FIXED INCOME | Q4 2025

Investment Grade Corporate

Market Review and Outlook

Figure 1 | Market Review

	Sector	OAS TSY	QTD OAS Δ	YTD OAS Δ	QTD Total Return	YTD Total Return	QTD Excess Return*	YTD Excess Return*
	US Aggregate Index	27	-1	-7	1.10%	7.30%	0.16%	0.78%
	US Credit Index	73	3	-4	0.87%	7.83%	-0.02%	1.26%
	US Corporate Index	78	4	-2	0.84%	7.77%	-0.04%	1.19%
	Industrials	76	4	-2	0.65%	7.50%	-0.17%	0.93%
	Financials	78	4	-4	1.17%	8.24%	0.14%	1.66%
	Utilities	85	3	2	0.82%	7.76%	0.06%	1.10%
	Non-Corporate Credit	40	2	-8	1.12%	7.91%	0.11%	1.47%
Quality	A	64	3	-4	0.92%	7.84%	0.04%	1.28%
	Baa	97	5	0	0.85%	7.93%	-0.07%	1.26%
Maturity	Intermediate	70	4	-1	1.29%	7.95%	0.13%	1.31%
	Long	94	4	-4	-0.11%	7.44%	-0.39%	1.04%

*Compared to duration matched treasuries.
Source: Bloomberg. As of December 31, 2025.

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The U.S. fixed income market demonstrated considerable resilience in the face of persistent economic uncertainty and a U.S. government shutdown. Fourth quarter returns within the investment grade credit space were mixed though, with excess returns modestly negative (-0.02% excess return) and total returns that were positive (0.87% total return) – supported by a dovish Federal Reserve policy stance, expectations for rate cuts and strong investor appetite for relatively attractive yields. On a year-to-date basis, investor appetite for risk assets showed through better with positive excess returns of 1.26% and total returns of 7.83% on credit. Spreads on the credit index finished the quarter just 3 basis points (bps) wider from where they entered at 73 bps after a brief episode of widening over November reaching as wide as 80 bps. AI-driven growth dynamics and easing tariff concerns further contributed to positive sentiment. Notably though, a prolonged federal government shutdown into December disrupted economic data reporting, yet both market conditions and investor confidence remained firm, allowing spread sectors to withstand economic pressures such as rising unemployment.[1]

On the macroeconomic front, U.S. GDP growth surprised to the upside, reaching 4.3% as of the third quarter of 2025, with resilient consumer spending serving as the primary driver. This robust figure surprised many, given the foundation began to show signs of strain as job growth slowed and labor market conditions softened. Inflation, while still elevated, appeared to be moderating, with year-over-year CPI at approximately 2.7% through November 2025. The labor market reflected this cooling trend, as private employment growth decelerated to just 64,000 jobs added in November, while the unemployment rate edged up to 4.6%. Consumer confidence showed a modest improvement in early December, with the University of Michigan's Consumer Sentiment Index rising to 52.9 from 51.0 in November, largely due to improved expectations for personal finances among younger consumers. Nevertheless, overall sentiment remained subdued, weighed down by persistent concerns over high prices and a softening labor market, and confidence levels continued to lag historical averages.[1,2]

