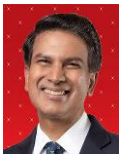
MACRO INSIGHTS
Living with 5%+ US bond yield

5 October 2026



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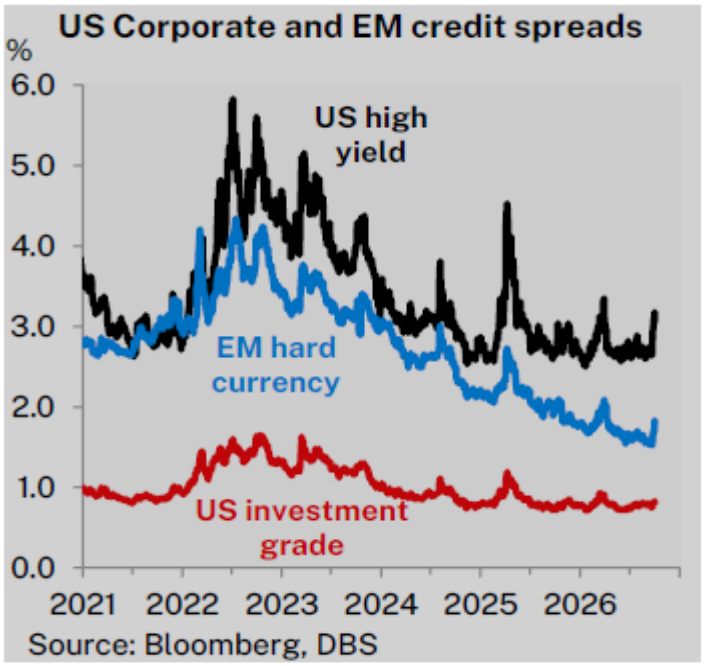
- *Mortgage rates above 7% squeeze affordability, discourage supply, and raise rollover risks.*
- *Consumers remain resilient, but high rates, energy costs, and weak real wages threaten credit health.*
- *AI-linked borrowing is surging; investment-grade spreads hold while high-yield spreads are widening.*
- *Bond inflows reduce equity support; earnings misses or stagflation could trigger a sharp sell-off.*
- *A global debt crisis is unlikely, but prolonged high rates would spread economic pain worldwide.*

CHART OF THE WEEK: CREDIT CHECK

Credit markets are showing some stress after a multi-year rally. Inflation, war, investment surge, and lack of fiscal progress have pushed up US bond yields to over 5%, while high yield corporate issuances so far this year have reached USD250bn. As a result, such bonds are now trading at over 8%, a 17-month high. A robust calendar of issuance for the rest of year would likely keep spreads elevated. Demand has been good, but the market's absorptive capacity is increasingly suspect.



COMMENTARY: LIVING WITH 5%+ US BOND YIELD

A sizeable shifting of yield curves this year has the potential to affect markets and economies worldwide. Putting aside AI-driven euphoria and that sector's seeming invulnerability to rising rates, there is a clear-cut relationship between interest rates, economic activity, and asset valuation. We explore some of these channels, with the context that past episodes of recessions and financial crises have almost always been associated with rising rates.

Housing: With 30-yr US mortgage rates heading past 7%, a level rarely seen in a quarter century, implications for the housing market are clear. Those lucky enough to lock into lower rates in recent years will not be interested in selling. Those brave enough to buy now will find the dwindling supply of homes not going down in prices. As housing prices remain sticky, affordability metrics would worsen, and mortgage-backed securities will find only few bids. This dynamic would unfold globally, and perhaps with even greater speed as a very large portion of mortgage holders outside the US have variable rate products, accentuating the imminent rollover risk.

Consumer credit: US consumers are spending robustly, with retail sales up 6%yoy through August, But the high cost of energy, high interest rates, and barely positive real wage growth will cause their financial health to weaken. Relatively low leverage and unemployment levels make an imminent worsening of consumer credit unlikely, but if rates remain high, servicing loans will become challenging in a matter of months, in our view.

Corporate borrowing: A borrowing binge is taking place both at the investment grade and high yield areas, led by funding for the AI build-up. Markets seem unworried about investment grade credit, with spreads well-anchored. But high yield spreads have begun to widen, as the combination of rising treasury rates and massive supply begin to weigh in on the sector.

Financial stability: High rates have made bonds more attractive, with flows into bond funds rising in the past two months. Equity markets are bound to see less support as a result, even if a group of AI-stocks remain well-bid. With such precarious dynamic in place, even a modest disappointment in earnings could trigger a major stock market sell-off. Additional financial stability concern stems from a stagflation scenario, in which high rates weaken activities, but Iran and Ukraine wars keep energy prices elevated, thus providing no respite to short-term inflation or policy rate expectations.

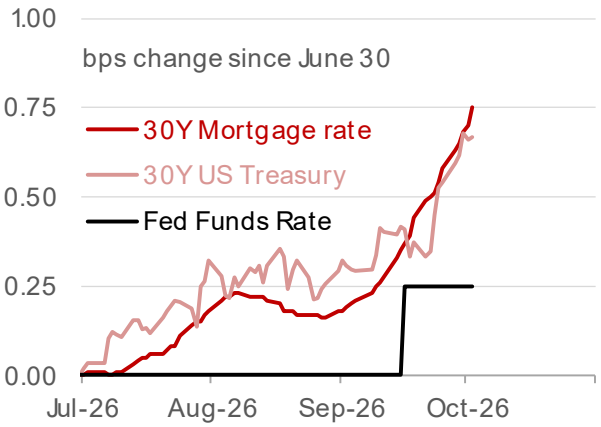
International spillover: Rising yields in the world's largest public debt market is having major spillovers, with yield curves getting pushed up everywhere. We don't see a global debt crisis around the corner, as liquidity is ample and bond markets continue to function well. But if rates stay in the present vicinity for a couple of more quarters, the pain would be felt far and wide.

