

One Oil Shock, A Knock on Five Doors

Eight months into the war, the resulting energy shock continues to add to bond-market pressures as governments contend with rising financing costs, inflation risks and uncertain growth prospects. Yet the conditions for a probable reversal differ across the US, euro area, France, Japan and India.



The central argument

The global bond sell-off is testing more than inflation expectations. Brent crude above \$100 is reviving inflation risks just as governments are issuing large volumes of debt, central banks are less able to provide support and AI infra investment is increasing private-sector demand for capital. The result is a higher hurdle for both public and private borrowers.

But this is not a uniform global debt crisis. The US is testing the market's appetite for duration; the euro area is testing how far the ECB must respond to renewed inflation; France is testing fiscal and political credibility; Japan is testing whether its domestic investor base can absorb debt as monetary policy normalises; and India is testing whether domestic demand can withstand inflation and currency pressures.

The key question is not whether yields can rise further, but what would make investors stop demanding additional compensation. History suggests that reversals tend to follow a change in the policy outlook, a credible fiscal decision or an improvement in the supply-demand balance, **not simply the passage of time.**

MARKET

WHERE IT STANDS

US: 10-year Treasury

Hovering around 5.1-5.2%, a decline from the 5.36% peak, after the CPI release, September headline CPI rose to 3.7% YoY from 3.4% in August; core CPI increased to 2.6% from 2.4%. The hotter print has renewed expectations of further Fed tightening.

Euro area: 10-year Bund

3.4-3.5%. September euro-area inflation rose to 3.8% from 3.2%, with energy inflation accelerating to 18.8%. The recent yield retreat therefore reflects market repricing and safe-haven flows,

France: 10-year OAT

4.9%, with the OAT-Bund spread near 140-150bp. French harmonised inflation rose to 3.4% in September from 2.6% in August. Budget approval and fiscal credibility remain important drivers of the spread.

Japan: 10-year JGB

~ 3.0%, after reaching higher levels earlier in the month; the 30-year yield reached a record near 4.15%.

India: 10-year G-sec

7.38-7.40%, September retail inflation rose to 5.54% from 4.83% in August, while wholesale inflation accelerated to 11.39% from 9.92%.

Five markets, five different turning points

MARKET	HISTORICAL REFERENCE AND WHAT TURNED YIELDS	WHAT IS DIFFERENT TODAY	WHAT THE PRECEDENT TELLS US TO WATCH
US	2023 Treasury sell-off: the 10-year yield rose above 5%, then fell by more than 100bp by year-end. Softer inflation data, a less restrictive expected Fed path and reduced planned long-dated issuance helped reverse the move.	Unlike in 2023, when the Fed's final hike had already occurred before Treasury yields peaked, the current sell-off follows a renewed rate hike, with further tightening still possible. Persistent Treasury supply and competition for capital, including AI-related investment could keep term premia elevated even if rate expectations stabilise.	A policy repricing may not be enough. Inflation surprises, the expected Fed path, term-premium compression and whether Treasury auctions clear without demanding higher yields.
Euro area	2011-12 sovereign crisis: peripheral yields exceeded 7% amid sovereign-debt and euro-breakup fears, while German Bunds benefited from safe-haven demand. The ECB's intervention helped compress spreads.	The current pressure is being amplified by energy inflation. The ECB faces a trade-off between containing inflation and avoiding further damage to growth; a sovereign backstop cannot remove that trade-off.	Distinguish overall yield levels from sovereign spreads: lower energy inflation could ease ECB rate expectations, while renewed fiscal stress may widen country-specific spreads.
France	2011-12-euro crisis: ECB intervention helped reduce broad sovereign-risk premia across the currency union. This is a useful precedent for spread compression, but not a direct match for France's current fiscal-political problem.	High debt, persistent deficits and political fragmentation make budget approval and credible fiscal adjustment central to the French risk premium.	the OAT-Bund spread, not just the French yield. A credible budget could narrow France's premium; a fall in Bund yields alone would not demonstrate that French fiscal concerns have eased.
Japan	2003 JGB volatility: The 10-year yield fell to around 0.4% in June before rebounding sharply as growth, US yields and BoJ policy expectations shifted.	The 10-year yield is now around 3.0% , versus 0.4% in 2003. August CPI inflation was 1.9% , while September wholesale inflation was 6.8% . The proposed food consumption-tax cut from 8% to 1% for two years is estimated to reduce annual revenue by around ¥5tn , raising questions over fiscal funding.	The key test is absorption capacity. issuance plans, BoJ policy and whether domestic banks and insurers sustain their JGB purchases as yields rise. Recent buying is encouraging, but it is too early to assume a broad repatriation of capital.
India	2013 taper tantrum: rising US yields and capital-flow pressure hit Indian bonds and the rupee. RBI liquidity and foreign-exchange measures helped contain stress as external conditions evolved.	The present pressure combines external vulnerability with domestic drivers: oil-led inflation, rupee weakness, tighter RBI liquidity and government borrowing supply. The RBI has also shifted towards calibrated tightening.	External stabilisation may not be sufficient. Lower oil prices and a steadier rupee would help, but a durable bond-market turn also needs manageable liquidity conditions and stronger demand at government auctions.

The common lesson is that **yields wont reverse simply because they have risen a long way**. They turn when the market revises the path of policy rates, the perceived risk of sovereign funding, the supply of duration or the amount of compensation needed to hold it.

AI and growth: A silver lining with a financing cost

AI-driven productivity gains could support growth and future tax revenues, but investment in data centres, chips and power infrastructure may add to financing needs and compete with government borrowing for capital. If financing costs rise before productivity gains materialise like they have started to, both private investment and fiscal flexibility could come under pressure. AI is therefore a potential source of both growth support and financing risk.



Conclusion: The next move will be local, even if the shock is global

The recent pullback in some bond yields suggests that higher yields are attracting buyers, but it does not yet establish a durable turning point. The latest US inflation data have renewed rate-hike concerns, while Europe's energy-driven inflation, France's fiscal uncertainty, Japan's changing policy regime and India's external risks continue to create distinct risks.

The key distinction is between a yield peak and a change in the forces driving yields. A sustained reversal would require more than a temporary decline in oil or short-covering: it would need a clearer policy outlook, resilient auction demand, easing sovereign-risk premia and lower compensation for holding long-duration debt.

The likely path is therefore uneven across markets. Higher yields may eventually support demand for government bonds and restrain inflation, but if they persist, they will also raise refinancing costs, constrain fiscal flexibility and weigh on private investment. The coming weeks will test whether improving demand can offset these pressures or whether inflation and financing needs force markets to demand still higher yields.

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