Global Strategy

Rates Map - The real message of global yield curves

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Less central bank gradualism and higher energy prices have a real cost

Higher yields have been the path of least resistance for markets as policymakers have turned cautious on not just asset purchases but also forward guidance and will need time to digest the ongoing energy supply shock. Globally traded liquid bond markets are sending a relatively consistent message, even if the market may be underestimating cross-country differences in economic impact and central bank reaction functions (Figure 4). Last week, 10y rates rose even more than 2y rates, in a break with the underperformance of 2y bonds seen since the Iran conflict started. Investors want higher yields to hold duration risk. This is in line with Bernanke's view that a gradualist approach to monetary policy "may increase the ability of the Fed to affect long-term rates and thus influence economic behaviour." A less gradualist approach in favour of what Bernanke has called a "cold turkey" approach would then lead to higher long-term rates and more volatility.

Japan re-joins the rates peloton and SNB pricing went to two hikes

Last week was a reminder that Japan has returned as an important driver to global bond markets (Figure 4). A total of 29 bps of Fed hikes is now priced by the Fed's March '27 meeting, but US 10y still rose to 4.60%, crossing our Q2 forecast of 4.50%. Meanwhile US 5y real rates, implied by Treasury Inflation-Protected Securities, rose 33 bps so far in May (to 1.55%) as the Fed is being repriced in line with stronger US data. Our takeaway from a range of meetings is that especially hedge funds had been positioning for the move higher in US rates and that April's US CPI validated this positioning. But SNB pricing also went to two hikes by Sep '27 as Swiss Q1 flash CPI was better than expected.

German 10y vs US widens further

The stop on our long 10y bunds is 3.25% and we remain long. We think that the euro area is facing the larger adverse terms-of-trade shock and this limits how hawkish the ECB will get. We still forecast 10y US vs Germany to rise 150 (from 144 currently).

Neutral on eur country spreads

We remain neutral on Italy, France and Spain against Germany but would not lean against further tightening in spreads. The European Commission is reviewing the escape clause for fiscal rules but we do not see a repeat of the fiscal support granted in the pandemic. That being said, we think that near-term EGB issuance could lead to some modest widening of sovereign rates versus swap rates as EGB issuance is running slightly below its 3y average, but we did not pick up material concerns on US or EUR funding markets in recent client meetings. German 30y yields (at 3.66%) are trading 40 bps above 30y EUR swap rates (at 3.26%), with the spread 17 bps higher year-to-date.

UK 10y not a buy yet - Receiving June 'BoE

We have been telling clients not to go long UK 10y bonds as we think that political risks had been underpriced. The lesson from the mini budget of Liz Truss is that UK rates can price sharply higher on political uncertainty. There is more: the UK is an energy importer with inflation running above target for a while, so the bond market is also especially vulnerable to higher oil prices or higher US rates.

Clients have been asking how much gilt yields could reprice in response to political developments. As a reference point, we estimate that around 90bps of additional term premium was priced into 10-year gilts in 2022 following Liz Truss's mini-budget. However, at that time the BoE was in the middle of a rapid tightening cycle, which was also pushing up long-term rate expectations. Looking ahead, we think renewed fiscal concerns could add roughly 25–50bps to the term premium at the 10-year tenor from last week Monday's level of ~ 5% (more in the note here).

Front-end - Stopped out of long SNB Sep '27 but unchanged otherwise
We continue to receive July ECB, June BoE, and 1y1y SEK vs US. We opened a long 1y1y SEK vs USD Tuesday 5 May given the persistent inflation undershoots vs target and relatively soft labour market in Sweden versus a drift up in US rate expectations. We move the target to 180 bps (from 165 bps) and put the new stop at 155 bps. We are also still paying Jun '27 vs Jun '28 Euribor.

Curves - Adding UK 5s10s steepener to Japan steepener
We added a 5s10s steepener in UK to our 2s10s steepener in Japan (6 months forward). We see scope for a pick-up in rates volatility, some disinflationary impulse to the US economy and flatter 5s30s curve if Fed communication turns less gradualist under Kevin Warsh.

