RBC BlueBay
Asset Management

Marketing communication

Kept in the dark

Market malaise and unknown unknowns!

Key points:

- **U.S. inflation data:** July CPI came in as expected this week, with the headline rate at 3.4% and core at 2.5% year-on-year.

- **Fed communication strategy:** Chair Warsh's no-guidance approach has continued, raising questions about whether he can control the FOMC narrative effectively.

- **Credit market resilience:** U.S. investment grade corporate spreads have remained stable, supported by strong demand from yield-targeting investors despite higher issuance.

- **Middle East energy risks:** TTF gas futures have pushed higher amid ongoing conflict, with diesel crack spreads near Q2 highs, threatening European inflation outlook.

- **Looking ahead:** markets may face a quiet August period, but energy inflation risks, Fed policy uncertainty and geopolitical tensions remain - and it can be exactly in these quiet moments when surprises catch markets off guard.

London, 14 August 2026: Market movements were relatively muted over the past week, with the mid-summer heatwave and the solar eclipse seeming to be the most notable talking points in Europe over the past few days. U.S. CPI for July was released in line with expectations, at 3.4% on the headline and 2.5% on the core measure.

Coming in the wake of a soft U.S. payrolls report last week, this has seen the market implied probability of a September interest rate hike from the Federal Reserve drop to just 35%, from being nearly fully priced just a few weeks ago. However, it is worth remembering that prior to this September policy meeting, we will see further data for the month of August and with higher energy prices showing up in those numbers, so we are inclined to see inflation moving back higher once more.

Consequently, we think that it would be premature to conclude that the FOMC won't raise rates in September and if economic data are consistent with our own views over the next several weeks, then we still expect a majority of the Committee to vote for a 25bps hike at that time.

In the absence of forward guidance, data takes on more significance in shaping expectations, though in this respect, the data calendar for the rest of this month is relatively quiet. Markets will want to look towards what Warsh has to share at the annual Jackson Hole gathering at the end of this month.

Yet, with the Chair's Task Forces still some weeks and months away from sharing their findings, it seems that Warsh will be in a position to share very little. In this respect, if 'no forward guidance' characterises the policy framework, then this means that markets will need to become accustomed to the Fed Chair saying much less, as was the case under Alan Greenspan and others in the less recent past.

However, this approach will only work if Warsh can bear down on the other members of the FOMC to hold their views more to themselves, as well. Otherwise, Warsh's own silence could risk him losing control of the narrative to others, and so it will be interesting to get a sense of whether he is winning the argument on this front.

Meanwhile, there has been further Fed chatter in the wake of the U.S. Treasury's intervention with respect to the yen. This utilised an obscure FIMA repo line, with some suggesting interference in Fed policy on the part of the Treasury, if part of the underlying intent has been to use the Fed's balance sheet to contain the risk of higher long-dated U.S. Treasury yields.

As Fabio Natalucci of Andersen has astutely observed, only Warsh, Williams and Jefferson at the Federal Reserve, are needed to approve Scott Bessent's subsequent suggestion to increase the counterparty limit on this quasi swap line above USD60 billion. Misuse of this FIMA repo line could reignite concerns with respect to Fed independence and the risk of fiscal dominance.

Treasury yields and investment grade corporate spreads traded in a narrow range over the past week. Notwithstanding the noise with respect to rising corporate bond supply, which has seen spreads for the AI hyperscalers moving progressively wider over the past few months, the reality is that the US Investment Grade Corporate Index spread has continued to trade in a narrow range between 75bps and 80bps since the end of April, mirroring the level where we sat at the end of December last year.

Credit demand has been helped by higher absolute nominal yields over the past number of months, with demand from yield-targeting investors. With recession risk low and financial conditions accommodative, so an abundance of liquidity has meant that it has been possible to generate demand for new debt (and equity) issuance in recent months. Though with the debt pipeline only continuing to spiral higher, one possible concern is whether demand will dry up, as and when policy is tightened and liquidity drains from the system.

Economic theory dictates that a relentless upward march in government bond and corporate bond issuance will eventually lead to the 'crowding out' of prospective borrowers. In this respect, it is worth remembering that default cycles ultimately occur, at the point where borrowers are unable to re-finance their rolling debt at viable terms.

