Portfolio Management Outlook

Positioned for Opportunity in a Shifting Market Environment

Yields and total return potential remain enticing, but credit selection is critical.

As we move through 2025, the fixed-income landscape presents compelling opportunities despite market uncertainty. Yields remain historically attractive, creating a favorable risk-return profile for long-term investors. Credit spreads have widened to historical averages, creating opportunities in higher quality assets in an environment of spread decompression. Strong technicals support the market as elevated yields constrain supply while simultaneously boosting investor demand. Fundamentals remain solid for higher quality credits despite broader economic concerns. Idiosyncratic credit themes are likely to continue to pop up, either from policy changes or market reaction, which should increase performance dispersion and favor active management.

Strategic Credit Positioning

In this environment of heightened volatility, we're emphasizing:

- Select investment-grade and BB corporates as spreads have widened, in addition to high grade structured products (ABS, CLOs, non-Agency RMBS) and Agency MBS (favoring higher coupon structures).
- Tactical yield curve positioning with a bias toward the belly of the curve (2–5 year segment), which historically outperforms during easing cycles.
- Maintaining strategic liquidity buffers to capitalize on market dislocations while providing downside protection.
- Opportunistic additions to Treasury inflation-protected securities (TIPS) during periods when inflation breakevens fall to particularly low levels.

Interest Rate Outlook

The Federal Reserve (Fed) faces a challenging balancing act in the months ahead. We anticipate continued policy and economic volatility, which should manifest in a lower policy rate over time, with four to six rate cuts over the next year as labor market conditions soften. This should support a steepening yield curve, with:

- Front-end rates likely to move and remain below 4 percent as the markets price in Fed easing.
- The 10-year Treasury yield expected to trade in its recent two-year range: 3.5–4.75 percent.
- Long-end yields potentially remaining elevated due to inflation concerns and Treasury issuance needs.

Summary

The extreme market volatility we've witnessed recently—with the S&P 500 trading in a 15 percent range and high yield spreads moving 120 basis points in a single week—underscores the importance of active management and maintaining flexibility. By positioning portfolios to potentially benefit from these dynamics while maintaining disciplined risk management, we believe investors can capture attractive risk-adjusted returns even amid market uncertainty.

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One basis point is equal to 0.01%.

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