



CIO Insights

Cusson Leung, Chief Investment Officer,
International Wealth Management

Rising Bond Yield: Not a Crisis

A Potential Reversal by the End of 1Q27

16 October 2026



Rising U.S. Bond Yields Suppress Valuations in Theory

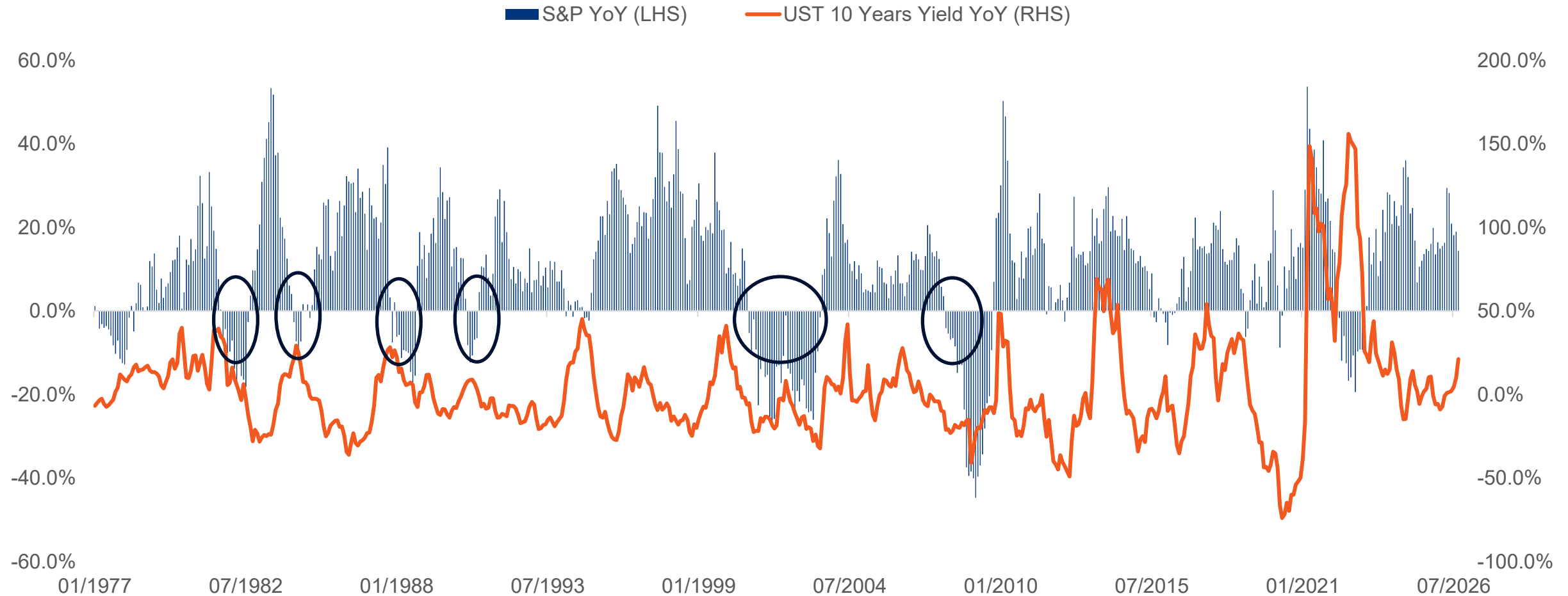
Yet Rising Bond Yields Have Coincided with Rising Markets



Source: Bloomberg, KGI

Could Rising Bond Yields Trigger a Crisis?

A Significant Market Correction Usually Is Not Caused by Rising Bond Yields



Source: Bloomberg, KGI

Rising Yields Are a Precondition, Not the Cause, of a Crisis

A Trend Can Be Managed by Markets. An Out-of-Protocol Event Cannot

- **The trend is a precondition, not the cause of a crisis.** An unfolding trend – good or bad – is observable. Participants price it, hedge it, fund it and build rules around it. That is why a trend, however severe, rarely causes a crisis by itself. It creates vulnerability; it does not create the crisis.
- **The trigger is an unexpected event** – a surprise relative to expectations, not absolute size. The rupture comes from something that consensus did not anticipate. That is why an event's magnitude matters far less than its unexpectedness.
- **The protocol fails – and that is the true cause of a crisis.** Every participant and authority carries a playbook: the central bank has a reaction function, the hedge fund has a risk model and the treasury has a funding plan. The playbook is calibrated to the trend. A surprise the protocol can absorb is merely a shock; a surprise it cannot absorb becomes a crisis.
- **Do not focus on the yield level** – focus on the speed of change and on who is forced to sell. The level is merely the trend; the gap is the shock; the forced seller is the crisis.

