

The Factors Pushing DM Rates Higher

WEEKLY VIEW FROM THE DESK | May 18, 2026

[LINK TO WEEKLY RETURNS TABLE](#)

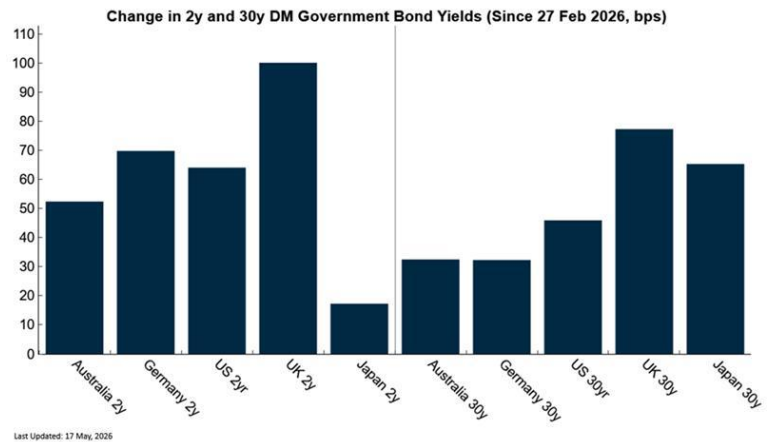
MACRO

- The repricing in long-term developed market interest rates reflects a combination of resilient economic activity, inflation persistence, and fiscal concerns, particularly in the UK. The front-end selloff was also notable and was tightly linked to the repricing of Fed expectations in the face of higher energy prices and a strong U.S. economy. Higher U.S. yields were behind the gains in the USD relative to most major currencies.
- It's an environment where the AI boom, fiscal stimulus, and buoyant equity markets are providing meaningful tailwinds to demand while the ongoing supply shock from Iran continues. Rates and inflation markets have significantly repriced the Fed and inflation expectations. On the inflation front, the market sees elevated inflation again in the 1-year inflation swap, but interestingly the 1Y1Y inflation swap (see chart), which reflects expectations around more persistent price pressures, sits at the top end of the post 2022 range.
- Our view on the recently concluded U.S.-China summit consists of a reframing of the U.S.-China relationship toward "constructive strategic stability" with a proposed 3-year framework and both sides signaling desire to avoid trade escalation.
- In the near term, it's a positive market outcome, but perhaps more negative for the U.S. in the long term given the limited progress on China's structural advantages, such as manufacturing dominance, and the risk of the U.S. conceding strategic ground. The durability of the detente depends heavily on Taiwan policy decisions.



DEVELOPED MARKET RATES

- Bond yields have risen across G10 economies since the Iran-US conflict began. In most cases the repricing has been more aggressive at the front-end, reflecting the need for central banks to tighten policy to contain the impact of higher energy prices on inflation. This has led to flatter yield curves in all five countries in the chart to the right but Japan.
- The moves in the UK are notable and they reflect at least three developments. First, the UK relies on imported energy and therefore is directly exposed to the war in Iran. Second, inflation in the UK has been persistently high even in the face of a soggy economy. Third, gilts markets have been engulfed by political noise.
- We've taken a more constructive stance in the MBS market given signs of rate stabilization and still supportive technicals/carry profile. It's an attractive backdrop for primary sources of local demand with signs of rate stabilization/vol containment. The market has absorbed forced selling from servicer community, which is typically an effective contrarian indicator. We also expect supply to settle in lower (~3B per day) after last week's modest flush.



IG CORPORATES

- Last week saw about \$50B in new issuance, among 35 issuers, leaving May at just under \$100B and YTD at about \$950B. Deals last week were 4x oversubscribed. Yields continue to keep the buying strong both from insurance accounts and overseas buyers. Rate volatility could impact the market, but if rates remain at current levels it will continue to be supportive.
- NextEra has agreed to buy Dominion Energy in an all-stock deal valued at about \$67B, marrying two large utilities as demand for electricity to power data centers continues to surge.
- In Europe, IG continues to benefit from positive technicals and over €14B was issued last week, with demand still strong and concessions remaining healthy. All eyes remain on Hormuz Strait headlines with the market continuing to price in an opening in the shortish term, though we remain cautious.
- U.K. politics added to gilts volatility as fears of a leadership challenge to Prime Minister Keir Starmer may lead to a distinctly more left-leaning PM, which in turn leads to spending fears and lower gilts.

