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Research

The Home Straight....

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Deutsche Bank Research Institute

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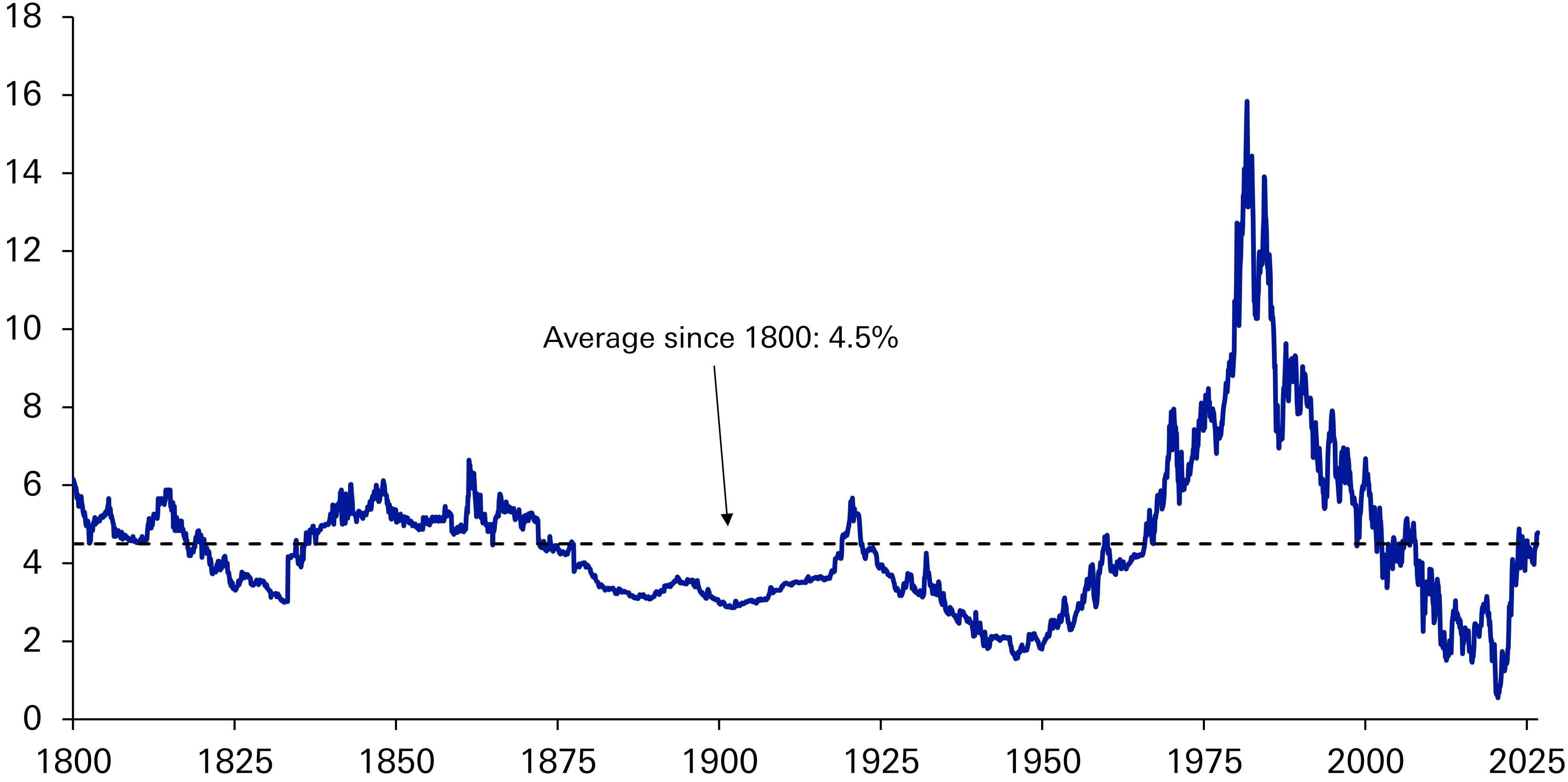
The bond sell-off in perspective…

We would see the recent rise in yields as a continuation of a long normalisation process. 10yr US Treasury yields are now “only” slightly above their long-term average yield since 1800... so they are certainly not extreme....

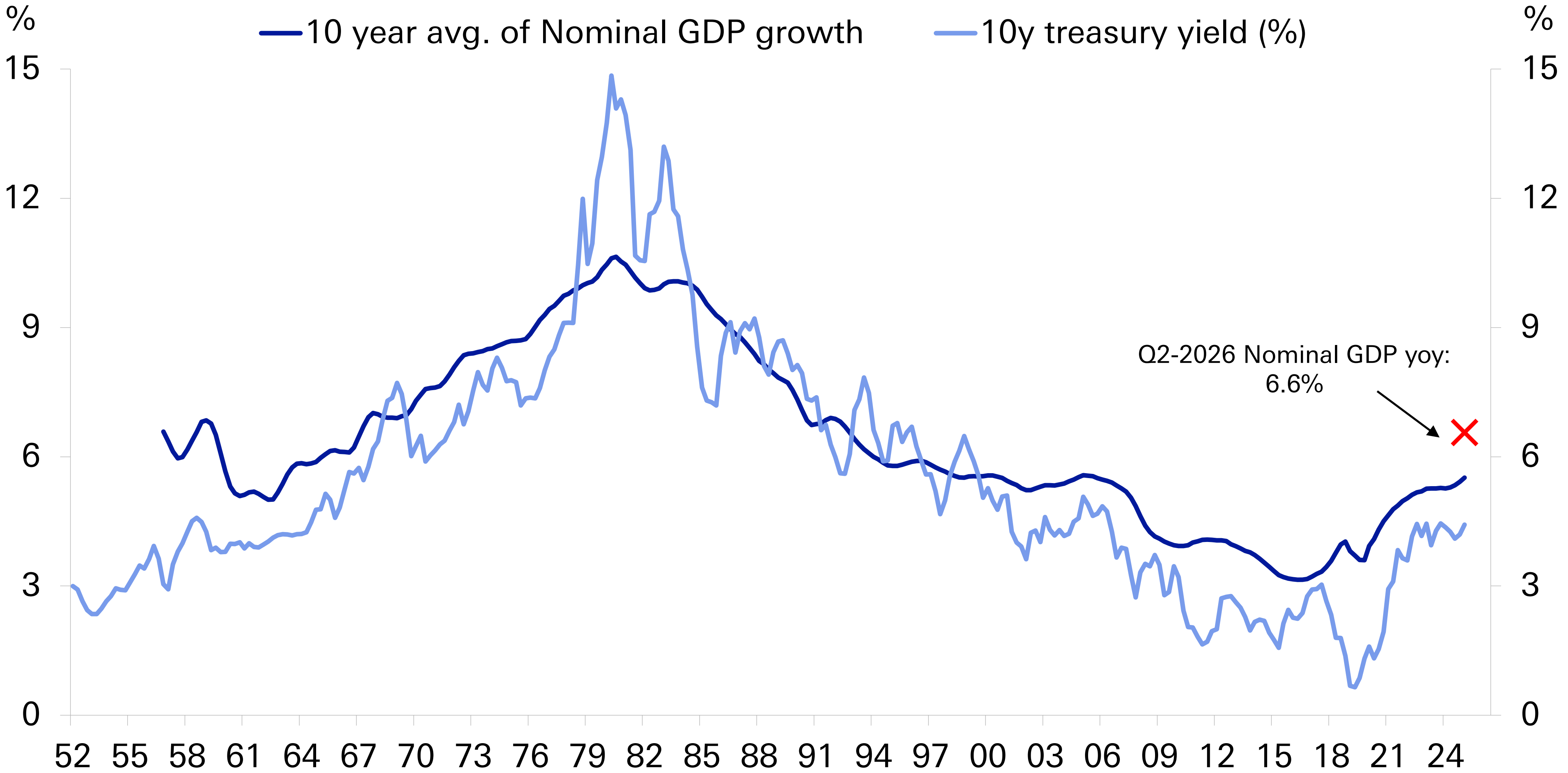
10-year US treasury yields



Source: Finaeon, Deutsche Bank

Since the early 1960s, 10 yr UST yields have typically tracked Nominal GDP apart from late 70s/early 80s when they soared above and in the 2010s when they were significantly below. The average gap over this period is around 70bps (NGDP>10yr USTs). 10yr average NGDP is c.5.5% so 4.8% seems broadly fair. However current NGDP is 6.6%. Do we need to factor this in?

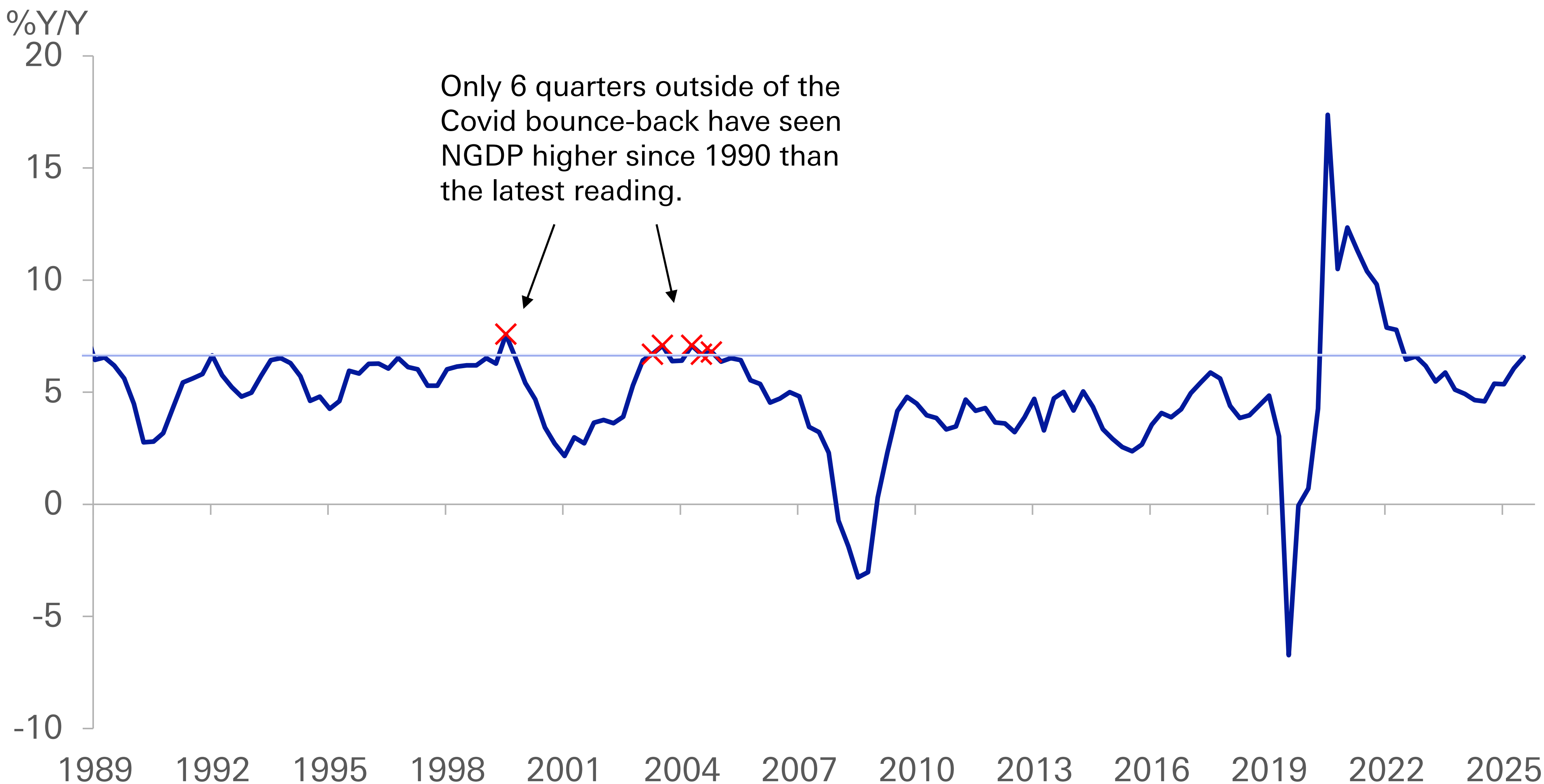
10yr average nominal GDP growth and the 10yr Treasury yield



Source: BEA, FRB, Haver, Deutsche Bank

At 6.6%, current YoY US Nominal GDP is at the highest YoY rate since 2005 outside of the Covid bounce-back period. So even if not sustainable at these levels, this level of nominal growth has helped push UST yields higher....

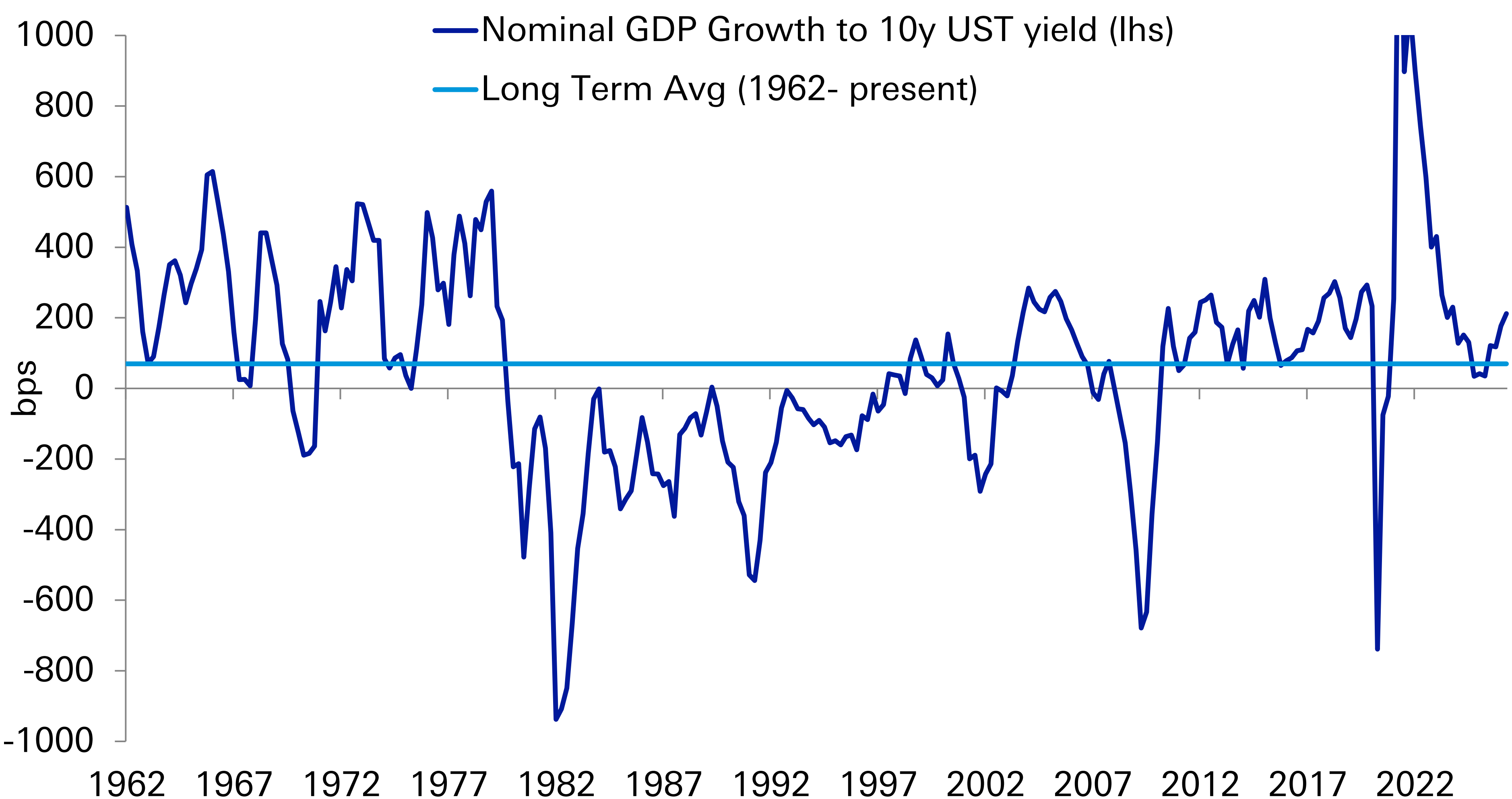
US Nominal GDP growth with red crosses being the only time nominal GDP was higher than the current 6.6% outside of the post COVID rebound



Source : BEA, Haver, Deutsche Bank

With spot Nominal GDP at 6.6% YoY, the current gap to 10yr yields is around 180bps. Clearly nominal GDP may be inflated by energy prices but overall it's hard to say US yields are too high based on this. If nominal GDP settles at 5.5% then 4.8% would be historically average. If we settle at 6% due to AI and inflation, then around 5.3% is reasonable before factoring in fiscal concerns.

US Nominal GDP minus 10yr UST yields



Source: Haver, Bloomberg Finance LP, Deutsche Bank

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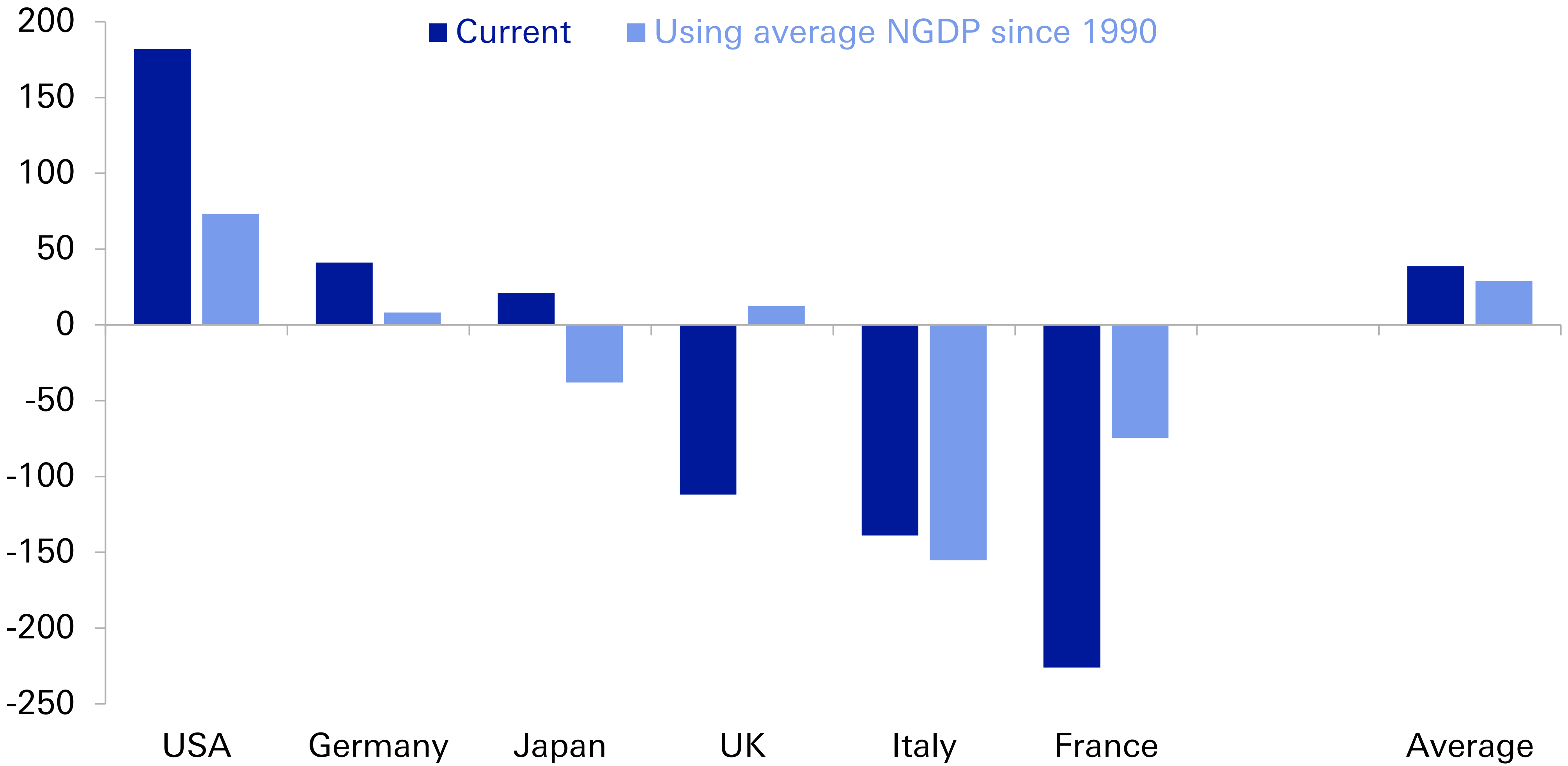
The US has the largest positive gap between current Nominal GDP and 10yr yields illustrating that growth is currently comfortably above funding costs. France, Italy and the UK are the most negative and have yields comfortably above current nominal growth.

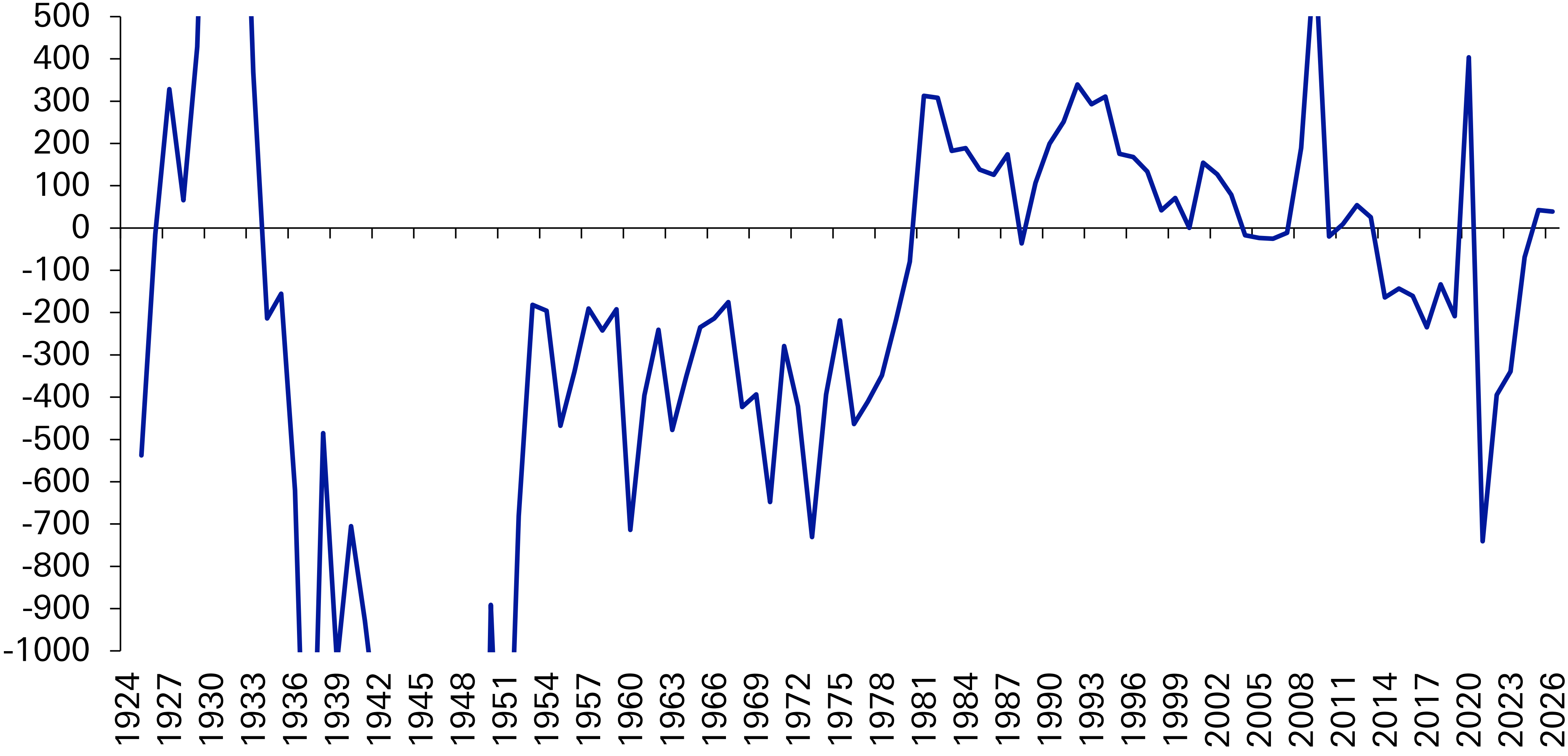
Gap between Nominal GDP growth and 10y yields (bps)



Source: Finaeon, Deutsche Bank

Across DMs, funding costs are now above nominal GDP on average. In the post GFC period of high debt and financial repression, yields were consistently below nominal GDP thus helping the funding situation….

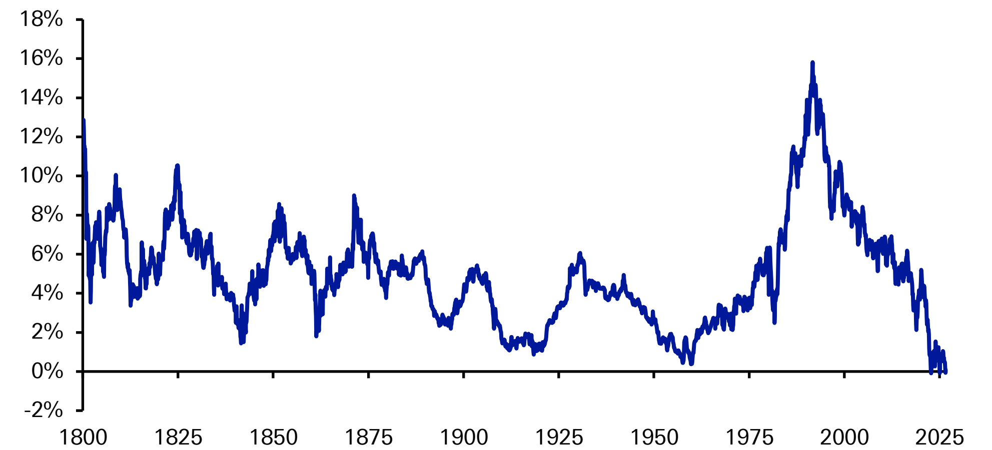
Average difference between Nominal GDP and 10yr Govt. bonds for US, UK, Germany, France, Italy and Japan (in bps)



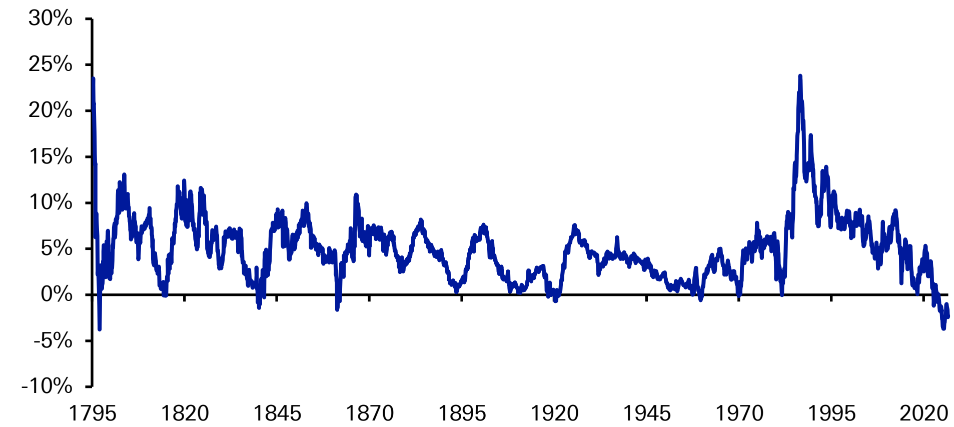
Source: Finaeon, Deutsche Bank

For 10yr Treasury yields, we are still hovering around the worst 5- and 10-year rolling nominal returns on record but it's clear that even with yields again approaching multi-year highs, returns have been stabilising more recently due to the higher coupons…

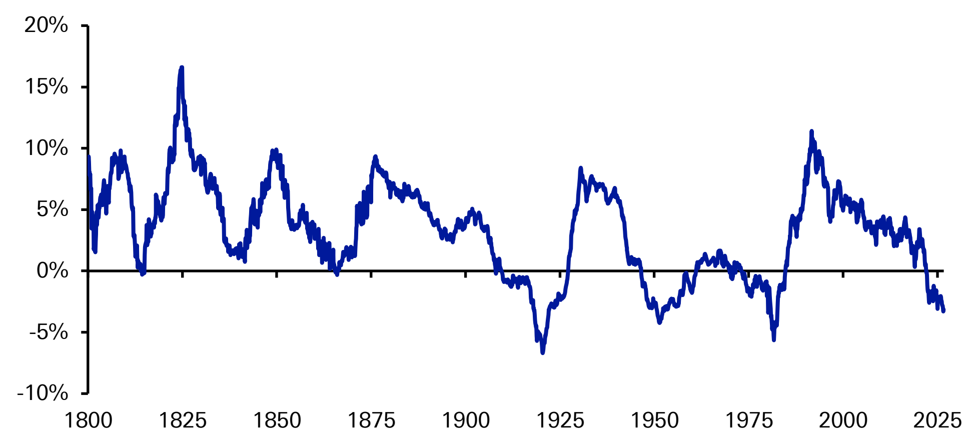
10yr Rolling Nominal Return (Annualised)



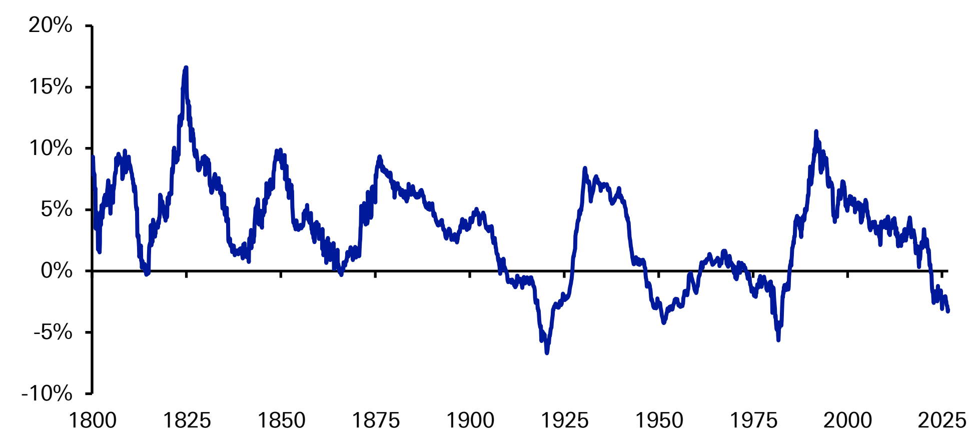
5yr Rolling Nominal Return (Annualised)



10yr Rolling Real Return (Annualised)



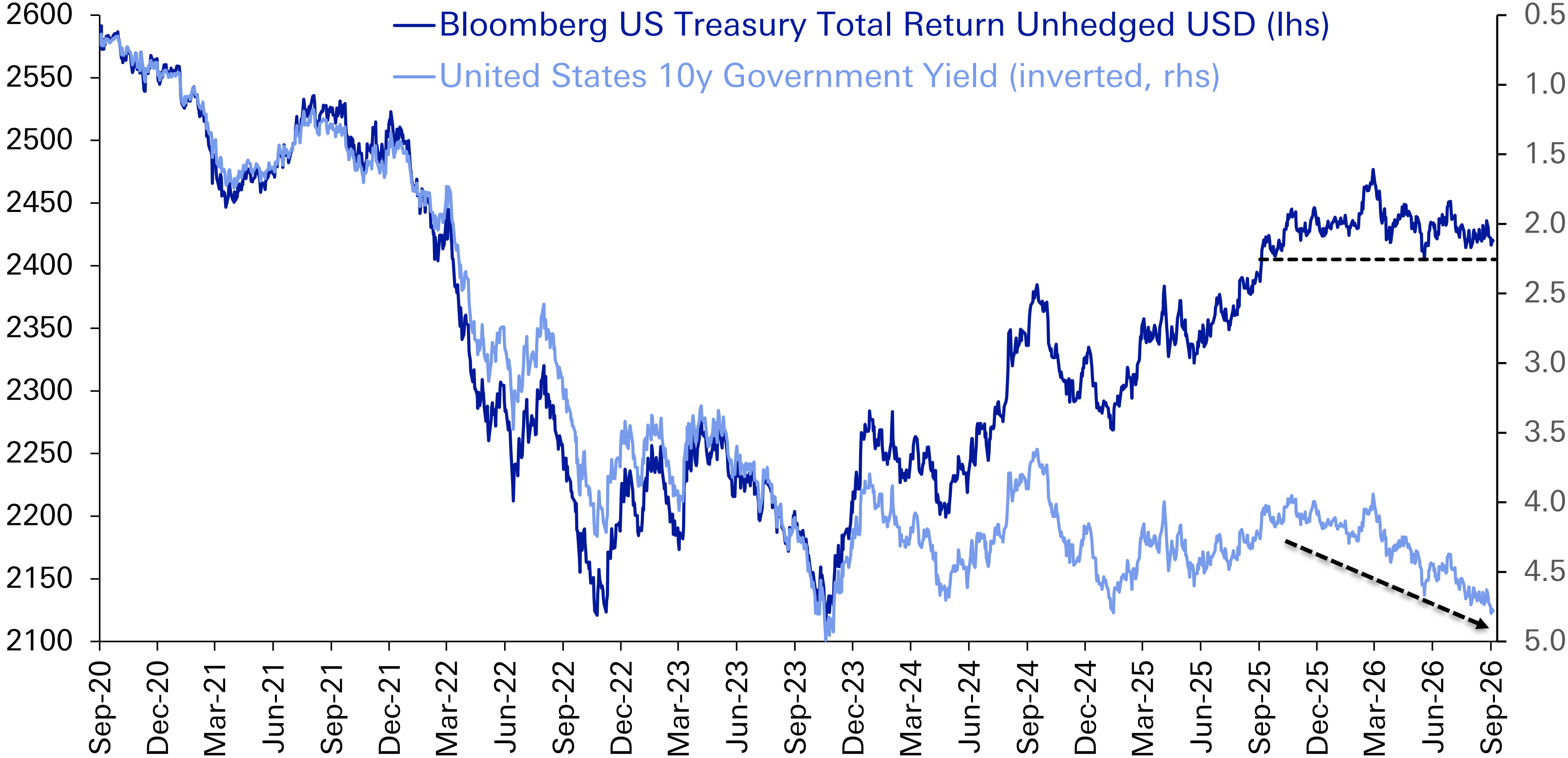
5yr Rolling Real Return (Annualised)



Source: Finaeon, Deutsche Bank

At least we're getting a decent compensatory yield now versus the 2010s and early 2020s. Over the last 12 months the US treasury total return index is higher even with a c.60bp rise in 10yr yields.. Since yields peaked in October 2023, the index has returned nearly 15%

US Treasury Index Returns vs. 10y Govt. Yields. Over the last year returns have been positive even with a notable rise in yields.

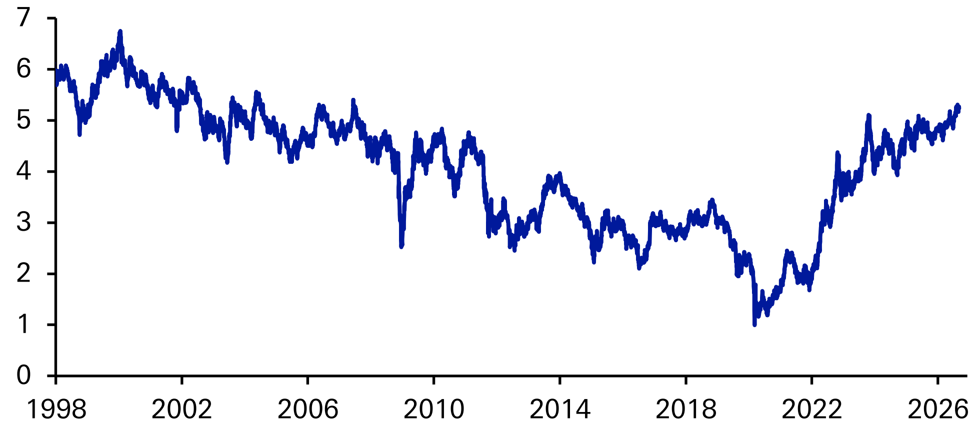


Source : Bloomberg Finance LP, Deutsche Bank, Last update: Sep 7

Clearly it's a global phenomenon. For example, 30-year yields are hitting decade plus or multi decade highs in several countries.

