2025 FIXED INCOME OUTLOOK

Setting the pace

OPINION PIECE. PLEASE SEE IMPORTANT DISCLOSURES IN THE ENDNOTES.

What's inside

OPINION PIECE. PLEASE SEE IMPORTANT DISCLOSURES IN THE ENDNOTES.

Investment themes for 2025

Anders Persson, CFA®

Chief Investment Officer, Head of Global Fixed Income

Naming our outlook *Setting the Pace* emphasizes our view that global fixed income markets will likely take their lead from the U.S. We expect a stronger U.S. economy and the uncertainty surrounding the incoming administration's policies to set the tone.

The implications of this across the different regional economies are highlighted in the next section. From the U.S.'s soft landing and Japan's uptick in rates, to Europe's diverging fortunes and China's economic struggles, we discuss the global macroeconomic factors that will shape 2025.

These factors will influence the investment opportunities and risks across fixed income markets, and we explore what that means in the sector outlooks. Although valuations appear stretched across most global fixed income sectors, the key point for the year ahead is that fundamentals and technicals remain strong.

For a successful year in fixed income markets, investors should remain opportunistic and flexible in their allocation decisions. Four themes are guiding our investment decision making in 2025:

1. The current environment offers the best starting yields in over 15 years, representing a compelling entry point for fixed income investors.
2. Persistently elevated short- and long-term rates provide ongoing income opportunities for investors.
3. Positioning for bouts of market volatility amid potential policy shifts and a slowing economy is critical for optimizing risk-adjusted returns.
4. Balancing duration with credit risk across multi-sector portfolios will be key to achieving diversification and stability.

2025 presents a unique set of challenges and opportunities for investors. By staying attuned to economic trends, aligning with central bank policy expectations and employing diversified strategies, investors can navigate this environment with confidence.

U.S. to set global tone

While rates may have peaked in many – but not all – developed bond markets, the potential for healthy fixed income returns can be seen across sectors. Global fixed income markets will likely take their lead from the U.S. in 2025, with a stronger U.S. economy and uncertainty surrounding the incoming administration's policies setting the tone.

Fears of a U.S. recession, which dominated attention in early 2024, have receded materially. We expect a soft landing in 2025, likely characterized by slower real growth, moderating inflation and additional U.S. Federal Reserve (Fed) rate cuts. That said, the fiscal and regulatory aspects of the economy under a Trump administration present new uncertainty for economies and financial markets globally.

U.S. economic strength

Economic activity has slowed slightly but remains solid. Real GDP is on track to expand around 2.5% in 2024, down from the blistering pace of 3.2% in 2023. We expect this trend to continue, with growth slightly below 2.0% next year (Figure 1). The labor market has already slowed markedly, with unemployment up around 0.7% from its cyclical low. We expect that softening to continue.

Inflation uncertainty

Higher unemployment and the parallel slowdown in household income growth should weigh on overall economic growth moving forward, but it also should ease some inflationary pressures. In contrast, the likelihood of further tax cuts and looser fiscal policy in the U.S. could act as a counterbalance. We expect inflation to remain relatively sticky as these forces compete. Core goods inflation has already returned to target, that for core services remains stubbornly elevated, especially housing.

Potential near-term stimulus

In this environment, we expect the Fed will remain biased toward easing, but the central bank will proceed cautiously, likely leading to fewer cuts than previously anticipated. Our forecast is for a fed funds "terminal rate" of 3.75% – 4.00%. That is materially higher than the Fed's projections that assume a longer-run rate of just below 3.0%.

The gap largely reflects our expectations for near-term fiscal stimulus, which looks increasingly likely given the 2024 U.S. election results. Instead of dragging on growth in 2026-27, tax cuts will likely provide a small fiscal boost. The Fed is likely to partially offset that dynamic, resulting in relatively higher near-term interest rates than otherwise expected.

Trade policy risks

The incoming administration has proposed broad tariffs of 10% on all imports and more targeted, higher tariffs on goods from specific countries, notably China. These measures would likely quickly drive prices higher, lead to retaliatory tariffs from other countries and drive appreciation in the dollar. Altogether, the net effect would likely be a medium-term drag on growth.

Attractive yield levels

Given our macro and policy outlook, we expect the 10-year U.S. Treasury yield to remain roughly anchored around 4.25 – 4.75% in 2025. The upside risks to that forecast would come from greater fiscal stimulus, a resurgence in inflation or surprising labor market strength. On the other hand, downside risks to growth include more aggressive tariffs that could shift rates lower.

European growth on the horizon

In Europe, economic activity is on track to increase by a modest 1% in 2024, backed by resilient labor markets and the European Central Bank exiting restrictive policy rates. The central bank is poised to extend its rate cutting cycle through 2025 with the deposit rate likely to reach 1.75% by year-end. Further economic expansion in 2025 could be boosted by looser monetary policy alongside an increase in consumer spending supported by rising real incomes, a potential lift to export demand from China stimulus and a rebuilding of inventories as de-stocking has likely run its course. That said, uncertainty around U.S. trade tariffs could weigh on confidence and subsequently could shave 0.3% to 0.5% off real GDP growth in 2025, underpinning a forecast of sub-1% growth next year.

Sluggish Germany

Sentiment in Germany, Europe's largest economy, is already depressed amid high energy costs, geopolitical tensions and a structural slowdown in manufacturing activity. The risk of U.S. tariffs could further impede confidence, tipping Germany into a mild recession and heightening the need for fiscal support.

German bond investors began pricing in the scope for such stimulus after the recent collapse of the country's governing coalition. While a new government could lead to a more stable coalition and pave the way for fiscal flexibility, material changes are unlikely through 2025 given the likelihood of protracted negotiations. There may also be political resistance to reforming Germany's debt brake, a constitutional law that limits annual budget deficits to 0.35% of GDP.

In our view, the rise in German bond yields from fiscal developments appears excessive and renewed appetite for bonds is likely. Periphery spreads, such as Spain and Italy, could also be supported as the hunt for yield offsets any widening pressure from geopolitics while an unfavorable fiscal backdrop could further curb demand for French sovereign bonds.

