JULY 2026

Fixed Income Focus

Summary

1. **First Fed meeting with Kevin Warsh:** The June FOMC marked a clear policy shift: inflation is now the main risk, and the Fed has dropped forward guidance, increasing the likelihood of market surprises and volatility. We now expect a single rate hike in December, after the midterms and amid a tightening labor market.

2. **ECB hiked as largely expected:** The ECB, operating under a stricter inflation-targeting framework raised its policy rate in June 2026 to counter inflationary pressures. We expect a wait-and-see approach thereafter.

3. **Neutral our opinion on US bonds:** The expected balance sheet reduction and the removal of the so-called forward guidance suggests a comeback of the higher risk premium for longer-dated bonds. We have increased our 12-month target for the US 10-year yield to 4.50%.

4. **We downgrade core Eurozone govies from Positive to Neutral.** Yields fell back and the expected return is less attractive. We favour maturities of 7-10 years. We keep our target on the German 10-year yield at 2.75%.

5. **We downgrade to Neutral our opinion on UK bonds:** Yields fell back after the political pressure started to come down. We keep our target on the 10-year UK government bond yield at 4.30%.

6. **Selective opportunities in corporate bonds:** We prefer EUR and GBP IG corporate bonds (Positive view) over USD IG bonds (Neutral view).

7. **Upgrade high yield bonds from Negative to Neutral:** The outlook has improved after a deal to end the conflict was announced, significantly reducing recession concerns. However, the expected return remains limited as risk premiums stay near historical lows.

8. **Too early to come back on EM Bonds:** The three primary drivers—valuation, currency outlook, and monetary policy expectations— are not supportive. We need to monitor the developments in the Middle-East and the expected re-opening of the Strait of Hormuz.

Writing completed on July 2nd 2026

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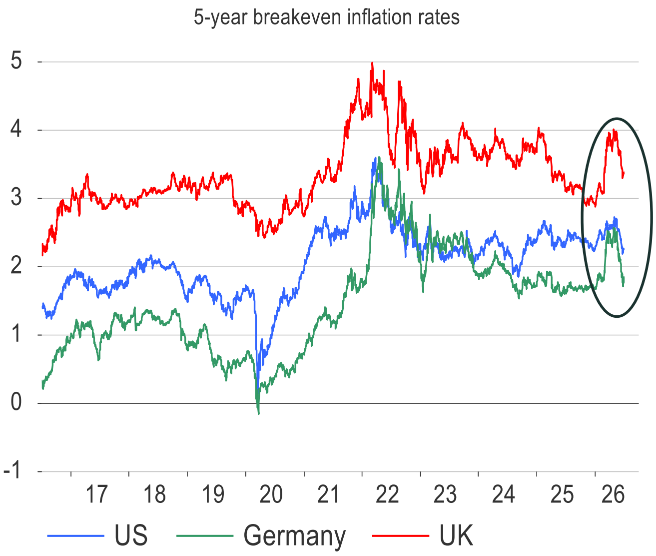
CHART OF THE MONTH: INFLATION EXPECTATIONS – BREAKEVEN 5Y



Source: LSEG Datastream, 03/07/2026

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BNP PARIBAS WEALTH MANAGEMENT

The bank for a changing world

Topics in Focus

Key takeaways from the first Warsh Fed meeting

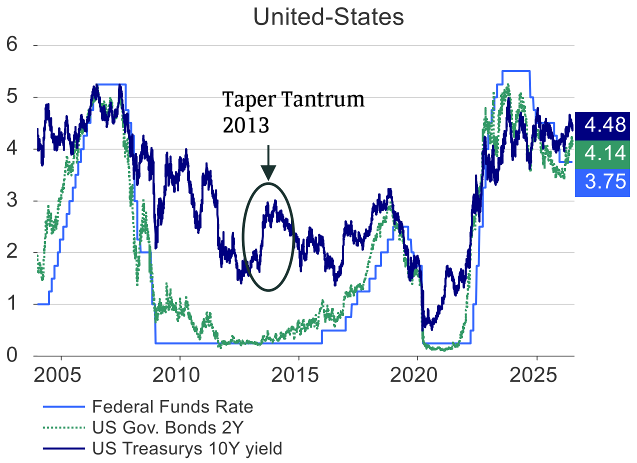
We see 2 takeaways from the first Fed meeting with Kevin Warsh: (1) A more hawkish tone that led us to anticipate a rate hike in December; (2) Confirmation of the balance sheet reduction and the removal of forward guidance.