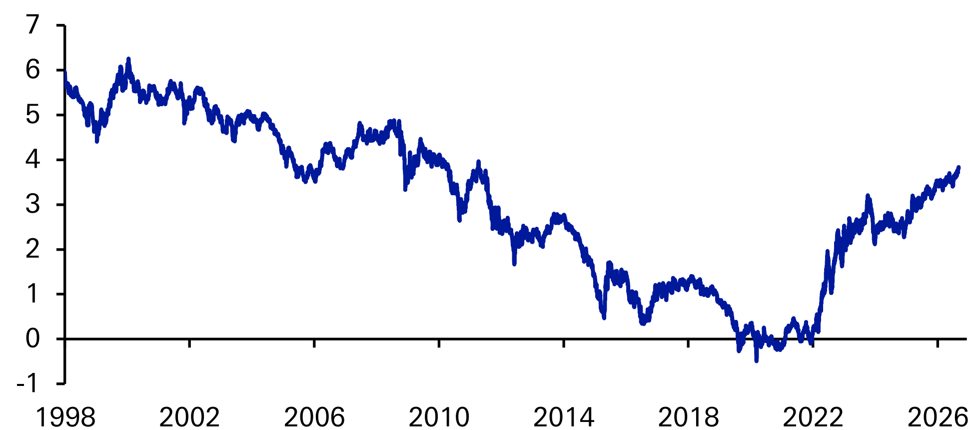
30yr Gilt Yields (%)

30yr Treasury Yields (%)



30yr JGB Yields

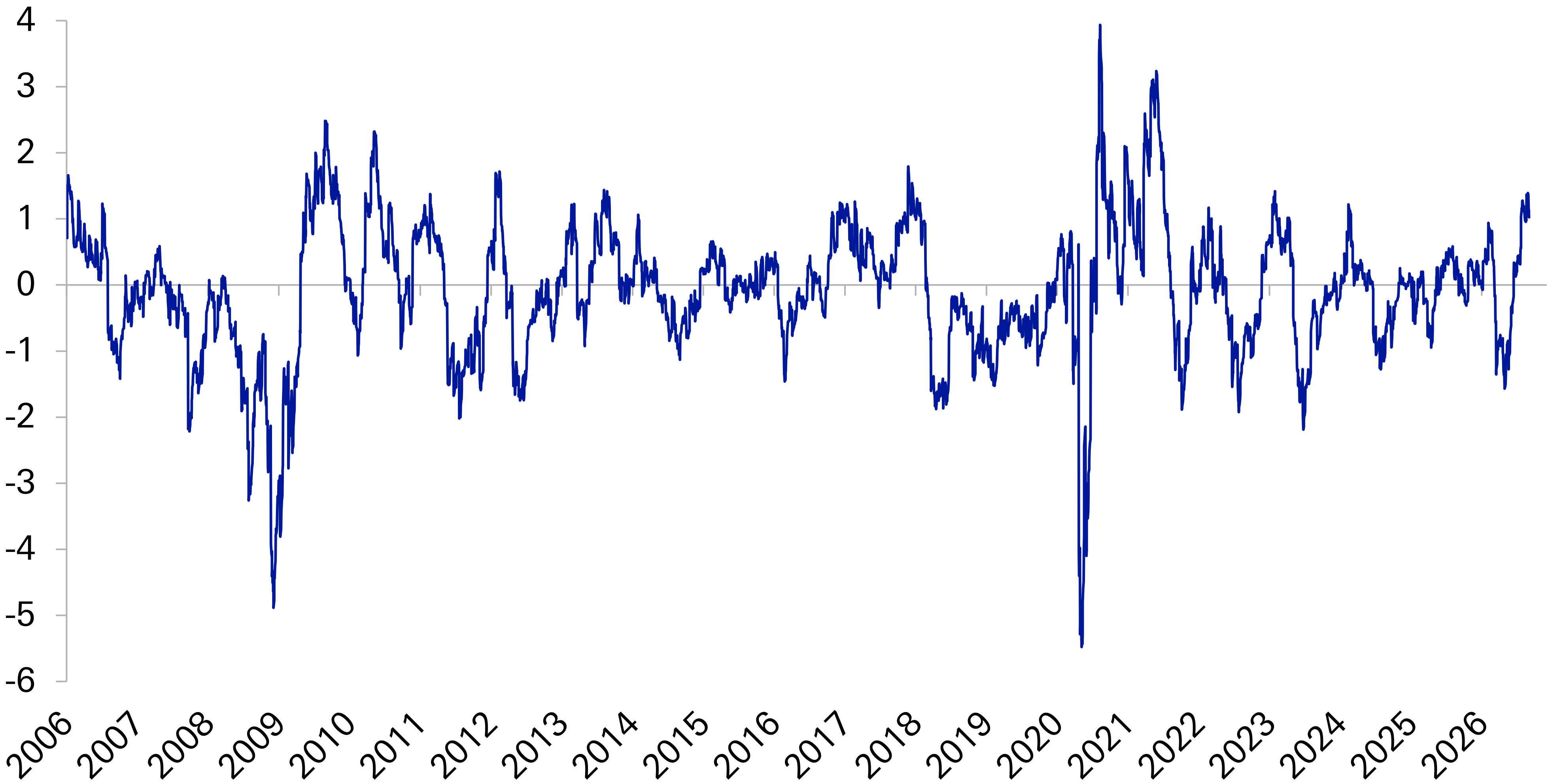
30yr German Yields (%)



Source: Bloomberg Finance LP, Deutsche Bank, Last update Sep 7

But some of this is justified by the data. For example, European growth surprises are nudging up against 20-year highs outside of the post Covid and GFC bounce-backs.

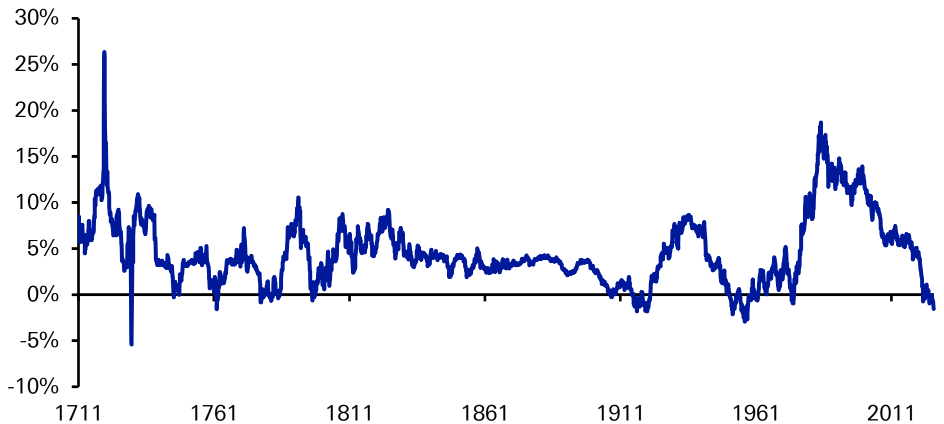
Deutsche Bank SIREN Surprise Index - Euroarea



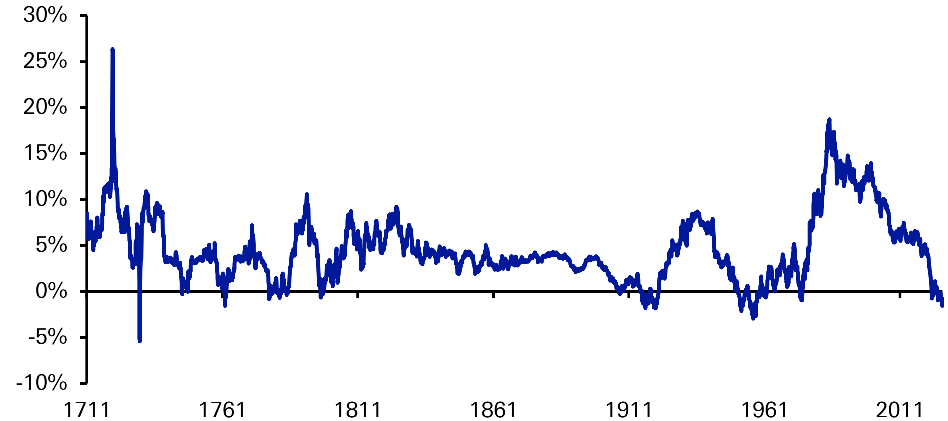
Source: Bloomberg Finance LP, Deutsche Bank; Last update : Sep 7

10yr UK gilts have also had a tough time in recent years. Rolling 5 and 10yr total returns are still near the lows..

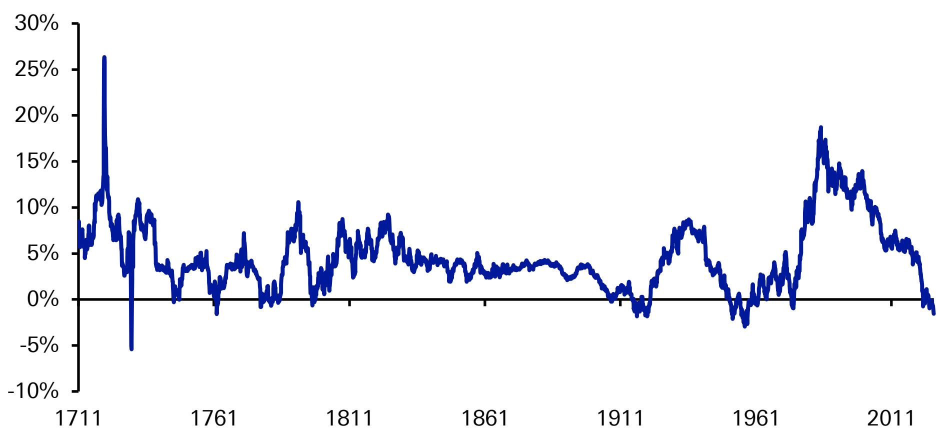
10yr Rolling Nominal Return (Annualised)



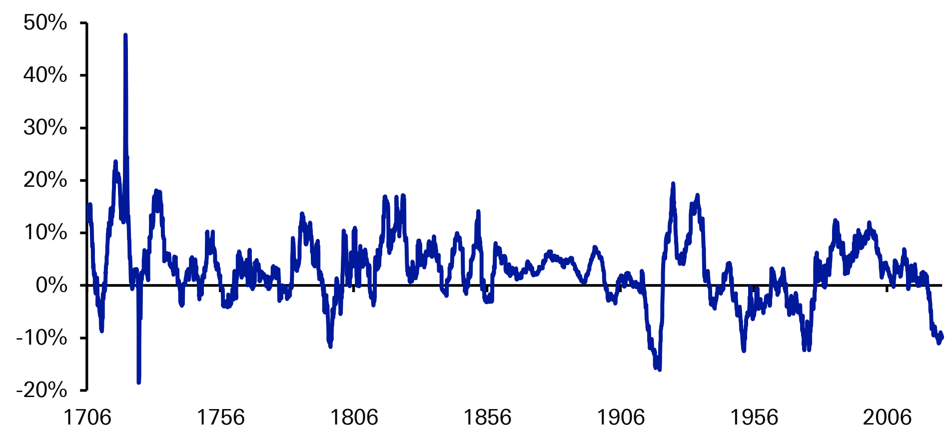
5yr Rolling Nominal Return (Annualised)



10yr Rolling Real Return (Annualised)



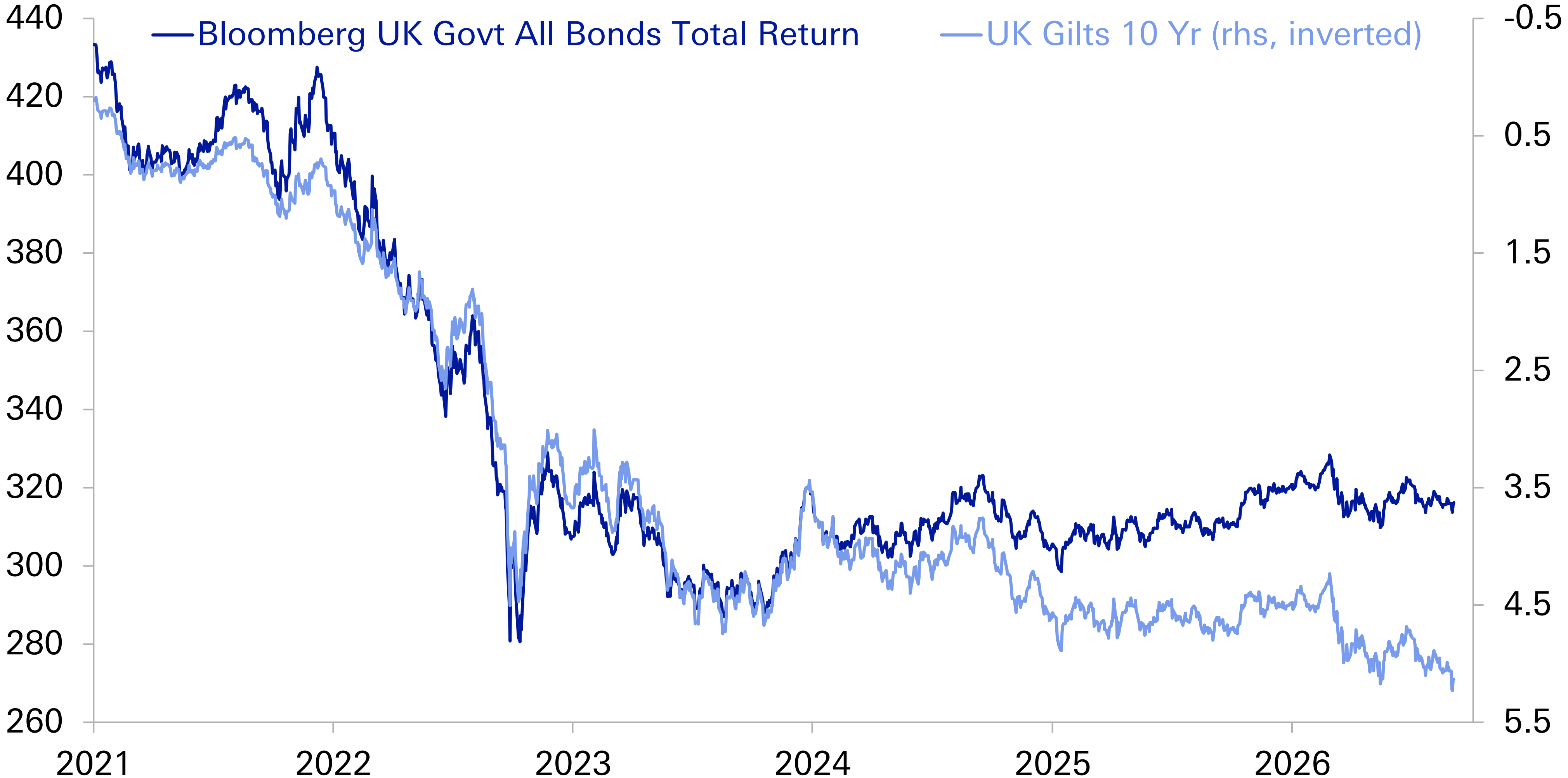
5yr Rolling Real Return (Annualised)



Source: Finaeon, Deutsche Bank

But even with all the negative headlines in the four years since the Truss mini-budget/LDI crisis, Gilt returns have generally crept higher even as yields have returned back to the highs. 10yr yields are currently around 65bps higher than their "crisis" peak in October 2022, yet the total return index is around 12% higher..

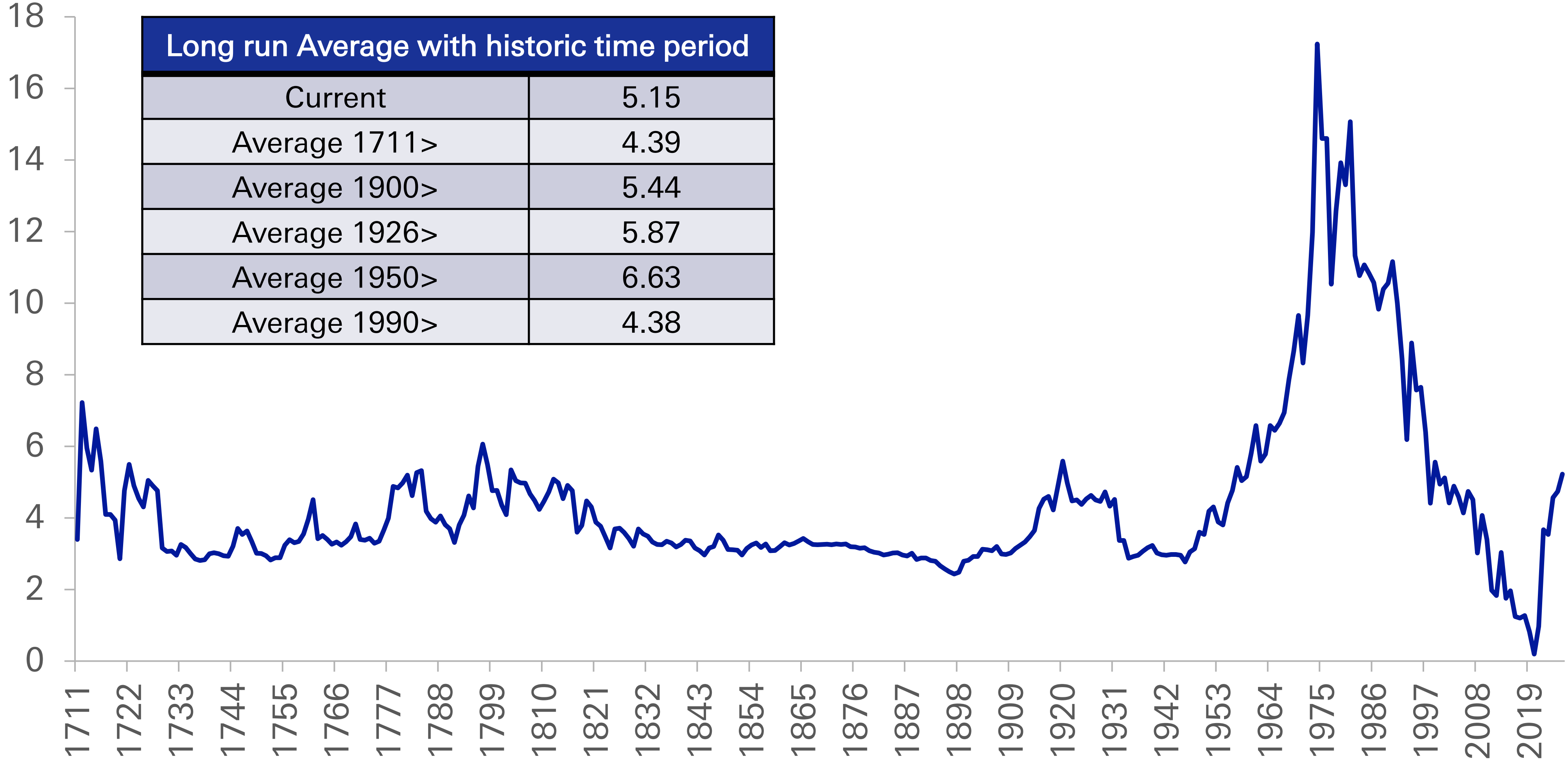
UK Gilt Index Returns vs. 10y Govt. Yields.



Source : Bloomberg Finance LP, Deutsche Bank, last update Sep 7

What average yield should you use in the UK? Over the long-run (since 1711- and since 1900-) the median is around one percentage point less than the average which is heavily influenced by 1960-1997 where 10yr yields were permanently above 5.5%. Outside of that period the current yield is at the top end of the historical range.

10yr govt yields in UK

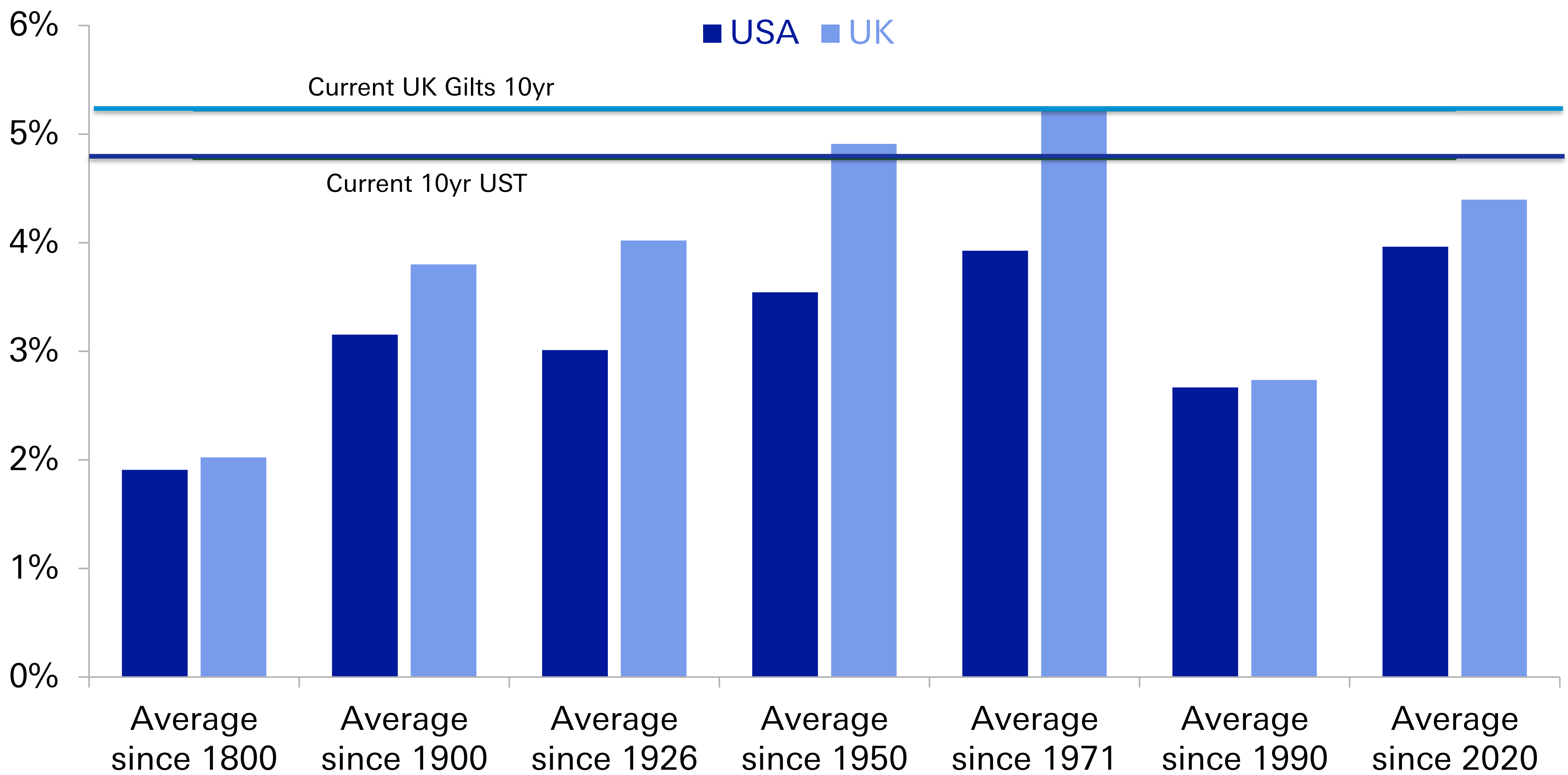


Long run Average with historic time period	
Current	5.15
Average 1711>	4.39
Average 1900>	5.44
Average 1926>	5.87
Average 1950>	6.63
Average 1990>	4.38

Source: Finaeon, Deutsche Bank

At least US and UK Bond yields are mostly above average inflation seen over virtually all extended periods through history...

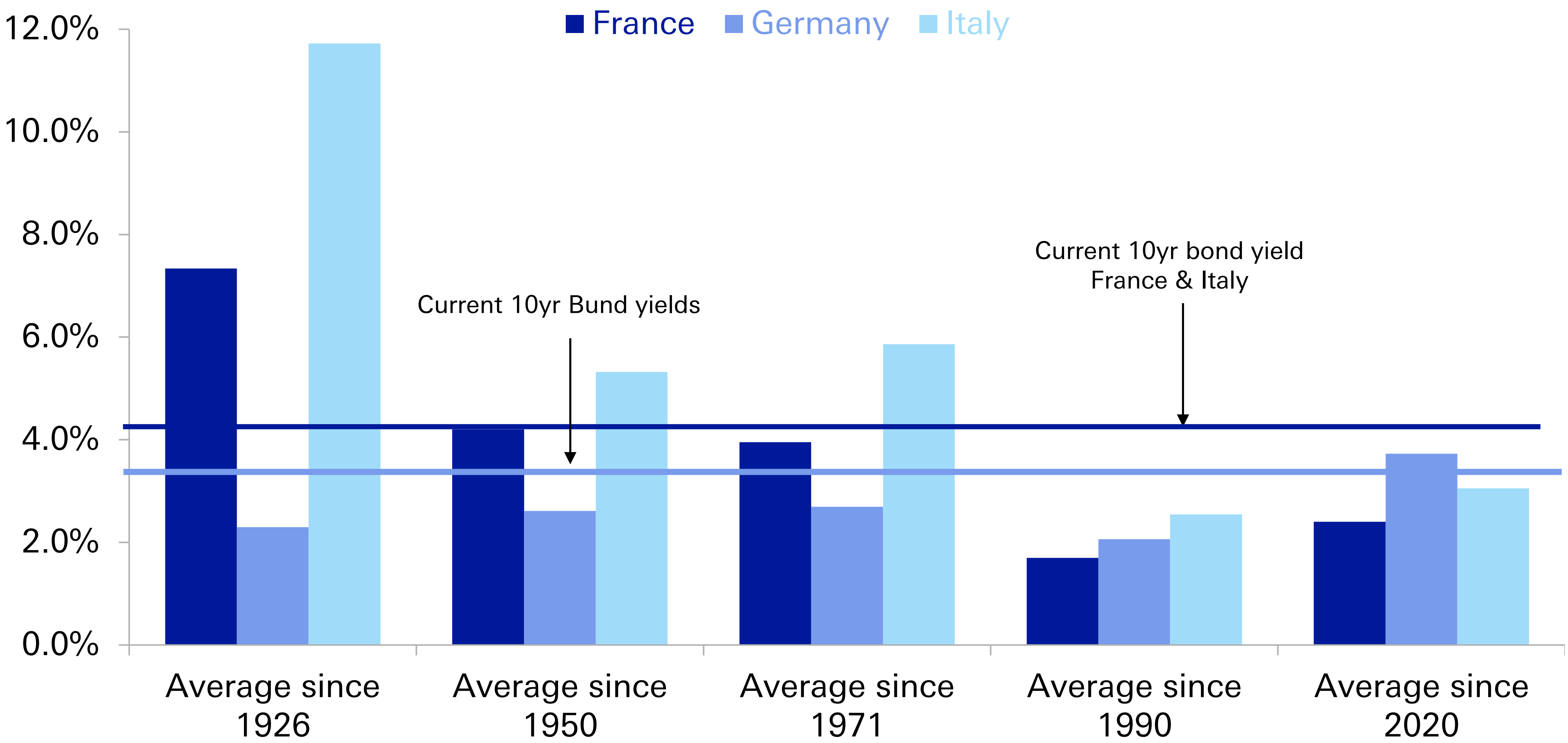
Average inflation over various periods in the US and UK and the current 10 year bond yield



Source: Finaeon, Deutsche Bank

WWII makes this more complicated for European countries, as do lower current yields.

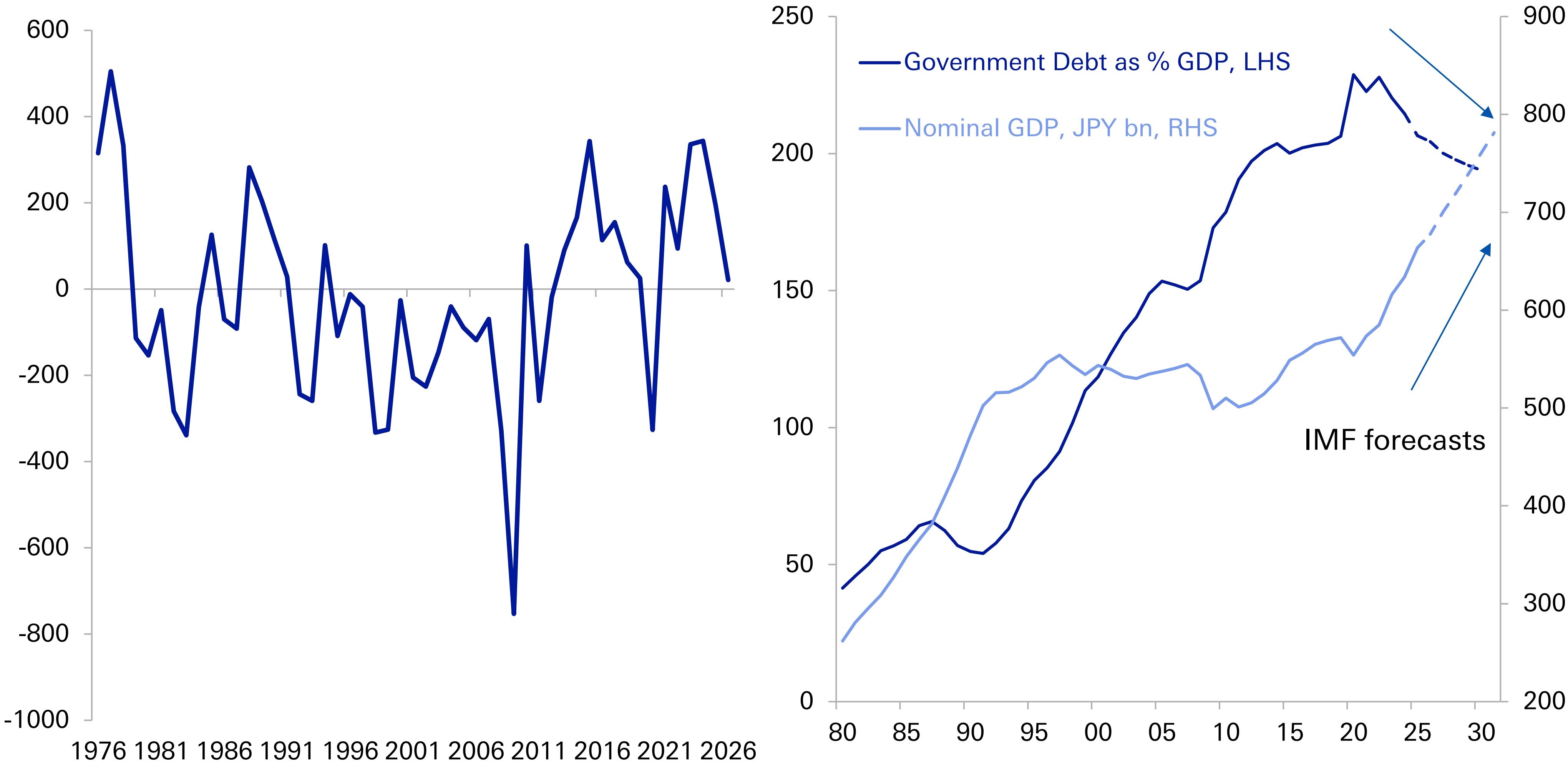
Average inflation over various periods in the France, Germany and Italy and the current 10-year bond yield



Source: Finaeon, Deutsche Bank

For Japan, rising yields and dipping nominal GDP do threaten what has been a falling debt/GDP since Covid when nominal GDP took off after being broadly flat for a couple of decades. Since 2021, Japanese nominal GDP has averaged over 220bps more than 10yr JGB yields. Today that stands at only around 40bps on a spot basis.

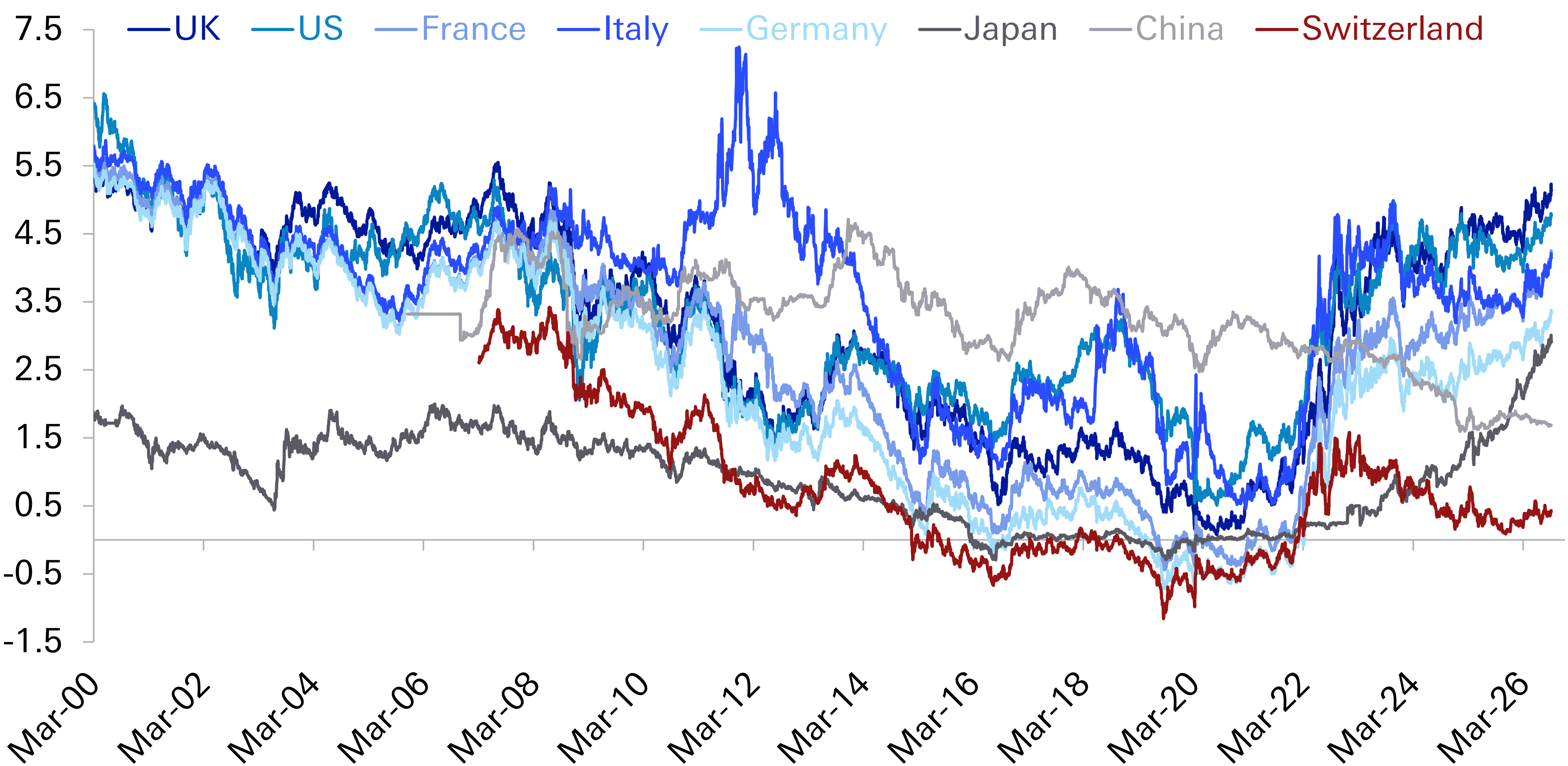
Japan: nominal GDP growth & 10yr JGB spread (left) & nominal GDP vs Govt debt (right)



Source: Finaeon , Deutsche Bank Research, Haver Analytics, IMF

Interestingly, while most global yields hit multi-decade highs, Swiss and China yields have been flat or moving lower...