Japanese rates at multi-year highs

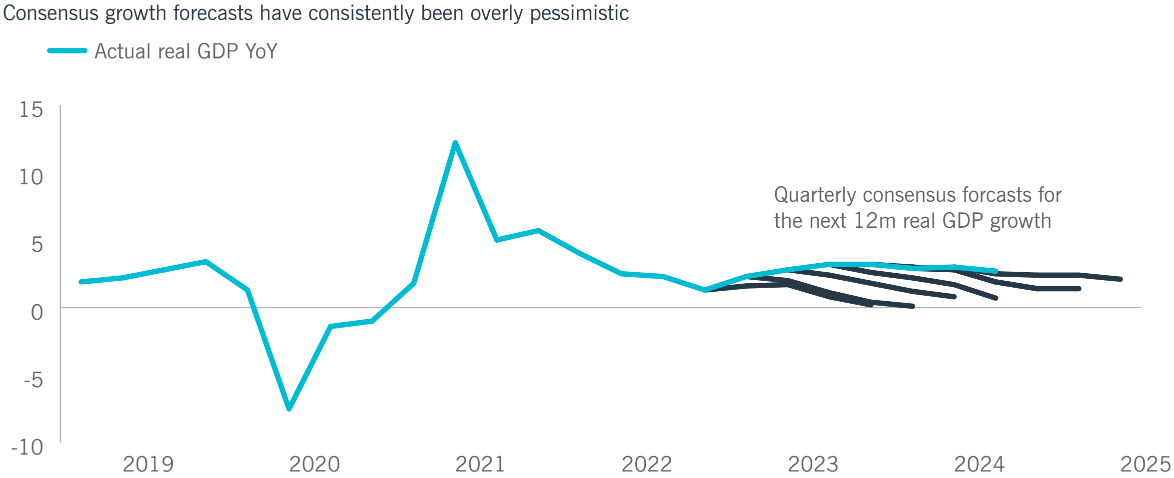
In contrast to other monetary authorities easing policies, signs of sustained inflation should prompt the Bank of Japan to extend its path to policy normalization through 2025. While political uncertainty in the wake of the national election tilts toward fiscal easing and a greater impulse to tighten monetary policy, a gradual pace of rate hikes should bring the policy rate to 1% by year-end with 1.2% real GDP growth forecasted. The last time this rate was 1% was almost 30 years ago – in 1995.

Divergent emerging market performance

A backdrop of higher-for-longer U.S. rates and geopolitical tensions also cloud the outlook for emerging markets economies. Countries with stable economic and political backdrops are best equipped to navigate geopolitical risks while those with greater exposure to U.S. trade restrictions are poised to underperform. As such, there are downside risks to China's growth, though uncertainty on the timing of tariffs points to a range of real GDP growth expectations from 4.3% to 4.8% in 2025, according to our analysis.

Figure 1: Underestimating U.S. – and global – growth expectations

Consensus growth forecasts have consistently been overly pessimistic



Data sources: Bloomberg and BEA (Bureau of Economic Analysis), 31 Mar 2019 – 30 Jun 2025.

Sector outlook

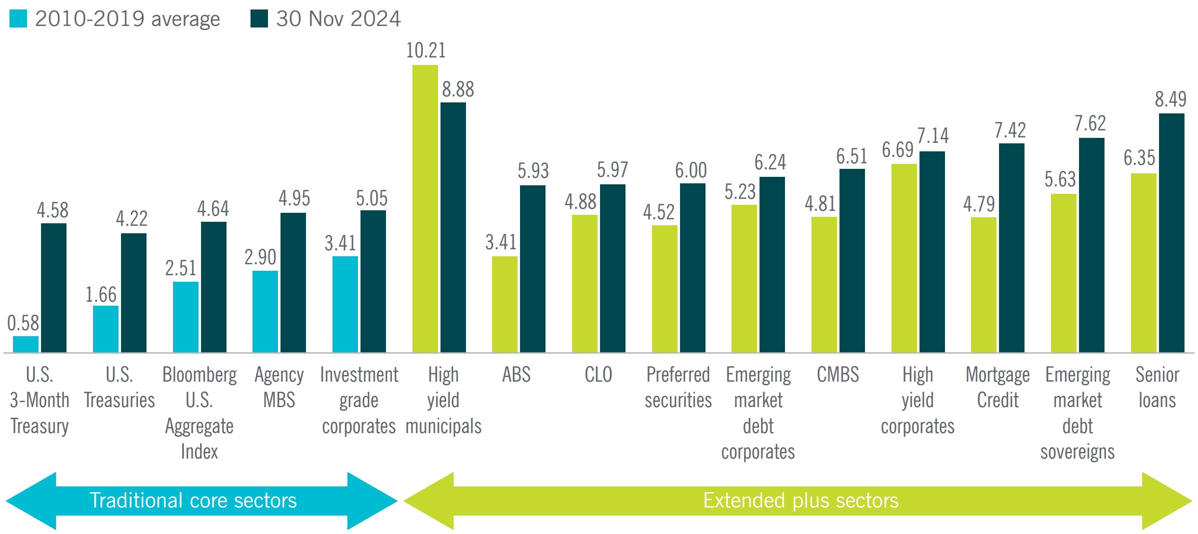
Leveraged finance

Broadly syndicated loans (BSL)

- With pro-growth policies expected from the Trump administration, both front-end and overall rates should remain elevated, providing a tailwind for BSL to deliver high levels of current income while insulating investors from traditional interest rate risk (Figure 2).
- Market technicals should support secondary price levels, while M&A activity should produce new issue opportunities to deploy cash at attractive yields. Net new issuance has nearly doubled in 2024 year to date versus 2023, and we expect significant growth in 2025.
- The unique floating-rate coupon structure of BSL has resulted in low correlation versus broad-based U.S. fixed income. And a loan's first lien position within the capital structure means low volatility per unit of return, resulting in attractive risk-adjusted returns.
- While default rates should remain relatively low given positive tailwinds from pro-growth policies, maintaining a liquid portfolio remains important. Active management and a focus on avoiding downside risks are critical.

Figure 2: Senior loans remain one of the highest yielding asset classes in public markets

Yield-to-worst by fixed income sector



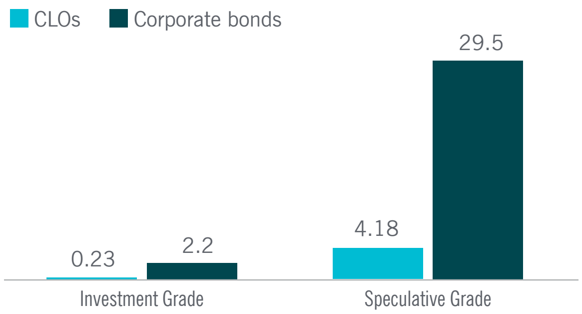
Data sources: BofA, Bloomberg LP, Credit Suisse, as of 30 Nov 2024. **Representative indices: U.S. Treasuries:** Bloomberg U.S. Treasury Index; **3-Month Treasury:** U.S Treasury 3-Month yield; **High yield municipal:** Bloomberg Municipal Bond (HY) Index (TEY at a 40.8% tax rate); **Mortgage-backed securities (MBS):** Bloomberg U.S. Mortgage-Backed Securities Index; **Commercial mortgage-backed securities (CMBS):** ICE BofA AA-BBB US Fixed Rate CMBS; **Asset-backed securities (ABS):** ICE BofA AA-BBB US Fixed Rate ABS; **Investment grade corporates:** Bloomberg U.S. Corporate Investment Grade Index; **Emerging market debt sovereigns:** JPM EMBI Global Diversified; **Emerging market debt corporates:** JPM CEMBI Diversified; **Preferred securities:** ICE BofA U.S. All Capital Securities Index; **Senior loans:** Credit Suisse Leveraged Loan Index; **High yield corporates:** Bloomberg U.S. Corporate High Yield 2% Issuer Capped Index; **Mortgage credit:** JPM CRT Mortgage Credit Reference Index. P**erformance data shown represents past performance and does not predict or guarantee future results.It is not possible to invest directly in an index.**