Recent Notes

Weekly Supply - Deep dive on Euro issuance (15 May)

Client views - Oil vs Fed vs ECB vs Carry vs Political risk (14 May)

UK curve: Higher and steeper for longer (12 May)

2026 Outlook – Iran conflict meets hawkish US (11 May)

AI releases did not lower rates or reduce fiscal risks in '25-26 (8 May)

Not long 10y UK at 4.94% - Rate uncertainty, politics and oil (7 May)

Receive 1y1y SEK versus USD (5 May)

AI - No clear path to lower rates (5 May)

Receiving July ECB at 19 bps, still short June '27 vs June '28 Euribor (30 Apr)

US Refunding - Revising expected '26 coupon supply slightly lower (29 Apr)

Receive BoE June Meeting at 19 bps (29 Apr)

Warsh vs Bernanke Fed - More volatile rates ahead? (28 Apr)

UK Remit Revisions and Supply Chart Pack (23 Apr)

IMF Takeaways - Trading "one transitory shock after another" (20 April)

UK 10y higher for longer: 4.75% at end '26 (from 4.05%) (20 April)

End '26 Forecast: 10y US at 4.25% (4%) - bund at 2.75% (3%) (16 April)

Summary of views

Figure 1: Open Trades

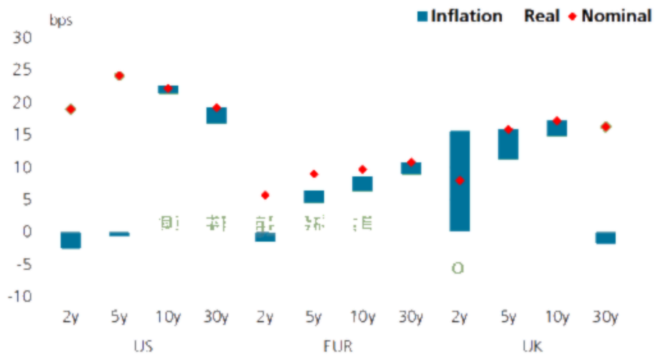
Market	Position	Entry Date	Entry Level	Current Level	Target	Stop	Gain (bps)
USD	Long 2s7s10s SOFR butterfly	27-Mar-26	-8	1	-40	10	-9
EUR	Receive July ECB	30-Apr-26	19	14	0	28	5
EUR	Long 10y EU vs Germany	27-Mar-26	35	34	20	45	1
EUR	Long 10y bunds (%)	26-Mar-26	3.00	3.17	2.75	3.25	-17
EUR	Pay June '27 Euribor vs receive June '28 Euribo	21-Mar-26	-3	-11	-30	-10	8
GBP	Long nominal 5s10s steepener	12-May-26	45	47	65	30	2
GBP	Receive BoE June Meeting	29-Apr-26	19	9	0	30	11
AUD	Receive 5y2y (%)	14-Jan-26	4.83	5.12	4.40	5.10	-29
JPY	Long 6m fwd 2s10s steepener	09-Feb-26	64	98	100	55	34
SEK VS USD	Receive 1y1y SEK vs USD (%)	05-May-26	-1.31	-1.67	-1.80	-1.55	36

Source: Bloomberg, UBS. Note: Target extended and stop revised for SEK vs USD trade on 18-May-26

The Map is our summary on the rates outlook. We would like to thank Deepak Joy and Mehak Bhalla, our research support service professionals in our Hyderabad Research BSC, for assisting in preparing this research report.

