

OCTOBER 2026

Fixed Income Focus

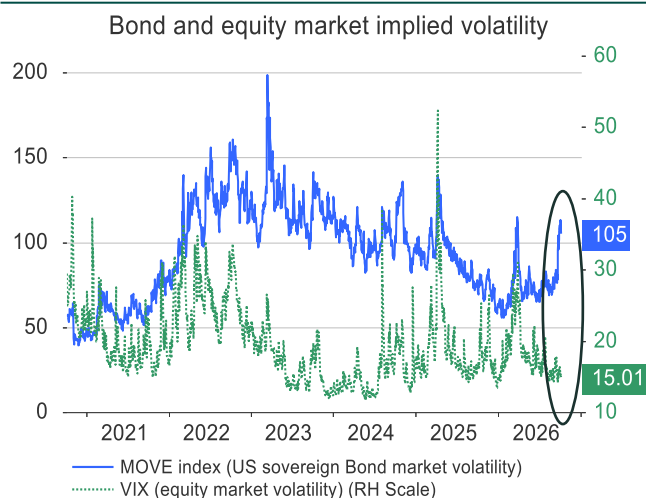
Summary

- 1. More rate hikes to come:** Due to resilient economic growth, sustained high energy prices and high-interest rate volatility, we are adding one 25bp hike to our US Fed and ECB forecasts. The Fed would hike in December and January while the ECB would hike in December. We now see a BoE hike in November (previously December). The Bank of Japan is expected to hike about every quarter with a terminal rate around 2.5% in 2028.
- 2. We revise our bond yield targets higher:** The recent surge in government bond yields has been driven by real yields via AI-related investment capital and upward revisions in the natural rate of interest, suggesting a “higher for longer” environment. Accordingly, we have raised our 12-month yield targets by 25bp for the US, Germany, and the UK. The new targets are 4.75%, 3% and 4.65%.
- 3. We remain positive on core Eurozone govies** The 10-year German Bund yield rose to 3.30%, while the Eurozone average 10-year yield was above 3.7%. Our new 10-year target for the German 10-year yield is 3%
- 4. We keep upgrade UK bonds from Neutral to Positive:** U.K. Yields on 10-year government bonds hover around 5.3%. The government has given more signals on the its commitment for fiscal discipline. Yields are again attractive.
- 5. Selective opportunities in corporate bonds:** We prefer EUR IG corporate bonds (Positive view) over USD IG bonds (Neutral view). We upgrade again UK IG corporate bonds to positive.
- 6. We keep a neutral opinion on high yield corporate and Emerging Market bonds:** Spreads remain very low and expected return are too low. EM bonds, the three primary drivers—valuation, currency outlook, and monetary policy expectations— are not supportive at this stage.

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CHART OF THE MONTH: SHARP RISE IN YIELDS



Source: LSEG Datastream, 07/10/2026

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Central banks

We add one more rate hike for the Fed and ECB to the scenario

European Central Bank (ECB)

The underlying tone of the ECB's September communication reinforces our view that the tightening cycle is not yet over. We now forecast an additional hike in December, followed by an extended hold in mildly restrictive territory throughout 2027. While the economy continues to be resilient, both headline CPI and core CPI inflation remain above target (at 3.2% and 2.4% respectively). Although there are no clear signs of the second-round effects suggested by ECB wage data, continued pressure on oil and gas prices, partially due to refinery issues, indicates a shift toward the ECB's adverse scenario. Market expectations mirror those for the US and appear even more aggressive.