Collateralized loan obligations (CLOs)

- As U.S. policies seem likely to support growth, increased M&A activity should drive an uptick in new senior loan issuance in 2025 which should benefit CLO new issuance as senior loan supply and demand dynamics become more balanced.
- CLO activity boomed in 2024, driven by robust reset and refinancing activity as the decline in CLO liability spreads reduced financing costs for transactions issued during the last couple of years. CLO issuance at $364 billion through mid-November 2024 was second only to the $381 billion level in 2021. CLO issuance in 2025 is expected to outpace 2024.
- 2024 volume was well absorbed by investors driven by a mix of (i) new entrants in the market, (ii) attractive yield relative to other comparable / related asset classes and (iii) increased sensitivity to interest rate duration risk. We expect these factors to persist (in varying degrees) in 2025 (Figure 3).
- We expect that the combination of favorable senior loan and CLO technicals and fundamentals will support CLO liabilities spreads and provide a tailwind for CLO equity in 2025.
- CLOs have moved into the mainstream as an attractive complement to other alternative asset classes and traditional fixed income, with the CLO capital structure offering a spectrum of risk/return options.

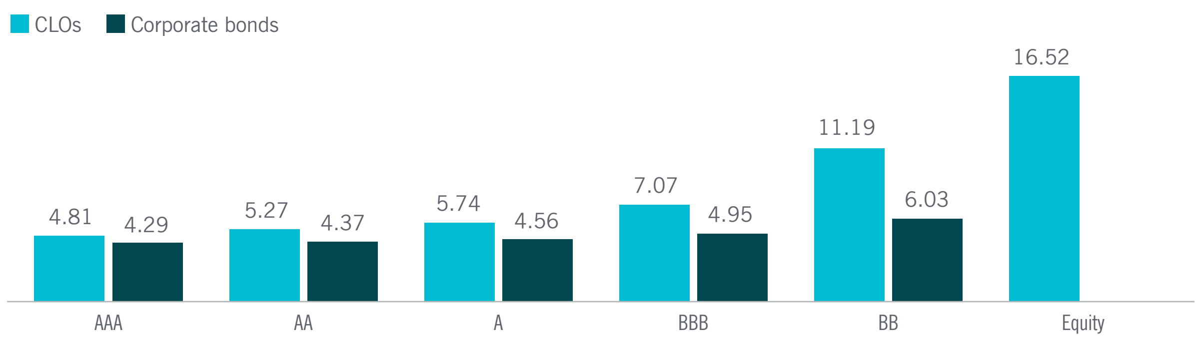
Figure 3: Lower CLO defaults with enhanced yield versus corporate credits

Cumulative default/impairment rates for CLOs (1993-2023) and corporates (1998-2023)



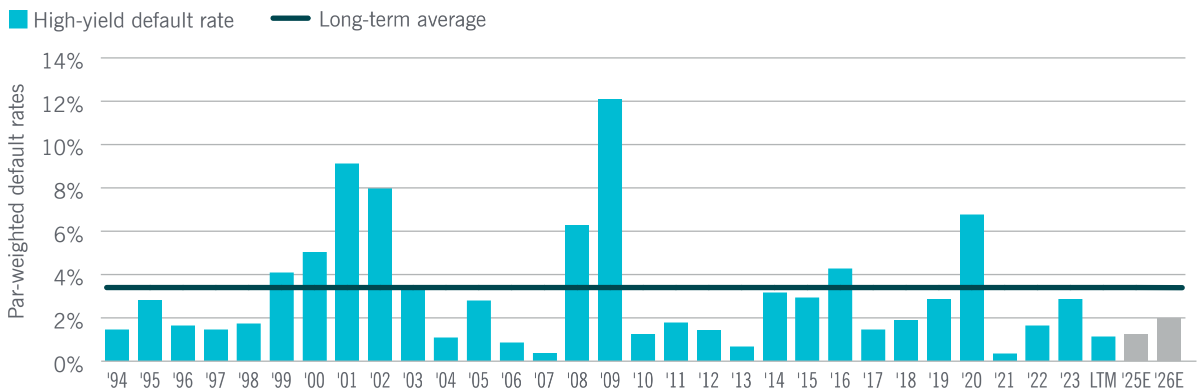
Data sources: Corporates: 10-year horizon average cumulative issuer-weighted global default rates by alphanumeric rating, 1998-2023 from Moody's "Default Trends – Global: Annual default study: Corporate default rate to moderate in 2024 but remain near its long-term average"; CLOs: US CLOs, 10-year horizon WR unadjusted cumulative impairment rates by original rating, 1993-2023 from Moody's "Impairment and loss rates of global CLOs: 1993-2023."

CLO debt yields compared to similarly rated corporate bonds (%)[2]



Data sources: Nuveen, Bloomberg, JPMorgan and Bank of America as of 30 Sep 2024. **Representative indexes: Investment grade corporates AAA-BBB:** Bloomberg U.S. Corporate Investment Grade Index; **High yield corporates BB-B:** ICE BofA US High Yield Index; **Investment grade and high yield CLOs AAA-BBB:** J.P. Morgan Collateralized Loan Obligation Index (CLOIE); **CLO equity:** US BSL CLO Equity Distributions (IO) median. Different benchmarks, economic periods, methodologies and market conditions will produce different results. There is no assurance that any asset class or index will provide positive performance over time. **It is not possible to invest directly in an index.**

Figure 4: 2025 default rates are expected to remain below the historical average



Data source: J.P. Morgan, 2000 - 2026 (estimated) as of Nov 2024. LTM: Last twelve months.

