

## US Rates Strategy Weekly

September 18, 2026

Joseph Abate, US Rates Strategy  
[joseph.abate@smbcnikko-si.com](mailto:joseph.abate@smbcnikko-si.com)  
1 212 893-1592

Monty Gandhi, US Rates Strategy  
[mgandhi@smbc-cm.com](mailto:mgandhi@smbc-cm.com)  
1 212 224-5114

Troy Ludtka, US Economics  
[troy.ludtka@smbcnikko-si.com](mailto:troy.ludtka@smbcnikko-si.com)  
1 212-224-5483

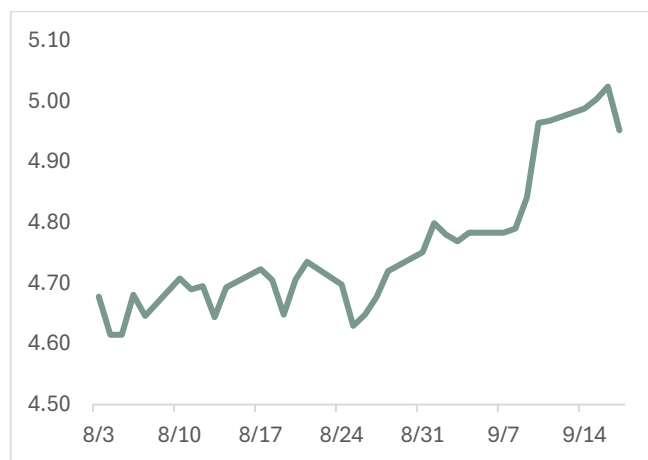
- **Ironically, the path to lower term interest rates may be through higher short-term rates.** The increase in 10y yields since Jackson Hole likely reflects growth expectations more than term supply. Term premium fell about 10-15bp after the buyback announcement. But the effect on 10y rates was offset by the hawkish Jackson Hole speech.
- The increase in the fed funds rate, a more hawkish reaction function and Warsh's reference to "dose" removal were not enough to lower 10y yields this week. **Instead, the Fed may need to narrow the 50bp gap between where the market is pricing the terminal fed funds rate and its median 2027 dot.**
- **We are skeptical that the Treasury will move more aggressively to bring term rates lower – at least in the near-term.** In theory, it might be able to amp up the size of its bill issuance and use the extra cash raised to buy back vintage term debt.
- **But suddenly cutting the issuance of longer-maturity securities to twist the yield curve is not something the Treasury would undertake lightly.** And while we expect bill issuance to increase next year, we look for the bill/debt ratio to remain below 23%. It is not clear that the Treasury will find it as cheap to issue more bills at 25% of outstanding debt as it has at 22%.
- In the unlikely event that the Treasury takes actions to reduce net supply, it could help catalyze a short-term duration positioning unwind, particularly in the long-end. However, the scale of benchmark-related demand tied to the 10-year sector suggests that a non-fundamental rally would face offsetting flows over time.
- **We look for new home sales to increase 0.3% m/m in August.** New home sales have trended sideways since 2017. Because the supply of new homes has been strong, median prices have fallen below median existing home prices for the first time

## Lowering yields

**Ironically, the path to lower term interest rates may be through higher short-term rates.** We thought that by delivering the expected rate hike, the Fed would convince the market enough of its inflation-fighting *bona fides* to bring 10y yields lower. And while yields fell a few basis points since the FOMC meeting, they remain above their August level (Figure 1).

This week, Chair Warsh identified three reasons behind the backup in 10y yields: geopolitics, corporate debt issuance and growth expectations. These effects are overlapping and time varying. The earliest and most consistent (geopolitics) began with the Iran conflict and the increase in oil prices since March. Oil prices cooled in June but have increased in recent weeks as the conflict has intensified. We think corporate debt issuance may account for some – perhaps 10-15bp – of the increase in term rates since March (about 10-15%). However, since issuance was relatively slow in August, our sense is that most of the 28bp increase in 10y yields since August 18 is growth-related.

