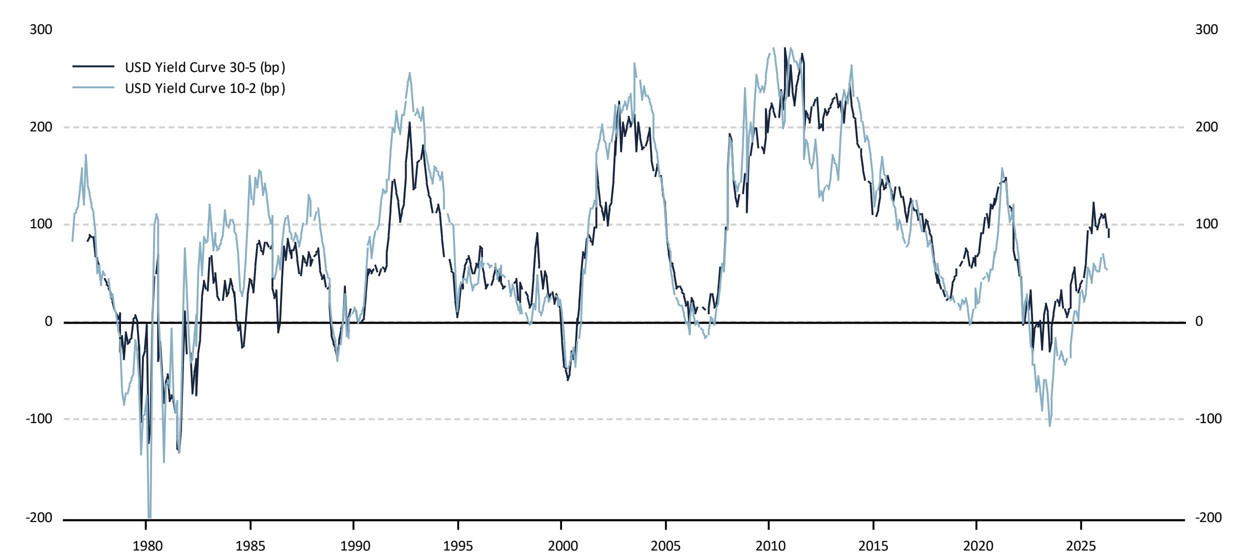
weekly investment focus

The flexiweekly that reaches new heights - published on 25 May 2026

"THE YIELD CURVE HAS NOT YET PASSED THE BATON"

- The Fed has a new chair, but the Warsh Trade is being challenged by inflation
- The bond market is tightening, and yield curves are struggling to steepen
- Paradoxically, this situation is a boon for investors
- As in a relay race, the 30-5 favours safety whilst the 10-2 targets performance

CHART OF THE WEEK: "A permanent divergence or a gap to be closed?"



Source: Bloomberg, Altitude IS

BOND MARKET ANALYSIS

The US yield curve is sending an unusual signal. The interest rate spread between 30-year and 5-year bonds is almost twice as wide as the spread between 10-year and 2-year bonds: 87 basis points compared with 52. Historically, these two curves have overlapped and, when they do not, they quickly converge towards one another (see Chart of the Week). The current divergence raises a question. Is the 10-2 spread exceptionally lagging, has the 30-5 spread gone too far, or is this a structural and lasting change? The answer will bring up many related questions, but **understanding this paradox has become essential for bond investors.**

To solve this puzzle, it is worth recalling what these two yield curves measure. **The spread between the 10-year and 2-year yields is the classic barometer of the US economic cycle.** When GDP is overheating, investors anticipate a tightening of monetary policy and 10-year yields rise even before short-term rates adjust (see Fig. 2). Conversely, during a cooling-off phase and, a fortiori, during recessions, the curve anticipates easing by the central bank and 10-year rates fall in line with 2-year rates at an early stage. The message from the 10-2 spread is therefore quite straightforward. It reflects investor sentiment regarding monetary policy.

