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WEEKLY MARKET SIGNALS

Have bond yields gone too far—or just far enough?

FROM OUR U.S. PARTNERS.

Fidelity Institutional Capital Markets Strategy Group | August 31, 2026

Long-term Treasury yields have climbed to nearly two-decade highs, testing equities, housing, corporate borrowers, and traditional portfolio construction. But the same sell-off may also be creating a more compelling entry point for duration—and a chance to earn meaningful income from high-quality bonds.

Key takeaways

- **Why are yields moving?** The long end is being pulled by a tug-of-war between negative forces—deficits, debt burdens, aging demographics, and heavier Treasury issuance—and positive forces, including AI-driven productivity, capital investment, labor augmentation, and potentially stronger real growth.
- **Why does policy matter now?** Treasury's expanded long-end buybacks signaled that some policymakers believe yields have risen enough. That does not eliminate fiscal or inflation risk, but it does suggest policy may lean against further disorderly increases in long rates.
- **Where is the opportunity?** With nominal and real yields now modestly attractive, the better risk/reward may be in high-quality income and the belly of the curve rather than a broad call to extend duration aggressively. Bank loans may also offer a more compelling inflation-sensitive complement than Treasury Inflation-Protected Securities (TIPS) in portfolios that can tolerate credit risk.

Markets had plenty of news to digest over the past week, from the U.S.–Canada tariff spat, to the economic escalation against Iran, to Fed policymakers meeting in Jackson Hole, Wyoming. But markets kept their eyes mostly on one segment: bonds. The normally staid bond market has moved from background noise to front-page signal. The 30-year Treasury yield recently climbed above 5.3%, its highest level in nearly two decades, even after a run of softer economic data that normally would have pulled yields lower. Yields quickly fell after Treasury signaled it would step up support for longer-dated debt (more detail on Treasury's buyback announcement below). Markets heard a clear message: policymakers are paying attention to the long end of the curve.

The question is not simply whether yields can rise further, but rather what higher yields are telling us. If they reflect inflation risk and fiscal deterioration, investors should be cautious. If they reflect stronger real growth, productivity, and a higher-return capital investment cycle, higher rates may be less threatening—and potentially more investable. That distinction matters for portfolio allocation.

Why are long-term yields rising?

This is more than a simple inflation scare. Recent rates research argues the rise in long-end yields looks more like a real term-premium story than a loss of confidence in the Fed's inflation target. The break-even inflation rate remains broadly consistent with a 2% inflation environment, while the long end has had to absorb a worsening fiscal outlook, heavier Treasury supply, AI-related corporate duration issuance, and a buyer base that is more private and more price-sensitive than it was a decade ago.

That supply-demand story now has a new twist: AI. Data center construction and hyperscaler capital spending have continued despite higher rates because expected returns and strategic capacity needs remain high. That may help explain why the economy has slowed less than many expected when the Fed began hiking. It also means the bond market is absorbing not only a larger public-sector borrowing requirement, but also a private-sector investment boom that competes for long-duration capital.

Why did Treasury's buyback announcement matter?

Treasury said it would increase liquidity-support buybacks in the 10-to-30-year sector, raising the maximum size of each operation from $2 billion to at least $4 billion from September 9 through November 4. The immediate reaction—lower long-end yields and firmer risk assets—suggested the market interpreted the announcement as more than a technical adjustment.

The program itself is not large enough to permanently solve the oversupply problem. But the signal matters. Treasury buybacks, potential changes to coupon issuance, regulatory changes that could encourage bank Treasury demand, and political pressure on the Fed all point in the same direction: policy may increasingly lean against higher real yields.

What does this mean across asset classes?

For equities, the message is nuanced. Higher long-term yields raise the hurdle rate for valuations, particularly for long-duration growth stocks. But higher rates are not automatically bearish if they reflect stronger real growth, better productivity, and a powerful capital investment cycle. The key is separating companies that can earn returns above their cost of capital from those that simply benefited from the 2009–2022 era of cheap money.