**Figure 1: 10y yields (%)**



Source: Bloomberg, SMBC Nikko

**Figure 2: Terminal fed funds rate (%)**



Source: Bloomberg, SMBC Nikko

**Importantly, the Fed can directly influence only one of these three factors – growth expectations.** Exogenous influences like lower oil prices or falling equity prices might also pull term interest rates lower. However, we think more hawkish commentary accompanied by additional rate hikes might be more effective in reversing the 30bp increase in 10y yields since Jackson Hole. The increase in the fed funds rate, a more hawkish reaction function and Warsh's reference to "dose" removal were not enough to accomplish this. **Instead, the Fed may need to narrow the 50bp gap between where the market is pricing the terminal fed funds rate and its median 2027 dot** (Figure 2). That said, we think the FOMC may be closer to the market's terminal fed funds rate than the median dot suggests. More FOMC members look for an additional rate hike next year (8) than those expecting the funds rate to hold between 4.00-4.25% (6).<sup>1</sup>

## Listen only mode

**One issue with the Fed's new communications strategy could be a tendency for the market to wander.** Without a clearer sense of the Fed's reaction function, the market may price in too many rate hikes. Indeed, we think the market may be pricing in more hikes into expectations than FOMC members

<sup>1</sup> Four look for two or more rate cuts.

are prepared to deliver next year. A Fed that “listens” more and “speaks” less creates a dilemma when market pricing disagrees with the Fed’s. How can the Fed steer market expectations without forward guidance? Instead, the Fed must rely on the data flow to tilt market expectations closer to its views. Alternatively, as Warsh argued at Jackson Hole, the “collective wisdom” of the market provides the purest signal of the economy and rates, so policy should move closer to the market’s viewpoint.

## Supply story

**Our sense is that term higher rates reflect growth rather than supply expectations.** Term premium fell about 10-15bp after the buyback announcement. But the effect on 10y rates was offset by the hawkish Jackson Hole speech. Term premium has been rangebound this year between 70-90bp.

**We are skeptical that the Treasury will move more aggressively to bring term rates lower – at least in the near-term.** Its capacity to engineer lower rates is not as broad as the Fed’s; the Treasury must still finance a budget deficit approaching 6% of GDP annually.<sup>2</sup> Mechanically, the Treasury can adjust the maturity distribution of its outstanding debt quickly because it sells bills weekly. So, in theory, it might be able to amp up the size of its bill issuance and use the extra cash raised to buy back vintage term debt.

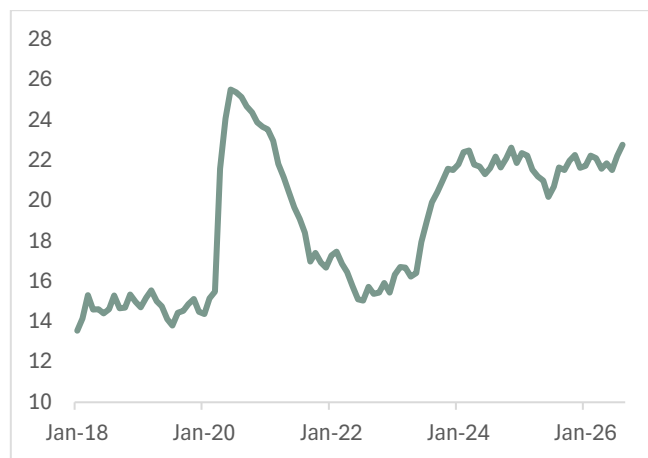
But while we expect bill issuance to increase next year, we look for the bill/debt ratio to remain below 23% - supply is expected to increase \$800bn. It is not clear that the Treasury will find it as cheap to issue more bills at 25% of outstanding debt as it has at 22% (Figure 3). The Treasury was able to increase bill issuance since 2023 without much widening in bill-OIS spreads because money fund balances increased with higher interest rates and the money that came out of non-interest-bearing bank deposits (Figure 4). We look for more moderate growth in money fund balances – around 4%/y – which might accommodate an additional \$200bn in bill demand without changes to their allocations or wider bill-OIS spreads. Money funds hold \$3.5trn in bills that are generally rolled depending on the level of overnight repo rates.