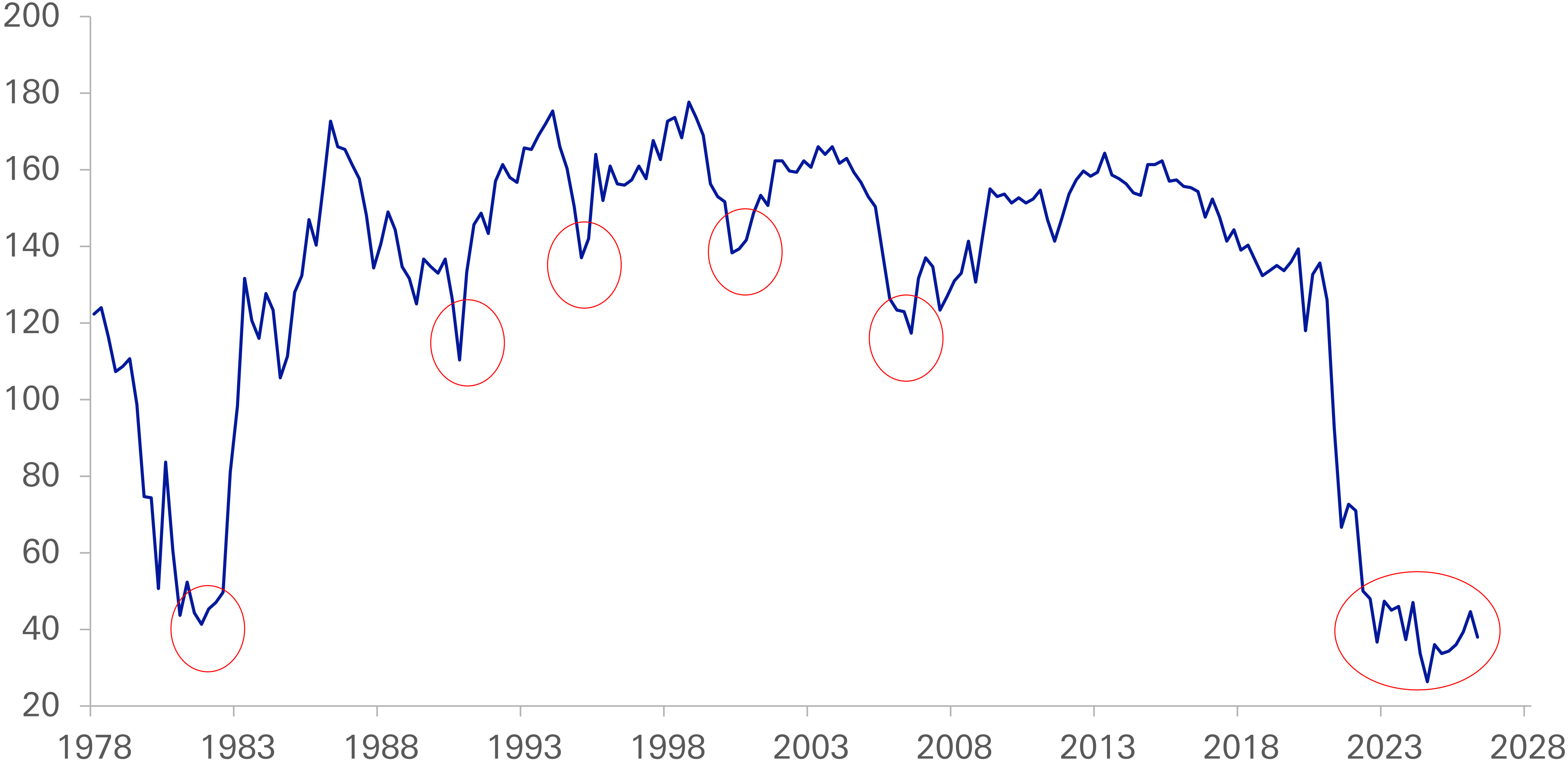
10y Government yields across major economies (%)



Source : Bloomberg Finance LP, Deutsche Bank, last update Sep 7, Note: Countries are ordered by current yield from high to low

Rising yields make the fiscal arithmetic more challenging but also continue to keep US housing affordability near record lows... Full employment and a lack of activity are the main thing holding prices up

UMICH: Current Conditions for Buying Houses (Index Score): sentiments hit rock bottom for buyers

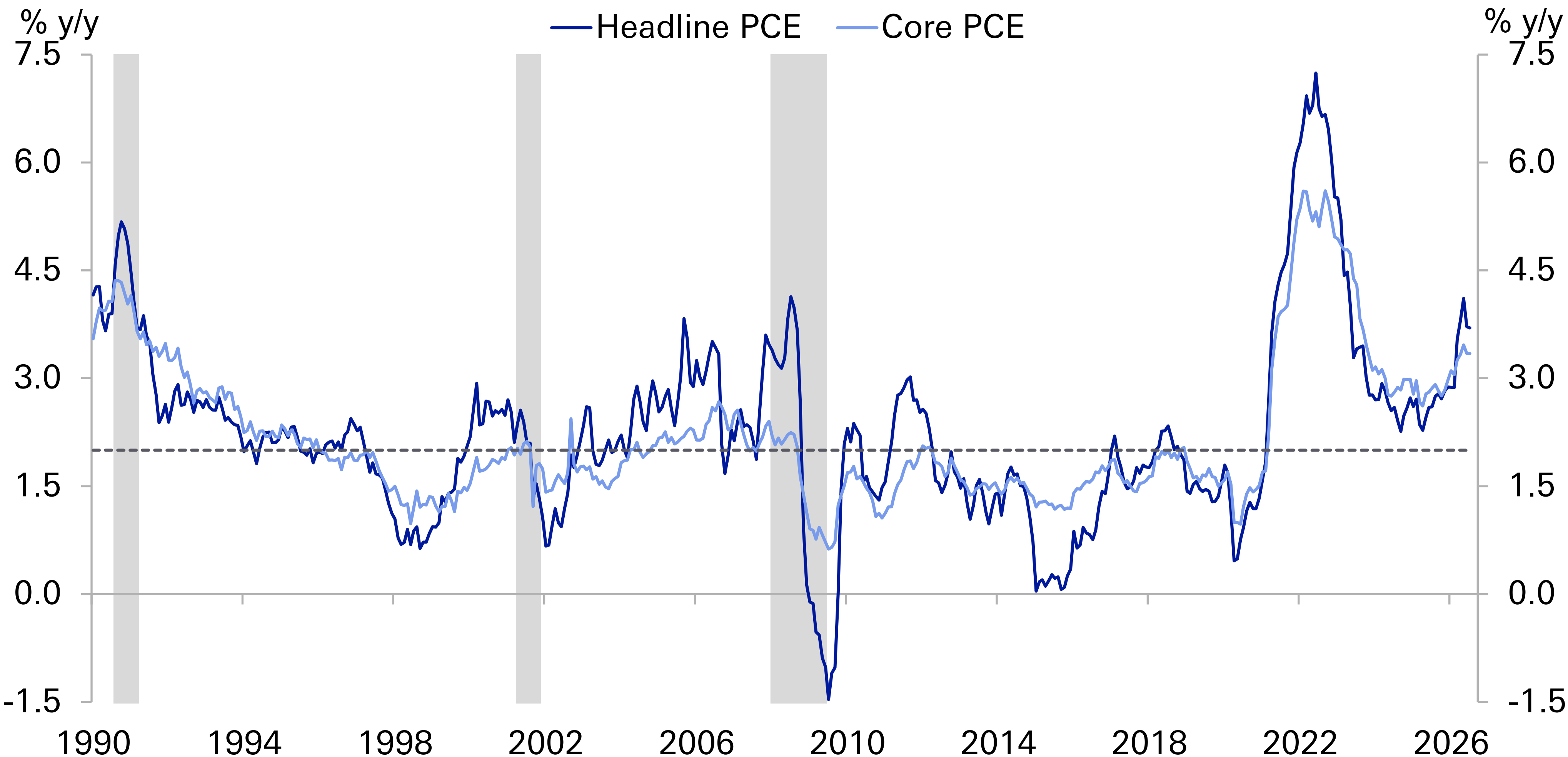


Source: UMICH, Haver, Deutsche Bank

Should the Fed raise rates...?

PCE inflation remains elevated far above the Fed's 2% target. Excluding the pandemic anomaly, core PCE is only 15bps off its 34-year high seen in May

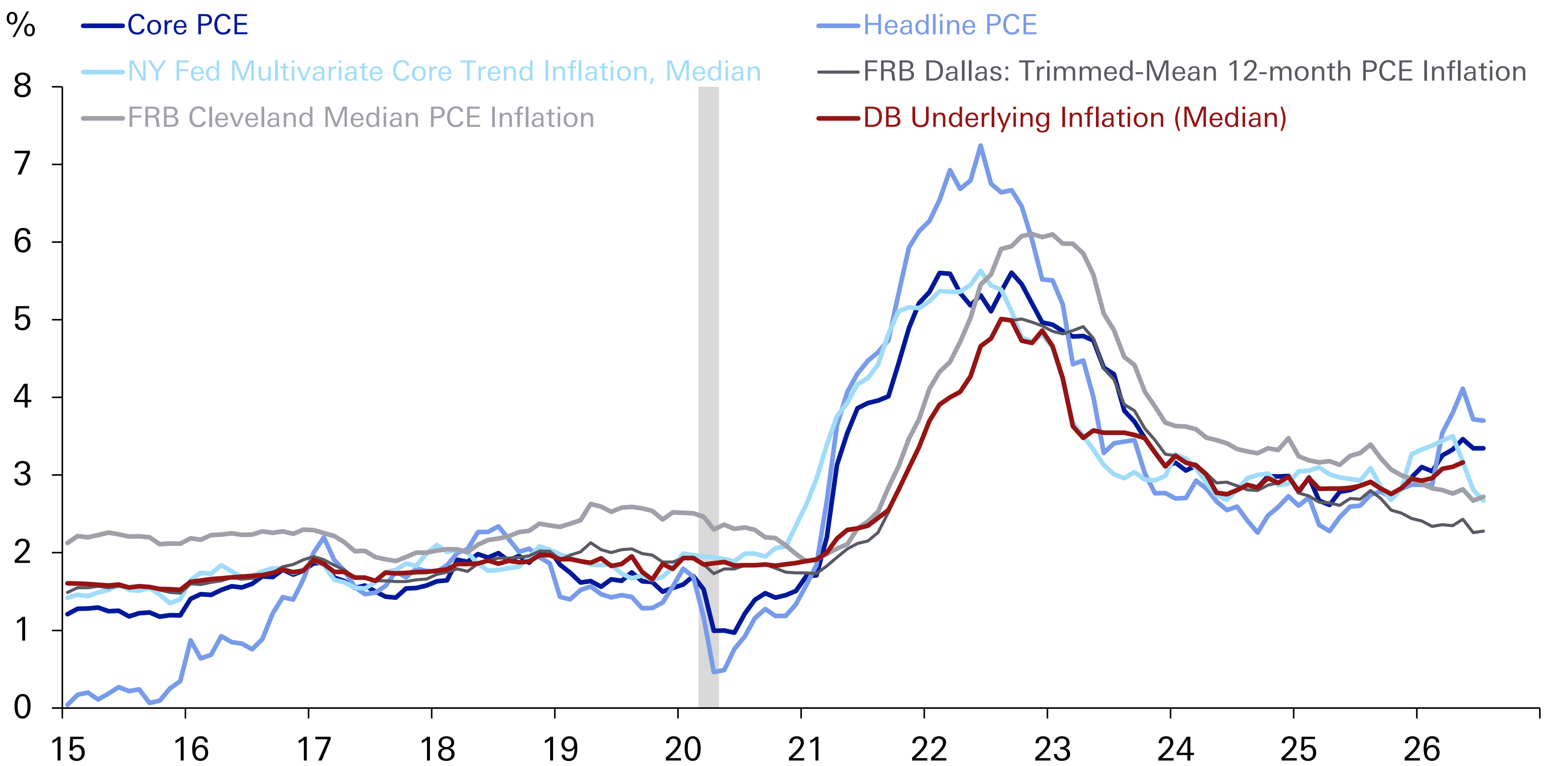
US PCE inflation



Source: BEA, Haver Analytics, Deutsche Bank

On most measures, trend inflation seems to be sticky at around 3%....

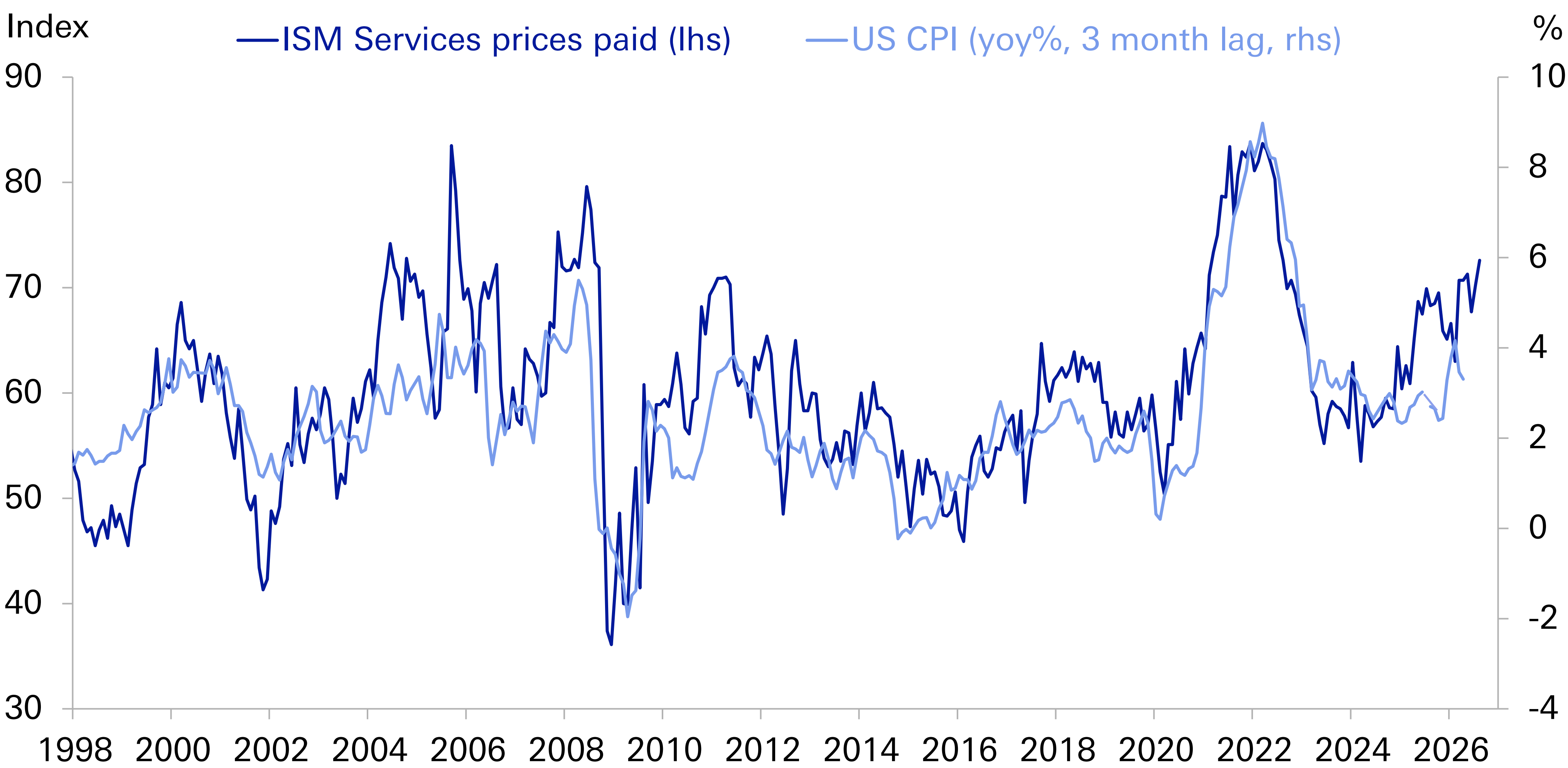
Alternative measures of trend PCE inflation



Source: BEA, FRB NY, FRB Dallas, FRB Cleveland, Haver, Deutsche Bank

Meanwhile, the ISM services prices paid component has been tightly correlated to inflation with a 3-month lag in the past… it's at a 4-year high and was consistent with CPI above 5% in the last inflation wave… While the correlation shouldn't be taken too literally, it highlights that price pressures remain in the pipeline…

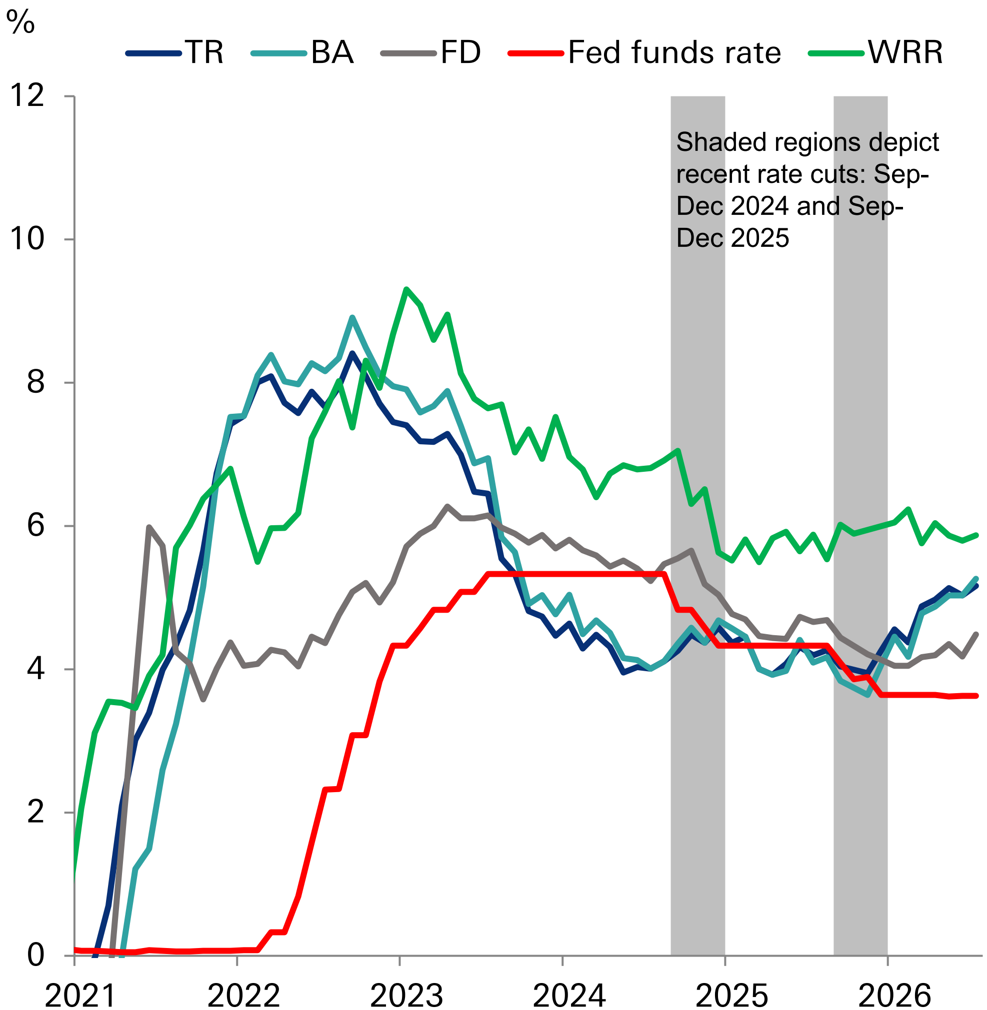
US CPI Inflation and ISM Services Prices Paid



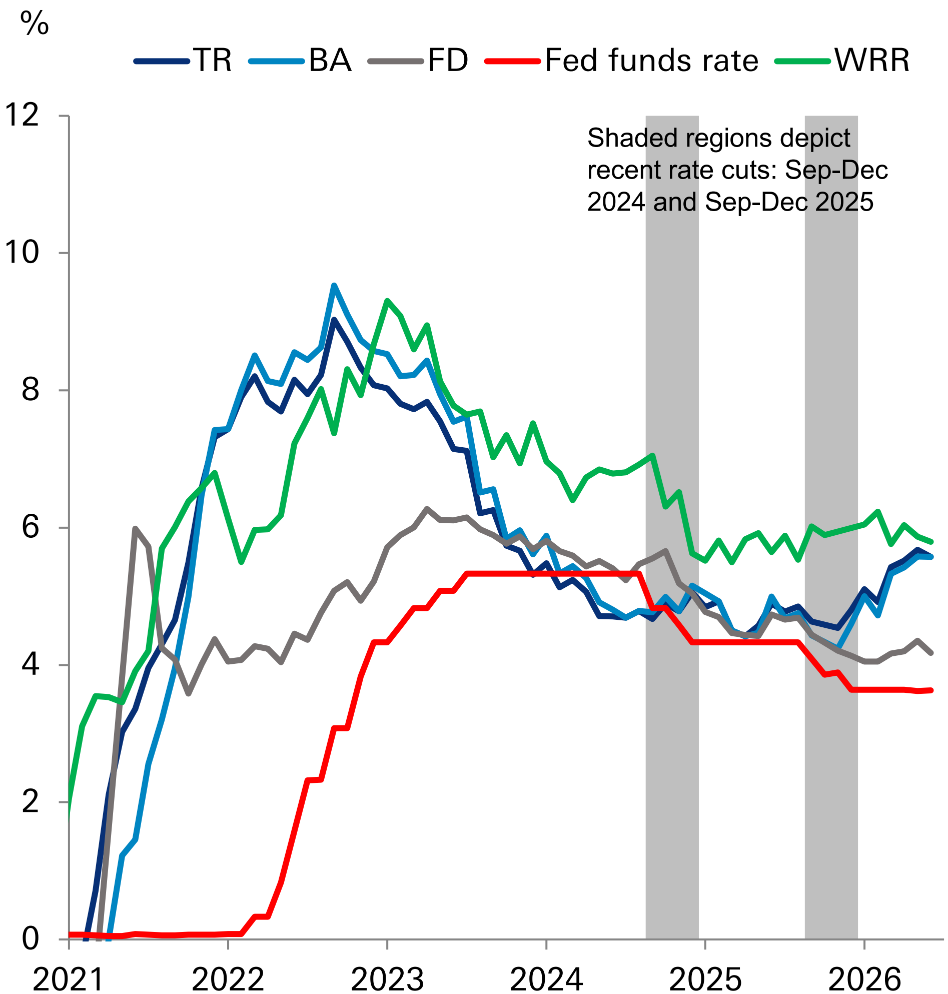
Source: ISM , BLS, Haver Analytics, Deutsche Bank

The policy rate has moved comfortably below policy rules after last year's "insurance" cuts

Fed funds rate versus rules w/ Fed r-star



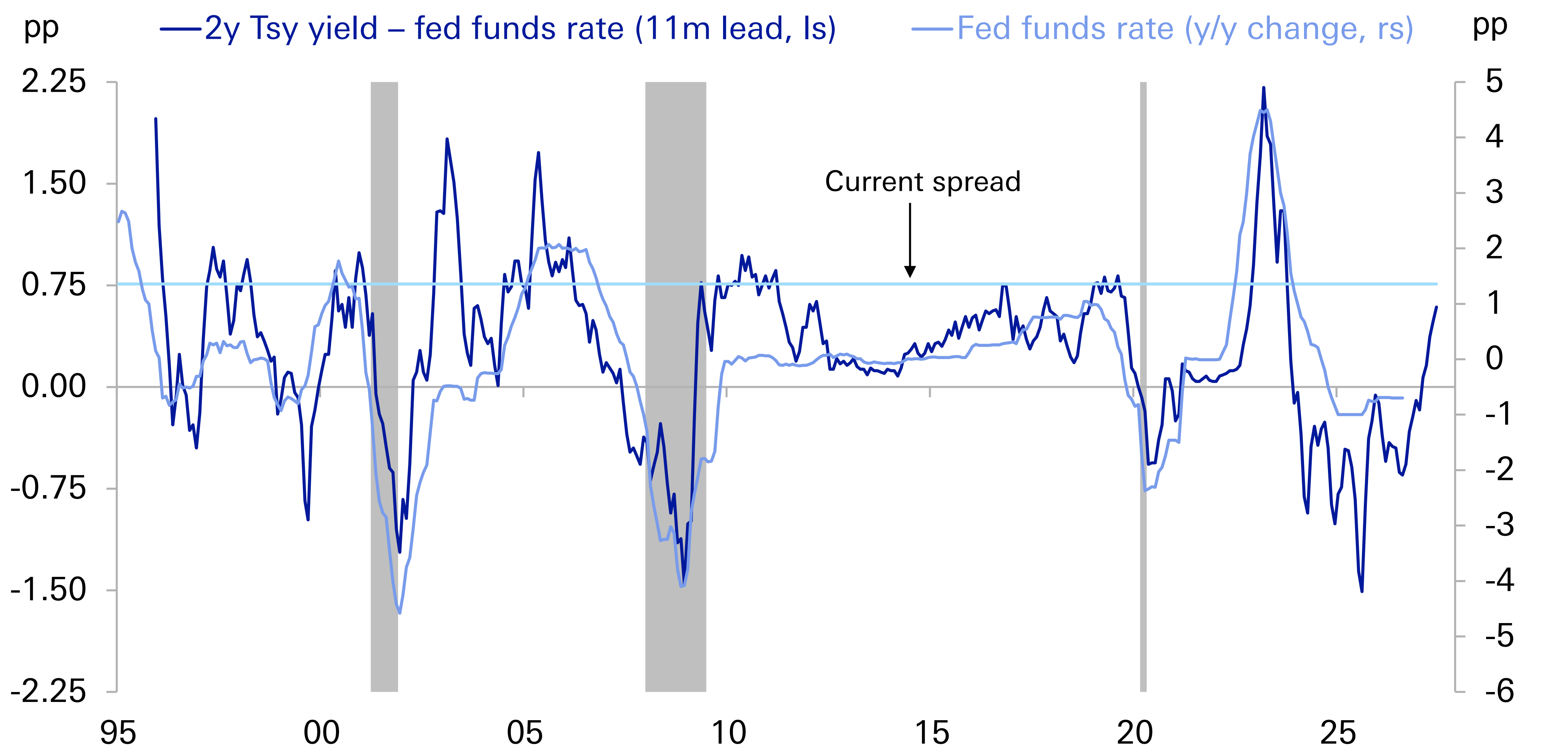
Fed funds rate versus rules w/ DB r-star



Source: FRB, BLS, CBO, Haver Analytics, Deutsche Bank

The wide gap between 2y yields and fed funds rate also predicts rate hikes

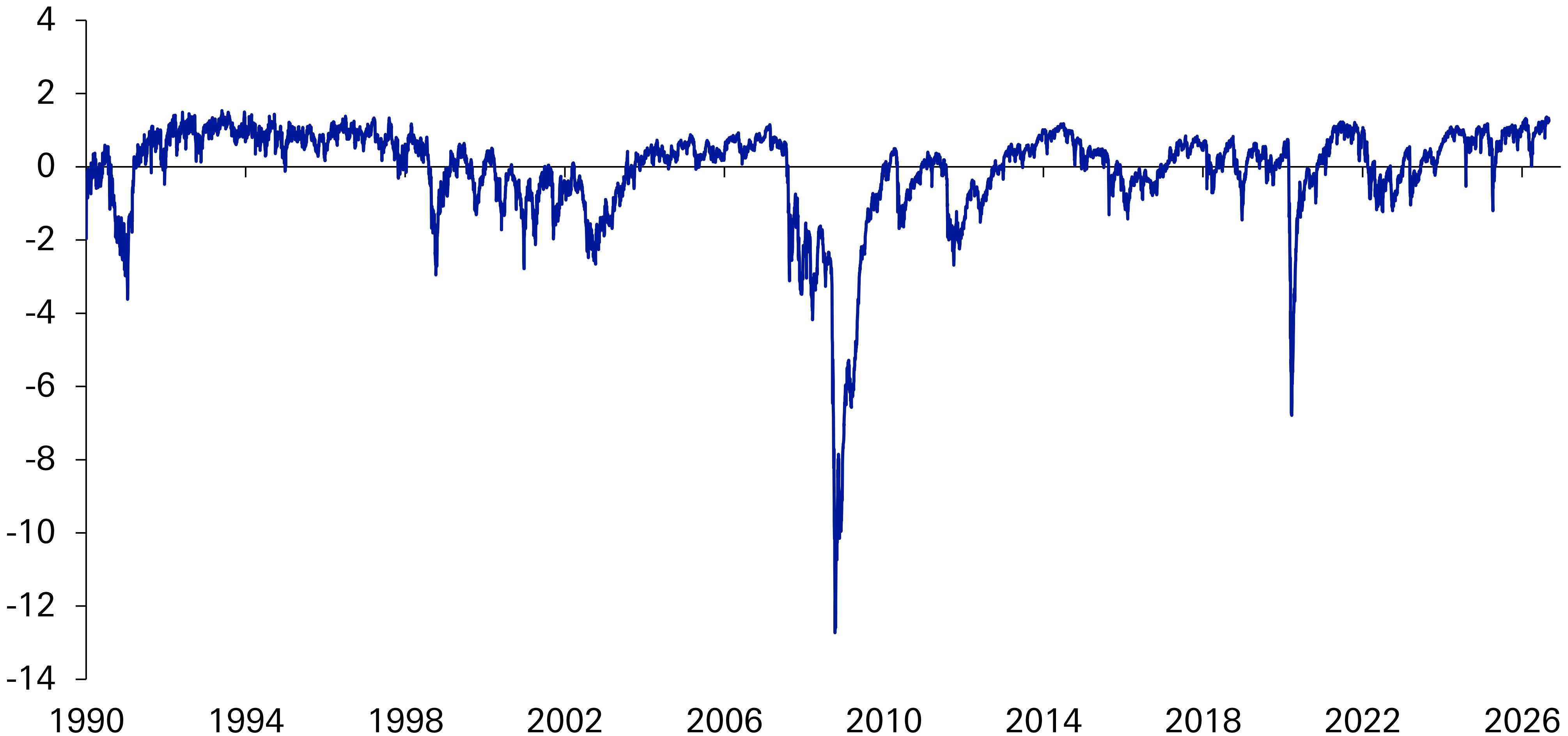
2y yield – fed funds rate and future rate changes



Source: FRB, Haver Analytics, Deutsche Bank

Financial conditions are broadly bumping up against the loosest they've been since 1990…

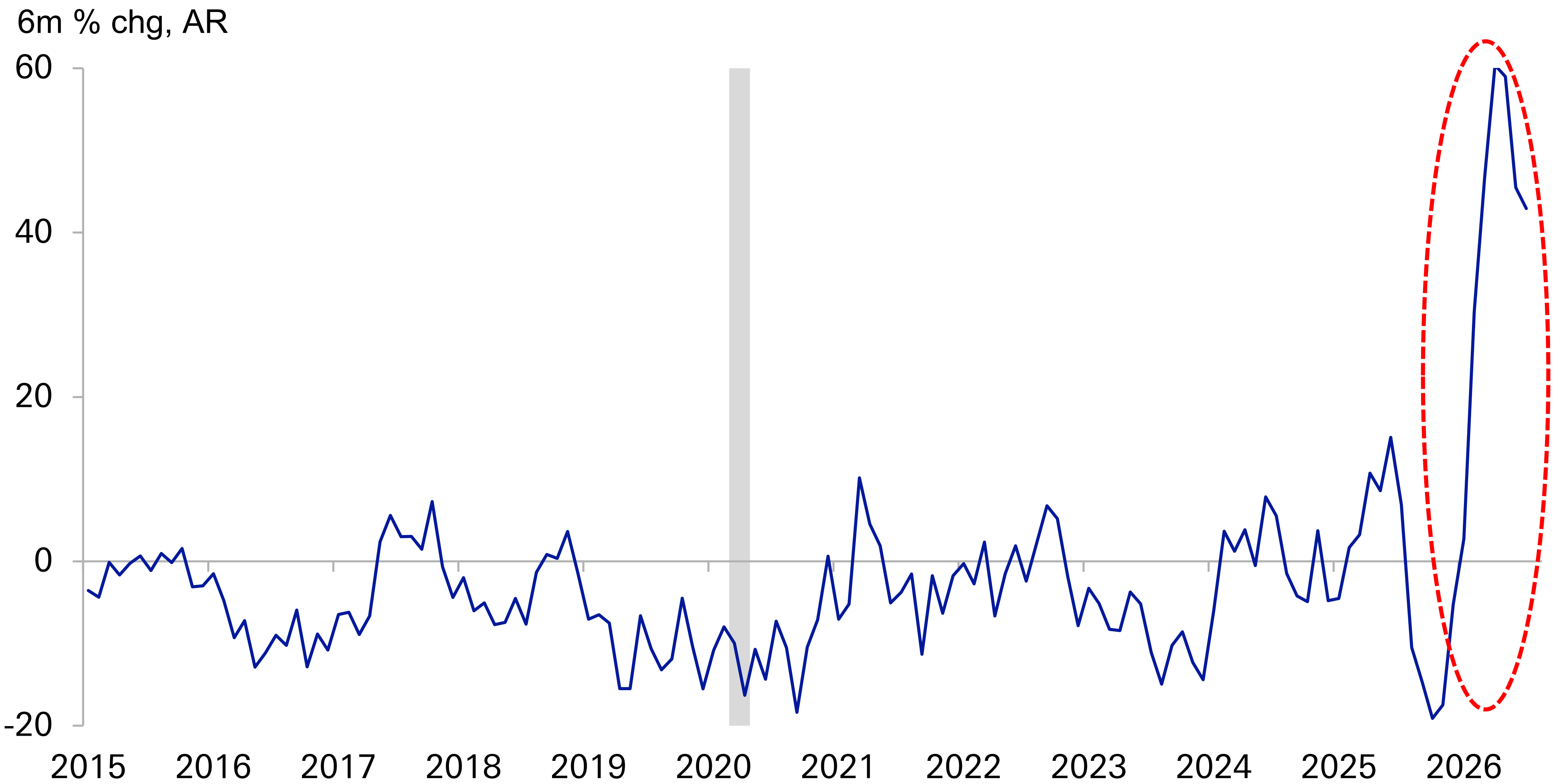
Bloomberg United States FCI



Source: Bloomberg Finance LP, Deutsche Bank; Last update : Sep 7; Note: Bloomberg U.S. Financial Conditions Index tracks the overall level of financial stress in the U.S. money, bond, and equity markets to help assess the availability and cost of credit. A positive value indicates accommodative financial conditions, while a negative value indicates tighter financial conditions relative to pre-crisis norms.

AI is an inflationary force today

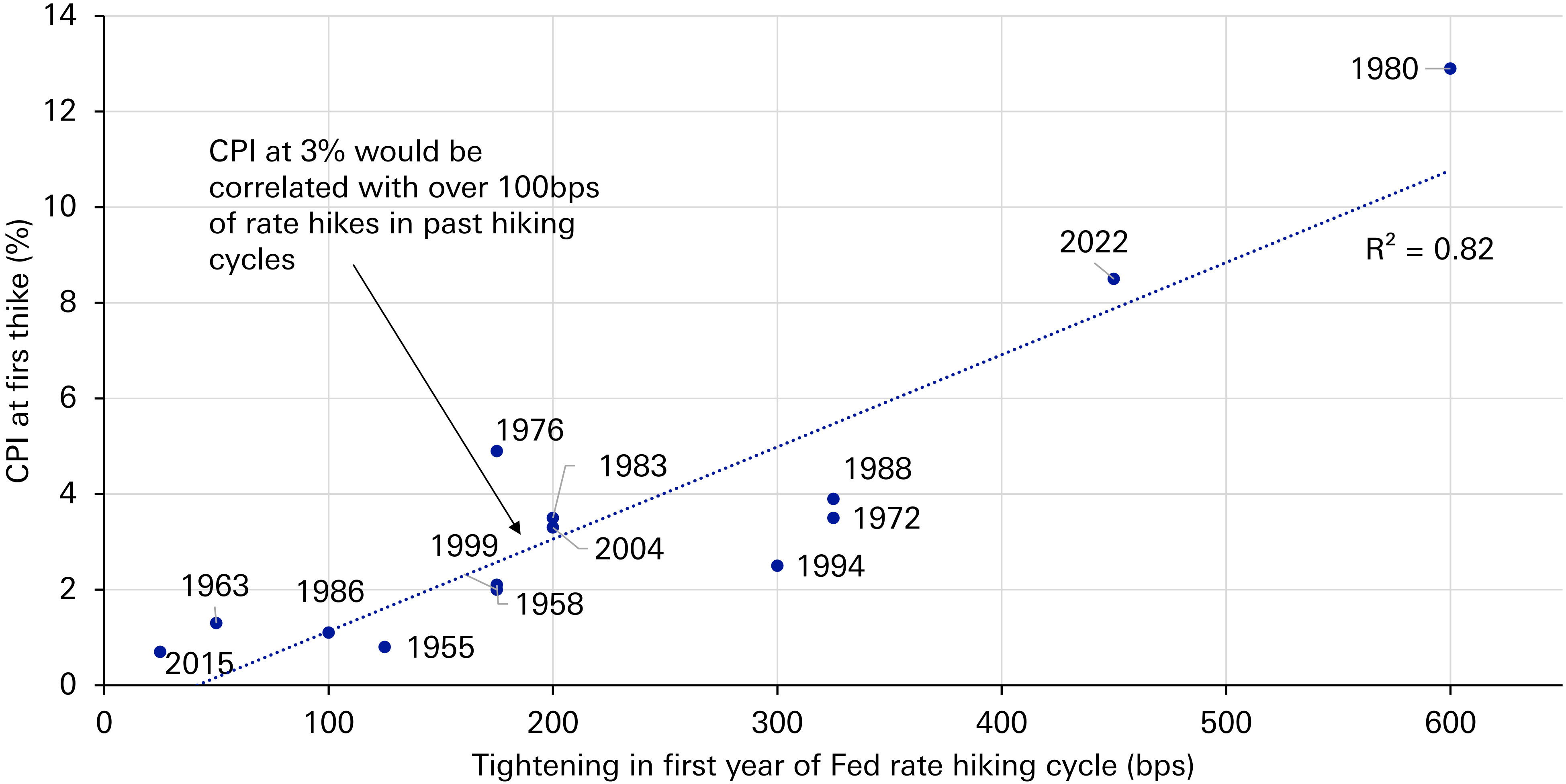
PCE: software and accessories inflation



Source: BEA, Haver Analytics, Deutsche Bank

Historically, there's been a tight correlation between CPI inflation when the Fed starts hiking and how much they hike in the first year… with CPI at 3.4% in July, that would correlate to well over 100bps today… far above all expectations…

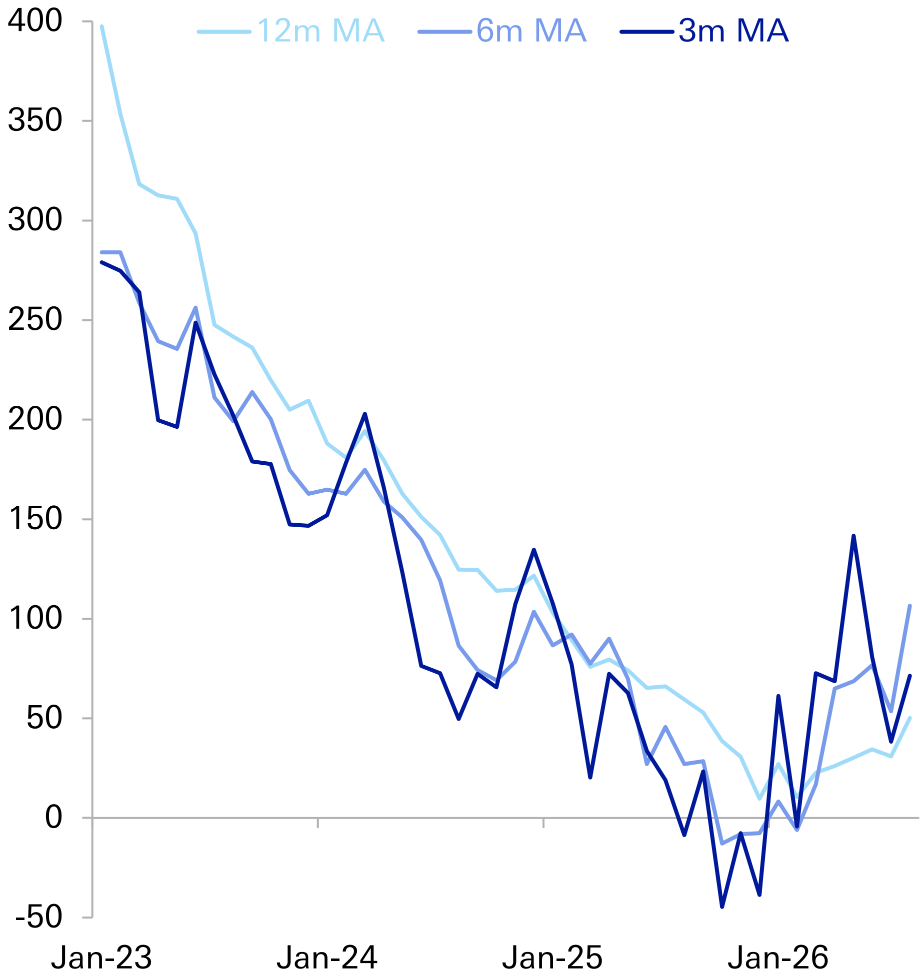
CPI and the amount of Fed tightening in the first year of a hiking cycle



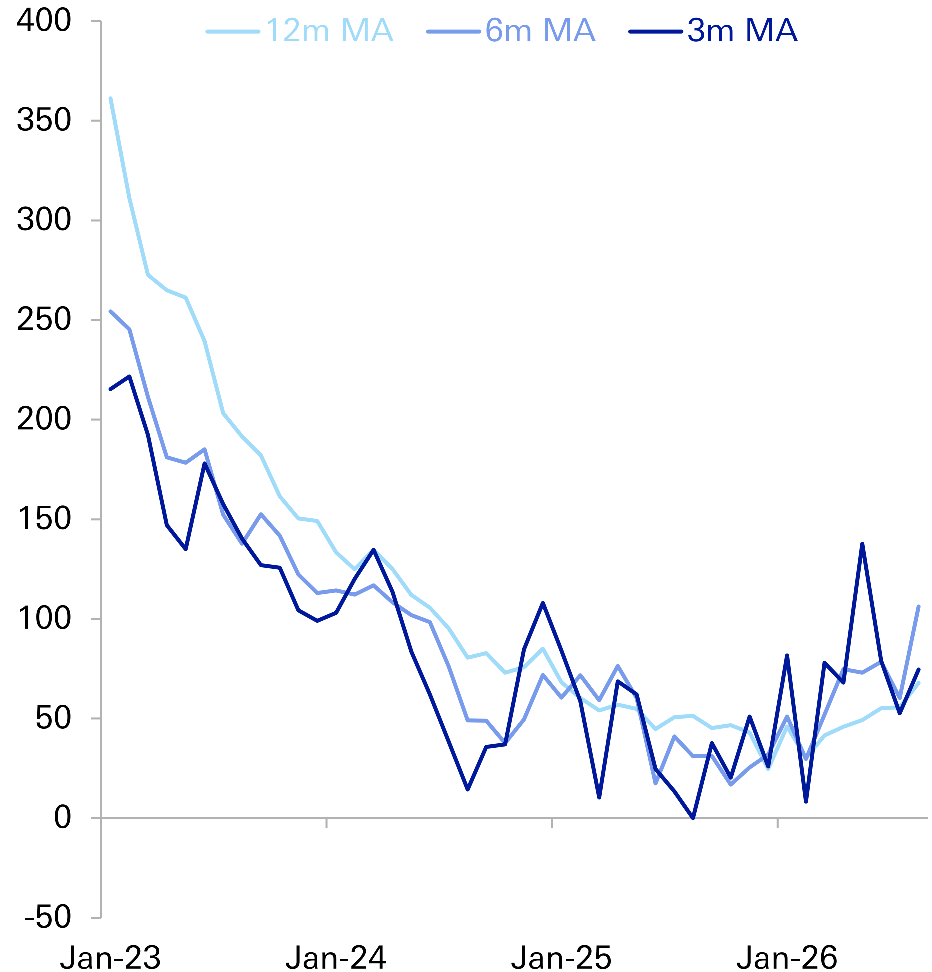
Source: Bloomberg Finance LP, Haver Analytics, Deutsche Bank

Payrolls did slow in 2025 which encouraged the insurance cuts but although volatile, there are clear signs that they have trended up in 2026.

