

Rates Spark: Path to higher euro rates is almost cleared

As expected, yesterday brought [no cut from the ECB](#), but the press conference did leave us with a hawkish aftertaste. After a series of decent PMIs, the ongoing trade tensions are the only remaining hurdle for rates to test higher. A trade deal would enable the 10Y euro swap rate to push for levels closer to 3%



More and more support for higher euro rates

ECB President Christine Lagarde happily emphasised that the European Central Bank was in a 'good place', giving a signal that a cut in September will probably not be necessary. Markets reduced the probability of a September cut from 50% to 25%, although they seem to agree that the ECB will have to cut to 1.75% eventually. The key uncertainty remains the ongoing trade tensions, which still bear the risk of escalation involving retaliatory measures from both sides.

After good PMI numbers and a positive tone from the ECB, the path towards higher rates is becoming even clearer. If a trade deal gets signed, we should see rates move up further, with the 10Y swap rate hitting at least 2.8%. The stretch towards 3% should be slower and will be contingent on growth numbers continuing the upward trend. Passing the 3% mark would probably require the impact from fiscal stimulus to show in the data, which may not be until later in 2026.

On the other hand, we do also have to deal with disinflationary risks, partly because of base effects

and partly because of the stronger euro. The ECB is opting to look through these and focus on the projections, but the question is whether markets can do the same. The 10Y inflation swap stands at exactly 2%, which is still on the low side when considering an inflation risk premium of around 30bp. This signals that markets remain wary that maintaining inflation at target is not a done deal.

Friday's events and market views

From Germany, we'll first have the Ifo survey results, which should support the improving business sentiment. The ECB will publish the numbers from the survey of professional forecasts, but these are usually not market-moving. Later in the day, we have the durable goods orders coming in from the US, which will be watched closely for signs of weakness.

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