US Rates Strategy Weekly

November 6, 2026

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- **The current continuing resolution funding the Federal government expires on December 11**. We look for a short-term extension. Congress is likely to use the appropriation process to push its agenda.

- We expect Congress to impose limits on new and continued financing of the Iran conflict to push for a diplomatic solution.

- **We think there may be bipartisan support for reducing healthcare costs**. However, while Republicans may support a temporary extension of the ACA tax subsidies, repealing the Medicaid changes is unlikely.

- Congress is unlikely to reverse tariffs. Legal challenges focus on their implementation not the legality of their imposition.

- Outside of the appropriations bills and the threat of a government shutdown, Congress may have more leverage with the upcoming debt ceiling. But historically, these episodes produced only modest fiscal concessions.

- **We think the Treasury has room under the current debt ceiling past the April tax date.** It may not need to draw on its extraordinary measures until summer. But by September or October it will run out of room under these measures and have little remaining cash.

- Risk-off and growth concerns are pulling yields lower, but resilient data and Iran-related inflation risks increasingly favor a range trade. The front end has absorbed much of the risk-off adjustment, while a break below 4.80%-4.85% in 10s may require clearer evidence of weaker growth.

- We are forecasting gains of 0.29% m/m for headline CPI and 0.28% m/m for core CPI in October. Year-on-year measures use the interpolated data from the October 2025 report.

Appropriations

The election turned on affordability. Now that Congress has turned over, what near-term changes can we expect to bring down prices? Ultimately, this may depend on how aggressively the new Congress wants to achieve its agenda through the budget appropriations process and, later, the debt ceiling.

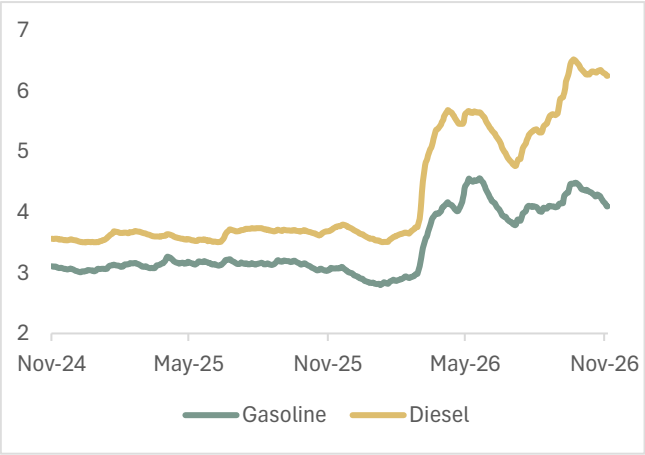
The current continuing resolution funding the Federal government expires on December 11. We do not think the lame duck Congress has the appetite to threaten a budget standoff after this week's election results and ahead of the holidays. Instead, we expect this Congress will agree to a short-term

extension of a few weeks so that passing the 12 annual appropriations bills becomes the new Congress' task.

We think there may be bipartisan support for reducing healthcare costs. While Republicans are opposed to permanently extending the ACA tax subsidies, they may be amenable to a temporary extension. In January 2026, the House passed a bill to extend them for 2y (203 to 196) but it stalled in the Senate over issues related to abortion funding. **There could be enough Senate support to push this legislation forward**. CBO noted, that a three-year extension would cost about $80bn. Plans to reverse the Medicaid cuts included in the OBBB face a higher bipartisan hurdle given their significantly higher price tag.

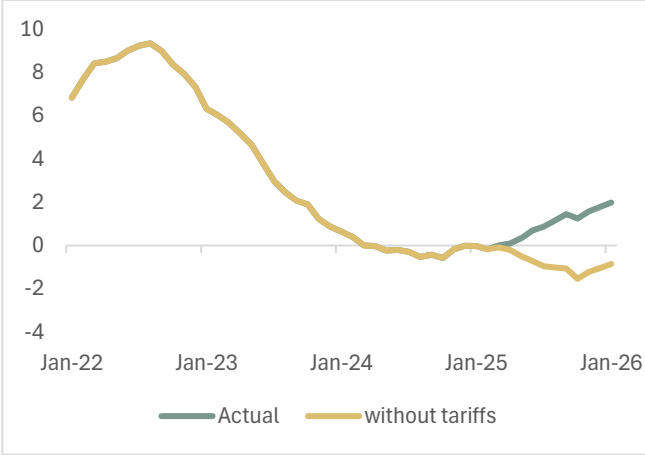
Voters were clearly peeved by the high gasoline and diesel prices caused by the Iran conflict (Figure 1). On Wednesday, rate markets rallied on hopes that the new Congress would end the conflict and bring about lower energy prices (with a possibly lower fed funds path). Rates rallied further on Thursday as equities sold off on data center construction fears. There was some speculative discussion that the new Congress could use the War Powers Act to end the conflict. However, Congress has tried this before unsuccessfully – as recently as September. Even with a majority in both houses, the legislation **might not overcome a presidential veto.**