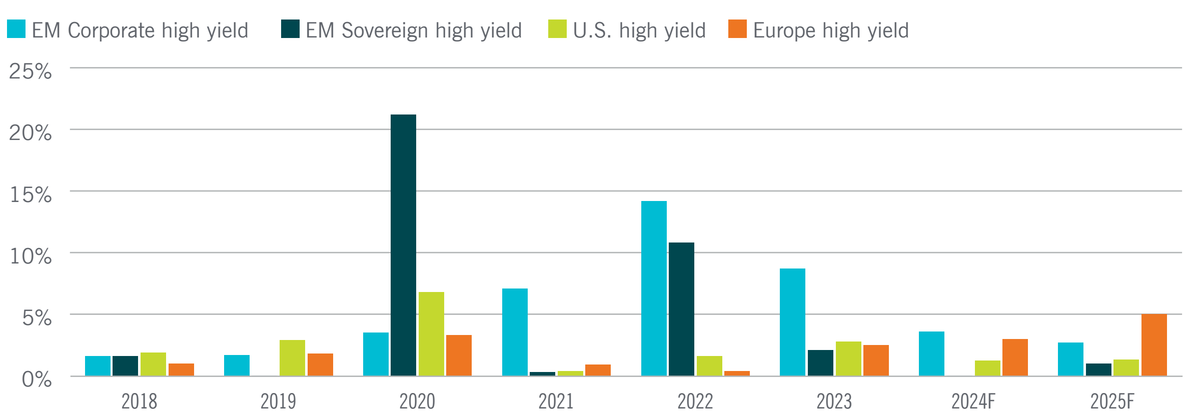
U.S. high yield corporates

- The U.S. high yield bond market offers attractive yields, currently above 7%. Trade policies, immigration reform and regulatory changes could impact the Fed's easing cycle and contribute to significant performance differences across sectors. With an average duration of about three years, high yield bonds offer better protection against interest rate volatility compared to investment-grade bonds and Treasuries. And the higher all-in yield today provides stronger downside protection than equities. Additionally, most high yield issuers are small-cap companies with predominantly U.S.-focused revenue, making them more insulated from tariffs than larger-cap companies with broader global exposure.
- Absent a severe economic downturn, high-yield bonds should continue to deliver attractive risk-adjusted returns. While credit spreads have tightened to historically low levels, the market's fundamentals remain strong, and defaults are projected to remain low (Figure 4). The asset class benefits from a higher quality composition, with nearly 50% of the outstanding debt rated BB and just about 10% rated CCC. Issuers generally have strong balance sheets, and supportive macroeconomic conditions further enhance the outlook for high yield bonds.
- Investors should remain vigilant, as macro uncertainties will cause performance to vary widely among sectors and issuers. This should allow active managers with robust credit underwriting processes to take advantage of relative value opportunities and generate alpha in the liquid part of the market. For our total return portfolios, and more selectively in higher quality portfolios, we are targeting bonds yielding 7%-10% (or spread of +300-500 over 5-year U.S. Treasury). The telecom sector is one area of value, where select issuers are well-positioned to benefit from growth drivers like artificial intelligence.

Emerging markets debt (EM)

- The fundamental picture for EM is healthy entering 2025. Economic buffers have largely been rebuilt, several with International Monetary Fund (IMF) backstops, and many troubled economies have recently completed debt restructurings. The 2:1 ratio of upgrades versus downgrades is also a supportive trend. We are encouraged by the open market access for corporate and sovereign bonds, even in the high yield space.
- We project a sustained backdrop of strong fundamentals. EM corporate high yield default rates are projected to decline to 2.7%, their lowest level since 2019 and well below long-term averages. Similarly, we project 2025 sovereign high yield defaults under 1%, well below the nearly 7% average over the past five years and the 20-year average of approximately 2% (Figure 5).
- Diversification remains one of the most appealing elements of the asset class. We see areas of attractive value, but investors should be discerning given tighter credit spreads and that much of the "easy money" in distressed recoveries has been realized.
- EM corporates continue to present exceptional alpha opportunities and they are best complemented with sovereigns in a diversified portfolio. We favor corporates in steady countries, such as Mexico, Brazil and South Africa. Despite tariff concerns, Mexico's strong ties to the U.S. supports corporate credit. Brazil offers ample opportunities for globally-competitive companies with experienced management teams. South Africa's stable government and electricity generation provides an improving corporate operating environment. In Turkey, a laggard country, we are favorable toward companies well-positioned to withstand currency volatility. We remain skeptical of corporate opportunities in Argentina.
- For EM sovereign bonds, excess risk premium and relative value against historically tight developed markets credit spreads remains. Steady countries with fundamentally stable credit profiles such as Peru, Hungary, and Saudi Arabia offer deep, liquid bond curves with attractive spread pickup. In terms of frontier countries, we like Angola and Egypt, where near double-digit yields offer opportunity. Among reformers, we see value in Ivory Coast where the government continues to make strides. Among the more stressed countries, we see upside in Ecuador as authorities demonstrate a willingness to make fiscal adjustments.
- Improving fundamentals and broad-based orthodoxy from a policymaking perspective provides an important source of stability for EM local markets. We see premiums in countries where easing cycles have been more measured, such as South Africa and Poland. Given tariff concerns, we are monitoring differentiation in domestic policy stances and expect currencies with greater USD to perform well against the Euro, such as the Uruguayan peso and select frontier currencies.

Figure 5: EM corporate high yield default rates are projected to decline



Data source: J.P. Morgan as of 26 Nov 2024. EM default rates include distressed exchanges.

Non-U.S. developed markets (DM)

- Uncertainties entering 2025 require maintaining liquidity and balancing portfolios' risk postures given tight valuations. We are focused on ensuring optimal rates positioning across key markets and finding relative value among credit markets that should outperform the overall market.
- In rates, we anticipate possible divergence in monetary policy, though the Fed will likely still be a strong influence. We see scope for more cuts from the European Central Bank and Bank of England, while Japan should continue to tighten. Though we should see differentiation among global government bonds, we remain cautious overall on duration and favor a more neutral stance.
- Politics will remain at the forefront as new U.S. policy details unfold, particularly on tariffs and international engagement. Elections will also take place in Germany, Canada and Australia. German elections will be important, particularly against the backdrop of slow growth and the need for EU leadership amid French political divisions. U.S./China tensions feature strategic competition.
- We see value in longer-dated Japanese government bonds and view Germany as a defensive allocation for sovereigns. France remains plagued by political uncertainty, leading us to maintain an underweight, short-duration stance. However, if French spreads to German bonds widen significantly and overshoot, we could revisit this adding opportunistically. The lead-up to notable elections in Canada, Australia and Germany could mean extended periods of rate-driven volatility, and we will remain nimble.
- In the corporate sector, an expanding China challenges Germany's auto sector, underlining the pressure on cyclical sectors. European financial sectors provide good value, while European investment grade credit remains a solid yield-boosting option in short-duration positions.
- China remains a pace setter in developed markets, as we await the results of potentially aggressive U.S. tariffs. Stimulus packages for China's economy could be felt in the developed markets, where trade continues. Any uptick in tensions with the U.S. – including increased altercations with Taiwan and the Philippines – could worsen the geopolitical climate.
- Japan is set to continue to tighten policy, and we expect two more hikes. We are also closely monitoring possible U.S. tariffs and the potential for fiscal expansion, though early signs are it will have a modest impact on rates.