Smoothed monthly gains in nonfarm headline payrolls



Smoothed monthly gains in private nonfarm headline payrolls



Source: BLS, Haver, Deutsche Bank

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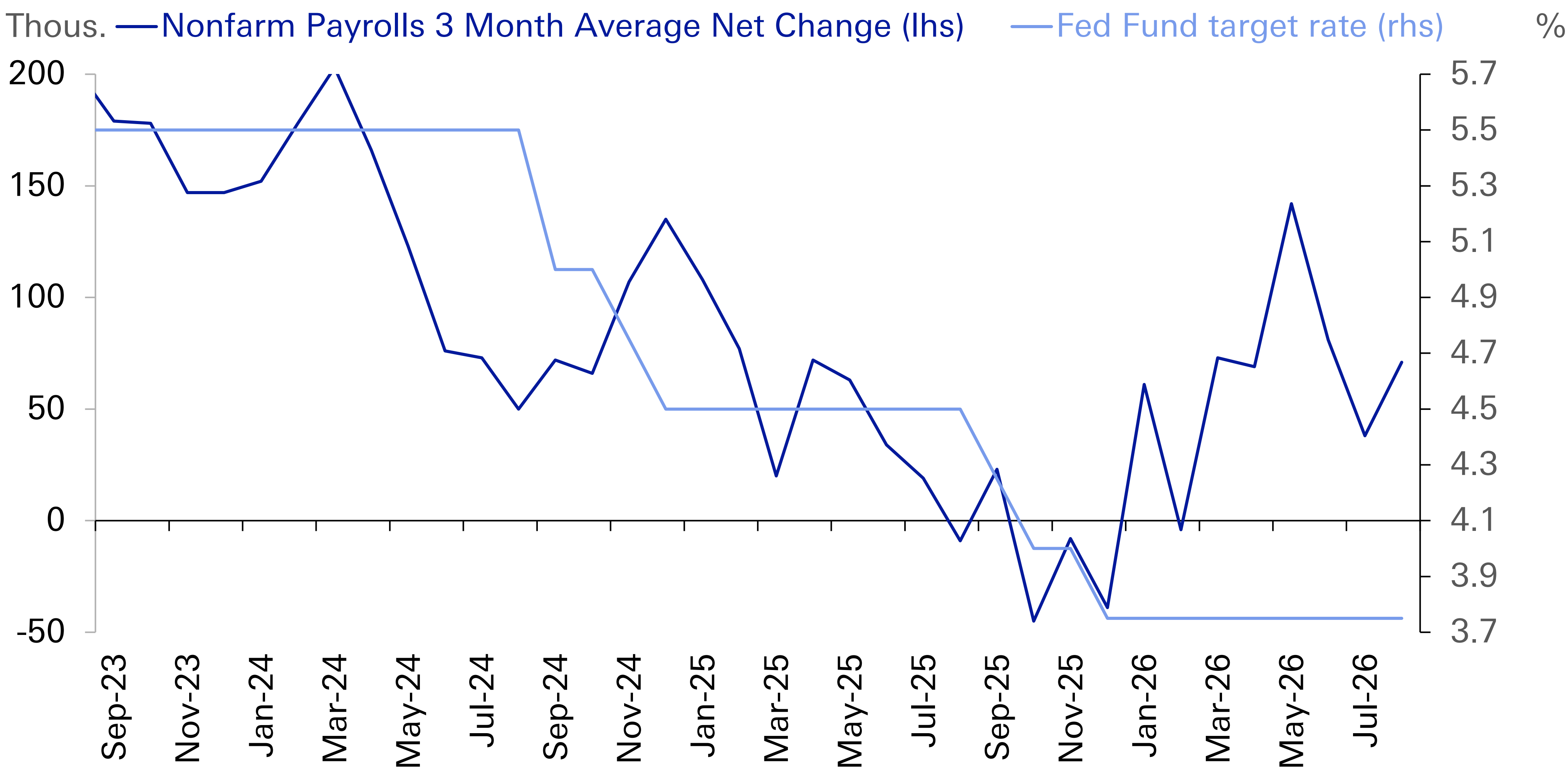
Indeed, with payrolls turning higher, those insurance cuts look ripe to be reversed…

Nonfarm payroll vs. Fed funds

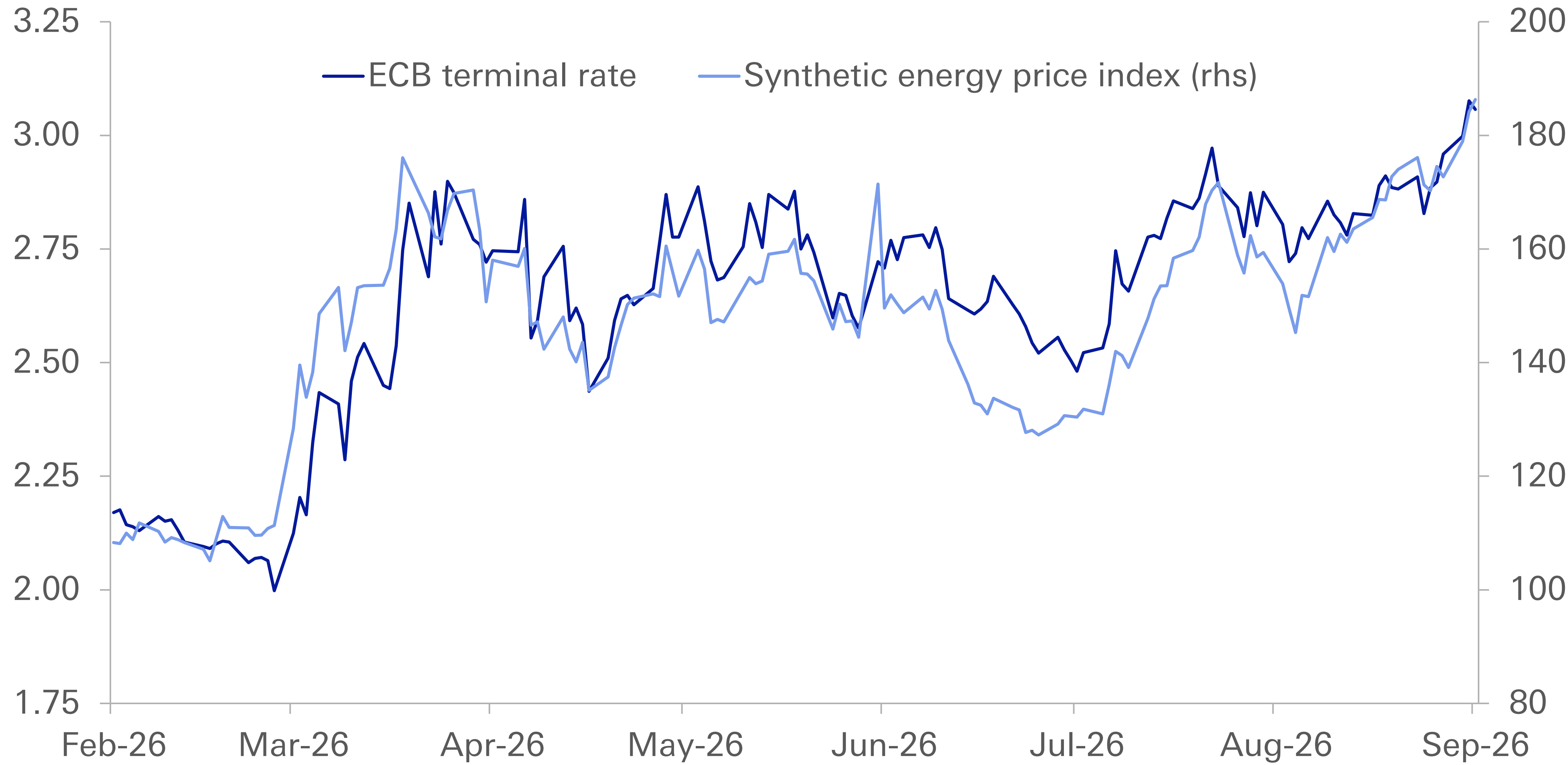


Source: Bloomberg Finance LP, Deutsche Bank

Should the ECB raise rates…?

ECB rate expectations (75bps more hikes) have tracked a synthetic energy price index.

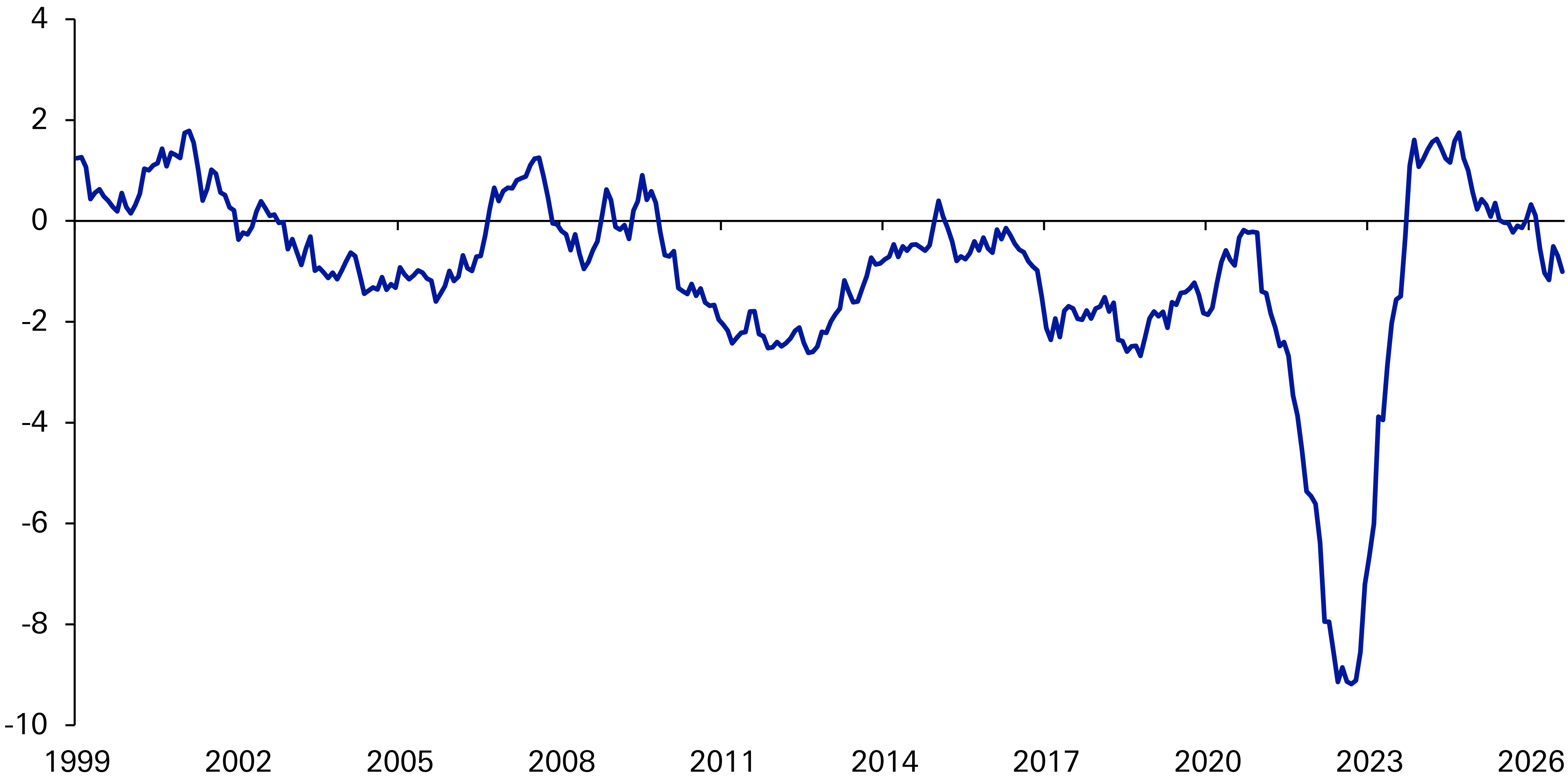
ECB rate expectations & synthetic energy prices



Source: Bloomberg Finance LP, Deutsche Bank. The index is an equal weighting of spot and 12M forward oil and gas prices

In February before the Iran conflict, the real adjusted ECB's deposit rate was still positive. But the energy shock pushed it back into negative territory again…

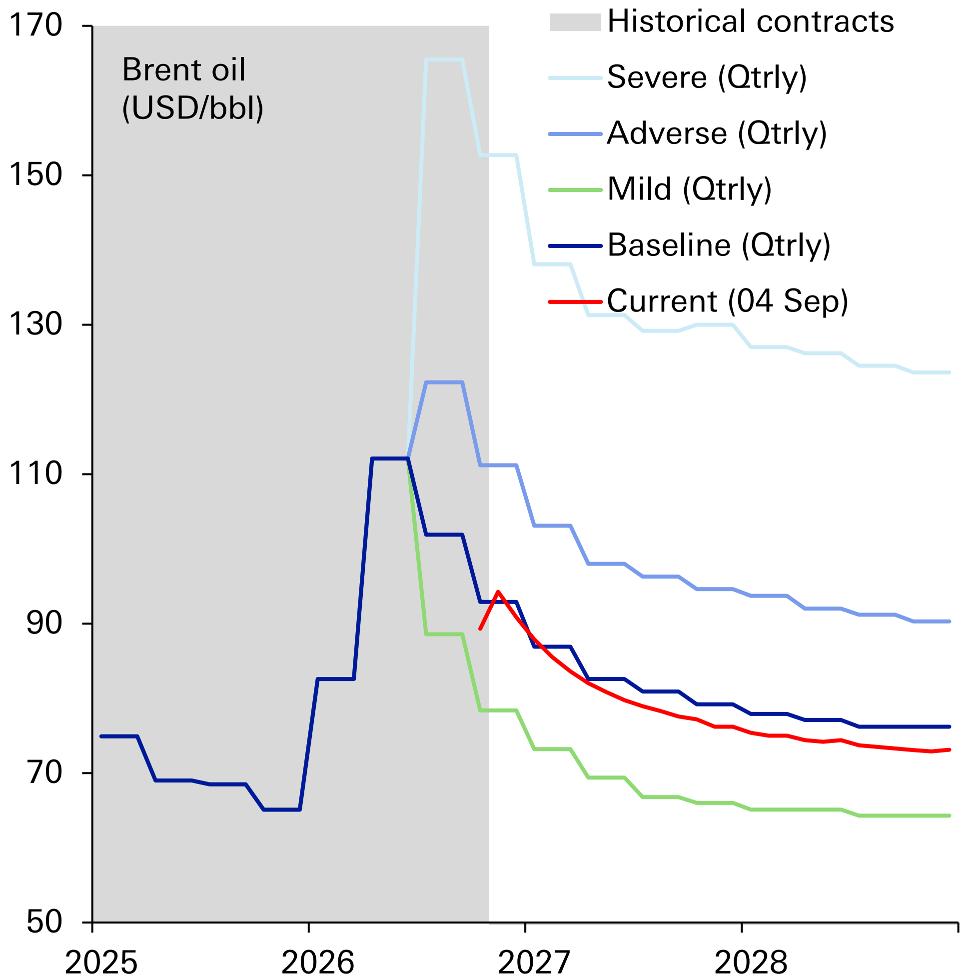
Real ECB Deposit Rate (the Deposit Rate minus year-on-year HICP inflation)

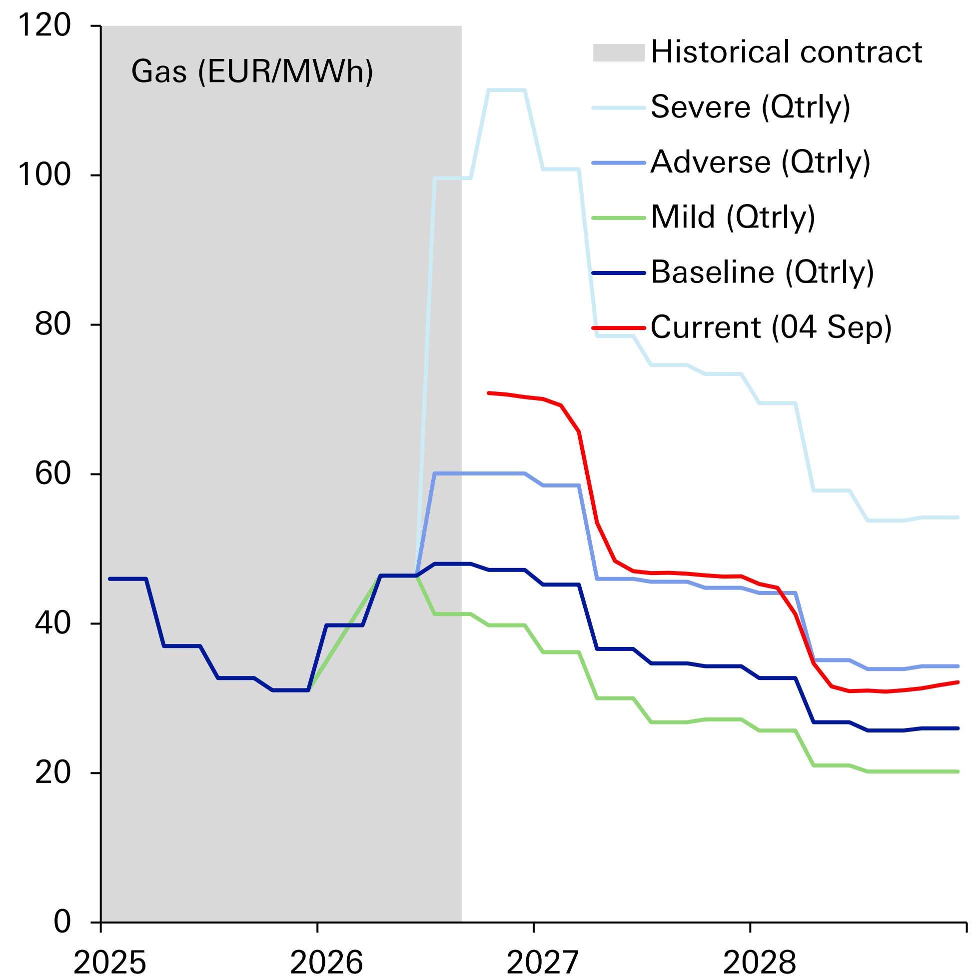


Source: Haver Analytics, Deutsche Bank

Brent is currently in-line with the ECB base case scenario from June but gas is now just above the adverse one. You can see our economics team's preview of the ECB meeting here. They expect a hike this week and another to 2.75% in December. Note they have also upgraded '26 and '27 GDP to 0.8% and 1.2% (up 0.3pp and 0.1pp) respectively.

Oil prices (left) and Gas prices (right) vs. ECB baseline and alternative scenario

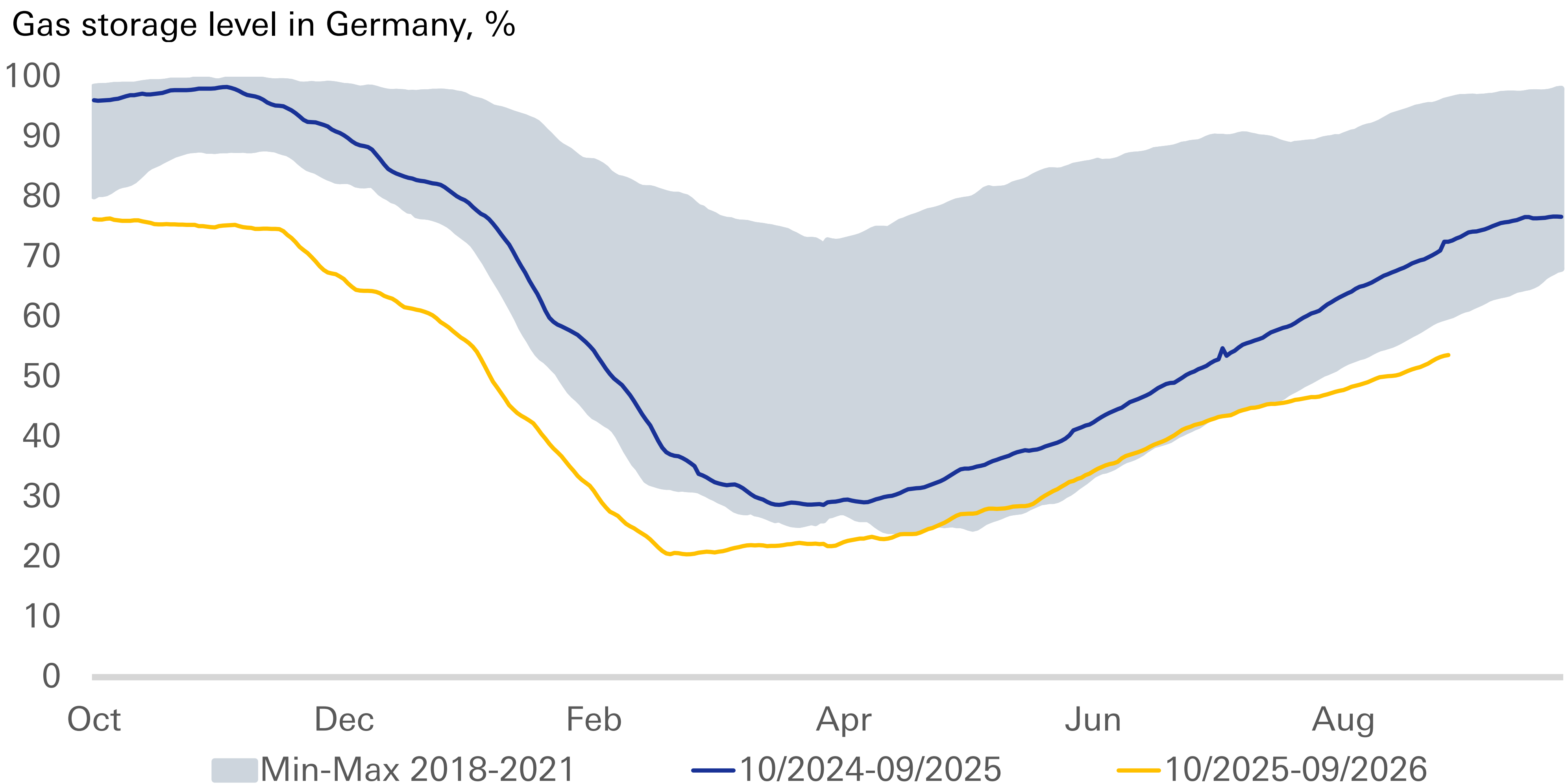




Source: ECB, Bloomberg Finance LP, Deutsche Bank Research

Gas storage levels haven't been an issue since the early days of the Russia-Ukraine conflict but we're starting to see low storage levels again ahead of the winter heating season. See Eric Heymann's blog here for more on this… Maybe El Nino will help prevent a cold winter!!

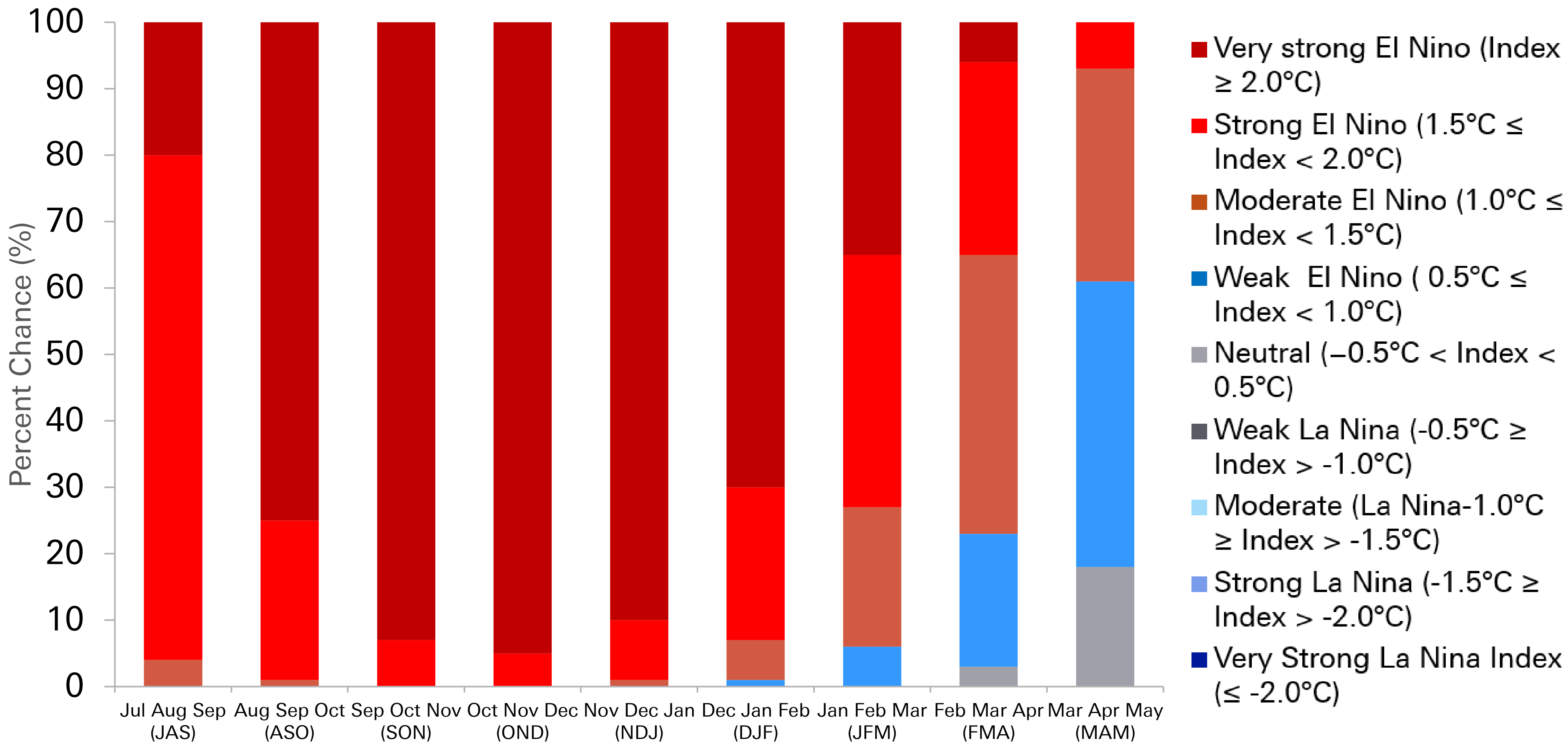
Gas Storage level in Germany



Source: Federal Network Agency, Deutsche Bank Research

Note that by the end of the year we could be seeing an El Nino unlike any we've seen before. Darkest red indicates the highest heat probabilities. This may have inflation and macro implications…

Official NOAA CPC ENSO Strength Probabilities (Issued August 2026)

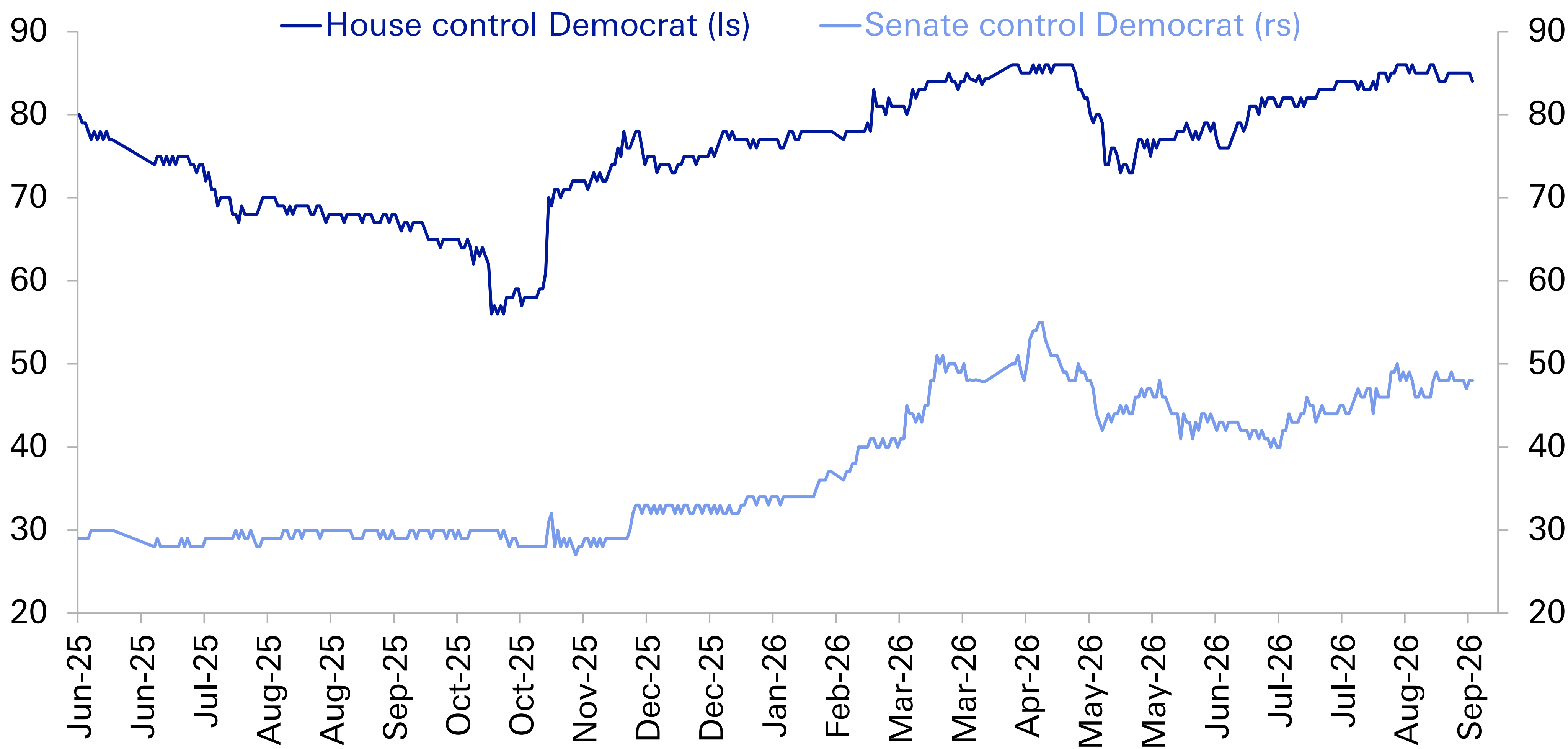


Source: NOAA, Deutsche Bank ; Note: The bars show the chance of El Niño, ENSO-Neutral, and La Niña provided for 9 upcoming, overlapping 3-month seasons (each letter represents a month).