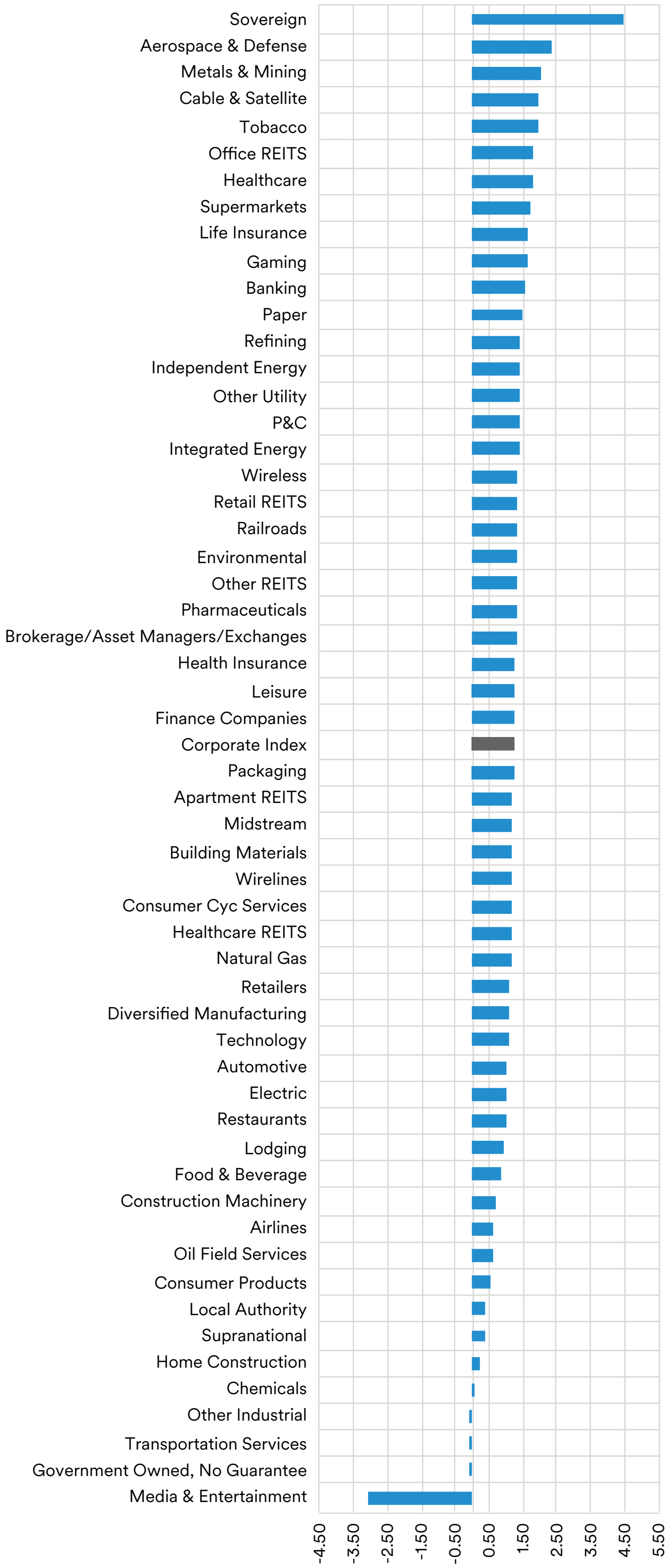
The 2s10s curve materially steepened over December, rising to 69 bps by year-end. This shift continued to signal market expectations for rate cuts at the front end, while longer-term yields remained stable to slightly elevated, likely due to lingering inflation/fiscal risk concerns. The 5s30s curve also steepened, with the spread increasing by about 13 bps over the period. This move continued to highlight investors' demand for a higher premium for long-duration risk, reflecting persistent anxieties regarding long-term inflation, government deficits or supply-side fiscal issues.[1,2]

In the fourth quarter, the U.S. corporate fixed income market experienced sustained demand from yield-focused investors, who continued to allocate capital to the asset class despite credit spreads remaining near multi-year lows. This robust demand was met by a significant surge in supply, driven primarily by a wave of large-scale AI-related issuance. This issuance came with significant concessions due to the size of the deals, which not only pressured existing hyperscaler debt but also the broader market, as this largely high-quality issuance reframed many relative value relationships. This wave of issuance pushed spreads wider for most of the quarter, only to see them retrace in December as activity in the primary market waned leading up the holidays.[1,2]

Across sectors, Banking (0.17% excess return) within Financials maintained stable credit profiles, benefiting from strong earnings, while BDC's and Finance Companies (0.08% excess return) were pressured by idiosyncratic credit events in the underlying leveraged finance markets. Energy (0.23% excess return) and Utilities (0.06 excess return) remained active in the market, financing capital expenditures tied to electrification and data center expansion. The top performer in terms of excess return was the smaller Transportation Services sector, which achieved a 0.55% excess return. Similarly, Automotives – a much larger sector, posted a 0.54% excess return over the period, which continued to be buoyed by easing input costs and production efficiencies. Conversely, the Cable & Satellite sector was the worst performer, with a -1.63% excess return, reflecting severe structural challenges in traditional media distribution. Sector divergence was also notable this quarter, with defensive sectors such as Consumer Non-Cyclicals (0.22% excess return) outperforming and weakness in sectors such as Technology (-1.14% excess return) and Communications (-0.83% excess return) given the overhang of the potential from AI capital expenditures and ongoing M&A within Media and Cable & Satellite.[1,2]

