RATES & MACRO · FIXED INCOME

Bonds on *Edge*

Strong payrolls, hawkish Fed talk, and the debt-deficit conundrum push yields higher across the US, Europe and the UK, with all eyes now on CPI.

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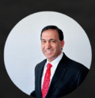

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STRONG PAYROLLS. ALL EYES ON CPI

It's not that the US debt or deficit have changed in the last few weeks — what has changed is the market focus. Treasury yields have spiked from 4.35% levels end Jun to 4.78% (4.82% 2 days back). Strong Aug payrolls (162K vs. 56K consensus) aren't helping, neither is Warsh's hawkish statement at Jackson Hole. Rate increase probabilities (16th Sep) are elevated at two-thirds, up from one-third pre-Jackson Hole.

> **The rout in bonds is universal across US, Europe, UK. While inflation is a causal factor, the larger issue, and an unsolvable one, is the debt-deficit conundrum that central banks face. With no real political will for austerity, the only way is to inflate their way out. Neither is a palatable option for policy makers.**

IMPACT & POSITIONING (IN ORDER)

- **Precious Metals (negative)** — Higher yields = Negative for Gold in particular. Gold has retrenched 7% over the last 8 trading sessions. While the fundamental case remains and if anything strengthens on dollar debasement, without a reprieve on rates, the path is murky in the short-term.
- **Growth Sectors / AI Capex (slight negative)** — With large, debt funding needed for AI capex, higher yields are a negative, *however*, elevated margins, tight credit spreads, offset the basis impact. *Credit spread dispersion is likely, and will be a differentiator. Position for quality, not yield.*
- **Duration (negative, but priced in?)** — While the debt-deficit combo will keep a floor on yields, there doesn't appear to be a case for a run-away increase in yields. Negatives appear priced in — not a case for extending duration, but equally the best gains on shorting long-dated bonds appear to be behind.
- **TIPS (positive)** — Inflationary concerns benefit TIPS.
- **Industrial Commodities (positive)** — Stronger growth metrics support demand, especially related to AI Capex. Energy remains a beneficiary of a fractured geopolitical set up.

A WIDESPREAD ROUT IN BONDS…

source: Keenai Global, CIO Office

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