A more hawkish tone: The June FOMC meeting signaled that tightening of policy is on track for this year. The meeting statement also contained a very strong assertion about inflation: "The Committee will deliver price stability." Our view that the Fed will raise rates in December rests on the expectation that the labor market may tighten, but only moderately. A move before the elections could be politically sensitive. Further hikes seem unlikely because we expect inflation to peak later this year, and the Fed's wage tracker does not indicate major pressure. The Fed is also building the argument that AI is a productivity shock, which could limit the need for additional rate hikes.

Towards a higher term premium: As mentioned in our last month publication, past episodes illustrate the sensitivity of rates to balance sheet signaling. In 2013, the "taper tantrum" caused real yields to jump about 100 bps after the Fed hinted at tapering QE. With a gradual and well communicated runoff, market disruption should remain limited this time. It is likely that the Fed will simply stop reinvesting bonds that come to maturity. The second—and more important—driver of a higher spread for long dated maturities is that the Fed intends to stop using forward guidance. Forward guidance allows the Fed to shape the probability distribution of future policy rates, keeping that distribution narrow and stable. By doing so, it anchors inflation expectations near its target and reduces the volatility of both expectations and actual inflation. Removing forward guidance therefore creates room for a larger term premium.

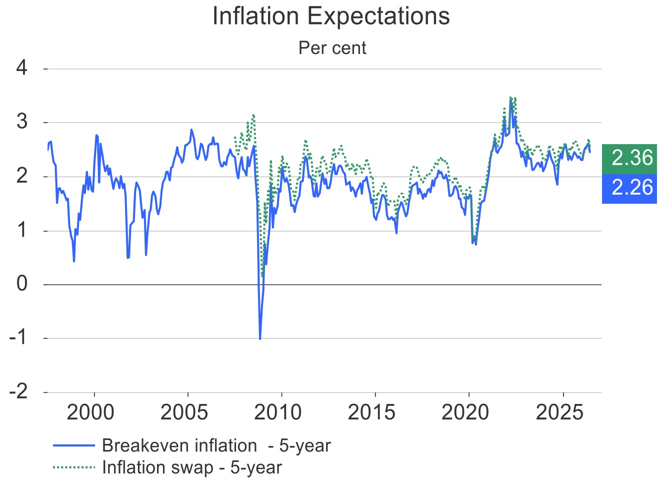
We upgraded our 12-month yield target for the 10-year U.S. government bond to 4.50%.

THE STRUCTURE OF US RATES



Source: LSEG Datastream, 03/07/2026

LONG-TERM INFLATION EXPECTATIONS



Source: LSEG Datastream, 02/07/2026

Investment Conclusion

The June FOMC meeting signaled a more hawkish tone. Our view that the Fed will raise rates in December rests on the expectation that the labor market may tighten, but only moderately. We expect a moderate rise in long-term yields due to the upcoming balance sheet reduction. A second driver of a higher spread for long dated maturities is that the Fed intends to stop using forward guidance. Indeed, that could augment the volatility of inflation expectations.

Central banks

Fed is expected to hike in December

European Central Bank (ECB)

The ECB raised rates by 25 basis points in June, emphasizing that the move responded to current economic conditions rather than being a pre-emptive step. President Lagarde described the decision as “robust” and dismissed worries that tightening would exacerbate supply side shocks. She referred back to her March speech, in which she outlined three possible scenarios: (1) A short lived shock – now considered implausible; (2) A temporary shock that calls for a “measured” response; (3) A persistent shock that requires a “forceful” reaction. Since ECB Member Isabel Schnabel has characterized the shock as “very large” and enduring, the bank is leaning toward the latter two scenarios.