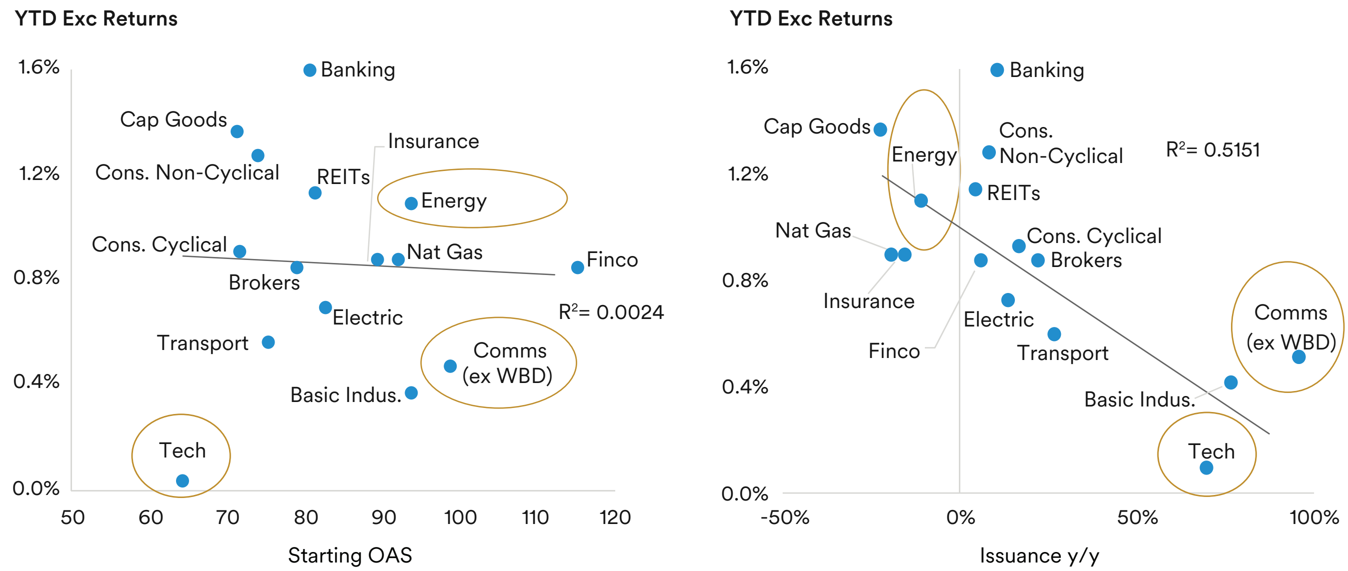
Figures 2 & 3 | 4Q 2025 Credit Excess Return (%) and 2025 Credit Excess Return (%)

Source: MIM, Bloomberg. As of December 31, 2025.



Source: MIM, Bloomberg. As of December 31, 2025.

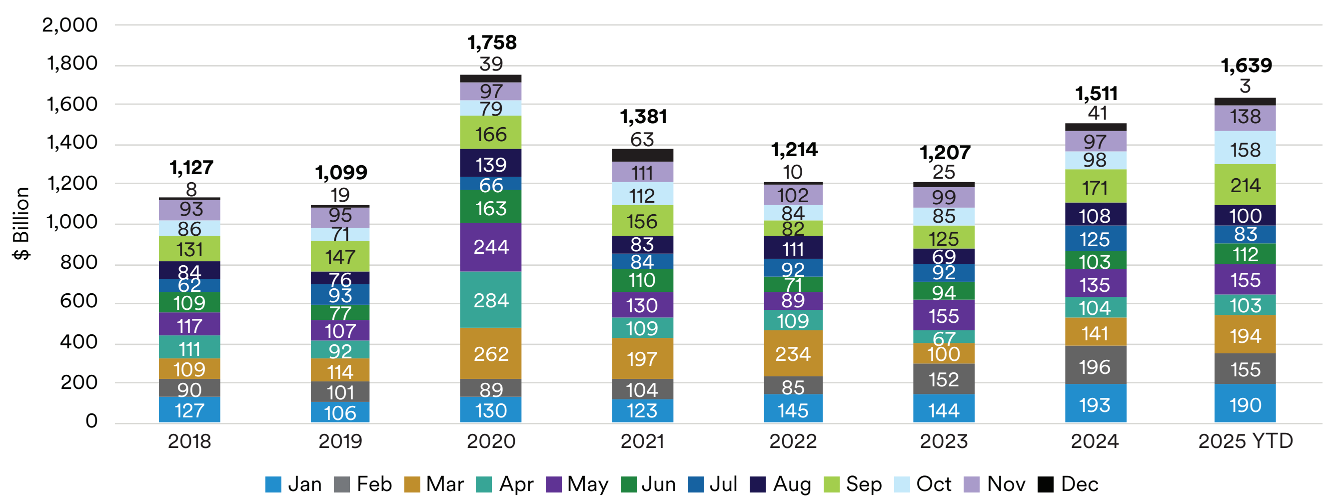
Figures 4 & 5 | Supply Was More Indicative of Performance at the Sector Level Than Starting OAS



Source: MIM, Barclays, Bloomberg LP. As of December 31, 2025.

