



RATHBONES

RATHBONE GREENBANK GLOBAL SUSTAINABLE BOND FUND

MONTHLY UPDATE AUGUST 2026

August reinforced the message that bond markets have entered a more demanding phase. While broad unease about the scale of developed governments' spending abounds, the month's sharp rise in government bond yields was actually driven by expectations that central banks will hike interest rates by roughly a full percentage point. While the Bank of England (BoE) held off raising after month-end, the US Federal Reserve did start tightening once more, taking the benchmark overnight rate to the 3.75-4.00% band. We used the broad-based weakness in global government bond yields to add to our 'duration' (the sensitivity of our portfolio's value to changes in interest rates).

We think central banks are more likely to make one to two hikes over the coming year, depending on how the Middle East conflict proceeds and how it flows through to Western inflation via energy and fertiliser prices. That's roughly half the tightening that the market expects. Here in the UK especially, domestic inflation is weak, employment data is uninspiring, and the risks remain skewed to recession as opposed to an overheating economy. While the Middle East energy shock will likely push the BoE to hike rates, that would make the chance of an economic recovery even less probable. Given the much stronger starting point for the US economy (partially driven by AI capex spending), that's where we see the greatest chance of a central bank being able to deliver rate hikes in line with current market pricing.

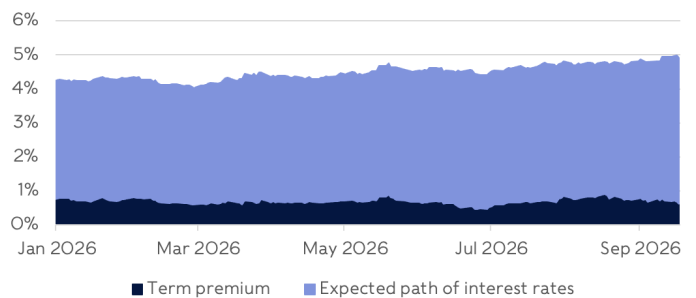
While the market effects of worsening government fiscal deficits and greater borrowing are higher than they've been in recent years, and these concerns are cropping up a lot in news coverage, they aren't the primary driver of recent upticks in yields. As you can see from the chart below, the US 'term premium' – the portion of a government bond yield that can't be explained by the market's expectations of how short-term rates will shift in the future – has actually fallen back in the last month or so. This term premium is influenced by several factors, but generally rises with uncertainty about the path of rates and falls when the market is more benign or when safe-haven assets are in high demand.

Concerns about heavy government borrowing and supply-and-demand dynamics are exerting a greater influence on both government bond and credit markets than in previous years, however. And higher yields are making public debts look increasingly unsustainable. We are taking this risk seriously. Yet, given that much of the most recent uptick in yields has been driven by what we think are overly aggressive forecasts of rate hikes, we felt it was prudent to increase our duration as bonds sold off.

Putting repricing in context

Investors are now demanding much higher yields: most developed countries' 10-year government bond yields have spiked much higher over the last couple of months. The 10-year US Treasury yield, for example, was 4.47% at the start of June and had risen to just above 5.0% at the time of writing, while the 10-year gilt yield rose from 4.90% to more than 5.30% over the same period.

FUTURE RATE HIKES LARGEST DRIVER OF HIGHER US 10-YEAR YIELDS



Source: New York Fed; Adrian, Crump, and Moench model-implied term premium between 1 January 2026 and 17 September 2026

During August, the yield moves were starkest at the longer-dated end of the curve. Mid-month, very long-dated government bond yields across the world's major economies were brushing up against multi-decade highs – the UK 30-year flirted with 6%.

The surge in longer-dated sovereign yields eased after the US Treasury started supporting the long end of the Treasury market by making larger buybacks of longer-dated Treasuries, and after the Fed announced a unanimous 25-basis-point rate hike in mid-September. We think there's probably a ceiling on how much further government bond yields will rise from here.

Treasury Secretary Scott Bessent's interventions in the Treasury market show that policymakers aren't comfortable with Treasury yields drifting much higher. And the Fed's decision to raise rates in September (its first hike in three years) seems to be doing the opposite of what hikes usually do. Instead of driving up Treasury yields further, they've levelled out since the Fed announced the move, mainly because the hike has helped instil confidence that the Fed will be sufficiently hawkish to prevent inflation getting out of control.

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Here in the UK, the BoE has finally addressed how its quantitative tightening (QT) programme has been pushing gilt yields unnecessarily higher. QT is where the BoE steadily sells down the huge amount of gilts bought during the quantitative easing of the past two decades. It has been doing this much faster than other central banks, which increases the supply of gilts that the market must absorb. This has been particularly acute in the 30-year space. We have long argued that the BoE should stop operations at the long end of the curve, given the pressure we have seen on yields there.

The BoE has come around to our way of thinking: in early September, it announced a big overhaul to its strategy. It will now hold about 70% of its remaining gilts to maturity instead of selling them over the coming years. It will halt its QT sales until April at the earliest while it investigates selling roughly £150 billion of them to the Debt Management Office (the government, essentially), rather than continuing to drop them into the market. That way just one public body (the DMO) would again be in charge of selling government debt, which would help make the market more efficient. It has also indefinitely stopped selling very long-dated bonds.