The spread between 30-year and 5-year yields tells a different story. It serves as an indicator of confidence in the country's ability to repay its debt (see Fig. 3). The 30-year rate incorporates the term premium, budget deficits, rollover requirements for historical debt, inflation uncertainty, as well as the demand for duration from insurers, pension funds and foreign investors. As for the 5-year rate, it lies further along the curve. It remains slightly sensitive to the economic cycle, but also to debt sustainability. Thus, when the 30-5 spread steepens, the market is not necessarily signalling that the Fed is about to adjust its rates. Investors are primarily demanding a higher return for bearing very long-term risk.

Fig. 2 – 10-Fed curve and the economic cycle

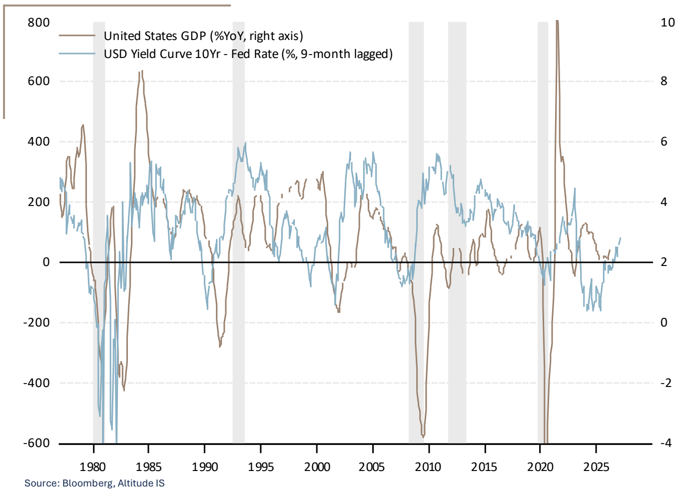
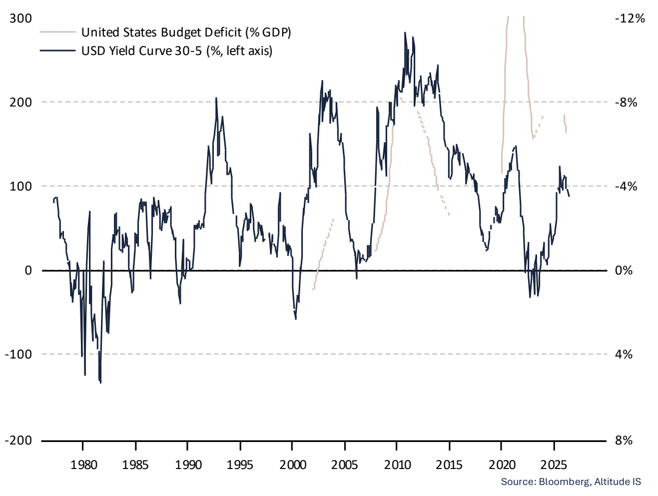


Fig. 3 – 30-5 curve and budget deficit



The current phase is particularly interesting because the 30-5 spread has already sent a clear signal of steepening, whilst the 10-2 spread is struggling to widen further (see Chart of the Week). The term premium has increased, whilst the economic outlook is not considered to be definitively promising. Since the end of the zero-interest rate policy, the bond market has not been the same. **With US public debt remaining very high, interest costs are soaring. Unsurprisingly, investors are demanding greater compensation to offset the risk they are taking on by putting their capital at risk for 30 years.** Against this backdrop, the 30-5 curve is steepening again, but at the less usual end – the long end.

Conversely, the lag in the 10-2 spread can be explained by the inertia in the short end of the curve. This maturity remains constrained by the Fed's reaction function. As long as inflation does not provide a sufficiently reassuring signal, as long as the economy continues to create jobs, and as long as growth does not slow significantly, bond investors will be reluctant to anticipate an aggressive series of rate cuts. The yield on 2-year bonds will not fall enough to propel the 10-2 spread upwards. As for the 10-year rate, it is caught between two opposing forces. On the one hand, expectations of a slowdown are pulling it downwards. On the other, the term premium is pushing it upwards. Since April 2025, the 10-2 spread has seemed stuck between 45 and 70 basis points. **It is waiting for a clear signal of monetary policy easing to reach, or even exceed, the 87 basis points offered by the 30-5 spread.**

This pattern is not unique to US government bonds. Globally, fiscal concerns have driven up the term premium. In most developed countries, the 30-5 spread exceeds the 10-2 spread (see Fig. 4). In Germany, the Bund shows spreads of 82 and 43 basis points, respectively. The Japanese market has a particularly steep curve, whilst the Swiss curve, anchored by a near-zero policy rate, is flatter.