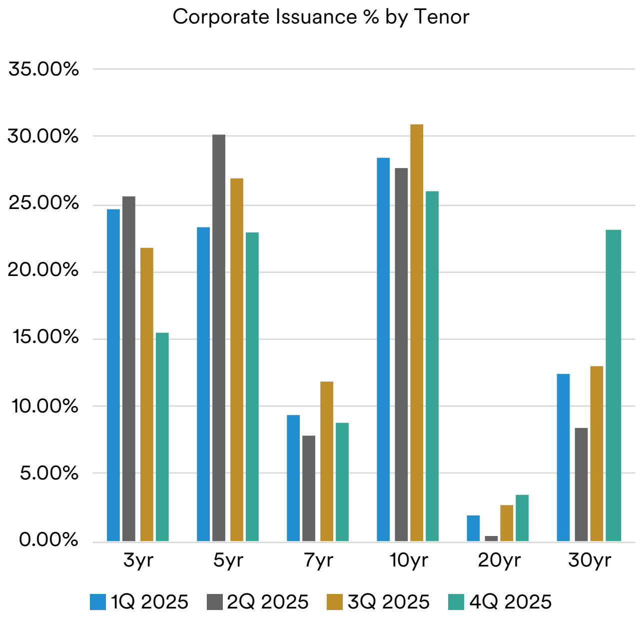
Fourth quarter issuance totaled $332 billion led by Non-Financials $241 billion or 73% of total issuance. October and November's issuance were robust, printing $159 billion and $138 billion, respectively. While M&A activity was less robust than we had anticipated this year, we saw activity and headlines start to pick up, led by the Technology, Media and Telecommunications (TMT) sector. However, the overarching theme of the fourth quarter issuance was AI hyperscaler capital needs, which are expected to continue into 2026. With the $15 billion Amazon deal and $17.5 billion Google deal priced in November, the five hyperscalers (AMZN, GOOGL, META, MSFT, ORCL) have collectively issued $81 billion in USD investment grade supply since September. Including a couple more deals earlier in the year and the $27 billion RPLDCI deal from October, total supply equated to $121 billion year to date – a figure that is up from the $28 billion average over the prior five years. This sheer volume of issuance contributed to Technology, Cable & Satellite, Media & Entertainment dragging in recent months.

Figure 6 | 2025 Issuance Outpaced 2024 Following a Robust Fourth Quarter

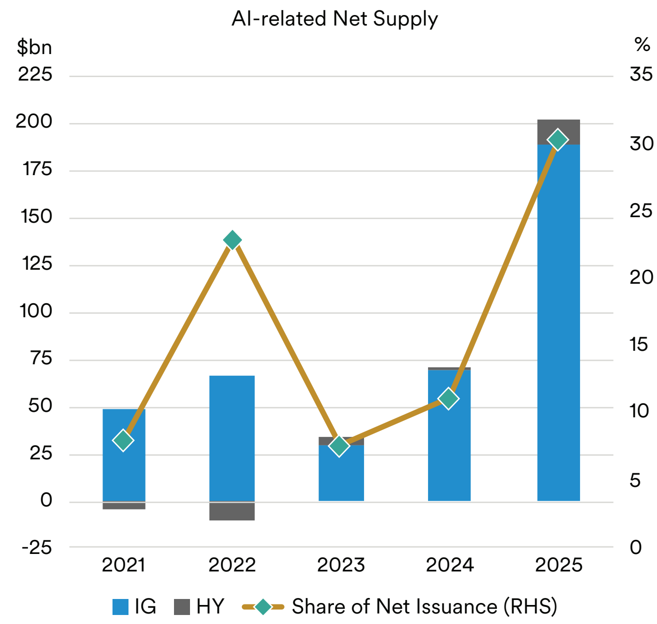


Source: JP Morgan. As of December 31, 2025.

Figures 7 & 8 | Long-Dated Issuance Surged in the Fourth Quarter, Led By AI-Related Supply

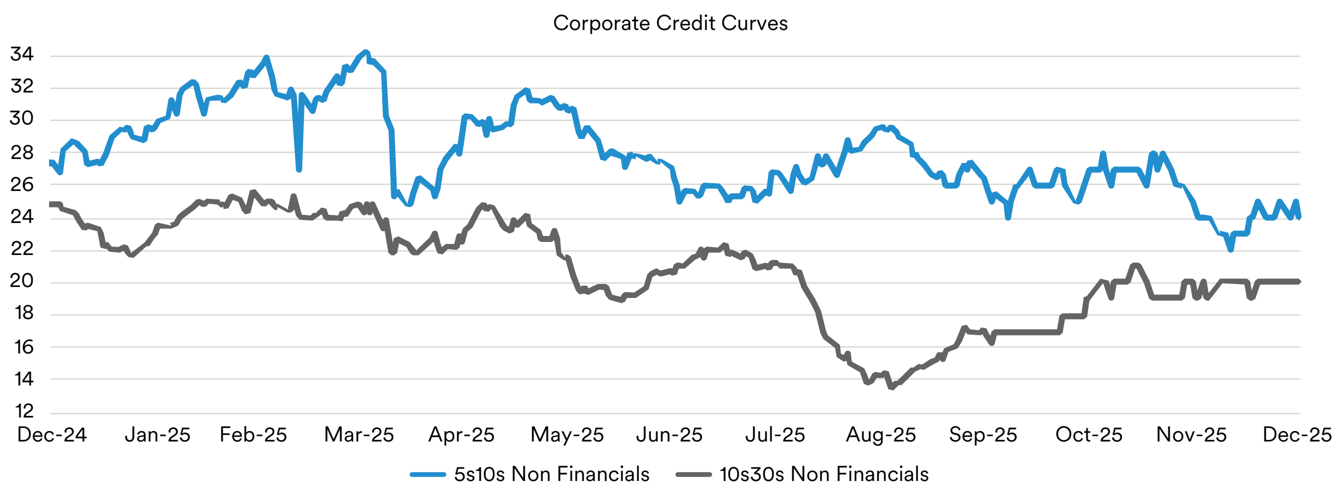


Source: JP Morgan. As of December 31, 2025.



