

Strong Demand for Long-Duration Bonds Despite Rich Valuations

This report is excerpted from the *Third Quarter 2025 Fixed-Income Sector Views*.

We prefer defensive sectors given historically tight spreads and policy uncertainty.

Investment-grade (IG) credit markets have remained resilient and technically strong, with spreads at or near year-to-date tight levels. Despite macroeconomic uncertainties, including fiscal policy shifts, trade tensions, and geopolitical risks, supportive fundamentals such as robust corporate earnings, elevated all-in yields, and strong technicals from limited net primary supply are expected to support investment-grade spreads in the third quarter. This outlook underscores the market's capacity to navigate potential headwinds while capitalizing on favorable conditions.

Sector Commentary

- Insurance and institutional demand for long-duration investment-grade bonds remains robust, particularly when yields approach 6 percent. However, stretched valuations limit bullish sentiment.
- Primary market activity is steady, skewed toward financial issuers and shorter maturities. New issue concessions are low, and oversubscriptions are high.
- Higher ongoing coupon payments support higher reinvestment in the sector. Owing partially to this dynamic, net supply is down materially versus 2024 and on a three-year look back.
- Credit fundamentals remain solid, with debt growth slowing, leverage normalizing, and interest coverage remaining high, despite rising interest expenses.
- Foreign demand for U.S. IG remains intact despite concerns regarding overseas selling, as its relative value has improved compared to European IG.

Investment Themes

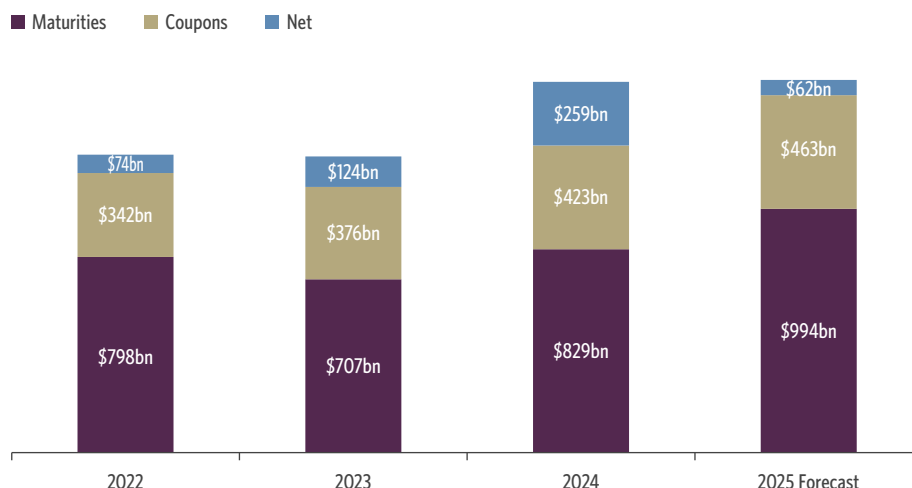
- We anticipate the IG market will remain rangebound, with dips likely to be shallow and bought. However, the risk/reward for further spread tightening appears unattractive.
- We prefer long-duration corporates from a yield and supply technical perspective, as negative net bond supply is more pronounced in the 30-year maturity bucket. In the front end of the credit curve, two-year BBB corporates offer good potential carry and roll down.
- We favor preferred securities with high current dividends or short callable vintages, with comparable yield-to-call. These securities also benefit from negative net issuance.
- Given historically tight spreads and macroeconomic uncertainties, we prefer more defensive sectors such as telecom, utilities, aerospace/defense, life insurance, and banks.

By Justin Takata

Due to a wave of COVID era bonds maturing with higher coupons payments from the increase in rates, net supply is down materially versus 2024 and on a three-year look back.

IG Net Supply Is Down Significantly Compared to Prior Years

IG Corporate Issuance, \$bn



Source: Guggenheim Investments, JP Morgan. Data as of 6.30.2025.

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Investing involves risk, including the possible loss of principal. In general, the value of a fixed-income security falls when interest rates rise and rises when interest rates fall. Longer term bonds are more sensitive to interest rate changes and subject to greater volatility than those with shorter maturities. During periods of declining rates, the interest rates on floating rate securities generally reset downward and their value is unlikely to rise to the same extent as comparable fixed rate securities. High yield and unrated debt securities are at a greater risk of default than investment grade bonds and may be less liquid, which may increase volatility. Investors in asset-backed securities, including mortgage-backed securities and collateralized loan obligations (“CLOs”), generally receive payments that are part interest and part return of principal. These payments may vary based on the rate loans are repaid. Some asset-backed securities may have structures that make their reaction to interest rates and other factors difficult to predict, making their prices volatile and they are subject to liquidity and valuation risk. CLOs bear similar risks to investing in loans directly, such as credit, interest rate, counterparty, prepayment, liquidity, and valuation risks. Loans are often below investment grade, may be unrated, and typically offer a fixed or floating interest rate.

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