Securitized credit

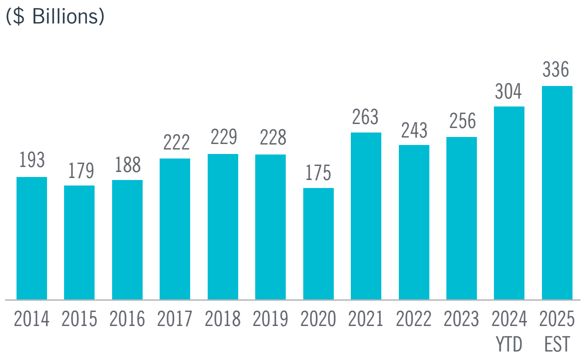
Mortgage-backed securities (MBS)

- Investor demand for MBS remains high from insurance companies and money managers. A decline in net new issuance in 2025 should support valuations and provide total return opportunities.
- Further capital in the MBS markets will come from banks as regulation and the yield curve environment become more favorable.
- Mortgage credit fundamentals remain strong with home prices expected to appreciate between 3% and 5% throughout the year. MBS instruments offer attractive yields compared to corporate and sovereign securities on a credit-neutral basis.
- Opportunities should shift to the up-in-quality sectors: agency MBS and high-credit quality non-agency securities provide strong technicals, solid fundamentals and yield. Across securitized credit, diversifying portfolios by leaning into the strengths of each segment buffers potential market volatility.

Commercial mortgage-backed securities (CMBS)

- CMBS valuations have been challenged similarly to the broader commercial real estate market. While parts of the office market will remain under stress in 2025, we believe ideas of a broader commercial real estate (CRE) default contagion are largely a perception issue driven by sensationalism.
- Loans funding CRE acquisitions are expected to be a larger share of the market in 2025. Buyers are looking to return to the space after 2024's muted transaction volumes due to higher costs of capital and market uncertainty.
- Borrowers are accepting that cheap capital is no longer the norm, and transactions are slowly returning. Certain office exposures, as well as seasoned conduit bonds, are being overlooked and can offer attractive total return opportunities.

Figure 6: Growth of the ABS market



Data source: JP Morgan 2025 outlook 2014 - 2025 (estimated), data as of 26 Nov 2024.

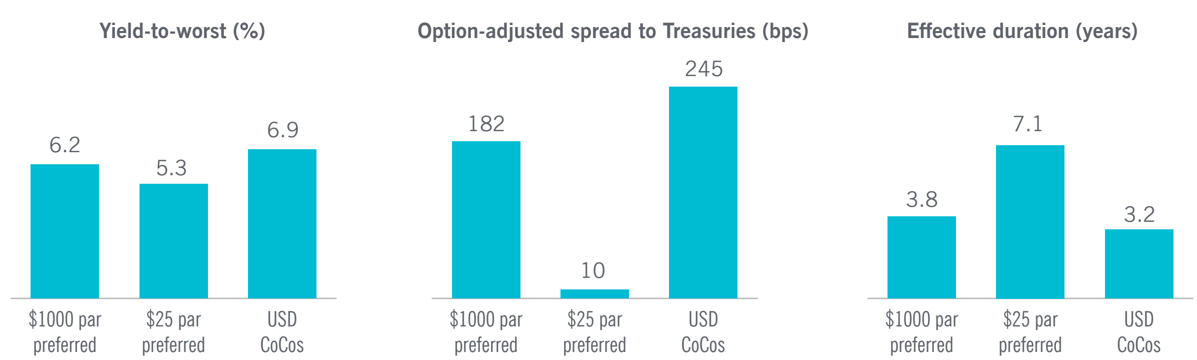
Asset-backed securities (ABS)

- In 2024, the ABS market saw record new issuance in the post-GFC era, and the market expanded by several measures, including the number of sponsors and collateral types (Figure 6). We believe it will be hard to sustain this record growth in the range of 25%-30% annually, but some areas should continue to experience secular tailwinds.
- Esoteric ABS should be a major contributor to growth, given market expansion. Investors have embraced this segment, which is likely to continue to be a significant source of opportunity to capture attractive risk-adjusted returns. Esoterics offer attractive spreads, resilient cash flow profiles and diversification away from more traditional asset classes.
- While we expect a soft landing, ABS market conditions going forward should be primarily driven by macro factors, such as employment, economic growth and inflation. We expect credit performance to remain resilient against the backdrop of a soft landing.

Preferred securities

- A soft landing for the U.S. economy should prove constructive for preferreds. Bank balance sheets remain strong, with high capital requirements supporting high-quality ratings. Under a Trump administration, Fed policy and the regulatory environment are less clear. From a credit perspective, high capital requirements and rigorous regulatory oversight have supported strong fundamentals, buoying investor demand along with attractive tax-advantaged yields. We expect this demand to continue throughout 2025.
- $1000 par preferred and USD contingent capital (CoCo) securities have higher option-adjusted spreads (OAS) and higher yields relative to $25 par preferred securities. $1000 par and USD CoCo securities also have average durations about half of $25 par preferreds, making the former two segments even more attractive on a risk-adjusted basis (Figure 7).
- We expect net supply in 2025 to be modestly positive. A recent change by Moody's to its methodology for assigning equity content to hybrid

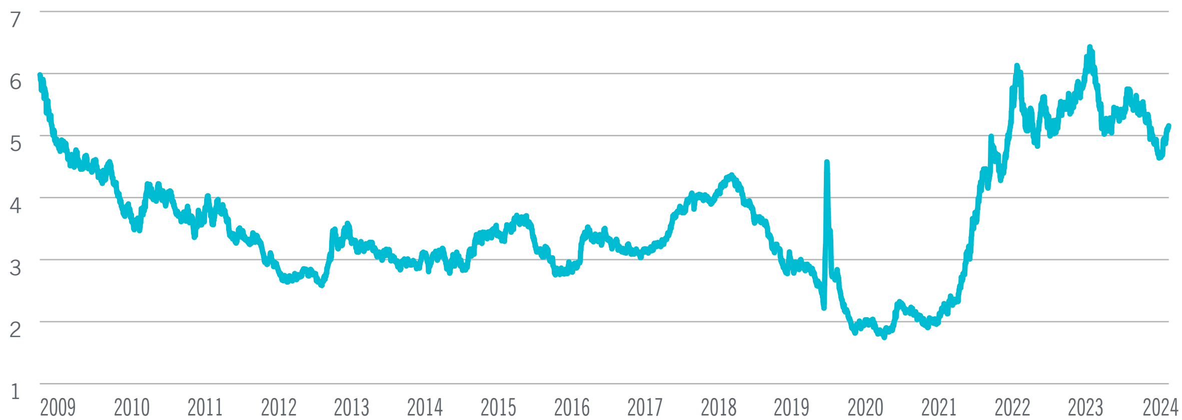
Figure 7: $1000 par and CoCo securities offer attractive spreads, yields and duration



