

Rates Spark: All eyes on US CPI

Markets remain highly sensitive to anything inflation related, as highlighted by the strong reaction to Tuesday's US PPI. A key test for the bullish undertone is CPI, where we think an in-line reading might not be enough to spur on bond bulls. EUR rates again proved more sticky, reflected in further tightening of the UST-Bund spread



An in-line CPI might not be enough to spur the bulls on

The sensitivity of US rates to anything inflation related was highlighted by Tuesday's PPI release. As the figures were released the market's first reaction was to sell off, with 10Y yields ticking 3bp higher to 4.51%. But they then went on to rally towards 4.44%.

On closer inspection, the rise in the monthly core rate to 0.5% was balanced off against downward revisions for the prior month, as well as some of the sub components pointing to a possibly more benign PCE release. So far this was enough for the rates bulls to find themselves confirmed. But it is the CPI release later today that will be the key test with the consensus looking for slightly lower, but still too hot monthly core reading of 0.3%.

Also on the wires on Tuesday was Fed Chair Powell, and his remarks will have resonated with more bullish views, or at least not put them off. For one, he described the current policy stance as restrictive by many measures and saw it as unlikely that the next move would be a hike and more

likely that the Fed would hold. While pointing out remaining uncertainty and less confidence than when heading into 2024, he does see signs of gradual cooling and rebalancing in the jobs market and also expects inflation to move back down on a monthly basis.

Eurozone rates being more sticky was confirmed on Tuesday, partly on the back of the heavier primary market activity. The Bund yield climbed to 2.54% even as Treasury yields dipped. This resulted in the 10Y UST-Bund spread narrowing more than 5bp to 193bp. On the eurozone data front there was a small beat in the German ZEW sentiment indicator and we saw ECB's Wunsch reiterating his view that the ECB should refrain from back-to-back cuts even if two cuts this year were close to a "no brainer". But cutting in June and again in July could signal that the ECB was going to cut at every meeting this cycle, which he clearly does not see as a given. The market's pricing for this year's ECB easing slid below 70bp.

Today's events and market view

The key release today is US CPI . Recall that it was last month's hotter release that pushed 10y UST yields above 4.5% again for the first time since last November. A very broad consensus of economists sees the crucial monthly core rate coming in at 0.3%, down from 0.4%. Only a handful diverge seeing it steady or coming in lower. From the Fed we have Kashkari speaking on the economy.

In the eurozone eyes are on the preliminary 1Q GDP readings as well as the March industrial production data. There will also be a few more ECB speakers to follow, with Muller, Rehn, Villeroy and Makhoulouf having scheduled appearances.

In primary markets Germany taps two 30Y bonds for €1bn each. The UK taps its 9Y green Gilt for £3bn.

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