A crisis may or may not materialize. But with (1) elevated bond yields, (2) a large funding gap for AI capex and (3) market concentration, already in place as crisis pre-conditions, the backdrop is primed for higher volatility – even if the market trend remains positive.

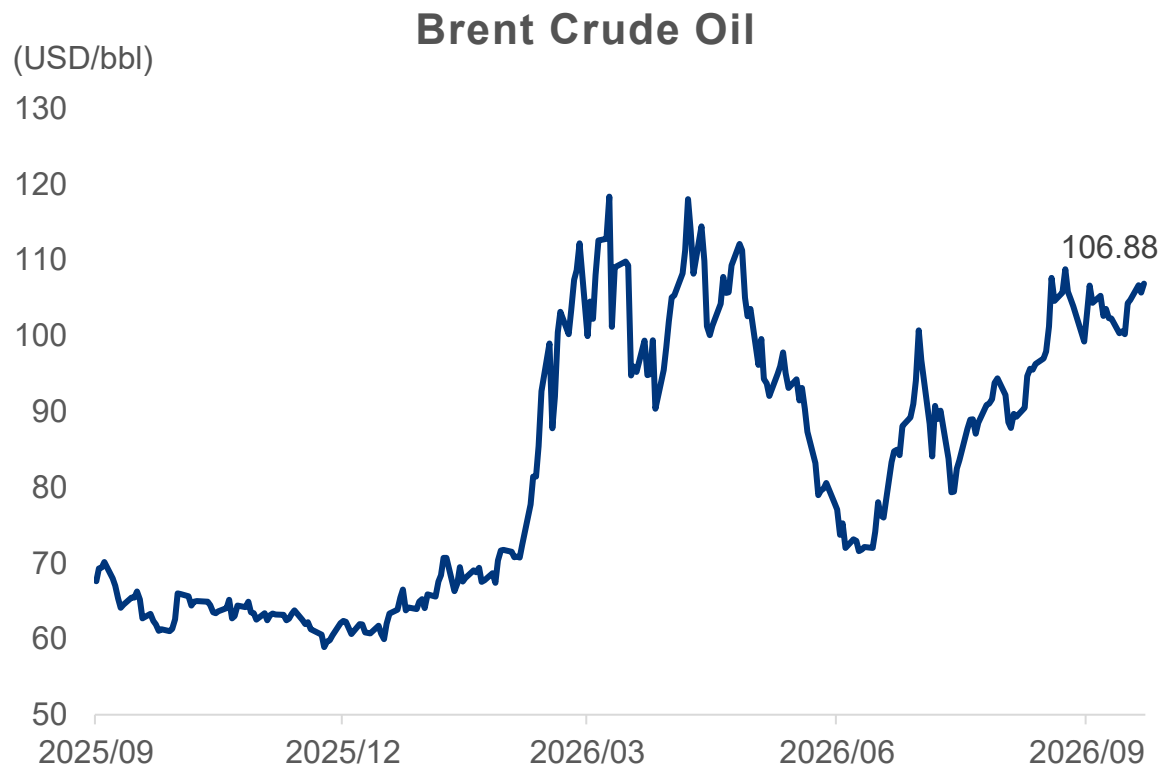
Long-Bond Yield Levels Are Driven by More Than Inflation

The Term Premium Is Global: German Bunds, UK Gilts and JGBs All Feed Through to USTs