Midterms are fast coming into view…

While the House race has long been in favour of the Democrats, the Senate was firmly leaning GOP in prediction markets until this year and especially since the Iran conflict lifted inflation…

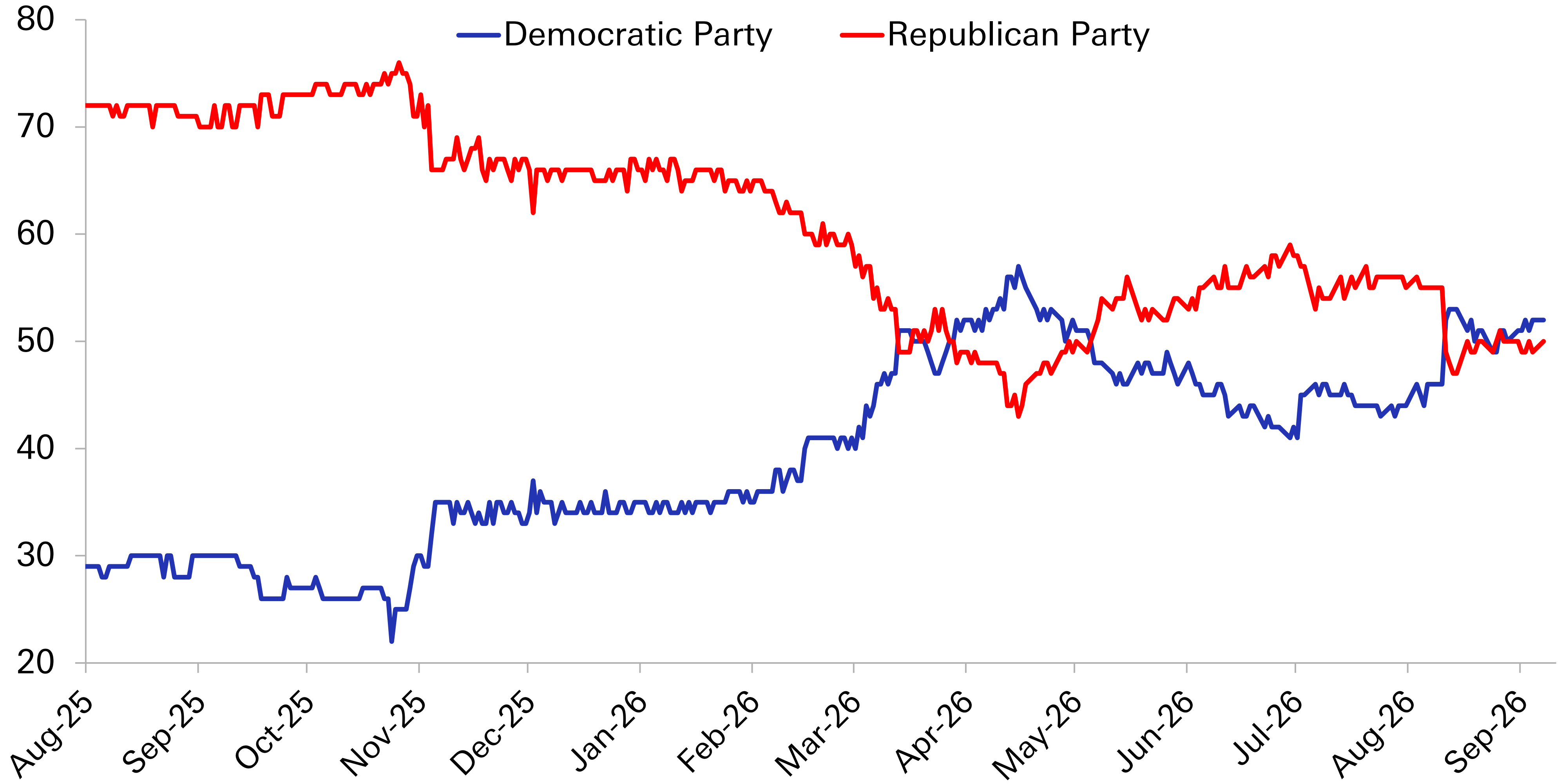
Predicted 2026 Mid-term election outcome



Source : Bloomberg Finance LP, Deutsche Bank, Polymarket, updated through Sep7

Since around the time the Iran strikes began, the Democrats have caught up in the race to retake control of the Senate… that would have a big impact on appointments like Fed Governors, cabinet members and Supreme Court justices, which all require Senate approval… Surely the Senate matters to Trump…

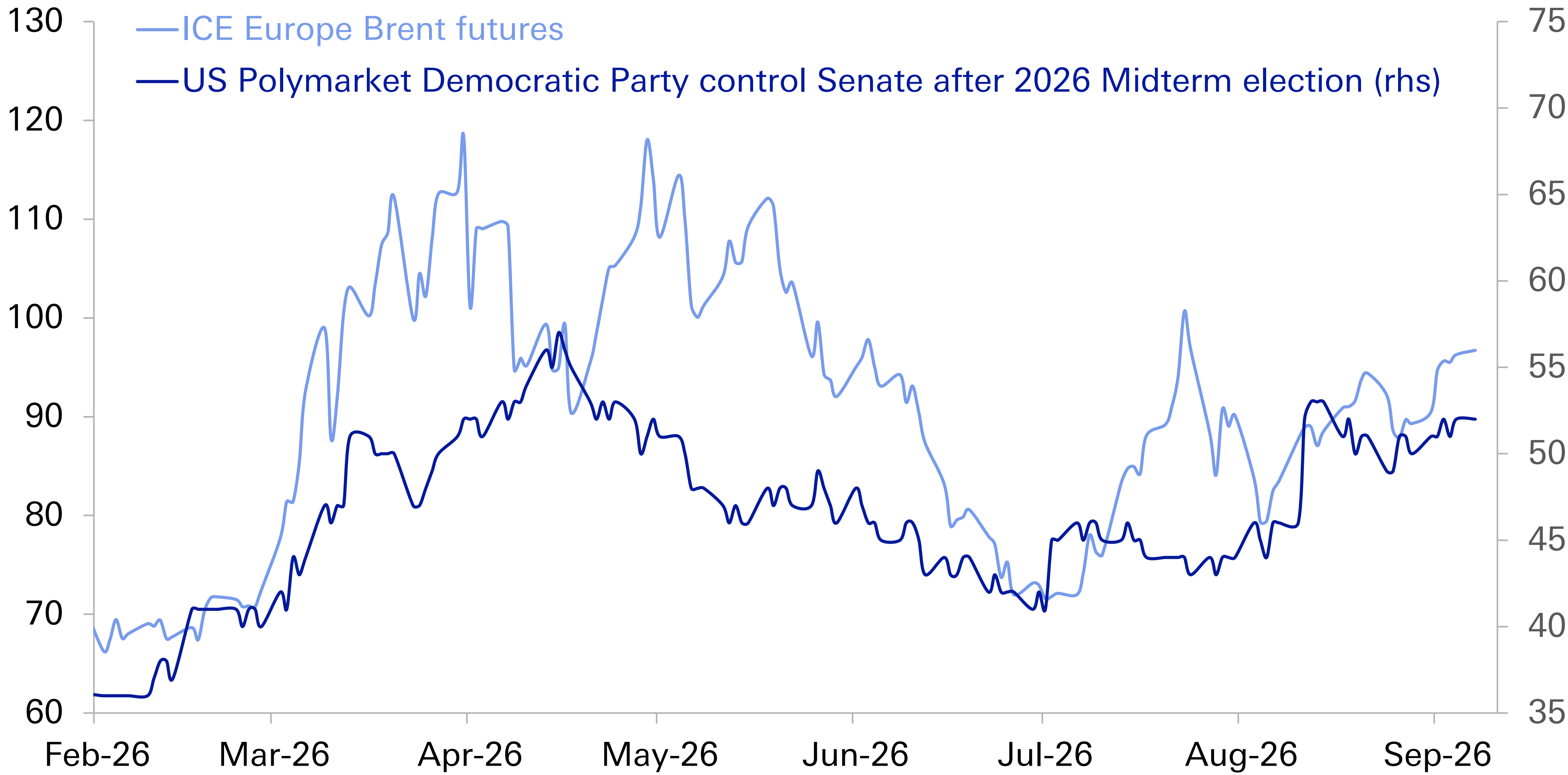
US Polymarket Party control Senate after 2026 Midterm election



Source : Bloomberg Finance LP, Deutsche Bank, updated through Sep 7

There is a decent correlation between Brent and the probability of Senate control

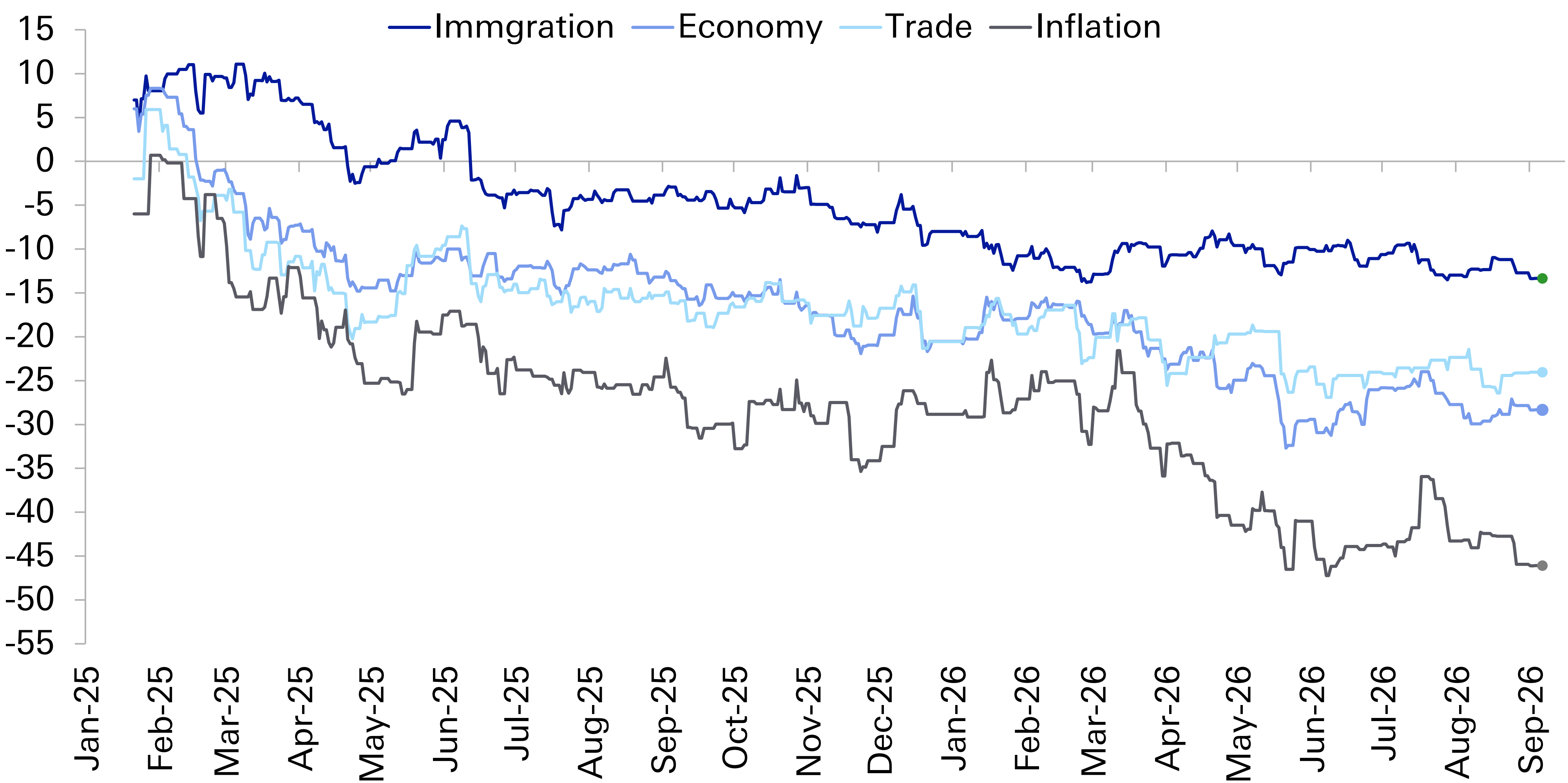
Probability of Democrat control of the Senate after mid-terms and Brent price



Source : Bloomberg Finance LP, Deutsche Bank, updated through Sep 7

Inflation is where Trump's approval rating seems most challenged and fell further after the Iran conflict began.

An updated polling average of Donald Trump's net approval rating on immigration, the economy, trade, and inflation, accounting for each poll's quality, recency, sample size, and partisan lean



Source: Nate Silver, Deutsche Bank, Last update : Sep 7

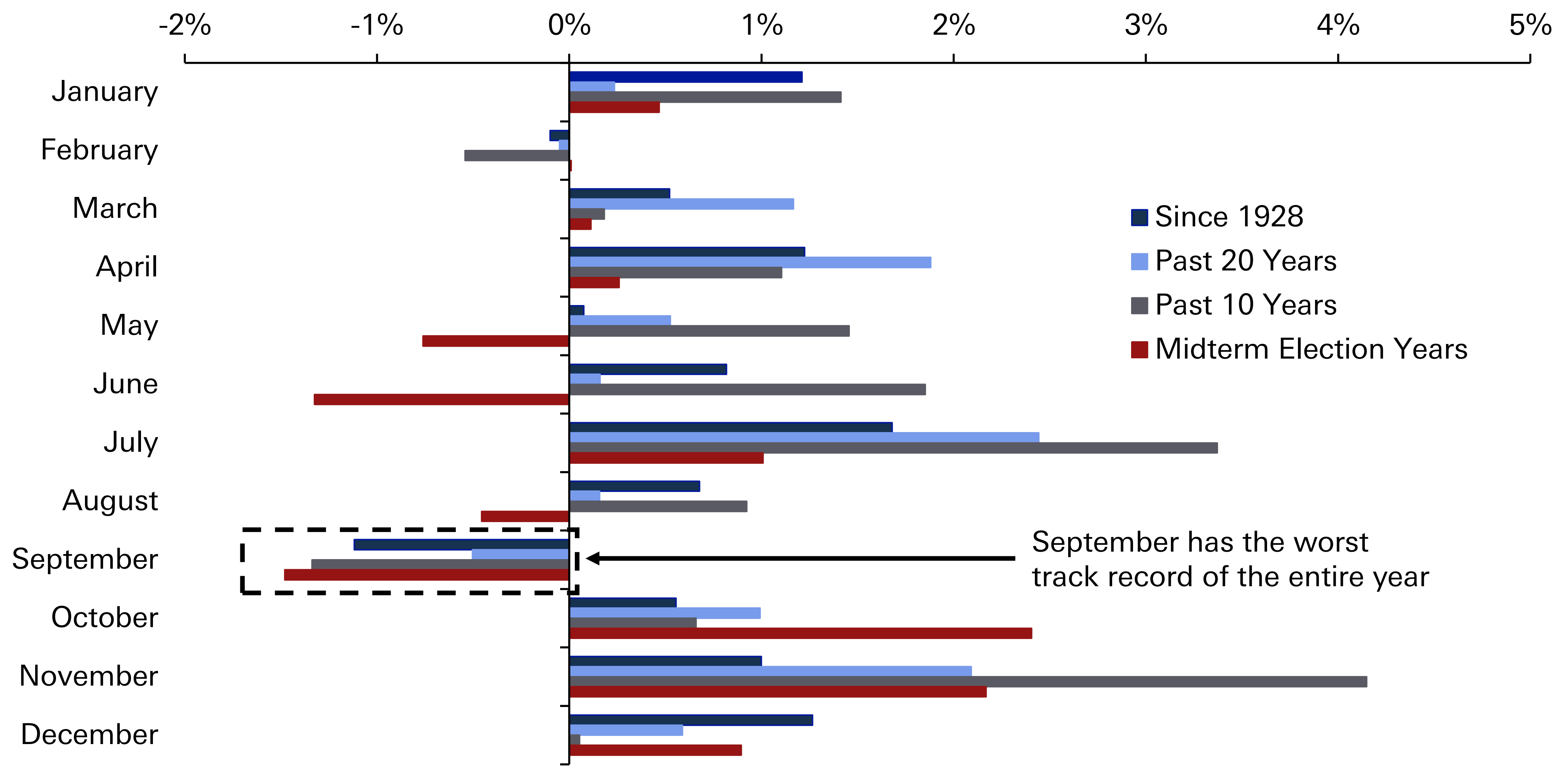
Mid-term years often see a weaker start to H2 for the S&P 500 and a fall into October as summer fades. After mid-terms the market tends to be strong regardless… 2026 initially followed the script but markets have been climbing since early August…

Average S&P 500 performance (first trading close on or after July 1 = 100)

Source: Bloomberg Finance LP, Deutsche Bank

Throughout history and in recent years, the S&P 500 has consistently seen its worst month of the year in September... Midterm years are tougher but note that just before and after mid-terms, the market fully recovers so is this enough to justify lightening up?

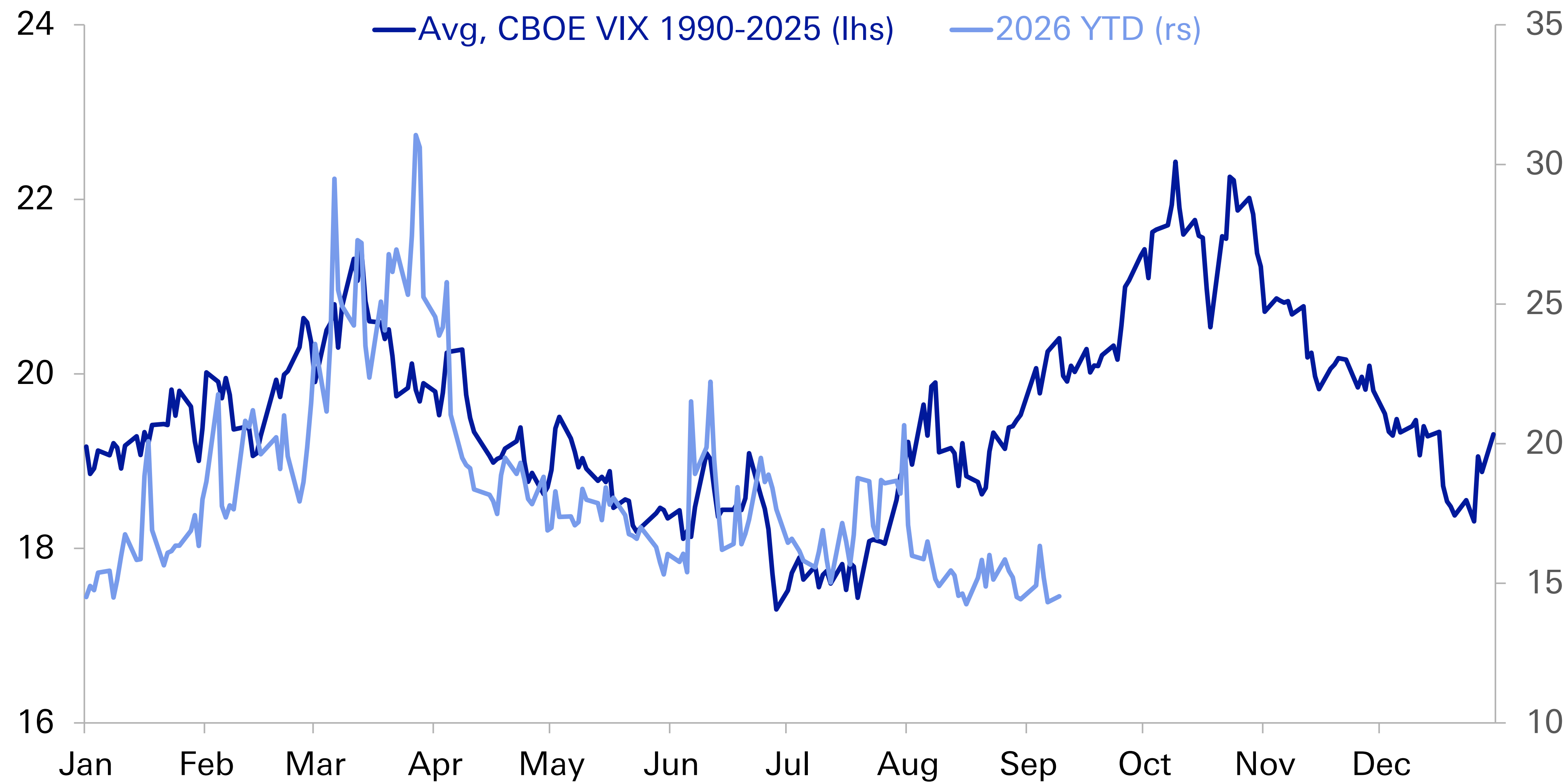
Monthly Performance of the S&P 500 (1928-2025)



Source: Bloomberg Finance LP, Deutsche Bank

Even though there are a few ongoing concerns (e.g. Iran, oil, rising yields, mid-terms etc.), so far 2026 is resisting the seasonal pattern in terms of volatility…

Seasonality of the VIX index



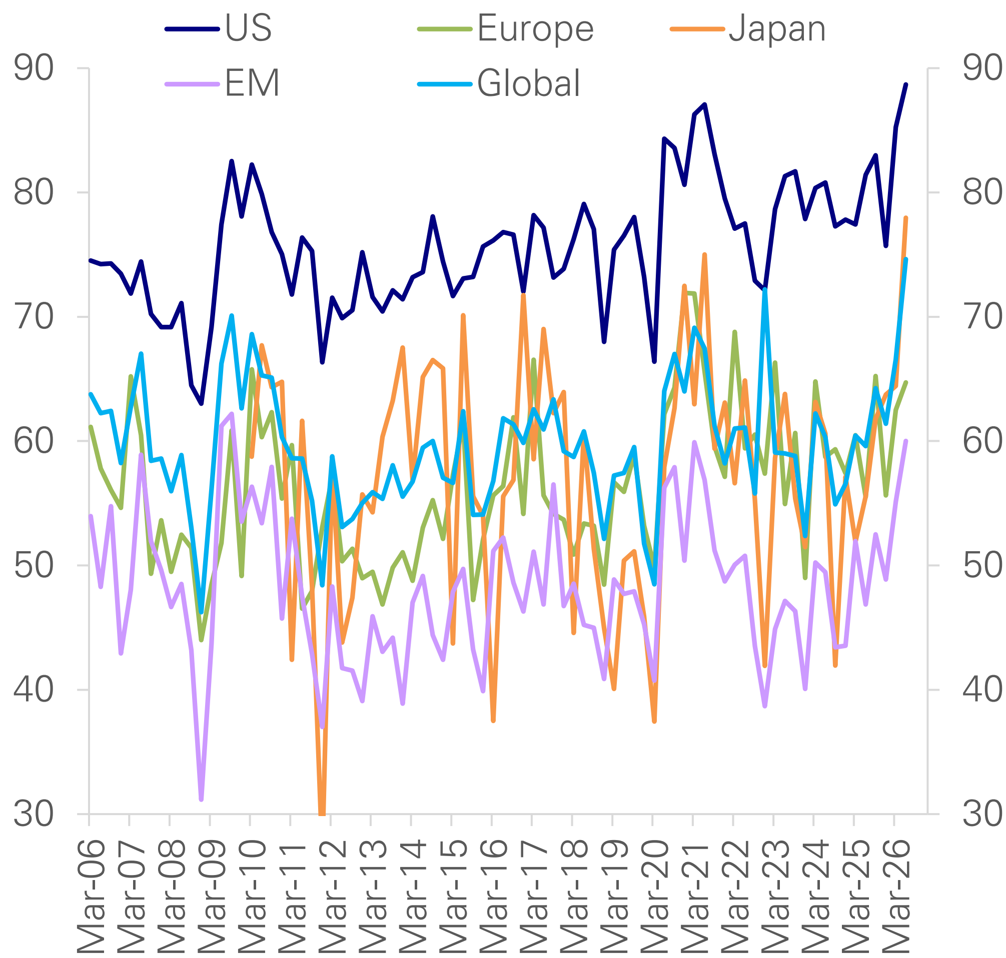
Source: Bloomberg Finance LP, Deutsche Bank, Last update: Sep 7

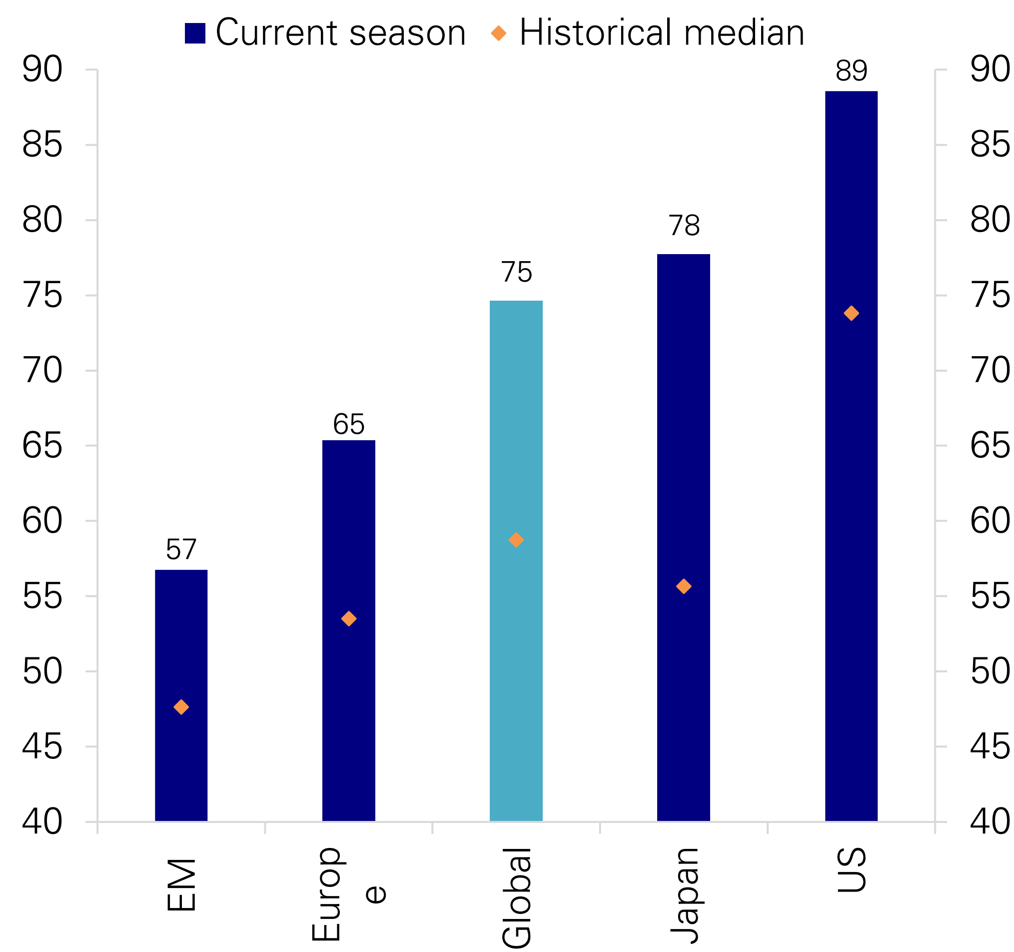
Global earnings may never have been stronger…

Please see Parag Thatte and Binky Chadha's excellent piece reviewing global earnings here

The breadth of companies beating expectations hit record peaks in Q2 in the US and Japan and remained well above historical averages in Europe and EM

Proportion of companies beating on earnings (%)





Source: Bloomberg Finance LP, Deutsche Bank Asset Allocation

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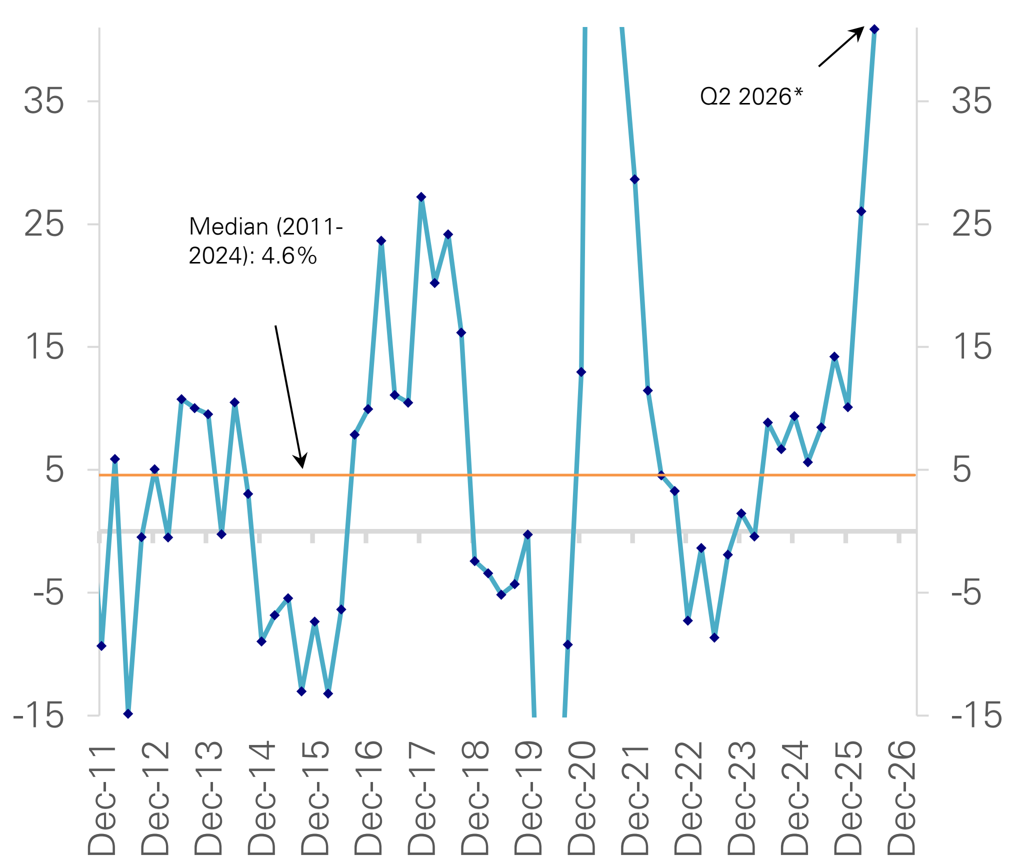
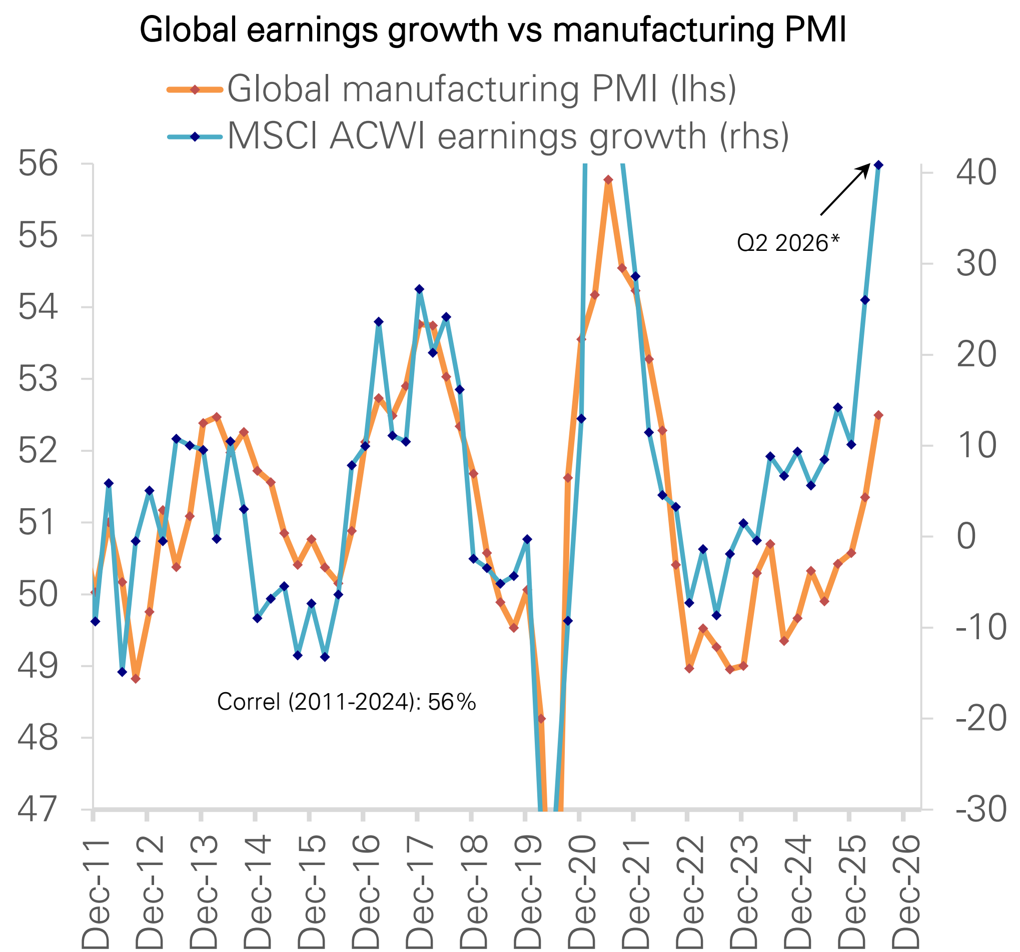
And we haven't beaten low expectations. In Q2 we saw the strongest non-pandemic YoY global earnings expansion on record, driven by synchronised cyclical and commodity tailwinds.

Global YoY Earnings growth



*Q2 is blended, assumes companies yet to report beat at current beat rate; growth in USD

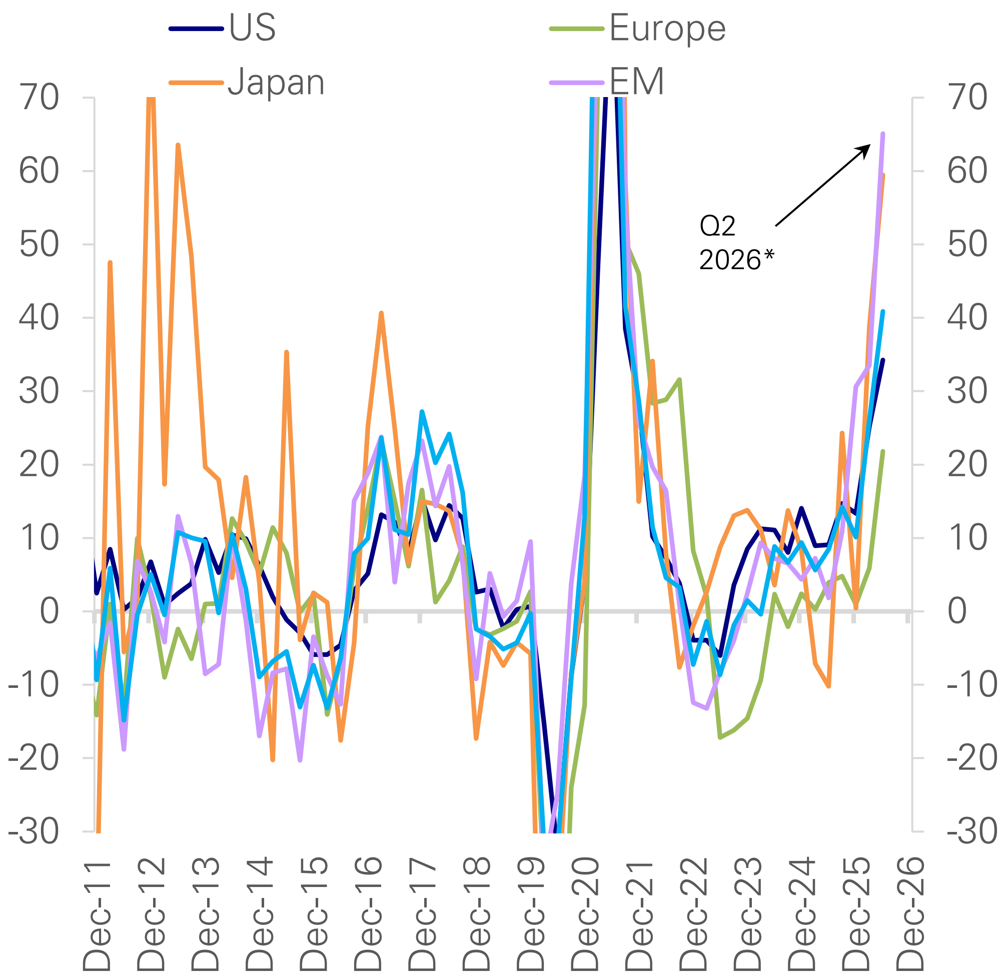


*Q2 is blended, assumes companies yet to report beat at current beat rate

Source: Bloomberg Finance LP, Deutsche Bank Asset Allocation

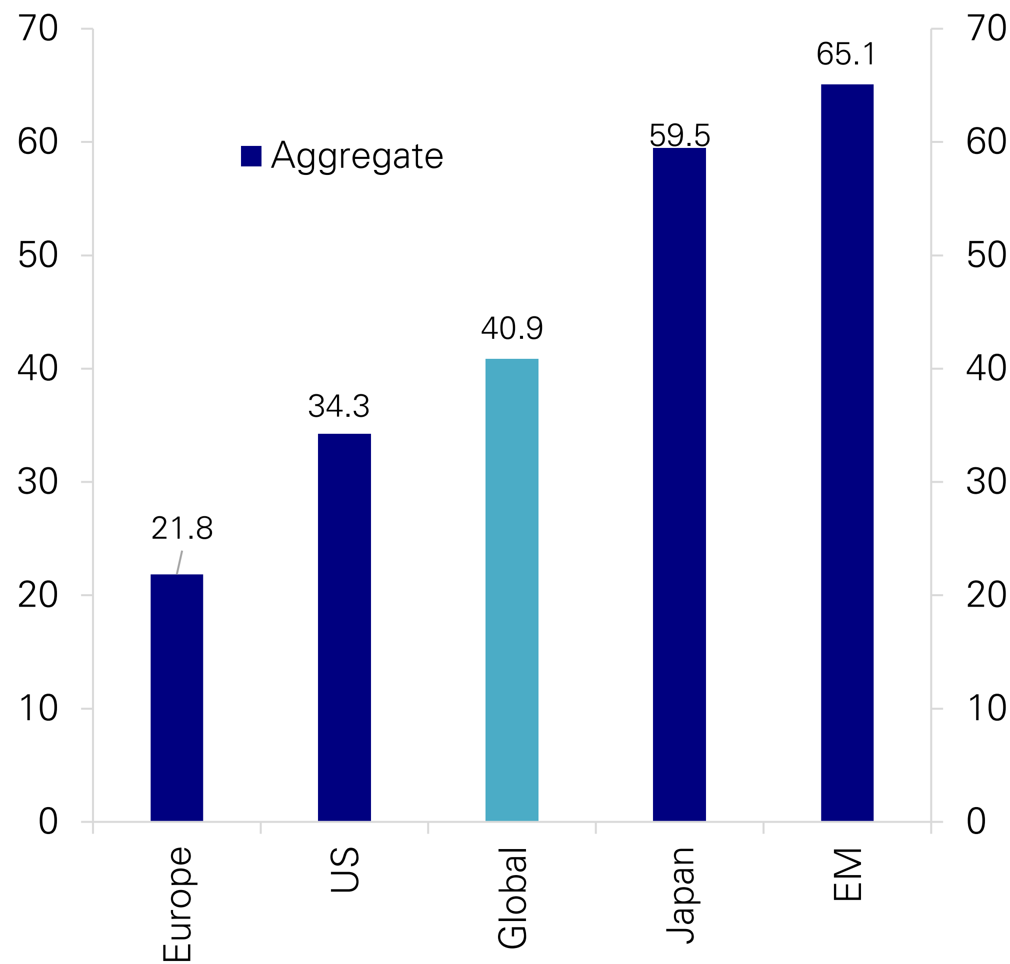
Earnings growth has accelerated across all regions

