EUROPEAN CENTRAL BANK

EUROSYSTEM

8 April 2025

ECB Bond Market Contact Group

7 April 2025
Summary of the discussion

1) Review of recent market developments

Members gave their views on market developments given the high volatility in recent days, following US President Trump's tariff announcements.

Despite the significant market movements members were of the view that market functioning remains orderly. Government bond market liquidity has held up well thus far, with only a modest widening of bid-ask spreads relative to the surge in volatility, with no amplification effects reported.

The absence of margin call-trigged forced selling by hedge funds was noted by members. This so far benign outcome was put down to hedge funds having entered the tariff announcement lightly positioned and seemingly well-prepared. Moreover members commented that repo market remained relatively calm, which was found to provide some reassurance.

Members pointed to an apparent disparity between policy makers' communication and current market pricing of rate cuts. This was deemed most acute in the US, where some members did not think the close-to-100 bps of rate cuts, which was priced at the time of the discussion, was consistent with the most recent communication by Fed Chair Powell. Other members interpreted the current market pricing as indicating that the disinflationary impact from lower growth would more than offset the inflationary impact of tariffs, especially over the medium to long term. The divergence in inflation dynamics across the Atlantic was also discussed, with the euro area experiencing disinflationary pressures, contrary to the US.

The group discussed the market's sensitivity to news having increased to very elevated levels. The extreme price swings on the day's trading session (Monday 7 April), which was driven by a false headline, was given as an example that highlights how "jittery" the market currently is.

Some members noted how investors were thinking about potential underlying shifts in the global order and how they may play out in markets, with some quite extreme tail risk scenarios being openly discussed by investors. The increased probability of a global recession was also noted, with some members highlighting that moves in commodity markets were pointing in that direction.

In terms of credit markets, members held differing viewpoints. On investment grade credit, some members highlighted that such bonds had performed quite well relative to equities. Other members cautioned that once the primary market re-opened it could trigger a re-pricing of secondary market levels. On high-yield assets, members were generally quite pessimistic noting significant spread widening and refinancing risks looming in some sub-sectors affected by tariffs.