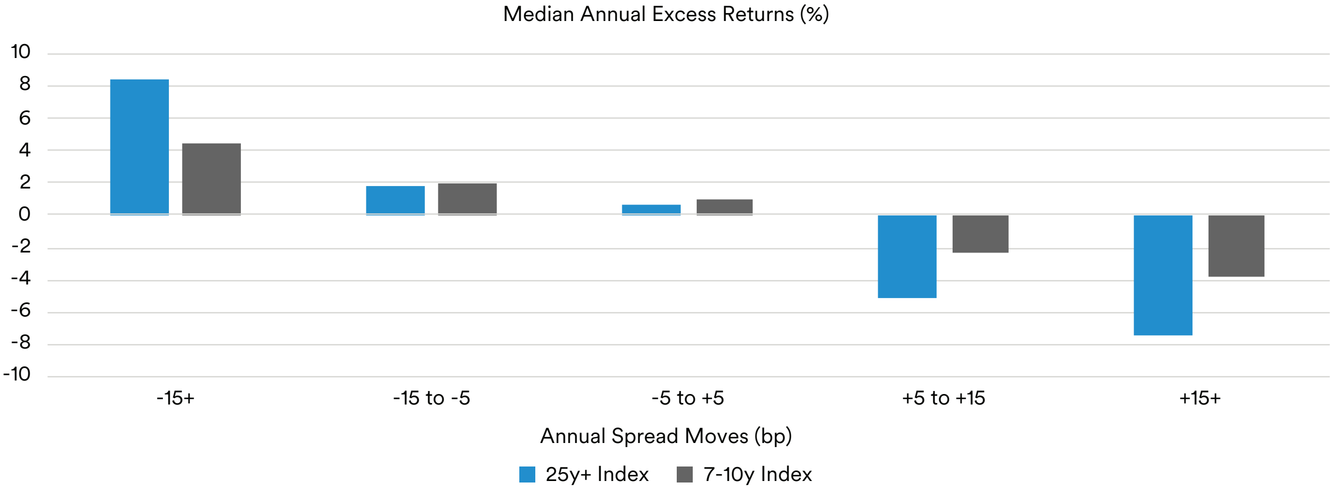
Source: Goldman Sachs FICC and Equities, Goldman Sachs Global Investment Research, Bloomberg. As of December 31, 2025.

Figure 9 | The Tenor and Magnitude of Issuance Pressured Spreads Out the Curve



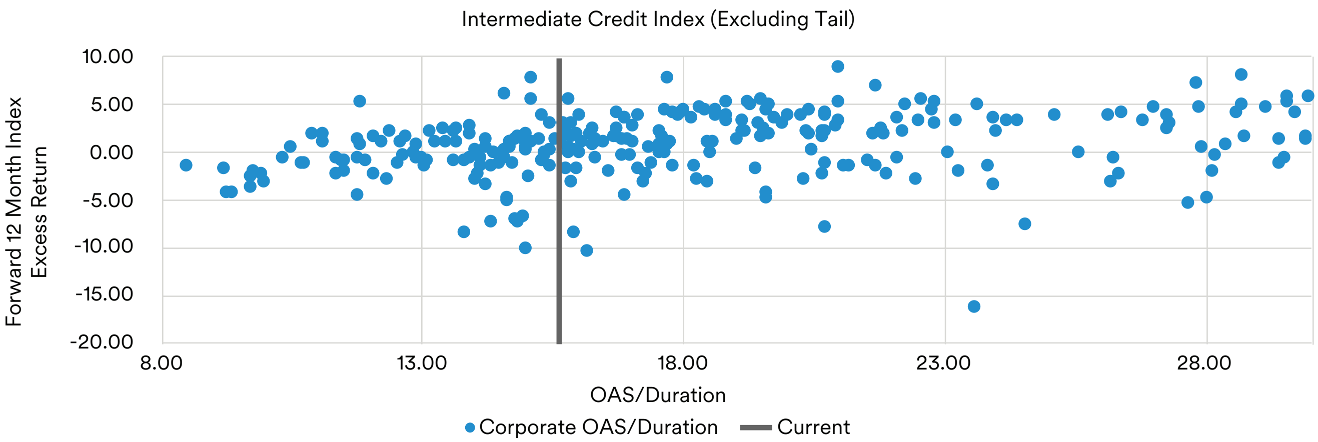
Source: ICE Bank of America Merrill Lynch. As of December 31, 2025.