Fig. 4 – Yield spreads, by country

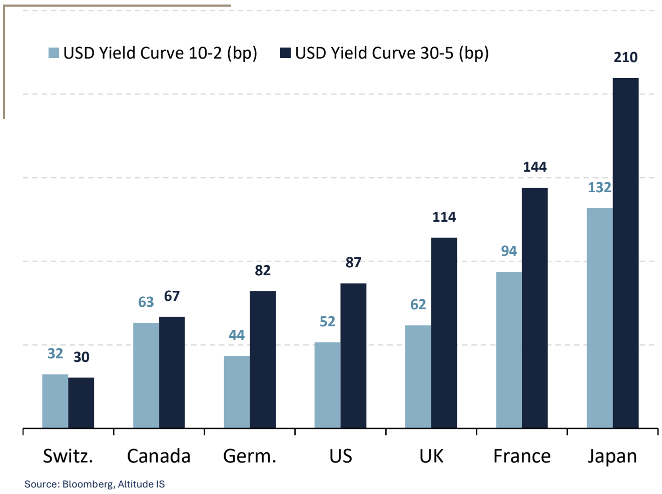
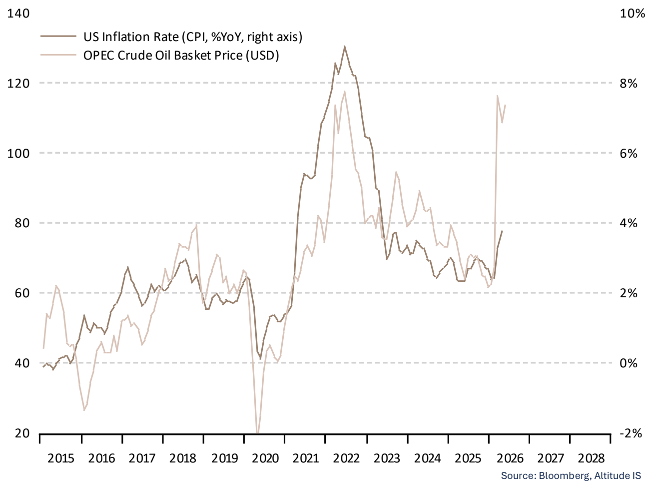


