SEPTEMBER 2026

Active Fixed Income Perspectives—Monthly Pulse

Key takeaways

1. **Our base case remains for trend U.S. growth, supported by sustained business investment. With the trend of labor market data remaining firm and inflation elevated, the Fed raised rates by 25 basis points this month, and our base case now includes up to one additional hike in 2026.**
2. **Robust AI-related capital spending and stronger-than-expected corporate earnings are supporting growth and reinforcing strong underlying fundamentals in credit markets.**
3. **Higher energy prices from the prolonged war in Iran and an intensifying competition for capital driven by elevated sovereign borrowing and surging hyperscaler issuance are also contributing to the recent increase in global yields.**
4. **Overall, fixed income remains attractive, with real yields across the curve near 20-year highs. Our positioning reflects neutral U.S. duration, an overweight to high-quality credit, and an emphasis on carry and security selection with attractive long-end opportunities in municipals.**

Outlook: Trend growth as the Fed tightens amidst strong investment and a prolonged Iran conflict.

Our base case remains for trend U.S. growth, supported by sustained business investment. Recent labor-market data has been firmer than expected, while inflation remains elevated, driven in part by one-off factors such as tariffs and higher energy prices. Given this strong trend in the data, our expectations for Fed policy have shifted toward further tightening. The Fed raised rates by 25 basis points this month, and our base case now includes up to one additional rate hike in 2026 as they look to recalibrate the policy rate.

AI-related capital spending remains robust, contributing to strong economic growth while also adding to inflationary pressures. The meaningful productivity gains associated with that investment still appear further out. Corporate earnings have also exceeded expectations, reinforcing strong underlying fundamentals despite increasing dispersion in valuations.

The prolonged war in Iran has pushed energy prices higher, adding to inflationary pressures. Competition for capital also remains intense, with elevated global sovereign borrowing needs compounded by the substantial year-to-date issuance from hyperscalers. These developments have also contributed to the recent rise in rates.

Risks to the downside include a slowdown in AI investment or a prolonged supply shock that slows demand. Conversely, faster AI productivity gains or broader economic growth could lead to a stronger growth scenario.

Our active positioning: neutral duration in U.S. rates, up-in-quality carry in credit, curve-focused value in munis.

Rates: In U.S. rates, we have moved to neutral duration while maintaining an overweight to German bunds relative to U.S. Treasuries. Outside the U.S., we remain short duration with a curve-flattening bias in Japan and maintain underweights to France and Italy as a hedge against our credit overweight. In mortgage-backed securities, we hold an overweight position expressed through hybrid ARMs, CMOs, and non-agency RMBS.

Credit: We remain overweight credit, supported by strong fundamentals, but with the potential for further Fed tightening likely to limit additional spread compression. We continue to emphasize high-quality carry and security selection, favoring banks and utilities within investment grade while limiting high-yield exposure.

Municipals: The steep municipal curve and attractive long-end valuations continue to support a long-duration position, which serves as a hedge against our credit overweight. We are also selectively rotating out of credit and into attractive high-grade municipal structures.

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