# Rates Spark: The push and pull between US and EU rates

We identify conflicting impulses from next week's US election. If the betting markets are right and Trump wins, then US Treasury yields are likely primed to keep on rising. But a Trump win could at the same time pose issues for eurozone risk assets, putting a bid into Bunds. Friday's payrolls report is pivotal ahead of that, potentially taming Treasuries

## US Treasuries touch 4.3%, marking a significant backup in yields post a first rate cut

As the US 10yr briefly touched 4.3% on Monday, it marked a 70bp move to the upside from the moment the Fed cut by 50bp on 18 September. We have continued to emphasise that a rise in the 10yr yield post a first cut from the Fed is not unusual. In fact it has happened around 50% of the time in the past number of decades. However, the extent of the rise has typically not been more than 50bp. So the cumulative 70bp move seen is large.

The move from 3.6% to 3.85% is down to a tendency for the 10yr yield to rise post exuberance into a first rate cut. The move from 3.85% to 4.10% is down to the last payrolls report, which surprised practically everyone with its robustness. The subsequent move from 4.1% to 4.3% is a combination of two factors. The first is that most data this week are expected to be firm (e.g. third quarter GDP expected at 3% and the threat of a 0.3% month-on-month on the core PCE price index). The second is the growing Trump discount, on a theory that we get a repeat of what happened in 2016, when there as a 50bp rise in the 10yr yield within the first week of the election outcome.

The big question is whether the Trump trade is done as of yet. We are now exactly a week out from the election, and the betting markets continue to have Trump as the winner. The US 10yr is in no mood to move lower given the combination of circumstances it is dealing with. But there is one potential surprise factor that we need to get through – Friday's payrolls report. We had hurricanes and strikes in play for this report, which gives it the potential to print on the low side. Estimates have been pared back in the past week practically on a daily basis. The latest is 110k, which is weak, but not catastrophically so. And the unemployment estimate is firm at 4.1%. Get this, as the bearish tone persists.

That said, there is a greater potential than usual for this particular payrolls report to surprise to the downside. If we were to get, say, a 50k outcome (or even something in the 50k-100k area) it could be enough to mark a pause in the Treasury bear market tone. But then we are straight into the election next week. Treasury market bulls would then fret on the possibility for a Trump win. That limits the downside for the 10yr yield. A materially weak payrolls report, say sub-50k, would cause the election outcome to play second fiddle, as market rates then shift lower significantly.

But unless or until we get confirmation of material weakness in the payrolls report, we, in the meantime, maintain a tactically bearish preference for the 10yr Treasury yield.

## Plenty of events lined up that could trigger lower EUR rates

In the eurozone, the dovish sentiment continues, helped by lower oil prices, and markets are now positioned for 125bp of more European Central Bank easing by mid-2025. The implied endpoint stands at around 1.75% and seems to be edging more and more below neutral territory. Much boils down to the US elections, given that the most recent economic data doesn’t warrant such pessimism. And with the ECB signalling a strong willingness to ease further, we doubt euro rate markets will turn before the election outcome is clear.

Also, the back end of the curve may find itself lower during these rather eventful days. The 10Y ESTR OIS rate is now 2.25% and is starting to move more independently from 10Y UST yields. Where a Trump victory is considered inflationary in the US, the feared trade tensions are weighing down on eurozone rates in the opposite direction. The uncertainty around 10Y EUR swap rates remains high and implied volatility over the next three months has jumped up again in anticipation of next week.

In terms of the downside risks to EUR rates, we could have multiple things line up, leading to a potentially large drop over the next week. From the eurozone we have CPI numbers that could (again) surprise to the downside, in the US payroll numbers may not meet expectations, and then a Trump victory on top of that would severely hurt eurozone risk sentiment. Putting these things together, and we could very well see 10Y OIS break the 2% handle in the near term.

## Tuesday's events and market view

US data releases include JOLTS job openings and the Conference Board consumer confidence index. Job openings are expected to nudge down slightly, whereas consensus sees higher consumer confidence. Markets may show some sensitivity to the JOLTS report given payroll numbers are lined up for later this week. For the eurozone we'll have to wait until Wednesday for key data releases.

The UK will auction £4bn of 5Y Gilts, while Germany is scheduled to issue €4bn of 5Y Bobls. From the US we have a new 2Y FRN and new 7Y note, together valued at $74bn.


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