The summer's big reset in sovereign debt yields (and the resulting falls in bond prices) has been unsettling. Government bonds are generally expected to provide stability, so the scale of the moves at the long end has attracted a lot of attention. But higher yields also mean more income relative to the price investors pay. After the big rise in bonds' starting yields over the last four years, that income now provides a more meaningful cushion against near-term price volatility, particularly in higher-yielding markets such as the UK.

Are hyperscalers the new sovereigns?

There's a lot of talk, too, about the AI debt boom 'crowding out' government bonds. Much of the recent deluge of new debt from the world's largest tech companies – issued to pay for the computing power, data centres and energy infrastructure needed to build out AI at scale – comes at long maturities and carries very strong credit ratings, often in the AA to AAA range. That gives it some of the characteristics long-duration investors have traditionally looked for in government bonds.

Because the hyperscalers have issued so much so quickly, they're having to sweeten their yields to attract investors. In mid-August, Google parent Alphabet paid 1.05% over US Treasuries on the 20-year tranche of its August USD issuance – this compares with 0.75% over Treasuries for the 20-year tranche of its February USD issuance. We can also see this in Alphabet's inaugural Australian dollar bond issuance in August – the company had to pay just under 7% total on the 20-year tranche of this deal, its highest cost of borrowing ever. This does suggest that the hyperscalers are having to pay higher borrowing costs to get deals away. In turn, this may be helping drive up governments' long-term borrowing costs as they try to compete with the tech giants to attract a limited pool of long-duration capital.

Leaning into duration

In August, we extended the fund's duration (sensitivity to the direction of interest rates), especially our US duration exposure. We did this by buying more US dollar supranational organisation **Inter-American Development Bank (IADB) 3.2% 2042s**. As a reminder, we don't own US Treasuries because they don't meet our screening criteria. Instead, when we want exposure to US interest-rate movements, we favour US dollar-denominated debt issued by highly rated supranationals like the IADB, which we expect to behave in a similar way to Treasuries. We also bought more **UK Treasury Green Gilt 1.5% 2053s**, thereby increasing our exposure to the direction of UK rates.

We felt the summer's rise in longer-dated sovereign bond yields had created a more attractive entry point for duration exposure. With yields now much higher than in recent years, investors are being paid considerably more income, providing a stronger cushion against any further price volatility. At the same time, longer-dated government bonds retain the potential to generate capital gains at some point.

More broadly, we prefer to concentrate our duration exposure in supranational debt and government bonds rather than credit. That's because very long-dated corporate bonds carry significant 'spread-duration risk' (the risk that any widening in credit spreads farther into the future could offset some or all the gains generated by falling government bond yields). This preference helps explain why we haven't been tempted by any of the ultra-long-dated issuance from the AI hyperscalers. These companies enjoy strong credit fundamentals, but we worry that the additional spread available on their very long-dated corporate bonds doesn't always adequately compensate investors for the extra spread-duration risk they're taking.

Credit holds its nerve

While the big surge in government bond yields exerted downward pressure on corporate bond prices in August, credit spreads barely moved. Spreads, as measured by the ICE Bank of America Global Corporate Bond Index, widened very modestly, starting August at 79 basis points (bps) and ending it at 80bps.

Against this backdrop, we added selectively to bonds we already owned that we felt still looked attractively valued. For example, we bought some more French renewable energy supplier **Engie 4% 2035s**. We also bought more asset manager/insurer **Legal & General 5.55% 2052s**, as we think there's a good chance these bonds will be called (redeemed) early so we don't view them as carrying the duration risk typically associated with a bond maturing in 2052.

We also added to our subordinated bonds issued by a range of banks, buying some US dollar **Lloyds Bank 5.696% 2037s**, **Santander USA 5.22% 2032s** and Italian bank **Intesa Sanpaolo 6.005% 2037s**. The sharp rise in US Treasury yields has pushed these bonds' all-in yields to very attractive levels, allowing us to secure compelling income through exposure to some very strong issuers.

To fund these purchases, we sold a range of bonds, including some euro-denominated German renewables-focused energy supplier **ENBW 4% 2035s**, Finnish insurer **Sampo Oyj 3.375% 2049s** and luggage firm **Samsonite 4.375% 2033s**. All these sales reflected our ongoing relative value approach, whereby we look to recycle money from bonds whose valuations have become less compelling to buy bonds with broadly similar risk profiles that we believe offer better value. In addition, the returns available on these bonds once hedged back into sterling had become less attractive.

Compensation for uncertainty

As we move through the remainder of the year, bond markets are unlikely to enjoy a smooth ride. Questions around inflation, government borrowing and fiscal sustainability are likely to stay centre stage. And investors may continue to demand more compensation than in past for lending to governments long term.

For active managers like us, the more demanding backdrop is creating opportunities as well as risks. In August, we responded to market volatility by selectively adding to our longer-dated US dollar supranational debt and long-dated gilts where yields looked compelling, avoiding areas of very long-dated credit where we felt spread risk was not adequately rewarded, and adding to corporate bonds where we believed valuations and underlying fundamentals look attractive.



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For more info on our fund, including factsheets, performance and fund manager views, please click [here](#).

If you require further clarification on this commentary, then please contact your adviser or Rathbones at the contact details below.

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