**Suddenly cutting the issuance of longer-maturity securities to twist the yield curve is not something the Treasury would undertake lightly.** The Treasury spends years interviewing investors and dealers when contemplating a new maturity. While a surprise auction adjustment would squeeze shorts and pull 10y yields lower, it would be so unexpected and contrary to the Treasury’s longstanding stated policy of regular and predictable issuance that any yield decline might be short-lived as term premium moved higher on the possibility of other, unexpected actions.

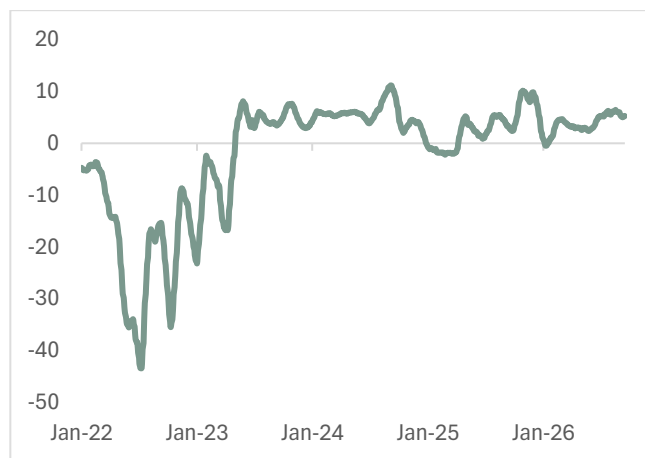
Instead, it is possible the Treasury increases the size of next week’s 20y-30y buybacks. Markets were disappointed by the size of the last operation and were instead looking for something closer to \$10bn than the \$6bn that was announced. Likewise, markets expected the Treasury would buyback the full \$6bn. **That said we don’t think a \$10bn operation would bring down 10y yields as much as say, an October rate hike.** October pricing is around 50% as markets are torn between looking for more of a rate cycle and the politics of hiking just before the mid-term election.

---

<sup>2</sup> CBO projects the deficit will approach 7% by 2036 and Treasury’s interest servicing costs rise.