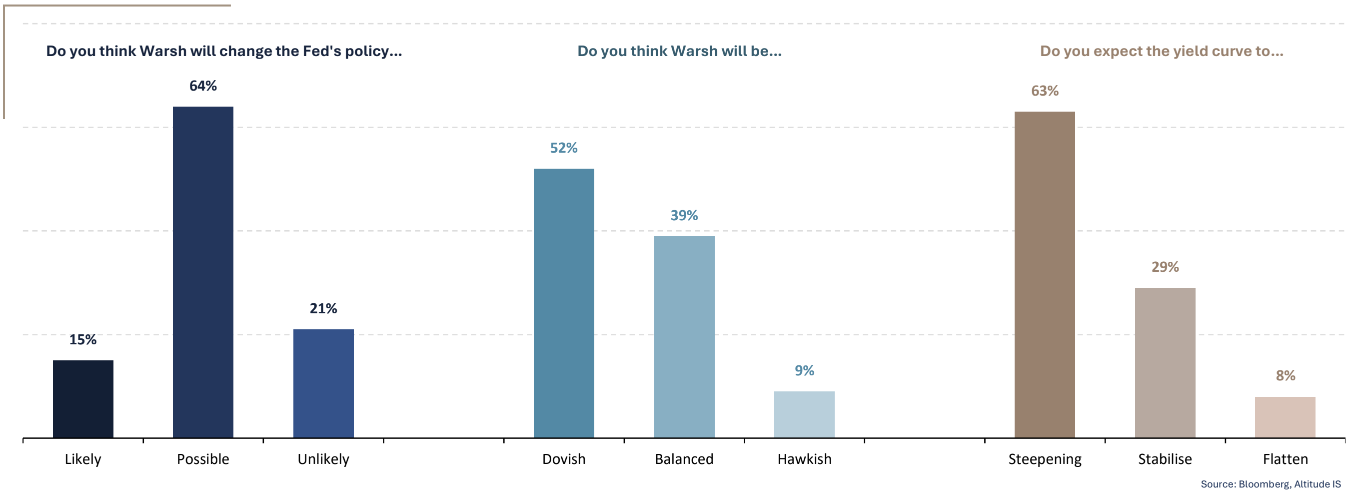
Fig. 5 – Inflation & oil prices



The appointment, and subsequent arrival, of Kevin Warsh as Chair of the Fed should have helped to resolve this anomaly. Known for his desire to simultaneously reduce the central bank's balance sheet and key interest rates, as well as for his intention to provide fewer forward guidance signals to the markets, he embodies an accommodative stance that traders have sought to translate into an investment strategy. **The Warsh Trade is based on the idea that a more dovish chair would favour rate cuts, despite inflation still being evident** (see Fig. 6). At the same time, the loss of predictability in monetary policy should widen the term premium demanded on long-term maturities. Under these conditions, the yield curve had every reason to steepen, particularly the 10-2 spread, which appeared to be lagging.

This investment scenario was suddenly called into question in February 2026, when investors began to anticipate the inflationary impact of a war in the Middle East. The ensuing oil shock proved them right, as US inflation jumped from 2.4% to 3.8% between February and April (see Fig. 5). The trend for May and June remains one of accelerating prices. Gradually, the Warsh Trade is becoming less a bet on falling rates and more a bet on the loss of predictability from the Federal Reserve and on long-term rates remaining higher for longer. This tactical shift is far less convincing. Proof, if any were needed, is that yields have risen across the board and the yield curve has flattened slightly. 30-year Treasuries have risen from 4.60% to 5.15%, whilst investors no longer anticipate any rate cuts from the Fed this year, compared with two to three 25bp cuts previously.

Fig. 6 – Investors' perception of Kevin Warsh and his monetary policy



The mechanics of yield curves can be rewritten as follows: **(30-year – 5-year) – (10-year – 2-year) = (30-year – 10-year) – (5-year – 2-year)**. Behind this new identity lies an illuminating insight. When the 30-5 spread is above the 10-2 spread, this means that the 30-10 segment is much steeper than the 5-2 segment. This is precisely what the PIMCO fund is exploiting at the moment, as the fund managers consider the yen yield curve to be too steep. In other words, the distortion of the curve stems mainly from the very long end. **Investors have already repriced the risk of default, but they are not pricing in monetary easing. The curve is therefore moving at two speeds.**

It would probably be fair to say that investors have not **yet** bought into the **need** for monetary easing. Indeed, an analysis of previous cycles leads to a very convincing conclusion, whatever those who believe that "this time is different" may think. **It is extremely rare to see the 30-5 yield begin a sustained fall before the 10-2 yield has caught up with it, or even overtaken it** (see Chart of the Week). The 30-5 yield may occasionally correct tactically, but major periods of yield curve flattening begin when the 10-2 yield is higher than the 30-5 yield. Historically, the 2-year rate has always ended up falling, sometimes very sharply, when investors have realised that the Fed would have no choice but to ease its monetary policy to support employment, credit or debt financing. **Each time, the 10-2 has taken up the baton passed by the 30-5 to complete its steepening run.**

To be exhaustive, there is no law of arbitrage imposing this convergence. A 'this time it's different' scenario remains possible. For this to happen, the Fed would need to refrain from cutting its key rates, meaning that inflation remains stubbornly high and job creation holds up against the wave of productivity driven by AI. In this case, described as 'higher for longer', the 10-2 spread could remain narrow, and the 30-5 spread could eventually compress, either through tightening in the 5-year yield or a decline in the term premium. This scenario would be unprecedented.

