

Where are we now directionally for the US 10yr?

We called the way up – it made sense to us. But the move on the way down has been a tad tougher. The pop in MoM inflation and risk-on are complications for the rate cut story. So, bonds need a weak payrolls report, else they're vulnerable. Weakness would be a sub-150k headline and a meaningful move to(wards) a 4% unemployment rate, and extrapolation of more



The move from 3.8% to 4.3% on the US 10yr coincided with an unwind of rate cut discounts. First no March cut, then no May cut and then 50:50 for June. The key drivers were: 1) retracement from what was perceived as a festive overshoot to the downside, 2) pops in January inflation readings (0.4% month-on-month) and 3) a firm January payrolls report (353k). It really started with the latter, which is why Friday's payrolls report is key.

The subsequent move in the US 10yr from 4.3% to sub-4.1% (currently) was kicked off by a core PCE deflator number that was high (0.4%), but better than many feared (the whisper was 0.5%), and the prior month was revised down to 0.1%. Since then, most data has been weak, allowing 10's to do its persistent drift lower in yield.

However, 1) the Fed is not budging on the cut narrative (no urgency), 2) we remain in a risk-on mode (antithesis to a rate cut narrative) and 3) we really need to see the February readings for inflation come at 0.2%, yet the discount for core CPI is 0.3%. The latter was why we'd been reluctant to call for the recent move lower in market rates.

Yet, the pendulum has swung to a clear re-build of the discount for a June cut, now knocking on the door of a 70% probability. The re-build correlated with the 10yr yield slipping lower of late. The 80% to 90% probability area is one where the Fed would be expected to deliver what's discounted. Getting there likely has the 10yr back below 4%. But there has to be some payrolls cooling first, and the 200k market expectation is not a cooling.

The market is trading in a way that sets itself up for a much weaker payrolls number (say 100k). If we get it, then fine, we sail below 4% on the 10yr. But if we get the market discount number of 200k delivered, we really don't have the ammunition to go below 4%. Theoretically a 200k outcome is as expected and should leave little market reaction. But we'd argue it would more likely be a catalyst for yields to back up again (report details notwithstanding).

Bonds need a weak payrolls outcome, else they're quite vulnerable. Weakness would be a sub-150k headline and a meaningful move to(wards) a 4% unemployment rate, and extrapolation of more to come...

Author

Padhraic Garvey, CFA

Regional Head of Research, Americas

padhraic.garvey@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and

which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.