For housing and consumers, the transmission is more direct through the 10-year Treasury yield, which is more closely tied to mortgage rates than the 30-year bond. A sustained move higher in intermediate and long-term yields can weigh on affordability, housing turnover, and refinancing activity. For corporate borrowers, the impact depends on balance-sheet quality: cash-rich companies with high-return investment opportunities can keep spending, while weaker borrowers face a higher refinancing hurdle.

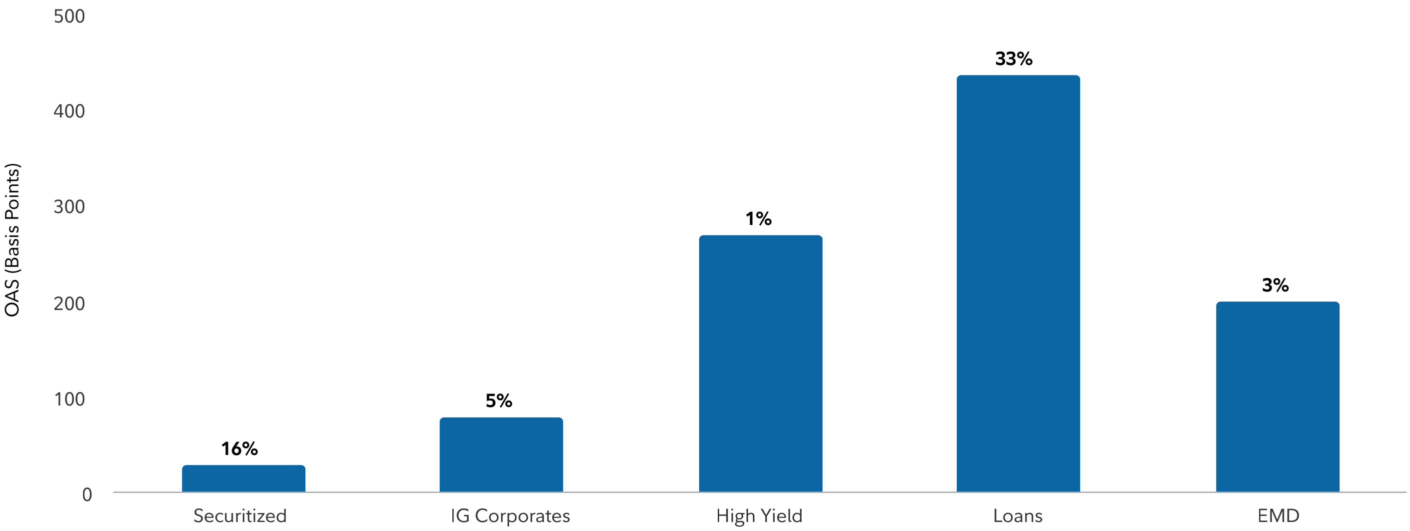
For portfolio construction, the message may be even bigger. The economic regime is changing, and the zero-rate playbook that worked from 2009 through 2022 is becoming less reliable. Investors may need more balance: Assets that benefit from productivity and nominal growth, paired with fixed income that now offers income, diversification, and potential downside protection if growth disappoints.

Where are the opportunities in fixed income?

The opportunity is that starting yields are now doing more of the work. From both a nominal and real yield perspective, Treasuries look modestly attractive relative to long-term assumptions. Some signals may support a more constructive stance toward bonds: Yields have risen more than the historical mid-cycle average, inflation expectations appear largely priced in, global growth signals are only modestly positive; technical momentum may be ripe for reversal, and policy pressure is increasingly pointing toward lower rates. That does not require a large duration extension beyond the broader bond market. The more balanced opportunity may be holding a duration profile closer to the Barclays Aggregate Bond Index while emphasizing the belly of the curve, where investors can potentially benefit from income, rolldown, and any decline in rates without making an outsized long-duration bet. As outlined in Exhibit 1, spreads across many higher-risk bond sectors are near their tightest levels in two decades, suggesting attractive opportunities for higher-quality fixed income.