Since late 2023, investors have been keen on steepening strategies, and the facts suggest they are right. As a reminder, a steepener generates a return equal to a multiple of the spread between the long end and the short end of the yield curve. Many variations are used, but the two most common are steepeners on the 10-2 and the 30-5. Today, the difference between yield spreads helps explain why most slope structures offer a better multiple on the 10-2 than on the 30-5. This is not a free anomaly. As the 30-5 is more ‘in the money’, the probability of gains is higher, but the returns are lower. Conversely, as the 10-2 depends on an uncertain catalyst (a fall in the 2-year rate), it will deliver a better performance if the catch-up occurs. **Therefore, there is not a good and a bad steepener, but there are two distinct exposures to the yield curve.** The 30-5 reflects a movement that is already underway, whilst the 10-2 reflects a movement that is still latent. If history repeats itself, then this lag could prove valuable.

Conclusion:

The gap between the 30-5 and the 10-2 reveals a two-speed yield curve. The 30-5 reflects the long-term risk premium. The 10-2 still needs to anticipate monetary easing by the Fed. Until the latter catches up with the former, the steepening of the curve will appear incomplete. In bond markets, as in relay races, it is not always the first baton-bearer who determines the final performance.

RETURN ON FINANCIAL ASSETS

Markets Performances (local currencies)	Last Price	Momentum Indicator (RSI)	1-Week (%)	1-Month (%)	2026 Year-to-Date (%)	2025 (%)	2024 (%)
Equities							
World (MSCI)	1 112.6	66.45	1.3%	4.1%	10.5%	22.9%	18.0%
USA (S&P 500)	7 473	68.14	0.9%	4.8%	9.7%	17.9%	25.0%
USA (Dow Jones)	50 580	64.84	2.2%	2.4%	5.9%	14.9%	15.0%
USA (Nasdaq)	26 344	67.59	0.5%	6.9%	13.6%	21.2%	29.6%
Euro Area (DJ EuroStoxx)	646.0	59.58	3.3%	3.4%	7.6%	21.2%	10.2%
UK (FTSE 100)	10 466	55.38	2.8%	0.3%	7.0%	25.7%	9.6%
Switzerland (SMI)	13 503	64.42	2.3%	3.6%	4.8%	18.0%	7.5%
Japan (Nikkei)	65 338	64.13	3.1%	6.3%	26.8%	28.7%	21.3%
Emerging (MSCI)	1 686	59.08	1.1%	5.1%	20.9%	34.3%	8.0%
Brasil (IBOVESPA)	176 210	35.68	-0.6%	-8.6%	9.4%	34.0%	-10.4%
Mexico (IPC)	68 333	46.71	0.6%	-0.3%	7.2%	35.1%	-11.0%
India (SENSEX)	76 155	44.12	0.3%	-3.8%	-11.2%	10.5%	9.6%
China (CSI)	4 889	53.95	-0.3%	1.1%	5.1%	21.0%	18.2%
Com. Services (MSCI World)	172.5	54.89	-1.1%	2.9%	5.5%	33.0%	31.9%
Cons. Discretionary (MSCI World)	449.0	55.79	1.2%	0.4%	-1.4%	9.8%	20.7%
Cons. Staples (MSCI World)	306.1	50.31	-0.2%	2.2%	6.9%	9.3%	4.7%
Energy (MSCI World)	340.2	52.78	0.1%	3.6%	30.4%	14.8%	2.9%
Financials (MSCI World)	225.2	56.69	1.9%	0.2%	1.0%	29.5%	25.1%
Health Care (MSCI World)	380.6	58.98	2.8%	1.3%	-2.7%	15.3%	1.5%
Industrials (MSCI World)	518.3	50.82	0.7%	0.6%	11.8%	26.2%	12.8%
Info. Tech. (MSCI World)	1 204.0	71.50	2.0%	12.0%	24.9%	26.6%	31.9%
Materials (MSCI World)	434.9	45.71	-0.2%	-2.8%	11.3%	32.5%	-7.6%