Outlook: Further hikes are unlikely unless wage driven inflation becomes more evident. The current debate centers on whether persistent inflation will demand additional tightening. After the June 2026 rate rise, the ECB is expected to keep policy rates unchanged for the rest of the year.

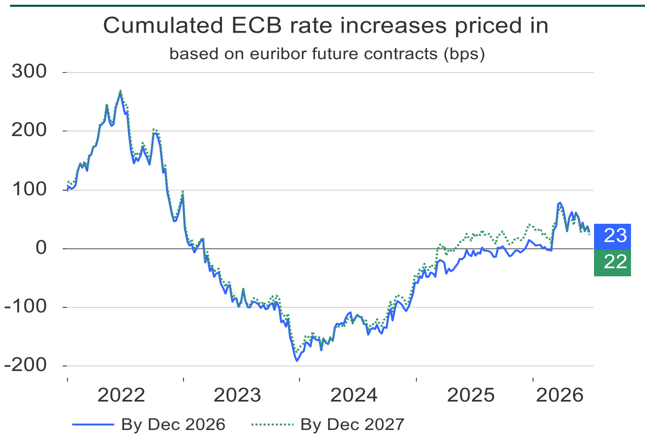
US Federal Reserve (Fed)

The June FOMC, chaired by the newly appointed Chair Kevin Warsh, signaled a decisive policy pivot. Fed officials moved away from an anticipated rate cut and, for the first time, nine members now forecast at least one hike before the end of the year. In addition, the Fed abandoned the Powell era “dual mandate balance” between inflation and employment, flagging inflation as the primary risk.

Chair Warsh also announced the creation of five expert task forces to examine, among other topics, inflation targeting frameworks, balance sheet policy, and the economic implications of artificial intelligence. Their findings are expected by late 2026. In contrast to his predecessor, Warsh provided no forward guidance, raising the likelihood of market surprises and heightened volatility and ushering in a more data driven era for Fed policy.

Outlook: Markets are currently pricing in almost a full percentage point hike at the October meeting, but we disagree. Given the political sensitivity of the November elections, we now expect a single rate increase to be postponed until December, after the midterms and amid a still tightening labour market.

MARKET PRICING FOR THE ECB



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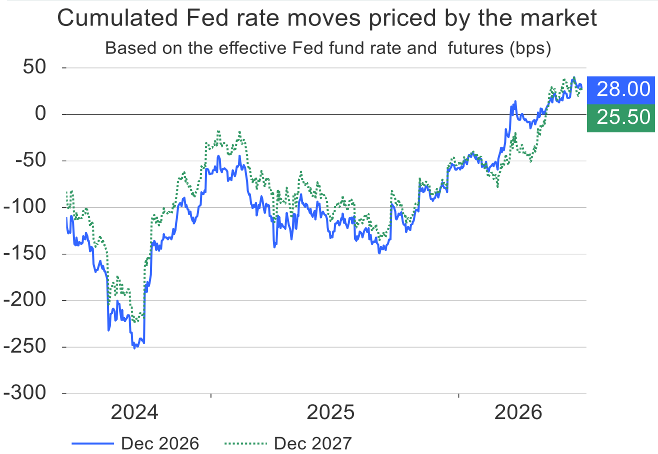
MARKET PRICING FOR THE FED



Source: LSEG Datastream, 03/07/2026

INVESTMENT CONCLUSION

The June FOMC meeting signaled that policy tightening is proceeding as inflation remains high. Consequently, we now expect only one additional rate hike in December. This outlook rests on two assumptions: first, that labor-market conditions will tighten only gradually; and second, that policymakers will be reluctant to act in the immediate run-up to the November midterm elections. In the euro area, the ECB is expected to keep rates unchanged for the remainder of the year.

