NEUBERGER BERMAN

Fixed Income Investment Outlook 1Q 2025

Navigating New Fiscal Forces

With inflation continuing to improve, the downward path of central bank rates remains on track, if uneven geographically given U.S. economic strength. Now, amid political turbulence, attention is shifting toward fiscal issues—spending and tax policy—that could affect issuance patterns and yields, particularly at the longer end of the curve. We are constructive on fixed income for 2025, seeing potential in shorter durations and in optimizing carry amid narrow credit spreads. At the same time, the unpredictability of political cycles could make for an eventful year that requires vigilance in guarding against risk.

NEUBERGER | BERMAN

Neuberger Berman is an employee-owned, private, independent investment manager founded in 1939 with over 2,800 employees in 26 countries. The firm manages $508 billion of equities, fixed income, private equity, real estate and hedge fund portfolios for global institutions, advisors and individuals. Neuberger Berman's investment philosophy is founded on active management, fundamental research and engaged ownership. The PRI identified the firm as part of the Leader's Group, a designation awarded to fewer than 1% of investment firms for excellence in environmental, social and governance practices. Neuberger Berman has been named by *Pensions & Investments* as the #1 or #2 Best Place to Work in Money Management for each of the last eleven years (firms with more than 1,000 employees). Visit www.nb.com for more information. Data as of December 31, 2024.

Navigating New Fiscal Forces

After several years of fixed income markets driven largely by central bank policy, attention will likely focus more this year on fiscal actions—policy and revenue decisions by the new Trump administration as well as those other governments reorienting their priorities or beset by financial strains.

Ever since COVID-19, investors have focused largely on central banks for clues as to fixed income performance, from instituting zero-rate policy and financial liquidity to maintain the global economy during the pandemic, to tightening to offset the inflation surge of 2021 and 2022, to the widely anticipated start of the current easing cycle. With inflation continuing to recede, we are moving into a period of gradual central bank rate reductions.

The U.S. stands out for its relatively robust growth, which we believe could surprise modestly to the upside this year. However, slow progress on inflation may limit the Federal Reserve's capacity to cut interest rates further. Europe appears more vulnerable to a stilted export environment, particularly to China, but with more wriggle room for easing. At the same time, anxiety is growing around the long-term fiscal picture in the U.S. and select other countries, which could pressure longer-term rates and help steepen the yield curve. Given the upward adjustment in longer yields late last year, the chances of further rate shocks appear limited. However, we remain relatively cautious on duration, seeing opportunities for trading more at the shorter end of the curve.

In the credit market, all-in yields remain robust, but spreads are exceptionally narrow, with few areas displaying the obvious dislocations seen a year ago. This limits the value of credit exposure overall while reinforcing the benefits of identifying value to maximize carry. Floating rate loans and some segments of the emerging markets universe, among others, currently meet this criterion.

In some ways, the coming year may prove trickier for investors than 2024, as the past high-conviction idea of lower central bank rates has been displaced by political dynamics and questions around the longer-term course of government budgets and interest rates. In the U.S., looming policy shifts, including potential changes to taxes and the use of tariffs, could heighten market volatility and will likely be an ongoing consideration throughout 2025.

Our key market and investment themes appear on the following pages.

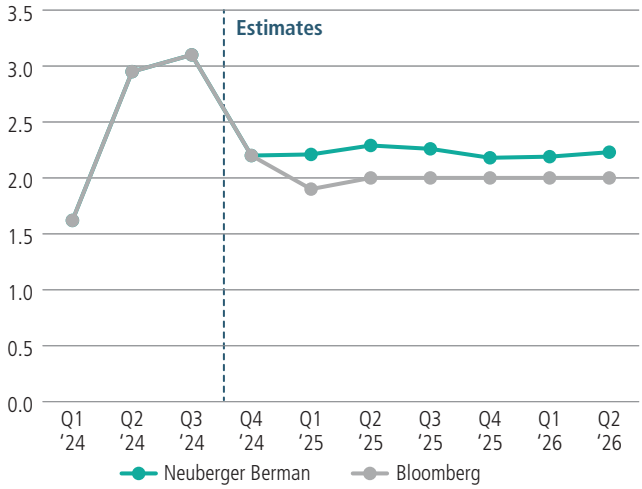
1. U.S. Economic Momentum, Vulnerability in Europe

The U.S. has consistently outpaced growth expectations in recent years, and while few believe that the country will experience recession, some anticipate downside risk to forecasts from here. In contrast, we believe that U.S. growth could actually surprise on the upside with continued momentum in the low 2% range. This would largely be driven by the consumer, who we believe will likely increase spending on durable goods, while services should remain steady. We anticipate softening gross domestic fixed investment near term, while net exports and government expenditures should slow.