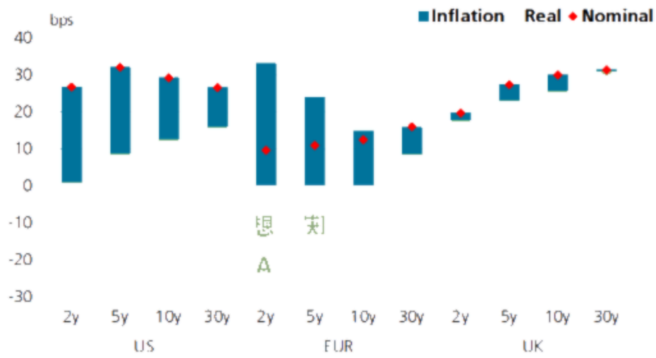
Charts of the week

Figure 2: Month-to-date nominal and real moves in May '26 so far



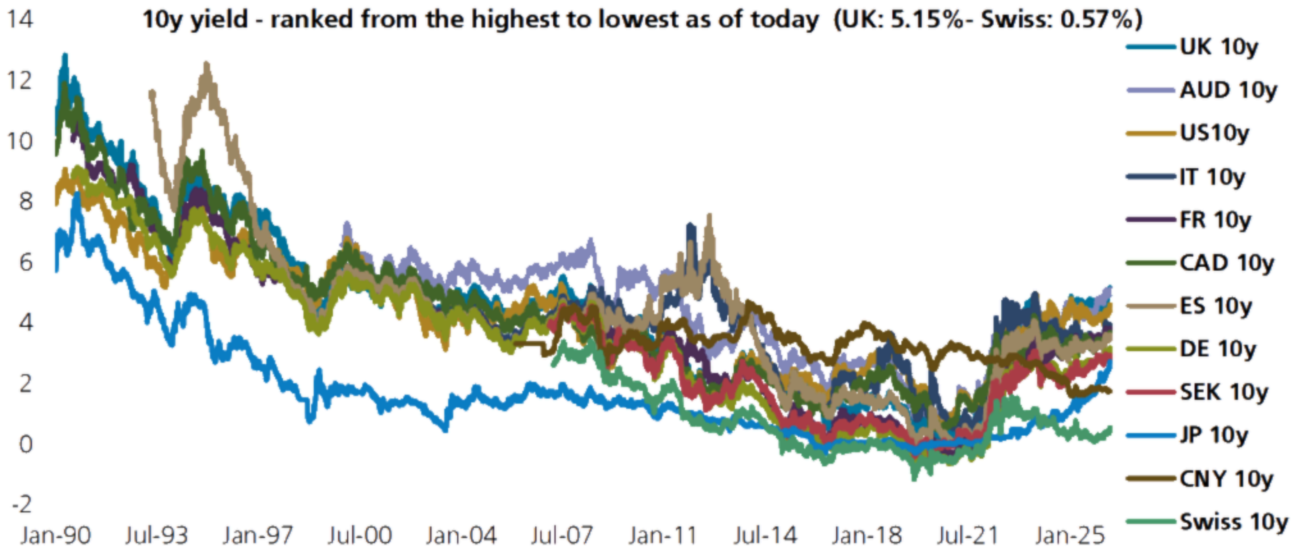
Source: Bloomberg, UBS

Figure 3: Apr- till now nominal and real moves



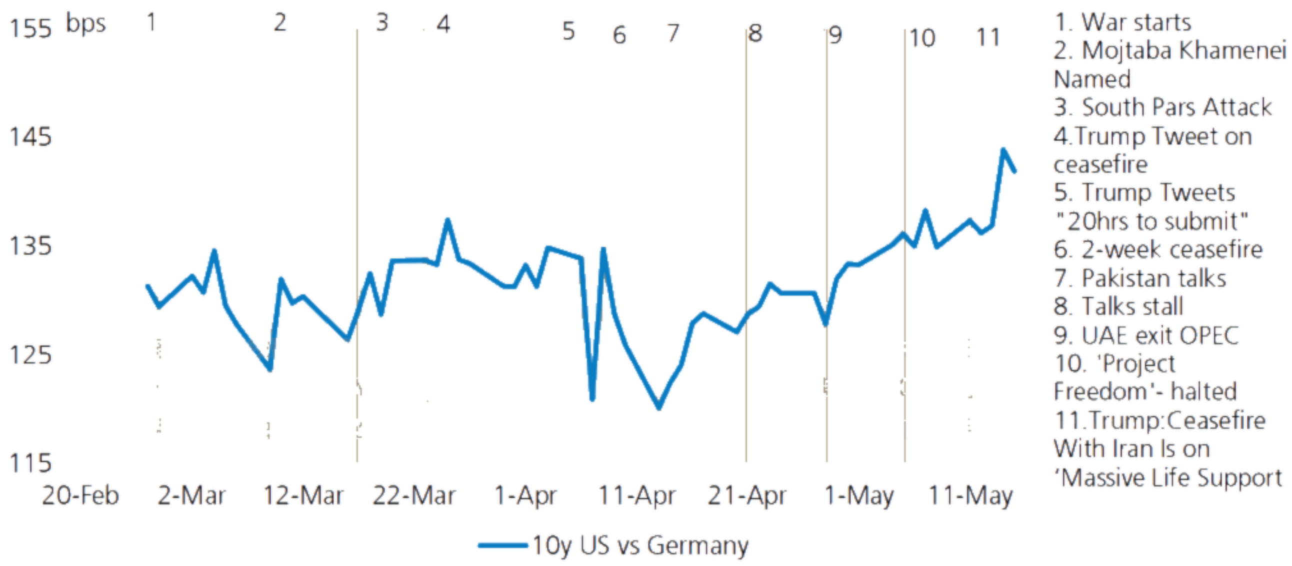
Source: Bloomberg, UBS

Figure 4: Globally traded liquid yield curves - Japan re-joins the peloton



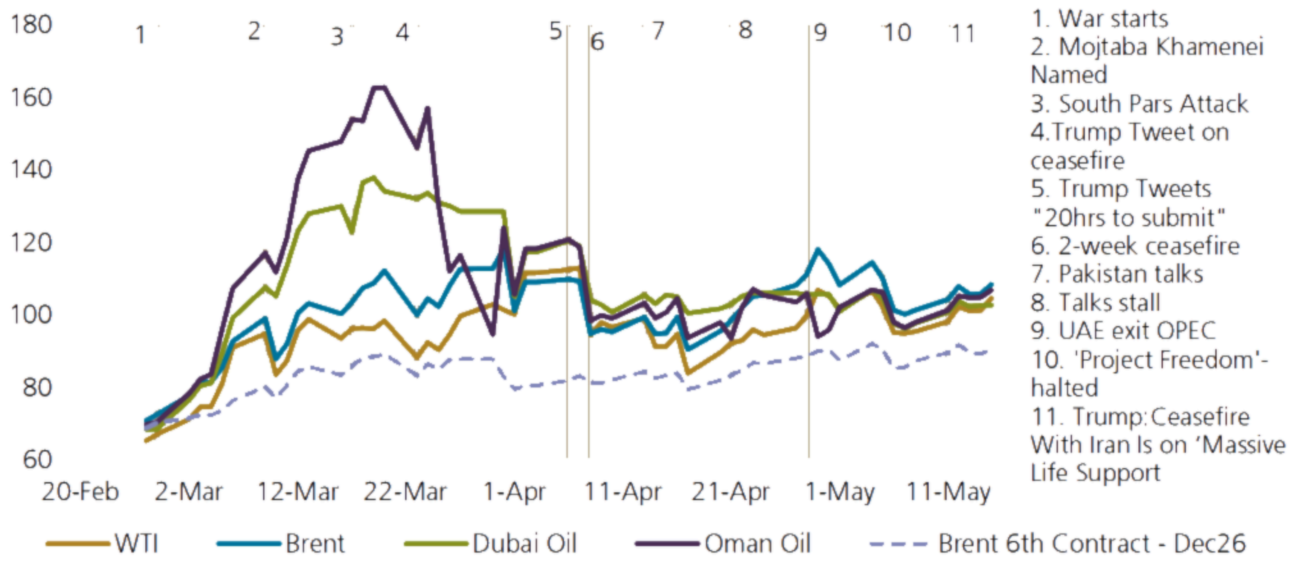
Source: Bloomberg, UBS

