

Rates Spark: EUR curve wants to steepen, but faces resistance

Improving eurozone hard data and a stable ECB mean the EUR swap curve should steepen from here. The complexity of estimating Dutch pension reform flows doesn't help the case for a steeper 10s30s. In the US, Treasuries are trading heavily in post-FOMC, and look like they can attempt to continue to do so



Higher 10Y euro swap rates through steeper curves

With hard data confirming eurozone growth is on a recovery trajectory, we think 10-year euro swap rates should start considering a push higher. Additionally, inflation came in hotter, bringing the 10-year inflation swap a tick closer to the 2% target again. We acknowledge that the upside potential for euro rates remains limited this year, and we target a 10-year rate of some 10 basis points above the current 2.65%. With growth on track to improve further in 2026, that's when we aim for the 10Y to look at 3% as the new equilibrium.

For the front end, the wiggle room is much more limited as the ECB's mantra of being "in a good place" is set on repeat. That means that the 2Y swap rate is firmly anchored between 2.1% and 2.2%. The rise in longer-dated yields must therefore come from steeper curves. That steepening faces resistance from the US, however, where 10Y UST yields dove from 4.5% to 4.0% over the past

months. As 10-year US rates stabilise, or even rise as we predict, the 2s10s of the euro curve should feel more comfortable steepening.

Dutch pension reforms too complex to push for steeper 10s30s by itself

Besides US spillovers, we have flattening pressures from the very long-end to deal with, whereby the 10s30s steepener seems to have come to a halt. The 10s30s dynamics this year have been almost entirely dictated by the US, but Dutch pension reforms may also play a role. Whilst we still anticipate significant unwinds of 30Y becomes and bonds starting in January, we feel the trade may have become too crowded over the summer.

Estimating the timing and size of the flows stemming from the pension reforms is extremely complex, if not impossible, given the available data. Each fund of the 30 scheduled to transition on 1 January 2026 has a unique maturity profile and hedging strategy. Additionally, we remain concerned that IT problems could result in last-minute delays. And now that the US macro landscape is less supportive of 10s30s steepeners, we understand that the trade has become less attractive from a risk-reward perspective.

US Treasuries continue to trade heavily post-FOMC

As the dust settles following Wednesday's Federal Open Market Committee outcome, the new levels for the 2-year and 10-year combo are 3.6% and 4.1%, respectively (both up 10 basis points). The net feeling centres on a Fed Chair that has no problem leaving the funds rate unchanged at the December meeting, if that is deemed the thing to do. It comes with residual comfort in the economy. The fact that a 4.3% unemployment rate was specifically referenced as "low" amplifies this point. Instead, there is a degree of discomfort with inflation running at 3%, and likely heading higher.

At the same time, there has not been a material change in the ultimate landing level for the funds rate. It's now slightly above 3%, but still within the 3% range. And the 5yr rate continues to trade below the straight line that can be drawn between the 2yr and 10yr rates in a steady fashion. This signals an unwavering expectation that the Fed is, in fact, far from done — it's just a matter of timing. The question now is how robust (or not) the economy manages to be in the next month or so. Yields may continue to push higher—particularly for longer maturities—despite the current pause. However, the lack of hard data remains a challenge due to the ongoing government shutdown. It is an opportunity for the 10yr yield to have a go at testing higher. It might not go too far, but there is a data vacuum that can be filled in, at least until we gain more clarity.

Friday's events and market views

We start with eurozone inflation numbers. The headline French CPI number is expected to come in at just 0.9% year-on-year, a tick below the 1.1% from September. Italian inflation is also expected to nudge lower, from 1.8% YoY to 1.6%. This would then help the eurozone aggregate core CPI down from 2.4% YoY to 2.3%. Due to the US government shutdown, we only expect the Market News International (MNI) Chicago PMI to stand out as notable data.

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