

WSJ Print Edition

image

Soaring Bond Yields Can Protect Against AI Bubble

Rising Treasury yields this year have been explained as markets finally recognizing various potential disasters: Soaring inflation! Loss of trust in the Fed! Insane government borrowing!

All are reasonable concerns. Yet each of these struggles on its own to explain what's been going on, which is a general selloff in bonds maturing both soon and in the distant future.

Oil-driven inflation could mean higher Federal Reserve interest rates, which ought to increase yields on cash and near-term bonds but have less effect on bonds maturing further in the future— in bond jargon, flattening the curve of yields across time. It explains some of what's going on, but not why 10- and 30-year yields are up so much.

A loss of trust in the Fed should make investors worry more about inflation in future, and so demand a higher yield to hold longer-dated bonds—steepening the curve and pushing up the so-called breakeven inflation priced into bond markets. Yet the curve flattened and far-ahead breakevens barely moved.

The vast fiscal deficit and lack of political will to tackle it should make investors leery of lending to the government, again with more concern about lending for longer periods. Again, this didn't happen.

An alternative explanation—also not perfect—is that investors now expect a stronger economy, as they bask in the warm glow emanating from artificial intelligence.

“The market's shifted from a 'Goldilocks' regime [not too hot, not too cold] at the start of the year to reflation,” says Christian Mueller-Glissmann, head of asset allocation research at Goldman Sachs.

Reflation is the sort of inflation shareholders like, as a strong economy boosts stocks along with bond yields. AI contributes directly to a stronger economy via massive data-center spending and by making shareholders feel richer.

Investors are also betting that AI will raise productivity, meaning the boost to economic growth lasts and so brings permanently higher rates. That should lift bond yields across all maturities, and unlike the three negative explanations I started with, fits with record stock prices.

The AI explanation isn't perfect because recently on days when stocks rose, bond yields mostly fell.

The S&P 500 and 10-year Treasury yields had the strongest inverse relationship over two months, or 42 trading days, since 1999, measured by the correlation of daily changes. If AI is driving them both, I'd expect them to rise and fall together, but big oil-price swings may be interfering by affecting bond yields more than share prices.

All the “bad” explanations continue to pose a threat to bond investors. Inflation, a weak central bank and fiscal incontinence are all potentially terrible for bonds.

But investors who worry that AI euphoria has gone too far should consider Treasuries as an alternative with a chance to benefit if AI excitement fades and brings down yields.

— *James Mackintosh*

The following is a digital replica of content from the print newspaper and is intended for the personal use of our members. For commercial reproduction or distribution of Dow Jones printed content, contact: Dow Jones Reprints & Licensing at (800) 843-0008 or visit djreprints.com.

Thursday, 05/28/2026 Page .B012

Copyright (c)2026 Dow Jones & Company, Inc. All Rights Reserved. 5/28/2026

For personal, non-commercial use only.