**Figure 3: Bill share (% debt)**


Source: Bloomberg, SMBC Nikko

**Figure 4: 3m bill less OIS (bp)**


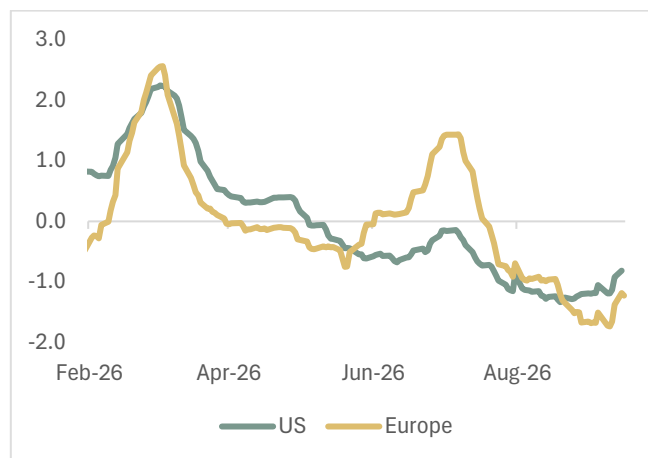
Source: Bloomberg, SMBC Nikko

### Catalyzing a position unwind?

Investors remain underweight duration globally. In theory, the Treasury can contribute to conditions that encourage a positioning unwind. Figure 5 shows that CTAs and other trend-following investors continue to hold sizable short-duration exposures. A sufficiently strong rally could trigger short covering, creating additional buying pressure. Similarly, CFTC futures data (Figure 6) show leveraged funds reducing long-end short positions. Leveraged funds maintain a structural short bias in long-end Treasury futures as part of their relative value strategies, so not all shorts represent outright bearish duration views. Yet, the elevated short positioning in 2026 suggests that broad short covering episodes could be amplified. Reducing supply, improving sentiment or increasing expectations of official sector demand, such as discussion of a sovereign wealth fund, could purchase Treasuries, could help bring such a move.

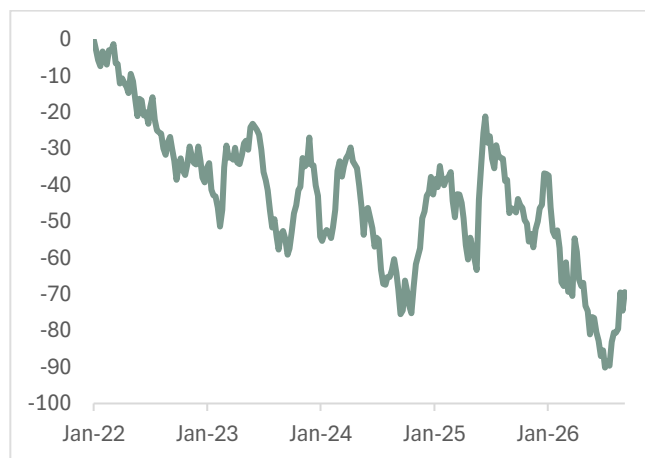
There are, however, limitations. Any attempt to influence market pricing would likely have a greater impact in the long end (10y +) than in the benchmark 10-year sector. The 10-year Treasury sits at the center of multiple markets and investor bases. Beyond traditional Treasury investors, the sector serves as a key reference point for assets linked to the Bloomberg U.S. Aggregate Bond Index, which is estimated to track roughly \$2-5 trillion in assets, as well as the approximately \$11 trillion agency MBS market. Because these investors are likely to respond more to valuations and fundamentals than to non-fundamental attempts to lower yields any rally in the 10-year sector that is perceived to be short-term would likely attract offsetting flows over time. As a result, any effort to catalyze a broad-based repositioning of investors is likely to be far more challenging in the belly (5y-10y) of the curve than at the long end.