Government Bond yields

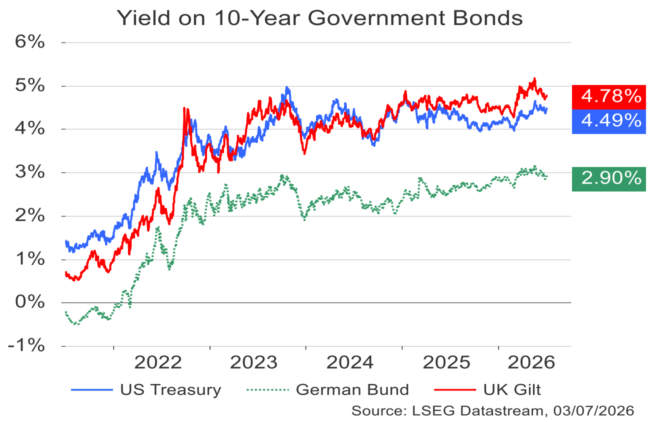
Back to neutral eurozone and UK Govies

Neutral Core Eurozone Long Dated Bonds: We downgrade core Eurozone govies from Positive to Neutral. Yields fell back as inflation expectations decreased in line with lower oil prices. The expected return is less attractive. We favor maturities of 7-10 years.

Neutral Stance on UK Government Bonds: Andy Burnham is expected to assume leadership by September. Markets are likely to remain cautious, and any lingering fiscal uncertainty ahead of the next budget could keep a small risk premium. Yields fell back in line with lower oil prices. The expected return is less attractive.

Neutral Stance on US Government Bonds: The US 10-year yield is hovering in a narrow band around 4.40 % after briefly breaking 4.60% mid-May. We have increased our 12-month target to 4.50% and we could see the yield overshooting our new target.

10-YEAR GOVERNMENT BOND YIELDS



	Maturity (years)	02/07/2026	3-month target	12-month target
USA	Policy rate	3.75	3.75	4.00
	2	4.11	4.10	4.00
	5	4.19	4.20	4.20
	10	4.45	4.50	4.50
	30	4.97	4.95	4.95
Germany	Policy rate	2.25	2.25	2.25
	2	2.48	2.50	2.25
	5	2.60	2.70	2.60
	10	2.89	2.90	2.75
	30	3.48	3.40	3.25
UK	Policy rate	3.75	4.00	4.00
	2	4.10	4.15	4.00
	5	4.29	4.25	3.90
	10	4.76	4.80	4.30
	30	5.48	5.40	5.10
Japan	Policy rate	1.00	1.00	1.50
	2	1.37	1.40	1.40
	5	1.92	1.90	1.90
	10	2.76	2.75	2.75
	30	4	4	4

Source: Refinitiv Datastream, BNP Paribas WM

Investment Conclusion

We turned neutral on core-Eurozone long-dated bonds and on UK gilts. Indeed, yields fell back as inflation expectations decreased in line with lower oil prices. Expected return are less attractive. We remain neutral on U.S. Treasuries. Yields are close to our new target and medium-term upside risks for the yield remain high.

More visibility for corporate bond markets

Risks are lower given the recent deal announcement and oil price fall

With governments still issuing plenty of debt while companies have become more selective, investors are finding a noticeable gap between the two. That "scarcity" of corporate bonds has helped push spreads – the extra yield investors demand for taking on credit risk – to tighter levels, especially for higher quality issuers.

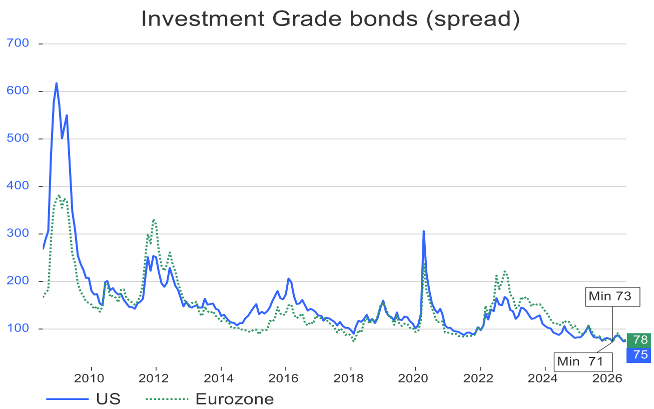
In the United States, spreads have already slipped into the 60 basis point range, a level not seen for several years, as the market digests a relatively modest supply of new issues. The picture is similar in Europe, where the "compression" of spreads is becoming a theme; many issuers are now trading at almost the same price, suggesting a "law of one price" is emerging. Sector by sector, the most attractive IG opportunities are in areas with limited new issuance. "Old economy" segments such as autos, chemicals and railroads have stayed quiet on the capital raising front, making their bonds relatively scarce and therefore appealing to yield seeking investors.

