Article | 17 August 2026 RATES SPARK

Rates Spark: Long-end risks, ECB conviction and UK data tests

Lower Fed hike odds have calmed front-end USD rates, but long-end Treasuries remain vulnerable to higher real yields, fiscal supply pressure and yen spillovers. In Europe, markets remain focused on a September ECB hike, while hawkish UK pricing faces key labour and CPI tests

Despite benign US CPI data, we think long-end rates remain vulnerable to the upside on higher real yields and a deteriorating fiscal position

Treasuries: A vulnerable long end

Last week's CPI data was benign, and markets have scaled back Federal Reserve rate hike expectations, with September hike odds now at just over 30% rather than 50% as seen ahead of the release.

Until we get to the Jackson Hole Economic Policy Symposium at the end of this month, a quieter calendar should also argue for less volatility from this angle. It will only be early next month when we get the next set of jobs and inflation data ahead of the September Fed meeting. This week we will see the S&P PMIs, where consensus expects a marginal softening. Overall, they should remain solidly in expansionary territory. Given they are also less influential than their ISM counterparts, they should not change the market's thinking unless there is a huge downside surprise. The FOMC minutes of the July meeting, released on Wednesday, might be more helpful for refining expectations as they should present the views of the broader committee.

While we continue to see scope for lower front-end USD rates as we still look for the Fed to eventually cut rates next year, long-end rates remain vulnerable in the meantime. Higher real yields and fiscal deterioration raising Treasury supply pressure can keep upward pressure on 10Y Treasury yields. We are also on the lookout for potential spill-overs from the yen story. We see yields still gravitating more toward the upper end of the recent range.

Bunds: Very little to distract markets from a September hike

Given an absence of noteworthy eurozone-specific data, EUR rates have remained closely tied to US dynamics. Another main driver is energy price dynamics. While the link remains closest with oil as a gauge of Middle East tensions, gas prices should be monitored as they approach crisis highs again. With efforts to fill gas storage lagging behind those of previous years, pressures could still build further down the line. The continuing drought and the disruption it causes to supply routes and energy generation can add to inflationary pressures. At the same time, it is also likely to become a drag on growth, with Germany particularly vulnerable.

In any case, the market is solidly pricing a rate hike from the European Central Bank in September after President Christine Lagarde paved the way at the July meeting. Beyond that, the market is eyeing a further tightening of 25bp early next year. While we are less certain about the latter, a September hike is also our forecast. The bar to changing that view looks high, and the geopolitical dynamics also suggest little relief in the near term.

On the data side, this week's German ZEW and the subsequent eurozone flash PMIs will be important data inputs ahead of the September ECB meeting. But it would require a substantial downside surprise from the marginal softening the consensus expects to shift the market discount away from a hike.

What we will be watching is a likely restart of primary markets in the broader EUR Sovereign, Supranational and Agency sectors. Last week we had a first small deal, but it is usually at this time of August that German SSA issuers come back to reopen the market.

Gilts: Continued hawkish pricing to be tested by data inputs

We continue to see sterling markets as too hawkish, with 50bp of policy tightening priced until mid-next year. While rates have been tracking the global dynamics of late – dominated by geopolitical and US narratives – the focus could turn more domestic again given the releases of unemployment and wage data as well as the CPI release this week.

These releases should be relevant in shaping the Bank of England outlook and especially this year's hike expectations, which over the past week have held firm in fully pricing a hike by the end of the year.

Monday's events and market view

It will be a quiet start to the week in data, with few notable releases scheduled for the day. We will have the ECB's Chief Economist Philip Lane speaking on the macro and fiscal challenges around Europe's defence build-up. The US Treasury will publish its June TIC flow data, and we will see the NY Empire manufacturing index.

No government bond auctions are scheduled for Monday.

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