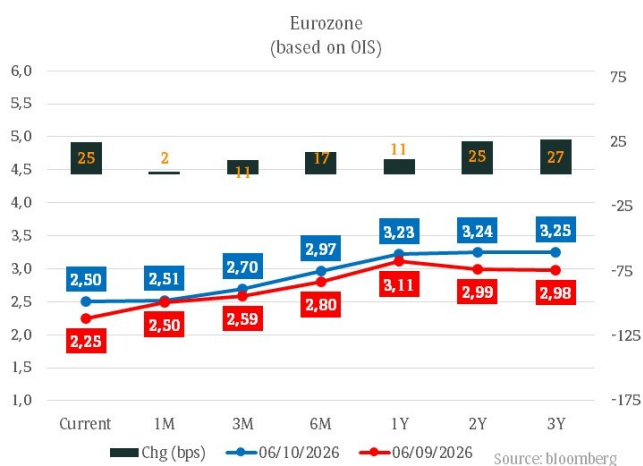
Outlook: The pressure remains high due the pressure on oil and especially gas prices. Consequently, we have revised our outlook for the ECB and now anticipate another rate increase in December. In contrast, markets are currently pricing in between 2 and 3 hikes (see chart below).

US Federal Reserve (Fed)

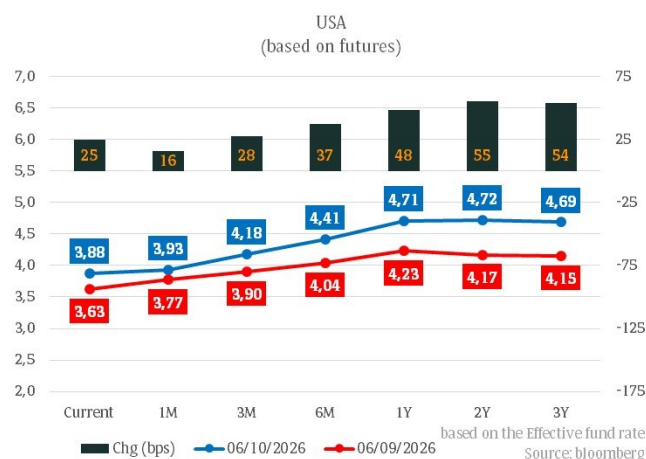
During the September meeting, Kevin Warsh acknowledged that policy was too loose, and inflation remained too high. This was probably intended to signal to the markets that the concerns driving the rise in long-term Treasury yields had been noted. As oil prices and bond yields have continued to climb in recent days, we have decided to add one rate hike to our forecast. We now expect the FOMC to raise rates in December and January, thereby unwinding the 2025 "insurance cuts" and returning the real policy stance to a roughly neutral level. In our base-case scenario, the FOMC would hike just enough to maintain a stable unemployment rate before pausing. We believe the markets' expectation of nearly four additional hikes over the next year is exaggerated.

Outlook: We now anticipate a rate increase in December and other one in January. The key assumptions are resilient economic growth, sustained high energy prices and high-interest rate volatility. In contrast, markets are currently pricing in approximately 3 hikes (see chart below).

MARKET PRICING FOR THE ECB



MARKET PRICING FOR THE FED



INVESTMENT CONCLUSION

We are adding one 25bp hike to our US Fed and ECB forecasts. We have thus revised our outlook for the ECB and now anticipate another 25 bp rate increase in December. For the US, we now expect a rate hike of 25bp hike in December and January.



