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Bonds Weekly

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U.S. inflation will test the bond market recovery

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Our View

Bond Market Movers – Review and Outlook

What drove the bond markets last week?

- Hopes for the imminent reopening of the Strait of Hormuz have gained fresh momentum. U.S. President Trump called off threatened massive attacks on Iran and instead hinted at an imminent new agreement. Whether there has actually been any measurable progress, however, remains unclear.
- According to the ISM indices, sentiment in the U.S. economy improved noticeably in July, particularly in the manufacturing sector. The index for the services sector rose slightly.
- The ADP report for July was disappointing, showing job growth of just 44,000 in the U.S. private sector, the lowest figure since January.
- U.S. productivity grew more strongly than expected in the second quarter, while unit labor costs rose less than anticipated.
- For the first time in 15 years, the U.S. and Japan jointly intervened in the foreign exchange market to prop up the yen. According to media reports, the U.S. government is working to enable Japan to carry out such interventions without selling U.S. Treasury securities.
- U.S. tech giant Alphabet is issuing another large bond offering on the U.S. bond market with maturities ranging from two to 40 years.
- According to its latest quarterly refunding statement, the U.S. Treasury is leaving the issuance volumes of longer-term government securities unchanged. The medium-term outlook confirms that no changes to the issuance strategy are expected for the time being.

What could drive the market next week?

- The financial markets remain focused on developments in the Middle East and trends in commodity prices. The susceptibility to another disappointment is rising following the latest signs of easing tensions.
- Expectations for the U.S. jobs report for July have been dampened by the slightly disappointing ADP report. This increases the potential for positive surprises.
- The U.S. inflation data for July will be the macroeconomic highlight of the week. According to our forecast, headline inflation has slowed for the second month in a row. Meanwhile, we expect the core rate to remain unchanged.
- The primary market for U.S. Treasury securities will have to absorb the next wave of long-term bond issuance next week. Meanwhile, the primary market for euro-denominated government bonds is heading into the summer lull. Compared to the previous week, the gross supply is expected to drop sharply, from just over 25 billion euros to 9 billion euros, only. Nevertheless, net cash flows are set to remain slightly negative due to a lack of reflows.

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U.S. inflation will test the bond market recovery

Hopes for a de-escalation in the Middle East trigger a price recovery

Following conflicting signals last week, signs of a de-escalation have recently come to the fore regarding the Middle East conflict. Shortly before carrying out the massive military strikes he had threatened against Iran, U.S. President Trump backed down and instead held out the prospect of a new agreement soon. Similar to what happened in June, this appears to be an intermediate step toward a comprehensive resolution of the conflict, the primary goal of which is to reopen the Strait of Hormuz. Iran and Oman have apparently reached an agreement on shipping routes through the strait, with Tehran pushing for the imposition of a toll, a measure the U.S. has so far rejected. The mullah regime therefore appears to be on the verge of securing further concessions in its dispute with the United States. It seems unclear how close an agreement is. However, energy prices have already responded to the positive turn in the news with a sharp decline. The price of Brent crude briefly dipped below the $80-per-barrel mark for the first time in about four weeks. Stock markets in both the U.S. and Europe rode the wave of momentum from the Middle East to surge to new all-time highs. Sentiment also improved in the major government bond markets on both sides of the Atlantic. Concerns about another surge in inflation, which would bring about the dreaded second-round effects, have eased somewhat. Based on forward rates in the euro money market, market participants currently expect the ECB to raise interest rates only two more times by spring 2027. The yield on 10-year German government bonds has once again bounced downward from the resistance zone around the 3.20% mark. From a chartist perspective, this resistance level appears to us to be increasingly solid (see the chart below). The likelihood that the EUR benchmark yield is in the process of peaking appears to mount – provided, however, that the signs of easing tensions in the Middle East prove to be sustainable this time.

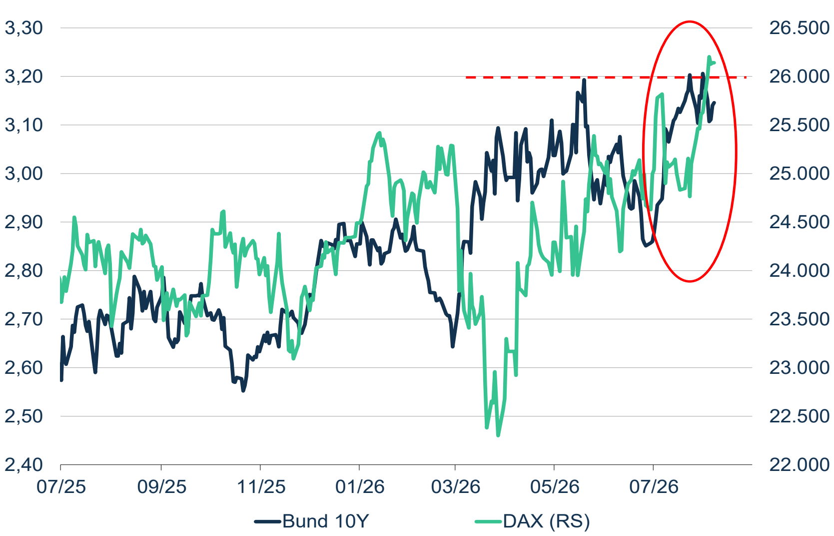
New hope for the Strait of Hormuz

Market curbing rate-hiking speculation

10-year Bund: Resistance zone at 3.20% has solidified

Chart of the Week

Yields on 10-Year German government bonds and DAX



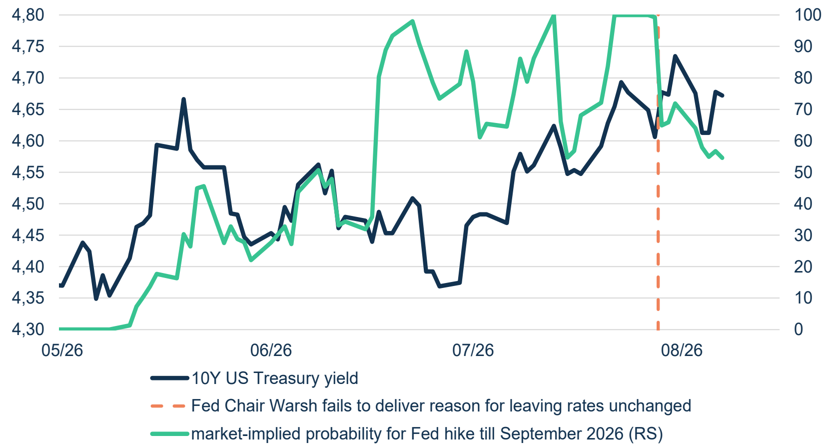
Source: Bloomberg, LBBW Research

In the U.S. interest rate market, investors are less certain than they were a week ago that the Fed will decide to raise the benchmark interest rate as early as its next meeting in September. The market-implied probability of a monetary policy tightening immediately after the summer break has fallen to just under 60% (see the chart below). At the long end of the U.S. dollar yield curve, the drop in energy prices appears to have halted the upward spiral in yields for the time being. In our view, however, it remains to be seen whether market participants have already come to terms with the doubts about the credibility of Fed Chairman Warsh's pledge of price stability, which arose in the wake of the central bank's most recent meeting.

Market: Probability of a Fed rate hike as of September at 55%

Market slightly scales back speculation on Fed rate hike

Yields on 10-Year U.S. Treasuries and market-implied probability of a Fed rate hike by September 2026



Source: Bloomberg, LBBW Research

U.S. government is watching the bond market with unease

Meanwhile, it seems that concerns about a continued rise in bond yields have also reached the U.S. government: As part of the recent coordinated intervention in the foreign exchange market to support the yen, the U.S. Treasury Department made a point of emphasizing that the Bank of Japan did not need to sell U.S. Treasury bonds to prop up its currency.

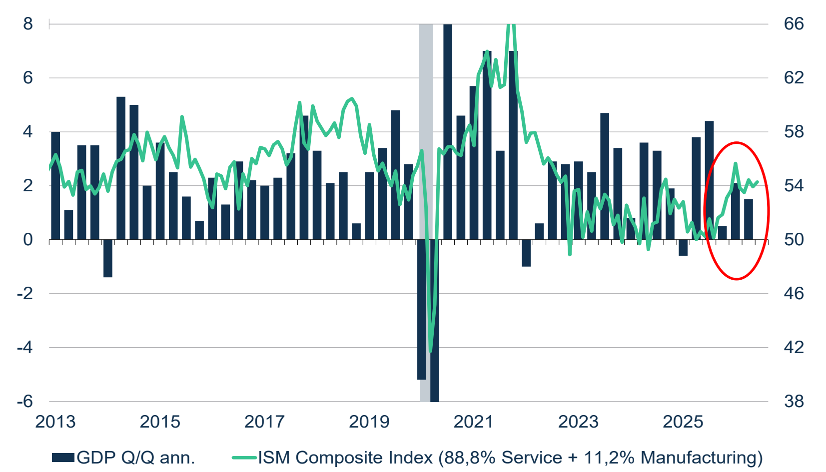
Mixed signals from U.S. macroeconomic data

Meanwhile, in our view, the flow of U.S. macroeconomic data over the past few days was, on the whole, not sufficient to steer the Fed's monetary policy debate in a new direction. If anything, the signals were ambiguous. On the one hand, the ISM indices have underscored the robust state of the U.S. economy.

ISM indices suggest no weakening growth trend

U.S. economy has remained robust

U.S. GDP growth (Q/Q, annualized) ISM composite index



Source: Bloomberg, LBBW Research

In the manufacturing sector, sentiment in July was as positive as it had been nearly four years ago, while the index for the service sector remained at a solid level, showing little change. As shown in the chart above, the slight overall improvement in sentiment in July underscores that the slowdown in U.S. growth reported for the second quarter does not (yet) mark the beginning of a prolonged economic downturn.

