

## Rates Spark: Both eurozone growth and Fed on hold

Consensus expects zero GDP growth from the eurozone in the second quarter, but the outlook remains positive, supporting our bearish take on rates. The Fed will most likely hold today, which could intensify Trump's campaign against Powell. This would feed the bearish narrative on longer-dated USTs. We still see the Fed cutting by the end of this year



Consensus expects 0% second-quarter GDP growth in the eurozone and we expect the Fed to keep rates on hold

### Low expectations for eurozone growth today, but the outlook is positive

It's likely to be a busy day for rates, with important economic data and of course the Fed meeting. The economic data for the eurozone has been on the more positive side of late, including the upside surprises from Spanish and French GDP numbers. Consensus sees a 0.0% eurozone aggregate GDP growth rate for the second quarter of this year, which of itself is no reason to be bearish on rates. But the outlook should improve and the tail risk of a full-blown trade war has abated somewhat.

If we get a disappointing growth reading, that could challenge eurozone government bond (EGBs)

spreads. The tight spreads may partly be explained by the idea that Europe was a safe haven to hide from the US-driven trade wars. But with Trump turning more constructive on making deals and seemingly successful in getting attractive terms, EGBs may lose some of that allure. If, on top of that, we get disappointing growth numbers, then that may be a catalyst for EGB spreads to start widening again.

## Trump won't like another Fed hold

We don't expect the Fed will cut rates today and the markets agree, but [we do see cuts later this year](#). After an initial bump higher in inflation from tariffs, we think the labour market will show significant cooling. This should allow the Fed to cut in December, maybe even by 50bp. The market also sees around 50bp of cuts by the end of this year. Going forward, we do, however, expect plenty of rates volatility on the back of contrasting forces from rising inflation numbers and downside economic surprises.

After holding rates – again – Trump's campaign against Powell may intensify. While the back end of the curve could find comfort in Trump's more constructive approach to trade deals, the Fed's independence remains a challenge. Previous speculation about firing Powell showed an upswing in 10Y UST yields, which may be a warning for what could come. Trump pushing a more dovish person as Fed Chair may see earlier cuts, and lower front-end rates, but the back end would be exposed to potential policy errors. Together with a deteriorating fiscal picture, a bearish case for USTs would be easily made.

### Wednesday's events and market views

Plenty of data and events to digest. We started this morning with French GDP numbers, which showed 0.3% QoQ growth for 2Q, well above the consensus of 0.1%. Later in the day, we will get the Italian GDP estimates and the aggregate eurozone figure. Other eurozone data includes Spanish CPI numbers, eurozone consumer confidence and the eurozone wage tracker.

From the US, besides the Fed meeting, we have 2Q GDP estimates, together with the quarterly PCE indices. Other data includes the ADP employment numbers and home sales. For the quarterly refunding announcement, we don't expect any surprises.

In terms of supply, we have the UK with a 27Y Gilt tender for £0.3bn. Italy will auction 5Y & 10Y BTPs together with a 9Y CCTeu for a total of €9bn.

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