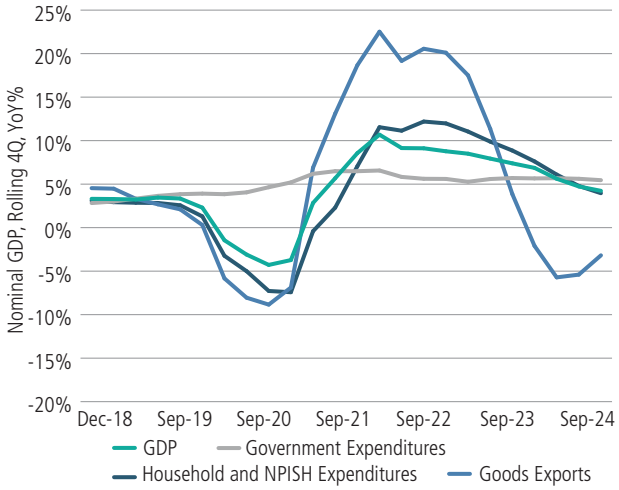
In the eurozone, although consumption represents more than half of regional GDP, exports and government spending also play a major role. Although demand has recovered somewhat recently, it remains largely dependent on the U.S. amid China weakness, and therefore vulnerable to trade actions. Meanwhile, government spending is currently north of 5% of GDP, which may be difficult to maintain.

U.S. GROWTH MAY SURPRISE ON THE UPSIDE

U.S. GDP YoY%



IN EUROPE, EXPORT PROSPECTS COULD BE A KEY ISSUE



Source: Left; BEA, BLS, Bloomberg, NB calculations, as of December 31, 2024; Right: Eurostat, Bloomberg, as of 3Q24. European GDP is neither calendar nor seasonally adjusted.

2. With Global Inflation Softening, Easing Remains on Tap

The year is likely to be a period of continued progress on inflation, which points the way to further reductions in policy rates. In the U.S., we see inflation remaining above target throughout the year, leading to just two cuts in 2025, with an additional reduction in each of 2026 and 2027 for an ultimate neutral rate of around 3.5%. Overall, we feel current growth, inflation and policy prospects lead to fair value for the 10-year U.S. Treasury of a range around 4.5%, or somewhat below recent trading levels.

In Europe, there are fewer obstacles to inflation normalization. Export weakness, coupled with the danger of renewed trade tensions with the U.S., provides more scope for reductions this year, with a neutral rate of about 1.75% achieved by July.

CENTRAL BANK EXPECTATIONS

Central Bank	Market Expectations	Neuberger Berman Expectations	Neuberger Berman Outlook
FED	• 2025: 1 Cut • 2026: 1 Cut • 2027: 0 Cuts • NR[1]: 4.00%	• 2025: 2 Cuts • 2026: 1 Cut • 2027: 1 Cut • NR[1]: 3.50%	• After recalibrating policy rates, the Fed is pivoting to a gradual phase of the easing cycle. Higher upside risks to inflation should keep the committee data-dependent for near-term policy adjustment. • We anticipate that the Fed will switch to a gradual pace of cuts, delivering two in 2025, and proceed cautiously thereafter until the neutral rate settles at around 3.25 – 3.75%. We acknowledge increasing uncertainty on the timing of reaching the neutral rate, due to a resilient economy with an inflationary tailwind.
ECB	• 2025: 4 Cuts • 2026: 0 Cuts • 2027: 0 Cuts • NR[1]: 2.00%	• 2025: 5 Cuts • 2026: 0 Cuts • 2027: 0 Cuts • NR[1]: 1.75%	• Weak potential growth (the European industry model no longer being efficient), reinforced by the potential return of the U.S. trade war and ongoing inflation normalization, should lead the ECB to remove its restrictive monetary policy as soon as possible. • We expect the ECB to cut its key rates at each meeting to reach a neutral rate of 1.75% by July 2025.
BOE	• 2025: 2 Cuts • 2026: ~1 Cut • 2027: 0 Cuts • NR[1]: 4.00%	• 2025: 4 Cuts • 2026: 2 Cuts • 2027: 0 Cuts • NR[1]: 3.25%	• BoE commentary has pointed toward more willingness to ease, even with some persistent inflation pressures given some lower growth dynamics. Concerns about stagflation due to fiscal policies are risks to the forecast. • We now expect a continuation of the rate-cutting cycle at a quarterly pace into 2025 and 2026, with the policy rate settling at around 3.25%.
BOJ	• 2025: 2 Hikes • 2026: 1 Hike • 2027: 0 Hikes • NR[1]: 1.00%	• 2025: 2 Hikes • 2026: 0 Hikes • 2027: 0 Cuts • NR[1]: 0.75%	• The BoJ held rates at 25bps at its final meeting of 2024, in line with its stated goal of gradually moving policy to a neutral level, opting to be cautious given political uncertainties in both Japan and the U.S. • We expect the BoJ to raise rates twice in 2025, with the first hike in the first quarter to bring policy rate to a neutral rate of around 0.75%.