ADP report plays right into the hands of the doves

On the other hand, according to the ADP report, job growth in the U.S. labor market slowed more sharply in July than analysts had expected. Employment growth was last lower in January. Taken on its own, this plays into the hands of those Fed officials who would like to stick to their wait-and-see stance on monetary policy for the time being. In our view, however, the slowdown in employment growth should not be overemphasized, as the ADP data suggest that the end of the World Cup in the U.S. temporarily skewed the job figures downward in some sectors.

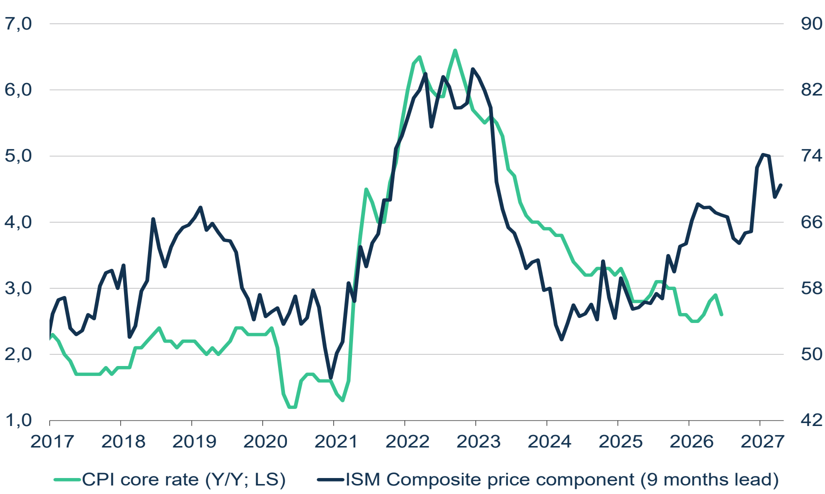
Outlook: U.S. inflation could provide new impetus for the Fed's policy

U.S. CPI will be the highlight of next week

The latest U.S. labor market data does suggest that the pressure on the Fed to take monetary policy action has receded a bit. However, the next set of U.S. inflation data – along with developments in the Middle East – is likely to be the key factor in determining how sustainable the recovery trends in the U.S. bond market are. On August 12, the U.S. Department of Labor will release the consumer price data for July, followed by the producer price data one day later. Last month, the widespread easing of price pressures at the consumer level was a particularly bond-positive surprise. Despite occasional upward price swings in the energy market, we expect that gasoline prices have had a dampening effect on overall inflation for the second month in a row. Headline inflation should therefore have fallen, again, year-over-year, although by nowhere near as much as in June. However, according to recent statements from the Federal Reserve, policymakers are focusing primarily on the continuation of underlying disinflationary trends. The key rate should therefore also be the primary focus among bond market participants.

Second-round effects on U.S. inflation remain in the pipeline

U.S. core inflation (Y/Y) and weighted average of ISM price components



Source: Bloomberg, LBBW Research

When will second-round effects show up?

The price components of the ISM indices recently served as a reminder not to downplay the risk of second-round effects from the energy price shock. In the service sector, the issue of price increases unexpectedly regained prominence in July, meaning that, as shown in the chart above, considerable upward pressure on underlying inflation remains in the pipeline over the medium term.

We expect core inflation to have remained flat at 2.6% (Y/Y) in July. Combined with falling headline inflation, this is unlikely to significantly alter the setting for the next Fed meeting for now. A resurgence in core inflation, on the other hand, would reignite concerns about second-round effects, which in turn would likely wipe out the improvement in sentiment on the U.S. bond market. Especially since, according to media reports, rising inflation could prompt the chair of the Federal Reserve to approve an interest rate hike in September.

Forecasts at a Glance

Euro Area	Spot	30.09.26	31.12.26	30.06.27
ECB Main Refinancing Rate	2,40	2,65	2,65	2,65
ECB Deposit Rate	2,25	2,50	2,50	2,50
Overnight Rate (€STR)	2,19	2,45	2,45	2,45
3M Euribor	2,48	2,55	2,55	2,55
Swap 2Y	2,97	2,80	2,85	2,75
Swap 5Y	3,02	2,85	2,90	2,85
Swap 10Y	3,18	3,05	3,10	3,15
Bund 2Y	2,76	2,60	2,70	2,65
Bund 5Y	2,88	2,70	2,80	2,80
Bund 10Y	3,14	3,00	3,10	3,20
Swap/Bund 2Y	21	20	15	10
Swap/Bund 5Y	15	15	10	5
Swap/Bund 10Y	4	5	0	-5
Spread BBB Corporates/Bund	90	100	110	120

USA	Spot	30.09.26	31.12.26	30.06.27
Fed Funds Target Rate	3,75	3,75	3,75	3,75
Overnight Rate (SOFR)	3,64	3,65	3,65	3,65
3M Money Market	3,76	3,75	3,75	3,65
Swap 2J (SOFR-OIS)	4,10	3,95	3,90	3,65
Swap 5J (SOFR-OIS)	4,11	3,85	3,85	3,75
Swap 10J (SOFR-OIS)	4,27	3,95	4,00	4,00
Treasury 2Y	4,25	4,10	4,10	3,85
Treasury 5Y	4,40	4,15	4,20	4,10
Treasury 10Y	4,68	4,40	4,50	4,55

G5		Spot	30.09.26	31.12.26	30.06.27
Japan	*Overnight Rate (TONAR)*	0,98	1,00	1,25	1,30
Japan	*10Y Government Bond*	2,80	2,75	2,80	2,90
UK	*Overnight Rate (SONIA)*	3,73	3,70	3,95	3,95
UK	*10Y Government Bond*	4,94	4,80	4,90	4,90
Switzerland	*Overnight Rate (SARON)*	-0,08	-0,05	-0,05	-0,05
Switzerland	*10Y Government Bond*	0,37	0,35	0,40	0,45

FX	Spot	30.09.26	31.12.26	30.06.27
EURCHF	0,9363	0,92	0,93	0,94
EURCNY	7,7760	8,01	7,91	7,62
EURGBP	0,8566	0,85	0,85	0,85
EURJPY	182,50	187	186	182
EURUSD	1,1524	1,17	1,18	1,19
USDCHF	0,8125	0,79	0,79	0,79
USDCNY	6,7470	6,85	6,70	6,40
GBPUSD	1,3454	1,38	1,39	1,40
USDJPY	158,36	160	158	153

Economic Development		2024	2025	2026e	2027e
Germany	*GDP*	0,0	0,4	0,5	0,8
	Inflation	2,3	2,2	2,7	2,3
Euro Area	*GDP*	1,0	1,5	0,8	1,0
	Inflation	2,4	2,1	2,9	2,4
UK	*GDP*	1,0	1,3	0,8	1,3
	Inflation	2,5	3,2	2,8	2,4
USA	*GDP*	2,8	2,1	2,2	1,6
	Inflation	3,0	2,7	3,6	2,2
Japan	*GDP*	-0,2	1,1	0,6	0,8
	Inflation	2,7	3,2	2,0	1,8
China	*GDP*	5,0	3,7	3,5	3,2
	Inflation	0,2	0,0	1,2	1,5
World	*GDP*	3,2	3,3	2,7	2,8
	Inflation	3,5	3,4	3,8	3,0

Changes to the foregoing week are marked by a (*)

Sources: LSEG, Bloomberg, LBBW Research

Main Events of the Past Week

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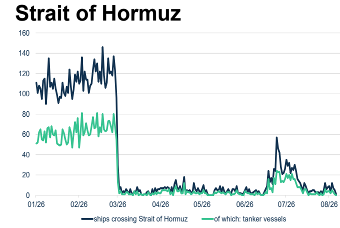
- *Currency Market:* For the first time in 15 years, the finance ministries of Japan and the U.S. jointly intervened in the foreign exchange market to prop up the yen – Japan had previously supported its own currency on multiple occasions – U.S. Treasury Department (in cooperation with the Fed) used euro liquidity for the intervention so as not to undermine its policy of a strong dollar – Treasury Secretary Bessent explicitly leaves the door open for further interventions.
- *Middle East Conflict:* U.S. President Trump calls off a threatened massive attack on Iranian infrastructure at the last minute, citing Tehran's willingness to conclude a new agreement – observers speculate that Arab U.S. allies, who fear the conflict could spread throughout the region, may have intervened.

New hope in the Strait of Hormuz

- *Middle East Conflict:* Optimism is growing regarding a short-term negotiated solution to reopen the Strait of Hormuz – Qatar says the parties to the conflict are willing to conclude an agreement valid for 60 days – Oman and Iran have apparently reached an agreement on shipping routes through the strait, though Iranian sources are tempering optimism regarding an immediate reopening – According to media reports, Iran intends to impose a high toll, which is formally to be paid "voluntarily" – Furthermore, key fundamental points of contention, foremost among them Iran's nuclear program, remain unresolved for the time being.

Strait of Hormuz



Sources: Bloomberg, LBBW Research

- *Middle East Conflict – Energy Price Crisis:* As of early August, the fill level of European natural gas storage facilities stood at 57%, the lowest level for this time of year since records began – a price spike caused by the war in Iran is slowing the refilling process – Observers see a growing risk of shortages this coming winter – the average fill level of German gas storage facilities stands at just 47%.
- *Geopolitics:* According to media reports, U.S. authorities are banning the import of certain data center components from China – a measure intended to prevent potential hacking or espionage attacks on data that is critical to the AI boom.

