Rates Spark: US payrolls more exciting than first ECB cut

The ECB announced the first rate cut, with euro rates only up a few basis points. With little concrete forward guidance from the press conference, euro rates will also be watching US data for signals justifying one or two more cuts this year. US payrolls today will grab the spotlight and in our view a consensus reading could bring UST yields higher

First rate cut by ECB brings little excitement

There it was, just as everyone expected, the first 25bp cut was announced by the European Central Bank. The cut is not an entirely uncontroversial one with many sounding the risk that the move comes too early against a backdrop of lingering inflation. But for the past months markets have been more focused on the potential easing path hereafter since the June cut was a given. Unfortunately we did not get much wiser about the path forward from Lagarde's press conference.

The 2-year euro swap rate jumped by around 4bp after the decision, which is a relatively muted reaction considering the symbolic weight of a first cut. The uptick could be attributed to the statement's mention of wage strength and slightly higher inflation in the inflation projections. The 10-year yield joined up and thus the 2y10y slope closed the day on the same level as the open.

Short-end rates don't seem to have a clear direction on where to aim for next, with markets divided on whether to expect one or two more cuts this year. We think the deciding push towards two more cuts, in September and December, will be coming from further US weakness. Any surprises in the US payrolls figures later today (either way) could therefore have a considerable impact on the short end of euro curves.

Rate markets set for US payrolls disappointment

US payroll figures will likely cause more excitement than the ECB cut. With US rates down significantly since last week, markets seem to be prepositioned for an economic disappointment. Consensus sees numbers coming in at 185k for the nonfarm payrolls for May, a touch above the 175k last month.

Any reading close to consensus, however, would in our view actually be a catalyst for higher yields. The number would be well below this year's average, but it would not reflect worrisome economic weakness. And with inflation still not where the Fed needs it to be, we think the 10y UST should see higher yields in that case.

Today's events and market view

US payroll figures will clearly take the most prominent place on the stage, but will have to share it with a number of ECB speakers. Austria's Holzmann is among the speakers, who was apparently the only Governing Council member in disagreement with yesterday's rate cut and will be keen to share his hawkish view. Centeno from Portugal will provide some balance and is known to be on the dovish side of the spectrum.

No notable issuance is scheduled.

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