LEVERAGED FINANCE

- U.S. high yield spreads were tighter last week, despite higher bond yields, climbing inflation data, and ongoing geopolitical concerns. Capital market activity remains robust but easily absorbed as technicals remain strong and inflows continue. Strong YTD AI-related issuance is nudging the market into a net supply surplus—the first in many years.
- All credit tiers saw negative total returns last week, with higher quality outperforming. Recent spread tightening in BBs has pushed the CCC/BB spread ratio to 10-year highs as accounts continue to bid up the higher-rated portion of the market. Meanwhile, total returns were mixed across sectors, with paper (+2.45%), containers (-0.16%), and energy (-0.17%) outperforming. HY funds reported their sixth consecutive weekly inflow totaling +\$943M, which amounts to +\$7.2B over the period. YTD, outflows for HY bond funds now total -\$2.9B. Fourteen high yield bond deals priced last week for \$9.6B.
- U.S. bank loans saw another positive week, with BBs leading the way. The primary market remained busy, with 33 deals launching last week and 27 pricing for \$32B. The vast majority of issuance continues to be opportunistic in nature (e.g., dividend recaps and repricings). Medline notably priced a \$2.75B facility at SOFR+150, which is among the tightest spreads in recent memory. Meanwhile, repricing activity continues, with about 14 issuers already in the queue this week to reprice their loans lower.
- European high yield bond spreads continued to tighten last week and are now tighter for the year. Amid the tightening, BB spreads now reside in the fifth percentile of the past three years and in the first percentile since 2010 as performing credit remains in high demand. Primary issuance was busy, with €3B in total issuance. However, just €350M of that was new money. On the loan side, activity picked up following the recent pause, but new-money issuance remains scant.

EMERGING MARKETS

- We are constructively cautious in our short-term view for EM hard currency sovereign spreads. The global backdrop is “supportive enough,” but cracks are beginning to appear. There is uncertainty about the status of Iran talks, movement through the Strait, and the supply shock’s economic impact. These factors pressured some risk markets, especially given a selloff in DM rates markets. Last week saw modest spread decompression, but the theme remains dispersion within and across credit rating and sensitivity categories. EM flows have recovered and remain positive. While investors have increased risk, most are not maxed out, as evidenced by continued appetite for record new issuance. However, it’s more about relative positioning in the current environment. We have reduced overall market risk and magnified our conviction overweights and underweights.
- There was broad weakness across regions in EMFX last week, as the USD strengthened and global yields climbed. An effective stalemate in the Iran conflict is keeping pressure on oil, so the market fears more prolonged inflation as well as growth risks. USD went from what we thought was poor performance to now showing signs of life. We think over the near term, USD is likely to benefit from higher yields that can potentially trigger volatility across assets. We have reduced short USD beta.
- EM rates also came under pressure from the selloff in core rates, and most yields are now higher than their worst levels in mid-March. The only exception is Hungary amid an EU convergence story and NBH cutting the FX swap rate. As USD strengthened, curves started to bear steepen instead of the bear flattening that we observed in early March. In our portfolio, we have taken down risk by increasing our underweight in Chile and Poland and reducing our overweight in Mexico and South Africa. Without progress in the Strait soon, we could see further weakening in global fixed income and even spread products. A rise in the broad USD is a further headwind to EM local markets. Market conditions require caution and nimbleness.
- EM corporate spreads tightened last week, as prices were slower to adjust to rising rates. Earnings season continued to progress with credit-neutral results from Marfrig, among others. Vedanta, which we own across accounts, was upgraded to BB- by S&P with bonds compressing to low 7%. The new issue market remained active, and we played in the Pampa Energia tap for corporate accounts to cover underweights. We added to our CSN position in some corporate and high-risk accounts. Braskem’s first-quarter results showed an improvement in EBITDA as expected but higher-than-expected cash burn due to working capital usage.

