Mizuho Brief: Bonds

Economics & Strategy | Asia ex-Japan

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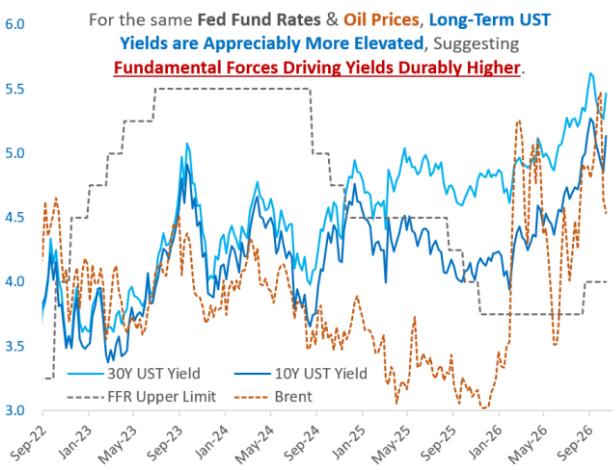
Vishnu Varathan | Head Macro Research, Asia ex-Japan

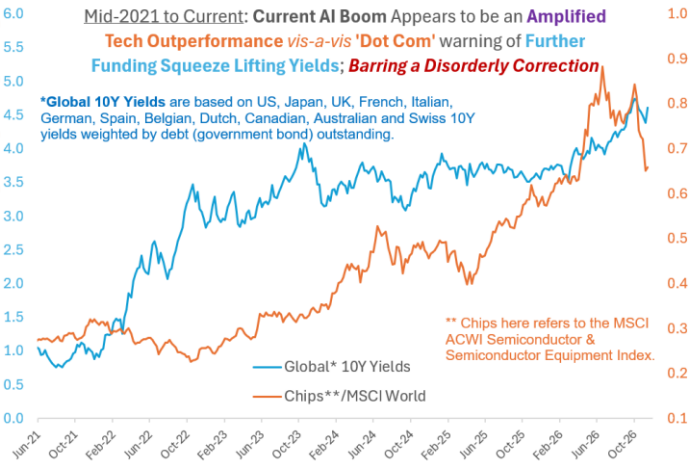
Why Bond Bears May Persist Rather Than Plateau

"The probability lies in that direction." – **Sherlock Holmes**

In a Nutshell:

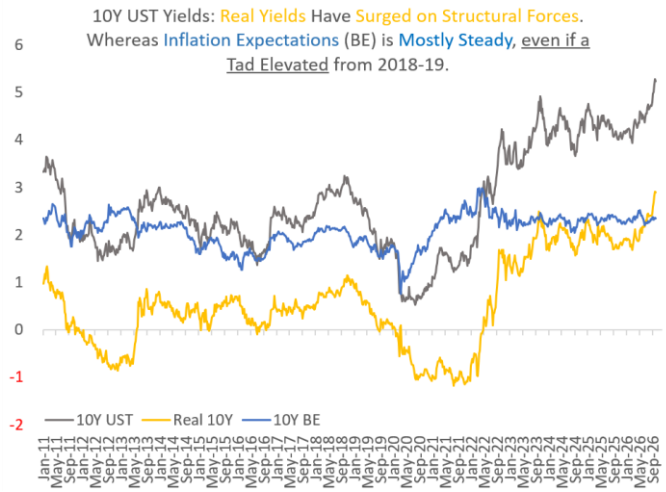
- The relief in UST yields (Oct through early-Nov) has proven premature and fleeting, exaggerated by cover amid (French/A.I.) risk-off rather than fundamental forces.
- Whereas the structural case remains for **higher yields and a steeper curve**, with **5% increasingly replacing 4% as the 10Y baseline**
- For one, **a hawkish Fed remains an immediate headwind.** With markets pricing another **3–4 hikes**, persistent hawkish *signalling could defer the peak in yields toward* ***Q2 2027****, limiting the durability of duration rallies.*
- *Crucially,* **AI intensifies the capital squeeze.** Accelerating AI capex and first-mover pressures should drive *substantial financing needs, reinforcing upward pressure on long-end yields and curve steepening.*
- *More broadly,* **underpinning the abrupt shift in savings-investment balance,** with *capital demand increasingly straining available savings.* In turn, **leaving yields biased higher**, absent a disorderly AI correction or demand shock sufficiently severe to trigger forceful easing.
- **Ultimately, the regime-change** involving the intersection of Geopolitics, technology, demographics and fiscal deterioration (that profoundly weaken fiat confidence) warrant higher term premia. And so, the **tilt of risks warrants guarding against 10Y USTs approaching 6%.**