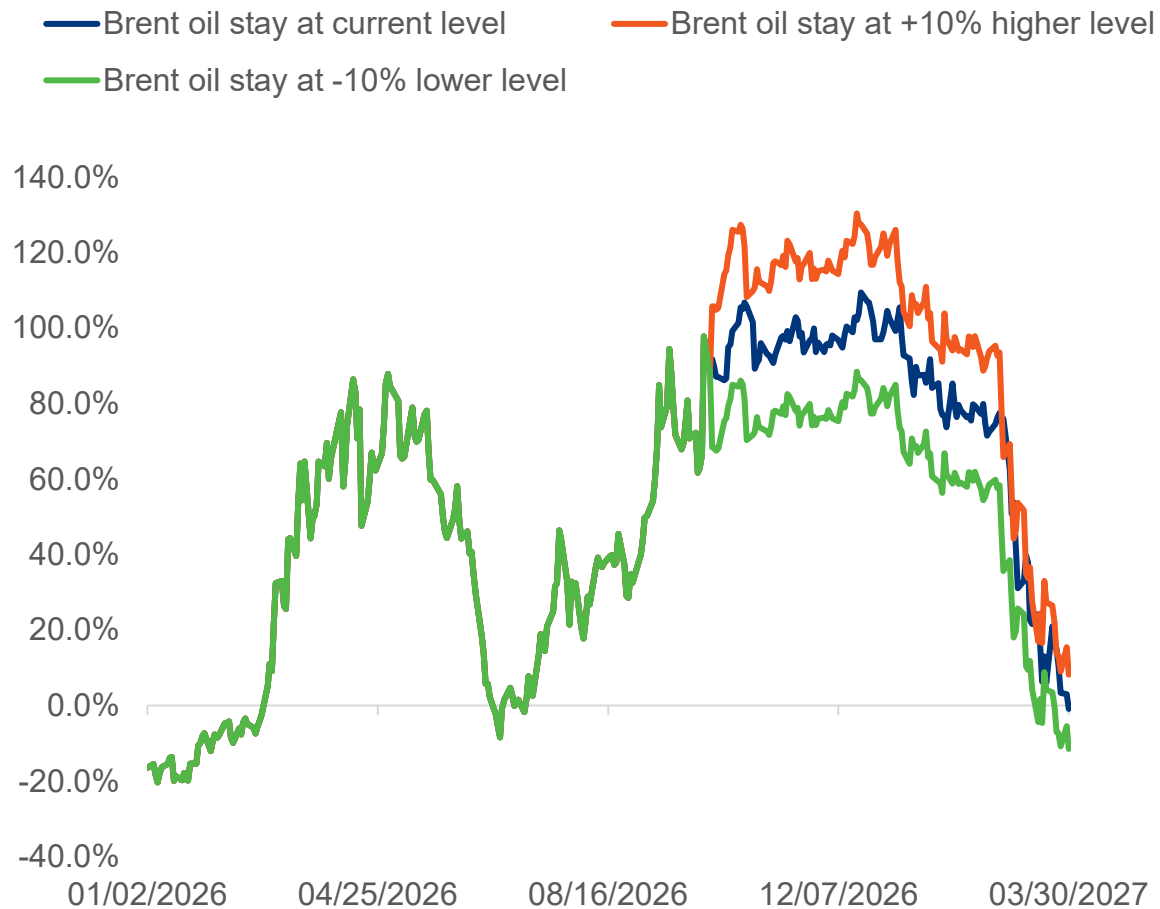
- **Inflation expectations.** The key question is whether expectations remain anchored at 2%. Sticky services inflation, wages, shelter, tariffs and deglobalization raise the risk premium.
- **Growth expectations.** Strong growth and productivity lift real yields; recession fears drive a flight to quality and lower long yields – even before the Fed moves.
- **U.S. debt / fiscal.** This is reflected primarily in the term premium, not the policy rate. A 6-7% of GDP deficit, debt-to-GDP above 120%, heavy coupon issuance, weak auction tails and a shrinking base of price-insensitive buyers (the Fed conducting QT and foreign central banks stepping back) all lift the term premium.
- **Global capital competition.** Japan is a live example: the 10-year JGB recently broke 3% for the first time since 1996 (3.11% on 7 October). As JGBs and hedged foreign yields become more attractive, Japanese capital repatriates, the yen carry trade unwinds and global duration is repriced – a higher-for-longer world. The term premium is global: German Bunds, UK gilts and JGBs feed through to USTs.
- **The dollar / de-dollarization / politics.** A deliberate strong-dollar policy generally means higher U.S. rates than peers. Yet de-dollarization is a real structural trend: the ECB reported in June 2026 that gold had overtaken U.S. Treasuries as the largest official reserve asset. Lower foreign central-bank demand means a higher term premium for U.S. taxpayers.