[1] NR = Neutral Rate

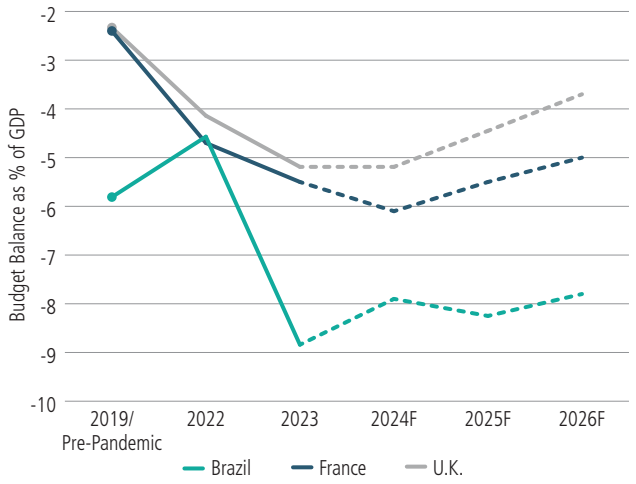
Source: Bloomberg and Neuberger Berman. As of January 2, 2025.

3. Fiscal Issues Come to the Fore

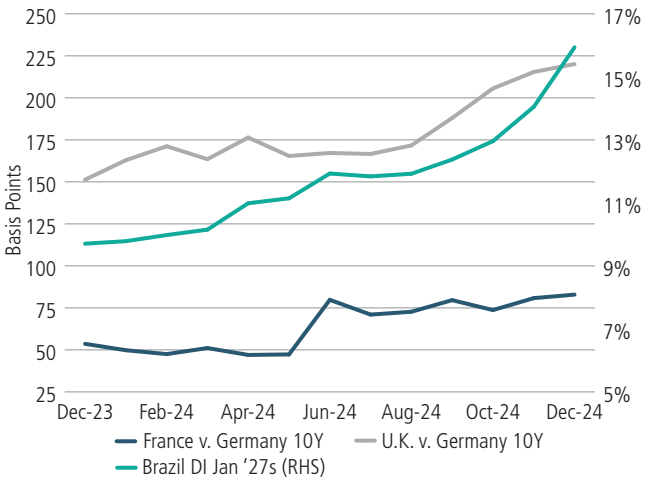
For the past few years, all eyes have been on central banks and policy shifts: first, decreases to combat COVID-related weakness, then hikes to counter runaway inflation tied to supply chains and excess stimulus, and more recently, in the anticipated pullback of tightening. However, fiscal issues are now looming far larger. In the U.S., Republicans are focused on extending provisions within the Tax Cuts and Jobs Act of 2017, while considering new proposals like eliminating taxes on tips and Social Security income, and introducing tariffs, which, depending on their scope, could prove inflationary.

In the meantime, various other countries are facing fiscal stresses and higher borrowing costs. For example, proposed belt-tightening in Brazil was dismissed by markets as too limited, causing an increase in the country's interest rates. France has also been struggling to contain spending and, after Germany announced flash elections, bunds traded wide of their swaps for the first time in history.

BUDGETARY PRESSURES IN SOME COUNTRIES…



…HAVE SHARPLY INCREASED BORROWING COSTS



Source: Bloomberg. Forecasts as of January 2, 2025, rates data as of December 2024.