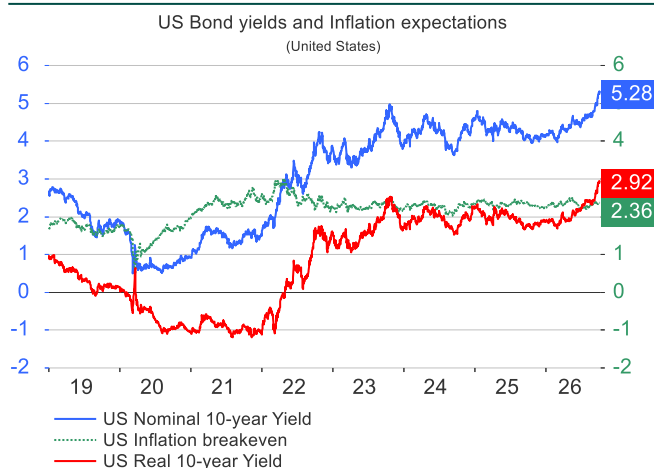
Topics in Focus

We revise our bond yields targets higher for US, UK and Germany

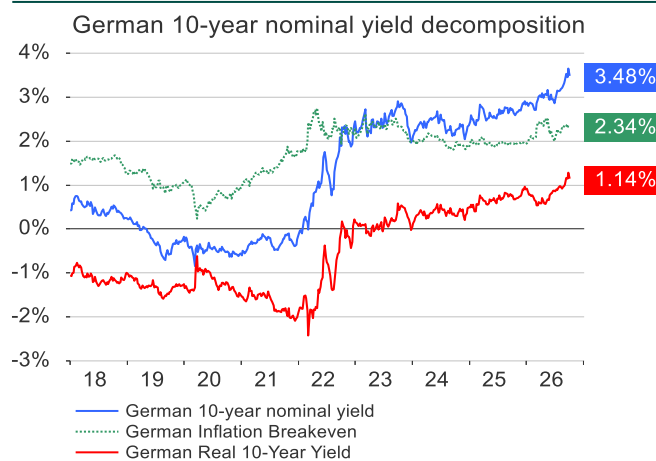
US Treasuries have sold off aggressively across the curve since mid-summer, with the 10-year yield rising by nearly 80bp. This trend has accelerated particularly over the last few weeks. The resilience of growth was further confirmed by a stronger-than-expected preliminary September Composite PMI index. Meanwhile, oil and gas prices have risen again and could remain high in the coming weeks. The primary driver of US yields remains the real yield, likely reflecting expectations of increased capital demand in the coming years. A higher term premium, growing deficits and debt have likely also contributed. Breakeven inflation remains stable, hovering at around 2.25%. The term premium has retraced from its August peak. While we maintain that US yields are overshooting their fair value, we have increased our 12-month target from 4.50% to 4.75%. **Given the Fed's hiking cycle and no imminent cuts expected, investors should remain cautious and patient.**

A further market push towards 5.50% would offer a more attractive entry point. Indeed, we have some doubts about the latest revisions of the natural rate of interest linked to AI. In the eurozone, the 10-year German government bond yield has also risen significantly, with a move which is similar in magnitude to that of the US since early July. This trend is driven by the same fundamental factors as in the US, namely debt and deficit dynamics. Consequently, we are raising our 12-month target from 2.75% to 3%, though we see limited further upside from current levels. We remain Positive on core eurozone government bonds. A similar pattern has emerged in the UK, where we are raising our 12-month target from 4.4% to 4.65%. Although current levels are above our long-term fair value estimates, we are increasingly confident that the government will take the necessary steps to stabilize debt dynamics.

BOND YIELD DECOMPOSITION US



BOND YIELD DECOMPOSITION GERMANY



INVESTMENT CONCLUSION

The recent surge in government bond yields has been driven by real yields via AI-related investment capital and upward revisions in the natural rate of interest, suggesting a "higher for longer" environment. Accordingly, we have raised our 12-month yield targets by 25bp for the US, Germany, and the UK. The new targets are 4.75%, 3% and 4.60%.



Government Bond yields

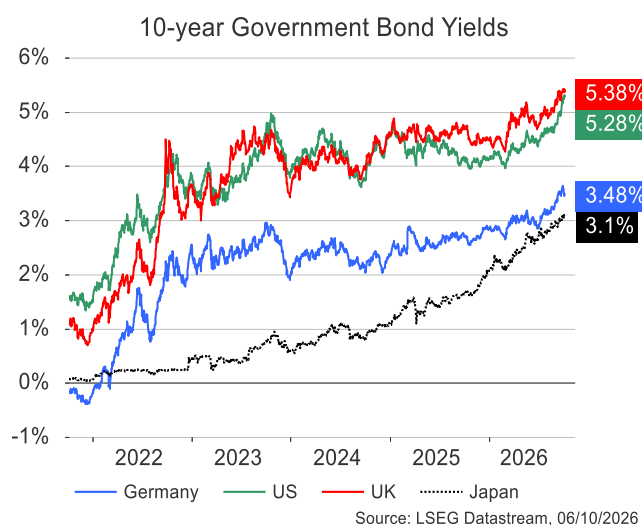
Upgrade to positive on core eurozone Govies