Data source: Bank of America, 31 Oct 2024. **PerfTrmance data shown represents past performance and does not predict or guarantee future results. Representative indexes: $1,000 par preferred:** ICE BofA U.S. Institutional Capital Securities Index; **$25 par preferred:** ICE BofA Core Plus Fixed Rate Preferred Index; **contingent capital (CoCo):** ICE USD Contingent Capital Index.

Figure 8: Investment grade yields remain attractive

U.S. investment grade yield-to-worst (%)



Data source: Bloomberg, 30 Jun 2009 - 31 Oct 2024, daily yield-to-worst. **Performance data shown represents past performance and does not predict or guarantee future results. Representative index: U.S. investment grade:** Bloomberg U.S. Corporate Index.

securities, coupled with booming capex needs from the utility sector fueled by the needs from AI, should support a healthy new issue calendar. But we expect this new supply to be met with robust investor demand, thus muting the impact on overall valuations.

- Given the highly regulated nature of banks, insurance companies and utilities, we view preferred securities as a lower risk opportunity to capture more spread and yield by investing further down the capital structure.

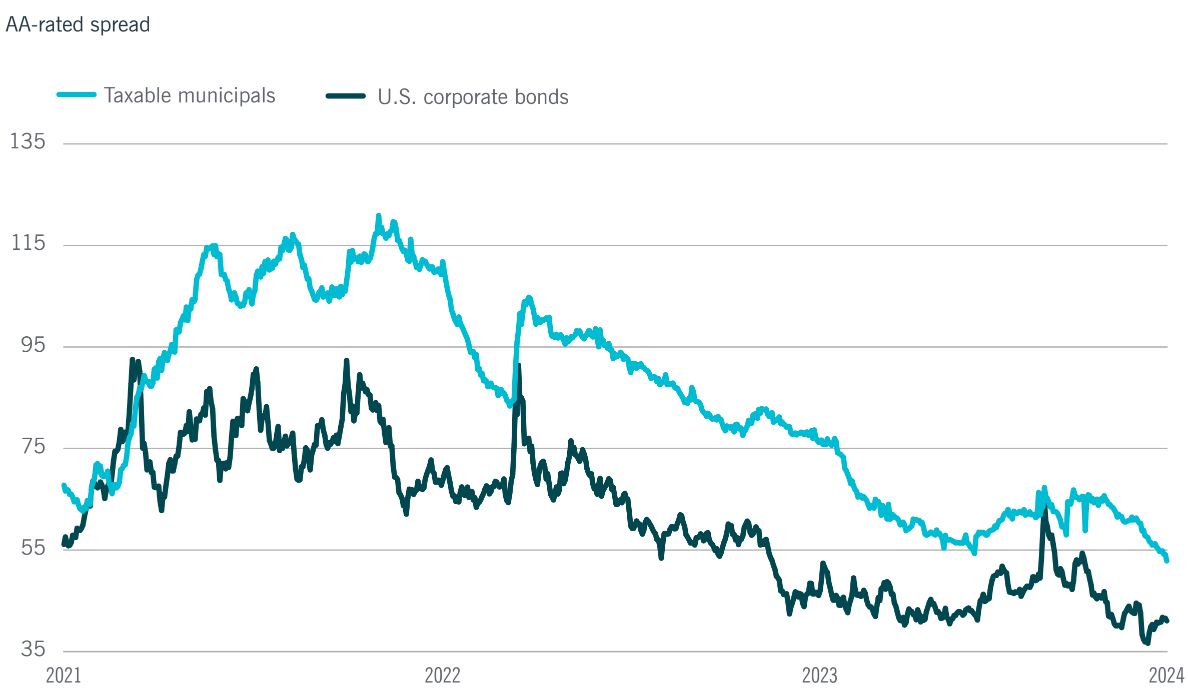
Investment grade credit

- The constructive U.S. economic outlook, solid corporate fundamentals and positive technicals provide a supportive backdrop for investment grade corporates. We expect corporate profits and cash flows to increase in 2025.
- Issuance should increase, driven by maturities, increased capital expenditures and potential M&A activity. Borrowers sought to secure shorter-duration financing leading up to the U.S. election, and this trend should continue until there is greater certainty around policy. The long end of the credit curve remains too flat, with some overpricing. The 5- to 10-year duration segment offers greater value with attractive yields (Figure 8).
- Long-term structural tailwinds support the banking sector, which benefits from strong asset quality, loan growth and capital markets activity. Telecommunications, including towers and data centers, are well-positioned to benefit from good underlying demand and high barriers to entry. Elevated issuance in utilities should present attractive entry points to add exposure. Demand should continue, backed by the sector's nearly non-cyclical nature and ability to tap into power demands for technology.
- M&A activity should return in 2025, and selectivity will be essential to identify quality securities that may benefit. Companies seeking to fund acquisitions primarily through debt present higher risk. Health care, energy and regional banks will likely be among the most active for consolidation. Investors with deep understanding of the fundamentals should be better positioned to navigate this environment.

Taxable municipal bonds

- Taxable municipal bond fundamentals remain largely insulated from national U.S. political changes. The asset class is well-positioned to weather potential economic uncertainty due to continued tax revenue growth and strong local government cash reserves.
- The taxable muni market will likely continue to benefit from a supply and demand imbalance, and any new issuance in 2025 should be readily absorbed.
- While some tightening has occurred, high-quality, AA-rated taxable muni spreads remain wider than U.S. investment grade corporate bonds at the end of November (Figure 9). Taxable munis can be an attractive diversifier for fixed income allocations.
- We see risks with hedging costs and spreads to U.S. Treasuries for non-U.S. investors. Hedging costs, especially in Japan, have remained elevated against U.S. dollar exposure. If this continues, it could suppress demand for taxable munis. Regarding Treasury spreads, the taxable muni market has a longer duration and could be more exposed to significant yield volatility. Any runaway deficits could cause demand concerns.
- The market is buoyed because the underlying credits are providers of essential services. With highly rated bonds, low default risk, a continued supply and demand imbalance and attractive correlations to other market segments, taxable municipal bonds continue to offer investors long-duration investment opportunities with attractive downside risk.

