

## Rates Spark: Data does the talking

Yield curves bull steepened as European inflation rates dropped and Fed officials made a case for skipping the June meeting. In the end it will all come down to the data, where core inflation dynamics are key in Europe today, and US jobs data is released.



### Bull steepening on lower inflation prints

Yield curves are in bull steepening mode. While underlying risk sentiment was dampened by softer Chinese data, it was the first European inflation readings that provided the push lower in the European session. Notably it was sterling rates that outperformed, but we attribute that to its generally higher beta and, as we highlighted before, that it displayed the highest discrepancy between market levels and central bank messaging to begin with. But also in the eurozone the market is now no longer fully discounting two more 25bp hikes from the European Central Bank.

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*Inflation data will be subject to more noise given government interventions*

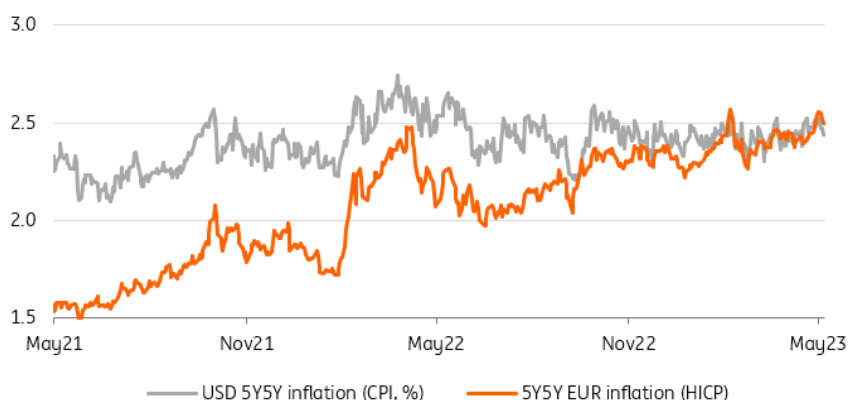
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The releases itself, German and then French preliminary country data, showed headline inflation

dropping faster than anticipated. Our economist [sees signs of broadening disinflationary trends](#), but also cautions that inflation data will be subject to more statistical noise given government interventions such as the newly introduced €49 monthly train tickets in Germany, which pushed inflation down in May.

Some ECB officials have also reacted with cautious optimism to the inflation data. France's Villeroy noted that we will probably have seen the peak in French inflation now with the monetary policy tightening also starting to show its effect. In his view it was a sign that "rather than the level of the terminal rate [...], it's how long we remain there that is essential". The ECB's hawks, who had been more vocal in recent weeks, might still question whether the tightening delivered so far is sufficient. Looking at market-based expectations of inflation they could point to 5y5y inflation swap forwards, while falling again is still sitting above 2.5%. And despite encouraging developments in the headline, it is the underlying dynamics of core inflation that remains key.

## The downtick in inflation forwards is good news but elevated levels remain a cause for concern



Source: Refinitiv, ING

## Key Fed officials make the case for skipping June

The US session saw more volatility around a mixed bag of data releases. Regional PMIs were weaker while data on job openings came in stronger than expected. More interesting – and with larger effect on front end pricing – were comments from two key Federal Open Market Committee voting members. Fed Governor Jefferson and Philadelphia Fed President Harker both made the case for skipping the June FOMC meeting. After all, the anecdotal evidence provided in the Fed's Beige book released yesterday showed hints of a cooling job market and also more signs of disinflationary dynamics gaining traction.

### *Strong jobs and inflation data can still mean a hike in June*

The Fed funds forward for the June meeting period dropped by some 8bp to below 10bp in the wake of the comments. The forward for July, marking the high point in the forwards, ie, terminal rate, also dropped 5bp with 21bp hikes now discounted. Markets, and in the end also the Fed, will be looking to the key data ahead, such as the payrolls report due tomorrow and the next CPI

report. Strong readings here would still make the case for a June hike.

## Today's events and market view

Month-end has passed and with it probably also some of the short covering that has helped push rates lower again in recent days. In the end, the data will dictate direction and today's session already has to offer some key releases.

In the eurozone the focus is on the eurozone flash CPI. Country data has already primed markets for a larger drop in the headline rate, key will now be the core rate that is seen edging down only marginally from 5.6% to 5.5% year-on-year. Apart from scheduled appearances of ECB's Lagarde and Knot we will also get the ECB accounts of the May meeting. They may shed more light on the internal deliberations and perhaps any bargains between dovish and hawkish camps. Recall, the ECB slowed the pace to hiking by only 25bp, but added a hawkish twist by announcing a full stop to APP reinvestments. Also, look out for any concerns surrounding upcoming TLTRO repayments.

In the US markets will be looking to the ADP payrolls report ahead of tomorrow's official jobs data. More important could be the ISM manufacturing index with a more detailed read on the underlying trends in employment and prices than the disappointing regional indices of late.

In primary markets we will see longer dated bond supply from France and auctions from Spain. Slovakia mandated a new 10y bond yesterday.

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