

Rates Spark: Diverging ideas

The Fed delivered a hawkish pivot this week, and the Bank of England a dovish 75bp hike. Barring a clearer decoupling between the Fed and other central banks, today's US job report and next week's CPI will be key. Even if both ease, we expect rates to keep rising, and curves to steepen, on supply



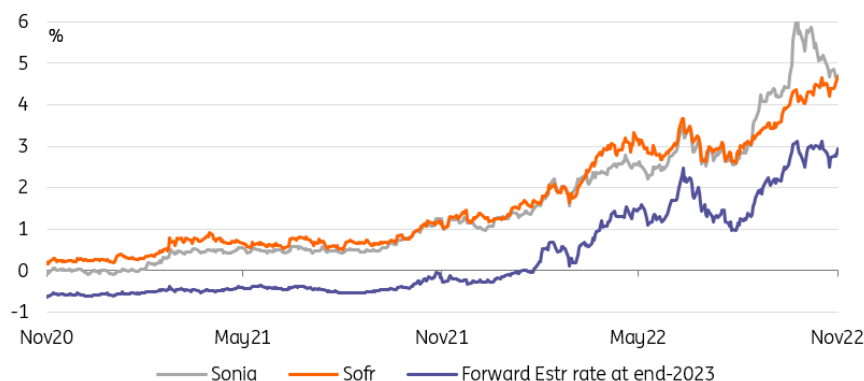
The Fed takes with one hand and takes with the other

Viewed from abroad, [the Fed's balanced message](#) didn't come across as a hint of less hawkish days to come. The Fed has come to be viewed as one of the main reasons other central banks accelerated their hikes to 50bp or even 75bp increments. Even in case of a slowdown in Fed hikes to 50bp in December, the main risk for markets is now that this hiking cycle stretches well into 2023, and so forces the hand of the Fed's foreign peers. With a pause in hiking cycles being pushed farther over the horizon, we expect appetite to own duration to remain limited into year-end, save for investors with very long investment horizons.

Supply still tips the scales in favour of higher rates

Having made the case that Fed policy is so central to the fate of foreign fixed income markets, it is clear that today's US employment report (non-farms payroll), and next week's CPI will also play a role. As it happens, consensus is for a cooling of both, so markets can in theory look forward to more stable performance in bonds next week. However, this being one of the last weeks in which bond issuers can practically conclude their 2022 funding plan, or pre-fund for 2023, supply still tips the scales in favour of higher rates in our view. Even if we're wrong, the US Treasury is due to sell 10Y and 30Y notes/bonds next week, so the odds are that any post-NFP spike will be sold into.

A more hawkish Fed is pressuring foreign rates ever higher



Source: Refinitiv, ING

The BoE actually managed to deliver a dovish message, and markets listened

Given the strength of the dovish message that accompanied [the BoE's 75bp hike yesterday](#), many were left wondering why it didn't only hike 50bp. In a sense, most of the Bank's pushback concerned the amount of hikes priced by the curve for subsequent meetings, but the hawkish justifications for accelerating its hiking pace were conspicuously missing. GBP front-end rates did close the day higher, but given the Fed's hawkish message, and sell-off at the front-end of the EUR and USD curve, we conclude that at least some of the BoE's dovish message has been heard. This was far from a foregone conclusion, markets have had a well-defined tendency to ignore BoE dovish soundbites at recent meetings.

The long-end remains the sector most likely to come unmoored in case of a pick-up in volatility

What was more interesting is the underperformance of long-end gilts. That the curve steepens on a dovish message is not altogether surprising but we get the feeling that the long-end remains the sector most likely to come unmoored in case of a pick-up in volatility. Perhaps this is also a reflection of the fact that the [shortage of collateral and short-dated gilts](#) is preventing the front-end from participating fully in any sell-off. In any case, we think curve steepening remains the path of least resistance, especially if the BoE joins in on the dovish pivot operated by other central banks globally, such as the Reserve Bank of Australia, Bank of Canada, Norges Bank, and likely the

European Central Bank soon.

EUR and USD curves should follow their GBP peer into steepening next week



Source: Refinitiv, ING

Today's events and market view

Various measures of eurozone member state industrial production figures are released this morning, alongside services PMIs. Eurozone PPI is expected to decline slightly from dizzily high levels.

Central bank speakers will be omnipresent, once again. From the ECB, Christine Lagarde, Joachim Nagel, and Luis de Guindos will be making the headlines. Huw Pill's take on yesterday's BoE decision will also be closely watched.

In spite of all the interesting central bank comments we're sure to receive, the most market-moving event will probably be the US job report. Job creation is expected to revert to its long-term average around 200k. An uptick in unemployment and downtick in hourly earnings could take the edge off Jerome Powell's hawkish comments earlier this week, but a resumption of supply next week tilts the odds in favour of higher rates still, especially at the long-end.

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