Figure 5: 10y US vs Germany Spread moves across the Hormuz timeline



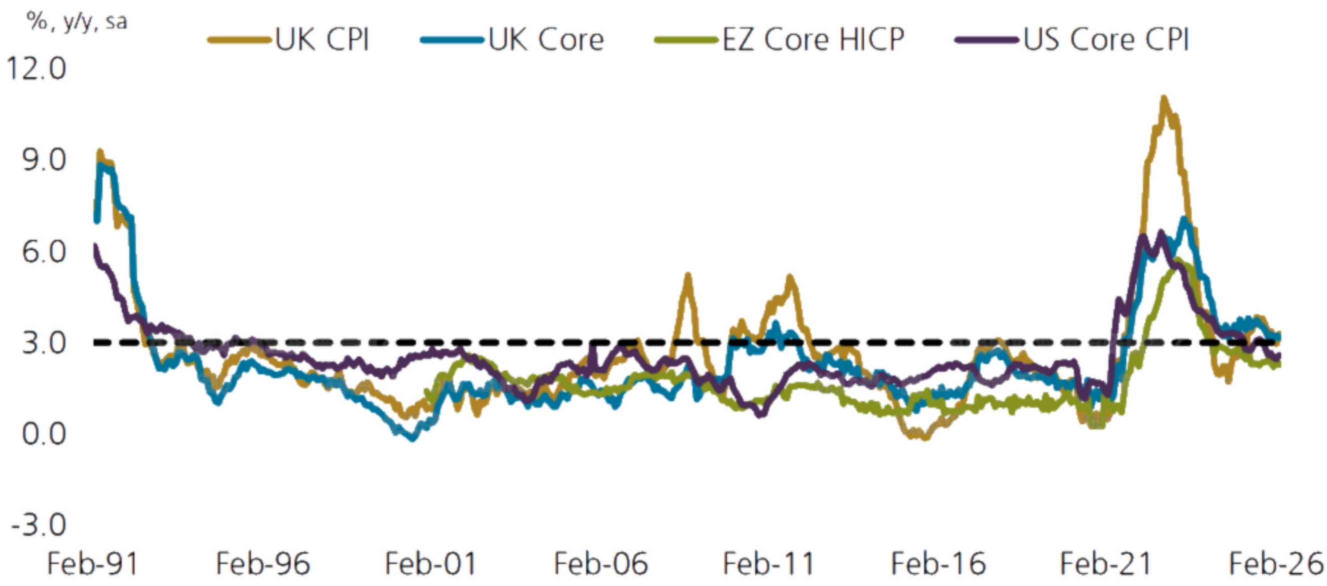
Source: Bloomberg, UBS

Figure 6: Timeline on oil pricing



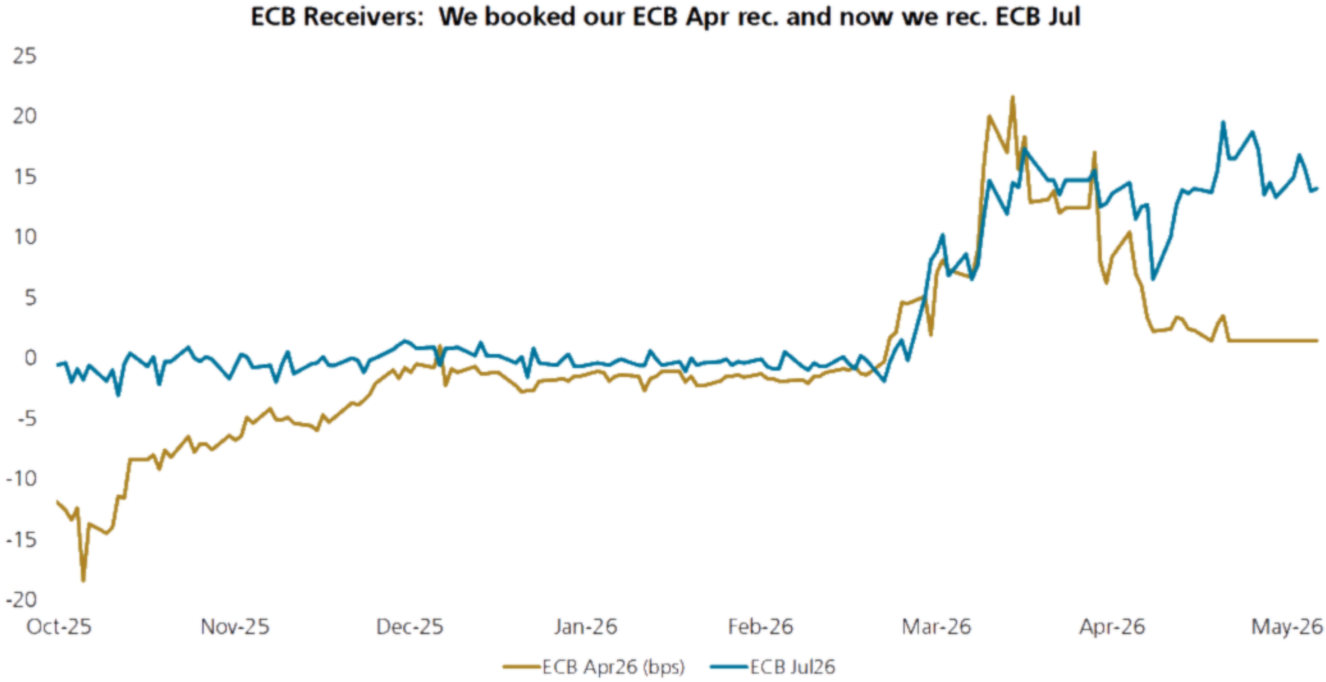
Source: Bloomberg, UBS

Figure 7: UK Inflation prints hovering around 3% mark



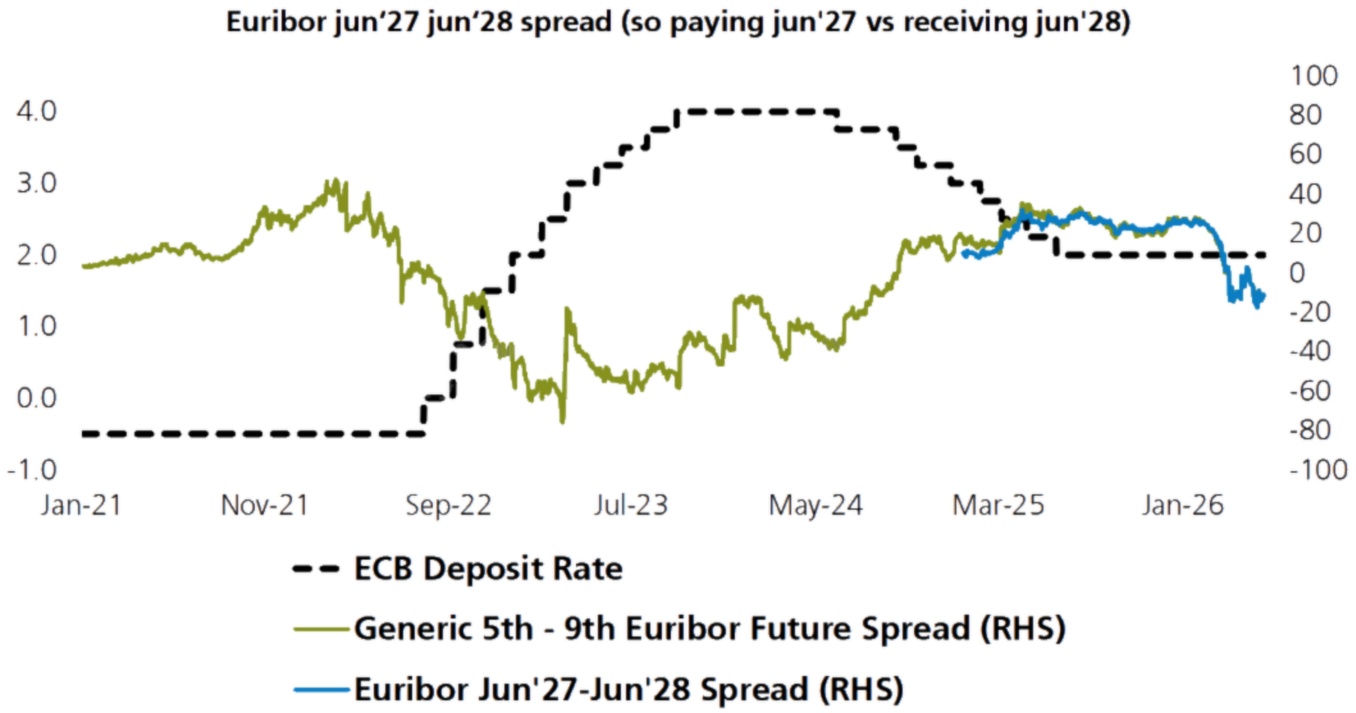
Source: Haver, UBS

Figure 8: ECB Receivers



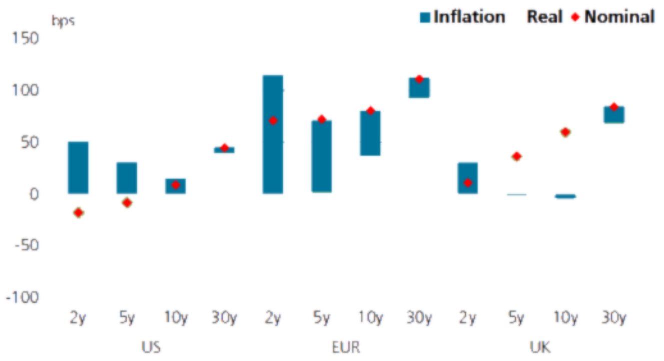
Source: Bloomberg and UBS

