

## Rates Spark: Rate cuts pushed back again

The latest data shows that a full-blown global easing cycle is still a long shot. The pricing for European Central Bank cuts in 2024 is down to 60bp, which means two cuts are now deemed more likely than three. And the pricing could go even lower in our view. For the US, the case for higher yields based on the latest figures is even stronger



### Rate cut expectations fall further on good economic data

Yesterday's data was another reminder that the timing for a full-blown global easing cycle is still a long shot. First, we had the eurozone PMIs maintaining their upward momentum and cementing confidence that growth is recovering in the region. Manufacturing numbers remained below 50 but exceeded expectations by good margins. Then US PMI numbers were even more impressive, with manufacturing back above 50 and the composite index jumping from 51.3 to 54.4. The services PMI made a similar jump up, which was a relief given that the ISM equivalent showed a large decline in its last reading.

We have argued before that euro markets will focus more on growth dynamics now that inflation is slowly coming down. In our view, the momentum in eurozone PMIs can continue into the second half of this year, reducing the need for imminent rate cuts. The gradual pickup in growth cannot be ignored and yesterday's uptick in ECB wage numbers was a stark reminder that the battle against

inflation is not over.

The trend of pushing back against rate cuts – which has been going on since January – continues. Yesterday's price action was led by the 2y point on the curve, for both euro and dollar rates. The pricing for ECB cuts in 2024 is down to 60bp, which means two cuts are now deemed more likely than three. The momentum in the economic data is simply not supportive of rate cuts beyond June. As long as the eurozone continues recovering and inflation numbers show signs of stickiness, markets are unlikely to change course and we can expect short-end yields to still move higher from here in the near term.

For the US, the case for higher rates from these numbers is even stronger. Inflation numbers have come in hot for multiple readings, so better macro data will only add to the yield pressures. The jobless claims numbers yesterday were also strong, so it's not just the PMI survey data that portrayed a resilient economy. Correlations between the back end of US and euro curves have been tight these past months and thus we can expect higher UST yields to spill over to Bunds.

## Elections called in the UK but markets unfazed for good reason

In the UK, the surprise did not come from PMIs but rather PM Rishi Sunak calling elections for 4 July the night before. Having said that, markets [can be quite relaxed](#) by the news as this time the elections likely offer less excitement than previous ones. In our view, Gilt yields have been trading higher than we deem fair value since the beginning of the year and the 5s10s is still steeper than for UST and Bunds, both suggesting some risk premium is already built in. Given the benign expectations, we maintain a downward bias for outright Gilt yields.

### Today's events and market views

A data-light Friday as usual. The highlight will be US durable goods orders, which are expected to shrink by 0.8% month-on-month. But given that this series is quite noisy the reading can be difficult to interpret.

Among the ECB speakers are Isabel Schnabel, Joachim Nagel and Pablo Hernández De Cos, together making a nice lineup. The Fed's Christopher Waller will discuss  $R^*$  which can always provide interesting insights into the expected terminal policy rate.

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