Real Estate (MSCI World)	1 050	50.72	1.4%	0.1%	6.6%	3.6%	-0.4%
Utilities (MSCI World)	208.1	46.13	2.7%	-0.7%	8.8%	24.7%	13.0%
Bonds (Bloomberg)							
World (Aggregate)	3.87%	44.33	0.3%	-0.9%	-0.5%	8.2%	-1.7%
USA (Sovereign)	4.41%	40.93	0.2%	-1.1%	-0.8%	6.3%	0.6%
Euro Area (Sovereign)	3.23%	55.07	0.8%	0.1%	0.0%	0.6%	1.9%
Germany (Sovereign)	2.90%	54.11	0.7%	-0.1%	-0.2%	-1.6%	0.6%
UK (Sovereign)	4.86%	56.79	2.0%	0.3%	-0.9%	6.1%	-3.0%
Switzerland (Sovereign)	0.76%	37.68	-0.3%	-1.3%	-1.4%	0.3%	5.4%
Japan (Sovereign)	2.39%	26.89	-0.2%	-1.7%	-3.0%	-4.6%	-2.1%
Emerging (Sovereign)	6.26%	46.05	0.3%	-0.8%	0.2%	13.1%	7.0%
USA (IG Corp.)	5.26%	46.71	0.3%	-0.8%	-0.3%	7.8%	2.1%
Euro Area (IG Corp.)	3.60%	57.24	0.5%	0.2%	0.3%	3.0%	4.7%
Emerging (IG Corp.)	6.42%	47.24	0.0%	-0.4%	0.8%	8.1%	7.0%
USA (HY Corp.)	7.12%	53.04	0.3%	-0.1%	1.1%	8.6%	8.2%
Euro Area (HY Corp.)	6.12%	64.46	0.1%	0.4%	0.8%	5.2%	8.2%
Emerging (HY Corp.)	7.63%	50.73	0.2%	-0.2%	1.9%	13.9%	14.9%
World (Convertibles)	628.9	62.28	0.9%	4.4%	16.7%	22.4%	9.4%
USA (Convertibles)	833.6	61.82	0.8%	4.8%	19.1%	16.9%	10.1%
Euro Area (Convertibles)	307.6	56.42	0.4%	0.7%	5.8%	24.8%	14.7%
Switzerland (Convertibles)	294.2	54.50	0.3%	0.0%	4.0%	17.5%	-10.5%
Japan (Convertibles)	315.9	73.58	2.9%	8.5%	22.5%	13.8%	6.4%
Hedge Funds (Bloomberg)							
Hedge Funds Industry	1 878	77.70	n.a.	3.5%	n.a.	3.8%	11.1%
Macro	1 550	73.98	n.a.	2.4%	n.a.	5.6%	7.4%
Equity Long Only	2 488	64.29	n.a.	4.8%	n.a.	0.6%	12.0%
Equity Long/Short	2 063	76.67	n.a.	5.2%	n.a.	4.7%	14.0%
Event Driven	1 979	76.02	n.a.	2.6%	n.a.	3.1%	8.7%
Fundamental Equity Mkt Neutral	1 959	86.49	n.a.	1.5%	n.a.	4.6%	12.4%
Quantitative Equity Mkt Neutral	1 842	77.20	n.a.	2.3%	n.a.	1.8%	9.8%
Credit	1 753	90.65	n.a.	1.5%	n.a.	2.0%	8.5%
Credit Long/Short	1 788	95.60	n.a.	1.5%	n.a.	3.1%	10.0%
Commodity	2 089	81.40	n.a.	1.5%	n.a.	4.4%	14.7%
Commodity Trading Advisors	1 568	70.10	n.a.	2.5%	n.a.	10.4%	7.9%
Volatility							
VIX	16.70	40.75	-9.4%	-11.7%	11.7%	-13.8%	39.4%
VSTOXX	21.14	43.07	-5.1%	-9.5%	43.6%	-13.5%	25.3%
Commodities							
Commodities (CRB)	565.3	n.a.	1.0%	2.4%	4.7%	0.6%	5.1%
Gold (Troy Ounce)	4 562	n.a.	-0.1%	-2.6%	5.6%	64.6%	27.2%
Silver (Troy Ounce)	77.91	n.a.	0.3%	3.2%	8.7%	148.0%	21.5%
Oil (WTI, Barrel)	100.93	n.a.	-4.3%	4.0%	75.8%	-19.9%	0.1%
Oil (Brent, Barrel)	107.20	n.a.	-4.4%	-4.1%	71.7%	-15.7%	-4.6%
Currencies (vs USD)							
USD (Dollar Index)	99.04	54.56	-0.2%	0.5%	0.7%	-9.4%	7.1%
EUR	1.1638	45.40	-0.2%	-0.7%	-0.9%	13.4%	-6.2%
JPY	158.89	46.26	0.0%	0.3%	-1.4%	0.3%	-10.3%
GBP	1.3479	50.49	0.3%	-0.4%	0.0%	7.7%	-1.7%
AUD	0.7167	51.17	0.0%	-0.3%	7.4%	7.8%	-9.2%
CAD	1.3808	35.58	-0.5%	-1.3%	-0.6%	4.8%	-7.9%
CHF	0.7821	53.53	0.3%	0.4%	1.3%	14.5%	-7.3%
CNY	6.7816	64.44	0.3%	-0.7%	3.0%	4.5%	-2.7%
MXN	17.270	54.47	0.0%	0.6%	4.3%	15.7%	-18.5%
EM (Emerging Index)	1 863.8	46.59	0.0%	-0.5%	0.6%	7.2%	-0.7%
XBT	77 060	n.a.	-0.8%	-0.6%	-12.1%	-6.5%	120.5%

