Fixed Income Weekly

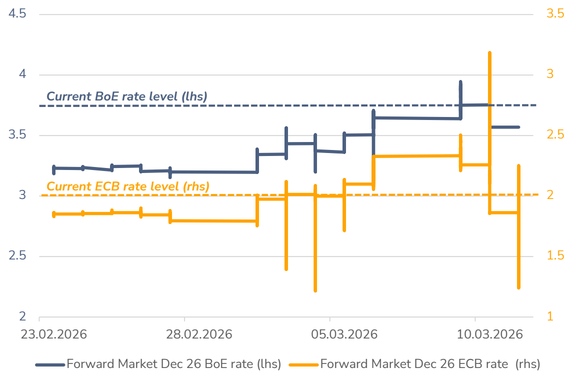
An interest rate shock coming from energy prices

Syz Fixed Income Research – Week from 02 to 06 March 2026

Surging energy prices shake rate markets, spreads face moderate upside pressures so far

The Chart of the Week

Wild swings in expectations around European central banks' rates



From quiet and dull to highly uncertain. Among all the spectacular movements witnessed since the beginning of the US and Israeli strikes on Iran, fluctuations in future pricing of central banks' key rates in Europe have been particularly remarkable and have fueled volatility across fixed income markets.

Prior to the strikes, the outlook for European Central Bank rates in 2026 appeared clear: the ECB was set to keep its rates unchanged this year in a context of stabilizing growth dynamics and moderating inflationary pressures, with a 25bp rate cut being a possibility. Meanwhile, in the UK, slowing inflationary pressures and concerns about the growth outlook had cemented expectations for two 25bp rate cuts by the Bank of England in the months ahead.

However, the sudden surge in energy prices and its potential impact on European economies, highly sensitive and vulnerable to rising energy costs, has abruptly shifted expectations. The risk of a stagflation scenario, combined with fears of second-round effects amplified by currency movements, has led futures markets to expect tighter monetary policy in Europe.

On Monday 9 March, two 25bp rate hikes were briefly priced in for the ECB before those expectations eased following the pullback in oil prices. A rate hike was also briefly priced in for the BoE, a notable reversal from the rate-cut path expected until late February.

Central banks are likely to wait for greater visibility on the duration of the energy price shock and its impact on inflation and growth dynamics before reacting. In the meantime, futures market expectations are likely to remain highly volatile and continue driving movements in rate markets in the days ahead.

What happened last week?

Central banks

The conflict in the Middle East and the surge in oil prices suddenly cast an unusual amount of uncertainty around the outlook for inflation and monetary policy across most major central banks. Federal Reserve officials signaled a broadly cautious stance as inflation remains above target and geopolitical risks add uncertainty to the outlook. Several officials, including regional presidents, warned against complacency and highlighted persistent price pressures in services and sectors such as healthcare. The surge in oil prices following US and Israeli strikes on Iran has further complicated the outlook, with some policymakers noting that prolonged energy shocks could delay easing. Minneapolis Fed President Neel Kashkari said the conflict makes him less certain about a rate cut this year, while Richmond Fed President Tom Barkin stressed the need to assess whether the shock proves temporary or persistent.

ECB officials also struck a measured tone as the Middle East conflict drives energy-price volatility and clouds the euro-area outlook. Several of them warned that sustained increases in energy costs could trigger second-round effects on inflation but stressed that temporary price swings should not prompt immediate action. Markets have begun to price the possibility of a rate hike later this year, though ECB President Christine Lagarde and colleagues stressed that decisions will remain data dependent.

A similar approach was mentioned by Bank of England policymaker Alan Taylor who urged central banks not to overreact to energy-price shocks, arguing that monetary policy cannot fully offset such supply-driven spikes. He emphasized that policymakers should focus on underlying inflation trends rather than temporary price swings and warned that the UK's economic backdrop remains fragile, suggesting prolonged tight policy could eventually weaken demand.

Central banks appear unlikely to react immediately to the recent developments in oil prices, waiting for more clarity on the length of the conflict and of higher energy prices, and the impact on inflation and growth before possibly altering their views. In the meantime, market expectations around monetary policy will likely remain volatile in the near future.

Rates

Global sovereign bond markets experienced a sharp sell-off last week as investors reacted to the risk of a sustained oil price shock and its implications for inflation. European fixed income was hit particularly hard, with yields rising markedly across the curve. Germany's 10-year Bund yield climbed 22bps to 2.86%, marking its largest weekly increase since the announcement of Germany's debt brake reform last year. Shorter maturities rose even more sharply, with the 2-year Bund yield up 31bps. Other European sovereign markets saw even steeper moves. UK 10-year Gilt yields surged 39bps to 4.63%, while French OATs and Italian BTPs rose 29bps and 35bps respectively. Peripheral spreads remained broadly stable despite the magnitude of the sell-off. The sharp repricing translated into negative performance for bond funds, with euro government bond ETFs falling between -1.4% and -2.6% over the week.

In the US, the adjustment was more moderate but still significant. Treasury yields rose across the curve, with the 2-year yield up 19bps to 3.56% and the 10-year yield increasing 20bps to 4.14%. Inflation expectations also moved higher, with the 10-year breakeven rate rising 10bps to 2.35%. Longer-duration Treasury ETFs posted the largest losses, declining up to -2.6% over the week.

