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Global Markets Strategy

16 October 2026

J.P.Morgan

Treasuries

The trees are stripped bare of all they wear, what do I care?

- Treasury yields ignored strong inflation and labor market data, declining amid concerns over equity valuations globally
- Growing concern over higher rate levels and the impact on equity markets seems to be reflexively impacting rates markets here, and given the move in long end yields and swap spreads this week, it could also reflect heightened expectations about a shift in debt management strategy...
- ...It could also indicate positioning is cleaner than indicated by our Treasury Client Survey. On balance, even with the latest moves, the front end appears modestly cheap after accounting for Fed rhetoric and growth expectations...
- ...but the curve has lagged after accounting for the recent shift at the front end, and 10s/30s appears 3bp flat given the level of rates. We like adding 10s/30s steepeners as a tactical low-beta proxy for long exposure at the front end, with some relative value protection in case the bearish impulse resumes. The steepener should also work if Treasury gives no indication long-end supply cuts are imminent
- Actively-managed core bond funds had outperformed index by nearly 40bp through August, only to give this performance back through September. We find vol to be the most statistically significant driver of returns in recent months, with duration and steepening exposure pared back over the summer

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Market views

Treasury yields retraced to new highs on Wednesday following a firm CPI report, but quickly reversed lower amid growing concerns over AI equity valuations, evident in the 15% fall in the KOSPI this week and the ongoing underperformance of the NASDAQ relative to other domestic equity indices (**Figure 1**). Moreover, commentary from Fed officials this week ahead of the blackout period gave no indication of the need to hike at consecutive meetings. Importantly, Governor Bowman spoke on the sidelines of the IMF/World Bank meetings in Bangkok, arguing that she did not "feel any urgency for taking further action at this point." These comments came prior to the CPI release, but given Chair Warsh likely had the CPI data, and that Bowman is politically aligned with the Chair, it's unlikely that she spoke out of turn. Warsh ratified these comments on Friday, expressing optimism about the US economy, and saying that the economy had "broadly conformed to our expectations" since the September meeting.

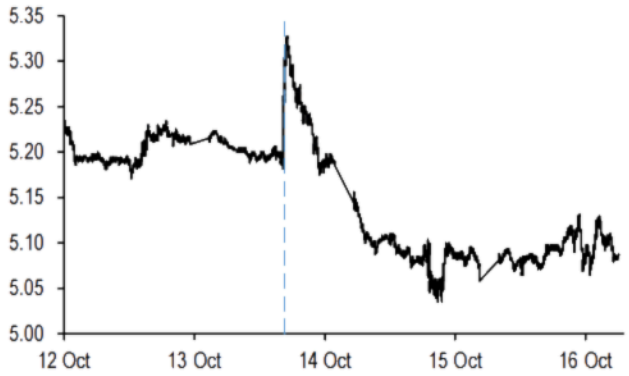
Though the likelihood of an October hike was quashed this week, the data does not support a one and done. The CPI print was strong across categories, and with the PPI data in hand, we forecast PCE rose 0.31% over the month, lifting the over-year-ago rate from 3.0% to 3.1% (see *US CPI & TIPS: On firmer footing*, Abiel Reinhart & Harry Downie, 10/14/26). Meanwhile, labor markets remain healthy as the four-week average of initial claims remains below 200k, and continuing claims declined to 1.71mn (consensus: 1.709mn), running counter to seasonal patterns and suggesting risks that the unemployment rate could fall in the coming months (see US: Continuing claims still point to lower unemployment, Abiel Reinhart, 10/15/26). In the wake of these developments, 2-, 5-, 10-, and 30-year yields declined 11bp, 17bp, 19bp, and 20bp, respectively, and the US outperformed its DM peers in the process (**Figure 2**).

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Figure 1: Treasury yields traded a 30bp range this week, ending lower...

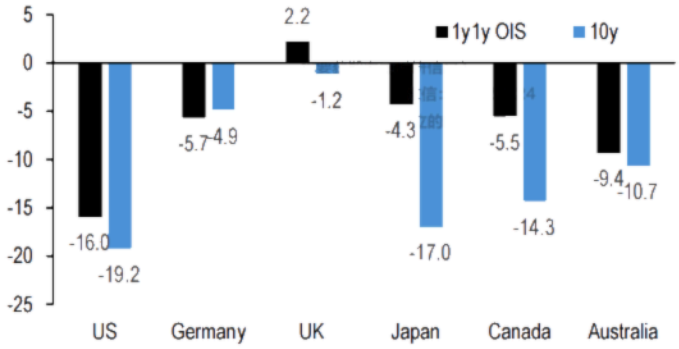
10-year Treasury yields intraday 10/13/26-10/16/26*; %



* Blue line denotes September CPI release
Source: Bloomberg Finance L.P.