Quarterly aggregate earnings growth (% yoy)



*Q2 is blended, assumes companies yet to report beat at current beat rate

Q2 2026 blended earnings growth (% yoy)



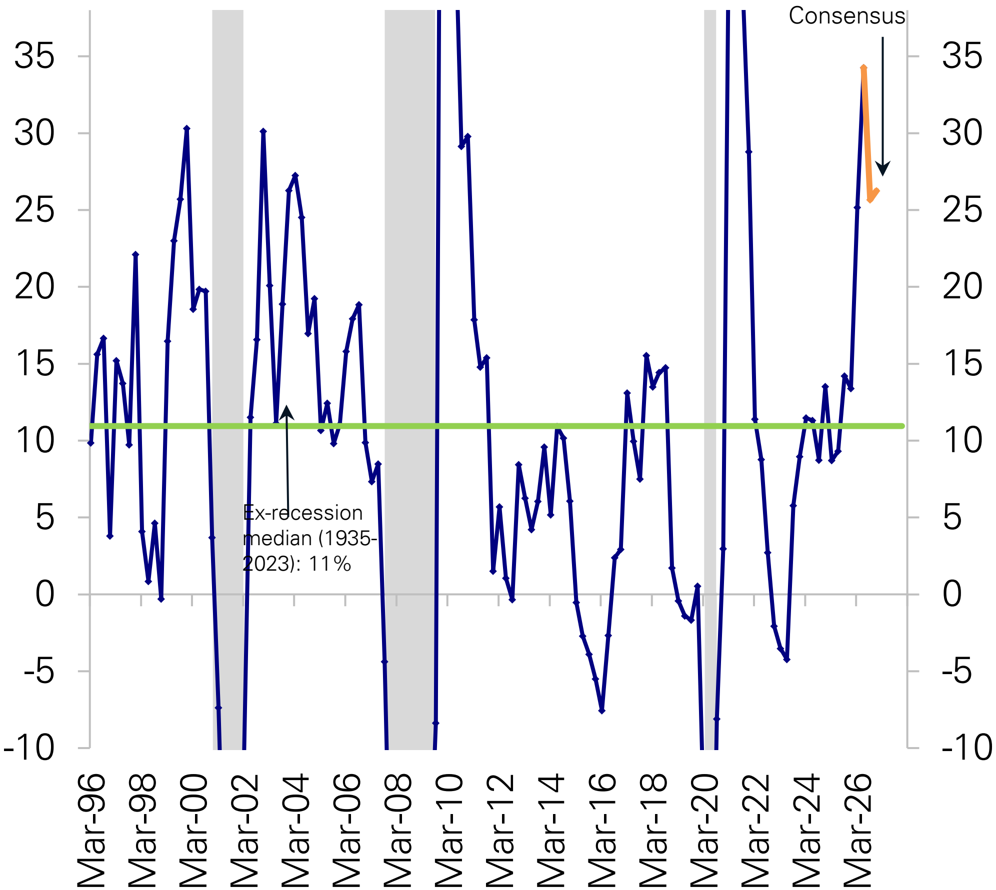
*Q2 is blended, assumes companies yet to report beat at current beat rate

Source: Bloomberg Finance LP, Deutsche Bank Asset Allocation

It's been a blockbuster Q2 for the US…

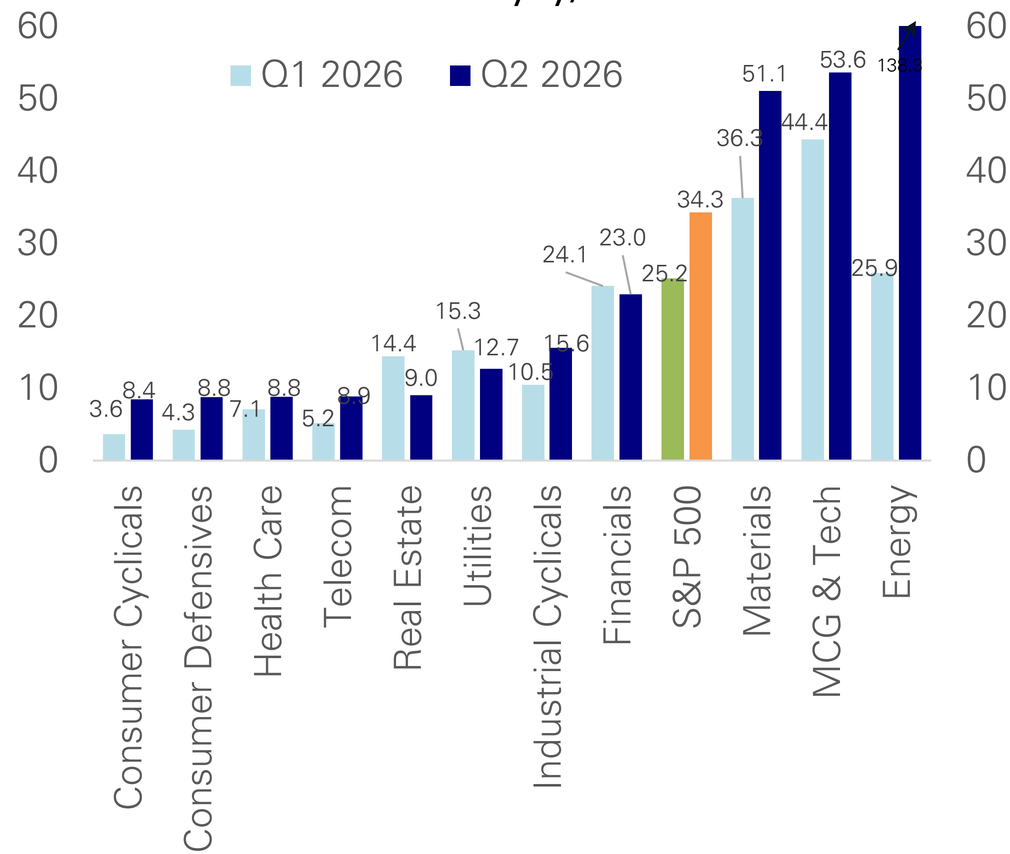
S&P 500 YoY earnings growth with sectors performance…

S&P 500 quarterly earnings growth* (% yoy)



* Excluding 2018 tax cut

Earnings growth by S&P 500 sector group (% yoy)



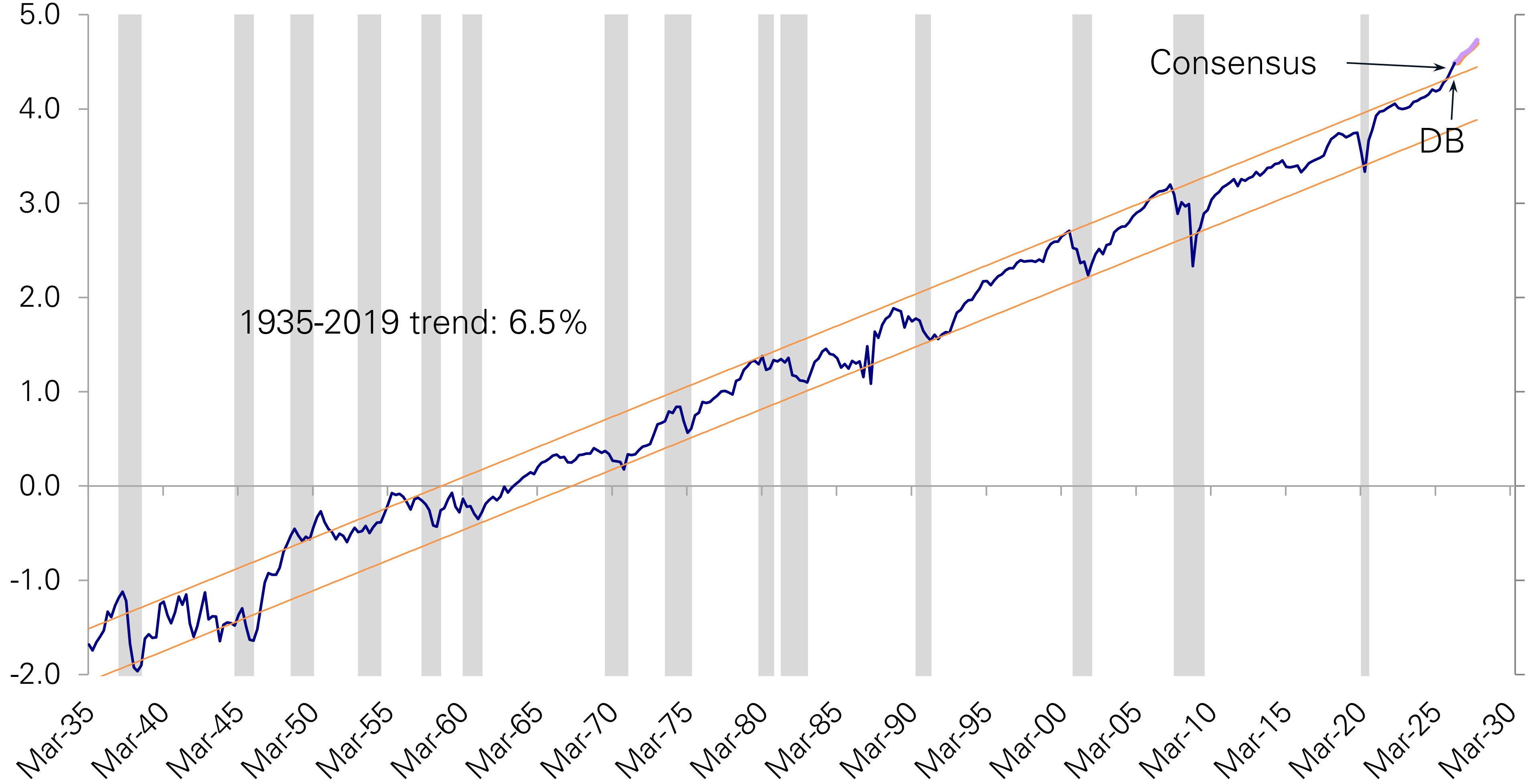
* Blended assumes companies that that report beat at the current beat rate

Source: Bloomberg Finance LP, Deutsche Bank Asset Allocation

Deutsche Bank Research Institute

US earnings are breaking out of a 90-year channel…. On the upside which is incredible when you consider the high growth periods of the past…. The debate will rage on as to whether this is a sustainable new plateau or an artificial period of AI related elevated earnings…

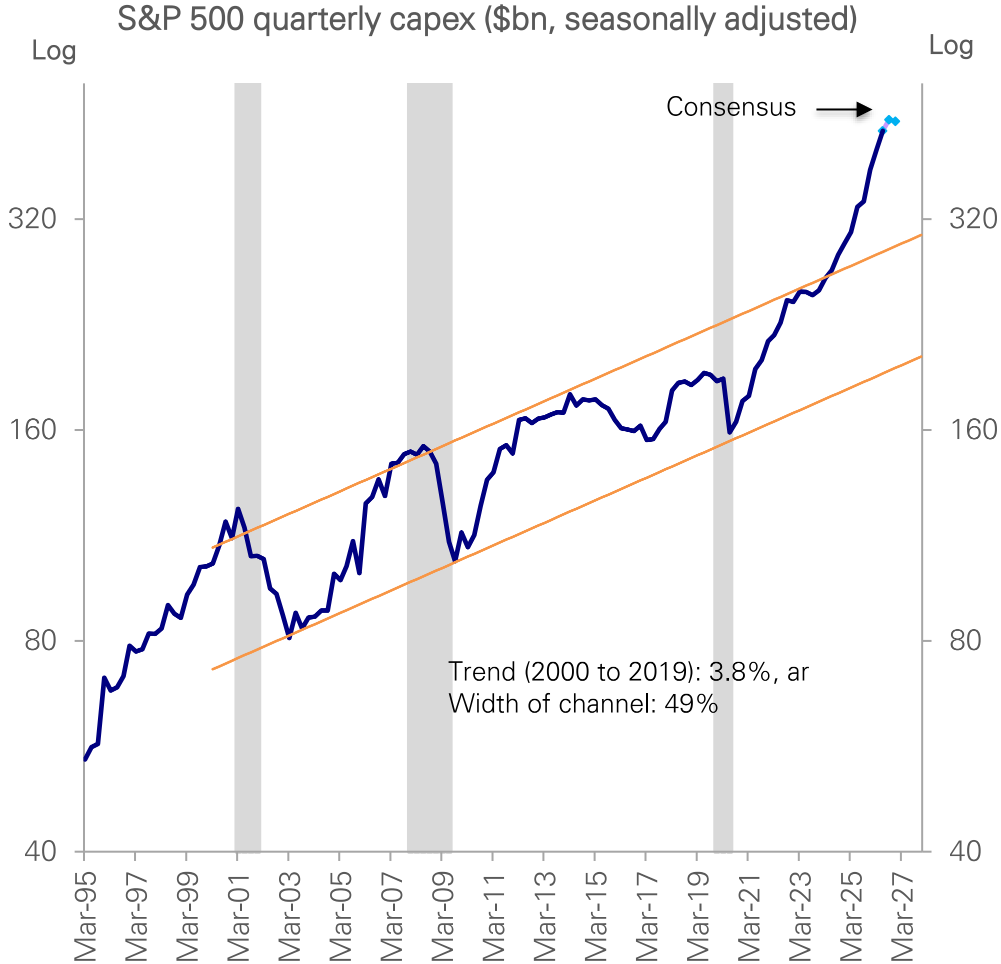
S&P 500 quarterly EPS seasonally adjusted (log)

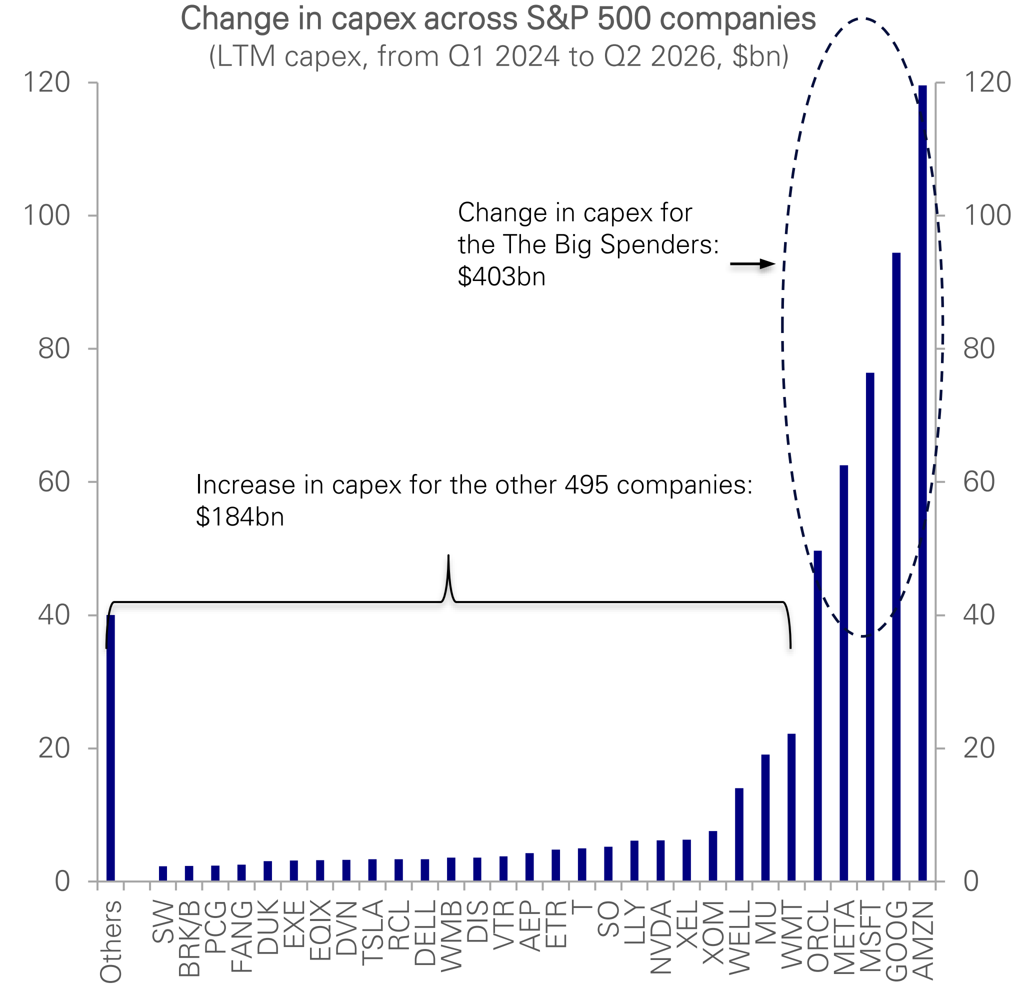


Source: Bloomberg Finance LP, Deutsche Bank Asset Allocation

We are clearly in an AI Capex boom. The top 5 capex spenders are spending more than double that of the remaining 495 in the S&P 500

S&P 500 Capex spending…

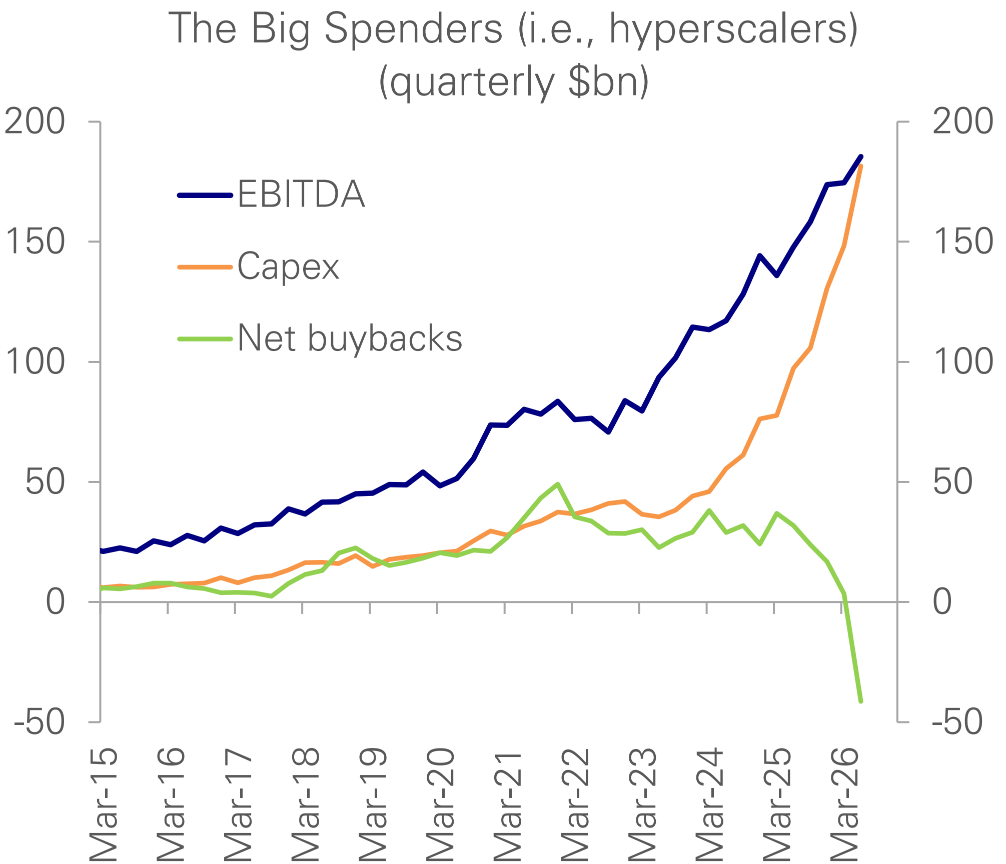




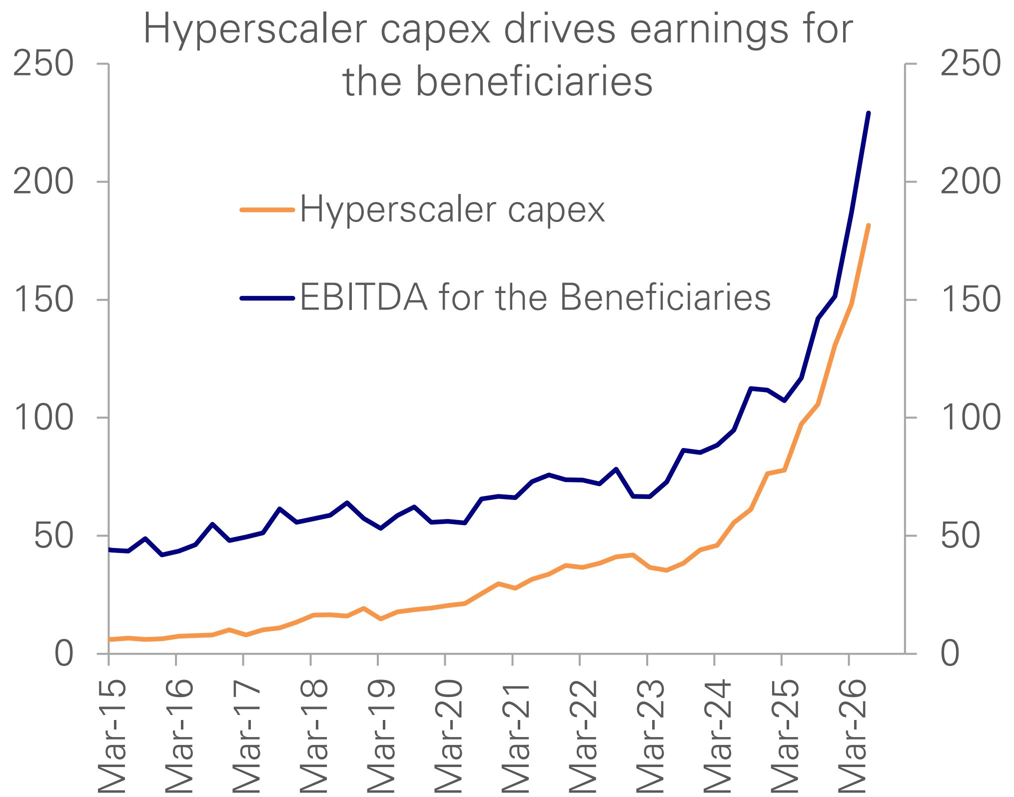
Source: Bloomberg Finance LP, Deutsche Bank Asset Allocation

Buy-backs have turned into issuance for the hyperscalers but their spending is massively helping the AI food chain…

US Hyperscaler Capex, earnings and buybacks



Hyperscalers: AMZN, GOOG, MSFT, META and ORCL



Hyperscalers AMZN, GOOG, MSFT, META and ORCL

Beneficiaries: Semis, Tech H/W & Equip., Construction & Engg., Electrical Equip., Electric Utilities, Independent Power Producers and Data Center REITs

Source: Bloomberg Finance LP, Deutsche Bank Asset Allocation

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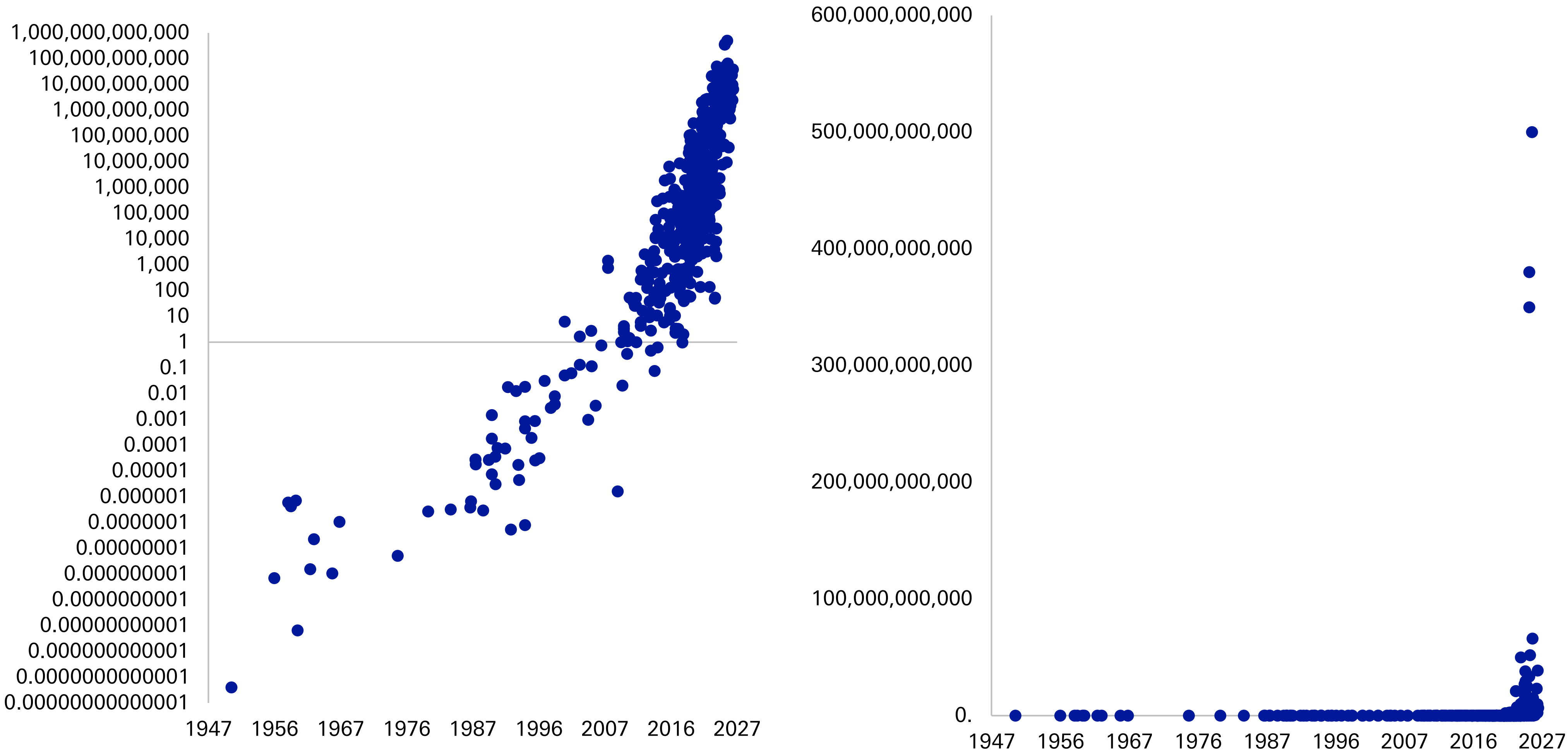
The AI train rolls on...

There is almost no doubt that computational power has exponentially increased in recent years. See Adrian Cox's excellent piece here on what 70 years of technological progress has looked like since AI was arguably born out of the Dartmouth Summer Research Project back in 1956

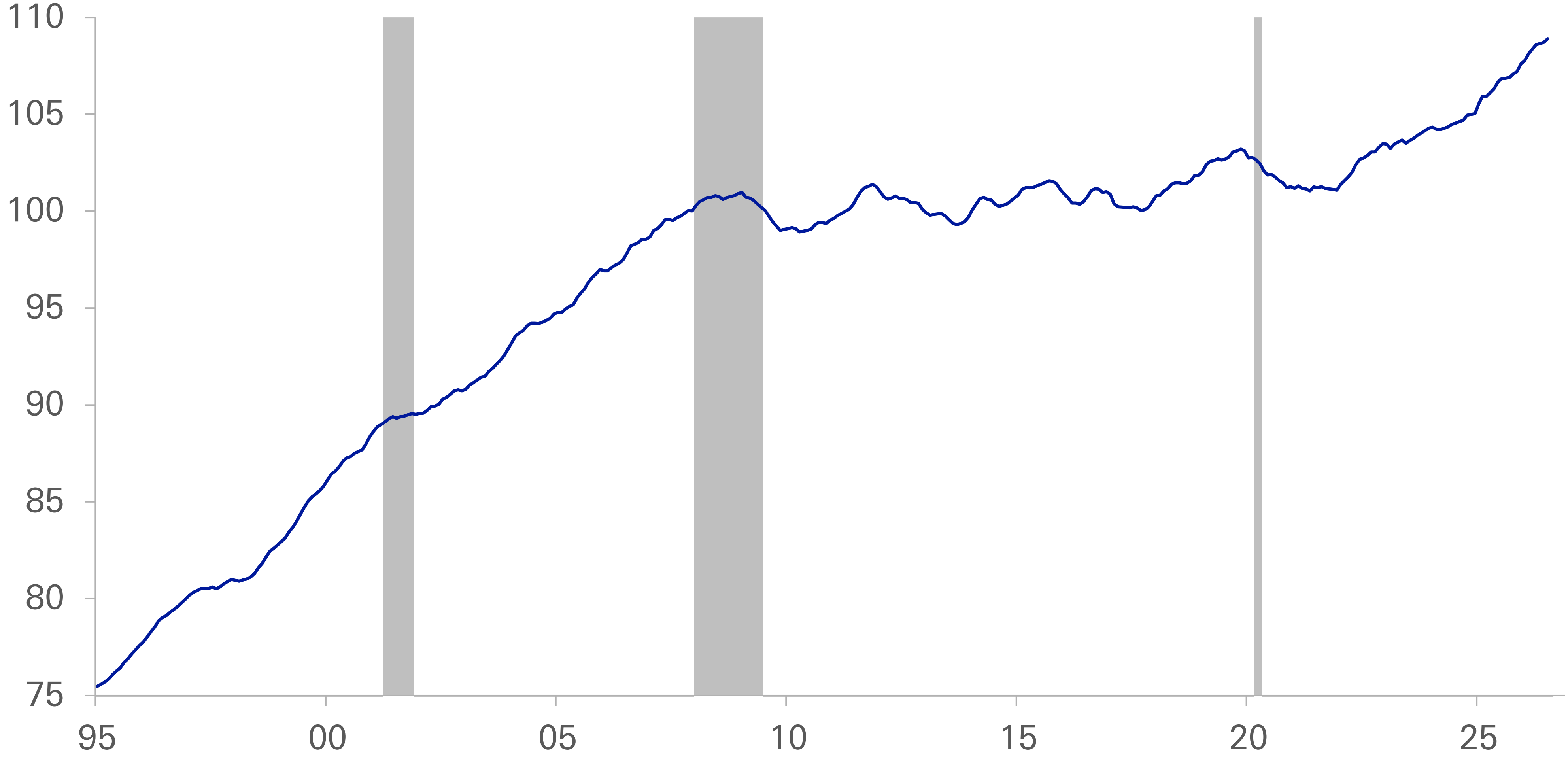
Computation used to train notable AI systems (petaFLOP): log scale (left) and Linear scale (right)



Source: Epoch AI (citing estimates from AI literature), Our World in Data, Deutsche Bank Research. Note: One FLOP (floating-point operation) represents a single arithmetic operation using floating point numbers; one petaFLOPis one quadrillion FLOPs

This exponential growth continues to drive demand for energy after a decade of stagnant demand…

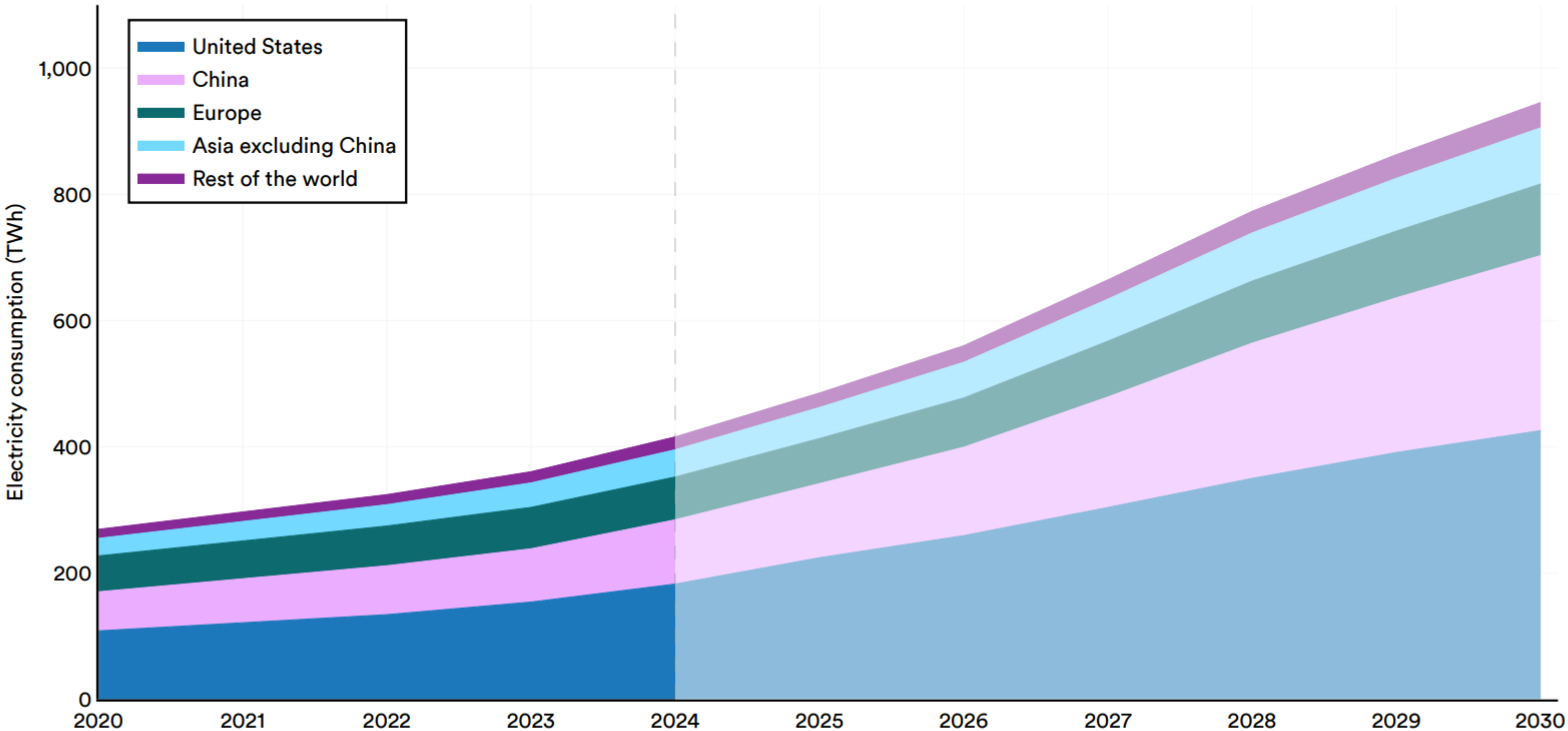
IP: Electric Power Generation, Transmission and Distribution , 24-month Moving Average



Source: FRB, Haver, Deutsche Bank

There is little sign that energy demand is going to wane...