Figure 9: Taxable municipal spreads remain wider than U.S. corporates

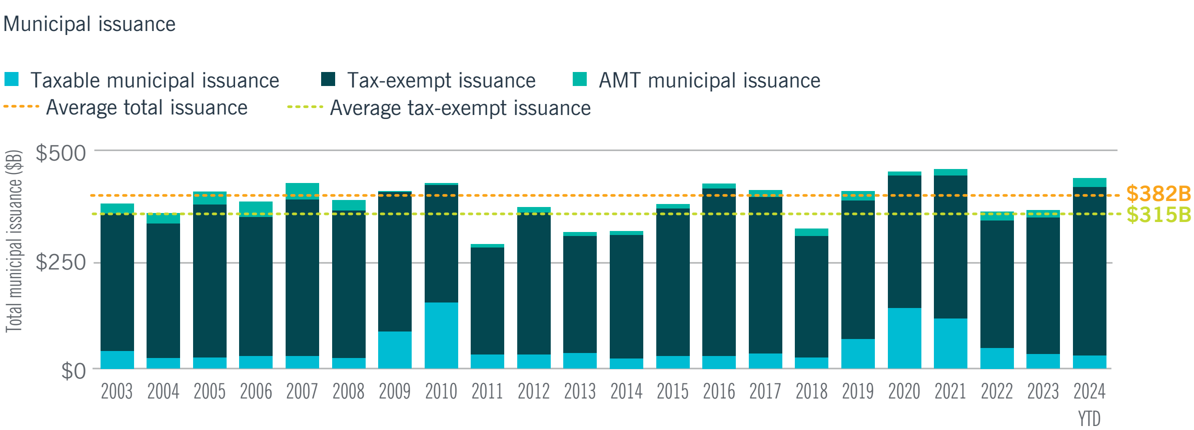


Data source: Bloomberg, L.P., 31 Jan 2018 – 29 Nov 2024, shown monthly. Spread represents option-adjusted spread (OAS). **Performance data shown represents past performance and does not predict or guarantee future results. Representative indexes: taxable municipals:** Bloomberg U.S. Taxable Municipal Bond Index; **U.S. corporate bonds:** Bloomberg U.S. Corporate Bond Index.

Tax-exempt municipal bonds

- The prospect of higher stimulative measures by the new administration, coupled with a less dovish Fed, could mean U.S. Treasury and municipal yields stay higher for longer. As the market shifts focus from monetary to fiscal policy, the debate over taxes will continue, but it should be status quo for muni investors. We anticipate a significant tax package, and Republicans will likely push to extend several key provisions set to expire as part of the 2017 Tax Cuts and Jobs Act, including the marginal tax rate levels for high-income earners and the cap on deductions for state and local government taxes.
- Municipal bond yields and spreads are compelling, which should garner demand across investment grade and high yield municipal bonds. While U.S. household wealth has been rising, the municipal market has not experienced the same growth in outstanding bonds, creating a supply/demand imbalance. In high yield municipals, credit spreads should remain favorable, and continued tightening is possible. We are not anticipating the risk of wider credit spreads as the environment is healthy, credit conditions are favorable, and market contagion risks are more controlled than in prior years.
- On the supply front, 2025 should be a robust year for tax-exempt municipals, after a strong year in 2024. Our research indicates that supply should be more diversified, with high yield issues to fund infrastructure in support of population growth, and as smaller issuers come to market with the prospect of rate cuts (Figure 10).
- Demand for municipals remains strong but investors are still holding cash equivalents, since rates have been declining more slowly. The municipal market has room to recover from the outflows in 2022 and 2023. As the yield curve is set to steepen in 2025, long duration municipal bonds become more attractive for investors waiting to deploy capital.
- Looking forward, robust revenues and record funding of reserves for state and local governments put municipal credit in a strong position to manage through any economic downturns. Select sectors may be influenced by the Republican sweep, notably health care, education and utilities. Many municipal issuers benefit from broad autonomy and local control, providing relative stability regarding revenues pledged to debt service. Our credit research team is carefully evaluating individual issuers and sectors as we seek to identify opportunities for relative value with strong upside potential.

Figure 10: We anticipate robust tax-exempt supply in 2025

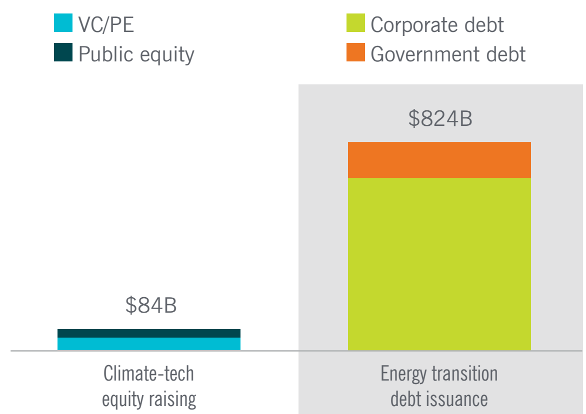


Data source: Securities Industry and Financial Markets Association (SIFMA.org), U.S. Bond Market Issuance and Outstanding, 04 Nov 2024 for period ending 31 Oct 2024. The average total issuance and average tax-exempt issuance shown are for the period 01 Jan 2003 – 31 Dec 2023. AMT municipal issuance is part of the tax-exempt municipal market.

Impact investing

- Labelled green, social, and sustainable (GSS) issuance in 2024 totalled $1 trillion for only the second time ever. We expect similar issuance in 2025, as issuers continue to gain comfort with use of proceeds-based structures. Further, a significant amount of bonds will mature in 2025, creating further market opportunities from refinancing of longer-term projects. In addition to falling costs derived from scaling of renewable generation technology, lower cost of capital improves margins for borrowers, improving their credit profile. We continue to focus on investment opportunities in which financed outcomes reinforce the success of the operating model, which in turn improves the likelihood of us being repaid as lenders (i.e. bond investors).
- The energy transition offers long-term structural tailwinds as climate targets and decarbonization initiatives become increasingly important globally. Given the massive capital outlays required, the debt market provides an efficient, scalable mechanism to marshal capital from investors and asset owners. Yet equity and venture funding require extensive sourcing, due diligence and negotiating cycles. Impact investors may find it appealing to put capital to work via the bond market, which offers much larger, more liquid and easier-to-access opportunities. Figure 11 illustrates this concept for capital raised globally in 2023. The debt market also offers myriad portfolio construction and diversification possibilities.
- The green bond market serves as an attractive entry point for impact investors and other credit investors. Green bonds feature use of proceeds that align with Nuveen's environmental impact themes. Renewable energy and climate change outcomes include construction or expansion of solar and wind generation, improving efficiency of power generation and transmission systems and projects resulting in the reduction of greenhouse gas emissions. Natural resources outcomes include land conservation and sustainable forestry, marine conservation and sustainable fishing practices, energy efficient buildings, remediation and redevelopment of polluted or contaminated sites, clean drinking water and waste management.
- We rely on deep analytical expertise to seek opportunities inside and outside the labelled bond market. Understanding each deal's use of proceeds and outcomes-based reporting framework allows us to analyze a bond that may not be labelled as impact.
- Spreads are near all-time tights across high grade and below investment grade corporate markets globally. Impact bonds can provide a complementary, diversifying credit allocation. The opportunity set provides short and long durations, a range of credit profiles, and exploitable inefficiencies in the securitized, municipal and blended finance sectors. As markets face political uncertainty, economic volatility and international concerns, the impact sector offers an important level of diversification to fixed income allocations.