Unless Oil Prices Rise Much Further from Current Levels

Year-on-Year Oil-Price Growth Should Flatten – or Turn Negative – from March 2027



This should support a rate-cut narrative by late 1Q27.



Source: Bloomberg, KGI

The September Hike Was an Inflation-Insurance Move

Current U.S. Economic Conditions Do Not Warrant a High-Interest-Rate Environment

Nonfarm Payrolls (September)

+29k

Well below consensus; hiring is weak

Unemployment Rate

4.2%

Up from 4.1%; a low-hire, low-fire labor market

U-Mich Sentiment

46.3

Five-month low; current-conditions index at a record low

Real GDP (Q2)

+2.2%

Solid, but growth is narrowing to AI and capex

AIER Leading Indicator

42

Down sharply from 88; housing and retail are weak

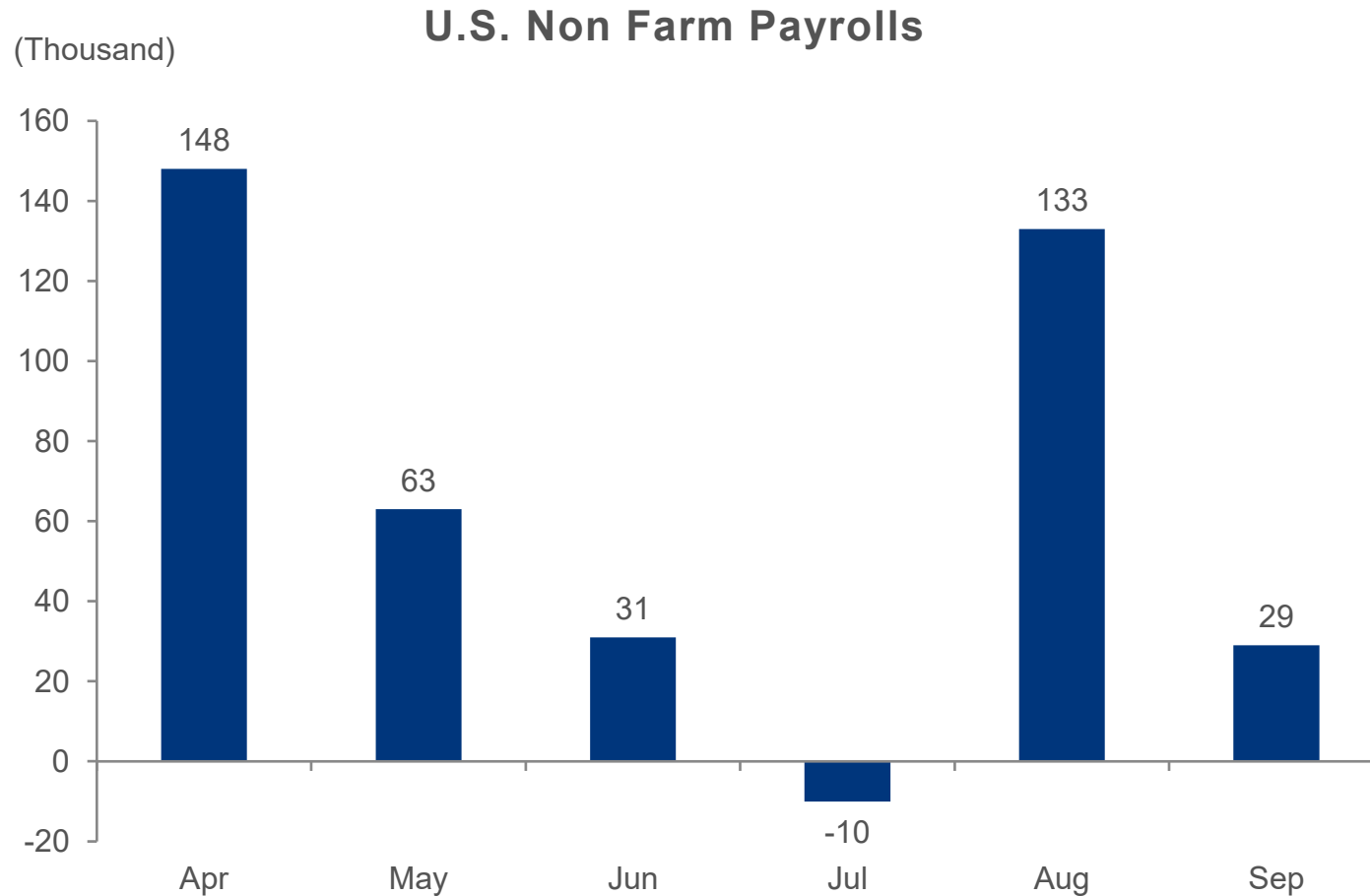
10-Year U.S. Treasury

~5.2%

Elevated yields; fiscal pressure persists

Labor Market: Hiring Has Stalled

September Payrolls: +29K. Prior Months Revised Lower. Unemployment Is Rising as Participation Softens

