

Developed Market Rates Q1 2026 Outlook with John Young

As we enter 2026, developed market yield curves are likely to continue steepening, extending the trends established in 2025.

U.S. Treasuries exhibited strong performance last year, driven by pronounced bull steepening. Front-end yields declined sharply following 75 basis points of Federal Reserve cuts in Q4, while long duration yields ended the year broadly unchanged.

With policy now closer to neutral, the market is approaching an inflection point. Recent Fed commentary suggests a higher bar for further easing, with additional cuts likely contingent on material weakening of economic data. At the same time, policy uncertainty is increasing as Chair Powell's term concludes in May. While leadership transitions may introduce near-term volatility, we expect the Fed to maintain a broadly dovish bias, with risks still skewed towards accommodation.

We believe the low volatility regime observed late last year is also unlikely to persist. As fiscal, geopolitical, and monetary uncertainties reemerge, volatility should normalize. In this environment, we expect continued curve steepening, driven by a gradual repricing of term premia and evolving expectations around future Fed leadership.

Curve steepening has been a global theme, most notably in Japan. The Bank of Japan's December hike to three quarters of a percent marked the highest policy rate in decades, and we expect an additional two to three hikes later this year. In Europe, curves have likewise steepened, as the European Central Bank signaled the end of its easing cycle. While 10-year Bund yields moved to multi-year highs, persistent downside risk to inflation leave scope for renewed ECB accommodation later this year.

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