

Rates Spark: Just assume tariffs are for good

Lots of talk of tariff "uncertainty" through Tuesday. There is no uncertainty. Tariffs remain and will remain. Rather upward pressure on longer-dated yields has become a global thing. And the Lisa Cook affair remains an issue for both ends of the US curve. Although in the eurozone, hawkish repricing of the front end is limiting steepening



Tariffs are not the driver of bonds, but in any case steepening from both ends is still the way to go

On the appeals court ruling that a rump of the Trump administration tariffs are illegal – don't lose sleep on interpreting what it means. The simple and straightforward way to view this is tariffs remain in place, and will remain in place going forward. It is true that the ruling could well make its way to the Supreme Court for a final look. But then again it might not. That's up to the Supreme Court. But if it did, and the Supreme Court agreed with the lower court ruling, even then, continue to assume that the tariffs remain in place.

Why assume this? First, there is no plan B. The Trump administration is all in on macro management via tariffs. Second, President Trump has other avenues within which he can exert tariff control, based off balance of payments positions or national security issues. Third, and most important, Congress can grant additional tariff powers to the executive branch through new

legislation, and this particular Congress is very likely to do what it needs to do to ensure continuation of existing tariff policy.

For all of these reasons, we are firmly of the opinion that the market movements on Tuesday (following the Labor Day holiday), had very little to do with tariff "uncertainty". It had more to do with a general trend with long-dated bond yields, and an echo of the Lisa Cook affair that continues to remind us of the attempted prodding of Federal Reserve to cut rates. While it's true that many agree that rates should indeed be cut (Chair Powell is now effectively one of them), the Lisa Cook push still feels a step too far, even if in a way with some justification.

That all being said, we remain of the opinion that path of least resistance is for the curve to continue to steepen from both ends.

New records for 30Y government bond yields

Globally, the long ends of yield curves remain under upward pressure amid a mix of fiscal concerns and worries about central bank independence. 30y Bund yields pushed beyond 3.4%, the highest since 2011, while 30y gilts briefly rose above 5.7%, a new high since 1998.

Who takes the lead on a given day seems influenced by supply activity, in this case sterling rates with the launch of a new 10y benchmark gilt. The one that appears to defy the trend to ever new long-term highs is US Treasuries where 30y yields just turned the corner at the 5% mark, but are still well below the latest high-water mark of 5.15% from May.

If we look through the lens of 10s30s curves the global trend is clearer and also the US curve is reaching new longer-term highs these days. A politically motivated Fed cut should only add to the steepening pressure.

The EUR front end has actually moderated some of the recent steepening pressure

Further down the curve 10y Bund yields touched 2.8% on Tuesday, a level they had previously breached only briefly in the days following the announcement of Germany's fiscal U-turn. Some of the latest upward pressure relates to the front end, one could argue actually moderating some of the global steepening pressure spilling over.

The EUR front end is starting to look through any final ECB late-cycle adjustments. The trough in the strip of 1m ESTR OIS forwards lies around nine months out and only 15bp lower from current levels, thereafter rates are up again and above current levels beyond 18 month out.

The latest push higher came on the back of the flash CPI for August pointing to slightly hotter than anticipated (core) inflation – and of course on the back of earlier hawkish comments from executive board member Schnabel who does not see any need for a further cut – even pointing out more ominously that globally central bank rate hikes could return sooner than the market thinks.

As a consequence, the German 2y Schatz yield has inched up to just below 2% again, a level that hasn't been surpassed since after 'Liberation Day'. The question is whether the front end will find the confidence to look at the actual possibility of rate hikes in the near future. Remaining downside risks to growth and even the open debate on inflation leave it prone to correct lower again we

think. The curve as a whole could see steepening impulses from the front end.

Wednesday's events and market view

The eurozone sees releases of the final services and composite PMIs for August alongside the producer prices for July.

The US will look at the JOLTS data for additional clues about the state of the jobs market ahead of Friday's official labour data.

No auctions were scheduled for Wednesday, but Lithuania has used this window to mandate the sale of new 10y and 20y benchmarks.

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