Figure 10 | In Times of Spread Widening, the Belly of the Curve Tends to Outperform the Long End

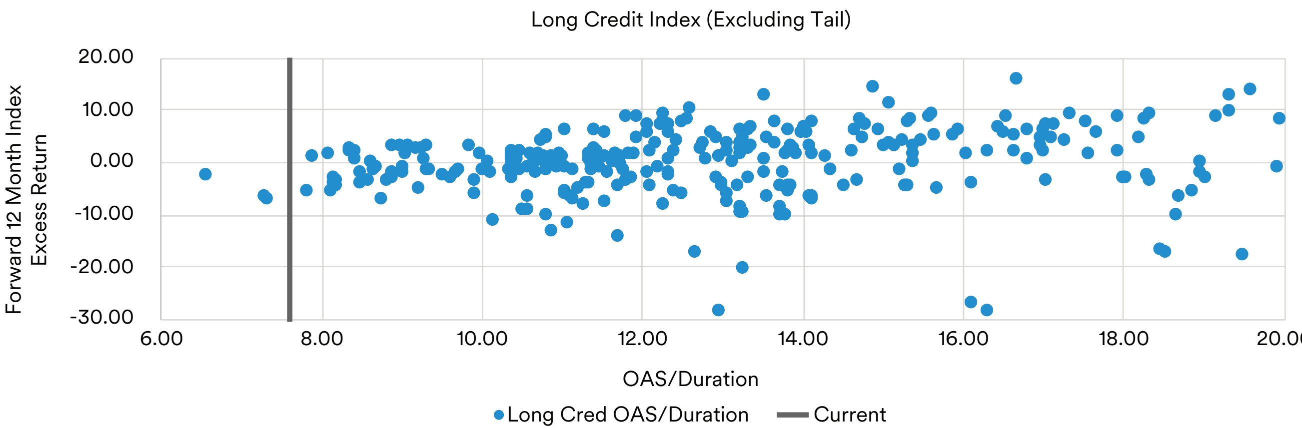


Note: Using data since 2000 to evaluate spreads and excess returns.
Source: MIM, Barclays, Bloomberg LP. As of December 31, 2025.

Figures 11 & 12 | Given the Prospects for 2026, We Still Favor Intermediate Relative to Long Credit

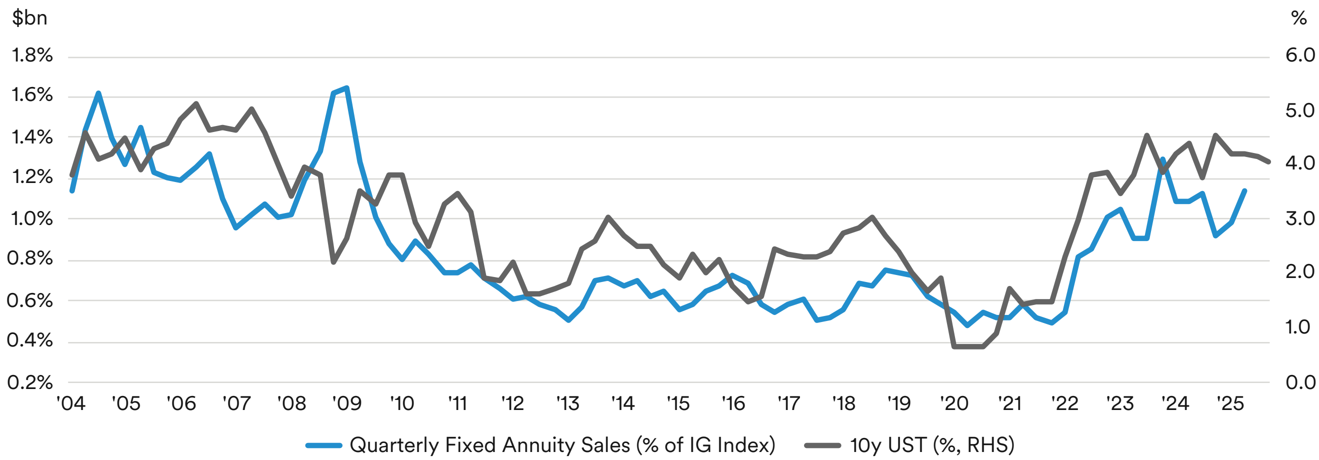


Source: MIM, Bloomberg. Data as of December 31, 2025.



