

## Rates Spark: More of the same is needed

The FOMC outcome was mixed. Rate cuts are still coming, but on a delayed path from the perspective of the Fed's dots. But nothing happened from the FOMC to negate the now dominant preference to continue to build a rate cut discount. That pitches 4% as a viable target for the 10yr yield. But if the inflation data fails to sit at 0.2% MoM, then 5% still looms as a risk



### Treasuries are on a rate cut-build path unless negated by data/events

Post the more subdued 0.2% month-on-month core consumer price inflation reading, Treasuries have been re-cobbling together the string of weaker observations seen in the past few weeks, and downsizing the importance of the firmer ones. We're back to the build of a rate cut bias, as had been seen in the couple of weeks prior to the firm payrolls report. The 10-year is back in the 4.3% area, and the 2-year at 4.7%. The target for both would be 4% should a rate cut theme really build. The only real issue is timing, especially with the Fed dots now down to just one for 2024.

If the stars align and the Federal Reserve does cut by September, the twist is that there is not a whole lot of room for the 10-year to stay below 4% for too long. If the Fed just gets to 4%, that would imply no term premium in the 10-year and a completely flat curve. Add the large fiscal

deficit to the equation and we'd ultimately need to see a material term premium in the area of 100-150bp. That easily brings a 5% yield back into the conversation. But 4% first, provided the data behaves and allows for the build in the rate cut discount, in particular for 2024 delivery.

Meanwhile, liquidity conditions remain ample but on a tightening trend. The past couple of months saw volumes going back to the Fed stalling the area of US\$400bn. Extrapolate that and bank reserves will shrink, which will tighten liquidity conditions in a wider sense. The Fed continues to voice a broadly agnostic stance on all of this. This is mostly as the central bank is pre-positioned given the tapering in quantitative easing is already in place. As an aside, liquidity in Treasuries has deteriorated, adding another layer of issues that can spike volatility ahead.

## Today's events and market views

Markets are likely to remain particularly sensitive to US data, even if more optimism should be baked into the curve following the CPI reading yesterday. Of interest should be the PPI data for May, where also many elements feed into the Fed's preferred inflation measure – the PCE is due on 28 June. The initial jobless claims, also up for release on Thursday, have recently nudged up slightly, adding to the sense of a cooling jobs market even as the latest non-farm payrolls figure surprised to the upside. Calendars are quieter on the European side, with only industrial production data to note.

In primary markets, Italy is scheduled to sell a new 3-year bond alongside reopening of three other bonds out to the 30-year maturity, all in all for up to €9bn. Focus will later turn to the US Treasury re-opening its 30-year note after Tuesday night's strong 10-year auction triggered a notable rally in rates.

## Author

### Padhraic Garvey, CFA

Regional Head of Research, Americas

[padhraic.garvey@ing.com](mailto:padhraic.garvey@ing.com)

### Benjamin Schroeder

Senior Rates Strategist

[benjamin.schroeder@ing.com](mailto:benjamin.schroeder@ing.com)

### Michiel Tukker

Senior European Rates Strategist

[michiel.tukker@ing.com](mailto: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](http://www.ing.com).