

Rates Spark: Rate markets have shifted focus from inflation to jobs

US CPI numbers were hotter than expected but didn't distract markets from focusing on the deteriorating labour market. The ECB will cut by 25bp and we'll be listening for forward guidance about the possibility of an October cut (we don't expect one). The ECB's main refinancing rate will undergo a technical tweak which won't impact market rates



European Central Bank
President Christine
Lagarde

Upside surprise to US CPI, but doesn't distract from focus on jobs

Only a few economists had predicted a 0.3% month-on-month core CPI reading in August and thus markets were surprised by this figure. The pricing of a September cut is now 28bp, so a 25bp cut clearly has preference. Nevertheless markets were not completely spooked by the uptick which shows that the deterioration of the labour market is the new focus. The yield curve remained disinverted, albeit barely, with the 2Y10Y flattening to just 2bp.

PPI data on Thursday is the next input in shaping inflation expectations, but the weekly jobless claims numbers could end up drawing more attention. Last reading was well in line with consensus and this time expectations are for the number to remain stable. With lingering concerns about a

sharp deterioration of the jobs market, a significant downside surprise could persuade markets that a 50bp cut in September is still a possibility.

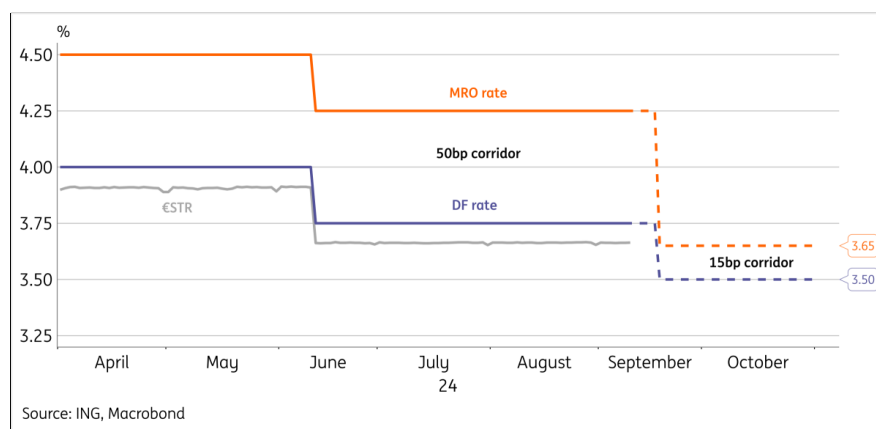
ECB will cut again, but a consecutive October cut seems unlikely

All economists on Bloomberg predict a 25bp cut by the ECB, and here markets will certainly not be caught by surprise. More interesting may be the forward guidance with which the cut is delivered, although [we don't have high expectations](#) about this. Instead, the ECB is likely to just reiterate the data-dependent approach and leave the path forward completely open.

Looking ahead, markets are still pricing in around a 40% chance of another cut for October, which in our eyes is highly unlikely. If Christine Lagarde emphasises the importance of quarterly projections during the communications then that percentage could diminish considerably. Only a severe deterioration of the economy would warrant an October cut, but given the limited amount of additional data available by then this chance seems negligible.

The ECB will also narrow the corridor between the main refinancing rate and the deposit facility rate from 50bp to 15bp, as part of the broader review of the operational framework. This should be seen as a technical adjustment and not a loosening of monetary policy. With plenty of excess liquidity in the system, the deposit rate is the important policy rate for now and thus market rates (i.e. ESTR) should not be impacted by this tweak.

ECB will tweak the main refinancing rate, but this shouldn't impact market rates



Thursday's events and market views

Besides the ECB's policy rate decision, we have US PPI numbers. The PPI excluding food, energy and trade is expected to come in at 0.2% MoM, which should help inflation converge towards the target.

Supply includes 3Y & 7Y BTP auctions from Italy (totalling €6.5bn), and Ireland with a 7y green bond and a 10y bond, for a total of €1bn. Later in the day, we have the US with a 30Y Bond for \$22bn.

Authors

Michiel Tukker

Senior European Rates Strategist

michiel.tukker@ing.com

Benjamin Schroeder

Senior Rates Strategist

benjamin.schroeder@ing.com

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@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>.