Conversely, the technology "hyperscalers" that are pouring money into AI are still issuing heavily, which keeps their spreads a touch wider. For investors who prefer a steadier profile, European financials and the new economy technology space (excluding the biggest AI driven issuers) look attractive.

Overall, the outlook for IG bonds remains upbeat: high yields continue to draw demand, the macro backdrop is still supportive, and the limited supply in many sectors should help keep spreads reasonably tight through the summer.

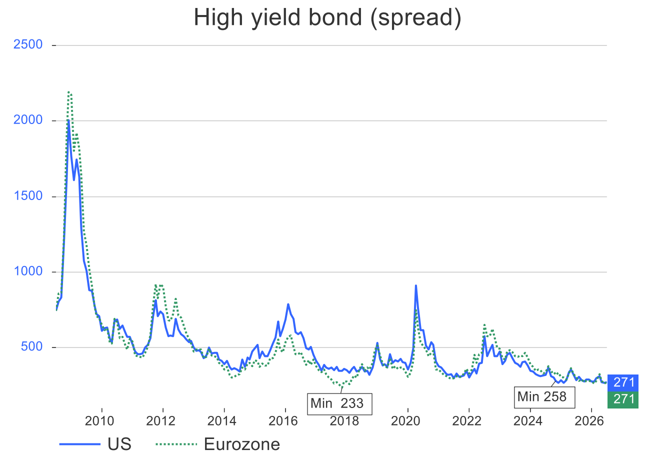
We upgraded corporate high yields back to Neutral mid June as a deal was announced. This deal and the sharp fall in oil prices reduced quite a lot the tail risk for corporate defaults. We do not think that those bonds will outperform other bonds as the risk premium (high yield corporate spreads) remains close to historical lows. We will need to monitor closely how the deal is implemented and to what extend the risks related to inflation and potential rate hikes falls further.

INVESTMENT GRADE CORPORATE BONDS



Source: LSEG Datastream, 02/07/2026

CORPORATE HIGH YIELD BONDS



Source: LSEG Datastream, 02/07/2026

INVESTMENT CONCLUSION

Overall, the outlook for IG bonds remains upbeat. the macro backdrop is still supportive, and the limited supply in many sectors should help keep spreads reasonably tight through the summer. We upgraded corporate high yields back to Neutral mid-June as a deal with Iran was announced. This deal and the sharp fall in oil prices reduced quite a lot the tail risk for corporate defaults. The expected return remain low given the recent valuation.

Our Investment Recommendations

Asset class	Zone	Our opinion	
Government bonds	Germany and core eurozone	=	We downgrade core Eurozone govies and UK govies from Positive to Neutral. Yields fell back and the expected return is less attractive. We favour maturities of 7-10 years.
	Non-core Peripheral countries	=	Neutral on non-core peripheral debt (Portugal, Italy, Spain, Greece).
	United Kingdom	=	Neutral on UK government bonds.
	United States	=	We are Neutral and prefer 2-5 years maturities. Neutral on TIPS.
Corporate bonds Investment Grade (IG)	Eurozone/United Kingdom United States	+ =	• Positive on eurozone and UK IG corporate bonds, and Neutral on US corporate bonds. • We prefer maturities up to 7 years in the eurozone and up to 5 years in the US. • Neutral on convertible bonds.
Corporate bonds High Yield (HY)	Eurozone and United States	=	• Neutral on corporate HY bonds. • Neutral on fallen angels and rising stars.
Emerging bonds	In hard currency	=	Neutral on EM hard currency bonds (sovereign and corporate).
	In local currency	=	Neutral on EM local currency government bonds to neutral.