Democratic federal states are suing over Trump's tariffs

- *U.S. – Trade Policy:* A group of 25 states governed by Democrats has filed a lawsuit against the tariffs recently imposed by the U.S. government on imports from about 60 countries – the government had cited alleged links to forced labor as the basis for the tariffs.
- *Monetary Policy – Fed:* The Financial Times reports, citing central bank sources, that Fed Chairman Warsh is willing to raise the benchmark interest rate in September if upcoming inflation data is hot.
- *Germany – Economy:* Factory orders surprise with a 3.1% increase in June (M/M), following +0.3% in May – sharp rise in domestic orders (+7.8%) acts as the main driver, while foreign orders increased by 0.2% – Industrial production grows by 0.2% (M/M), after +0.7% in May.

Concerns about hybrid attacks are growing

- *Germany – Homeland Security:* An attempted attack using an explosive-laden drone at Leipzig Airport is fueling concerns about an escalation of hybrid warfare by Russia – the airport has been used, among other things, to transport military supplies to Ukraine.
- *Germany – Pension Policy:* CDU parliamentary group leader Frei reaffirms the federal government's commitment to fully implementing the pension reform proposals and thus rejects the call by several federal state prime ministers to maintain early retirement without penalties for long-term contributors.

Mounting economic worries due to low river levels

- *Germany – River Water Levels:* Concerns are growing about economic disruption and additional inflationary pressure resulting from low water levels in major rivers – Rhine water level at the Kaub measuring station has reached its lowest point since 1880 amid persistent heat and drought – Freight rates for inland waterway vessels have skyrocketed due to significantly reduced transport capacity – The IW Economic Research Institute warns of a looming recession if navigability on the Rhine remains restricted for an extended period.
- *Europe – River Levels:* Water levels in the Danube have also reached new record lows – Hungary and Romania are sliding into an energy crisis due to low water levels, as power plants located along the river must be shut down.
- *Eurozone – Economy:* A recent ECB study estimates that economic uncertainty has resulted in a loss of growth of 0.4 percentage points for the period from Q1 2025 to Q1 2026 – companies are holding back on investments due to uncertainty – Consumers are postponing spending or even forgoing it entirely – Meanwhile, the ECB sees an opportunity for a shift in the composition of investment toward intangible assets, such as AI, to act as a buffer against economic shocks.

EMU inflation rising slightly

- *Eurozone – Inflation:* Inflation accelerated in July to a rate of 2.9% (Y/Y), up from 2.8% in June – core rate also rose, from 2.4% to 2.5% – stronger price pressures in the energy sector, and inflation in the services sector also picked up slightly again.
- *U.S. – Economy:* ISM Manufacturing Index rose more than expected in July, from 53.3 to 55.6 points – highest level since May 2022 – Price pressure eases for the third consecutive month but remains above average – index for the service sector improves slightly from 54.0 to 54.1 points – price component here unexpectedly turned upwards again, from 67.7 to 70.3 points.

U.S. productivity grows more than expected

- *U.S. – Economy:* Productivity grew significantly faster than expected in the second quarter, rising by 1.4% (Q/Q, annualized), following 0.8% in the first quarter – while unit labor costs remained below expectations at +1.3%, following also 1.3% in the previous quarter.
- *U.S. – Labor Market:* ADP report for July fell short of expectations, showing job growth of 44,000 (M/M) in the U.S. private sector, following +95,000 in June – weakening partly due to one-time effects related to the end of the World Cup – ADP notes rising wage pressure due to labor shortages in some professions.
- *U.S. – Labor Market:* JOLTS statistics show a moderate decline in job openings for June, specifically by just over 2% (M/M) – layoffs have remained virtually unchanged.

Far-left candidate wins U.S. primary

- *U.S. – Midterm Elections:* A left-wing candidate has won the Democratic primary for a Senate seat in the state of Michigan – Abdul El-Sayed, who is aligned with the “Democratic Socialists” and holds staunchly progressive views, finished narrowly ahead of his centrist opponent, Haley Stevens.
- *China – Economy:* RatingDog’s Purchasing Managers’ Index for the manufacturing sector disappoints with a decline from 51.7 to 50.9 points in July – lowest reading since March – Meanwhile, the index for the service sector plunges from 54.1 to 50.4 points, the lowest level since September 2024.
- *EU – Migration:* A massive influx of migrants into the Spanish enclave of Ceuta in North Africa, resulting in numerous deaths, has sparked new tensions over migration policy within the EU – Calls to exclude Spain from the Schengen system are causing discontent – the Spanish government is working to allay fears of losing control – nearly all illegal migrants who arrived from Morocco have since been returned, it says.

- *AI:* U.S. tech giant Alphabet is issuing a new tranche of U.S. dollar-denominated bonds with maturities ranging from two to 40 years to finance rapidly rising AI expenditures – total issuance volume is expected to amount to USD 25 billion.
- *Oil Market:* OPEC+ countries have decided on a new step toward gradually increasing oil production – supply is set to rise by an additional 188,000 barrels per day, thereby fully reversing previous production cuts – monthly consultations on production policy will continue, with the next meeting scheduled for September 6.

Alphabet keeps wave of bond issuance rolling

Next Week's Data

TIME	COUNTRY		PERIOD	LBBW FORECAST	CONSENSUS FORECAST[1)]	LAST VALUE[2)]	IMPORTANCE
FRIDAY, 07.08.2026							
14:30	USA	Change in Nonfarm Payrolls (thous.)	Jul	140	80	57	***
14:30	USA	Unemployment Rate (sa)	Jul	4,2	4,2	4,2	***
14:30	USA	Average Hourly Earnings (M/M)	Jul	0,3	0,3	0,3	***
SUNDAY, 09.08.2026							
03:30	CHN	CPI (Y/Y)	Jul	0,9	0,8	1,0	**
03:30	CHN	PPI (Y/Y)	Jul	3,9	3,8	4,1	*
MONDAY, 10.08.2026							
10:30	EMU	Sentix Investor Confidence	Aug	0,5	-2,9	-3,1	*
TUESDAY, 11.08.2026							
12:00	USA	NFIB Small Business Optimism	Jul	98,5	97,3	97,4	*
16:00	USA	Existing Home Sales (mn)	Jul	4,12	4,05	4,09	**
WEDNESDAY, 12.08.2026							
08:00	GE	CPI (Y/Y) (final)	Jul	2,8	2,8	2,8	*
14:30	USA	CPI (M/M)	Jul	0,0	0,1	-0,4	***
14:30	USA	CPI Ex Food & Energy (M/M)	Jul	0,3	0,2	0,0	***
THURSDAY, 13.08.2026							
08:00	UK	GDP (Q/Q) (1st estimate)	Q2	0,4	0,4	0,6	**
11:00	EMU	Industrial Production (M/M)	Jun	0,5	0,2	-0,2	**
14:30	USA	Producer Price Index, Final Demand (M/M)	Jul	0,2	0,2	-0,3	*
FRIDAY, 14.08.2026							
11:00	EMU	GDP (Q/Q) (2nd estimate)	Q2	0,4	0,4	0,4	*
11:00	EMU	Trade Balance (bn EUR)	Jun	-	-	-5,0	*
14:30	USA	Advance Retail Sales (M/M)	Jul	-0,3	0,2	0,2	***
16:00	USA	Uni Michigan Consumer Confidence (prelim.)	Aug	53,0	54,1	55,2	***
	AUT	Rating Review Austria (Moody's®)					**

1) Consensus forecast according to Bloomberg/Reuters

2) Should a provisional estimate be available, it is stated instead of the reference figure of the previous period

Sources: Bloomberg, LBBW Research

Rates

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EUR government bonds: Middle East conflict cast a shadow over the start of summer

Year-to-Date Performance: Easy come, easy go

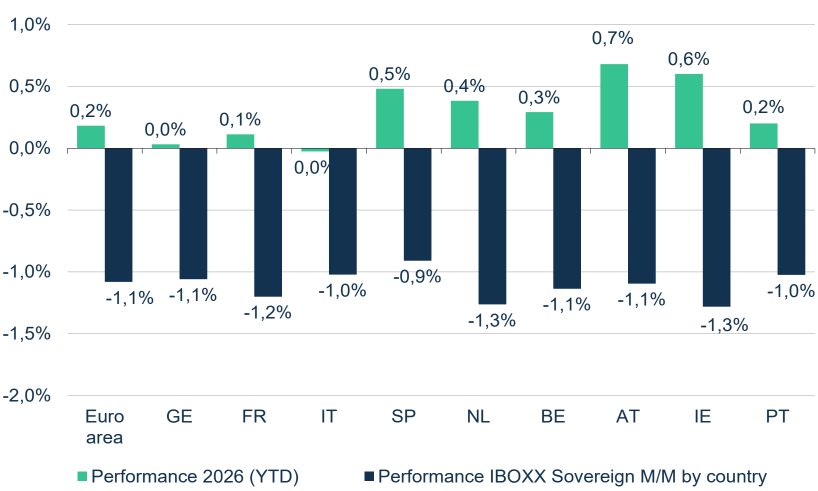
In recent weeks, the primary focus on geopolitical developments has led to repeated sharp turnarounds in sentiment in the euro-denominated government bond market. At the start of the third quarter, bond bulls initially had the upper hand because the U.S.-Iran agreement, which had been concluded shortly before, fueled hopes for a lasting resolution to the conflict that had erupted in late February. The subsequent termination of the ceasefire by U.S. President Trump and the resumption of massive fighting in the Middle East, in turn, fueled concerns about a second energy price shock. Investors were therefore once again increasingly looking to hedge against rising inflation and further interest rate hikes. As a result, the gains from the previous month evaporated on the euro government bond market. Bond bears also benefited from the fact that the eurozone performed better economically in the second quarter than had been feared. In addition, inflation picked up slightly again at the start of summer. The fact that the ECB initially held off on raising interest rates in July did little to reassure investors in this environment. Based on the iBoxx Euro Sovereign Index, the past month actually saw a price decline of 1.7%, following a gain of +0.5% in June. It was the strongest price fluctuation since the first "intense" phase of the war in March 2026. As a result, year-to-date performance temporarily slipped back below zero (currently: +0.2%) before hopes for a de-escalation in the Middle East began to resurface at the start of August.

