CRA contract (June CRA) and sell the farthest month CRA (September CRA). This strategy is called a calendar spread. The investor will buy 50 June CRA contracts and sell 50 September CRA contracts on July 2nd and will ultimately reverse the position on September 17th by selling 50 June CRA contracts and buying 50 September CRA contracts.

Results

Market conditions on September 17th

	June Contract	September Contract
CRA	95.050	95.125

Loss on the June CRA position:

50 contracts x (95.050-95.285) x 100 basis points per contract x $25 per basis point = ($29,375)

Gain on the September CRA position:

50 contracts x (95.495-95.125) x 100 basis points per contract x $25 per basis point = $46,250

Profit from calendar spread = $16,875

Comment

This type of yield curve view can be expressed using different horizons within the Canadian yield curve. Many portfolio managers use the CRA/CGB* spread to take advantage of a change (flattening, steepening) in the Canadian yield curve.

*CGB: 10-year Government of Canada Bond Futures.