

Rates Spark: Trump wants a lower 10yr yield too!

The latest Trump administration angle is for rates to be pushed lower through downward pressure on the 10yr yield, through lower inflation and a lower fiscal deficit. Achieve that and we'd agree. But achieve it first. Meanwhile, the Bank of England is likely to cut by 25bp, in line with market pricing. Going forward we see more GBP curve steepening



The US 10yr yield finally breaks below 4.5%, with a little nudge from Treasury Secretary Bessent

The US 10yr finally broke below 4.5%. It did feel like it was coming. Mutual funds data has consistently shown buying of duration pressure since the turn of the year, and the inflation data in the guise of CPI, PPI and PCE have just about played ball over consecutive weeks, at least in the guise of tamer month-on-month rates. This also comes after a material rise in the 10yr yield since the Fed started its rate-cutting cycle, with the higher 10yr yield practically in sync with the downsizing of rate cut expectations. Back in September the funds strip was discounting a landing rate at 3%. Now its closer to 4% (or just under). And its been stabilising in that area.

Wednesday also saw the release of Scott Bessent's re-funding plans, which were bang in line with Janet Yellen's – so a status quo there, downsizing some fears for more long-dated issuance. Treasury Secretary Bessent went on to comment that the Trump administration is minded to inject downward pressure on the 10yr Treasury yield, and it was here rather than through the funds rate that the administration could achieve lower rates. Some weakish ISM survey evidence conveniently helped that trade on the day. But beyond that it is hard to see where the big driver is for a lower 10yr yield from the Trump administration, apart from perhaps some huge successes from DOGE.

We've been tactically bullish Treasuries in the past couple of weeks, so all of this is moving in our (short-term) direction. However, we also assert there is not huge room to the downside for the 10yr yield. An effective floor is in place at just under 4% as determinable from the funds rate strip. That floor can of course shift lower, but would need a better reason than an approaching 10yr rate. And the 10yr Treasury yield sits some 50bp over this. So enjoy the move lower while it lasts. Another 10-20bp and it will begin to look like its gone too far, and that's where the backup starts.

Bank of England likely to cut and we see more to come

We think the Bank of England will cut by another 25bp, bringing the Bank Rate down to 4.5%. Markets are already fully pricing in this week's cut but going forward markets seem less certain. The currently priced in terminal rate of 3.75% looks high and should be closer to 3.25% in our view. A repricing lower may take some time, however, since market concerns about inflation continue to linger. We see the numbers moving in the right direction and thus see room for the front end to move lower later this year.

We'll be watching the vote split for any surprises. In our view an 8-1 vote is the most likely outcome, whereby the arch-hawk Catherine Mann would be in favour of holding the current rate. If she decides to support a cut, then that would be a strong dovish signal. Should, on the other hand, we have fewer votes in favour of a cut, and government spending is flagged as a dominant force in the growth picture, then we would expect a more hawkish reaction from markets.

Longer-dated gilts remain very much driven by US dynamics and the 10Y yield of 4.4% actually trades at exactly the same level as 10Y US Treasuries. In the meantime, concerns about the fiscal situation keep upward pressure on the back end of the curve too. And QT doesn't help with the supply pressures. So with the long end of the curve anchored at elevated levels, we think the next move for sterling rates would be one of bull steepening.

Too much focus on the ECB's neutral rate?

European Central Bank expectations are testing lower again given the dovish signals from the wage data. Rather than taking it at face value, the data should be interpreted as corroborating the ECB's inflation picture. But the c.3% wage growth for end-2025 fits neatly in Chief economist Lane's notion that it aligns with the ECB's 2% target accounting for 1% productivity growth in the medium term.

With more indicators giving the ECB room for further cuts – and markets room to price them – that puts the neutral rate at the centre of discussions of how far the ECB can go. But it appears that the ECB is uncomfortable with the attention the neutral rate is getting, especially after Lagarde deflected questions on the topic by pointing to an upcoming staff paper to be published on Friday. On Wednesday Vice President de Guindos pointed out that using the neutral rate as a reference to determine the monetary policy stance was “not the right approach” and “not very useful”. The ECB

always needs to take in all data to assess the appropriate policy stance, and indicators such as the bank lending survey “provide a much better indicator of the restrictiveness”.

Thursday's events and market view

The Bank of England is widely anticipated to cut rates on Thursday. In the US market participants will get more indicators to refine their read of the jobs market with the Challenger job cuts data and the initial claims published ahead of Friday's official payrolls numbers. Fed speakers on Thursday include Jefferson, Waller and Logan.

Out of the eurozone we will get retail sales, and we will also watch the appearances of the ECB's Nagel and Escriva.

France and Spain will be active in government bond primary markets. France will auction a new 10Y benchmark, while also tapping 11Y, 13Y and 30Y bond lines, overall up to €13bn. Spain auctions 3Y, 6Y and 30Y bonds as well as inflation linked bonds.

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