

Rising Treasury Yields: Causes, Consequences, and Risks for Global Markets



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Introduction

Bond yields have surged across the world to levels not seen in decades, reflecting growing concerns over inflation, debt sustainability, and the outlook for interest rates. In the United States, Treasury yields have reached multi-decade highs, with the 5-year yield rising above 5% for the first time since 2007, the benchmark 10-year yield climbing to its highest level since June 2007, and the 30-year yield reaching levels last seen in June 2004.

The rise is not limited to the United States. In France, the benchmark 10-year yield is approaching 5%, a level not seen in more than two decades. In Japan, the 10-year government bond yield has climbed above 3% for the first time in three decades, while the median 10-year sovereign yield across advanced economies has reached 4%, its highest level in over 15 years.

Part of this global increase reflects the dominant and leading role of US Treasury yields in international financial markets. As US yields rise, other countries often need to offer higher yields to attract and retain investor capital.

Given the central role of US Treasury yields in shaping global financial conditions, this report examines the main factors behind the surge in US Treasury yields, including stronger-than-expected economic growth, persistent inflation, tighter monetary policy expectations, growing AI-related borrowing, widening fiscal deficits, foreign selling of Treasuries, and technical market dynamics. It also explores how higher yields are affecting stocks, the US dollar, households, businesses, and the broader financial system, and assesses whether current debt trends pose a meaningful risk to US financial stability.

1. Factors Driving the Surge in US Yields

1.1. Strong Economic Growth

Bonds tend to be most attractive during economic downturns. During these times, investors often shift toward safe-haven assets such as US Treasury bonds.

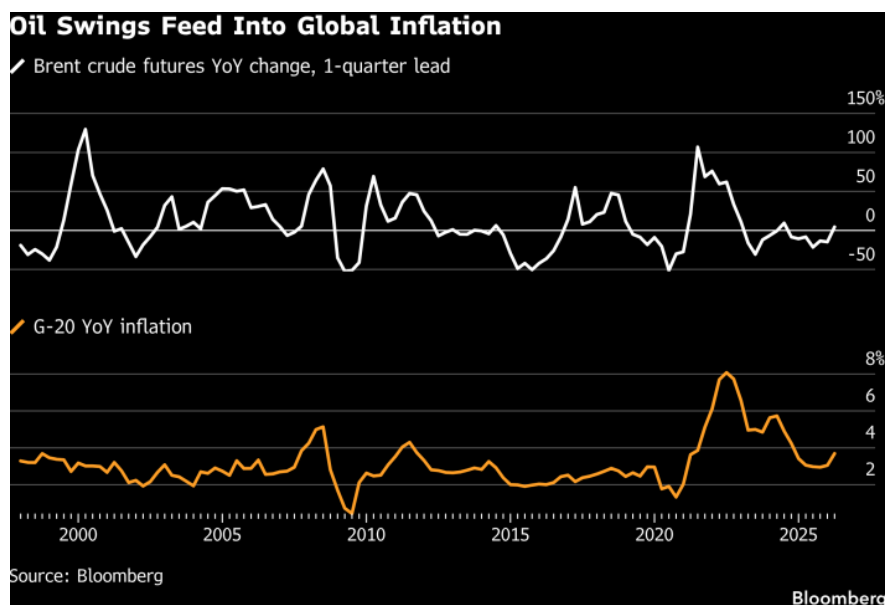
As per [The Economist](#), the US economy has consistently outperformed expectations this year. Late last year, economists forecast annualized growth of just 1.6% to 1.9% per quarter. However, GDP expanded by 2.5% in the first quarter and 2.2% in the second, driven by resilient consumer spending and growing investment in AI-related infrastructure. If the Atlanta Fed's nowcast proves accurate, third-quarter growth could come in at an even stronger rate of 3.7%.

1.2. Soaring Inflation

The US-Iran war had spillover effects across the global economy. Oil prices surged as disruptions to energy flows through the Strait of Hormuz raised supply concerns. Higher energy costs then fed into the prices of goods and services worldwide, while supply chains also faced disruptions.

In addition, Trump's trade war and the retaliatory tariffs imposed by trading partners increased the cost of imports, adding to inflationary pressures.

Consequently, investors demanded higher yields to buy bonds to make up for the decline in the purchasing power.