Data center electricity consumption by region, 2020–30



Source: International Energy Agency (2025), Energy and AI, IEA, Paris | Chart: 2026 AI Index report, Deutsche Bank

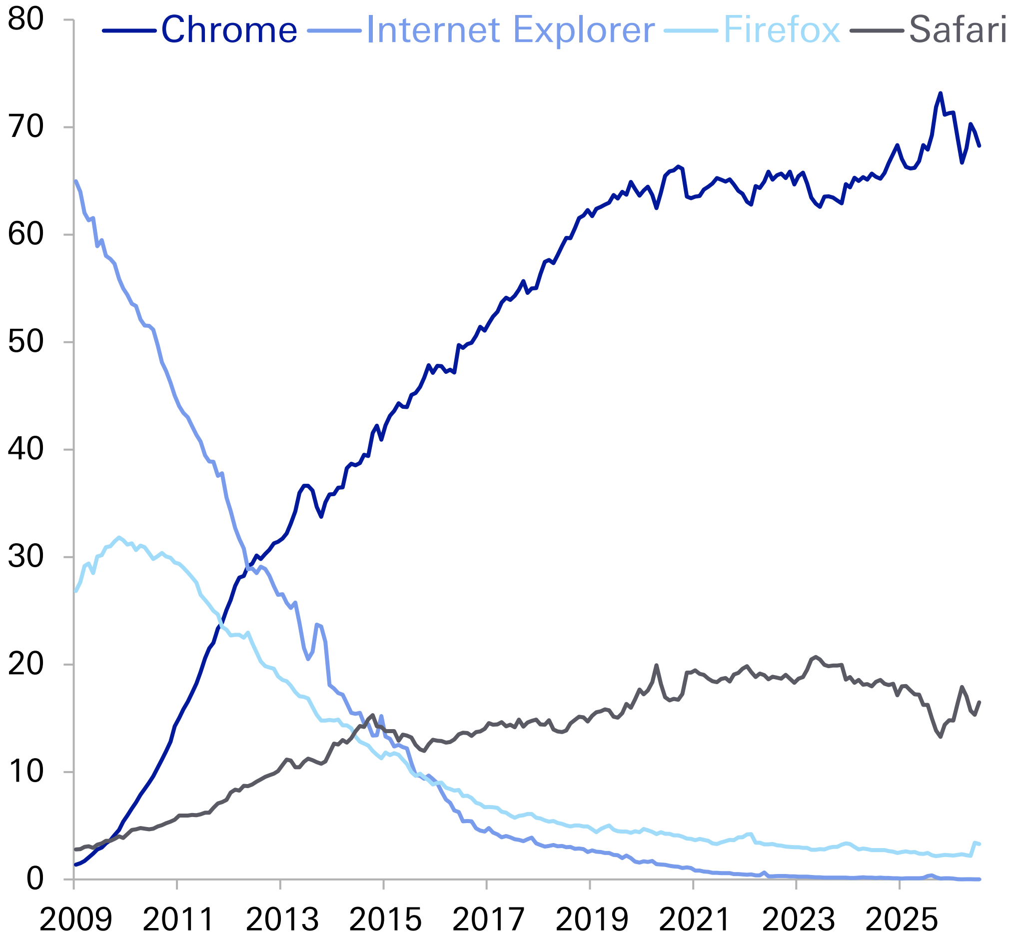
Token costs are collapsing again amid cheaper compute, more efficient systems and pricing pressure from cheaper open-weight models. Lower prices and more sophisticated uses are fuelling adoption, even if the economics of some of the expensive frontier models may be tested

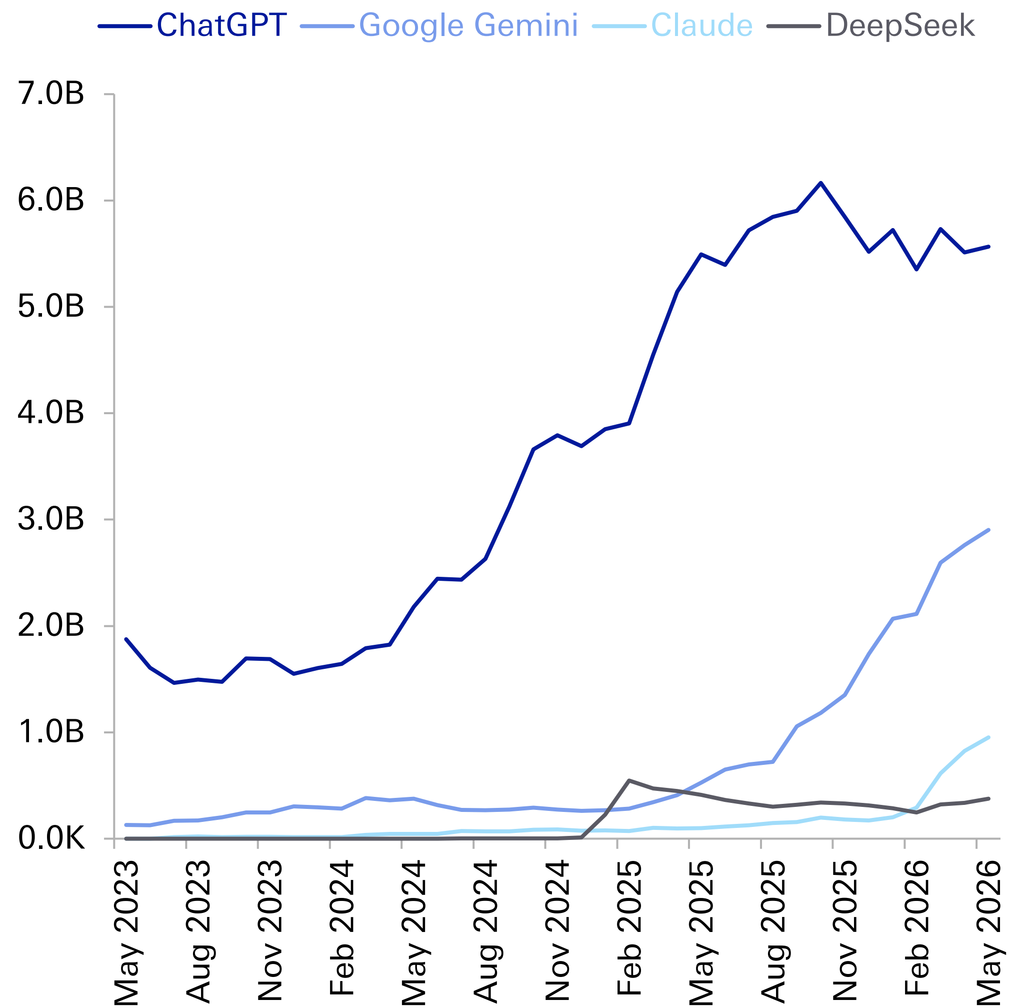
Silicon Data LLM Token Expenditure Index

Source: Bloomberg Finance LP, Deutsche Bank, Last update Sep 7

Remember the early winners don't always end up on top….

Browser market shares (%) (2009 to today) (right) and Top four generative AI platforms: monthly visits worldwide (desktop and mobile) (left)





Source: Similarweb, Deutsche Bank

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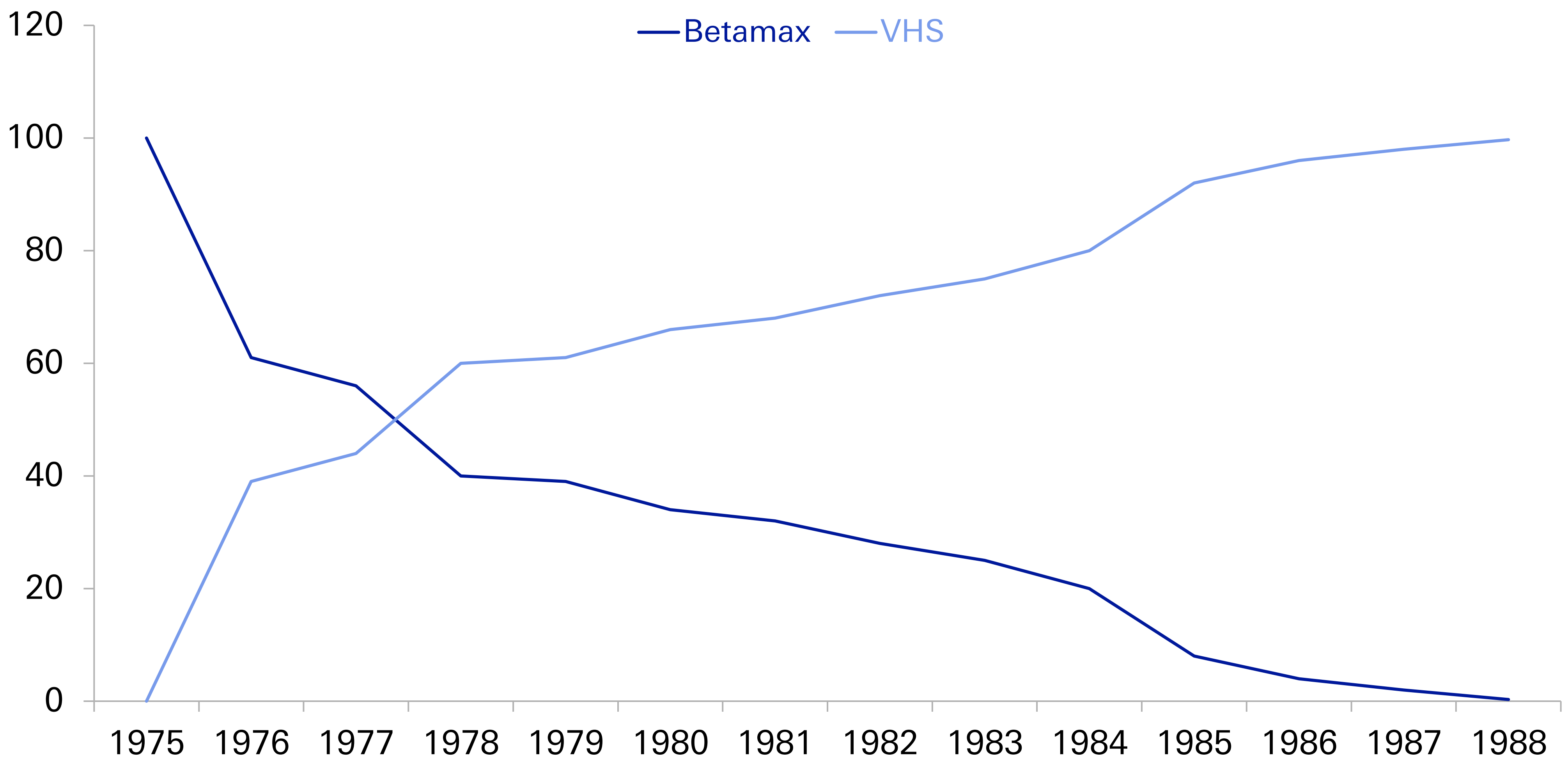
Research Institute

My favourite historical example of why winning early—and even having the better product—isn't always an advantage…

Betamax vs VHS market shares as proportion of annual production



Source: Strategic Maneuvering and Mass-Market Dynamics (Cusumano, Mylonadis, Rosenbloom, 1992), Deutsche Bank Research

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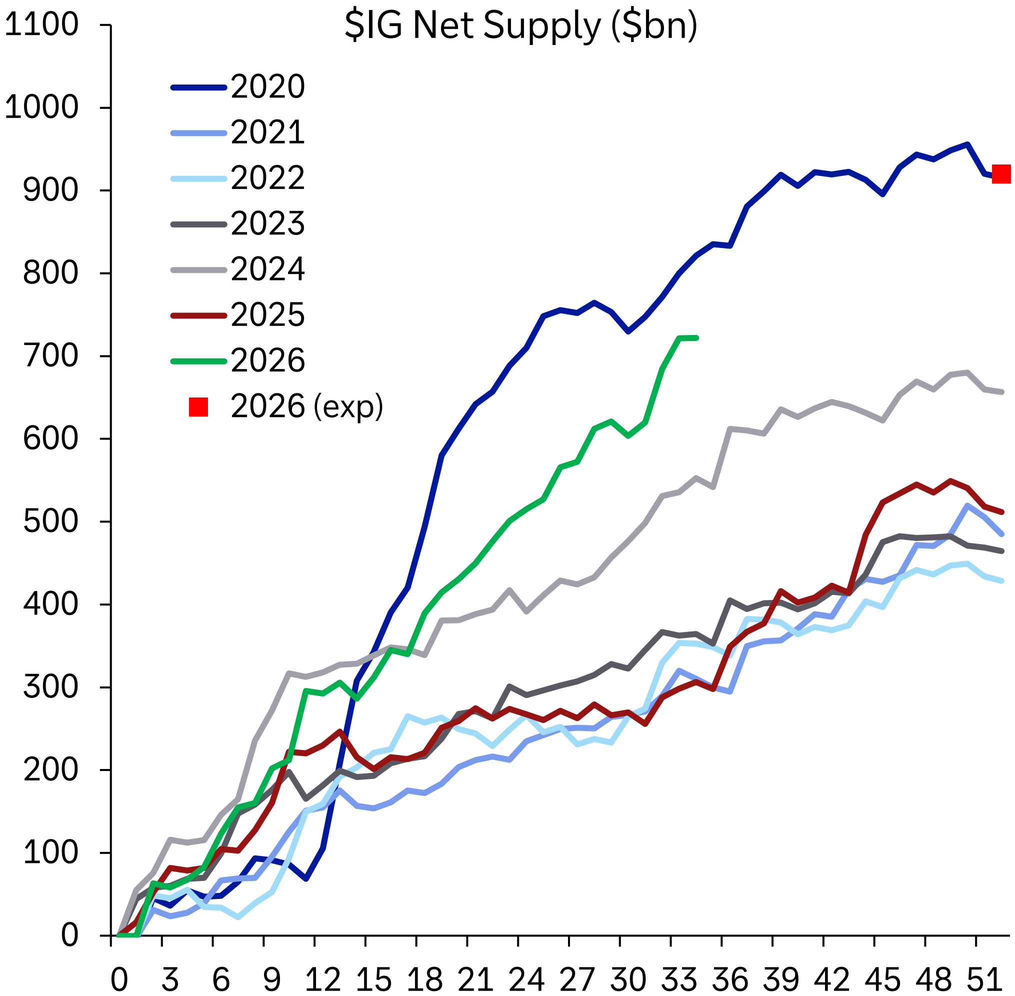
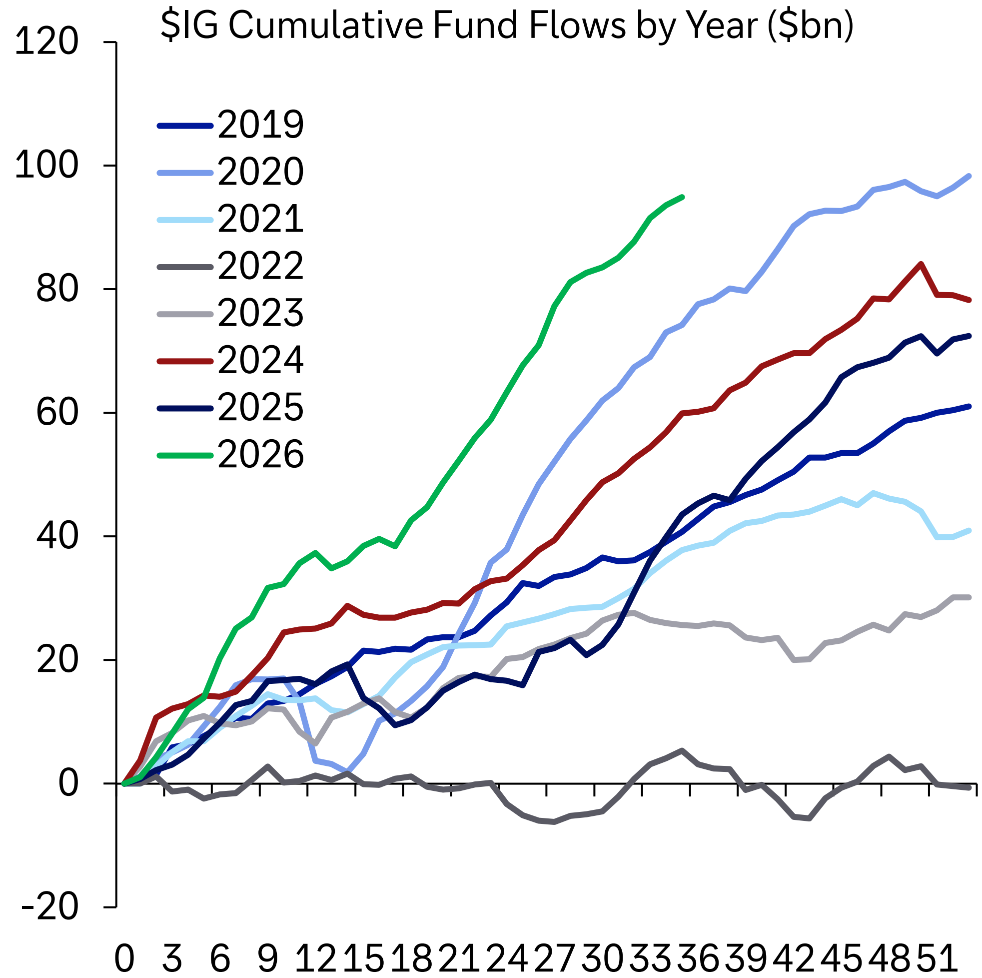
Technology—especially hyperscaler issuance—is helping put 2026 on course to surpass 2000 as the record year for US IG corporate net supply. However demand is also very high.

US IG Corporate Net Supply is likely to be the highest on record in 2026, but demand is also likely to be at a record…

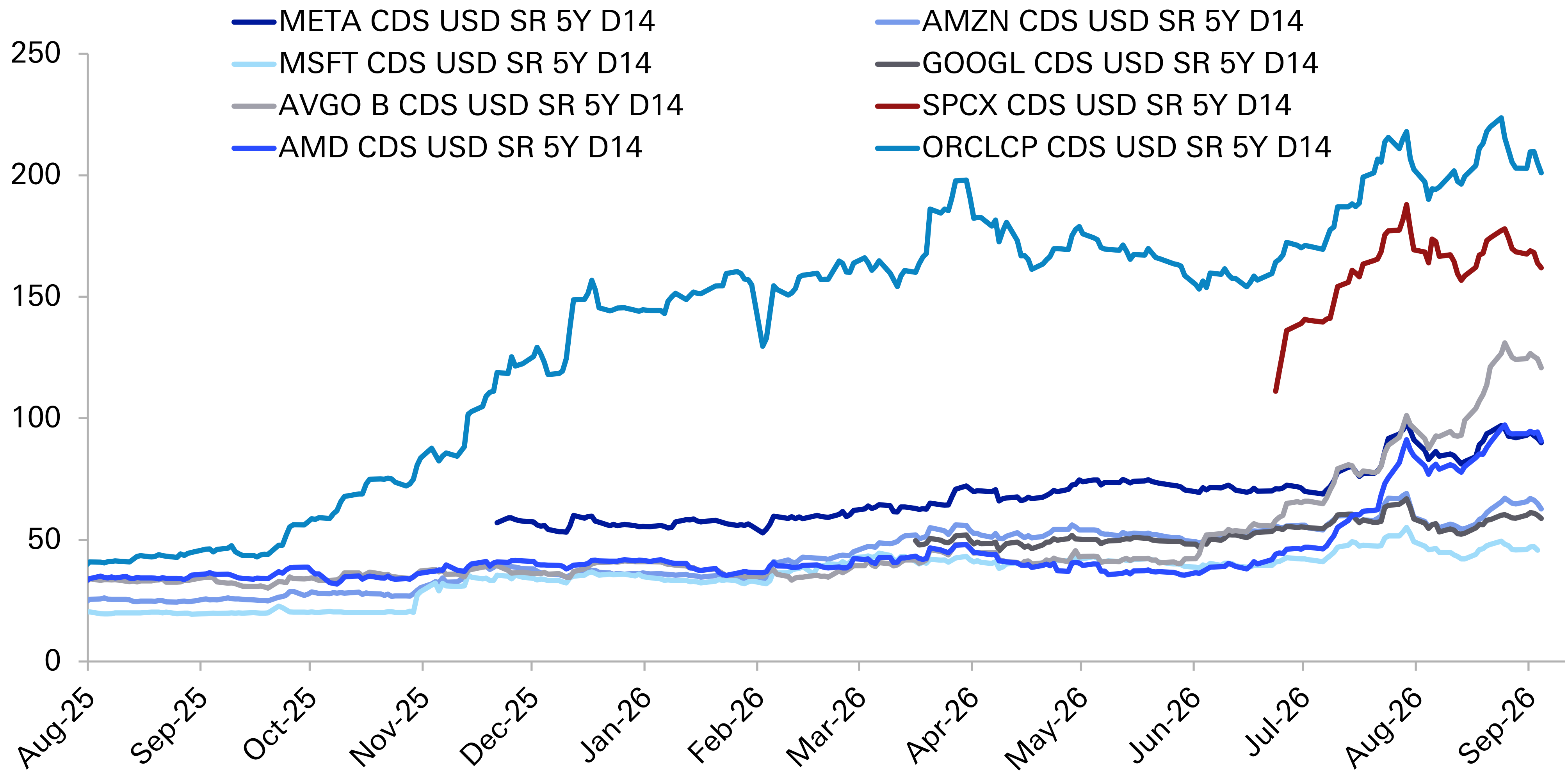




Source : EPFR, Bloomberg Finance LP, Deutsche Bank,

Hyperscaler (and related) CDS is climbing partly due to supply and increasing Capex but also as a hedge for all things AI-related so you have to be slightly careful in overinterpreting the moves...

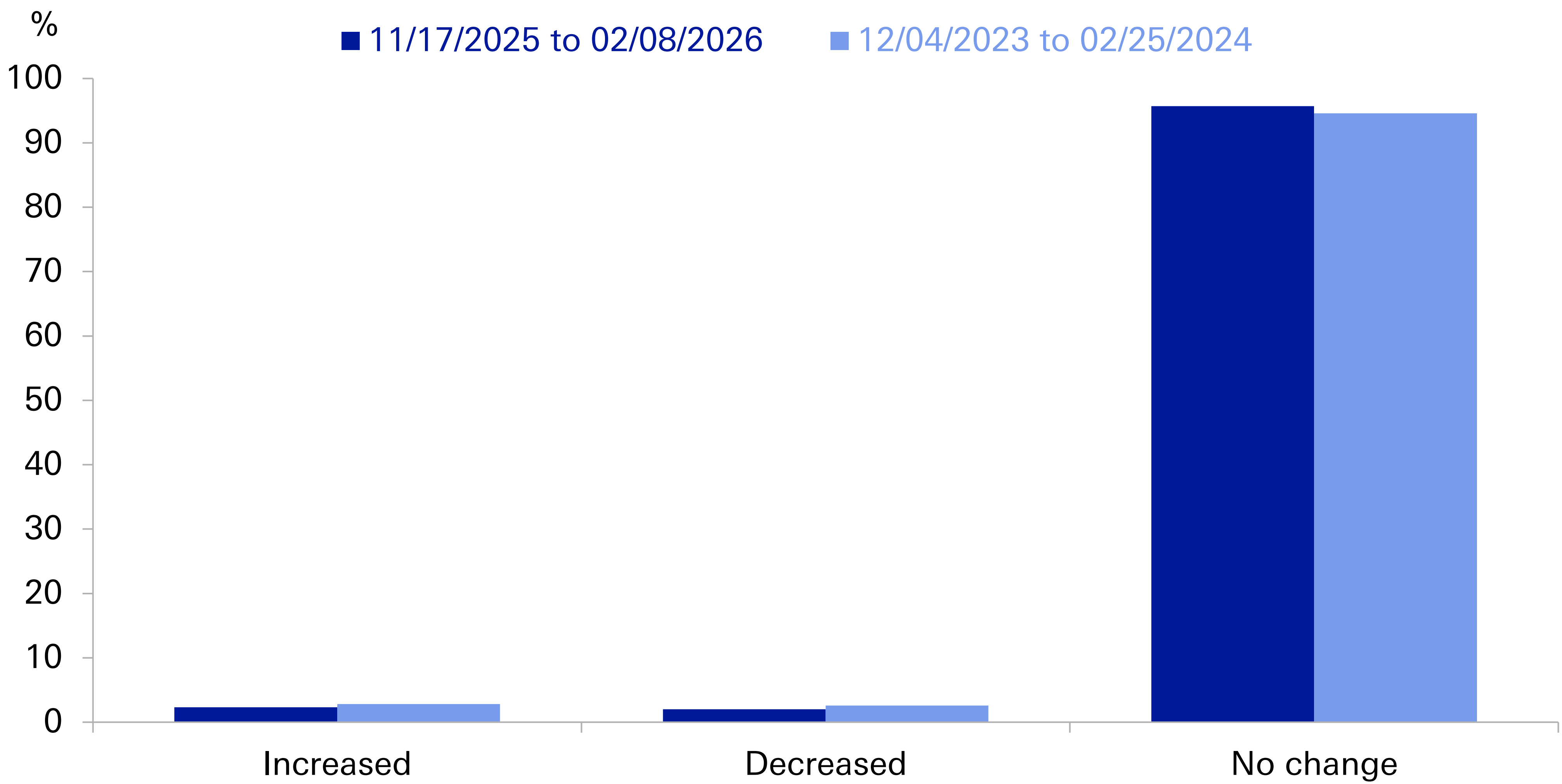
Hyperscaler CDS



Source: Bloomberg Finance LP, Deutsche Bank, Last update Sep 7

While AI adoption grows, a significant percentage of enterprises have not altered their workforce size as a direct result. We're still a long way from a revolution...

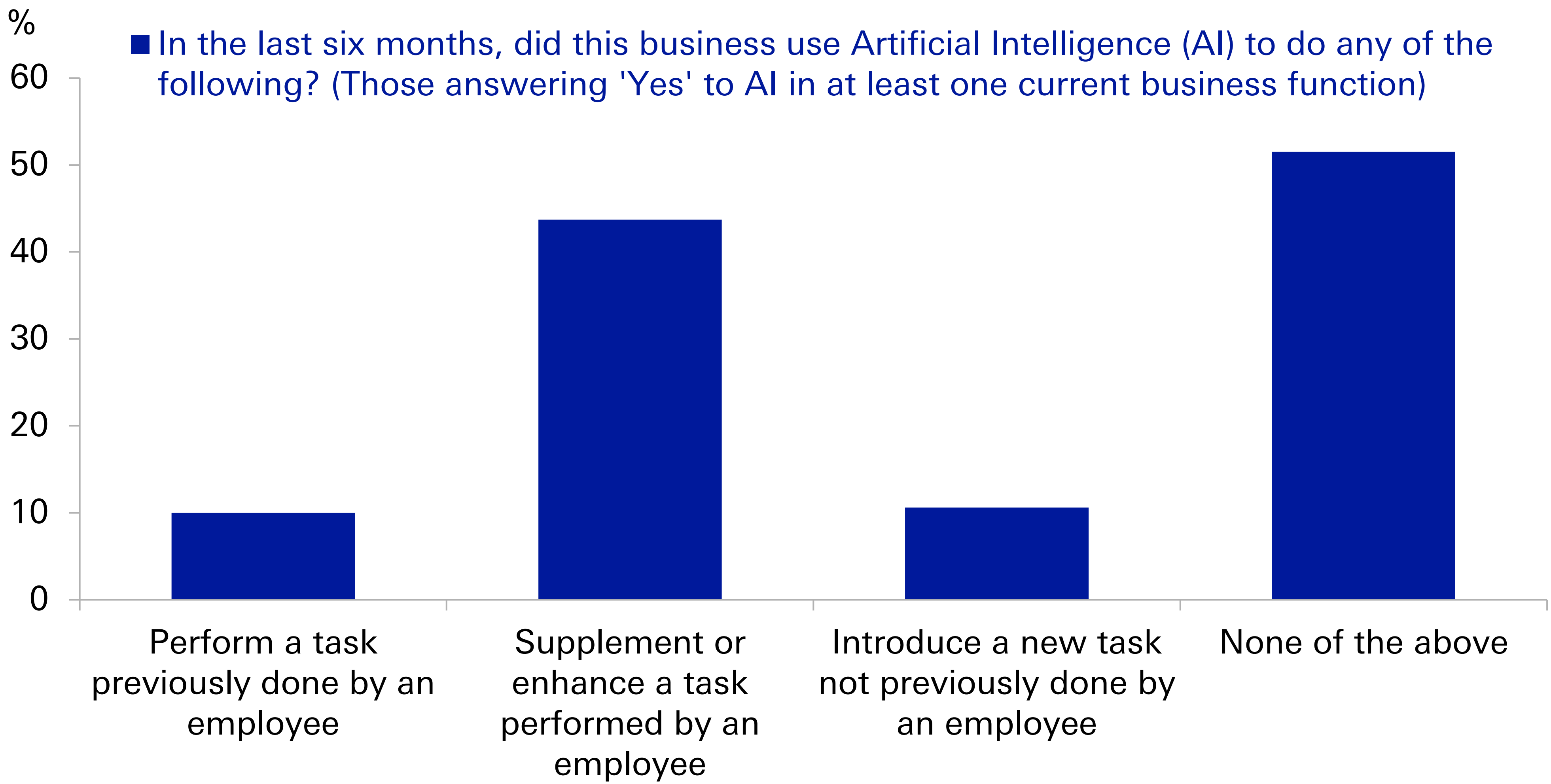
In last 6 months, how did use of AI affect business employment?



Source: BTOS, Census, Deutsche Bank

Companies adopting AI currently utilise it mainly to augment and enhance their employees' existing roles.

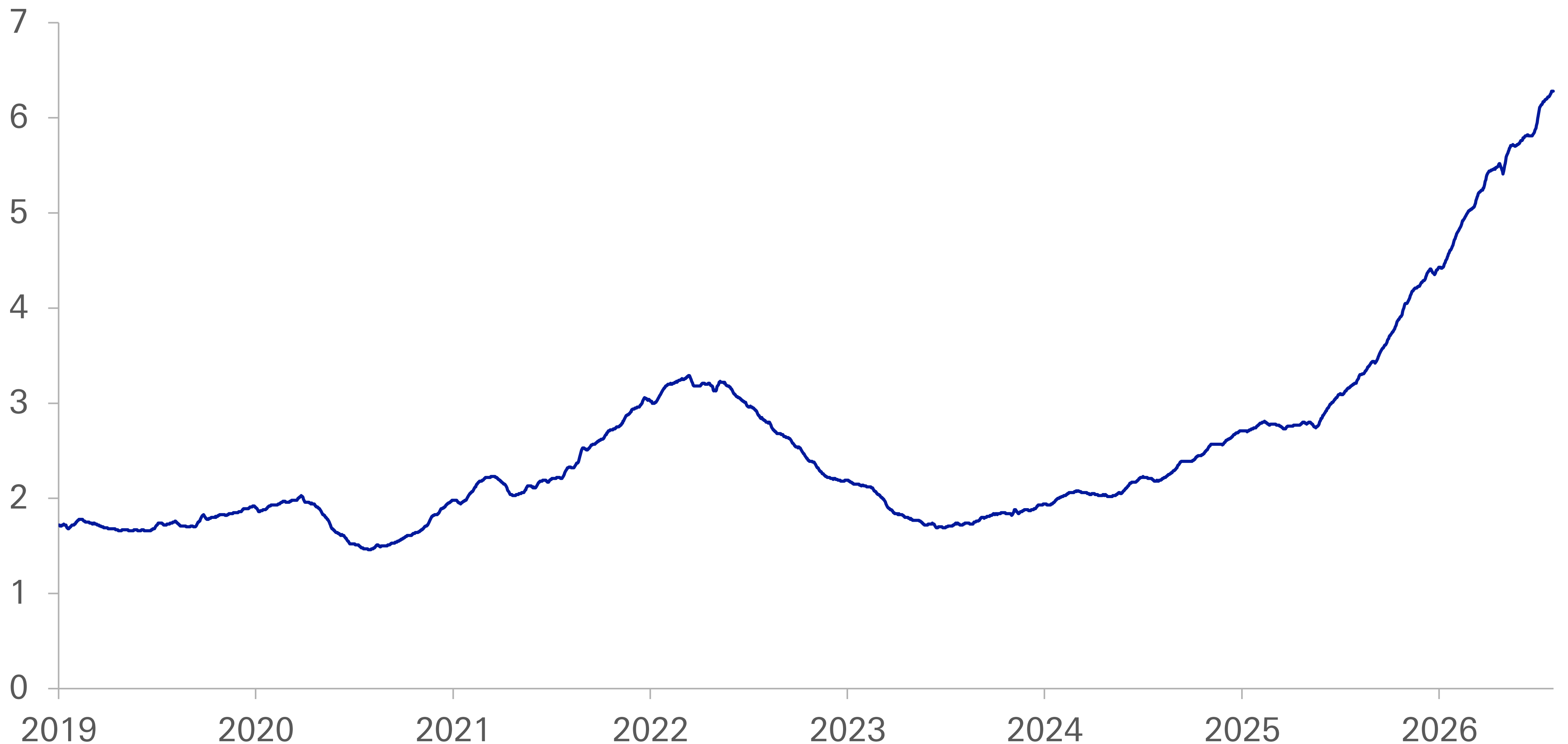
In the last 6 months, did this business use AI to do any of the following?



Source: BTOS, Census, Deutsche Bank

AI-related job postings have increased notably year-over-year in the US

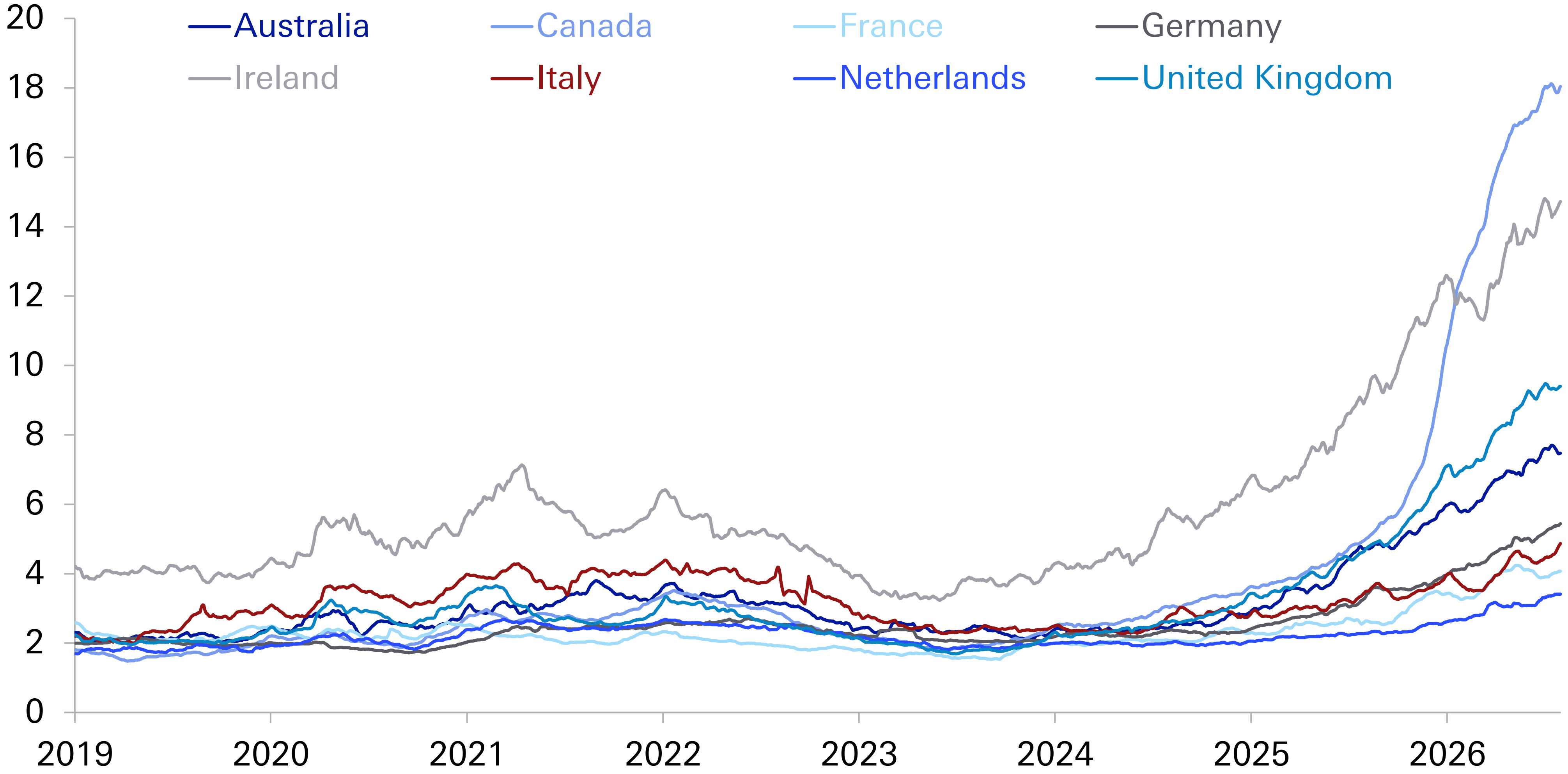
Indeed AI Tracker: Share (%) of job postings on Indeed containing Artificial Intelligence (AI) terms in United States



Source: Indeed Hiring Lab, Deutsche Bank

The share of job postings referencing AI is rising across countries. Is AI actually creating job openings rather than seeing them disappear?