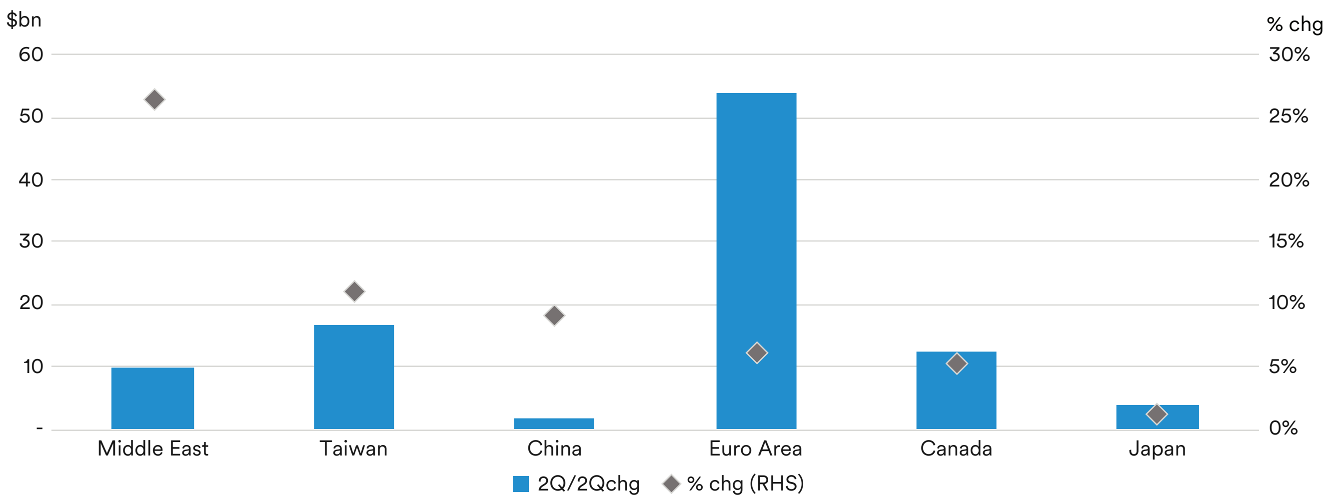
Source: MIM, Bloomberg. Data as of December 31, 2025.

Figure 13 | Yield-Oriented Buying Has Been a Consistent Source of Demand



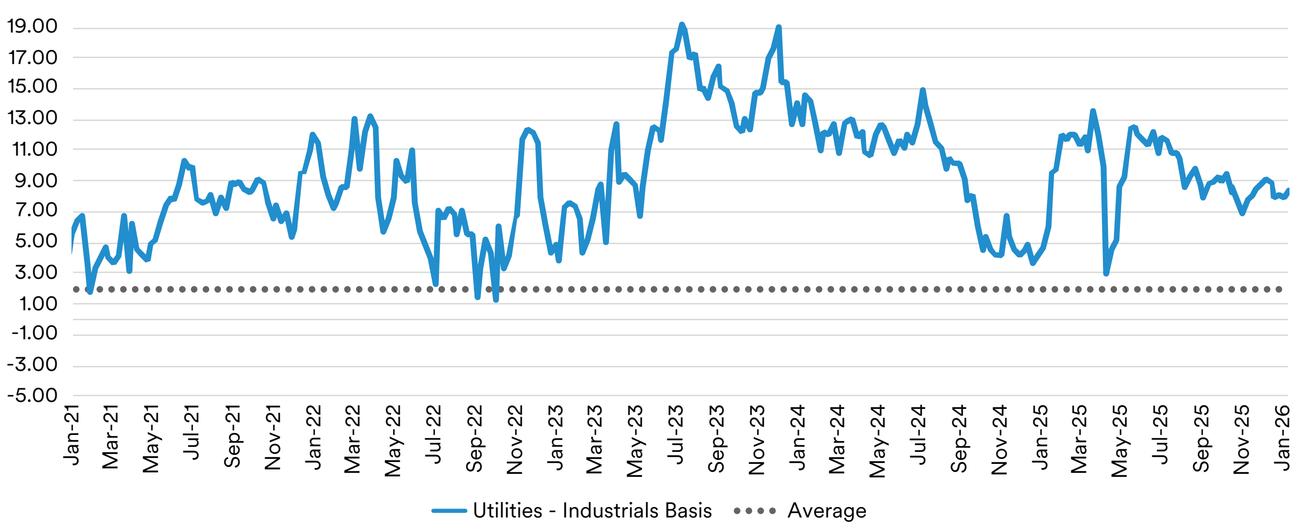
Source: MIM, LIMRA, Barclays. As of December 31, 2025.

Figure 14 | Overseas Demand Was Led by Buyers From Asia and the Middle East



Source: MIM, Barclays. As of December 31, 2025.

Figure 15 | Utilities Still Offer Defensive Opportunities Relative to Industrials



Source: MIM, Bloomberg. As of December 31, 2025.

Figure 16 | Banks Remain Attractive Versus Industrials, Despite Recent Spread Tightening

Source: MIM, Bloomberg. As of December 31, 2025.

As we reflect on 2025 and turn the page to 2026, the temptation was strong to simply copy and paste what we penned one year ago. Many of the themes expressed in client portfolios have not meaningfully changed over the course of the year. Certainly, from a valuation standpoint, very little has changed to warrant any material shifts in positioning. The Bloomberg Corporate Index tightened a measly 3 bps in 2025 and will usher in the new year at its tightest starting spread since 1997. At these levels, you would have a better chance of hitting the Powerball than to find a credit strategist that is willing to call valuations "attractive." That being said, it was another year of positive excess returns (albeit sequentially lower for the third consecutive year) and limited volatility away from the tariff-induced flareup in the second quarter. So, what is keeping spreads tethered to historically tight levels? Technicals. We highlighted that last year as the single strongest counterpoint to spread widening, and it came to fruition as supply remained modest and demand robust. Supply rose just 6%, with issuance (for most of the year) disproportionately favoring shorter maturities. Demand, meanwhile, remained bolstered by investors who continued to gravitate to 5+% yields like a moth to a flame. Insurance companies, foreign investors and retail investors were the main drivers of this demand (while sharply higher equity returns have kept pension demand muted for de-risking assets), overwhelming the slight bump in issuance. The fourth quarter, however, saw a decidedly different issuance trend, which is the clearest signal to us in quite some time that the technicals may be shifting in a way that may finally catalyze some degree of spread widening.