Figure 1: Gasoline and diesel prices ($/g)



Source: AAA, SMBC Nikko;

Figure 2: Consumer goods prices (% y/y)



Source: Amiti, Heise, and Weinstein, SMBC Nikko

Instead, we expect Congress to use the appropriations process to put limits (or, less likely, remove) financing for the conflict. **The defense budget includes $90bn in Iran-related funding that could become conditional on a diplomatic solution**. This is likely to be more contentious than authorizing an ACA tax subsidy extension. That said, it is unclear if the President feels strongly enough about ending the conflict to trigger a government shutdown early next year.

Congressional action on tariff policy is unlikely. A recent study examined tariff pass-through effects and concluded that the 2025 duties increased goods prices by 2.9% (Figure 2).[1] About 2/3 of this came from the higher price of imported goods. The remainder came from higher prices for imported materials and parts used in the manufacture of US consumer goods. While importers raised their prices immediately,

[1] See "How fast do tariffs pass through into consume prices", M. Amiti, S. Heise, and D. Weinstein, Liberty Street Economics, Federal Reserve Bank of New York, October 6, 2026

the effect on imported inputs took longer to flow through to consumer prices. As a result, the peak effect from the 2025 tariffs was in February 2026, so the effects on inflation are already waning. That said, the increase in Canadian tariffs beginning in January could add a few tenths to goods price inflation next year.

The biggest tariff revenue source is those duties imposed under Section 301. These apply taxes of 10 or 12.5% on goods from 87 countries because of their use of forced labor. These duties have been raising about $20bn/mo since late July.

Section 301 is currently facing a legal challenge in the US Court of International Trade. But the challenge is not over the Administration's imposition of the duties like it was with IEEPA. Instead, it reflects issues related to how the tariff is applied and the lack of specific findings on a country-by-country basis of unfair labor laws. A decision is expected in December or January. Regardless of the outcome, we expect it will be appealed to the Federal Circuit Court. As a result, we see little chance of broad-scale tariff relief in 2027.

Debt ceiling

Outside of the appropriations bills and the threat of a government shutdown, Congress may have more leverage with the upcoming debt ceiling. In July 2025, Congress agreed to a $5trn increase in the debt limit (to $41.1trn). As of this week, the Treasury has only $0.7trn remaining. The Treasury's latest quarterly borrowing estimates suggest it needs to raise $800bn in marketable borrowing in Q1'27 with a target cash balance of $1trn on March 31. But the Treasury's borrowing capacity rebounds in April and May so it might not need to tap its extraordinary (accounting) measures until June. These give the Treasury enough borrowing capacity through summer. We expect the Treasury will run out of cash and borrowing authority (that is, the x-date) in either September or October.

At that point, Congress may attempt to push forward with some of the more contentious aspects of its agenda. But historically, the gains have been modest. The party forcing the confrontation gets an increasing share of the blame for creating the financial market and economic risk. As a result, they modify their goals and accept concessions in return for agreeing to increase the limit. But unlike past confrontations where Republicans were pushing to cut discretionary spending, the Democratic agenda includes large (and popular) increases to healthcare spending which could mute some of the blame.

Post- Midterm drivers for Treasuries

Midterm results provided another tailwind for Treasuries, with Texas flipping blue adding to concerns over the pace of data-center investment. This gives another thrust to the AI-capex worries that helped drive the October reversal from the highs in yields. Until there is greater clarity on the policy implications of a Democratic Congress, the AI-capex outlook and the Iran conflict are likely to remain key drivers of the bond market.

A mid-December data-center audit in Texas could provide the next important read on the pace of that state's buildout. Texas has effectively paused new data-center approvals during the review. Governor-elect Gina Hinojosa has proposed a moratorium on data-center approvals until the Legislature meets in January and adopts protections around electricity costs, water use and other issues.