YTD performance close to zero

Spain has been an outperformer

Italy still slightly underperforming year-to-date

Performance of EUR Government Bonds since the end of June and since the start of 2026 (YTD)



Source: Bloomberg, LBBW Research

Spreads on EUR government bonds vs. swap (in bp)

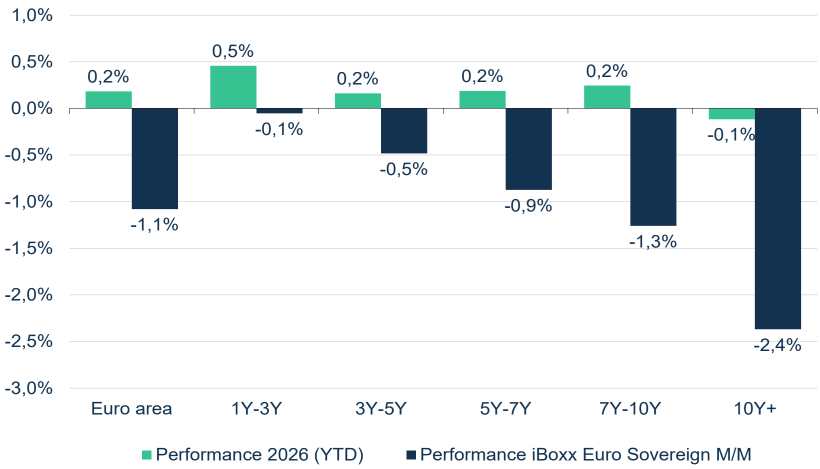
Spreads over swap (in Bp)	2Y	3Y	4Y	5Y	6Y	7Y	10Y
Germany	-24	-23	-19	-19	-16	-13	-4
Finland	-24	-13	-7	2	9	11	26
Netherlands	-26	-19	-15	-10	-6	-3	5
Austria	-17	-14	-7	-4	3	6	20
France	-5	0	10	21	34	44	71
Belgium	-18	-11	0	10	18	25	50
Slovakia	-24	-23	4	19	22	30	57
Latvia	-9	1	13	21	-	45	54
Slovenia	-28	-24	-13	-7	0	3	29
Ireland	-30	-22	-15	-11	-3	-3	11
Italy	-4	4	19	27	41	47	72
Spain	-19	-13	-7	2	7	17	36
Portugal	-27	-21	-10	-4	2	13	30

Ultra-long-term bonds suffer a heavy setback

In a reversal of the pattern that characterized the price recovery in May and June, the high duration leverage caused ultra-long-term government bonds to fall at an above-average rate in July. It is true that the relative weakness was somewhat mitigated by a flattening of the EUR yield curve at the long end. Nevertheless, on a year-to-date basis, ultra-long-term bonds slipped from their temporary role as outperformers back to the position of underperformers (see the chart below).

Long-term bonds falling behind

Long-term bonds fall back into the role of underperformers YTD
Performance of EUR government bonds by maturity segment: month-over-month and year-to-date (YTD)



Source: Bloomberg, LBBW Research

Sovereign spreads stuck within narrow ranges – Italy and France neck and neck

Meanwhile, the July bond sell-off has revealed hardly any spreading across the individual eurozone countries. Consequently, the distribution of performance has remained fairly even when viewed on a year-to-date basis, clustered closely around the zero mark. Italian government bonds kept their underperformance; in other words, they have not yet managed to fully shake off the relative weakness caused by the initial “Iran shock.”

Low volatility in sovereign spreads

Risk premiums for Italy are about 15 basis points above pre-war levels
France, Italy: Yield spreads on 10-year government bonds

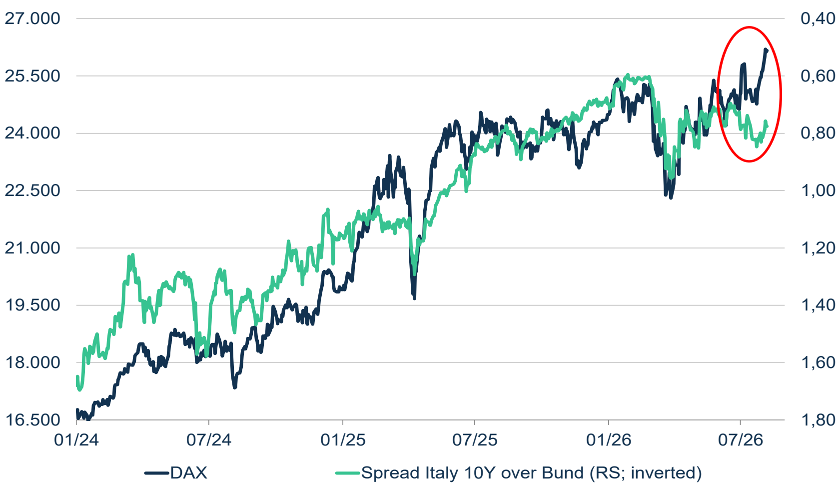
Source: Bloomberg, LBBW Research

Spreads for France and for Italy at around 75 bp, each

As the chart above shows, however, the recent back-and-forth between escalation and de-escalation in the Middle East has not caused credit spreads in the euro-denominated government bond market to fluctuate nearly as sharply as they did in March and April. In addition, the spreads for Italy and France have leveled off neck-and-neck. During the initial phase of sharply increased financial market turbulence, on the contrary, Italian government bonds had been significantly more vulnerable to spread widening than their French counterparts.

In our view, the relatively stable spread trends of the past few weeks reflect the fact that any signs of stress in global financial markets have been moderate overall. This is particularly evident in the global stock markets, where major indices have hit new highs despite ongoing uncertainty in the Middle East. EUR sovereign spreads have not fully priced out geopolitical concerns, as a return to the multi-year lows seen in February 2026 is not yet in sight (see the chart below)

Italian yield spread not keeping pace with new stock market highs
Yield spread of 10-Year Italian government bonds over Bunds and DAX



Source: Bloomberg, LBBW Research

DAX hitting record high, but Italian spread stuck clearly above February level

We draw a two-part conclusion: On the one hand, sovereign spreads appear to have become less susceptible to renewed spikes in uncertainty. On the other hand, investors appear to be reluctant to return to the broad-based yield convergence trades seen in the period before the “Iran shock.” The latter has, not least, shifted the monetary policy trend in the eurozone toward tightening. In our view, the prospect of at least one more ECB rate hike is preventing a new narrowing spread trend from taking shape.

Long-term bonds: Improved risk-reward profile

We also suspect that political risks to the fiscal management of key eurozone countries will gradually come back into focus as the European “super election year” of 2027 draws nearer. Even in a “risk-on” financial market environment, it is therefore difficult for a new wave of “convergence euphoria” to take hold. We therefore do not anticipate such a scenario. While we do believe that long-term EUR government bonds now offer an improved risk-reward profile from a tactical perspective following the recent price pullback. From a relative-value perspective, we would argue that long-term bonds from France, Italy, and Belgium are the most attractive when using the bond basis as a yardstick. Yield spreads in the cash market are higher than the respective premiums in the CDS market in each of these cases. In other words, the bond basis is negative (see adjacent tables: green = cheap/ red = rich).

Bond basis for selected EUR government bonds (in bps)

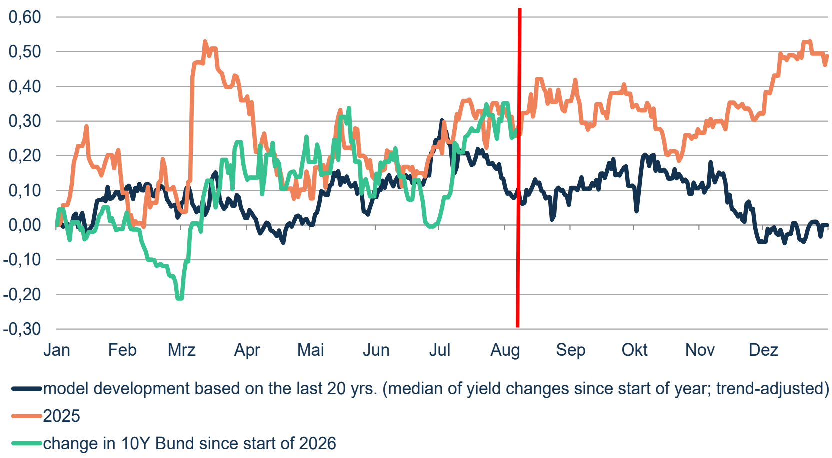
Basis (in Bp)	2 years	3 years	5 years	7 years	10 years
Germany	28	27	26	26	20
Finland	32	26	9	3	-6
Netherlands	30	25	18	15	13
Austria	24	22	15	10	2
France	19	19	10	0	-10
Belgium	24	21	8	0	-12

Basis (in Bp)	2 years	3 years	5 years	7 years	10 years
Ireland	37	30	26	23	16
Italy	16	14	2	-4	-13
Spain	26	23	14	7	-3
Portugal	34	30	18	12	3

Outlook: Will the seasonal pattern prevail after all?

For the time being, the overall market outlook for EUR government bonds remains dominated by the ongoing conflict in the Middle East. The latest diplomatic progress, which is intended to lead to the reliable reopening of the Strait of Hormuz, could still validate the bullish outlook suggested by the seasonal pattern. Statistically speaking, the peak summer months of July and August are therefore among the most promising periods. In addition, the net supply of euro-denominated government bonds on the primary market this month will likely be well below average (see the July 31, 2026, issue of *Bonds Weekly*).