Figure 11: Capital markets play a pivotal role in financing the energy transition



Data source: BloombergNEF, 31 Dec 2023. **Performance data shown represents past performance and does not predict or guarantee future results.** Regions represented include U.S., Europe, Asia and Rest of World.

Multi-sector

Within the multi-sector space we are focused on four key investment themes:

- Current yields present the best starting point for investors in over 15 years.
- Income opportunities are attractive from continued higher-for-longer short and long-term rates.
- Position for bouts of volatility amid potential policy shifts and a slowing economy.
- Balance duration with credit risk as sources of risk factor exposures.

Market volatility may well persist into the new year, with the pace of Fed rate cuts being slower than initially expected. Uncertainty concerning policy, economic data and further escalation of geopolitical tensions could expose markets to short-term shocks.

Looser regulatory policy under a Trump administration could increase cash flow for companies to address debt and interest payments. Companies at the lower end of the high yield segment may struggle with increased funding and interest costs, putting a greater focus on higher quality positions.

Investors are starting to be compensated for taking interest rate risk. We remain cautious about an overweight in the long end of the yield curve but will tactically add high quality longer exposure into portfolios as spreads widen.

Conditions should benefit nimble, diversified strategies. Volatility will create pressures, and experienced credit selection can provide opportunity to generate attractive yields. High yield should continue to benefit from overarching corporate tailwinds.

Authors

Sectors	*Portfolio Managers*	*Client Portfolio Managers*
Leveraged Finance	Scott Caraher Kevin Lorenz, CFA® Himani Trivedi	Ravi Chintapalli, CFA® Lindsay Gruhl Shannon Jin, CFA®
Emerging markets debt (EM)	Katherine Renfrew	Jeffrey C. Smith, CFA®
Non-U.S. developed markets (DM)	John Espinosa	Jeffrey C. Smith, CFA®
Securitized credit	Chris Jeltrup Aashh K. Parekh, CFA® Nicholas Travaglino	Jack Allen, CAIA Samira Mattin Fogarty
Preferred securities	Douglas M. Baker, CFA®	Lisa A. Segner, CFA® Kari Stanway, CFA®
Investment grade credit	Richard Cheng	Jack Allen, CAIA Samira Mattin Fogarty
Taxable municipal bonds	Daniel J. Close, CFA®	Christopher G. Barron
Tax-exempt municipal bonds	Daniel J. Close, CFA®	Andrew J. Luberto, CFA®
Impact investing	Stephen M. Liberatore, CFA®	Alan Papier, CFA®
Multi-sector	Joseph Higgins, CFA®	Jack Allen, CAIA David R. Wilson, CFA® Samira Mattin Fogarty

For more information, please visit nuveen.com.

Endnotes

This material is not intended to be a recommendation or investment advice, does not constitute a solicitation buy, sell or hold a security or an investment strategy, and is not provided in a fiduciary capacity. The information provided does not take into account the specific objectives or circumstances of any particular investor, or suggest any specific course of action. Investment decisions should be made based on an investor's objectives and circumstances and in consultation with his or her financial professionals.

The views and opinions expressed are for informational and educational purposes only as of the date of production/writing and may change without notice at any time based on numerous factors, such as market or other conditions, legal and regulatory developments, additional risks and uncertainties and may not come to pass. This material may contain "forward-looking" information that is not purely historical in nature. Such information may include, among other things, projections, forecasts, estimates of market returns, and proposed or expected portfolio composition. Any changes to assumptions that may have been made in preparing this material could have a material impact on the information presented herein by way of example. **Performance data shown represents past performance and does not predict or guarantee future results.** Investing involves risk; principal loss is possible.

All information has been obtained from sources believed to be reliable, but its accuracy is not guaranteed. There is no representation or warranty as to the current accuracy, reliability or completeness of, nor liability for, decisions based on such information and it should not be relied on as such. For term definitions and index descriptions, please access the glossary on nuveen.com. **Please note, it is not possible to invest directly in an index.**

Important information on risk

Investing involves risk; principal loss is possible. Debt or fixed income securities are subject to market risk, credit risk, interest rate risk, call risk, derivatives risk, dollar roll transaction risk and income risk. As interest rates rise, bond prices fall. Below investment grade or high yield debt securities are subject to liquidity risk and heightened credit risk. Preferred securities are subordinated to bonds and other debt instruments in a company's capital structure and therefore are subject to greater credit risk. Foreign investments involve additional risks, including currency fluctuation, political and economic instability, lack of liquidity and differing legal and accounting standards. Asset-backed and mortgage-backed securities are subject to additional risks such as prepayment risk, liquidity risk, default risk and adverse economic developments. The value of convertible securities may decline in response to such factors as rising interest rates and fluctuations in the market price of the underlying securities. Senior loans are subject to loan settlement risk due to the lack of established settlement standards or remedies for failure to settle. These investments are subject to credit risk and potentially limited liquidity, as well as interest rate risk, currency risk, prepayment and extension risk, and inflation risk. Investors should contact a tax professional regarding the appropriateness of tax-exempt investments in their portfolio. If sold prior to maturity, municipal securities are subject to gain/losses based on the level of interest rates, market conditions and the credit quality of the issuer. Income may be subject to the alternative minimum tax (AMT) and/or state and local taxes, based on the state of residence. Income from municipal bonds held by a portfolio could be declared taxable because of unfavorable changes in tax laws, adverse interpretations by the Internal Revenue Service or state tax authorities, or noncompliant conduct of a bond issuer. It is important to review your investment objectives, risk tolerance and liquidity needs before choosing an investment style or manager.

Nuveen, LLC provides investment solutions through its investment specialists.

This information does not constitute investment research as defined under MiFID.

nuveen
A TIAA Company

4163615-1126 2033450