Hopes for reduced long-end supply should fade for now, with the Treasury making only minor changes to its guidance in the refunding. Positioning may therefore be relatively overweight the long end, leaving it vulnerable once the market looks beyond the initial assumption that a blue sweep means less expansionary fiscal policy.

Range trade in the making?

We have been surprised that 10y yields have failed to decisively break the key 4.80%-4.85% support zone despite the sharp selloff in risk assets. After a roughly 50bp rally since early October, investors appear reluctant to chase Treasuries at current levels. The **front end has also borne much of the risk-off adjustment**, with the market pricing out hikes and now discounting only around 44bp of tightening in 2027 (Figure 3).

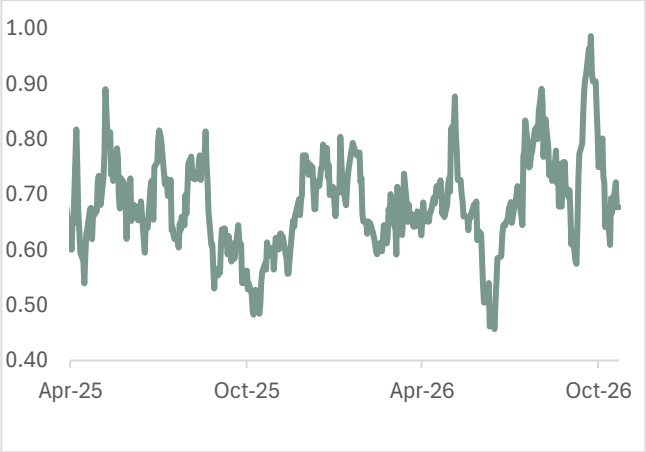
Term premium (Figure 4) looks relatively neutral rather than stretched: the ACM 10y term premium is around 67bp, roughly midway through its 45-90bp range since April 2025 and only 14bp higher since Warsh chaired his first meeting on June 17. Most of the back up in 10y yields since then reflects the Fed's more hawkish tone. With much of the tactical short positioning also likely unwound, there may be less fuel for the rally. Risk-off has taken yields to support, but a sustained break may require clearer evidence of deterioration in the growth outlook.

Figure 3: Hikes/cuts in 2027 SOFR futures (bps)



Source: CME, Bloomberg, SMBC Nikko

Figure 4: 10y term premium (ACM model, bps)



Source: FRB, Bloomberg, SMBC Nikko

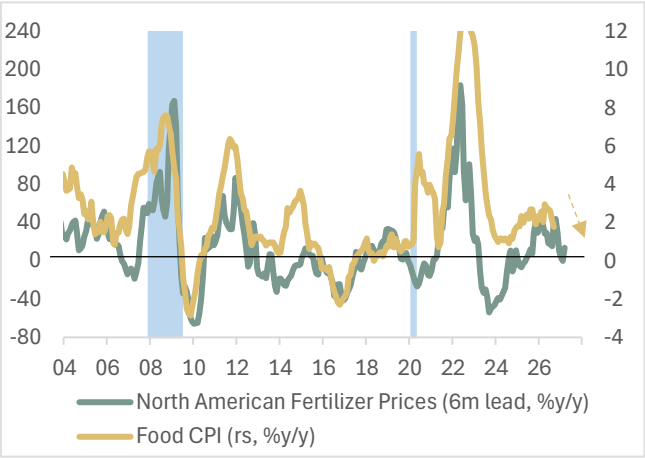
Week ahead

- **Consumer Prices (Oct, Tues)**: We are forecasting gains of 0.29% m/m for headline CPI and 0.28% m/m for core CPI. We look for CPI energy prices to rise 0.6%, driven by gains in crude oil and diesel prices. Food prices may increase only 0.1% m/m. Fertilizer prices suggest food costs could slow (Figure 5).

- **Producer Prices (Oct, Fri)**: We look for headline and core prices to increase 0.3% m/m in October. Producer prices have accelerated this year, rising 6.3% y/y (September). While energy prices have been a large contributor, this is also partly due to final demand trade services, which is a measurement of margins received by wholesalers and retailers. These have risen to 4.7% y/y (Figure 6). Firms appear to be maintaining their margins.