Credit

The magnitude of the credit spread moves, especially in investment grade (IG), was modest compared to TTF gas price and oil prices last week. Oil price increased by 34% higher and TTF rose +56%. EUR IG spreads widened by only one basis point last week, while USD IG spreads even tightened by one basis point. However, total returns were negative across all credit segments as US Treasury and Bund yields rose materially. Both US IG and EUR IG declined by 1.1%, US high yield (HY) fell 1.0%, and EUR HY fell dropped 1.3%.

Within EUR IG, the utility and insurance sectors outperformed. In EUR HY, the communication sector delivered the smallest total return loss. In USD IG, insurance sector underperformed, reflecting concerns about their exposure to private credit. In practice, US insurers' direct exposure remains low, while Europe's aggregate exposure is even smaller and typically well diversified. At this stage, only EUR High yield appears to have meaningfully priced a near-term energy shock. Lower-rated European companies tend to be more energy intensive.

Fund flows are the closest real time indicator of investor demand in the credit markets. EUR IG recorded a small net inflow, but long-term EUR IG funds experienced another week of outflows. Investors favour short- and medium-term duration segments of the market. US IG and US HY recorded a small inflow. Meanwhile, pan-European HY recorded its largest weekly outflows this year.

Should disruptions persist for several weeks, credit spreads could widen further. Europe is particularly exposed to the energy shock, while shortage of nitrogen fertiliser could affect food inflation globally.

Emerging market

EM sovereign bonds were pressured by higher US Treasury yield and a stronger USD. EM local currency debt led the decline, with the J.P. Morgan EM Local Currency Bond ETF down 3.3%, erasing year-to-date gains. The sell-off was notable in Bahrain and Abu Dhabi, while Argentina outperformed. EM sovereign USD bonds fell 1.6%, and EM corporate USD bonds held up better (-1.1%). Despite the volatility, global EM debt funds recorded a fourth consecutive week of inflows.

Several EM exporters could benefit from higher commodity prices. Brazil, Argentina, Colombia and Nigeria are net oil exporters, while Peru gains from stronger gold prices. Chile's fuel stabilisation mechanism smooths oil price adjustments over a 21-day period, cushioning consumers.

In Colombia, the primary election produced a fragmented congress, requiring coalition governance. While uncertainty remains ahead of the presidential elections in May and June, the risk of a left-wing majority has diminished.

Iranian drone attacks on Saudi refineries and Qatari gas infrastructure highlight how even temporary disruptions can significantly impact energy markets.

Saudi Arabia can reroute part of exports via the East-West pipeline to Yanbu and benefits from large financial buffers, including over $450 billion in foreign reserves and substantial sovereign wealth assets overseas.

Oman could benefit from ports and oil terminals outside the Strait of Hormuz (Duqm, Salalah, Mina Al Fahal), supporting trade continuity. Any tourism weakness could be partly offset by higher oil prices and increased production. Fitch estimates that each week of a Hormuz closure could add 0.2% to Oman’s GDP growth.

Morocco received a Positive outlook (Ba1) from Moody’s, following S&P’s upgrade last September. With over two-thirds of global phosphate reserves, it is well positioned if fertiliser markets tighten.

China set a 4.5–5% growth target in its five-year plan. Domestic energy prices have risen less than global levels thanks to large oil inventories of over 140 days. Iran accounts for 12–13% of China’s oil imports, a manageable share.

Net oil-importers have been hit harder. Beyond energy, the Strait of Hormuz is also a key route for fertilizers coinciding the spring planting season in North Hemisphere, raising the risk of food inflation ahead.

Our view on fixed income

Rates

NEGATIVE in current environment

We maintain a Negative stance on government bonds. Positive global growth dynamics, price pressures in the US and profligate fiscal policies reduce the attractiveness of long-term government bonds as a potential hedge for economic downturn and increase the risk of higher long-term yields. Limited prospects of further central banks' rate cuts and unattractive yield curve slopes at the front-end also reduce the attractiveness of government bonds on short-to-medium term maturities.

Investment Grade

NEUTRAL, harvest the carry

We find Investment Grade corporate bonds attractive in the current environment, given their yield level and our constructive economic scenario. However, tight credit spreads reduced the margin for safety in credit and make the asset class expensive from a valuation standpoint. As a result, we keep a Neutral stance on Investment Grade credit from an asset allocation perspective. The credit market's overall health is supported by robust demand and strategic maturity management.

High Yield

NEUTRAL, favor short maturities

We like High Yield bonds with short maturity for their attractive combination of yield and low sensitivity to interest rate movements. HY spreads have tightened, signaling economic stability and contained default risk in the short run. However, those tight spreads are not attractive for medium-to-long term maturities as they do not compensate adequately for a potential deterioration in the economic environment. As such, we hold a Neutral view for High Yield in an allocation, with a clear preference for short-duration investments. We continue to find value in subordinated debt.

EM

NEUTRAL, with opportunities

We advocate for a careful selection of issuers to benefit from attractive absolute yields. Global growth dynamic, a weaker US dollar, contained public debt & corporate leverage along with strong flows are supportive for EM debt However, risks persist, with rich valuations and unpredictable Trump's trade policies. Idiosyncratic risks also remain, notably in Brazil and India. Given this backdrop, we stay selective, favoring short and medium-duration opportunities while remaining Neutral on the broad EM debt asset class in a multi-asset portfolio context.