

## Rates Spark: Higher PCE inflation would keep the 10yr target at 5%

Today, we see the final April reading for US inflation, which is shaping up for confirmation of 0.3% month-on-month as a central outcome. That's too high for (Fed) comfort. Treasuries really need a 0.2% MoM reading, otherwise the path remains in place for a move towards 5% on the 10yr



### Direction for US Treasuries all on today's PCE deflator outcome

There is a chance we could see a 0.2% MoM outcome on the PCE deflator. The consensus is for 0.3%, but it's a close call. The details show the average running at 0.26%. Statistically, that's practically just as likely to round down to 0.2% MoM. If it does, it could be pivotal. For the bond market to rid itself of the bear dominance, it needs to see the start of monthly 0.2% outcomes. That can help avert further imminent moves to the upside for longer-dated bond yields.

But if we get what's expected - 0.3% MoM - we remain on a path towards 5% on the 10yr Treasury yield.

If realised, a (surprise) 0.2% MoM outcome could begin a run of them, which could be significantly bullish for bonds. However, a sneak preview of the core CPI reading for May, which is due in a few

weeks, has a 0.3% MoM expectation. This wouldn't be good. It would mark a run of five months with 0.3% or higher MoM outcomes. It keeps the pressure on market yields to have a bias to edge higher for another few weeks at the very least.

This week, some tailed auctions have added to the sense of bond market angst. It has not quite unravelled, but it has the potential to do so. Our central premise is that we're at or about normal yields now for the 10-year. This bond market really needs a break from a decent inflation reading to prevent it from sliding down the slippery slope that could see yields head north.

## **Eurozone flash CPI is unlikely to alter the picture of a 'hawkish' cut next week**

The eurozone has its own piece of inflation data to digest ahead of the policy meeting next week. Given prior country releases, markets normally already have some handle on what to expect. After a slightly hotter Dutch inflation figure, there is still a French reading to take into account this morning. Overall, there remains a bearish undertone for the market as the anticipated eurozone core CPI rate of 2.7% is still high. On top of that, Thursday has again seen somewhat better data with economic confidence in the eurozone rising – typically this has a good correlation with growth – and unemployment also falling to a new record low.

While an ECB cut next week still looks like a done deal in the eyes of the market, the communication surrounding it could turn out more hawkish. The probability for a follow-up cut in July is around 10%, but by October, a second cut is still fully priced in. A third cut before the end of the year is currently hanging in the balance.

### **Today's events and market view**

We're at the end of the month, which could cause some volatility around rebalancing flows. The key piece of data is the PCE inflation out of the US, where the market consensus is close, split between 0.2% or 0.3% for the crucial month-on-month core reading. Watch out, too, for personal income and spending data. In the eurozone, we will get the flash CPI estimates, where the headline rate is to nudge slightly higher to 2.5% from 2.4% while the core rate stays at a still elevated 2.7% year-on-year. Some focus will be on possible rating action tonight, with S&P having France (AA/Negative) on its review schedule.

Regarding central bank communication, the ECB has already entered its black-out period before next week's policy meeting. The Fed will enter its own at the weekend, allowing for some final messaging. However, no speakers are scheduled for today.

## Authors

### **Padhraic Garvey, CFA**

Regional Head of Research, Americas

[padhraic.garvey@ing.com](mailto:padhraic.garvey@ing.com)

### **Benjamin Schroeder**

Senior Rates Strategist

[benjamin.schroeder@ing.com](mailto:benjamin.schroeder@ing.com)

### **Michiel Tukker**

Senior European Rates Strategist

[michiel.tukker@ing.com](mailto:michiel.tukker@ing.com)

## Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. (“ING”) solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.