Rates Spark: Positive impulses, but Treasuries are not for moving

Wednesday probably sees daylight on the Supreme Court's decision on the IEEPA tariffs. It could rule them legit, and if so we just move on. We suspect they will be struck down, and we'll probably still just move on. This Treasury market is showing a remarkable capacity to just not care too much about stuff. It won't last, but it's what we've got for now

On Wednesday, the Supreme Court may decide on the legality of the IEEPA tariffs

The CPI report was net positive for bonds

The biggest number for the bond market on Tuesday was the CPI report. It was tolerably good, in the sense that a 0.2% month-on-month / 2.6% year-on-year outcome for core inflation some six months on from the instigation of a large rump of tariffs is a success, as the tariff effect is quite contained in terms of impact on consumer prices. The impact effect on the 10yr Treasury yield was impressive, as it snapped lower. But it recovered higher subsequently. The resilience of the 10yr yield to various cross winds has been remarkable of late. It's baulking at excuses to snap both lower and higher in yield. The auctions this week have been solid too, with 3's 10's and 30's all showing consistent negative tails and decent auction details. But still, minimal follow-through.

The US deficit data so far has also been, if anything, a net positive

The US fiscal deficit for the first quarter of fiscal year 2026 came in at $601 billion, which is actually $110 billion less than the same time last year. A big reason is that tax revenues jumped—up 13%, or $141 billion—thanks to higher income and payroll taxes and a bump in customs duties after tariff changes. Spending did go up a bit (2%, or $31 billion), but not enough to offset the revenue surge. There’s also a small wrinkle: some payments normally made on 1 January got pushed into December, but even adjusting for that, the deficit would still be about $112 billion lower than last year. Overall, revenues climbed faster than spending, giving the early year deficit a noticeable dip.

The angst with respect to the fiscal deficit has absolutely ramped down in recent months. The spread from 10yr SOFR to 10yr Treasuries is now into the 35bp area, following a steady trek down from the 55bp area seen in September 2025. That journey has coincided with gradual improvements in the fiscal deficit position, helped by tariff revenue. It's having a meaningful effect, as had the spread remained at 55bp, the 10yr Treasury yield today would be in the area of 4.4% (rather than the sub-4.2% we see currently).

Supreme Court decision should really be impactful, but it probably won't be

Wednesday may well see the Supreme Court decision on the legality of the IEEPA tariffs. Our basic assumption is for them to be struck down, and we think the market is generally of the same opinion. Confirmation of that would cause some consternation in the Trump administration, but we'd assume that a way will be found to re-erect the tariffs subsequently, either employing current acts of Congress, or writing new acts. There is no plan B to the tariff plan of President Trump, which he reiterated at Tuesday's speech in Detroit. We're not expecting a huge market reaction as a result, but it will be messy should there be an avalanche of demands for tariff refunds.

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