Figure 9: We pay June '27 ECB vs receiving June '28 ECB. We think that the EURIBOR market will continue to back load cuts in the 2y "red" segment



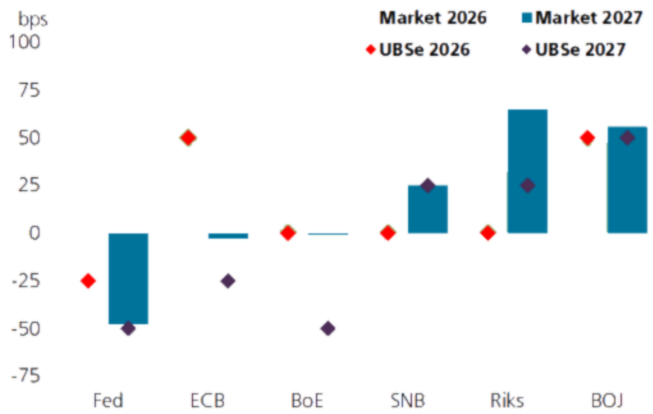
Source: Bloomberg and UBS.

Figure 10: YTD nominal and real moves



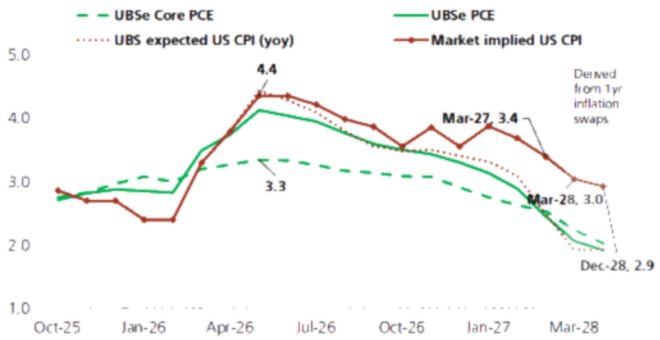
Source: Bloomberg, UBS

Figure 11: Central bank pricing - Market vs UBSe



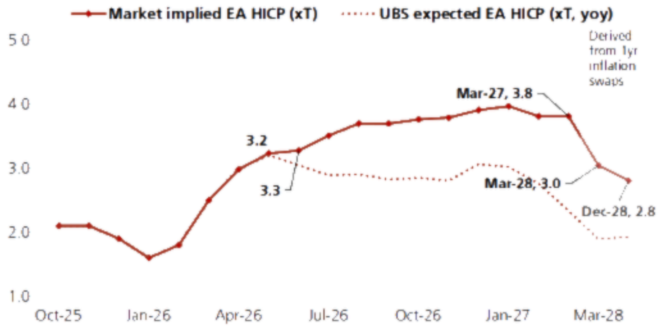
Source: Bloomberg, UBS

Figure 12: US market-based inflation expectations is expected to peak at 4.4% yoy in June '26 from 3.8% in April and 1y from now inflation (USSWIT1) is priced at 3.4%



Source: Bloomberg, UBS (incl. estimates)

Figure 13: Euro area market-based inflation peaks around Jan '27 at 4% yoy and 1y inflation expectation (EUSWI1) trades at 3.8%.



Source: Bloomberg, UBS (incl. estimates)

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Risks of multi-asset investing include but are not limited to market risk, credit risk, interest rate risk, and foreign exchange risk. Correlations of returns among different asset classes may deviate from historical patterns. Geopolitical events and policy shocks pose risks that can reduce asset returns. Valuations may be adversely affected during times of high market volatility, thin liquidity, and economic dislocation. Valuation methods across sectors include DCF, SOTP and multiples analysis.

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