SECURITIZED PRODUCTS

- CMBS conduit AAA spreads were 1-2 bps tighter. Subordinate tranches were 5 bps tighter, with As in the +180 context and BBB-'s in the mid +400s. SASB spreads tightened in the primary market. Top-tier AAA floaters are pricing in the +120-125 area. Fixed-rate seniors are trading in the low to mid- +90s amid increased dispersion by property type and sponsor. CRE CLO spreads were tighter, with AAA new issue in the low +130s, while tier-two issuers were 5-25 bps wider. Five deals priced—one SASB, two CRE CLO, and two agency.
- In RMBS, Non-QM new issuance remained firm, with COLT pricing AAAs at T+120 and mezzanine demand particularly strong. As were clearing at T+155, leaving only a 35 bp AAA/A gap. Sub-tranches also saw renewed interest, with BBBs at T+185 and BBs at T+270. Second-lien spreads tightened across the stack, with all classes coming in roughly 5 bps tighter than prior prints. CRT spreads were rangebound. Given recent tightening, we have turned slightly more cautious over the near term.
- U.S. CLO spreads tightened as technicals continue to benefit from elevated investor cash balances, though the pace of tightening is beginning to slow as AAA levels approach YTD tight. Dispersion is increasingly pronounced in the lower mezzanine tranches, reflecting differences in underlying portfolio quality and tail risk exposure. In European CLOs, spreads tightened last week and we expect sentiment to firm as demand continues to build. U.S. issuance was \$12B across 12 deals and European issuance was €2.9B across seven deals.
- ABS markets remain firm and spreads generally continued to grind tighter. ABS spreads are at, or through, beginning of the year levels. Primary market supply remains heavy, but demand is strong with most deals well oversubscribed and pricing well inside of initial guidance.

MUNICIPALS

- Muni rates rose on the week, following Treasury rates higher on an Iranian war and inflation narrative. Higher new issue supply, higher rates, and lighter reinvestment also pressured the market. With inflation coming back into focus and higher new issue supply we remain cautious around the muni market over the next couple of weeks, placing a higher premium on liquidity and keeping cash balances elevated.
- June marks the beginning of more positive technicals in the form of higher reinvestment and more modest new issuance, but we remain negative on the market, which is sitting near tight on a relative-value basis and will suffer from higher new issue supply in the near term. We’ve used the student loan new issue calendar as an opportunity to buy higher- quality cheaper paper, funding it with airport sales, which have tightened YTD.

THE RETURNS TABLE AS OF MAY 15, 2026

	Duration	YTM	OAS	WTD	Yield / OAS change (bps)				Total return (%)				
					MTD	QTD	YTD	Prior year	WTD	MTD	QTD	YTD	Prior year
Sovereign rates													
U.S. 2-Year	1.86	4.07	---	19	20	28	60	11	-0.27	-0.21	-0.07	0.16	3.14
U.S. 5-Year	4.44	4.26	---	26	25	32	53	20	-1.01	-0.89	-0.92	-0.93	2.92
U.S. 10-Year	7.99	4.59	---	24	22	28	43	16	-1.65	-1.36	-1.57	-1.67	3.24
U.S. 10-Year Breakeven	--	2.51	---	5	3	21	27	18	---	---	---	---	---
U.S. 10-Year TIPS	4.35	2.07	---	18	19	6	17	-1	-1.20	-0.78	0.73	0.66	5.83
U.S. 20-Year	12.43	5.14	---	22	18	22	34	22	-2.45	-1.73	-2.26	-2.53	1.71
U.S. 30-Year	15.29	5.12	---	18	15	21	27	23	-2.65	-1.89	-2.74	-2.45	1.23
U.S. SOFR	---	---	---	-5	-11	-13	-32	-76	0.07	0.15	0.46	1.38	4.13
UK 10-Year	7.46	5.17	---	26	16	26	70	51	-1.62	-0.86	-1.09	-2.56	1.54
Germany 10-Year	8.27	3.17	---	16	13	16	31	55	-1.11	-0.79	-0.75	-1.08	-0.97
Switzerland 10-Year	8.83	0.51	---	15	13	17	23	19	-1.20	-1.04	-1.35	-1.55	-1.23
Japan 10-Year	7.72	2.71	---	23	19	36	65	124	-1.41	-1.05	-1.98	-3.35	-6.59
Australia 10-Year	7.81	5.07	---	8	1	10	33	54	-0.44	0.21	0.02	-0.60	0.74
Canada 10-Year	7.97	3.69	---	22	15	22	26	54	-1.55	-0.96	-1.21	-0.71	-0.21
Major fixed income multi-sector indices YTW													
Global Aggregate Unhedged	6.30	3.92	27	0	0	-5	0	-7	-1.52	-0.96	0.27	-0.81	3.03
Global Aggregate Hedged	6.30	3.92	27	0	0	-5	0	-7	-0.93	-0.54	-0.25	-0.40	3.08
U.S. Aggregate	6.01	4.81	26	1	1	-4	0	-8	-1.14	-0.78	-0.66	-0.71	4.48
Euro-Aggregate (Unhedged)	6.26	3.38	43	1	-2	-8	1	-12	-0.83	-0.42	0.04	-0.60	0.54
Japanese Aggregate	7.90	2.35	1	0	0	0	0	0	-1.40	-1.11	-1.77	-3.34	-6.35
Major fixed income credit indices YTW													
Mortgage-Backed (Agency)	5.66	5.12	26	7	6	2	4	-11	-1.39	-0.95	-0.88	-0.48	5.77
Global IG Corporate Bonds	5.97	4.82	77	-3	-4	-16	-2	-19	-1.27	-0.73	0.54	-0.74	5.52
U.S. IG Corporate Bonds	6.90	5.27	73	-4	-5	-15	-4	-18	-1.04	-0.52	-0.07	-0.60	5.50
European IG Corporate	4.61	3.65	79	-2	-3	-18	1	-22	-0.48	-0.18	0.76	-0.24	1.96
U.S. High Yield Bonds	3.32	7.17	267	1	-1	-50	1	-42	-0.49	-0.30	1.38	0.88	7.12
European High Yield Bonds	3.16	5.83	277	-13	-20	-71	-5	-60	-0.12	0.36	2.29	0.76	3.99
U.S. Leveraged Loans	0.3	8.97	481	1	-7	-33	26	7	0.08	0.35	1.58	1.10	5.25
European Leveraged Loans	0.3	7.94	471	-5	-14	-66	-3	-1	0.23	0.47	2.20	1.36	3.84
EM Hard Currency Sovereigns	6.31	7.07	237	-1	-11	-52	-17	-96	-1.12	-0.30	2.56	2.02	12.68
EM Corporates	4.38	6.59	212	-9	-12	-37	-25	-58	-0.47	-0.17	1.44	1.23	7.70
EM Currencies	---	6.07	---	0	0	-1	0	0	-1.10	-0.04	2.35	1.59	7.24
EM Local Rates	5.24	6.32	6	0	0	0	0	0	-0.61	-0.21	0.82	-0.31	4.89
CMBS	3.73	4.89	64	-2	-3	-7	-11	-24	-0.75	-0.51	-0.34	-0.02	4.94
ABS	2.81	4.61	46	-2	-3	-7	-6	-18	-0.41	-0.22	0.07	0.38	4.64
CLOs	3.98	5.21	128	0	-1	-6	-4	-11	0.10	0.25	0.79	1.82	5.34
Municipal Bonds	6.31	3.77	---	11	9	0	18	-27	-0.58	-0.37	0.77	0.59	5.81

