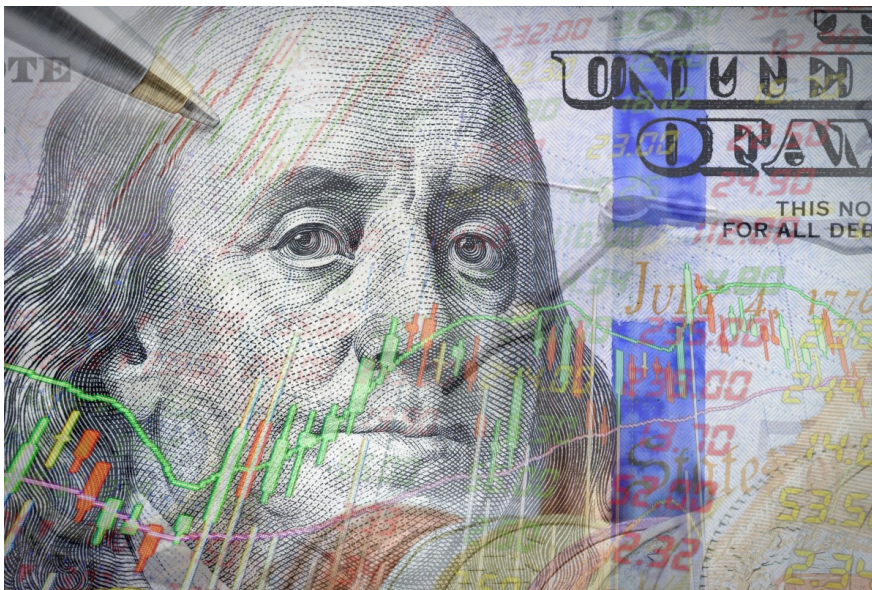


Rates Spark: Market rates still pressured higher

Even though Monday was a bit risk-off, the bigger picture theme remains risk-on. It's been the way so far in 2024 in fact. Eurozone spreads have narrowed too. And inflation data has been a tad uppity. It's not what could be termed a rate-cutting environment, yet. So we remain tactically bearish. Next big message to come from Friday's payrolls report



Likely to drift higher in market rates into Friday's payrolls

Reaction to Thursday's PCE deflator (a tad better than expected, but still elevated for January) continued through to the close of last week, but saw some reversal as a theme for Monday. Our central view has not changed, in the sense that we view the totality of circumstances not yet lined up for a capitulation fall in market rates into a rate-cutting theme. Not only have recent inflation prints been a tad uppity, but the mood of the risk asset space remains risk-on.

Monday was not risk-on per se, in fact it was risk-off. But it would take a more impressive moment of risk-off to take away from the wider risk-on theme, one that has in fact dominated so far in 2024. The same theme obtains on credit markets through the ratchet tighter in spreads, and the

continued outperformance of high yield. But also in quite subdued equity market volatility. There's a degree of frothiness about circumstances, but with no evidence of anything about to implode.

Basically this is not a market that is discounting a recession. So if there is one in the offing, then we'd need to see some of the headline data being more illustrative of this. Even when we look ahead this week to Friday's payrolls report, we find an expectation for the creation of 200,000 jobs. That's comfortably above the replacement number of 150k, a rate that is neutral (neither hot nor cold).

If we indeed get a 200k outcome confirmed for February, we'd suggest that would place ongoing upward pressure on market rates. Even though it would be in line with expectations, those expectations themselves are in line with maintenance of a firm macro underpinning when it comes to the labour market. Bond market bulls would need something far more subdued to gain the advantage of the bears.

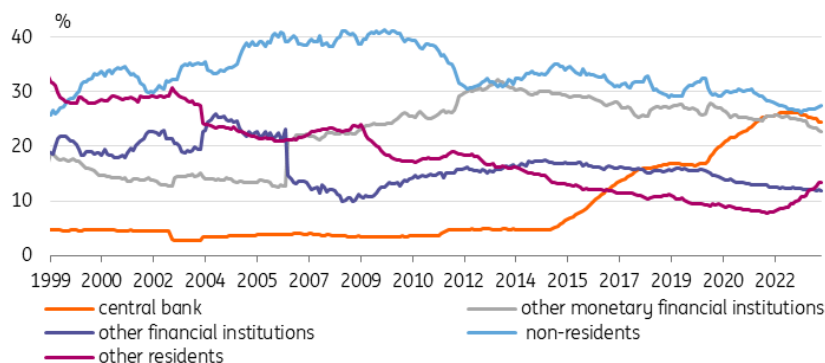
Eurozone periphery bond spreads had another good day

Spreads of eurozone periphery bonds over their German counterparts witnessed another day of strong tightening on Monday. Some of it can be attributed to sentiment having been bolstered by the positive rating action on Portugal by S&P over the weekend. But the outperformer was Italy where the key 10Y spread is closing in on the 140bp threshold. We will have then reached levels which since 2010 have only been undershot more lastingly during times where the ECB was actively buying bonds.

The situation now is clearly different. The ECB is running down its bond portfolios and by the end of the year also the reinvestments for the Pandemic Emergency Purchase Programme will have ended. But Italy has also been diversifying its investor base into the retail segment with another large BTP Valore issue of €18.3bn over the past week. By historical standards Italy still has room to expand that share. At the end of last year the share of Italian debt held by "other residents" – which includes households – was 13.4% coming from a low of 7.8% in early 2022. But in the early 2000s it was closer to 30% and dropped below 20% only in the wake of the global financial crisis.

So far markets have stuck with the positive stories. But headlines like the upward revision of the 2023 deficit to 7.2% of GDP from a previously envisaged 5.3% target highlight remaining risks. The large transfers to come from the EU's resilience fund are also fraught with implementation risks, something rating agencies are following closely. And on the political timeline all eyes are on the EU parliamentary election. Further smooth sailing is not guaranteed. The implication goes beyond periphery spreads and could also pose a headwind to the so far relentless underperformance of Bunds versus swaps.

Holders of Italian general government debt (in percent)



Source: Bank of Italy, ING

Tuesday's events and market view

After a quiet start to the week Tuesday's data slate is looking busier. In the eurozone we will get the January PPI figures. We will also get the final February services and composite PMIs, which also means first readings for Italy and Spain.

In data highlights are the factory orders and the ISM services. The latter should also help firm up expectations for Friday's jobs data. US political observers are focused on 'Super Tuesday' where numerous states hold primary elections.

Germany mandated a 30y bond tap via syndication, which should be Tuesday's business. In regular auction supply Germany also reopens a 5Y bond for €4bn, while Austria taps 6Y and 10Y bonds for a total of €2bn.

Author

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

Benjamin Schroeder

Senior Rates Strategist

benjamin.schroeder@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.