Rates Spark: Trump’s government is now a fact

Markets may have "bought" the rumour and will proceed to "sell" the fact now that Trump's inauguration is a done deal. Even if UST yields come down, we still see structurally higher US rates. On his first day of his second term as US President, Trump declared energy and border security emergencies, but has not enacted tariffs – yet. EUR rates reacted with mild relief, but the ECB will still tread cautiously

Markets may sell the fact on Trump's inauguration, but we still believe US rates have not peaked yet

Markets may "sell" the fact, but we still see structurally higher US rates

With US President Donald Trump officially back in office, the question is whether markets bought the rumours but will sell the facts. The month leading up to Trump’s election in November also saw a significant rally in UST yields, but that move faded in the weeks thereafter. Similarly, rates have risen steeply over the past month as we approached inauguration day. Trump has made his ambitions for radical changes immediately into his presidency clear, but whether those plans can materialise is still more uncertain.

Beyond the possibility of markets "selling" the fact, we still argue for higher US rates from a structural perspective. Plenty of Trump's intended policy measures are inflationary, and failing to address the growing deficit adds to the upward pressure for UST yields. We see the 10Y UST peaking above 5% later this year, but setting a date for the peak is challenging. A lot will depend on Trump's prioritisation of policy measures and the timing of the subsequent macro impact.

EUR rates are watching Trump closely, with cautious relief

The start into the week was uneventful but tense in anticipation of Trump's inauguration. First, WSJ headlines during the day that Trump would not go ahead with tariffs on day one but rather take a more deliberate approach were reason for some relief, allowing yields to even close slightly lower on the day. The headlines were later confirmed by officials and "by Bloomberg quoting a not yet published fact sheet". And yet later in the day the threats of tariffs on Mexico and Canada resurfaced more prominently. In the past, Trump's actions have often been unpredictable, so markets might be forgiven for waiting on the official version.

That should also apply to the European Central Bank. Avoiding an immediate global trade conflict should also come as a slight relief for the immediate outlook, though that news will likely come too late for the survey data this week to reflect it. We will see a prominent slate of ECB speakers starting in Davos starting tomorrow, but we doubt that anything could be won by providing much more guidance and jumping ahead of Trump. The tone will likely remain more balanced as in the past days.

Isabel Schnabel had indicated over the weekend that the ECB should be able to cut rates further though might need to progress with more caution as one nears the zone of neutral rate estimates. On Monday, Austria's Robert Holzmann remained true to his hawkish reputation, calling a cut next week not a done deal (the market is pricing just over 24bp), but Croatia's Boris Vujcic remarked that he felt comfortable with current market pricing (the anticipated landing zone is around 2% by year end).

Tuesday's events and market view

The main focus remains on Trump's actions in his first days as president, which is also helped by data calendars offering little else – of note is the German ZEW index given that Germany's weakness is at the centre of eurozone economic concerns. EU finance ministers will gather in the shadow of the Trump administration's first days, where next to discussing EU competitiveness and solidarity with Ukraine, they are also expected to adopt the recommendations for member states that are currently under an excessive deficit procedure.

Primary markets are busier with a syndicated 15y French bond sale likely today's business. In terms of scheduled auctions, Germany is reopening two green bond lines. The UK is slated for a syndicated 15y gilt reopening.

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