Source: Bloomberg, Altitude Investment Solutions

Total Return by asset class (Negative \ Positive Performance)

DISCLAIMER

This document is issued by Altitude Investment Solutions (hereinafter "Altitude IS"). It is not intended for distribution, publication, or use in any jurisdiction where such distribution, publication, or use would be unlawful, nor is it aimed at any person or entity to whom it would be unlawful to address such a document.

This document is provided for information purposes only. It does not constitute an offer or a recommendation to subscribe to, purchase, sell or hold any security or financial instrument. It contains the opinions of Altitude IS, as at the date of issue. These opinions and the information herein contained do not take into account an individual's specific circumstances, objectives, or needs. No representation is made that any investment or strategy is suitable or appropriate to individual circumstances or that any investment or strategy constitutes a personal recommendation to any investor. Each investor must make his/her own independent decisions regarding any securities or financial instruments mentioned herein. Tax treatment depends on the individual circumstances of each client and may be subject to change in the future. Altitude IS does not provide tax advice. Therefore, you must verify the above and all other information provided in the document or otherwise review it with your external tax advisors.

Investments are subject to a variety of risks. Before entering into any transaction, an investor should consult his/her investment advisor and, where necessary, obtain independent professional advice in respect of risks, as well as any legal, regulatory, credit, tax, and accounting consequences. The information and analysis contained herein are based on sources considered to be reliable. However, Altitude IS does not guarantee the timeliness, accuracy, or completeness of the information contained in this document, nor does it accept any liability for any loss or damage resulting from its use. All information and opinions as well as the prices, market valuations and calculations indicated herein may change without notice. Past performance is no guarantee of current or future returns, and the investor may receive back less than he invested. The investments mentioned in this document may carry risks that are difficult to quantify and integrate into an investment assessment. In general, products such as equities, bonds, securities lending, forex, or money market instruments bear risks, which are higher in the case of derivative, structured, and private equity products; these are aimed solely at investors who are able to understand their nature and characteristics and to and bear their associated risks. On request, Altitude IS will be pleased to provide investors with more detailed information concerning risks associated with given instruments.

The value of any investment in a currency other than the base currency of a portfolio is subject to the foreign exchange rates. These rates may fluctuate and adversely affect the value of the investment when it is realized and converted back into the investor's base currency. The liquidity of an investment is subject to supply and demand. Some products may not have a well-established secondary market or in extreme market conditions may be difficult to value, resulting in price volatility and making it difficult to obtain a price to dispose of the asset. If opinions from financial analysts are contained herein, such analysts attest that all of the opinions expressed accurately reflect their personal views about any given instruments. In order to ensure their independence, financial analysts are expressly prohibited from owning any securities that belong to the research universe they cover. Altitude IS may hold positions in securities as referred to in this document for and on behalf of its clients and/or such securities may be included in the portfolios of investment funds as managed by Altitude IS.