

Rates Spark: Treasuries bully direction

The end games for the Fed and ECB continue to pull in different directions. It's been quite the change in sentiment in the past six weeks. The Fed was supposed to be the big cutter on a delayed start. Now the pressure is greater on the ECB. This is manifesting in ongoing widening in the Treasury-Bund spread. And in the end, direction is being bullied by Treasuries



Treasuries continuing to test the upside for yields, and for good reason

The US 10yr yield has had a material breakout to the upside through Monday. And it's not a huge surprise. A number of factors continue to push in that direction. US macro data continues to refuse to lie down. Risk assets did not have a great day on Monday, but new highs were hit on many major indices in the past week or so. Trump doing better in the polls also pushes in the same direction. Neither one of these is in the driving seat, but importantly there is not much impulse out there to push things in the other direction. For example, the Israel war is not having a meaningful impact (but that can change).

And even the inflation data is being viewed with a renewed degree of scrutiny as we face into another round of core PCE data next week, with some murmurings of a 0.3% month-on-month for core PCE. The latest payrolls report also looms. A week ago the consensus was in the 100k region, as the "weather" spiked jobless claims. But payrolls estimates have been edging higher by the day since. The consensus estimate is now in the 140k area, just a smidgen below the 150k level that is bang on neutral for the economy. We think payrolls is primed to be weaker than this, but we need to wait another 12 days before we know either way.

We've argued that a trend towards 4.25% for the 10yr was probable until or unless we see a payrolls wobble. See [here](#). Given the big move through Monday, some stabilisation is likely first. The market moves through Monday sets out the stall for expectations of firmish data next week. Treasury bulls will be looking to negate that presumption. We're fine to switch to bullish on some weak data, but we need to see it first. Till then, we remain tactically bearish on Treasuries.

Repricing of ECB endpoint as recession fears lessen

Euro rates bounced higher again after the prevailing dovish sentiment in the wake of the European Central Bank meeting. But interestingly the very short-end remained relatively anchored, and the expectation of a December cut is still around 20%. Instead, the move could be more characterised as a repricing of the ECB endpoint, which at around 1.8% now, is slowly making its way back to 2%.

The market's trust in the ECB to manage growth issues can bolster the back-end of the curve, particularly if economic data doesn't worsen too quickly. We see the neutral rate of the ECB in the range of 2.0-2.25%, and thus the current 5Y EUR swap rate of 2.1% still has room to drift higher as recession risk fears lessen. Having said that, with the US elections in exactly two weeks, bond markets may want to sit that out before making a more confident move up.

Plenty of speakers to watch at the IMF's annual get-together

Meanwhile, the attention will go to a long list of central bankers speaking at the IMF these days. Given the ECB's cut last week was apparently a unanimous decision, much to the surprise of markets, we'll be listening to the change of tone of the more hawkish speakers, including the Austrian Holzmann and Knot from the Netherlands. Also, the Bank of England's Bailey will be one to watch, since we anticipate a more dovish tone going forward.

Tuesday's events and market views

Plenty of central bankers speaking at various IMF-related events, including Lagarde from the ECB and Bailey from the Bank of England. In terms of data the calendar is light, with US mortgage applications perhaps the highlight. The Richmond manufacturing index is expected to improve slightly from -17 to -21.

Italy announced a syndication for an estimated €13bn, including a new 7Y BTP and a 30Y BTP tap. The UK will auction a 20Y Gilt linker for £0.9bn. From Germany we have €5bn of new 2Y Schatz up for auction.

Author

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

Michiel Tukker

Senior European Rates Strategist

michiel.tukker@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.