1.3. Tighter Monetary Policy Expectations

The combination of persistent inflation and a stronger-than-expected economy has led investors to reassess the outlook for US monetary policy. Market expectations have changed dramatically since the war began. Investors had anticipated three Fed rate cuts by March 2027, but now expect interest rates to be 1.5% higher than previously forecast, at 4.25%-4.50%.

1.4. AI Borrowing

While major technology firms initially financed AI expansion through strong internal cashflows, mounting infrastructure costs are pushing the industry toward external borrowing. Bond issuance by hyperscalers reached \$230 billion this year, twice the amount raised in all of last year, as per [The Economist](#). Across the wider AI ecosystem, Goldman Sachs estimates that debt issuance approached \$500 billion by early August, with the US accounting for a large share of the total. The increase in corporate bond issuance has intensified competition for investor capital, forcing the US government to offer higher yields to maintain demand for its bonds.

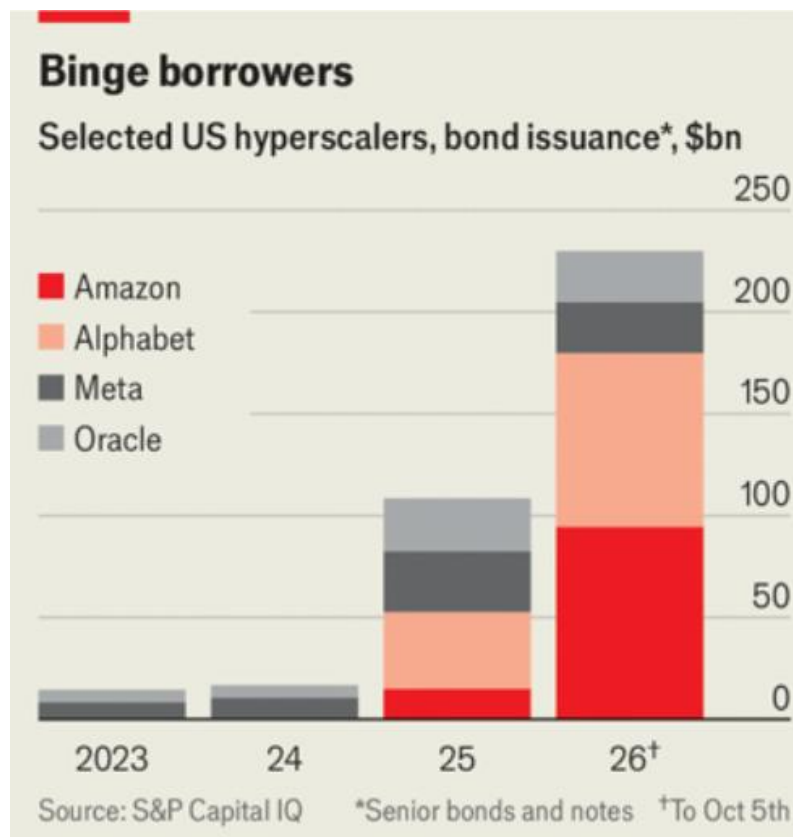
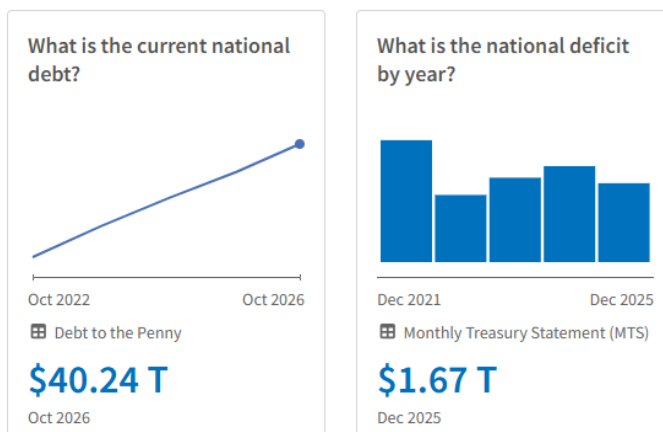