Figure 2: ...and the US outperforming its DM peers in the process

Changes in various DM 1y1y OIS and 10-year government bond yields, 10/2/26-10/16/26; bp



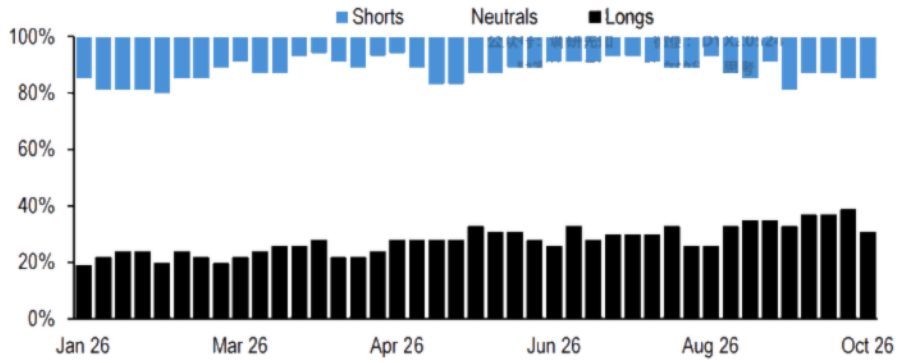
Source: J.P. Morgan

Overall, it is impressive that Treasury yields declined so sharply from their mid-week peaks, even in the face of strong data over the period. This rally could reflect one of three factors, or some combination of the three. **First**, as discussed above, the move in yields is finally affecting equity valuations. Our equity strategy team has found that there is an inverted "U" relationship between 10-year yields and S&P 500 multiples, and typically this relationship turns negative when yields sit above 5% (see *Global Equity Strategy: Implications of Higher Rates for Equity Fundamentals, Valuation, and Positioning*, Dubravko Lakos-Bujas et al., 9/14/26).

Second, position technicals could be cleaner than we had appreciated. Our most recent *Treasury Client Survey* shows duration overweights have been pared back, as the share of longs has declined to its lowest since August, but are still higher than where they began the year, and remains net long (**Figure 3**). As we have discussed in recent weeks, the Client Survey tends to lean neutral, if not short, in the early stages of even shallower hiking cycles (see Treasuries, *US Fixed Income Markets Weekly*, 9/25/26). The performance over the last 48 hours would either indicate otherwise, or that with the rally we've had, some momentum-driven investors are finally paring back on systematic shorts (see *Technical Analysis*).

Figure 3: Our Client Survey continues to show a net long position, albeit reduced from September, and this week's moves indicate positioning may be even cleaner

J.P. Morgan Treasury Client Survey; %



Source: J.P. Morgan

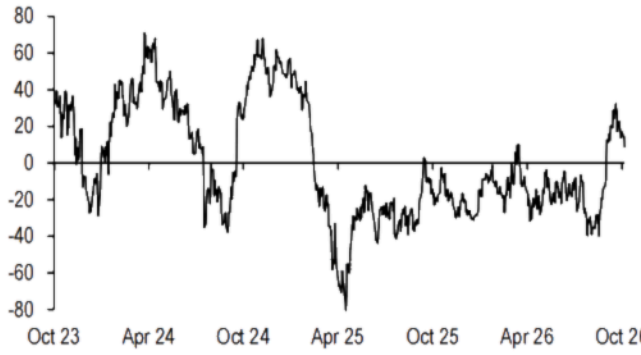
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Finally, it could be symptomatic of a shift in Treasury debt management strategy expectations: 30-year swap spreads widened by 3-4bp as long-end yields declined and the curve flattened this week. Treasury released its primary dealer questionnaire today, and there was no explicit mention of cutting or discontinuing long-end issuance. Treasury did inquire about trends in structural demand for Treasuries and how it should change auction sizes to reflect future expected shifts in demand, which market participants could perceive as leaving the door open for future cuts. We have argued for over a year now that the pace of demand for longer-duration assets should slow, as corporate DB funds are more than fully funded, their fixed income asset allocation has increased sizeably, and the expected vol of their surplus is relatively low (see *Before you ask...it's not QE: 2026 Treasury demand outlook*, 11/20/25). However, in the face of a looming funding gap in 2027 and beyond, it would be imprudent to cut one source of funding when end-user primary demand has been strong. Thus, we think future auction size increases should be focused in the 2- to 10-year sector, while keeping long-end sizes unchanged (see *US Treasury Market Daily*, 8/5/26).