We stay positive on Core Eurozone government bonds: The 10-year German Bond Yield remains close to 3.5%. Energy price volatility and higher issuance from increased capital needs keep the pressure high. As we believe the German Bund's fair value remains below 3%, we expect attractive returns at current levels. We favor maturities of 7-10 years.

We upgrade UK Government Bonds back to positive: U.K. government bond Yields hover around 5.40%. Fiscal uncertainty came down as the government has committed to keep fiscal discipline. Current levels are attractive again.

Neutral Stance on US Government Bonds: U.S. 10-year yields also rose sharply, driven by increased demand for capital especially AI-related. Yields could overshoot more. We could test 5.5% in the coming weeks. Too early to come back.

TREND IN BOND YIELDS



	Maturity (years)	06/10/2026	3-month target	12-month target
USA	Policy rate	4	4.25	4.50
	2	4.80	4.50	4.35
	5	5.05	4.70	4.50
	10	5.30	5	4.75
	30	5.65	5.50	5.10
Germany	Policy rate	2.5	2.75	2.75
	2	3.08	2.90	2.80
	5	3.23	3	2.90
	10	3.48	3.20	3
	30	3.85	3.60	3.40
UK	Policy rate	3.75	4	4
	2	4.82	4.35	4
	5	4.93	4.45	4.20
	10	5.38	5	4.65
	30	5.91	5.50	5.10
Japan	Policy rate	1.25	1.50	1.75
	2	1.92	2.10	2.4
	5	2.38	2.50	2.6
	10	3.09	3	3
	30	4.23	4.20	4

Source: Refinitiv Datastream, BNP Paribas WM

INVESTMENT CONCLUSION

The recent surge in government bond yields has been driven by real yields via AI-related investment capital and upward revisions in the natural rate of interest, suggesting a "higher for longer" environment. Accordingly, we have raised our 12-month yield targets by 25bp for the US, Germany, and the UK. The new targets are 4.75%, 3% and 4.65%. Given the renewed attractiveness of UK yields, we upgrade UK government bonds to Positive.



Selected opportunities in corporate bond markets

Prefer eurozone high grade corporate bonds – We upgrade UK IG corporate Bonds

The extended duration of a hiking cycle typically increases the probability of spread widening. Aggressive policy tightening heightens the risk of a slowdown and often brings credit vulnerabilities to the surface. By assessing the impact of the initial rate adjustment across hiking cycles over the past 70 years, our analysis indicates that credit spreads generally remain tight, characterized by limited volatility. We maintain that while the credit cycle is resilient to modest hikes, deterioration becomes more likely after a sequence of five or more increases. Furthermore, provided that rates do not become prohibitively restrictive, higher yields may curb supply and stimulate demand for Fixed Income, creating a supportive technical backdrop. At present, AI-driven investment appears to remain largely insensitive to rate fluctuations.