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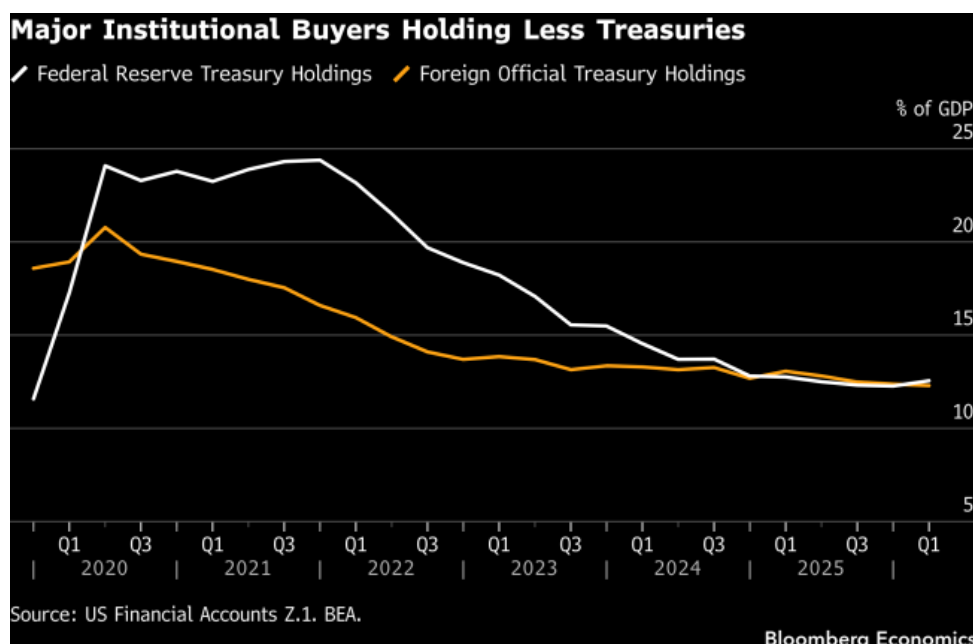
1.5. Fiscal Deficits and Rising Debt

As per the Department of the Treasury and the Bureau of the Fiscal Service's Fiscal Data website, US national debt reached a record **\$40.24 trillion in October 2026**. The increase reflects lower government revenues following tax cuts, alongside higher spending driven by rising energy costs and record military expenditures, which reached **\$1 trillion in fiscal year 2026**. As a result, the federal deficit widened, requiring additional borrowing.



1.6. Foreign Selling of US Treasuries

As per [Bloomberg](#), many countries sold US Treasuries this year, such as Japan to support its currency, and China to decrease dependence on the US financial system as US-China tensions escalate. The Fed and sovereign wealth funds followed.



1.7. Technical and Market Factors

As per a report titled [*US government debt rout triggers 'vicious loop' of selling*](#) published by the *Financial Times*, as higher interest rates discourage mortgage refinancing and early repayments, mortgage-backed securities become effectively longer-dated. Consequently, hedge funds and real estate investment trusts, which hold large portfolios of mortgage-backed securities, then sell long-term Treasuries to rebalance their portfolios, reinforcing the rise in Treasury yields.

At the same time, bond yields globally have been rising from France to Japan to others and bonds losses can have a domino effect across financial markets as investors rush to reduce portfolio risk, unwind leveraged positions, and raise cash. This often triggers simultaneous selling across other bonds, as well as equities and other financial assets, amplifying market volatility.