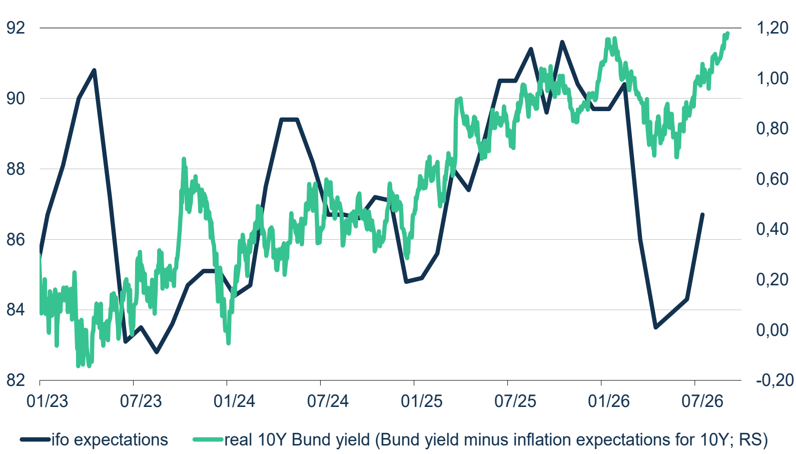
The seasonal pattern remains bullish in August
Cumulative change in the 10-year German government bond yield since the start of the year and model seasonal pattern



Source: Bloomberg, LBBW Research

On the other hand, the bond bears can point to the fact that underlying inflationary pressures across the eurozone also increased somewhat in July. At the same time, economic sentiment has also improved, which tends to free the ECB from some of the constraints of caution as it works to combat rising inflation. In our view, however, the bearish argument of an improved macro situation is limited by the fact that the real yield on 10-year Bunds, at just under 1.2%, had already hit its highest level in about 15 years by the end of July (see the chart below). The real yield has thus slightly exceeded the previous annual high from the period before the outbreak of the Iran War.

Real Bund yields back at pre-Iran war levels
Real yield on 10-year German government bonds (10Y Bund minus inflation expectations) and the ifo expectations component



Source: Bloomberg, LBBW Research

Has the Bund yield now surpassed its annual high?

Better economy is benefiting bears, …

… but the real yield is already at a 15-year high!

U.S. Treasury Market: Focus on funding continuity

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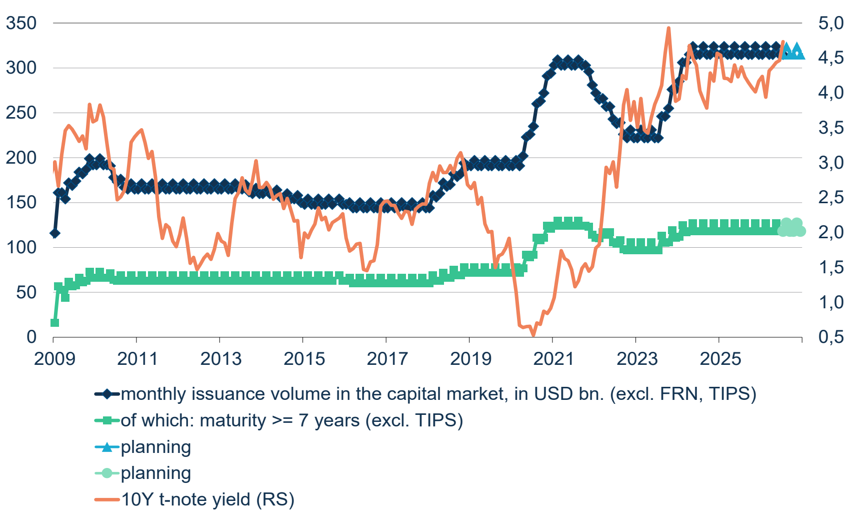
No indication of an imminent adjustment to issuance volumes in the capital market

Coupon bond issuance to total USD 324 billion in August

The U.S. Department of the Treasury remains committed to its current policy regarding the financing of the federal government's ballooning budget deficits. According to the quarterly refunding statement published on August 5, issuance volumes for coupon-bearing bonds with maturities of two years or more are to remain unchanged during the August to October period. The basis for comparison is the preceding fiscal quarter in each case. Excluding inflation-protected securities, whose issuance volumes have risen gradually through the fall of 2025, U.S. debt managers have kept their capital market offerings constant since the spring of 2024: Since then, the Treasury has been issuing monthly coupon-bearing bonds with a total value of up to USD 324 billion, which will also be the case in August 2026. Following the established pattern, a new 10-year T-note, as well as one new 20-year T-bond and one new 30-year T-bond, are issued in the first month of each fiscal quarter. The Treasury will top up the aforementioned (ultra-)long-term bonds in each of the following two months, with the reopenings amounting to USD 3 billion less than the corresponding new issuances in each case. In September and October, capital market issuance (excluding linkers) is therefore set to total 315 billion USD each. Of this total, government securities with a maturity of ten years or more will account for a share of just over 23%, calculated on a quarterly basis.

U.S. longer-term issuance has remained at a plateau since 2024
Monthly capital market issuance volumes by U.S. Treasury (excluding TIPS, in billions of USD) and yields on 10-year Treasury notes



Source: Bloomberg, LBBW Research

Ninth consecutive quarter of stable issuance volumes

Focus on mid-term guidance

Upon release of the quarterly refunding statement, U.S. bond market participants usually focus primarily on the accompanying guidance from debt managers for the coming quarters. Indications of an impending change in the issuance strategy always bear market-moving potential. However, the latest report did not contain any such indications of a change in strategy. As in the previous quarter, the debt managers left their “guidance” unchanged. Accordingly, no adjustment to issuance volumes on the capital market is expected “for at least the next several quarters.” Based on the interpretation commonly held among market experts, we believe that, from the current perspective, no increase in the supply of U.S. longer-term bonds is to be expected through spring 2027.

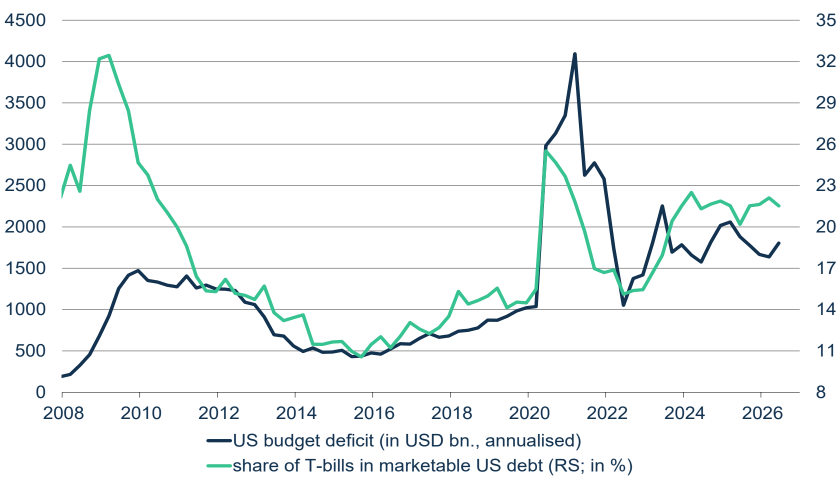
Warsh's Fed reform could stir things up

The Treasury is thus staying true to its strategy of covering any new budget shortfalls – such as those that could arise in the coming fiscal year due to higher military spending – by ramping up the issuance of short-term Treasury bills (T-bills). Over the past three years, the annual U.S. federal budget deficit has consistently been in the range of 2 billion USD (see the chart below). During this period, the share of T-bills in the total outstanding volume of U.S. government bonds has held at above 20%. This is the highest level on record outside of periods of acute economic crisis, such as the global financial crisis and the COVID-19 crisis, during which Treasury bills were typically used to finance a sudden surge in spending needs. The U.S. Treasury Department thus appears to be making this “crisis strategy” standard practice to some extent.

Treasury apparently plans no adjustment until spring 2027

U.S. government needs about 2 trillion USD in "fresh money" each year

U.S. budget deficit (in billions of USD, annualized) and share of T-Bills in marketable debt (in %)



Source: Bloomberg, LBBW Research

T-Bills account for approximately 22% of outstanding bond volume

In our view, how much longer the Treasury can continue to rely on continuity in long-term bond issuance volumes may also depend on the upcoming reforms at the Federal Reserve, which the new Fed Chair, Kevin Warsh, has initiated. One of the five working groups established is focusing on the future size of the Fed's balance sheet. The central bank currently holds USD 4.5 trillion in U.S. Treasury securities in its portfolio. It has long been an open secret that Mr. Warsh prefers a significantly smaller Fed balance sheet. If the aforementioned working group were to recommend reducing holdings, the Treasury would have to increase its borrowing on the money and/or capital markets in return. In this scenario, we assume that debt managers will continue to favor issuing more short-term bonds. However, an excessive imbalance at the short end might significantly drag down the average maturity of U.S. debt, which is currently targeted at about 70 months. If Kevin Warsh, contrary to our previous expectations, pushes through a substantial reduction in the balance sheet, then the Treasury will likely have little choice but to increase the supply of long-term U.S. Treasuries next year as well.

