

Rates Spark: Demand for safety to stay

Risk assets are benefiting from the delay in tariffs, but rate markets remain careful about outstanding risks. The US front end of the curve doesn't suggest a radical change in market perception yet. Increased volatility means safe assets such as 10Y bunds may see elevated demand for now



Traders on the floor of the New York Stock Exchange as markets continue to react to Trump's tariff moves

US Treasuries give the pause trade a mild thumbs up

Risk is back on since the tariff pause news, with material rallies on equity markets (the ones open) and some retightening in credit spreads (high yield 5yr CTX is tighter by a notable 60bp). This is understandable, as the general sense of anxiety has diminished. Market rates though are less excited, which is a reminder that there remains a material elevation of angst. This also makes sense, as the tariff barriers remain, albeit reduced in certain areas and only for 90 days.

Front-end market rates were initially up by 20bp but have since been pared back by 5bp. So still up, but not by enough to mark a material change in overall perception. There has been even less reaction on the 10yr yield, which now just feels comfortable up in the 4.4% area. Bonds are signalling that the pause is significant, yet not much has fundamentally changed. This could shift if the 90-day pause becomes permanent. Until then, the US bond market remains somewhat negatively impacted by the initial tariff actions.

Good news for the EU, but risk sentiment remains wary

A pause for now is good news for the eurozone and the 10Y swap rate is back at levels from before "Liberation Day". The significant rise in UST yields played an important role in this. The front end of the curve still trades at lower rates, reflecting the still-outstanding risks on investors' minds. Markets are reverting to an ECB landing zone between 1.75-2%, a range which was held for many months previously. But we remain wary that the situation could easily worsen again. The trade wars are still far from over and the EU still faces higher tariffs, especially on the car industry. Meanwhile, China and the US are clashing, and an end to their conflict does not seem to be in sight.

The increased volatility will also remain, preventing a full restoration of risk sentiment. Markets will not easily forget these episodes with wide market swings and thus the demand for safe assets should remain elevated. 10Y Bunds, for one, significantly outperformed swaps during the peak stress episode underscoring their safe haven role, even if they are now trading above the swap curve again.

Thursday's events and market view

With markets relieved by Trump's turnaround on tariffs, the main data points to digest come from the US in the form of the CPI and jobless claims numbers. The headline CPI is expected to fall to 2.5%, but with still substantial tariffs incoming it will have little signalling effect. More notably is that the monthly core CPI is seen at a relatively high 0.3% month-on-month. The afternoon will see a number of Fed speakers, including Logan Schmid and Goolsbee.

In primary markets Spain will auction 4y, 8y and 10y bonds for up to €6.5bn in total. The US Treasury will auction US\$22bn in 30y bonds which will be closely scrutinised. Last night's 10y auction did see strong demand with also a high share of non-dealer demand.

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