

## Rates Spark: Trump's bitter liberation

The biggest market impact from Trump's tariff announcement was felt by US assets, but it also led to a decline in eurozone equities and a rise in Bund futures. Looking ahead, we remain cautious about the fragile risk sentiment and adopt a tactical bullish stance on 10-year Bunds. The short end of the euro swap curve is more anchored



Trump shows an executive order on 'reciprocal tariffs' at the Rose Garden of the White House in Washington D.C.

### Markets clearly not pleased and rates impact is complex

Markets did not like the list of tariffs Trump presented yesterday, and the numbers [appear worse](#) than feared. The S&P 500 futures are down more than 2% from Wednesday's open and the UST 10Y yield came down from 4.20% to just above 4%. European markets saw the STOXX futures down 2.5% this morning, while the 10Y Bund future points to a 9bp drop in yields.

Looking ahead, the potential [impact on eurozone](#) growth is clearly negative, but the impact on inflation is more ambiguous, adding complexity to the rates outlook. Whilst the reduced growth outlook is a negative, the inflation impact will partly depend on the EU's reaction in terms of reciprocating the US tariffs. Proportional counter-tariffs would warrant more upside inflation risks in the near term.

We think markets will predominantly focus on the growth impact for now, warranting downward pressure on euro rates. Even if Trump decides to reduce the eventual percentages as negotiations

take shape, the uncertainty and confidence shock are enough to weigh on the economy with immediate effect. Inflation, on the other hand, is difficult to quantify and will take more time to show up in the data.

## The back end of the curve is where the action will be

The potential inflationary impact, however, prevents the short end of the euro curve from dipping lower. Markets have been rangebound to an ECB landing between 1.75% and 2% for six months now and are unlikely to break higher or lower for the time being. Markets may see the ECB moving towards 2% sooner, which would require two more 25bp cuts, and could be reached as soon as June. We expect less confidence for the pricing of a third consecutive cut.

Most action may, therefore, be at the back end of the curve, which is more sensitive to the shifts in risk sentiment. As we expected, the announcement leaves many questions unanswered, and thus a return in risk appetite will have to wait. We think Bunds can outperform swaps from current levels as investors seek safe assets to hedge their portfolio risk.

From a structural perspective, we still see room for euro rates to end higher by the end of this year. The EU spending plans support the growth outlook, which means the ECB won't have to cut into supportive territory. Meanwhile, supply pressures keep yields supported from the back end of the curve.

## Global risk sentiment still has potential to worsen

The [biggest market impact was still in the US](#), although it's easy to see the risk-off sentiment spreading more globally. China may play an important role in this, given that tariffs surged and are now close to the 60% Trump threatened. The previous retaliatory reaction from China was relatively muted and of a more symbolic nature, but we think the next [response will be stronger](#). Increasing tensions between the two would be a recipe for more volatility.

Risk sentiment in the eurozone is also being challenged, but measures like credit spreads and implied volatilities don't look stretched when looked over a longer horizon. An intensification of the trade wars can therefore still move markets significantly. If, for example, an escalating tit-for-tat strategy between the EU and China follows, then a global flight to quality could very well see flows towards safe havens, including USTs and Bunds.

### Today's events and market views

Markets will likely need the day to absorb the tariff news. In terms of data, the European morning will see Spanish and Italian PMIs, but markets will likely not place too much emphasis on these unless a significant undershoot amplifies the downbeat risk sentiment. The same can be said for the eurozone aggregate PPI numbers. More attention will likely be paid to the US ISM services indices later in the day. The headline index is expected to nudge down from 53.5 to 52.9. A lower number than consensus would add to the recent series of weaker US data readings and would weigh on UST yields.

From the European Central Bank, we have Isabel Schnabel speaking at an OECD event, but it's not sure whether she will provide any comments on Trump's announcements. In addition, we'll receive the minutes from the March meeting, which may tell us more about the inclination towards another cut in April.

Meanwhile, Spain will auction 3y, 6y and 14y SPGBs together with a 6y SPGBi for a total of €7.25bn. From France, we have 9y, 10y and 31y OATs for €12bn. The UK has scheduled a 15y gilt auction totalling £3.25bn.

## Author

### Michiel Tukker

Senior European Rates Strategist

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

### Padhraic Garvey, CFA

Regional Head of Research, Americas

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

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