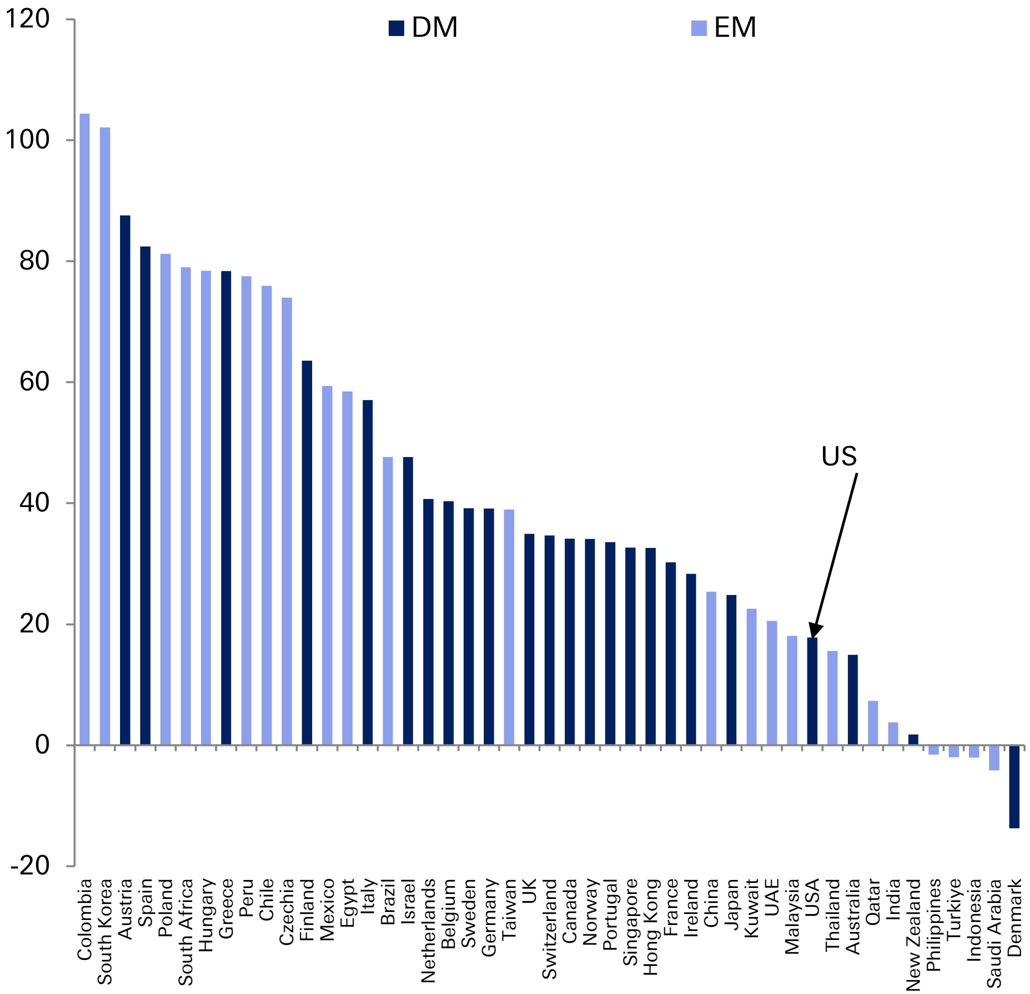
Indeed AI Tracker: Share (%) of job postings on Indeed containing Artificial Intelligence (AI) terms

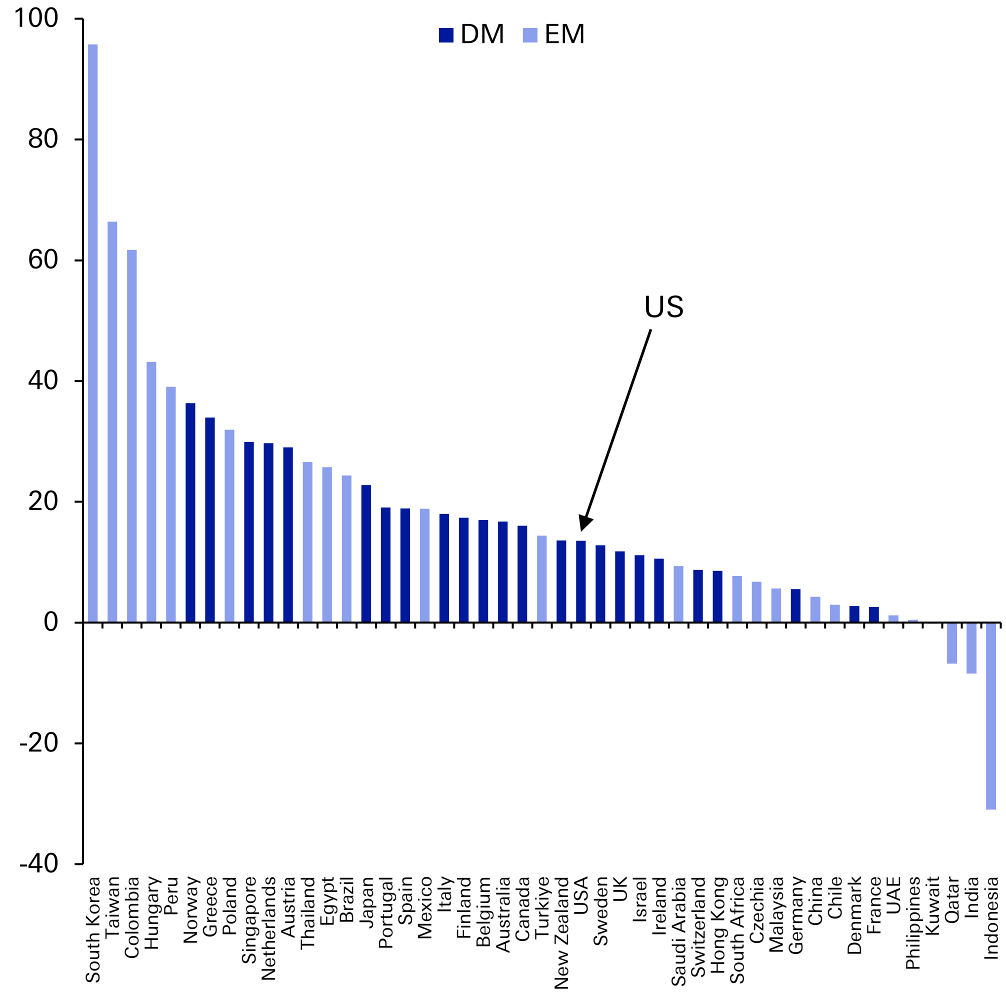


Source: Indeed Hiring Lab, Deutsche Bank

Global equity leadership has changed over the last two years as the AI cycle matures. The US has had two decent years but is in the middle of the global pack in 2026, after being around the bottom quartile in 2025…

Bloomberg large/mid-cap country stock market indices: 2025 total return in USD (%) (left) and 2026 YTD (right)

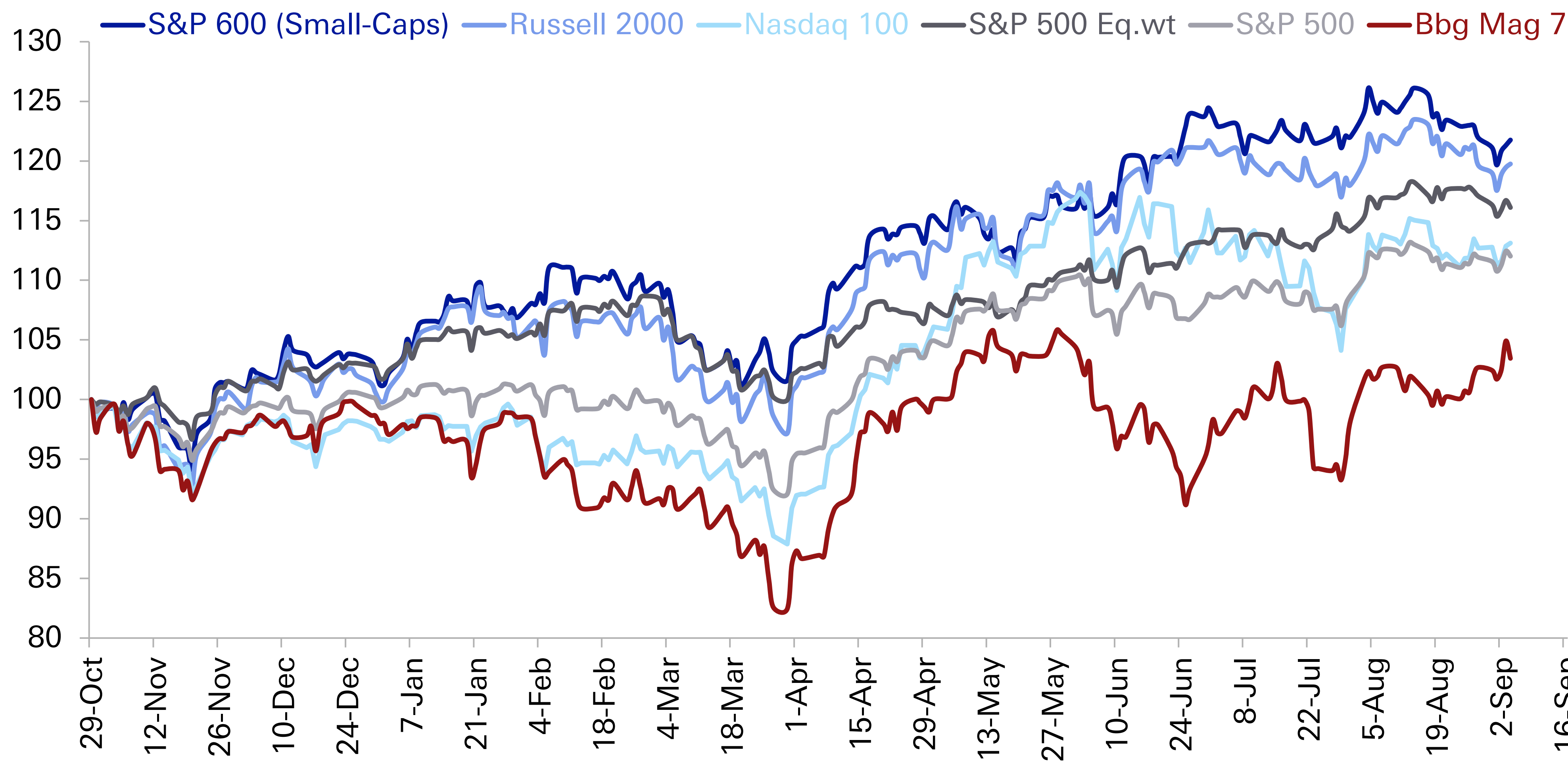




Source: Bloomberg Finance LP, Deutsche Bank, Note: 2026 YTD is updated through Sep 7

Since the end of last October, the Mag-7 have notably underperformed and are up less than 5%. However, other parts of the US market have performed strongly.

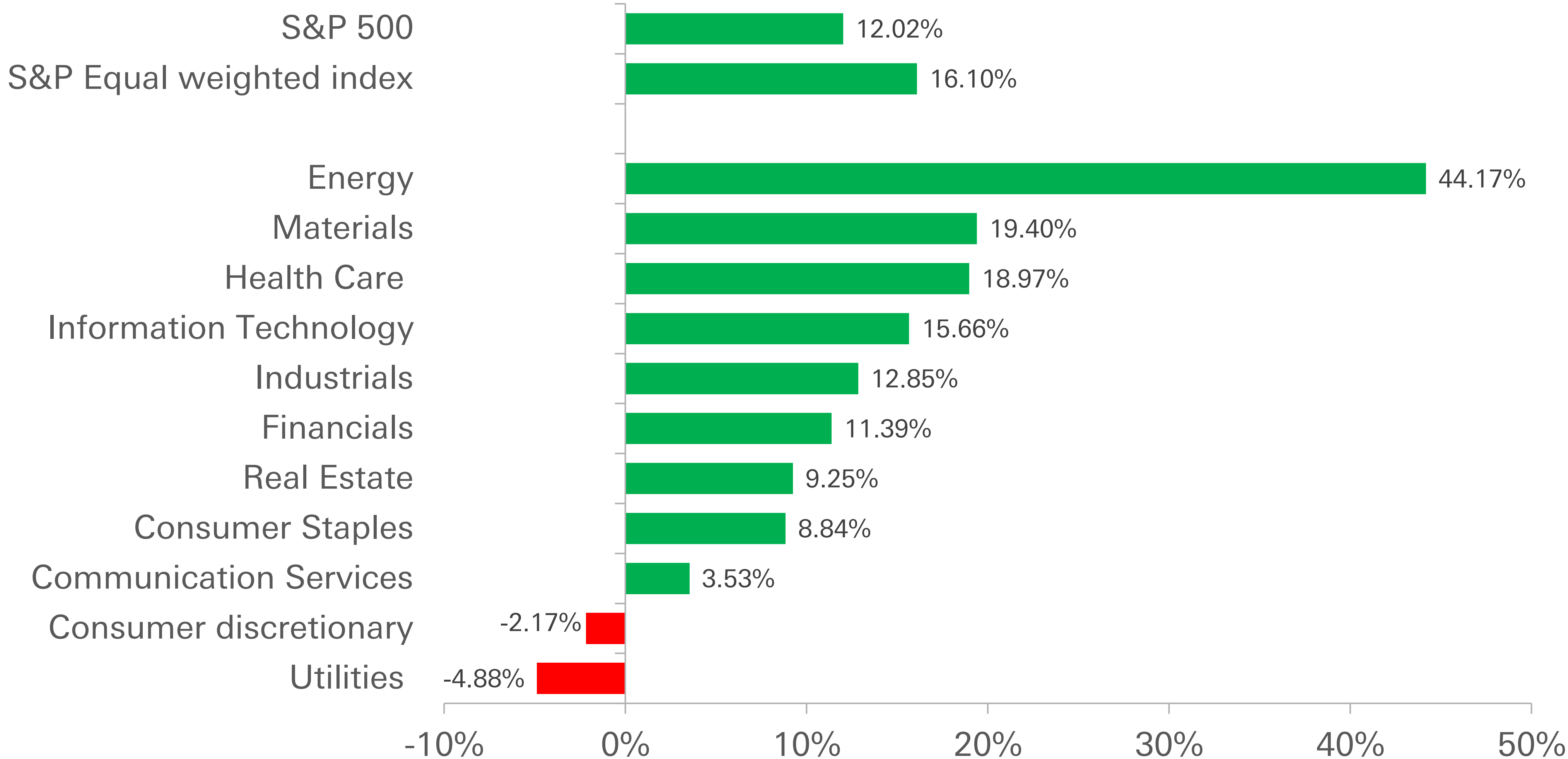
Rotation away from large cap tech. US Index performance (Oct 29,2025=100)



Source: Bloomberg Finance LP, Deutsche Bank., Last update Sep 7

Even with the Mag-7 underperforming, tech has performed in line with the market since tech started to see winners and losers emerge at the end of October last year. But tech has been outpaced by Energy, Materials and Health Care. The equal weight S&P 500 has outperformed.

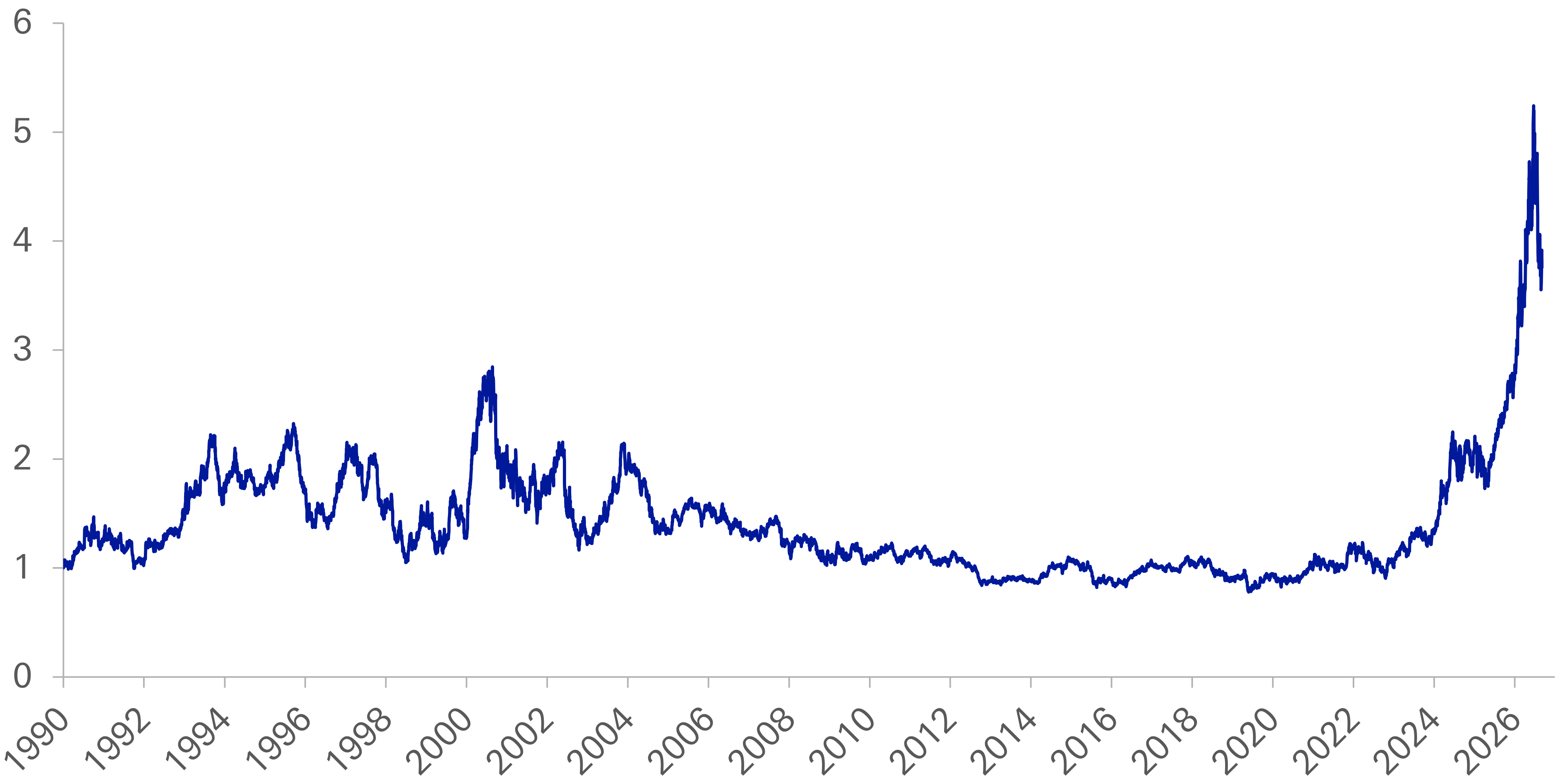
S&P Sectors return since October 29, 2025



Source : Bloomberg Finance LP, Deutsche Bank., Last update : Sep 7

The tech winners and laggards theme can best be summed up in this chart… both are sizable sub-components within the tech index… Since the end of June software and services have made a comeback relative to semis but the major underperformance over the past 18 months is clear …

S&P 500 semiconductors & equipment relative to software & services, total returns ratio, since 1990 (=1)

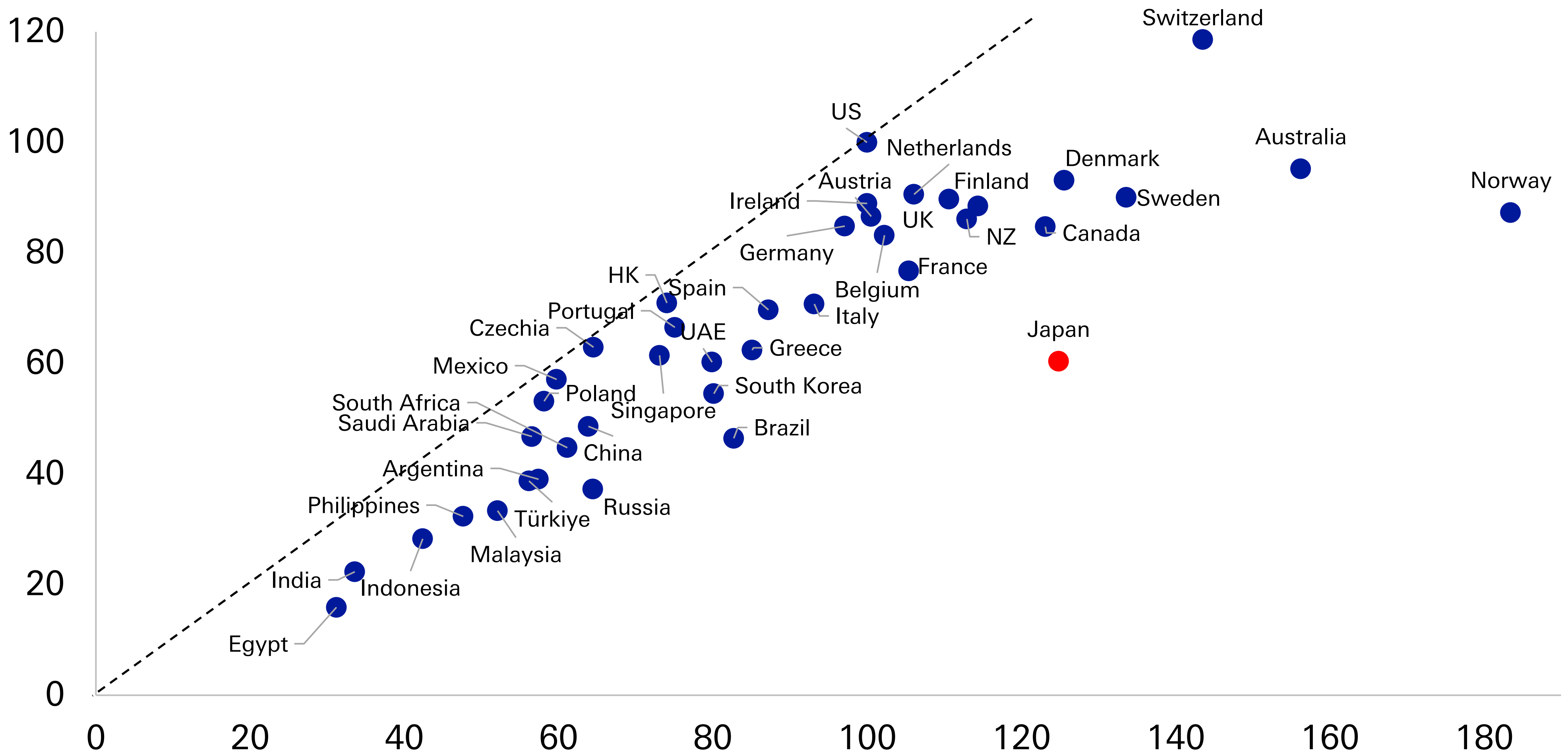


Source: Bloomberg Finance LP, Deutsche Bank, Last update: Sep 7.

Japan is worth a watch…

Japan has cheapened up extraordinarily since the early 2010s....

Relative Price Levels as Implied by PPP (US = 100), 2012 (x-axis) and 2025 (y-axis)



Source : IMF, WEO, Haver Analytics, Bloomberg Finance LP, Deutsche Bank calculations; Note: The PPP conversion rates as published by the IMF have been adjusted with actual foreign exchange rates (as on 31 December each year) to derive the implied price levels. Also note that some of the above numbers may not match those published last year exactly due to data revisions.

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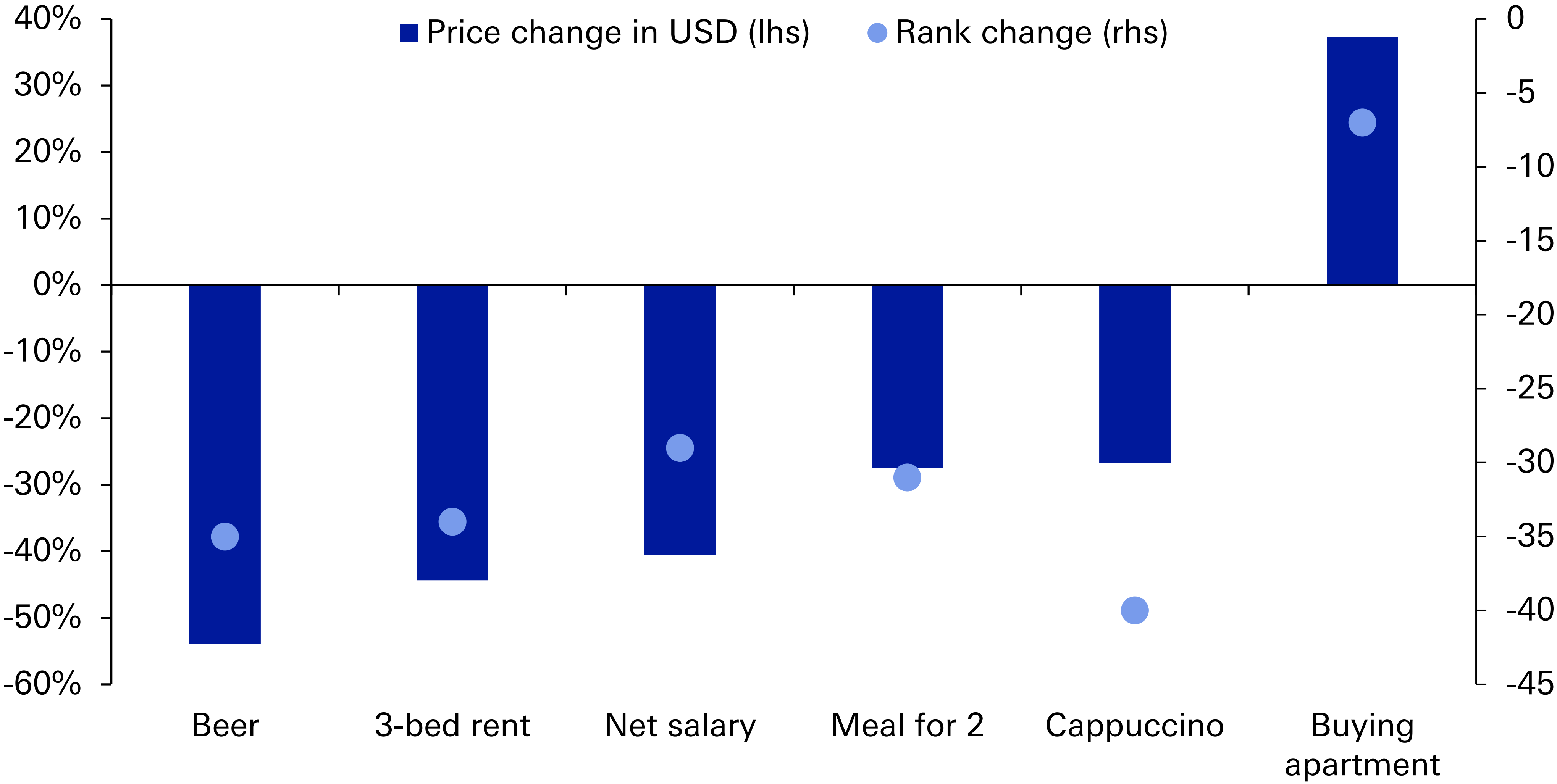
Is Tokyo the cheapest city in the world relative to its economic prowess? Maybe see you there for next year's holiday… its very cheap… See Mapping the World's Prices 2026 here for more evidence

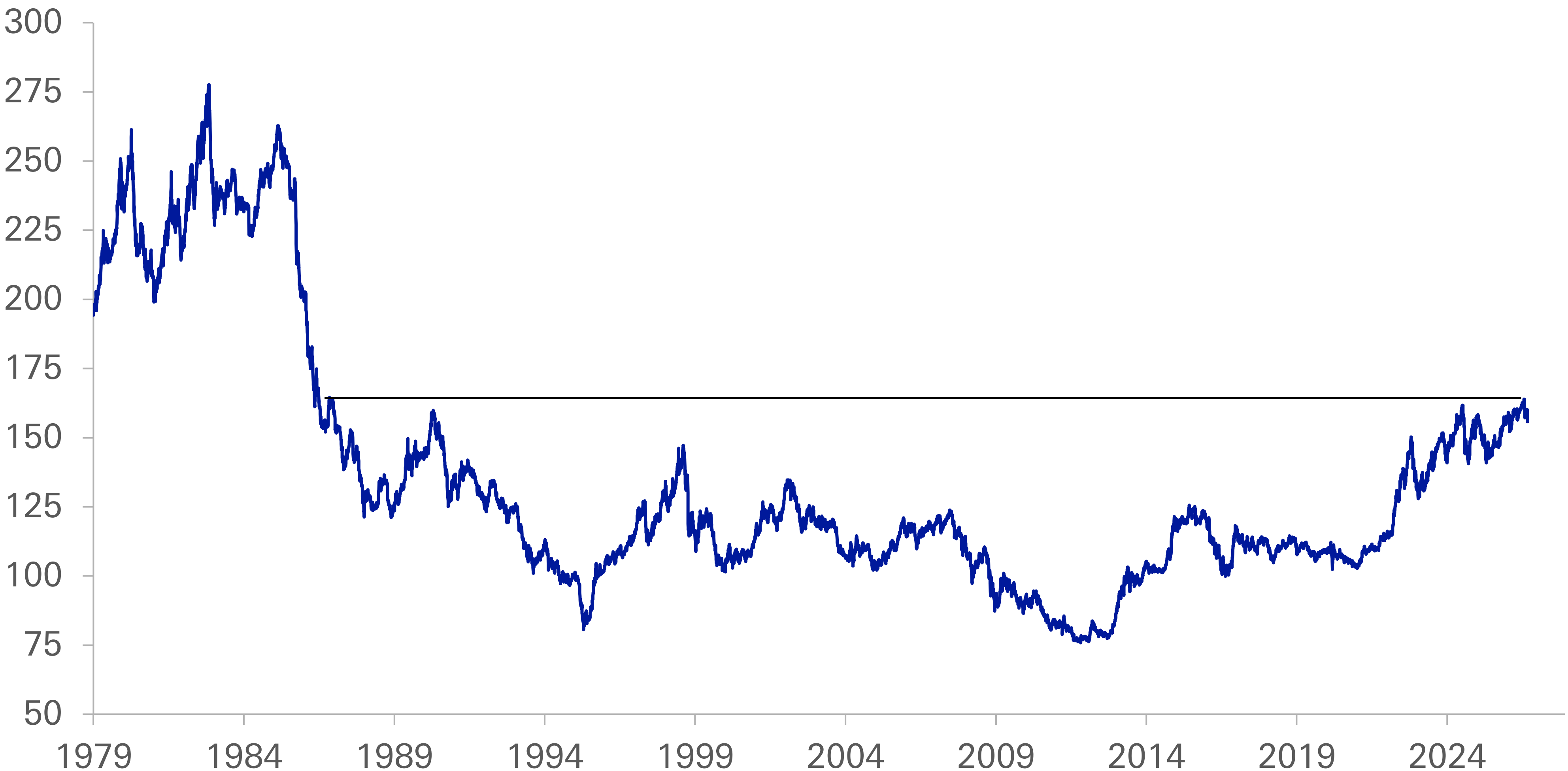
Changes in prices of goods and services in Tokyo relative to 2012 in USDs



Source : www.numbeo.com, Deutsche Bank

The Yen is bouncing off 40-year lows…

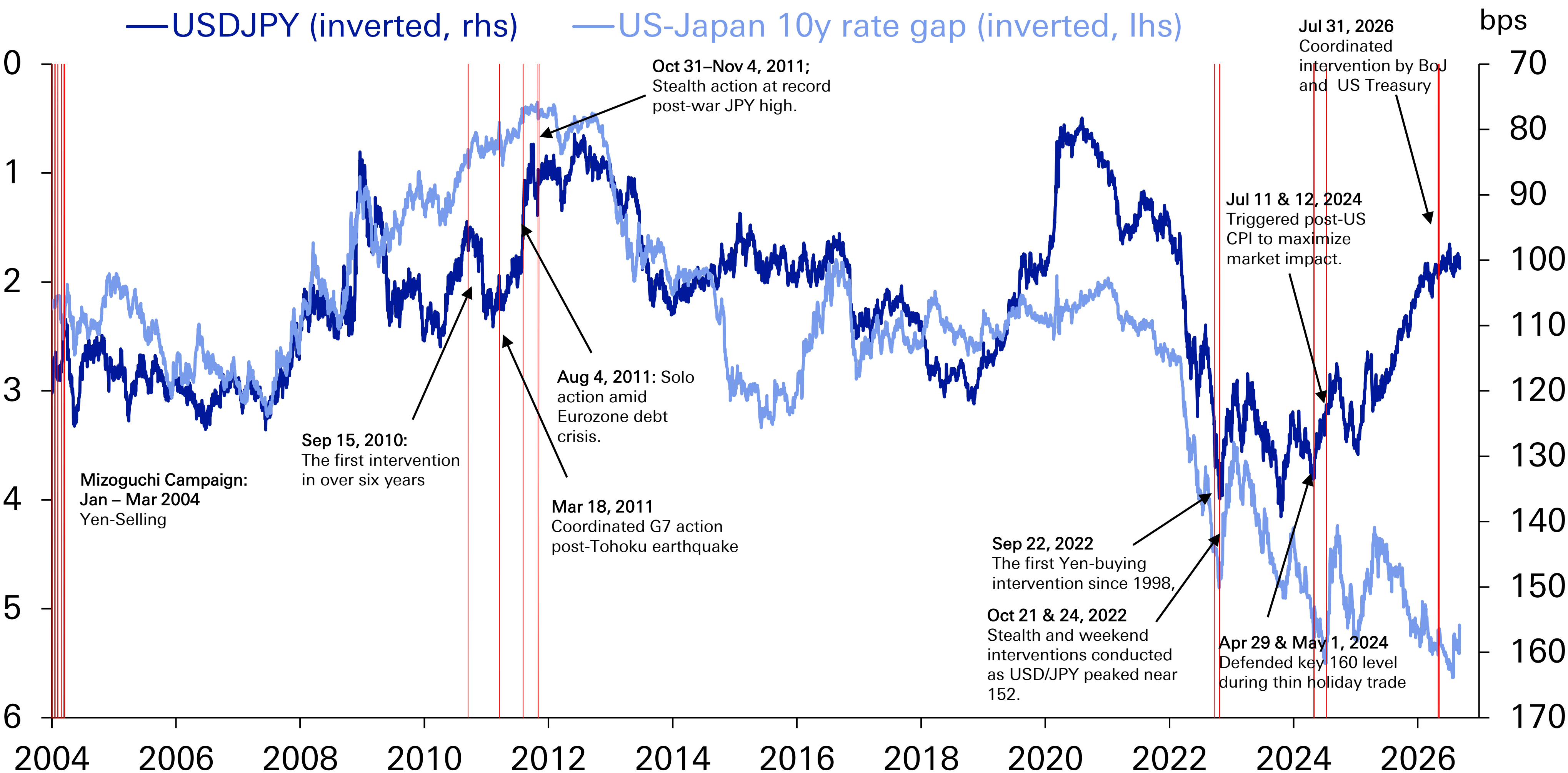
USDJPY Spot Exchange Rate - Price of 1 USD in JPY



Source: Bloomberg Finance, Deutsche Bank; Last update: Sep 7

Since early 2025, the Yen has decoupled from its traditional anchor: interest rate differentials, compressing yield gaps have failed to spark JPY strength... The BoJ is the most likely source of a sustainable rally

USD/JPY and 10y spread with BoJ intervention episodes annotated (inverted axis)



Source: Bloomberg Finance LP, Deutsche Bank, Last update Sep 7

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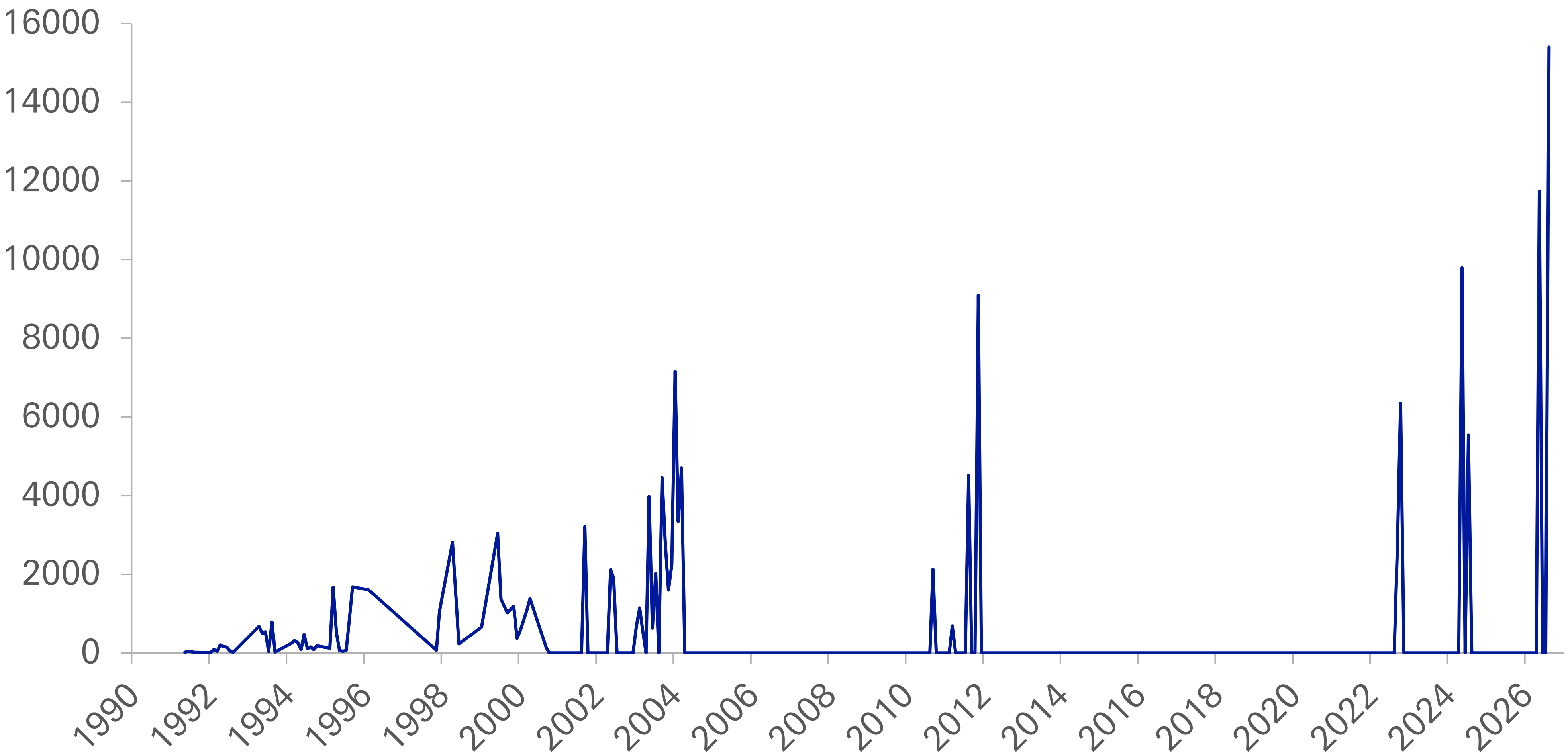
Japan spent ¥15.4tn on market intervention from April to August—the most since 1991

BOJ Japan Foreign Exchange Intervention Operations - Total Amount (JPY bil.)



Source: Bloomberg Finance LP, Deutsche Bank, Last update: Sep 7

Appendix 1

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