Consequently, this is a reminder of potential troubles that could lie ahead, though this does not seem to be a present concern that is making investors any more cautious. Indeed, the past several weeks have seen an increase in credit exposure reported in positioning surveys, as credit bears close hedges and find themselves squeezed back into markets at a time when low spread volatility means that earning an incremental 75bps over government bonds continues to offer some allure.

Elsewhere in global markets, Europe has been unsurprisingly quiet in the middle of August, with little to report. However, the ongoing impasse in the Middle East represents a building risk to the region, with TTF gas futures renewing a push higher, which will hold negative implications for regional inflation, later this year.

Although we have been enduring (and sometimes enjoying) sweltering summer temperatures, the reality is that a change of seasons is not now far away, and depleted gas reserves need to be replenished ahead of winter. Hopes for an end to conflict and lower prices have fallen away and more broadly it is also worth continuing to highlight crack spreads, now at USD65, meaning that many distillates, including diesel, are trading at levels not far below their highs recorded in Q2 this year.

Generally speaking, developments in the energy complex and the Middle East more broadly, remain consistent with a higher inflation outcome than is being priced in financial markets. In this respect, we continue to hold a favourable view on U.S. inflation-linked bonds and swaps. In Europe, a weaker growth backdrop means we are more constructive on duration, relatively speaking.

We continue to favour Norwegian rates (due to past FX strength subduing inflation), the front end of the UK (given a dovish Bank of England) and Hungarian and Icelandic assets (on a theme of potential EU convergence). On this latter point, Iceland has a referendum on re-starting EU talks on 29th August. Should this pass, then we perceive that Brussels and the rest of the EU would be very willing and enthusiastic to bring the country into the Union.

In Japan, the yen gave up a good portion of prior intervention gains and with the currency just below Y160, it will be interesting to see whether the yen bears test the limits of intervention in the coming days, or whether policymakers in Tokyo and Washington will look to jump back into the market on a pre-emptive basis. Within Japan, it seems that it is becoming increasingly apparent that the BoJ will need to be permitted to hike rates at its September meeting, accelerating the path of monetary policy normalisation, in order to stymie further pressure ahead. Their hope, in the short term, will be that intervention and the threat of intervention will be enough to contain price action until the next BoJ meeting takes place.

Although we are currently in a summer lull, we expect that more decisive trends will emerge which we can capture over the next few months and so otherwise, it is a time to remain disciplined with respect to risk taking and to be relatively patient.

Looking ahead

It may not come as a big surprise if the coming week is another quiet one. We are through earnings season, between central bank meetings, and facing a very light economic data calendar at a time of year when many are taking time away from their screens. That said, it can be exactly in these moments when surprises can catch markets off guard, and in this respect, we know that it is always the unknown unknowns, which can have the biggest market impacts.

As for unknowns, it was interesting to hear about recent plans to smuggle President Trump off Air Force One and onto an alternative plane, via a catering truck. Perhaps this is a tangible reminder of the dangerous times we currently live in. Mind you, there may be something that seems half comedic in this particular episode, perhaps more reminiscent of a Saturday Night Live sketch than a James Bond movie.

Mind you, if the rest of Air Force One was kept in the dark, prompting some sense of indignation after the event, so the same has been echoed around the corridors of the ECB, in the wake of the recent U.S. actions in the yen, which saw it unloading euros without any thought to prior consultation.

In a week where many of us were left in the dark by the eclipse this week, maybe this is a sign of the times! In that respect, you are left half-wondering what is currently going on which we are not being told about, and what will be the next major development that only comes to light after the event. We will certainly be doing our best to find out….

Contact:
Lydia Cambata
lcambata@bluebay.com

About RBC BlueBay Asset Management
RBC BlueBay Asset Management ("RBC BlueBay") represents RBC Global Asset Management outside of North America and is an active asset manager with expertise across fixed income, equities and alternatives.

RBC BlueBay's solutions-driven approach means it endeavours to empower clients with the knowledge they need to help shape their investment decisions. It works and evolves with clients, creating and customising investment products that meet their needs.

Responsible investment is embedded across RBC BlueBay's business. This means it is not just an investment focus but is also ingrained in its client service experience and work to deliver solutions that support real-world impact.