**Figure 5:** CTA positioning in US/European rates (z score)



Source: Bloomberg, SMBC Nikko

**Figure 6:** Leveraged players net long-end futures position, (\$mm DV01 cumulative year to date)

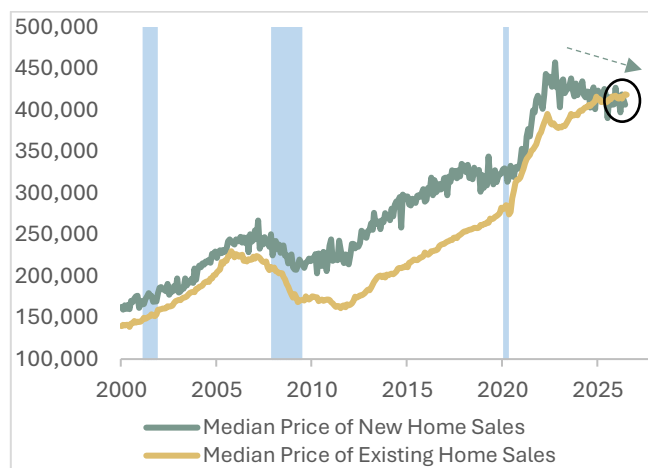


Source: CFTC, Bloomberg, SMBC Nikko

## Week ahead

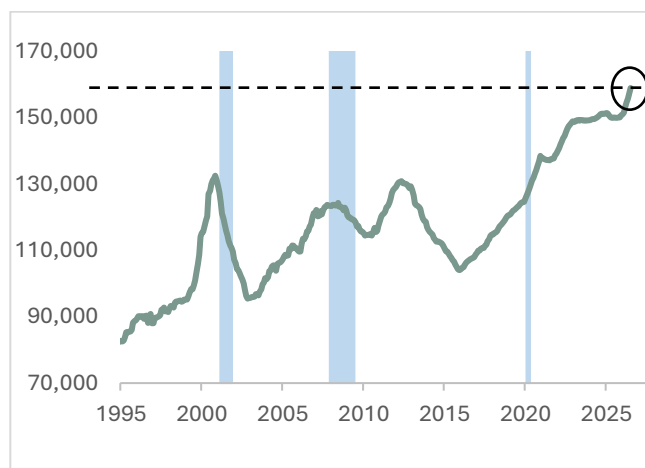
- **New Home Sales (Aug, Thursday):** We look for new home sales to increase 0.3% m/m in August. New home sales have trended sideways since 2017. Because the supply of new homes has been strong, median prices have fallen below median existing home prices for the first time (Figure 7).
- **Durable Goods Orders (Aug, Friday):** We expect durable goods orders to decline 0.5% in August. Excluding transportation equipment new orders are likely to rise 0.5%. That said, new orders, shipments and unfilled orders have all been boosted by the rapid buildout of AI infrastructure this year (Figure 8).

**Figure 7:** Median Price of New Homes (\$) and Existing Homes (\$)



Source: Census, NAR, Haver, SMBC Nikko

**Figure 8:** Unfilled Orders of Computers and Electronic Products (\$Millions)



Source: Census, Haver, SMBC Nikko

**Table 3: Economic indicator forecasts**

| Date   | Indicator                              | SMBC Forecast | Market Consensus (Median) | SMBC US Forecasts |               | Notes:                                                                                                             |
|--------|----------------------------------------|---------------|---------------------------|-------------------|---------------|--------------------------------------------------------------------------------------------------------------------|
|        |                                        |               |                           | Prior             | Range of Est. |                                                                                                                    |
| Sep 24 | New Home Sales (10 AM)                 | 0.3%          | 1.3%                      | -10.5%            | -2.3% - +2.2% | New home sales trending sideways since 2017. Mortgage applications declined -3.1% in August.                       |
| Sep 25 | Durable Goods New Orders (8:30 AM)     | -0.5%         | -0.5%                     | 1.1%              | -0.7% - +0.5% | Durable goods new orders (\$339B), shipments (\$334B) and unfilled orders (\$1.6T) all at all time highs.          |
| Sep 25 | Dur. Gds New Orders ex trans (8:30 AM) | 0.5%          | 0.5%                      | 0.4%              | 0.3% - +0.7%  | Durable goods new orders ex trans (\$223B), shipments (\$223B) and unfilled orders (\$593B) all at all time highs. |