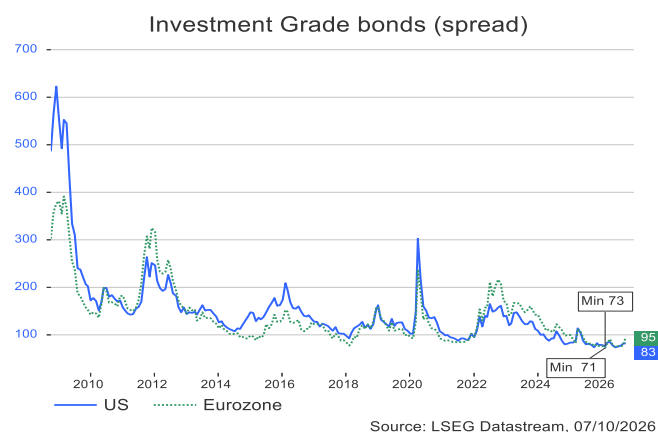
Positive eurozone and UK IG bonds: Fundamentals improved following strong earnings, which helped to moderate the upward trend in net leverage. In light of high earnings growth, we expect net leverage to remain broadly stable. EBITDA growth underpinned

a modest improvement in leverage, even as net debt edged higher. We have upgrade UK IG corporate bonds as yields and spreads are again supportive.

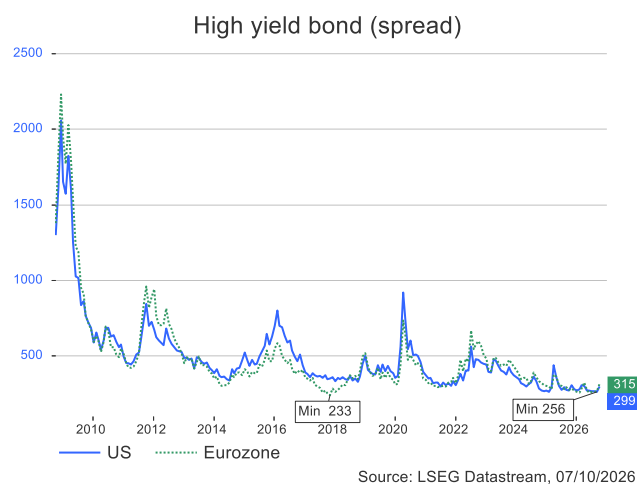
We are neutral on US IG: Overall fundamentals remain resilient. While issuance from "old economy" sectors remains range-bound, supply from hyperscalers continues to surge. These entities are predominantly high-quality names with low leverage, which sustains their capacity for further borrowing. However, we perceive a risk of an overshoot in Treasury yields; this presents a secondary risk to US Investment Grade (IG) bonds, given their significant duration sensitivity.

We keep a neutral stance on High yield bonds: We do not expect these bonds to outperform on a risk-adjusted basis. While tight spreads can be partially justified by ongoing improvements in credit quality across the asset class, the potential for further spread and yield compression appears limited. Consequently, any deterioration in the economic or interest rate environment could have a disproportionate impact on valuations.

INVESTMENT GRADE CORPORATE BONDS



CORPORATE HIGH YIELD BONDS



INVESTMENT CONCLUSION

We prefer eurozone IG which are supported by improved fundamentals following strong earnings figures across most sectors, which helped to moderate the upward trend in net leverage. We have upgrade UK IG corporate bonds as yields and spreads are again supportive.



Too early to come back to EM Bonds

We keep a neutral stance on Emerging Market Bonds

Emerging market (EM) growth has remained resilient over recent months despite high oil prices. Inflation has remained contained thus far, and the inflation surprise index has fallen. This reflects the fact that leading indicators for inflation have been released below expectations. Chinese consumer price inflation remains remarkably low, but producer price inflation showed a continuous rise over the past year. We do not expect a major acceleration in inflation in the major emerging market economies.

Most EM central banks have either held rates steady or hiked rates in recent weeks. The exception is Brazil with a recent cut in the policy rate.

EM local currency bond spreads moved sharply lower, despite sustained uncertainty in Middle-East. EM hard currency bond spreads were moderately higher. They have however been falling relative to US corporate high yield.

