RBC BlueBay Asset Management

Marketing communication

Fast and Furious

Trump starts 2026 in full force!

Key points:

- US economic growth continues to show strength, in sharp contrast to stagnation and depressed sentiment in Europe.
- Geopolitical tensions abound, however markets seem desensitised these days and US Treasuries continue to trade in a range.
- In Japan, Prime Minister Takaichi's policies are boosting investor sentiment, lifting the Nikkei and sparking a shift from cash to risk assets amidst growing economic optimism.
- Tariff rulings, elections, and policy shifts remain key catalysts for potential market disruption.
- One potential drive of volatility is a Supreme Court ruling against Trump's IEEPA tariffs, which could potentially open the door for repayment claims.

London, 16 Jan 2026: US economic data continued to support risk assets over the past week, with the Atlanta Fed Nowcast of GDP accelerating above 5% at the start of Q1, whilst core inflation remains stable at 2.6%. These are Goldilocks economic conditions for the US administration to reflect on. However, far from resting on his laurels, it seems that President Trump has been hyperactive in a Fast and Furious start to 2026, as he seeks to reshape the world around him on multiple fronts.

Reviewing some of the recent initiatives, last week's directive to the FNMA to purchase USD200 billion of mortgage securities can be viewed as a pseudo-QE via the back door, linked to the President's ideological zeal in bringing mortgage interest rates down.

Similarly, a desire to cap interest rates on credit cards at 10% (which is widely disregarded as unrealistic) is also seen as linked to a desire to address affordability, as a topic ahead of the mid-term elections this Fall. Meanwhile, Trump's frustration at the Fed's reluctance to cut more quickly was seen behind the DoJ subpoena issued to the Fed Chair in the past week.

This was something which saw widespread condemnation from the central banking community and in the wake of these headlines, it appeared that Trump quickly started to distance himself from this particular action. Certainly, the last thing that POTUS would want is for the courts to make something of a martyr out of Powell, especially since he only has a few short months left as the Fed Chair.

Financial markets were quick to look through the theatre surrounding the Fed, knowing that soon the President will announce his new pick as incoming Chair. In this context, it seems unlikely that the White House will want to continue to attack the institution beyond that time.

Moreover, the prevailing market narrative is that unless policy causes a material reassessment of the economic outlook, then there is little to see or do. This mindset has also been true with respect to geopolitical upheaval in the wake of headlines in Venezuela, Greenland and most recently Iran, over the past number of days.

It seems that markets have become desensitised to the change and upheaval that has been a hallmark of this administration over the past year. Although there is a risk that at some point this complacent mindset could suddenly change, as was witnessed last April, for now it seems difficult to identify a catalyst in the near term.

Consequently, US Treasuries have continued to trade in a range, with 10-year notes stuck between 4.00% and 4.25% since last September. With most of the major data releases for the month now behind us, it is tempting to look for an extension of this price action into the end of January, at least.
In FX, the dollar has also been in a narrow two-figure range versus the euro since last August. Here it is tempting to think that the greenback would actually be trading firmer were it not for ongoing attacks on US institutional credibility, which have weighed on sentiment.

Elsewhere, market moves in Japan have been more significant. With Prime Minister Takaichi set to call snap elections in order to strengthen her mandate, this has given a boost to domestic equities but has weighed on bonds and FX, due to fears for more dovish fiscal and monetary policy as a result. We think that some of these fears may be starting to become overstated. The budget for 2026 has been approved, and on interest rate policy, Takaichi has already demonstrated her willingness to allow the BoJ to hike interest rates, if only to stop the yen from continuing to slide weaker.

Takaichi is demonstrating that she is a leader with a popular touch. What will be key to her enduring success will be her ability to demonstrate a pragmatic and responsible approach that is able to keep financial markets on side, at a time when popular sentiment is becoming more optimistic.

This optimism is seen in an upward surge in sentiment in Japanese stocks, with the Nikkei index up an impressive 8% at the start of 2026. Anecdotally, this bullish mindset was also demonstrated by a record Tokyo fish auction price for the first tuna of 2026, with Kimura-san of the Sushi Zanmai chain bidding an impressive yen 510 million, well above the price recorded in recent years.

Large volumes of domestic savings in Japan are parked in cash and this made sense in an entrenched disinflationary economic environment. However, as inflation expectations normalise and Japanese companies make gains through increased labour efficiency, we could still be only at the start of a structural shift towards an increased risk appetite and a tilt back towards domestic markets on the part of wealthy Japanese household investors.

In Europe, the economic backdrop remains much more downbeat. It seems to be slowly dawning on policymakers that the EU is a horribly over-regulated regime which is pursuing a number of policy choices destined to structurally depress growth and sentiment for the foreseeable future.

