

## Rates Spark: bye bye hikes

Taking their cues from the US, developed market rates continue to price out rate hikes. The result is lower rates across the board, but also markedly steeper curves. An upside surprise to today's eurozone CPI is a risk to this move but the path lower in rates is not in doubt, in our view. A test of 0.50% in Bund yields this summer is not excluded

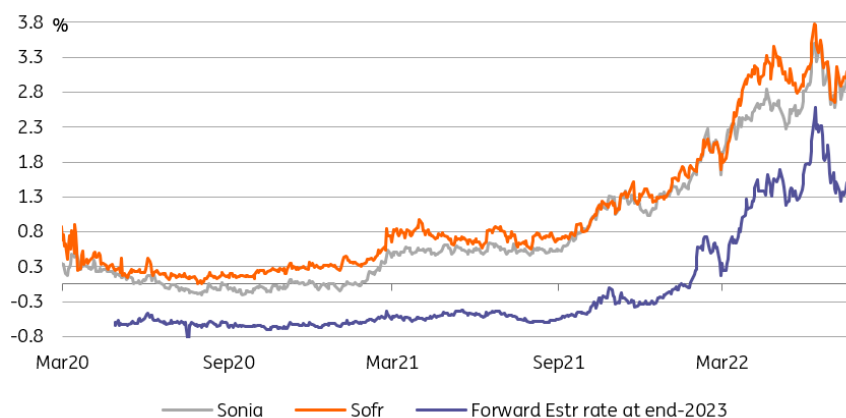


Global rates markets are taking their cues from the US Federal Reserve. Pictured: Fed Chair Jerome Powell

### Bond market puts central bank hikes on ice

Even accounting for a fair dose of confirmation bias, the rally in front-end rates this week is nothing short of spectacular. Once again, global rates markets are taking their cues from the US, where a more nuanced Fed tone was enough for bond yields to dive, and for curves to bull-steepen. Of course, a miss in US 2Q GDP added to buying pressure at the front-end, but we think the underlying conviction that the looming recession will scupper central banks' efforts to tighten policy is to blame.

## Swap curves are pricing our central bank hikes fast



Source: Refinitiv, ING

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*The looming recession will scupper central banks' efforts to tighten policy*

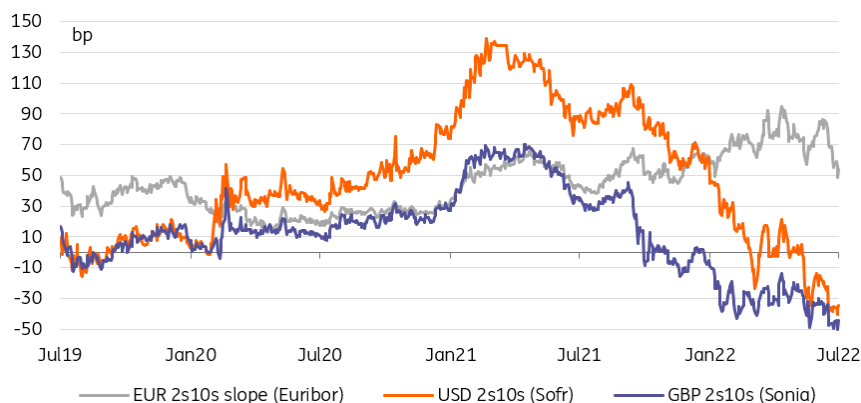
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To be clear, we do agree with recession calls and have long argued that the amount of hikes priced by the EUR and GBP swap curves were excessive. Throughout the bond sell-off, our economics team has called for no more than 100bp of hikes from the ECB in this cycle, compared to market pricing of more than 300bp at some point. This is to their credit. The market adjustment lower is probably closer to its end than to its beginning but we see more downside risks to rates on account of 1) risk aversion drawing more money into the relative safety of bonds, and 2) as the EUR curve still needs to price out roughly 50bp of hikes by the end of this year.

## Bund yields eyeing 0.5%, Bank of England to hike 50bp and stop

Of course, this adjustment will be far from a smooth journey. The upside surprise to [Germany's July CPI](#), as well as our forecast for persistently high inflation over the coming months, means some of the recent rally could well be reversed, in particular if eurozone core inflation released today accelerates as forecast. As a result, we think the size of the drop in rates at the long end might be smaller, but the transition looks to be smoother. We wouldn't be surprised to see Bund yields test the 0.5% level by the end of this summer.

## Yield curves have some re-steepening to do



Source: Refinitiv, ING

*Our forecasts have CPI returning below the 2% target as soon as the end of next year*

That policy dilemma is also one faced by the Bank of England. An upside surprise in inflation and a still robust job market tip the scales in favour of a 50bp hike at next week's meeting, but this may well be the last hike in this cycle. Our economics team summarised the factors affecting the Bank's decision in [a handy article](#) but, overall, they boil down the already high rates and looming recession risk cementing its expectations for lower inflation. Our forecasts have CPI returning below the 2% target as soon as the end of next year.

### Today's events and market view

This already exciting week concludes with no less than eurozone 2Q GDP and July inflation. Bonds shrugged the upside surprise in German CPI yesterday, rallying into and after the release. Worse, the curve bull-steepened as it priced out more ECB hikes.

This is also the last weekday of the month which tends to be favourable to curve flatteners and for duration more generally.

June personal income and spending kick off today's list of US releases, to be followed by the US June PCE deflator. The core measure is expected to stabilise at 4.7% after the quarterly number, released as part of 2Q GDP yesterday, slowed down to 4.4%. The inflation expectations component of the University of Michigan will be closely watched. Even if this is a final read on it, the figure has been liable to revisions in the past. Chicago PMI is also expected to point downwards.

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