FX: USD RALLY MEETS LIMIS

Philip Wee

The USD's three-week rally is running out of monetary-policy fuel. Senior Fed officials have pushed back against expectations for a back-to-back hike at the October 28 FOMC meeting. After softer US PCE inflation and nonfarm payrolls data, another concern is emerging. Financial conditions tightened rapidly since the September 16 Fed hike. Since end-June, the rise in the 30-year mortgage rate has overtaken the increase in the 10-year Treasury yield.

October Fed hike bets off



Sources: DBS Research, Bloomberg data

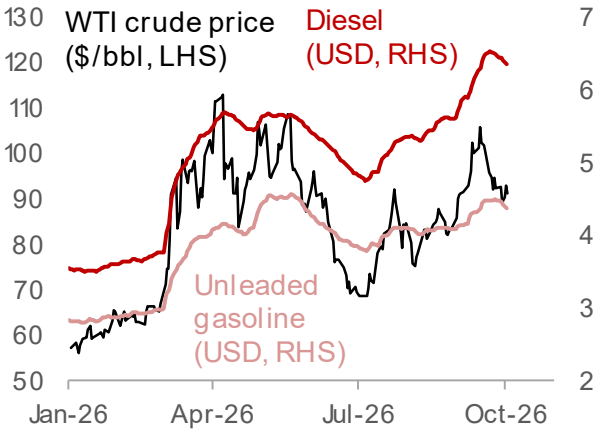
Attention could therefore rotate back towards the more uncomfortable reason **long-dated Treasury yields are approaching pre-Global Financial Crisis highs.** This distinction matters for the USD.

Higher yields driven by Fed tightening can support the USD. Higher term premia driven by concerns over debt supply, fiscal sustainability, and Treasury-market credibility need not. US Treasury Secretary Scott Bessent's renewed willingness to intervene alongside Japan to stabilize the JPY without adding selling pressure to Treasuries illustrates that tension.

However, USD/JPY has been trapped over the past fortnight, capped by intervention fears around 159-160 and supported around 156.50 by yield differentials favouring the Fed over the Bank of Japan.

The November 3 US midterm elections add another constraint. President Donald Trump and his administration face voter backlash over rising living costs. Tariffs and the Iran conflict have driven up grocery and fuel prices, while households are also confronting higher mortgage and other borrowing rates amid weak real wage growth.

Energy shock moves downstream



Sources: DBS Research, Bloomberg data

The energy price shock also migrated downstream. WTI crude oil prices have not revisited April's peak, but energy prices that matter more directly to US households and businesses have not followed crude lower. Gasoline has returned towards its 2026 high, while diesel has surged to new highs amid exceptionally tight distillate supplies.

That divergence helps explain President Donald Trump's pressure for coordinated G7 action to front-load diesel, alongside its coordinated release of 100 million barrels of emergency crude and fuel stocks. It **weakens the argument that US energy self-sufficiency leaves the US economy substantially insulated from global fuel-price shocks.**

If Republicans lose control of the House, markets could also reassess the US exceptionalism narrative that supported the USD after its post-Liberation Day sell-off.

Friday's post-NFP USD sell-off exposed a less uniform FX market than the DXY decline suggested.

CHF behaved like a haven again, balancing concerns surrounding both the USD and its "anti-USD," the EUR. Softer US inflation and payrolls coincided with France's sovereign debt concerns. EUR/CHF declined for a third consecutive week as widening French OAT-Bund spreads outweighed the Swiss National Bank's decision to buck the global tightening cycle and to temper its CHF intervention rhetoric. USD/CHF's retreat from its pivotal 0.84 resistance level leaves scope for consolidation around 0.82-0.84.

GBP's resilience told a different story. It looked more like a repricing of Fed hike expectations after the US payrolls report. Markets continue to distinguish the UK's difficult fiscal challenge from France's sovereign-debt stress. Despite elevated gilt yields, investors do not expect the October 28 UK Autumn Budget to reprise the 2022 mini-budget crisis. Fiscal discipline remains anchored by Chancellor John Healey's pledge to adhere to the fiscal rules and scrutiny by the Office for Budget Responsibility (OBR). The Bank of England's September 17 decision to pause gilt-sale auctions until April 2027 also reduced a potential source of pressure at the long-end.

EUR/USD's four-week decline reflected a changing balance of risks on both sides of the Atlantic. First, the Fed's return to tightening and market expectations of further Fed hikes eclipsed the European Central Bank's own tightening story. As rising US Treasury yields lifted French OAT yields faster than Germany Bund yields, France's fiscal problems also eclipsed America's.

But **markets should be careful about extrapolating France's fiscal difficulties into another euro-area sovereign debt crisis**. The widening OAT-Bund spread reflected a repricing of a known French fiscal problem that requires a credible response from Paris. This differs from the 2012 crisis when Greece's fiscal revelations triggered a "who's next?" loss of confidence across peripheral Europe. The ECB has stronger institutional firewalls today, including the Transmission Protection Instrument (TPI) to address country-specific stress that threatens monetary policy transmission.

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