In aggregate, given this week's moves, we think there are some interesting opportunities along the Treasury curve. We've been making the case in recent weeks that the front end had finally been flagging somewhat cheap after controlling for the shift in Fed rhetoric and rise in growth expectations, and a bit of that value has eroded given the rally in the last few days (**Figure 4**). Moreover, it's interesting that the curve move has been somewhat parallel in this rally, as we would have expected more steepening given the front-end repricing that has occurred. **Figure 5** shows that 1y1y OIS has explained close to 90% of the variation in 10s/30s over the last 6 months, demonstrating that this curve tends to steepen 2bp for each 10bp decline in front-end rates. The curve currently appears 3bp flat on this basis, and this whole decoupling has occurred this week.

Figure 4: The front end no longer screens very cheap after controlling for growth expectations and Fed rhetoric...

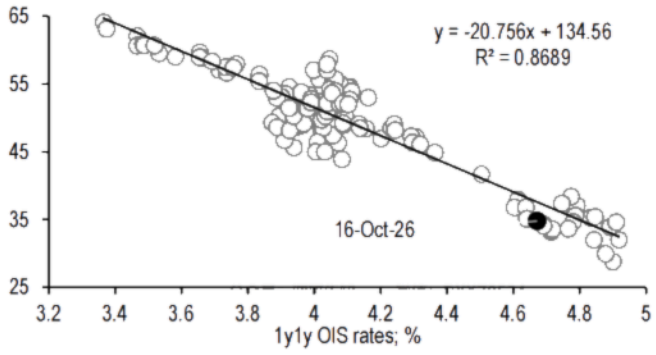
Residual* of 2-year Treasury yields regressed on Federal Reserve HDSI** and J.P. Morgan US Growth FRI***, regression over the last three years; bp



* 2-year UST yields = (0.026* Fed HDSI) - (0.1339* US FRI) +16.245. R-squared = 0.452, SE = 34bp
** For methodology, see *Can you hear me now? Updating the J.P. Morgan NLP model of Central Bank Speak—More accurate with richer content*, Joseph Lupton and Dan Weitzenfeld, 9/28/26
*** For methodology, see *Know thyself. Evaluating and using J.P. Morgan economic forecasts*, Joseph Lupton, 9/23/2014
Source: J.P. Morgan

Figure 5: ....but the curve appears too flat and offers value

10s/30s Treasury curve regressed on 1y1y OIS rates (%), regression over the last 6 months; bp



Source: J.P. Morgan

On balance, with the front end still flagging somewhat cheap and the curve appearing too flat given the level of front-end yields, we think 10s/30s steepeners are a low-beta way to get long the front end here, with some relative value to protect, given yields are now about 20bp off their local highs. This trade also offers value if Treasury does not give any indication that it will make cuts to long-end issuance at the quarterly refunding announcement on

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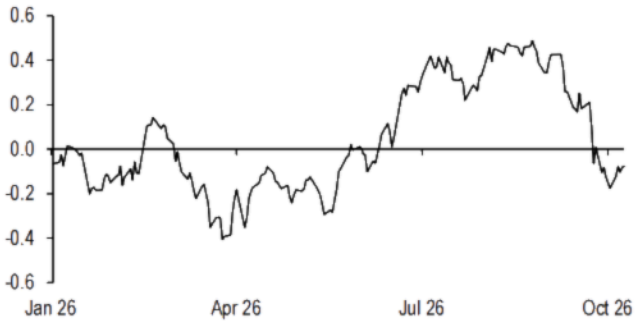
November 4th. **Accordingly, we recommended adding tactical 10s/30s steepening exposure earlier this week. We also recommend holding on to 10s/20s/30s belly cheapening butterflies.**

Core bond fund positioning update

Given our recent focus on headwinds coming from position technicals, we find it timely to evaluate how actively-managed core bond fund positioning has evolved since earlier this year. Amid broad market volatility and a difficult macro backdrop, our broad fixed income index, the GABI, is on track for its worst annual performance since 2022. Active core bond funds outperformed the broad index through the summer, before a resurgence of volatility amid a sharp repricing of Fed expectations through the month of September eroded excess returns, leaving cumulative performance just shy of the index YTD (**Figure 6**).