The overarching theme in Q4 was the sharp uptick in issuance to fund AI CapEx. Starting with a $27 billion deal secured by a Meta-leased data center (the largest security ever issued in the IG market) and followed by mega deals from Meta, Oracle, Google and Amazon that totaled another $80 billion of issuance – the race to spend is clearly on in the technology sector. These deals marked a sea change for trends in the credit market in a number of ways. One of the risks we flagged last year was a rise of "animal spirits" that would lead to large-scale issuance and balance sheet degradation. We were too early in this call, as the fluidity of government policy (primarily tariffs and the OBBB Act) delayed corporate activity, but the deluge of AI CapEx and likely uptick in M&A activity in 2026 leave this on the radar again as negative catalysts to monitor. The heavy Q4 issuance also underscored a shift in maturity preference, with the average tenor jumping a whopping three years, quarter over quarter, to 13 years – a level not seen in the last 23 quarters. We expect the long end to garner more share going forward, which should pressure 10s/30s spread curves. This was another theme in portfolios that we positioned for last year, and though it failed to materialize, we would note this as one of our higher-conviction ideas in 2026. Large financings tend to come with meaningful concessions, which can pressure the broader market. With capital markets forecasts as high as $2.25 trillion for 2026 (a 25% year-over-year increase that seemed unfathomable just a quarter ago), we would suggest the technicals that have largely been responsible for propping up valuations to 28-year tights are finally shifting in a way that could augur in the first year of spread widening in since 2022.

As it relates to how we will position portfolios for this shifting technical backdrop, we believe the case for employing ideas that fit the theme of “conservative carry” is stronger than ever. We will continue to look to take advantage of opportunities where we can move into more defensive credits, swap into lower USD securities and gain liquidity where such opportunities require minimal sacrifice of yield. We will continue to favor the front end and the belly of the curve where we can benefit from roll-down and attractive breakevens, rather than have to rely solely on spread tightening from the long end. This playbook worked during the brief April tumult, and we expect similarly positive results if we encounter another bout of macro volatility.

Looking at off-benchmark opportunities, last year we suggested emerging markets (EM) were one of the few areas that offered significant potential for spread compression. Our only regret here is not being more aggressive in our implementation, as EM credit was a significant outperformer in 2025. We are less enamored with that area of the market today, though an expected uptick in issuance could present some tactical opportunities. For portfolios that allow for high yield exposure, we would expect to continue to carry a below-average allocation, with the positions we do have likely to be concentrated in shorter-duration situations with compelling breakevens.

2025 featured a number of bumps along the way as well, with security selection being one of them. At these levels of spread, there are increasingly fewer credit stories that can conceivably generate outsized alpha. We noted last year that one key to performance would be getting some of these credit stories “right,” though we fell short of the standard to which we hold ourselves. Media and Technology were two topical sectors where we experienced a security selection drag – along with some challenged high yield situations. We expect these same stories to have potential to flip to positive contributors in 2026, while staying vigilant in uncovering new ideas that are underfollowed or underloved – areas that have historically been fertile ground for generating alpha via security selection, even in market environments where broader valuations are unenticing.

A less ballyhooed alpha driver is avoiding challenging credit stories, or those trading at overly lofty valuations. A benign macro backdrop has made the former less prevalent, but the proclivity of management teams to sacrifice the balance sheet (particularly now with better policy visibility) may mark a rise in creditor unfriendly behavior. Identifying and avoiding these situations will take on added importance in 2026. Conversely there were many examples of the latter, with high-quality credits trading at unfathomably tight spreads, where all it takes is issuance to quickly reprice the issuer’s curve. 2026 may well be a year (like 2024) when we spend more time talking about what we did not own than what we did.

We are excited about what lies ahead in 2026. A boring, compressed market is not our preferred environment, but the conditions are ripening to finally reintroduce dispersion and volatility into the market. Rather than try to craft a macro narrative as the driving rationale, we simply suggest that the technicals will flip, with issuance overwhelming demand and more bonds = wider spreads. Issuance is the drumbeat of the corporate market, and the resulting cacophony is likely to present us with a more robust opportunity set, than we have seen in some time, to lean into our passion for security selection to potentially uncover sources of alpha in credit portfolios.

Endnotes

1 Bloomberg. As of December 31, 2025.

2 Bank of America Merrill Lynch. As of December 31, 2025.

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