

## Rates Spark: More weakness needed for 50bp Fed cut

Firm US data has offset some of the recent declines in US Treasury and Bund yields and makes a 50bp cut in September less likely. Key upcoming US jobs data may tilt the balance in terms of cuts. For the European Central Bank, the need for aggressive cuts is even less probable and markets now see 65bp of cuts in 2024, which makes two more 25bp cuts the baseline



### Fed cuts are coming, but is it 25bp or 50bp?

The dip towards 3.8% for 10-year UST yields proved short-lived. A batch of firmer data, [from retail sales to initial jobless claims](#), pushed the yield above 3.9% again. The move was also accompanied by risk assets perking up again which comes amid the VIX continuing its slide lower as the ructions from early August wash out from the system.

The curve bear flattened as the US front end is pricing out expectations of an initial 50bp cut from the Federal Reserve. The implied probability for such a bigger move is now down to below 20%. The base case is now 25bp easing in September with a bit over 90bp of easing discounted until year-end.

That rate cuts are coming looks more certain and the Fed will likely use the upcoming Jackson Hole symposium to cement those views. That will likely continue to put a broader downward trend on rates, especially the front end. More near term though the question now centres on the size of the first cut. While the recent data has the market leaning towards 25bp, our economist would not rule out a larger 50bp cut just yet. Key will be the next jobs data early in September ahead of the Fed meeting.

## Aggressive pricing of ECB still appears more US inspired than fundamentally justified

Eurozone rates are following the US dynamic, as usual overall more muted in absolute terms. Nonetheless, the 10Y Bund yield rose well above 2.2% again, underperforming versus swaps which is also reflecting the improving risk tone. Similarly, sovereign spreads narrowed further. 10Y France over Germany is edging closer to 70bp, where it stood just ahead of the market gyrations early August.

As for the ECB pricing, the market is also moving back from a “three-more 25bp cuts” scenario. With 65bp it is still just about the base case. While the aggressive pricing was certainly inspired by the US moves, the backdrop for aggressive ECB easing remains less clear. Stories like those of a study showing that German real wages are still advancing at the fastest pace in a decade are but one example.

### Today's events and market views

After a data heavy week, Friday will have less on the agenda. From the US we have housing figures, which are expected to show some cooling. The Michigan sentiment index is expected to remain around current levels. UK retail sales numbers this morning came broadly in line with consensus.

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