Figure 6: Active core bond funds cumulative excess returns eroded in September amid broad market volatility and sharp rates repricing...

YTD cumulative excess returns of the active core bond fund index*; %



*Core bond fund index reflects the excess returns of the 25 largest active core bond funds by AUM relative to the GABI
Source: J.P. Morgan, Bloomberg Finance L.P.

Figure 7: ...unsurprisingly, implied volatility has grown in significance as a driver of excess returns in recent months

Model statistics for the excess performance of our active core bond fund index; units as indicated

Factor	3M Beta*	3M T-Stat	3M chg in factor	Beta, 3M ago	T-Stat, 3M ago
(-) 10Y UST Yields (%)	**-0.353**	**-1.60**	**0.62**	**-0.260**	**-1.17**
(+) 5s/30s UST curve (bp)	0.002	1.35	-28.31	0.004	1.70
(-) HG credit (bp)	**-0.002**	**-0.57**	**4.93**	**0.002**	**0.28**
(-) MBS OAS (bp)	0.009	2.79	13.16	0.004	0.80
(+) Vol (bp/day)	**-0.213**	**-4.28**	**1.83**	**-0.136**	**-2.00**
R-squared	50%				

* 3-month regression of daily excess returns on the core bond fund index versus daily changes in 1) 10-year US Treasury yields, 2) 5s/30s Treasury curve, 3) JULI spread to Treasuries, 4) MBS current coupon Treasury OAS, and 5) 3Mx10Y swaption volatility
Source: J.P. Morgan, Bloomberg Finance L.P.

Figure 7 details the statistics from our active core bond fund index model, compared with the same statistics from 3 months ago. This shows that volatility has represented the dominant driver of excess returns over the last 3 months, with short vol exposure eroding excess returns as implieds exhibited strong rate-vol directionality in September, increasing sharply on the back of the broader rise in yields. Away from volatility, an overweight in MBS amid widening OAS also likely hampered returns. Neither duration nor curve positioning represented statistically significant drivers of excess returns last quarter. The duration beta moved briefly overweight in June, before exposure was steadily reduced in the months following (**Figure 8**). This is somewhat differentiated from the other metrics of positioning we watch: our *Treasury Client Survey*, which represents a broader set of clients, has leaned persistently long this year even as Treasuries have sold off. As outright duration exposure has moved further underweight, the curve beta has also fallen, indicating that active core bond funds have reduced steepening exposure overall.

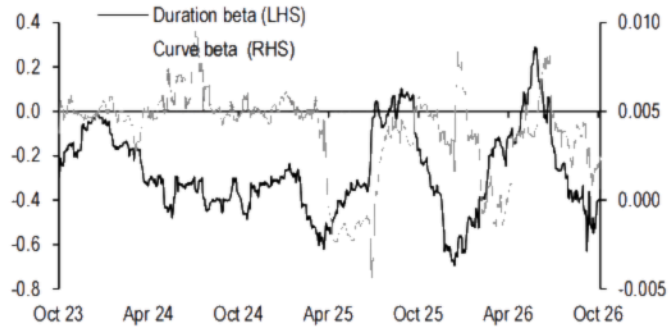
Notably, these findings are somewhat different than what we can obse
tioning. Asset managers traditionally prefer to express duration views
cash, given restrictions around repo usage and persistent credit ove
suggests that net long positions in the WN contract have decreased in
year, whereas long positions in the FV contract have stayed roughly

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Figure 8: Funds have added to durations underweights while reducing steepener exposure...

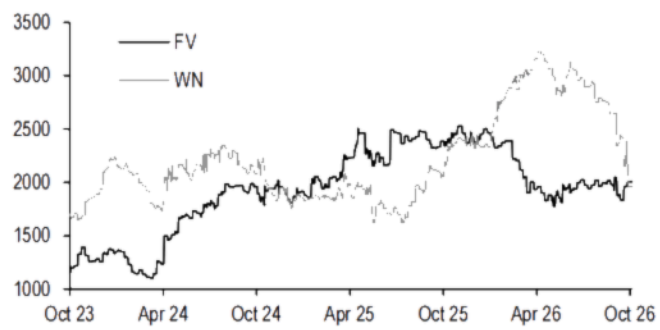
Core Bond fund beta to 10-year Treasury yields (lhs; %) and 5s/30s Treasury curve (rhs; bp)



Source: J.P. Morgan, Bloomberg Finance L.P.