Market Data

	10-year rate (%)	Spread to bund (bp)	Spread change 1 month (bp)
United States	4.49	---	
Germany	2.90	---	
France	3.71	81	19
Italy	3.70	80	7
Spain	3.40	50	8
Portugal	3.31	41	3
Greece	3.59	69	2

02/07/2026

Source: Refinitiv Datastream

	Yield (%)	Spread (bp)	Spread change 1 month (bp)
Corporate bonds IG EUR	3.44	78	2
Corporate bonds IG USD	5.21	75	1
Corporate bonds HY EUR	5.38	271	8
Corporate bonds HY USD	7.09	271	5
Emerging government bonds in hard currency	6.80	219	-13
Emerging government bonds in local currency	6.10	187	-13

02/07/2026

Source: Refinitiv Datastream

Valuation

Credits	Yield	Spread	10yr Avg Spread	2yr Spread Range		Spread Change			2yr Z-Score*
				Min	Max	Chg 1W	Chg 1M bp	Chg YTD	
Euro Corporate	3.44	78	117	71	127	1	2	0	▲
Single-A	3.36	70	101	64	116	0	1	-1	▲
Euro High Yield	5.38	271	376	256	429	7	8	1	▲
BB	4.42	173	277	158	303	1	6	4	▲

* Z-score 2y is based on the spread

Source: LSEG Datastream , BNP Paribas WM, 02/07/2026

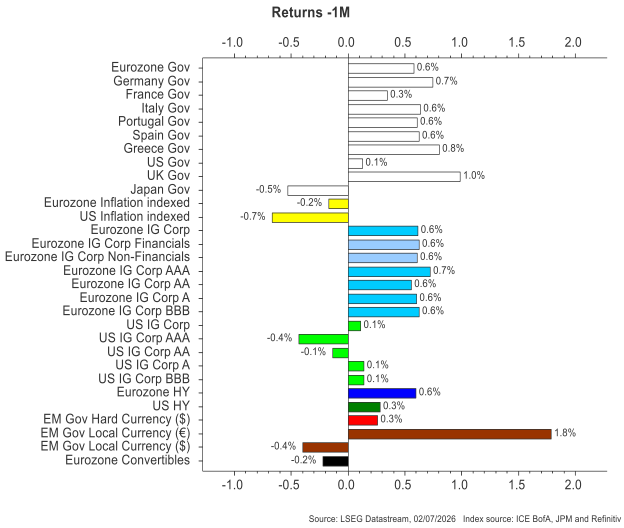
Credits	Yield	Spread	10yr Avg Spread	2yr Spread Range		Spread Change			2yr Z-Score*
				Min	Max	Chg 1W	Chg 1M bp	Chg 3m	
US Corporate	5.21	75	116	73	121	-1	1	-4	▲
Single-A	5.07	63	93	59	102	0	1	-2	▲
US High Yield	7.09	271	385	258	456	-3	5	-5	▲
BB	6.02	163	253	155	306	-4	2	-6	▲
EM HY ($)	6.80	219	344	207	379	0	4	-12	▲

* Z-score 2y is based on the spread

Source: LSEG Datastream , BNP Paribas WM, 02/07/2026

Return

OVER ONE MONTH



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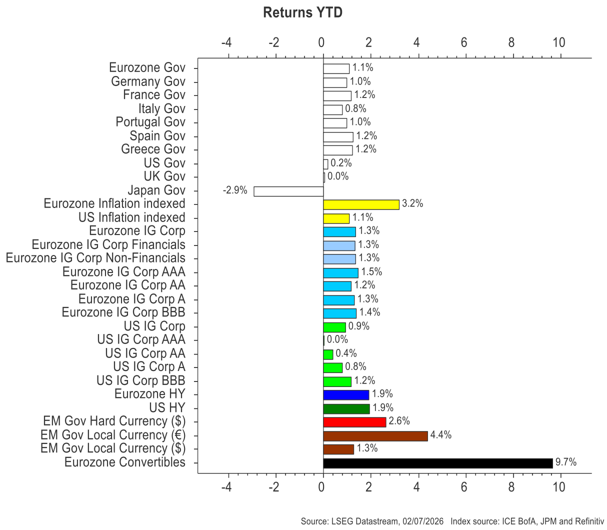

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