

Rates Spark: the novelty is wearing off

Unlike last week, rates largely shrugged off positive vaccine news. It appears that only a turnaround in the pandemic trajectory would allow markets to react with more conviction.



Vaccine

Source: Shutterstock

Overnight: central bank easing looks to be here to stay

ECB chief economist Lane confirmed that credit conditions will remain easy as long as the pandemic crisis lasts. He dismissed call to provide guidance on the increase of quantitative easing (QE) markets are expecting at the December meeting. Two other board members, Mersch and De Cos, were more specific, saying asset purchases (PEPP) and emergency loans (TLTRO) are the main tools likely to be recalibrated.

From the Fed, vice chair Clarida seemed more circumspect about the need of further easing in the near-term although he stressed the central bank is ready to use all the tools at its disposal. Despite similar near-term headwinds in Europe and the US, these comments underscore the reason why EUR and USD rates can diverge further.

Vaccine moment, shrugged

As we wrote since last week, rates find themselves caught in the crossfire of two opposite covid-related risks: vaccine progress and a worsening pandemic in some places. One of those risks materialised yesterday in encouraging interim results for Moderna's vaccine, only one week after similar reporting from Pfizer. The market's muted reaction confirmed something we have

suspected: the novelty is fading fast and investors likely have already included prospects of a vaccine in their economic outlook.

As one could have expected, USD rates have reacted more sharply than EUR on account of their greater volatility, but also because a reversion to the pre-covid regime would entail higher USD rates, and a wider spread between the two. Nevertheless, the muted reaction in both currencies was short-lived despite the fact that good vaccine news is 'additive', in the sense that two vaccines are better than one, that the Moderna vaccine has a reported efficacy even higher than the Pfizer one, and as it seems it poses fewer logistical challenges in its distribution.

This is unlikely (we hope) to be the last good news on that front, but we suspect investors in safe havens can afford to be more relaxed about the risk. What led markets to get over the results so quickly was the wave of additional social distancing measures, so we argue that only a turnaround in the pandemic trajectory would allow the market to celebrate good news with higher rates.

Today's events: US retail sales and IP

The economic calendar is mostly US-centric this morning. Retail sales, industrial production, and builders optimism are the main releases of note.

Central bank speakers include Lagarde.

Italy has mandated banks for a 5Y USD issue yesterday. This would add to a 2Y Germany auction.

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