Fed balance sheet runoff would impact issuance strategy

03 I

Credit Strategy

Hope for the Economy

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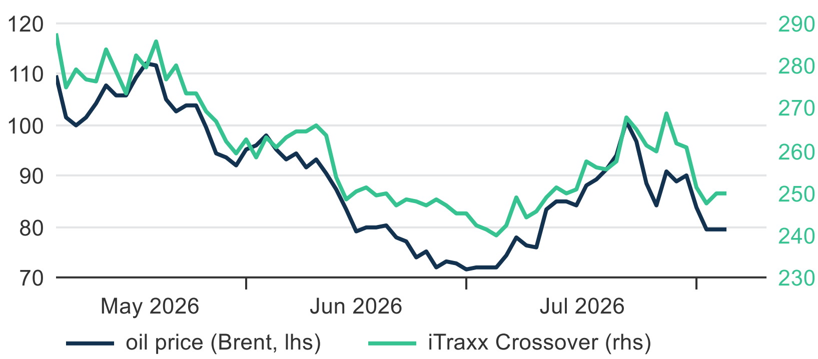
Easing Tensions in the Gulf Region Boosts Credits

The euphoria on the German stock markets continued this week, pushing the DAX above the 26,000-point mark for the first time. Falling oil prices amid a de-escalation of tensions in the Gulf region and positive surprises from the domestic economy were the main factors behind this. As crude oil prices fell, risk premiums in the European credit markets continued to decline. The iTraxx Crossover is thus trading at a very low level again when compared over several years. However, uncertainties such as the Fed's future interest rate policy and the fragile "ceasefires" in the Middle East remain.

iTraxx is looking up, again

Risk Premiums Fall Along with Oil Prices
iTraxx Crossover vs. Oil Price (Brent)

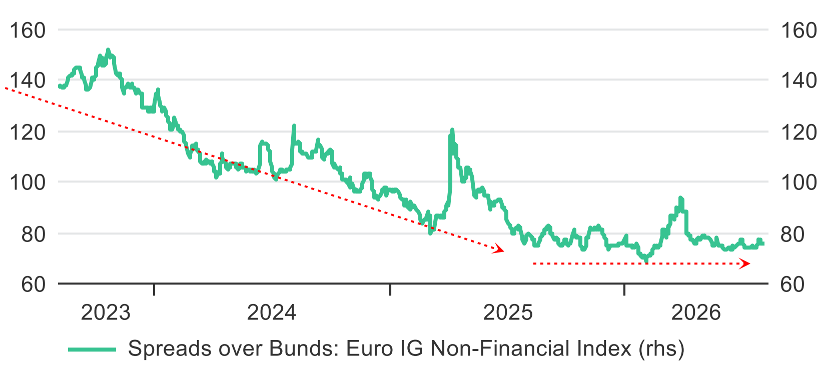


Source: LSEG, LBBW Research

IG spreads have remained largely unaffected by the sharp market fluctuations in recent months. The sideways trend, which has been ongoing for about a year, has continued recently. IG yields moved almost in lockstep with Bund yields. Consequently, credit spreads remained virtually unchanged despite some significant movements in interest rates.

IG yields track German government bond yields

IG Spreads Remain Unfazed
EUR IG Spreads Over Bunds (in Bp.)



Spreads are barely moving

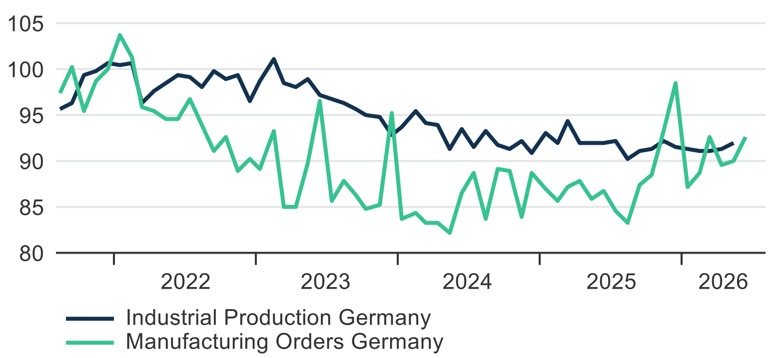
Source: LSEG, LBBW Research

While the service sector in particular had been the main driver of the German economy in recent years, there are now signs of a reversal in this trend: In terms of both the PMIs and new orders, the manufacturing sector in particular picked up again, while the services sector tended to weaken. New orders in the manufacturing sector rose significantly in June, up 3.1% from the previous month. Orders have recently picked up noticeably, especially in the domestic market. In terms of actual sales, this positive trend has not yet been reflected to the same extent; however, the previous decline in this area was not as severe.

More orders for industry

Revenue has not (yet) followed suit

More Orders for the Manufacturing Sector Once Again
Industrial Production and Manufacturing Index (2021 = 100)



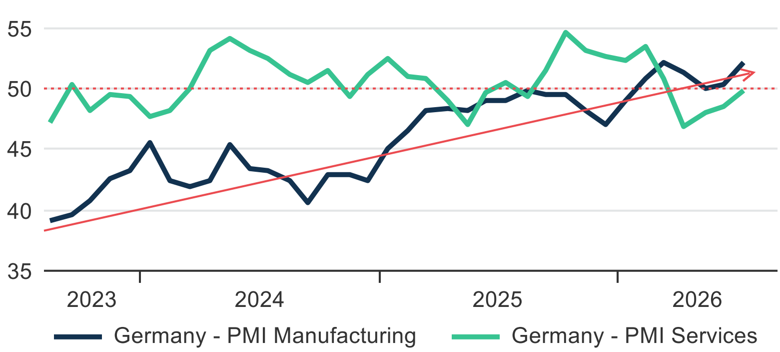
Source: LSEG, LBBW Research

The German composite PMI for July was revised upward once again this week. At 51.3 points, it was well above the expansion threshold, primarily due to the strong 52.2 points recorded in the manufacturing sector. As the conflict in the Gulf region escalated, purchasing managers' outlook for the German services sector had deteriorated significantly and had not yet recovered.

PMI for the manufacturing sector above 50 points

The services sector still struggling to recover

Optimism Is on the Rise Again for the Industry
Germany's PMIs: Manufacturing vs. Services



Source: LSEG, LBBW Research

CONCLUSION – Light at the End of the Tunnel

The renewed sense of confidence in the economy is currently providing a fundamental boost. However, we shouldn't overestimate it just yet. Trump's unpredictability continues to hang over the markets, and the risk of inflation picking up again remains. We are maintaining our recommendation for IG bonds because we continue to view them as a good middle ground between the higher risks associated with high-yield bonds and the lower yields on German government bonds.

IG bonds remain a stable middle ground

Several new corporate bonds with face value of 1,000 EUR in July

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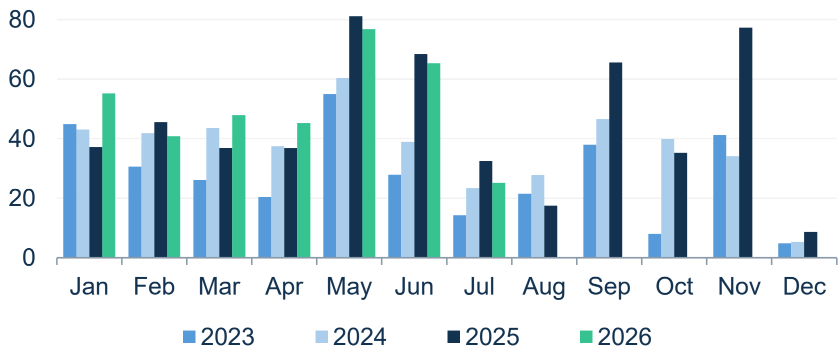
In July, 32 companies were active in the primary market and issued a total of 43 new euro-denominated bonds with a total volume of 25.2 billion euros. The 23% decline compared with the same month last year should be viewed in context: For one thing, July 2025 saw the highest July volume to date, at 32.5 billion EUR. On the other hand, companies had already issued a record volume of new shares in the first half of 2026 (+8% year-over-year). In the two preceding months, May and June, they recorded the third- and ninth-highest monthly volumes on record.

25 billion EUR in July 2026

New Issuances by Month
EUR Corporate Bonds, Volume in billions of EUR



Source: Bloomberg, LBBW Research

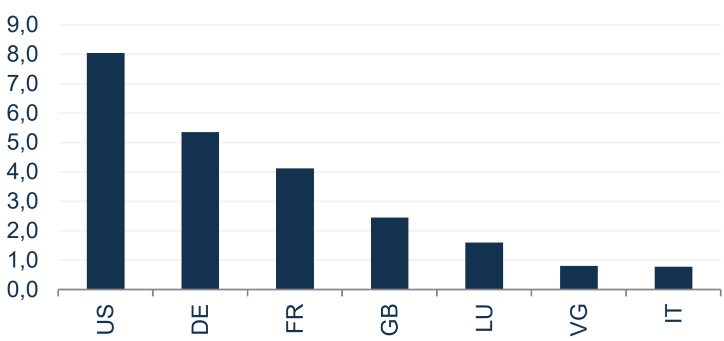
Jan-July 2026: +5% yoy

The average volume of new bonds in July was 585 million euros, and the average maturity was 6.7 years. The largest transaction of the month was also the third-largest year-to-date: The U.S. telecommunications company AT&T issued four bonds totaling 4.1 billion euros (with maturities ranging from 4 to 19 years).

The German utility company Tennet also succeeded in a major transaction: The four new green bonds, totaling 3.5 billion EUR and with maturities ranging from 4 to 20 years, were met with very strong demand (a total of six times the issued volume).

Tennet's green bonds in high demand

Group Headquarters by Country in July 2026
EUR Corporate Bonds, Volume in billions of EUR



Source: Bloomberg, LBBW Research

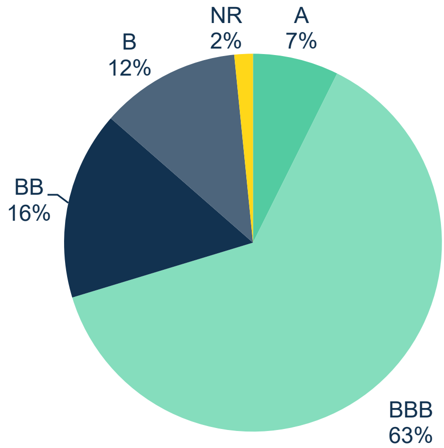
U.S. companies and German companies lead the way

U.S. corporations continued their high level of activity in EUR new issues and once again led the way in July with 8.1 billion euros. Next were corporations from Germany, with EUR 5.4 billion: In addition to Tennet, Fresenius, Hello Fresh, and Sixt were also represented. Now very rare: In July, almost all German companies (with the exception of HelloFresh)

7 bonds with minimum piece of 1,000 EUR

issued their new bonds in denominations of 1,000 EUR (rather than the usual 100,000 EUR).