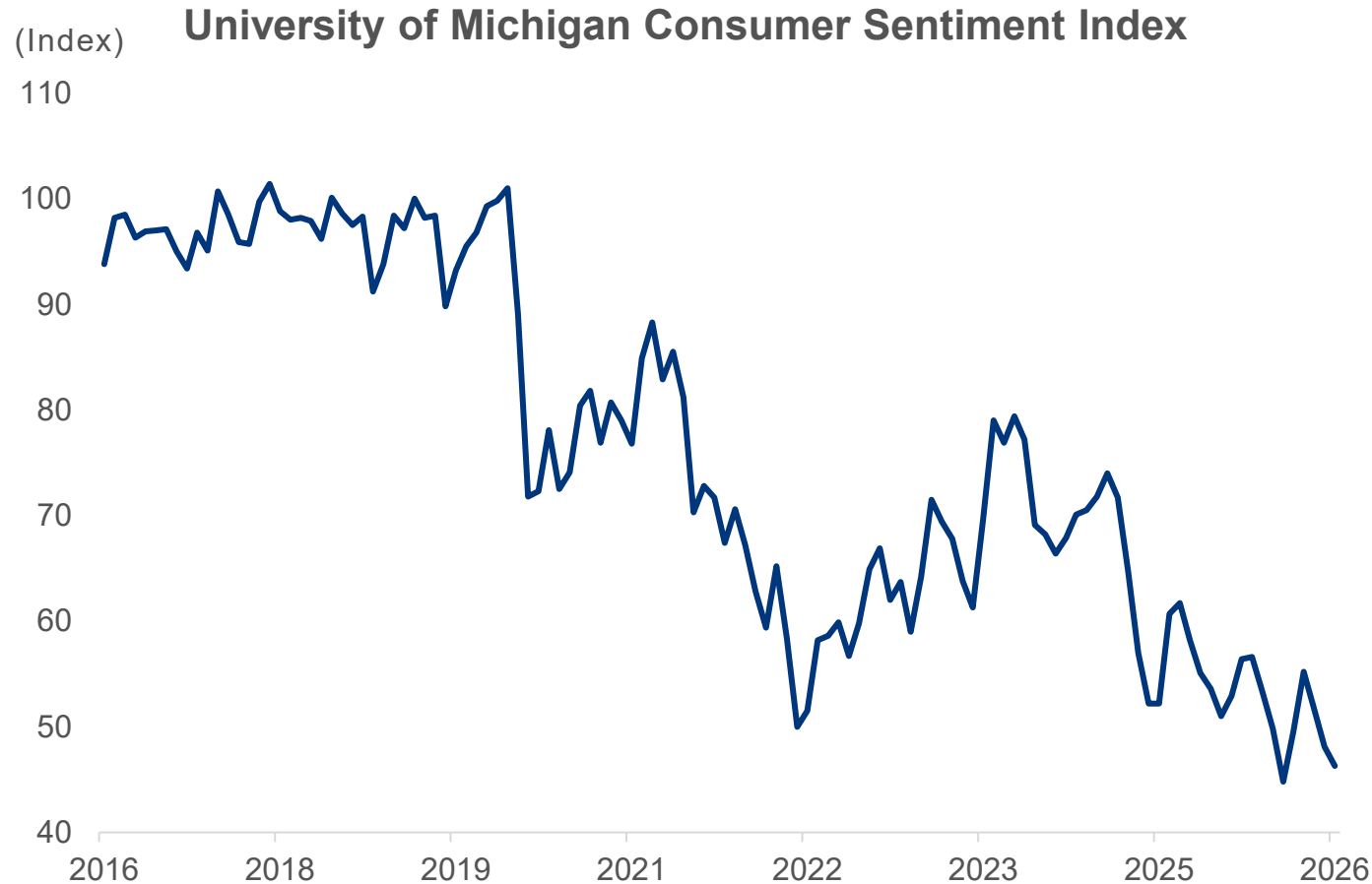


Key observations

- “Low-hire, low-fire” regime
- Household survey is weaker; labor force has declined
- Breakeven job growth is near zero as population growth slows
- Unemployment at 4.2% (up 0.1pp)

Consumer Sentiment Near Recessionary Levels

University of Michigan, Early October: 46.3. Current Conditions Hit a Record Low of 44.7