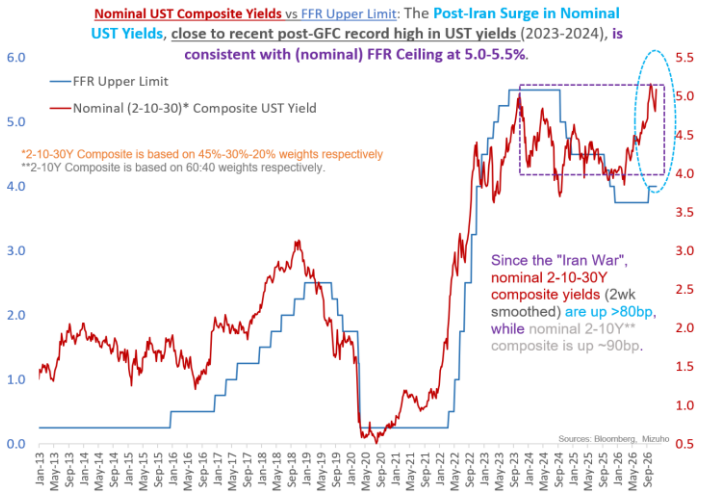




- *Fleetingly,* **markets** might have **earlier** been **lulled into peaking**, perhaps even softening **rates** (earlier in October and early-November) backing down from 5-6% (10Y UST) yields.
- ***But*** that **is a premature distraction** premised on reflex for relative cover (amid the French crisis hurting OATS and AI shakedown), not persistent depressurization on fundamental forces.
- Whereas the **case for structurally higher yields**, and especially **underpinned by a steeper curve**, is firmly intact. In turn, *underscoring our "5 is the new 4" (%) baseline for 10Y UST yields* **on four counts**.
- First, the **Fed is not done with its tightening detour** - with markets pricing in 3 to 4 more hikes.

- And the **hawkish punctuations between now and the last hike** means that ***even forward-looking yield pricing may not allow for peak yields into/approaching Q2 2027***.
- Second, *regardless of episodes of shakedowns that check excessive AI exuberance,* the **race for AI capex build out funding will only intensify**, *dragging rates higher (with a distinct steepening bias) in its wake*.
- And the **"winner-takes-all" mentality** conspiring with a **first mover advantage in pricing** means that expectations of further capital market funding squeeze are inevitably self-fulfilling.
- Third, ***barring bearish chain reactions*** involving disorderly AI corrections and/or demand destruction that triggers forceful dovish responses amid, the **interim structural forces are aligned with demand for capital far outstripping the supply of savings**.
- Fact is, the **impact of this "excess demand for capital" pressuring yields higher has already** *travelled from second derivative savings-demand dynamics to the first derivative.*
- Finally, the confluence of **profound geopolitical** (conflicts and disruptions), **demographic** (savings drawdown amid ageing in the affluent world) **and fiscal shifts** (chronic and arguably unsustainable debt dynamics) **suggest** that **excess savings are strained exactly when petrodollars and faith in fiat are compromised, if not shaken** -.
- Inevitably, this will result in **disproportionately higher premium demanded for fiat debt**.
- In which case, the *question is less about reversion to 4% long terms yields and more about whether 6% may be tripped as well*.
- Notably, given the **"regime change" of conspiring geo-politics (wars/conflict, US-China, etc), AI technology race and savings-investment imbalance amid demographic shifts**.





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