Exhibit 1: Spreads across many higher-risk bond sectors remain compressed, suggesting more attractive opportunities among higher quality issuance.

Spreads and 20-year percentile rankings



Source: FactSet, Pitchbook, a Morningstar Company, as of 8/21/26. Twenty-year percentile spread rankings for securitized, IG corporates, high yield, loans, and EMD segments, with the lower percentages suggesting spreads at their tightest levels over the time period. Securitized bonds represented by the Bloomberg US Aggregate Securitized Index (MBS, ABS, and CMBS); IG corporates represented by the Bloomberg US Corporate Investment Grade Bond Index; high yield represented by the ICE BofA US High Yield Constrained Index; Loans represented by the Morningstar LSTA US Leveraged Loan 100 Index (four-year discounted spreads). EMD represented by the JP Morgan Global Diversified Index. See endnotes for index definitions.

We see opportunities across the following segments, where actively-managed security selection will be key:

- **Intermediate Treasuries:** The belly of the curve may offer the best balance between income and rate risk, especially if the curve remains steep and policymakers lean against further long-end pressure.
- **Core bonds with aggregate-like duration:** Investors may not need to make an aggressive long-duration call to benefit if rates fall. A balanced core bond allocation can still participate through carry, rolldown, and measured duration exposure.
- **Shorter- and intermediate (1–7 years) duration:** limiting exposure to the 10+ year segment may provide less interest rate sensitivity.
- **Investment-grade corporates:** All-in yields remain attractive, but heavy long-dated issuance—especially from AI and hyperscaler borrowers—argues for quality, valuation discipline, and sector selectivity.
- **Securitized credit including agency mortgage-backed securities (MBS):** Higher mortgage rates have pressured housing, but agency MBS may benefit if rate volatility stabilizes and investors are compensated for spread and prepayment risk.
- **Municipal bonds:** Tax-equivalent yields may be compelling for higher-income clients, particularly where credit quality remains strong.
- **Bank loans:** For investors seeking an inflation-sensitive income stream, loans may be more attractive than TIPS because their floating-rate coupons can adjust with short-term rates, though credit quality and liquidity risks require selectivity.
- **High yield:** Carry remains appealing, but spreads are not wide enough to ignore refinancing risk. This is a market for selectivity, not yield-chasing.

What is the bottom line for portfolios?

The client conversation should start with one question: Are higher yields a threat, or are they finally the income opportunity investors have been waiting for? The answer is both. Higher rates can pressure valuations, housing, and lower-quality borrowers. But they also restore the role of fixed income as a source of income, ballast, and potential portfolio insurance.

For clients sitting in cash, today's market offers a chance to move selectively into higher-quality income rather than wait for the perfect entry point. For clients already invested, the focus should be on intentional duration, strong credit selection, and inflation-aware income—not simply reaching further out the curve. The bond market is sending a warning about fiscal supply and term premium, but it may also be flashing a rare green light for disciplined fixed-income investors who stay anchored in the belly of the curve and avoid overextending duration.

Disclosures

ICE BofA US High Yield Constrained Index is a modified market capitalization-weighted index of U.S. dollar-denominated, below-investment-grade corporate debt publicly issued in the U.S. domestic market.

The J.P. Morgan GBI-EM Global Diversified Index provides a comprehensive measure of local currency-denominated, fixed rate, government debt issued in emerging markets.

Morningstar LSTA US Leveraged Loan 100 Index is designed to measure the performance of the 100 largest facilities in the U.S. leveraged loan mark

The Bloomberg US Securitized Index represents the securitized portion of the Bloomberg U.S. Aggregate Index and includes MBS, ABS, and CMBS. It tracks all USD-denominated investment-grade, securitized issues within the parent index. MBS must have a weighted average maturity of at least one year. CMBS and ABS must have a remaining average life of at least one year.

The Bloomberg US Corporate Index measures the investment-grade, fixed-rate, taxable corporate bond market. It includes USD-denominated securities publicly issued by U.S. and non-U.S. industrial, utility, and financial issuers.

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