New Issuances in July 2026 by Rating Category
EUR Corporate Bonds, Percentage of Total Volume



Source: Bloomberg, LBBW Research

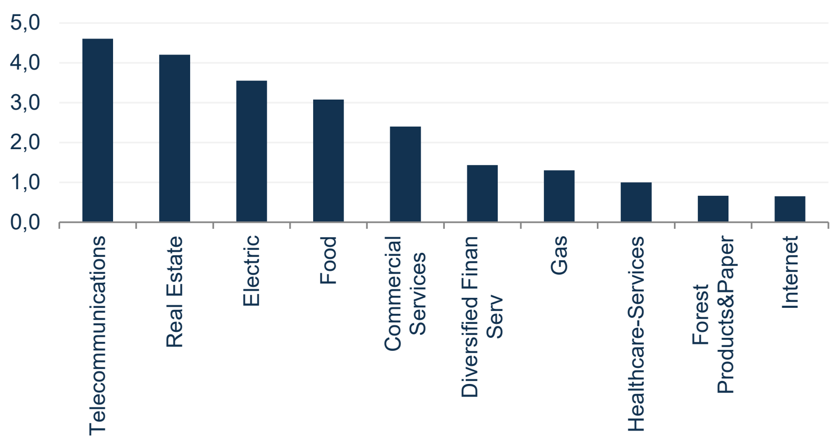
63% from the BBB category

As usual, new issues with a pure IG rating dominated in July (70%). The BBB rating category, in particular, was very well represented (63%). The high-yield segment accounted for an above-average 28% of the monthly volume (the remaining 2% came from unrated companies).

Industries: The traditional heavyweights – telecom and utilities – were among the top three sectors in July, along with the real estate sector.

Top 3: Telecoms, utilities, and real estate

Top 10 Sectors for New Issuances in July 2026
EUR Corporate Bonds, Volume in billions of EUR



Source: Bloomberg, LBBW Research

ESG: Following the record high in June, the ESG ratio remained high in July. 11 of the 43 new issues were issued as green bonds. Excluding U.S. corporations, the ESG ratio came to 30%.

High proportion of ESG bonds

Question: On average, investors subscribed for 3.7 times the volume that was ultimately placed. The published spreads over secondary market bonds averaged 7 basis points (June: 4 Bp.).

Conclusion and Outlook

After reaching a record volume in the first half of 2026, the pace slowed in July. Companies and investors were paying increasing attention to the summer vacation period. As a result, activity on the primary market is likely to remain somewhat subdued in the coming weeks—as is typical during the summer vacation month of August.

Summer break continues

04 I

Calendar/Analytics

Developed Markets Overview

	2 Years			10 Years		
Euro Area	**Yields**	**Spread**	**Change***	**Yields**	**Spread**	**Change***
Bund	2,76			3,14		
Jumbo	2,99	22	0	3,49	35	-1
Swap	2,97	21	0	3,18	4	0
Netherlands	2,73	-4	-2	3,23	9	0
Austria	2,79	2	-2	3,35	21	-2
France	2,93	17	0	3,93	79	0
Belgium	2,80	3	0	3,68	54	0
Italy	2,93	17	-1	3,92	78	-4
Spain	2,79	3	-1	3,58	44	-1
Ireland	n.a.	n.a.	n.a.	3,29	15	0
Portugal	2,73	-3	-1	3,48	34	-1
Greece	n.a.	n.a.	n.a.	3,82	68	-3
EX. EURO AREA	**Yields**	**Spread**	**Change***	**Yields**	**Spread**	**Change***
USA	4,25	148	1	4,68	154	1
Canada	2,93	16	7	3,62	48	2
Japan	1,60	-116	16	2,80	-34	6
UK	4,30	154	-4	4,94	180	-5
Switzerland	0,10	-267	-1	0,37	-277	0

* Weekly change of the spread w.r.t. Bund w/w

Sources: Bloomberg, LBBW Research

Issuing Calendar Government Bonds

Date	Country	Type	Maturity	Coupon	Size	Comment
11.08.2026	Germany	OBL	10/31	2.90%	€ 5.5 bn.	Tap
11.08.2026	Finland	RFGB			€ 1.5 bn.	Tap
11.08.2026	USA	T-Note	08/29		USD 58 bn.	New
12.08.2026	Japan	JGB I/L	10Y		JPY 250 bn.	
12.08.2026	Germany	Bund	30Y		€ 2.5 bn.	Tap
12.08.2026	UK	UKTI	9Y		GBP 1.5 bn.	Tap
12.08.2026	USA	T-Note	08/36		USD 42 bn.	New
13.08.2026	Italy	BTP	3Y - 30Y			Cancelled
13.08.2026	USA	T-Bond	08/56		USD 25 bn.	New