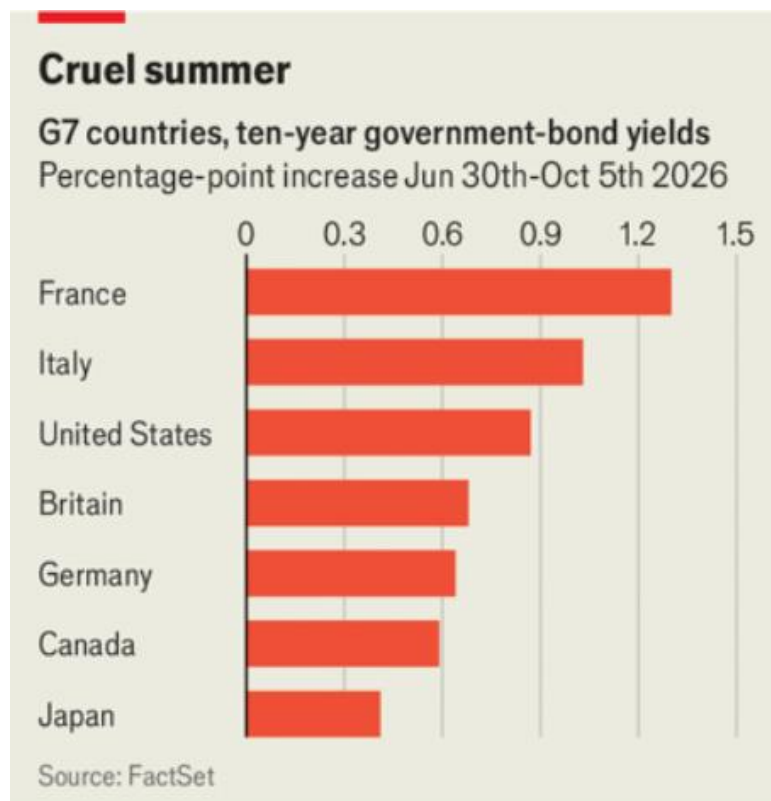


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2. Markets Reaction to Higher Yields

2.1. Stocks

In theory, rising bond yields tend to weigh on stocks as investors require higher returns to justify holding riskier assets over bonds. Higher yields also lower the present value of future corporate earnings, putting downward pressure on equity valuations. Furthermore, increased borrowing costs can squeeze corporate profit margins and slow business investment.

At the same time, as discussed in point number 1.7., bonds losses often triggers simultaneous selling across other financial classes such as equities.

But, expectations of continued growth driven by AI investments and that of a robust corporate earnings season have driven US equities toward record highs, outweighing concerns about higher inflation and rising bond yields.

2.2. Dollar Strengthening

The US Dollar Index (DXY), which measures the dollar against a basket of six major currencies, has risen by 4% since the start of 2026 to 102.233 points. The gain reflects not only dollar strength but also weakness among several major currencies, particularly the euro. A key factor behind the euro's decline has been growing concerns over France's fiscal outlook. French 10-year government bond yields have climbed from 3.5% to 4.9% this year amid growing concerns over the country's fiscal position and growing debt burden. With public debt nearing 120% of GDP, a budget deficit projected at 5.4% of GDP, and political uncertainty weighing on confidence, fears of a potential debt crisis have intensified. As investors reduce exposure to euro-denominated assets, many have shifted toward the dollar, supporting the DXY, while the euro has also weakened against currencies such as the pound and the yen.

In addition, the surge in energy prices following the US-Iran war boosted demand for the US dollar. Since oil is traded globally in dollars, higher oil prices require countries and companies to obtain more dollars to purchase the same amount of energy, providing additional support to the DXY.

Furthermore, persistently elevated inflation alongside a strong US economy has strengthened expectations of a tighter monetary policy stance. Higher interest rates make dollar-denominated assets more attractive to investors, providing additional support to the dollar.

However, concerns over AI-related spending and the US midterm elections in November could disrupt the dollar's rally.

3. Broader Implications of Rising Yields

3.1. Households and housing

Higher bond yields eventually translate into higher mortgage, auto loan, and other borrowing costs for households. As financing becomes more expensive, buyers can afford less for the same monthly payment, while homeowners with low fixed-rate mortgages become less willing to move. This tends to weigh on housing activity, construction, and consumer spending, hence the country's economy.

3.2. Private borrowers

Higher interest rates are also putting pressure on private borrowers. Defaults in private credit markets have risen sharply, according to [The Economist](#). Previous episodes such as the UK's 2022 pension fund crisis and the collapse of Silicon Valley Bank highlighted how rapidly rising yields can expose vulnerabilities across the financial system. If elevated yields persist, governments may ultimately be forced to raise taxes or reduce spending, as a return to the ultra-low interest rate environment of the 2010s appears increasingly unlikely. Such measures could slow economic activity.

4. Assessing US Debt Sustainability

Rising US Treasury yields risk creating a vicious cycle. As the cost of servicing US debt rises, the government needs to borrow more to cover larger interest expenses. The resulting increase in bond issuance boosts supply, which can push yields even higher and further increase borrowing costs.

In details, Goldman Sachs estimates that if current interest rates persist, they could reduce US economic growth by more than half a percentage point in 2027. Slower growth would make rising debt burdens harder to contain, while concerns over fiscal sustainability could prompt investors to demand higher yields, further increasing governments' financing costs.

Fortunately, as a report by *The Economist* titled [The countries most threatened by turbulent bond markets](#) shows, high debt can be manageable when an economy is growing rapidly, as debt becomes smaller relative to national income and tax revenues. However, when borrowing costs exceed economic growth, debt levels tend to rise relative to GDP unless governments increase taxes or reduce spending. The US is in a stronger position than many advanced economies thanks to solid growth and the potential productivity gains from AI investment, while countries such as France and Italy face weaker growth and higher borrowing costs.

