

Rates Spark: Even worse before it gets better

Brexit will likely grab the headlines again, but the broad rally of core bonds yesterday signals it is not the only worry for rates markets. US stimulus talk is caught up by partisan politics again, and stubbornly high infection rates foreshadow more containment measures even as the vaccine roll-out has begun.



Source: Shutterstock

Overnight: Last-ditch Brexit manoeuvres

EU's chief Brexit negotiator Barnier said yesterday that no deal was now the more likely than an agreement. In a last-ditch effort PM Johnson will travel to Brussels this evening to meet the EU's von der Leyen in a final attempt to reach a breakthrough. Contentious passages from the internal markets bill had been dropped earlier, but sticking points remain around the level playing field.

In the US it is still hard to gauge the odds of a fiscal stimulus deal emerging before the Biden administration is sworn in on January 20th, but a \$916bn counter-proposal by Treasury Secretary Mnuchin highlighted that both sides remain far apart, even on matters such as the amount of the one-off cheque payment.

Price action in Asian hours saw an extension of recent trends, with EUR bond futures outperforming their USD counterparts, while stock futures pushed higher following Wall Street's lead yesterday evening.

Near term reality check

It appears that after the euphoria of the past week rates markets have taken a step back to realize that not just Brexit, but indeed multiple issues still cloud the near- to medium-term outlook. A significant rough patch still has to be overcome that underscores the continued dependence on fiscal and/or monetary intervention.

Infection rates and hospitalizations remain stubbornly high, to a degree that some countries like Germany are mulling stricter containment measures again. And while the roll-out of the vaccines has begun, it will still leave large groups of the population vulnerable to infection for some time. In other politics the EU should soon know whether it has to resort to a plan B on the recovery fund, with Poland and Hungary momentarily still blocking the current framework. Given the EU summit in the coming days this could result in a catharsis of sorts on the political front, although European politics have had a habit of extending deadlines. Turning to the US, the initial optimism surrounding the restart of stimulus talks is being caught up by partisan politics, which would put the onus on the Fed again.

As rates markets turn gloomier, that ECB will have a hard time eliciting a dovish market reaction when it unleashes further stimulus tomorrow as widely expected, even as we expect the package itself to be generous. That should certainly be true for outright yields, with the 10Y Bund now trading below -0.6%. However, government spreads still have some room to retighten with the 10Y Italy/Germany spread having widened to 120bp over recent days.

Today's events: Final German bond supply, funding plans

Germany will issue €3bn in a 2Y Schatz today, marking the final bond supply for the year.

Concluding the supply activities turns the focus to the release of bond funding outlooks for 2021. Belgium released its [outlook](#) yesterday, penciling in €36bn of bond issuance in 2021 after €44.5bn this year. The lower target for bonds is not solely down to a lower overall financing requirement, but also result EU SURE loans received. Looking ahead the Netherlands is scheduled to release its outlook on Friday.

Authors

Benjamin Schroeder

Senior Rates Strategist

benjamin.schroeder@ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@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 <http://www.ing.com>.