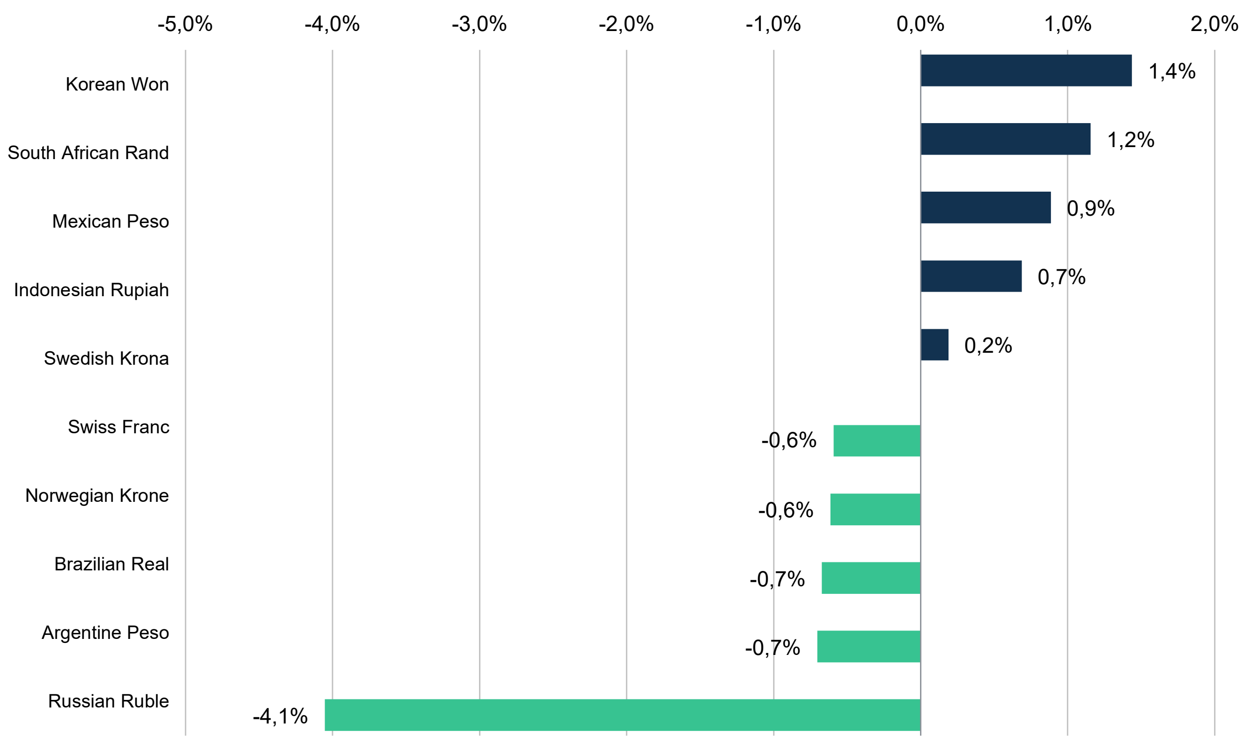
Sources: Bloomberg, LBBW Research

Central Banks and FX Monitor

Country	Next meeting	Current key rate	Latest change	Previous key rate	CPI YoY	6M trend	6M FX change ag. EUR	EUR-FX	6M EUR-FX Forward
Euro Area	10.09.26	2,25%	11.06.26	2,00%	2,9%	↑			
United States	16.09.26	3,75%	10.12.25	4,00%	3,5%	↗	3,3%	1,1521	1,1607
United Kingdom	17.09.26	3,75%	18.12.25	4,00%	2,6%	↘	1,6%	0,8565	0,8628
Japan	18.09.26	1,00%	16.06.26	0,75%	1,7%	↘	1,8%	182,49	181,15
China	***	2,00%	25.09.24	2,30%	1,0%	·	6,1%	7,77	7,72
Switzerland	24.09.26	0,00%	19.06.25	0,25%	0,4%	↗	-2,5%	0,9364	0,9239
Argentina	***	29,00%	31.01.25	32,00%	32,6%	↘	-2,0%	1.727,13	1.932,71
Australia	11.08.26	4,35%	05.05.26	4,10%	3,2%	↗	2,4%	1,64	1,66
Brazil	16.09.26	14,00%	05.08.26	14,25%	4,6%	·	4,8%	5,89	6,16
Canada	02.09.26	2,25%	29.10.25	2,50%	2,8%	↗	0,0%	1,62	1,61
Czech Republic	17.09.26	3,75%	18.06.26	3,50%	1,7%	·	-0,1%	24,25	24,36
Denmark	***	2,00%	12.06.26	1,75%	1,9%	·	-0,1%	7,48	7,46
Hong Kong	***	4,00%	08.11.24	4,25%	2,0%	↗	3,0%	9,04	9,06
Hungary	25.08.26	5,75%	21.07.26	6,00%	1,7%	↓	3,1%	365,44	370,17
India	07.10.26	5,25%	06.02.25	5,50%	4,4%	↑	-1,9%	109,77	112,31
Indonesia	19.08.26	5,75%	18.06.26	5,50%	2,9%	↘	-3,3%	20.625,44	21.094,56
Mexico	06.08.26	6,50%	07.05.26	6,75%	3,4%	↘	3,4%	19,82	20,27
New Zealand	02.09.26	2,50%	08.07.26	2,25%	4,1%	↑	0,1%	1,97	1,97
Norway	13.08.26	4,25%	07.05.26	4,00%	2,7%	↘	3,8%	10,99	11,10
Poland	09.09.26	3,75%	04.03.26	4,00%	3,0%	↗	-2,2%	4,30	4,33
Romania	10.08.26	6,50%	07.08.24	6,75%	10,4%	·	-3,1%	5,25	5,35
Russia	11.09.26	14,00%	24.07.26	14,25%	6,0%	·	-3,7%	95,37	101,66
Singapore	***	1,97%	n.a.	1,63%	1,9%	↗	2,0%	1,48	1,47
South Africa	23.09.26	7,00%	28.05.26	6,75%	5,0%	↑	0,5%	18,85	19,26
South Korea	27.08.26	2,75%	16.07.26	2,50%	2,8%	↗	6,0%	1.636,10	1.641,09
Sweden	20.08.26	1,75%	23.09.25	2,00%	0,2%	↘	-3,2%	10,97	10,94
Turkey	10.09.26	37,00%	22.01.26	38,00%	31,8%	·	-5,5%	54,99	64,33

Sources: Bloomberg, LBBW Research

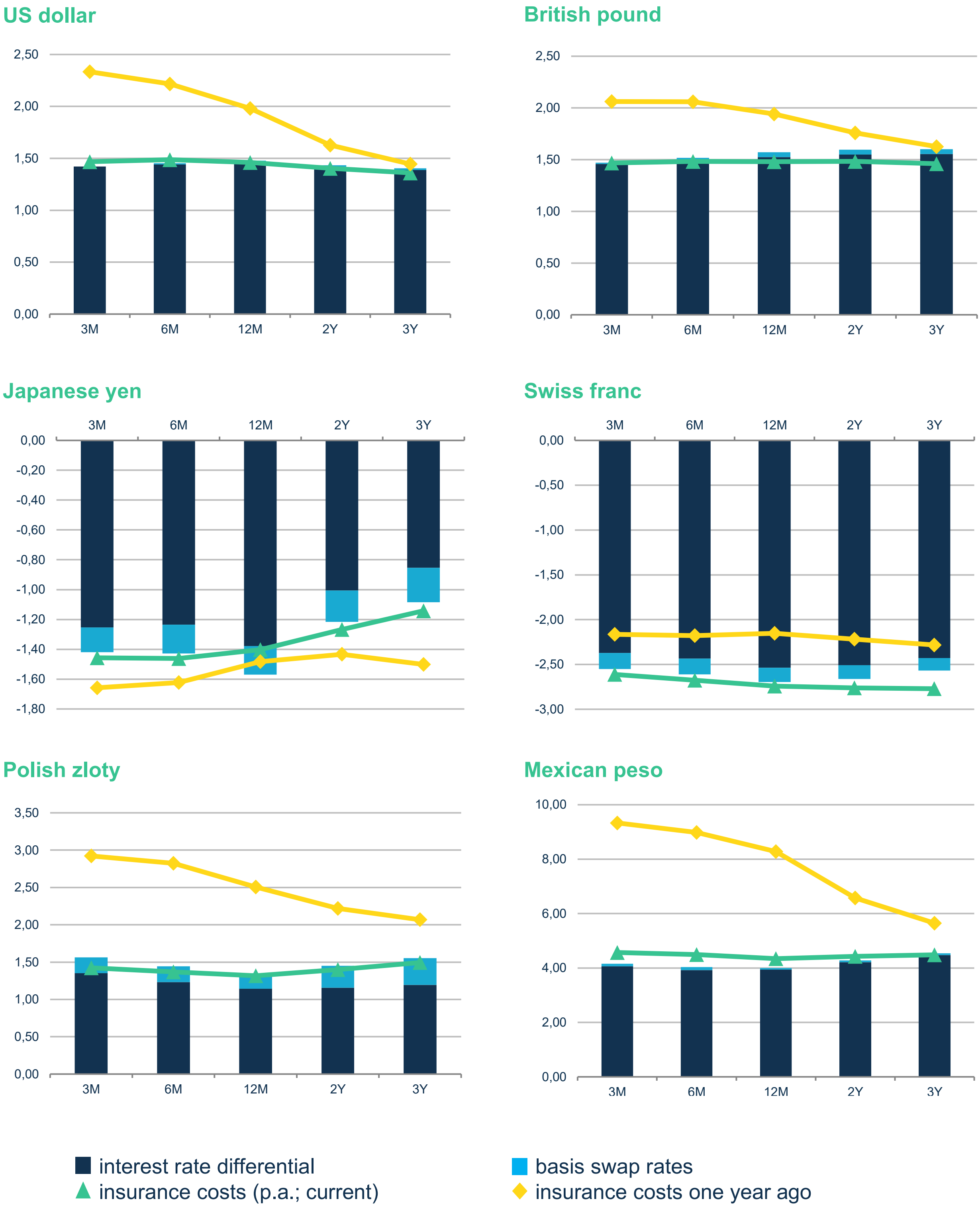
The Strongest Currency Appreciations and Depreciations Against the Euro This Week



Sources: Bloomberg, LBBW, Research

Interest rate differential and FX insurance costs vs. the Euro for selected currencies

interest rate differential, basis swap rates and insurance costs



Sources: Bloomberg, LBBW Research

Credit Spreads

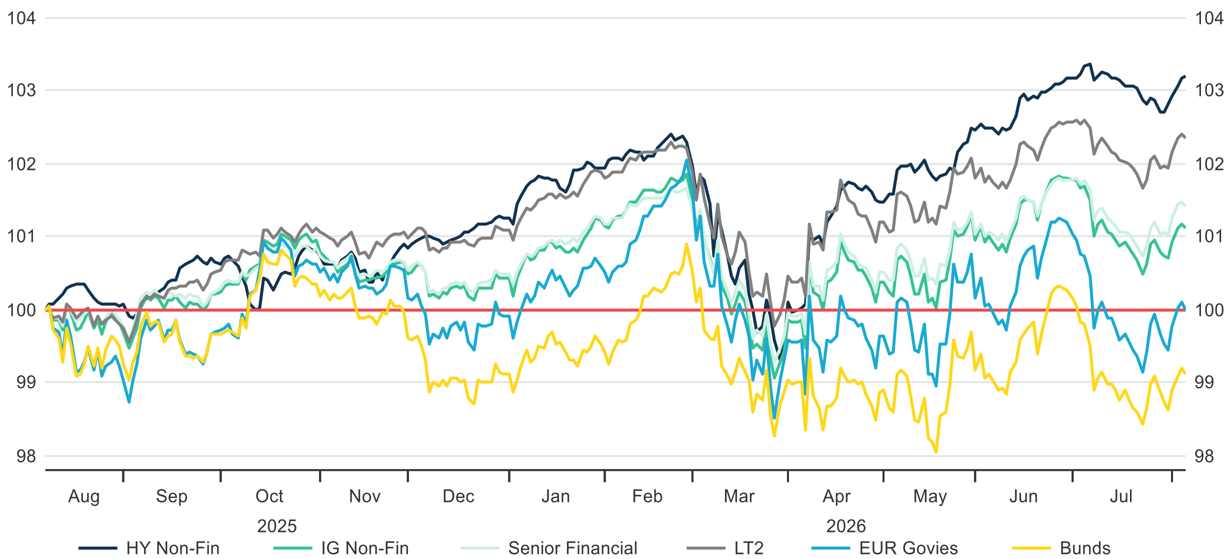
5Y CDS Spreads	Current	Changes 1W	1M	3M	6M	1Y
IG Corporates	51	-2	0	-5	0	-3
HY & NR Corporates	250	-11	8	-29	6	-21
Senior Financials	54	-2	0	-6	0	-5
Sub Financials	87	-3	-1	-11	-3	-7

EUR Indices	Current	Changes 1W	1M	3M	6M	1Y
Non-Financials	74	0	1	-4	2	-7
Banks Senior Preferred	49	-1	-3	-7	-5	-12
Banks Senior Bail-in	67	-2	-1	-8	-5	-11
Banks Subordinated	101	-2	-2	-10	-6	-23

*time lag of one day, Asset Swap Spreads 07.08.2026

Sources: LSEG, LBBW Research

Performance Credits vs. Bunds (LTM – last twelve months)



Quellen: LSEG, LBBW Research

Allocation recommendations (Credits vs. Bunds)

Under observation of 6 – 12 months

	Recommendation		Segments		Regions	Strategies
Rates	0/+	0	0-3 years	0/+	Euro periphery	Multi-Callables
		0/+	4-7 years	0	German Bunds	Inflation-linked bonds
		0	8-10 years	0/-	USD-Bonds	
Credit	0/+	0/+	Corporate Inv. Grade	0/-	Emerging Markets Debt	
		0	Corporate High Yield			
		0/+	Corporate Hybrids (IG)			
		0/+	Senior Financials			
		0/+	Covered Bonds/SSAs			
		0	Tier 2 Inv. Grade/ Sen. Non-Pref.			

Sources: LBBW Research

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Disclaimer

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