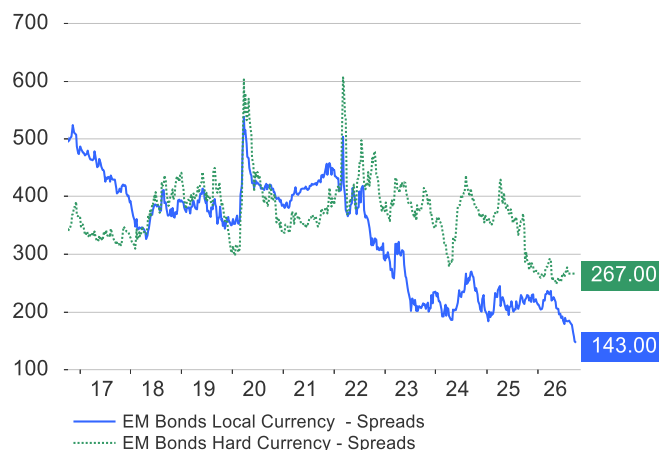
Neutral Stance: The three key performance drivers are: (1) valuation, (2) the outlook for the dollar, and (3) the potential for EM central bank rate cuts.

Valuation is not supportive: As shown in the chart below (left), the risk premia—measured by yield spreads—remain quite low especially for EM local currency bonds. This suggests limited upside for future returns.

Currencies are range-bound: A weaker dollar would benefit EM local-currency bonds, but dollar downside appears limited for the coming months.

No support from Monetary policy : Inflation remain moderate in emerging markets, but the uncertainty remains high. Market expectations suggest further hikes going forward (see table below). A change in perception and market pricing could be trigger to come back to local EM local currency bonds.

EM BONDS - VALUATION



MONETARY POLICY EXPECTATIONS

Emerging Central bank	Current Policy rate (%)	Market pricing			
		end 2026		+12m	
		Expected policy rate (%)	Cumul bp	Expected policy rate (%)	Cumul bp
Brazil	13,75	13,72	-3	12,82	-94
Chile	4,50	4,61	11	4,82	32
Colombia	12,25	12,67	42	12,50	25
Czech	3,75	3,91	16	3,87	12
Hungary	5,50	5,61	11	5,53	3
India	5,25	6,17	92	6,26	101
Indonesia	5,75	6,22	47	6,30	55
Korea	3,00	3,29	29	3,46	46
Mexico	6,50	6,87	37	6,93	43
Poland	3,75	3,93	18	5,41	166
Thailand	1,00	1,10	10	1,13	13
Turkey	37,00	33,99	-301	35,77	-123

INVESTMENT CONCLUSION

We keep a neutral stance on EM bonds. The three primary drivers — valuation, currency trends, and monetary policy expectations — do not offer a compelling case for investment. More opportunities could emerge if we see the potential for central banks to cut rates and/or a momentum for dollar depreciation.



Our Investment Recommendations

Asset class	Zone	Our opinion	
Government bonds	Germany and core eurozone	+	We remain positive on core Eurozone govies from Neutral to Positive. Yields rose again well above our targets, and the expected return is attractive again. We favour maturities of 7-10 years.
	Non-core Peripheral countries	=	Neutral on non-core peripheral debt (Portugal, Italy, Spain, Greece).
	United Kingdom	+	Positive 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. We upgrade UK IG corporates to Positive. We are 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	5,28	---	
Germany	3,48	---	
France	4,75	127	41
Italy	4,54	105	24
Spain	4,08	60	16
Portugal	3,95	47	14
Greece	4,39	91	23
06/10/2026			
Source: Refinitiv Datastream			

	Yield (%)	Spread (bp)	Spread change 1 month (bp)
Corporate bonds IG EUR	4,21	95	17
Corporate bonds IG USD	6,01	83	2
Corporate bonds HY EUR	6,48	315	49
Corporate bonds HY USD	8,14	299	35
Emerging government bonds in hard currency	6,97	219	-35
Emerging government bonds in local currency	6,47	143	-35
06/10/2026			
Source: Refinitiv Datastream, Bloomberg			



