

Rates Spark: Payrolls Friday looms

The market is running 10y USTs at 4.3% into a US payrolls figure with a 105k consensus – its lowest read since 2020. There is a lot to explain low levels away, but it seems the market may welcome an excuse to sell bonds just for a bit ahead of the elections where the trade has been higher yields into a Trump win. In EUR, the long-end is sensitive to US data



How low of a payrolls number can no longer be explained away by special factors?

Over the past 10 days it's been intriguing to see the "to and fro" in the consensus payrolls estimates for the October report. At one point there was a 140k report anticipated. It has been as low as 100k, and now on the verge of the release, it's at 105k. If it is 105k it would be the lowest reading since 2020 (the pandemic crescendo). But then again, interpretation can be tough. Is it low as the previous one was high, so there's an equalisation? Is it low due to miscellaneous October strikes? Or is it purely hurricane impacted? The latter aspect is the most telling. Yet, the ADP report, for the same month, was strong.

Yet again, we head into a payrolls report that has significant capacity to surprise the bond market.

If the ADP is to be believed, it will shock the markets to the upside. If the hurricane narrative dominates, a lowish number (at or around consensus) arguably should be less impactful for bonds, as it can be explained away. But if it's really low (say 50k or below), then it's hard to not have a material reaction lower in bond yields. The kicker is its just ahead of the presidential election, where the trade is for yields to test higher on the Trump win that the market is intent on pricing. It feels like the market could welcome an excuse to sell bonds just for a bit. But let's see the number first.

Our view? We see good reason it could be on the low side, but arguing why that is the case with the ADP ringing in our ears makes that a non-conviction call.

Back-end of the euro curve remains more sensitive to US macro data

The European Central Bank has revealed a reaction function more focused on growth and thus the hurdle for EUR data points to move the market is higher. Eurozone CPIs surprised to the upside, yet euro rates did not seem to be too fazed by this. [Unemployment in the eurozone](#) even ticked lower, but also this did little to distract markets, given many of the forward-looking indicators point at a cooling economy. The focus of markets is clear: US payrolls first and then the elections.

The 10Y ESTR OIS swap rate is now around 2.3%, well below the US SOFR 10Y of 3.8%, but the gap has narrowed slightly in the past few days. The back-end of the EUR curve is still closely correlated with US moves, especially for those driven by economic data. For moves related to the election there are fewer spillovers, as a Trump victory could see a flight to quality in the eurozone, dragging down euro rates.

Looking past payrolls and into next week, a Trump victory could push markets to frontload ECB cuts even more given that President Christine Lagarde already highlighted Trump-related risks during the last meeting. The probability priced in for a 50bp cut in December has come off from earlier peaks, but is still a good 20%. In our view, this week's data does not warrant the need for accelerated cuts. We still think a 50bp cut in December is unlikely, even in the case of a Trump victory, but we wouldn't push back against market pricing until we get a clearer view after the elections.

Friday's events and market view

US payrolls will be key for market direction. The median forecast sees them coming in at 105k, but everything from -10k to 180k is represented. It is the highest standard deviation around estimates since the January payrolls figure. The unemployment rate is expected to stay at 4.1%. The other data point to watch is the ISM manufacturing index. A slight uptick is expected, but it should again remain well in contractionary territory. The eurozone calendar is empty with many states out for All Saints Day.

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