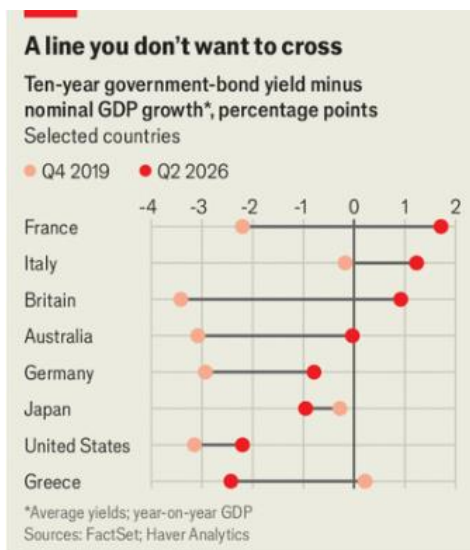


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The Economist remained cautious, publishing another article titled [Will bonds blow up?](#), where it said “America is learning that its AI-fuelled expansion will not much help it cope with its debts, because interest costs rise in tandem with growth. The federal government’s annual budget deficit of about 6% of GDP is unsustainable. Fortunately, Uncle Sam still has the immense advantage of issuing the world’s reserve currency. As bond yields have risen in recent weeks the dollar has soared in value. A fiscal reckoning must eventually come—but not yet.”

We agree with this assessment and believe the risk of a US sovereign default remains low in the short to medium term. Instead, policymakers are more likely to rely on debt-management measures to ease financing pressures, such as increasing buybacks of shorter-dated securities while extending the maturity of new issuance. Debt monetisation (creating new money to purchase government debt) remains a potential alternative, though we do not expect such measures to be considered until inflation is brought under control.

The asset management company Franklin Templeton offers a different perspective. In its article [The Reserve Manager Radar: What to Watch as Markets Enter the Final Quarter of 2026](#). The firm argues that rising fiscal pressures may not be reflected solely through higher Treasury yields. Instead, part of the adjustment could occur through a weaker dollar, as investors reduce exposure to dollar-denominated assets. A weaker dollar would make US assets more attractive to foreign investors, easing some of the upward pressure on bond yields.

Franklin Templeton remains unconvinced that current fiscal and debt trends are sufficient to undermine the dollar's long-term status as the world's leading reserve currency. The firm argues that the depth of US capital markets, the dollar's dominant role in global trade and finance, and the lack of a credible alternative currency continue to provide strong support. While reserve managers may gradually diversify their holdings, this does not necessarily imply a significant erosion of the dollar's reserve currency status.

We broadly agree with this view. While some countries may gradually reduce their reliance on the dollar, we do not expect it to lose its position as the world's leading reserve currency anytime soon. Besides, the 2008 financial crisis is a good example: even though the crisis started in the United States, investors still rushed into the dollar as a safe-haven asset. We therefore expect any decline in the dollar's reserve currency role to be slow and gradual rather than a rapid shift toward another currency.

Conclusion

In conclusion, while bond yields have risen globally to multi decade highs, not all yield increases are driven by the same factors. Yields can rise because growth is strong and investors expect higher profits and productivity, or because investors demand greater compensation for inflation, fiscal risks, and rising government borrowing. France falls under the second category, while the US reflects elements of both.

AI investment, resilient economic growth, and continued fiscal spending have supported higher yields from a growth perspective. At the same time, rising debt levels, persistent inflation concerns, and substantial Treasury financing needs have increased the compensation investors demand for holding long-term bonds.

Looking ahead, attention is turning to the November US midterm elections and their potential impact on fiscal policy. A divided government could make large spending packages harder to pass and reduce the scope for additional deficit-financed initiatives. However, such an outcome would do little to reduce the existing debt burden or the Treasury's substantial borrowing needs. With bond giant Pimco warning that “US benchmark borrowing costs risk hitting 6 per cent for the first time in 26 years”, as per the [Financial Times](#), bond markets are likely to remain a key driver of global financial conditions.

Ultimately, the path of Treasury yields will depend on which force proves stronger: economic growth and productivity gains, particularly from AI investment, or the rising cost of financing an ever-growing stock of debt.

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