**\*Forecasts subject to change\***

Source: SMBC Nikko Securities US Economics Forecasts

### Disclaimers

This document has been prepared by SMBC Group (including, collectively or individually, Sumitomo Mitsui Banking Corporation ("SMBC"), SMBC Nikko Securities America, Inc., SMBC Nikko Securities Canada, Ltd., SMBC Capital Markets, Inc., SMBC Leasing and Finance, Inc., and JRI America, Inc.) and is being furnished by SMBC Group solely for use by the client(s) or potential client(s) to whom such materials are directly addressed and delivered. SMBC Nikko Securities America, Inc. ("SMBC Nikko America") is a U.S.-registered broker-dealer. SMBC Nikko Securities Canada, Ltd. ("SMBC Nikko Canada") is a U.S. and Canadian registered broker-dealer. SMBC Capital Markets, Inc. ("SMBC Capital Markets") is a U.S. swap dealer registered with the Commodity Futures Trading Commission ("CFTC"). SMBC Group deal team members may be employees of any of the foregoing entities. In the U.S., capital markets and other investment banking activities for SMBC Group are performed by a combination of SMBC Nikko America, SMBC Nikko Canada, and SMBC Capital Markets. Derivative activities may be performed by SMBC Capital Markets or SMBC. Lending and other commercial banking activities are performed by SMBC and its banking affiliates. SMBC operates in the U.S. through state-licensed branches, and representative offices, and does not accept deposits from the general public. SMBC is not a member of the Federal Deposit Insurance Corporation ("FDIC") and is not an FDIC-insured institution. Deposits placed with SMBC are not insured by the FDIC. FDIC deposit insurance coverage only protects against the failure of an FDIC-insured depository institution. Non-deposit products are not insured by the FDIC; are not deposits; and may lose value, subject to certain limited exceptions.

This document is for informational purposes only and is not intended to be advice, a recommendation, an offer to sell or the solicitation of an offer to buy any securities, enter into any transaction or adopt any hedging, trading or investment strategy, or any commitment to underwrite, subscribe for or place any securities, is not an offer or commitment to provide any financing or extension of credit or service, and does not contain any tax, accounting, or legal advice. Any transactions or strategies discussed herein do not take into account the particular investment objectives, financial situations, or needs of any client, and may not be suitable for all parties. This document is not a research report, and neither this document nor its author(s) is subject to SMBC Group policies and procedures that apply to the globally branded research reports and research analysts of SMBC Group and its affiliates or to legal requirements designed to promote the independence of investment research. This document has been prepared for and is directed exclusively at Qualified Institutional Buyers, sophisticated institutional investors, and other market professionals. It is not intended for distribution to or use by retail customers.

SMBC Group makes no representations to, and does not warrant, this document's accuracy or completeness. In preparing this document, SMBC Group has relied on information available from third parties, including public sources, and we have assumed, without independent verification, the accuracy and completeness of such information. Any specific prices, indices or measures, including ranges, listed in this document were determined at or around the time the document was prepared and are subject to change without notice. SMBC Group expressly disclaims any liability for any results in connection with use of the information set forth herein, including, without limitation, any use of the information in the preparation of financial statements or accounting material. SMBC Group does not provide tax, accounting, or legal advice. Accordingly, any discussion of tax matters contained herein (including any attachments) is not intended or written to be used in connection with the promotion, marketing or recommendation by anyone for the purpose of avoiding any tax-related penalties. Prior to participating in any transaction or strategy, you should consult your own independent legal, tax, accounting and other professional advisors.

This document may contain forward-looking statements, which may include projections, forecasts, income estimates, yield or return, future performance targets, or similar analysis. Any such forward-looking statements, prices, indices, or measures are based upon certain assumptions. All forward-looking statements are based on the information available at the time the document was prepared and SMBC Group is not obligated to provide an update. Any opinions, projections, price/yield information or estimates are subject to change without notice. Actual events may differ from those assumptions or available information. There can be no assurance that any estimated returns or projections will be realized, that forward-looking statements will materialize, or that actual results will not be materially different from those presented herein. Past performance should not be taken as an indication or guarantee of future performance, and no representation or warranty, express or implied, is made regarding future performance. The value, price, or income from transactions or strategies may fall as well as rise. SMBC Group or an affiliate may have a position in any of the underlying instruments, assets, indices or rates mentioned in this document, at any time.

This document is confidential and is the property of SMBC Group, subject to copyright. Any reproduction of this document, in whole or in part, is prohibited, and you may not release this document to any person, except to your advisors and other professionals to assist you in evaluating the document, provided that they are obligated, by law or agreement, to keep the document confidential.

©2026 SMBC Group. SMBC CONNECT is a trademark of Sumitomo Mitsui Banking Corporation. All rights reserved.