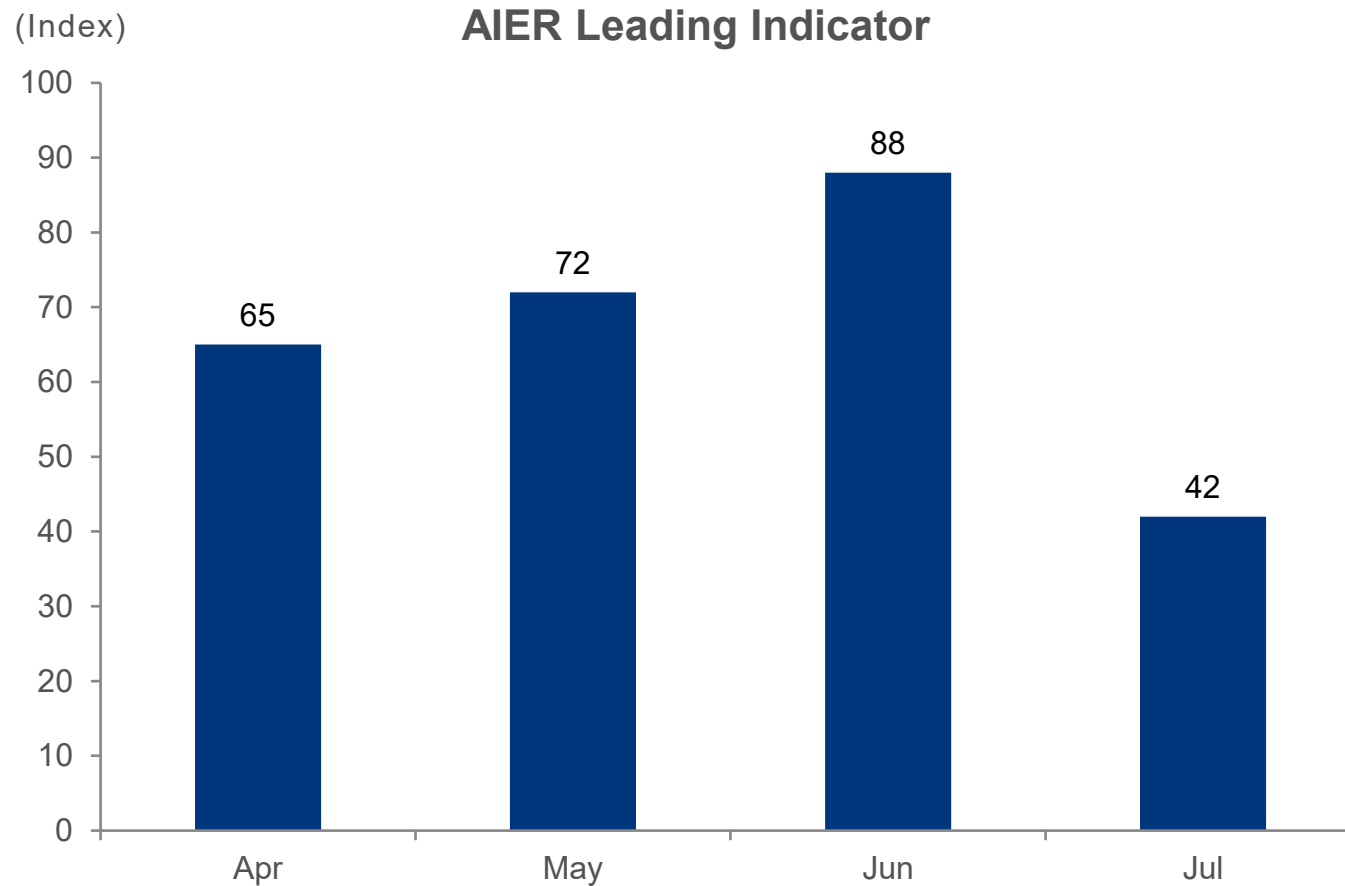


Why It Matters

- *Sentiment leads spending*
- *High gasoline prices and sticky inflation*
- *Only ~31% plan to maintain spending*
- *Divergence: aggregates remain strong, but households feel squeezed*

Leading Indicators Have Reversed Sharply

AIER's Business Conditions Leading Indicator Fell From 88 to 42 in July, With Weakness in Housing, Retail, Transportation, Capital Goods and the Yield Spread



Components Under Pressure

- *Housing and retail activity*
- *Transportation*
- *Capital-goods orders*
- *Yield-spread signal*

Coincident indicators remain sound – a classic late-cycle pattern

The Setup for 2027 – Investment Strategies

Both Inflation and Growth Momentum Are Slowing: Long-Bond Yields Should Fall Back Below 5%

- **Inflation:** From March 2027, a high oil-price base effect should push year-on-year oil-price changes toward flat or negative territory – unless oil prices rise much further. Inflation pressures should ease, reinforcing the case for rate cuts by late 1Q27.
- **Growth momentum:** Hiring has stalled, consumer sentiment is near recessionary levels and leading indicators are weakening across housing, retail, transportation and capital goods – an increasingly late-cycle profile.
- **Long bond yield:** In a textbook disinflationary slowdown, lower inflation expectations and softer real-growth expectations reduce the inflation and real-yield components of long rates. All else equal, long-bond yields should fall below 5%, although fiscal supply and term premium remain key risks. While investment-grade corporate bonds remain preferred for now, we expect flows to rotate increasingly toward long-dated Treasuries in 2027.
- **Equity valuation:** As long-bond yields decline, they should support valuations in the growth segment of the market. Funding costs for growth companies should also ease as upward pressure on benchmark rates recedes, reviving risk-on sentiment.
- **Structured-product equity exposure:** With short-term uncertainty still high, volatility is likely to persist until the market gains a clearer view of the interest-rate path. We suggest selectively selling puts or calls while volatility remains elevated.

Disclaimer and Important Notice

Hong Kong: The information contained in the document herein is confidential and is not intended for general public distribution or for use by any person or entity located or residing in any jurisdiction which restricts the distribution of such information by KGI Asia Limited ("KGI") or any affiliate of KGI. Re-distribution of the document herein and any part thereof by any means is strictly prohibited. Such information shall not be regarded as an offer, invitation, solicitation or recommendation to invest in or sell any securities or investment products to any person or entity in any jurisdiction. The above information (including but not limited to general financial and market information, news services, market analysis and product information) is for general information and reference purpose only and may not be reproduced or published (in whole or in part) for any purpose without the prior written consent of KGI Asia Ltd. Such information is not intended to provide investment advice and should not be relied upon in that regard. You are advised to exercise caution, and if you are in any doubt about such information, you should seek independent professional advice.