Valuation

	Yield	Spread	10yr Avg Spread	2yr Spread Range		Spread Change			2yr Z-Score*
				Min	Max	Chg 1W	Chg 1M bp	Chg YTD	
Euro Corporate	4,21	95	116	71	125	9	17	17	▲
Single-A	4,11	86	100	64	113	7	16	15	▲
Euro High Yield	6,48	315	372	248	429	21	49	45	▲
BB	5,44	210	273	155	303	18	45	41	▲

* Z-score 2y is based on the spread

Source: LSEG Datastream , BNP Paribas WM, 06/10/2026

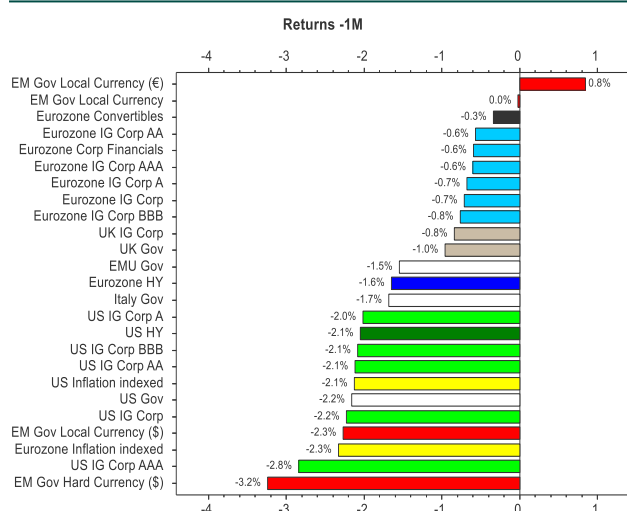
Credits	Yield	Spread	10yr Avg Spread	2yr Spread Range		Spread Change			2yr Z-Score*
				Min	Max	Chg 1W	Chg 1M bp	Chg 3m	
US Corporate	6,01	83	115	73	121	-1	2	4	▲
Single-A	5,86	70	92	59	102	-1	1	5	▲
US High Yield	8,14	299	379	256	456	-7	35	23	▲
BB	7,02	185	249	150	306	-4	30	16	▲
EM HY (\$)	6,97	219	340	207	354	0	0	-12	▲

* Z-score 2y is based on the spread

Source: LSEG Datastream , BNP Paribas WM, 06/10/2026

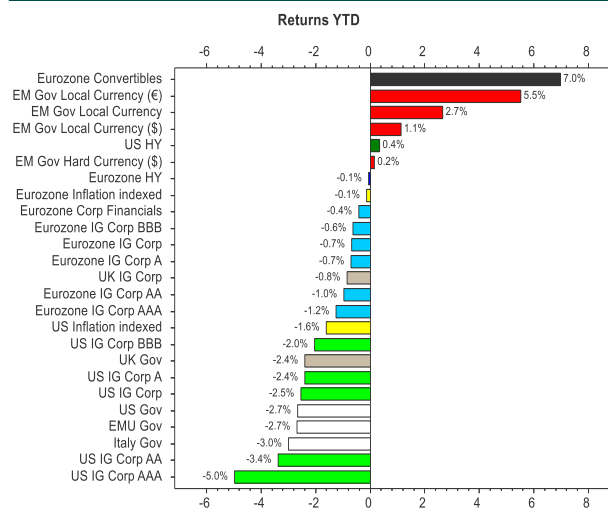
Return

OVER ONE MONTH



Source: LSEG Datastream, 06/10/2026 Index source: JPMorgan for Government Bonds and Emerging Markets (EM); Bloomberg Barclays for Investment Grade (IG) credit; ICE BofA for High Yield (HY) credit; Exane for Convertibles.

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Source: LSEG Datastream, 06/10/2026 Index source: JPMorgan for Government Bonds and Emerging Markets (EM); Bloomberg Barclays for Investment Grade (IG) credit; ICE BofA for High Yield (HY) credit; Exane for Convertibles.

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