	Total return (%)						Change (%)						
	Level	WTD	MTD	QTD	YTD	Prior year	Spot	WTD	MTD	QTD	YTD	Prior year	
Equity / volatility indices													
S&P 500 Index	7,409	0.2	2.8	13.6	8.7	26.7	FX / commodities						
DAX	23,951	-1.6	-1.4	5.6	-2.2	1.1	EUR / USD	1.2	-1.4	-0.9	0.6	-1.0	3.9
Stoxx 600	607	-0.7	-0.3	5.3	4.4	14.6	USD / JPY	158.7	1.3	1.4	0.0	1.3	9.0
Nikkei 225	61,409	-2.1	3.6	20.3	22.9	65.6	GBP / USD	1.3	-2.2	-2.0	0.7	-1.1	0.2
Shanghai Composite	4,135	-0.9	0.7	6.4	4.5	25.6	EUR / CHF	0.9	0.0	-0.2	-1.0	-1.7	-2.2
MSCI ACWI Index	1,099	-0.5	2.2	12.6	9.1	27.7	USD / CHF	0.8	1.3	0.7	-1.6	-0.7	-5.9
FTSE 100	10,195	-0.2	-1.5	0.7	4.2	21.8	USD (DXY)	99.3	1.4	1.3	-0.7	1.0	-1.6
MOVE Index	80	18.8	10.8	-16.8	24.9	-19.0	Oil	105.4	10.5	0.3	4.0	83.6	71.1
VIX Index	18	7.2	9.1	-27.0	23.3	3.4	Gold	4540.1	-3.7	-1.7	-2.7	5.1	40.1

Past performance is not a guarantee or a reliable indicator of future results. Sources: Bloomberg except EMD (J.P. Morgan), HY (ICE BofAML), Bank Loans (S&P), and CLOs (Palmer Square). European returns are unhedged in euros unless otherwise indicated. An investment cannot be made directly in an index.

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