You are advised to exercise caution and undertake your own independent review, and you should seek independent professional advice before making any investment decision. You should carefully consider whether investment is suitable in light of your own risk tolerance, financial situation, investment experience, investment objectives, investment horizon and investment knowledge.

No representation or warranty is given, whether express or implied, on the accuracy, adequacy or completeness of information provided herein. In all cases, anyone proposing to rely on or use the information contained herein should independently verify and check the accuracy, completeness, reliability and suitability of the information. Simulations, past and projected performance may not necessarily be indicative of future results. Information including the figures stated herein may not necessarily have been independently verified, and such information should not be relied upon in making investment decisions. None of KGI, its affiliates or their respective directors, officers, employees and representatives will be liable for any loss or damage of any kind (whether direct, indirect or consequential losses or other economic loss of any kind) suffered or incurred by any person or entity due to any omission, error, inaccuracy, incompleteness or otherwise, or any reliance on such information. Furthermore, none of KGI, its affiliates or their respective directors, officers, employees and representatives shall be liable for the content of information provided by or quoted from third parties.

Complex Products refers to an investment product whose terms, features and risks are not reasonably likely to be understood by a retail investor because of its complex structure. Investors should exercise caution in relation to complex products. Investors may lose the entire amount or more than the invested amount. For complex products with offering documents or information not reviewed by the Hong Kong Securities and Futures Commission (SFC), investors should exercise caution regarding the offer. For complex products described as SFC-approved, such approval does not imply official endorsement, and SFC recognition does not equate to a recommendation or assurance of the product's commercial viability or performance. Past performance data, if provided, is not indicative of future performance. Some complex products are only available to professional investors. Before making any investment decisions, investors should review the offering documents and other relevant information to understand the key nature, features, and risks of the complex products. Independent professional advice should be sought, and investors should have sufficient net assets to bear the potential risks and losses associated with the product. Members of the KGI group and their affiliates may provide services to any companies and affiliates of such companies mentioned herein. Members of the KGI group, their affiliates and their directors, officers, employees and representatives may from time to time have a position in any securities mentioned herein.

Bond investment is NOT equivalent to a time deposit. It is NOT protected under the Hong Kong Deposit Protection Scheme. Bondholders are exposed to a variety of risks, including but not limited to: (i) Credit risk - The issuer is responsible for payment of interest and repayment of principal of bonds. If the issuer defaults, the holder of bonds may not be able to receive interest and get back the principal. It should also be noted that credit ratings assigned by credit rating agencies do not guarantee the creditworthiness of the issuer; (ii) Liquidity risk - some bonds may not have active secondary markets and it would be difficult or impossible for investors to sell the bond before its maturity; (iii) Interest rate risk - When the interest rate rises, the price of a fixed rate bond will normally drop, and vice versa. If you want to sell your bond before it matures, you may get less than your purchase price. Do not invest in bond unless you fully understand and are willing to assume the risks associated with it. Please seek independent advice if you are unsure.

All investments involve risks. The prices of securities fluctuate, sometimes dramatically. The price of a security may move up or down, and may become valueless. It is as likely that losses will be incurred rather than profit made as a result of buying and selling securities. Prices of securities and fund units may go up as well as down and past performance information presented is not indicative of future performance. Investors should read the relevant fund's offering documents (including the full text of the risk factors stated therein (in particular those associated with investments in emerging markets for funds investing in emerging markets)) in detail before making any investment decision. You are advised to exercise caution and undertake your own independent review, and you should seek independent professional advice before making any investment decision. You should carefully consider whether investment is suitable in light of your own risk tolerance, financial situation, investment experience, investment objectives, investment horizon and investment knowledge.

Singapore: This document is provided for general information and circulation only, and is not an offer or a solicitation to deal in any securities or to enter into any legal relations, nor an advice or a recommendation with respect to any financial products mentioned herein. It does not have regard to the specific investment objectives, financial situation and the particular needs of any recipient hereof. You should ensure that you understand the risk(s) involved and should independently evaluate particular investments and consult an independent financial adviser before making any investment decisions. All information and opinions contained herein is based on certain assumptions, information and conditions available as at the date of this document and may be subject to change at any time without notice.