Figure 9: ...though asset manager positions in the WN contract have been reduced in 2H26, while FV positions have remained roughly unchanged

Asset manager net positions in FV and WN contracts; '000s of TY equivalents



Source: CFTC

Looking ahead, if our forecasts come to fruition, we see some headwinds for the asset manager community. While active core bond funds appear to be somewhat underweight corporate credit, our credit colleagues have shifted their YE spread targets tighter, as they expect the supply/demand balance to improve throughout Q4 against a backdrop of strong fundamentals (see *JPM Daily Credit Strategy Update*, Nathaniel Rosenbaum, 10/5/26). In the mortgage space, recent tightening has left spreads looking somewhat less attractive (see Agency MBS, *US Fixed Income Markets Weekly*, Nick Maciunas, 10/2/26). Meanwhile, we see value emerging in Treasuries at these levels, with current levels more fair versus fundamental drivers in both the front-end and intermediate sectors. On the other hand, our interest rate derivative colleagues remain soft bearish volatility, especially in longer tails, and with asset managers similarly positioned, this should buoy excess returns as volatility subsides (see Interest Rate Derivatives, *US Fixed Income Markets Weekly*, Ipek Ozil, 10/15/26).

Trade recommendations

- **Maintain 10s/30s steepeners**

- Stay long 100% risk, or $64.8mn notional of T 4.625% Aug-36s
- Stay short 100% risk, or $35.9mn notional of T 5.125% Aug-56s
- (*US Treasury Market Daily*, 10/15/26: P/L since inception: -0.2bp)

- **Maintain 10s/20s/30s belly-cheapening butterflies**

-Stay long 50% risk, or $32.1mn notional of T 4.625% Aug-36s
-Stay short 100% risk, or $41.2mn notional of T 5.125% Aug-46s
-Stay long 50% risk, or $16.9mn notional of T 5.125% Aug-56s
- (*US Treasury Market Daily*, 9/4/26: P/L since inception: -1.6bp)

- **Maintain 2.375% May-51 / 5.0% May-56s curve flatteners**

- Stay short 100% risk, or $25.1mn notional of T 2.375% May-51s
- Stay long 100% risk, or $16.6mn notional of T 5% May-56s
- (*US Fixed Income Markets Weekly*, 5/15/26: P/L since inception: -1.5bp)

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Figure 10: Closed trades in the last 12 months

P/L reported in bp of yield unless otherwise indicated

TRADE	ENTRY	EXIT	P/L
Duration			
50:50 weighted 2s/5s/10s belly-cheapening butterflies	**11/25/25**	**12/10/25**	**4.9**
2-year duration shorts	02/12/25	03/05/26	13.9
2-year duration longs	**03/20/26**	**04/02/26**	**9.4**
50:50 weighted 2s/5s/10s belly-cheapening butterflies	03/06/26	05/15/26	3.7
2-year duration longs	**05/15/26**	**06/04/26**	**3.8**
Short 10-year Treasuries versus 10-year Bunds	06/05/26	09/25/26	13.8
Curve			
5s/20s steepeners	**07/25/25**	**11/24/25**	**0.6**
2s/5s flatteners	12/16/25	01/05/26	-2.6
10s/30s flatteners	**01/09/26**	**01/20/26**	**1.9**
5s/20s steepeners	01/28/26	02/06/26	6.2
5s/20s steepeners	**02/20/26**	**03/11/26**	**0.7**
10s/30s flatteners	06/12/26	07/13/26	-0.4
5s/30s flatteners	**07/24/26**	**07/29/26**	**-5.8**
2s/10s steepeners	07/31/26	08/28/26	-7.6
Relative value			
67:37 4.00 Jun-32s/4.25 Aug-35s/4.75 Aug-55s belly-cheapening butterflies	**10/03/25**	**12/19/25**	**-3.4**
50:50 weighted 5s/10s/30s belly-cheapening butterflies	10/31/25	06/12/26	-5.8
Term premium			
64:11 weighted 3s/10s/30s belly-cheapening butterfly	**05/02/25**	**11/24/25**	**-18.3**
Number of positive trades			10
Number of negative trades			7
Hit rate			59%
Aggregate P/L			15.0

Source: J.P. Morgan