

Fixed Income

VIGILANTES LURK, BUT RATE VOLATILITY MAY PRESENT OPPORTUNITIES

The recent tariffs imposed and proposed by the Trump administration caused significant spikes in volatility, sending shock waves through the market. The 10-year Treasury term premium, which compensates investors for bearing the risk of future interest rate fluctuations, climbed. In our view, the 10-year Treasury yield outlook can be considered a function of several dynamics:

- Long-term inflation expectations remain anchored, which will be key for the Federal Reserve (the Fed).
- The expected path of the real federal funds rate looks to be lower, but inflationary pressures stabilizing at levels higher than the Fed's target could lead to slower or fewer cuts than the market expects.
- Potential increases in the term premium would raise the 10-year Treasury yield, slowing the economy. This would require less restrictive monetary policy to achieve the central bank's dual mandate, adding uncertainty to the path of real short-term interest rates and volatility to interest rates overall.
- The demand for borrowing is currently high, given the need to finance federal deficits. This will likely keep longer term rates higher, similar to those seen prior to the Covid-19 pandemic.

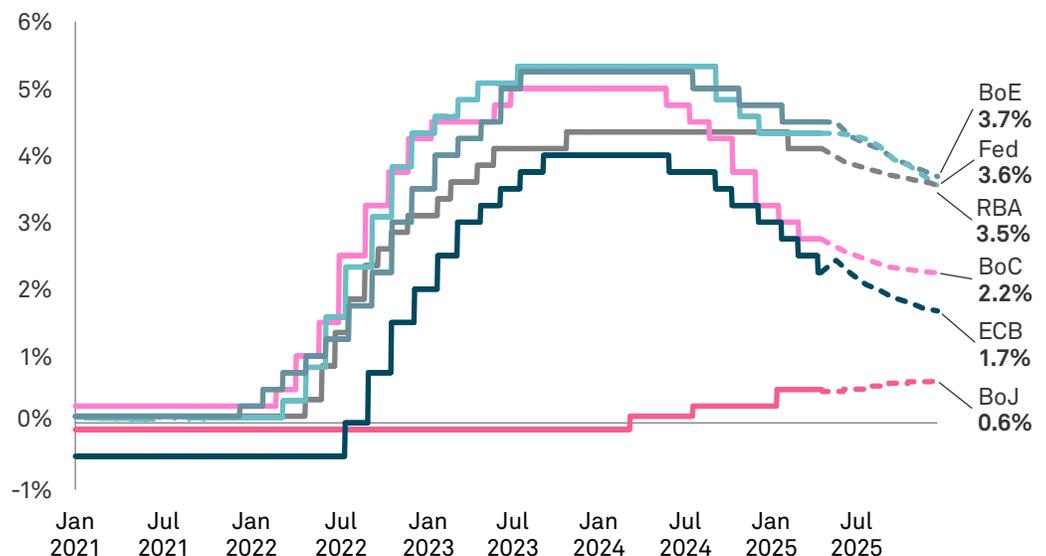
“Bond vigilantes” refers to investors who sell off bonds when they believe the government's fiscal policies are reckless. It was coined in the 1980s when traders reacted sharply to inflationary policies.

Central banks are expected to decrease rates in 2025 but the Fed will face the most challenging backdrop with the recent fluid trade policy.

CENTRAL BANK FUTURE RATES

Central bank policy rates and market-implied rate trajectories

- ECB (ESTR futures)
- BoE (SONIA futures)
- Fed (Fed funds futures)
- BoJ (EuroYen futures)
- BoC (Corra futures)
- RBA (ASX futures)



Sources: BNY Investment Institute and Macrobond as of April 30, 2025. The chart is for illustrative purposes and not indicative of the past or future performance of any BNY offering. ECB = European Central Bank; ESTR = Euro Short Term Rate; BoE = Bank of England; SONIA = Sterling Overnight Index Average; Fed = Federal funds futures; BoJ = Bank of Japan; Euro Yen = Euro/Japanese Yen; BoC = Bank of Canada; Corra = Canadian Overnight Repo Rate Average; RBA = Reserve Bank of Australia; ASX = Australian Securities Exchange.

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Compelling case for fixed income

Yields are near three-year highs but interest rate volatility is likely to remain elevated, driven by many supply side and demand side risks. Higher and more volatile yields are supportive of active management and with higher dispersion likely, bottom-up credit selection plays a more vital role.

We believe an active, intermediate-term approach in fixed income has the potential to perform well for investor portfolios in 2025. Maintaining quality within bonds enables portfolios to seek attractive yield, while potentially providing downside risk mitigation.

Recent stock-bond correlation has been volatile, but we expect the relationship to normalize toward its more typical low or negative correlation as inflation expectations reset lower. This dynamic could help buffer multi-asset class portfolios from growth shocks.

We believe a portfolio that includes a [core plus strategy](#) may complement a global allocation through exposure to broadly diversified sectors across the fixed income landscape with an emphasis on high-quality bonds.

However, in our view, this could be a particularly meaningful time for investors to consider global fixed

income to diversify and mitigate risk from US rate volatility and policy uncertainty. As noted in our report, [Bonds without Borders](#), we see potential opportunities and an array of interest rate exposures in global fixed income, as 60% of bond opportunities come from outside of the US.¹

Given recent market conditions, we believe global central banks are likely to continue lowering interest rates to buoy economic growth and offset tariff risks. Investing in global fixed income, particularly on a hedged basis, can provide diversified sources of return to a domestic-only fixed income portfolio.

¹ Source: FactSet, March 31, 2025.

IMPORTANT INFORMATION

All investments involve risk including loss of principal. Certain investments involve greater or unique risks that should be considered along with the objectives, fees, and expenses before investing.

Past performance is not necessarily indicative of future results.

Bottom-up selection involves the analysis of individual issuers to assess their risk and value.

Bonds are subject to interest-rate, credit, liquidity, call and market risks, to varying degrees. Generally, all other factors being equal, bond prices are inversely related to interest-rate changes and rate increases can cause price declines. **Investing in foreign denominated and/or domiciled securities** involves special risks, including changes in currency exchange rates, political, economic, and social instability, limited company information, differing auditing and legal standards, and less market liquidity. These risks generally are greater with emerging market countries.

The 10-Year US Treasuries Average Yield represents a range of Treasury securities adjusted to the equivalent of a ten-year maturity. **Correlation** is a statistical measurement that indicates how the prices of two or more assets move in relation to each other.

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