The vigour seen elsewhere seems only to echo the narrative that we are witnessing a generational decline in Europe’s significance and relevance. Twelve months ago, the EU thought that an erratic US President would enable the voice of the EU to become more ascendant in the world order, but this has hardly been the case in reality.

Fiscal expansion in 2026 infers that the Eurozone economy may continue to grow around 1%, with Southern Europe continuing to outperform on a relative basis within the region. The ECB is more likely to cut rates than hike in 2026, though no change in monetary policy is to be expected in the next couple of quarters, and we see bund yields largely tracking sideways in this environment.

Sovereign spreads within the Eurozone have squeezed tighter and there may be some further incremental gains in the next couple of months. However, local elections in France could serve as a springboard to focus on the 2027 French Presidential elections.

A focus on national politics could revive concerns with respect to the longer-term future of the Eurozone and from that perspective, this represents a longer-term hurdle to additional spread compression.

The economic backdrop in the UK also appears subdued. The labour market is showing signs of contraction, which should help subdue wage growth and cause the Bank of England to become more inclined to cut interest rates over the months ahead. Although the economy may avoid a recession, it is bumping along the bottom in a stagnant manner.

Elsewhere in Europe, high energy prices are killing the EU manufacturing industry. As a service economy, the UK should be less exposed, relatively speaking. However, anti-growth policies from the government continue to depress growth and drive a sense of national malaise. In the middle of winter, it is a cold and dark time, and optimism feels in very short supply across the country.

That said, this downbeat assessment could mean better news for gilts – at least for the time being. Later in the year, after local elections in May, we see scope for greater political upheaval and instability, though this should be contained in the next few months as few in Labour will want to inherit the widely expected drubbing that the party is set to experience at the polls at that time.

In credit markets, spreads remain at tight levels. The backdrop for very heavy supply will likely represent a strong headwind in 2026, though with US recession risk probabilities dropping below 10% in the year ahead, so it seems unlikely that spreads will widen by much, unless the broader macro narrative changes.

In the absence of spread compression, this has left investors looking for avenues to own carry. Carry opportunities exist in some higher yielding names in corporates and also sovereigns, such as Romania, where long-dated bonds continue to trade 300bps above German bunds.

We also see carry opportunities in EM local rates in markets such as Brazil and Colombia, where we think term premia is excessive and where we are hopeful for constructive political developments later in the year. Carry also appears attractive in FX at a time of low volatility. This can be seen in some of the very high yields and frontier markets including Egypt, Nigeria or Turkey. It is also seen in Europe in FX including the Norwegian and Icelandic krone.

Looking ahead

With the Treasury MOVE Index of yield volatility hitting a 4-year low this week, it seems that the current market equilibrium can continue to hold unless there is a material shock that prompts a revision in the assessment of the broader economic backdrop.

In this context, one potential driver of volatility could come in the scheduled ruling on Trump's use of IEEPA tariffs. A decision from the Supreme Court justices could come at any time and it may appear likely that the final decision will be to find against these tariffs, potentially opening the door for claims of repayment. Since the loss of this tariff revenue would push the deficit upwards by 1% of GDP, it is widely expected that other tariffs will be put in place in order to avert a situation where US fiscal finances are called back into question.

When looking at new tariffs that could be implemented, there are three potential avenues that the administration could use. The first pertains to Article 301 tariffs relating to National Security. These require a case to be prepared but since one already exists in the case of China, this is one tariff that could be hiked quickly. It is understood that the US already has completed the groundwork for a 301 tariff on the EU, in lieu of the bloc's Digital Service Tax and so this is also one to watch.

In addition, Article 232 on sectoral tariffs can be implemented alongside those that have already been put into place. However, an issue with these 232 tariffs is that they are subject to a vote in Congress after a 150-day period, and this is probably something Trump would be keen to avoid.

Lastly, article 122 tariffs can be aimed at countries running large bilateral current account surpluses with the US. Yet, looking at the upshot of all this, there is a sense that the national and sectoral contours of any tariff outcomes using this raft of provisions may look quite meaningfully different to what is in place today. As well as creating some uncertainty and potential volatility, it may also throw up a new list of relative winners and losers on a global basis.

We also find it worth reflecting on how Trump may behave in the face of an unfavourable outcome from the Supreme Court. It may appear that since the start of the year, the President has come out swinging at opponents left, right and centre.

Trump seems emboldened to think his will can prevail and he can get his own way. The worry is that with the President in a Fast and Furious mode, there may be a point when this leads to a more material moment of disruption in financial markets, as was seen in April last year.

However, in the short term, these worries seem very much contained. Many Trump sceptics and naysayers having been forced into retreat through the course of 2025. It may appear that the broader backdrop for financial markets continues to look mostly constructive at the start of 2026 and the question is – for how long can this continue to be the case?

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