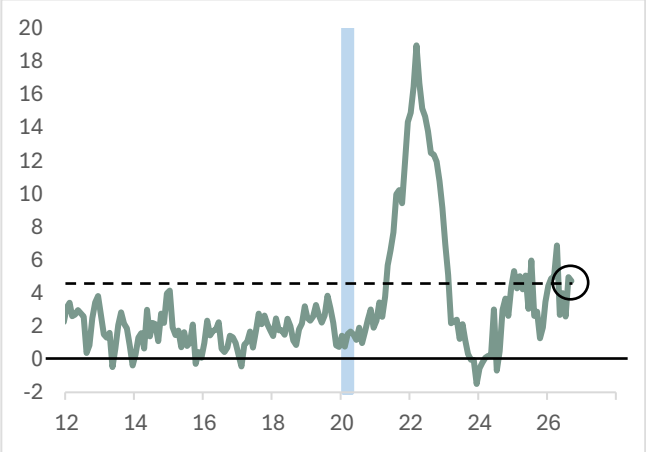
- **Existing Home Sales (Oct, Thur)**: We expect existing home sales to fall 3% m/m in October. At 3.99m, existing home sales are near record lows.

Figure 5: Fertilizer (%y/y) vs. CPI Food (%y/y)



Source: Green Markets, BLS, Haver, SMBC Nikko

Figure 6: PPI trade Services (%y/y)



Source: BLS, Haver, SMBC Nikko

Table 1: Economic indicator forecasts

SMBC US Forecasts						
Date	Indicator	SMBC Forecast	Market Consensus (Median)	Prior	Range of Est.	Notes:
Nov 10	CPI %m/m (8:30 AM)	0.29%	0.3%	0.6%	0.2% - +0.4%	Forecasting: food at 0.12%, energy at 0.64%
Nov 10	Core CPI %m/m (8:30 AM)	0.28%	0.2%	0.3%	0.2% - +0.3%	Forecasting shelter at 0.26%, core CPI ex shelter at 0.3%.
Nov 10	CPI %y/y (8:30 AM)	3.9%	-	3.7%	-	BLS not releasing y/y statistics due to October 2025 government shutdown.
Nov 10	Core CPI %y/y (8:30 AM)	2.6%	-	2.6%	-	BLS not releasing y/y statistics due to October 2025 government shutdown.
Nov 12	Existing Home Sales %m/m (10 AM)	-3.0%	-3.4%	1.5%	-4.8% - -0.1%	Mortgage applications for a home purchase fell -11.9% in October, to the lowest level since August 2024.
Nov 13	PPI %m/m (8:30 AM)	0.3%	0.4%	1.3%	0.2% - +0.5%	Crude oil increased by 1.3% in the month.
Nov 13	Core PPI %m/m (8:30 AM)	0.3%	0.3%	0.7%	0.2% - +0.4%	PPI trade services--margins received by wholesalers and retailers--has increased by a 4.7% y/y which is elevated.

Forecasts subject to change

Source: SMBC Nikko Securities US Economics Forecasts

Table 2: Federal Reserve communication

Federal Reserve Communication		
Nov 9	10:00 AM	Chicago Fed President Goolsbee (2027 voter) speaks in moderated Q&A. Text: No; Q&A: Yes.
Nov 9	12:15 PM	Richmond Fed President Barkin (2027 voter) speaks to Greer Chamber of Commerce. Text: Yes; Q&A: Yes.
Nov 10	4:00 AM	Fed Governor Waller (voter) Gives Keynote Speech. Text: TBD; Q&A: yes.
Nov 10	1:30 PM	KC Fed President Schmid (2028 voter) participated in fireside chat. Text: No; Q&A: Yes.
Nov 10	6:30 PM	Philadelphia Fed President Paulson (2026 voter) speaks on economic outlook. Text; Yes; Q&A: No
Nov 12	9:00 AM	Cleveland Fed's Hammack (2026, 2028 voter) speaks in moderated conversation. Text: No; Q&A: Yes.
Nov 12	11:30 AM	Chicago Fed President Goolsbee (2027 voter) speaks in moderated Q&A. Text: No; Q&A: Yes.
Nov 12	1:10 PM	SF Fed's Daly (2027 voter) delivers keynote remarks at Stanford. Text: No; Q&A: Yes.
Nov 12	6:30 PM	NY Fed's Williams (voter) participates in panel discussion. Text: No; Q&A: Yes.
Nov 13	12:00 PM	SF Fed's Daly (2027 voter) speaks in moderated discussion. Text: No; Q&A: Yes.
Nov 13	7:00 PM	Fed Governor Jefferson (voter) speaks at the UC San Diego Economics Roundtable. Text: TBD; Q&A: TBD.

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