

Rates Spark: Things are lining up for the doves

Friday's economic data could help build the case for more dovish market pricing. In the US, markets may start assigning a higher probability to a July cut. A stronger euro adds to the disinflationary forces at play and could push markets to consider a 1.5% landing zone again



Earlier Fed cuts could have dovish spillovers to the eurozone

The dovish vibe in US rates markets may be fuelled further by Friday's personal spending and PCE inflation data. The core PCE is likely to be just 0.1% month-on-month, which would by itself support a cut as early as next month. Of course, the fear of tariff-related inflation is not yet over. But if the personal spending numbers from May show significant weakening on the back of worsening consumer sentiment, then markets should be willing to increase the chance of a July cut. Right now, the probability already stands at around 25%, and with payroll numbers next week, a lot can still happen.

Lower US rates helped the dollar weaken and consequently pushed the euro stronger, weighing down on the eurozone's inflation outlook. The European Central Bank is well aware of the disinflationary impact a stronger euro has on its macroeconomic projections. Not only does a

stronger euro cheapen imports, it also poses a growth headwind through the exports channel. And with oil prices coming down significantly, the downside risks seem to dominate the inflation outlook at the moment. Friday's CPI numbers from France and Spain should confirm the mild inflation backdrop.

In the near term, we therefore expect the short end of the rate curves to contemplate an ECB landing zone of 1.5% again. With the 90-day tariff pause set to end on 9 July, there could be more volatility related to trade tensions, keeping the doves well fed. Meanwhile, the more hawkish German spending story won't move to the foreground until after a deal has been settled. The 10Y Bund yield already trades very close to 2.6%, which we consider the upper limit for now.

Friday's events and market views

We start the day with French and Spanish CPI numbers. For France, consensus sees a low 0.7% year-on-year headline inflation number, whilst for Spain this is 2.2%. Eurozone confidence indicators are expected to show little movement in June. From the US, the personal spending numbers will be closely watched, with the expectation of just 0.1% growth in May. Thereafter, we have PCE inflation data and the Michigan sentiment indices.

From Italy, we have auctions for 5Y and 10Y BTPs and a 9Y CCTeu for a total of €8.5bn.

Author

Michiel Tukker

Senior UK & Eurozone Rates Strategist

michiel.tukker@ing.com

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