

Rates Spark: No big surprises from US CPI

Markets are content with a 0.2% US core CPI reading and risk sentiment is now almost back to where it was before the recent turmoil. The number itself doesn't justify a 50bp cut by the Fed in September, but a further deterioration of the jobs market would argue in favour. In the near term we still see global yields going lower



Markets got their 0.2% US core CPI

We got what we wanted – a 0.2% month-on-month core [US CPI reading](#), well in line with economists' expectations. And yet, still markets jumped around a bit on the release. Yields moved up a few basis points across the curve initially; the 2-year even almost touched 4.0% again, and that while a 0.2% is good enough for the Fed to start cutting. Later in the day the curve came down again and ended slightly flatter than before.

Market pricing still shows a significant probability of a 50bp cut priced in for September, which this reading itself would not necessitate, and could explain part of the market reaction. This means that a 50bp cut would have to be wholly driven by the weakening labour market, for which the signs are slowly dripping in, but a full deterioration is not there yet. In effect, the pricing for a September cut was reduced by about 2bp post release.

Risk sentiment almost back to normal

Part of the initial rise in yields may also be attributed to a relief in risk assets, which have been holding their breath after last week's turmoil. The VIX dropped another point and is now close to levels from before the recent risk-off episodes. Implied rates volatility is still above the previous lows in July, but yesterday brought another sharp turn lower. Overall these indicators suggest risk sentiment is almost restored.

In the near term we still see the broader direction of yields lower as the first Fed cuts start closing in. With risk sentiment normalising, the potential from higher rates through the risk premium channel is now also more limited. Bund and Gilt yields are likely to follow USTs lower, and [yesterday's lower UK CPI](#) accelerated Gilts in that direction.

Today's events and market views

From the US we have plenty of data coming in, including retail sales, industrial production, capacity utilisation and jobless claims. Jobless numbers were able to move markets last week, but with plenty of other data to watch that may not be the case this time. Industrial production and retail sales will provide additional gauges on whether the economy is indeed cooling down rapidly.

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