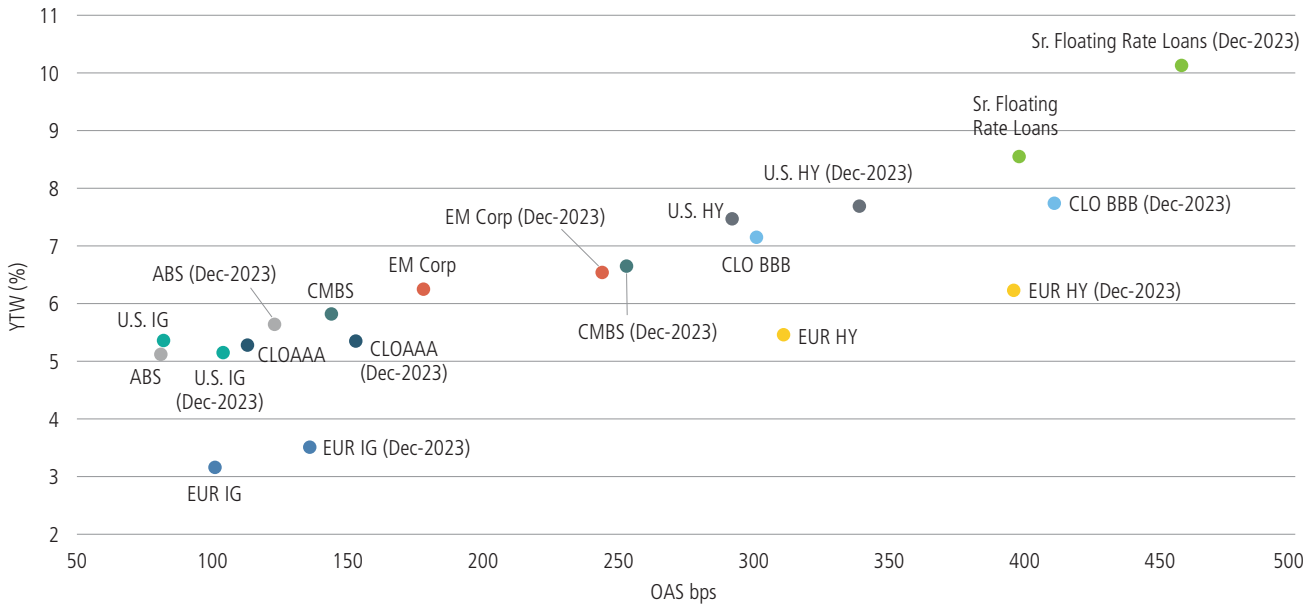
4. Amid Modest Credit Spreads, Focus on Carry

Last year, corporate credit spreads were relatively tight on the back of sturdy economic and business fundamentals. However, there were pockets of dislocation in spread sectors such as agency mortgage-backed securities, with mispricing based on technical issues or misunderstanding of market risks.

Today, however, we see few segments with such widespread anomalies, as reflected in the comparison of yields and option-adjusted spreads shown below. In general, fundamentals continue to justify narrow spreads, although we are seeing some deterioration around the edges. More broadly, with fewer obvious choices for capital, we favor a more incremental view of seeking to maximizing carry across a range of assets, without heavy bets on particular areas.

NARROW GETS NARROWER

Yield to Worst / Option-Adjusted Spread: Current vs. Dec. 2023

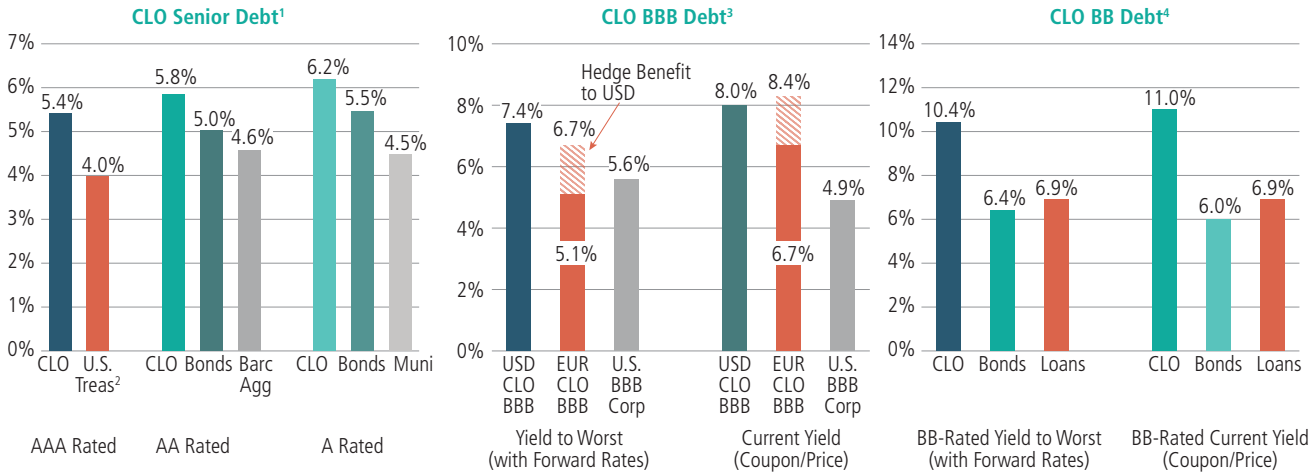


Source: ICE BofA, JPMorgan and Morningstar, as of December 31, 2024. Yields are in local terms (USD for EM Corp). ICE Indices shown: U.S. IG – C0A0; EUR IG – ER00; U.S. HY – H0A0; EUR HY – HE00; EM Corp – EMCL; CMBS – CMBS; ABS – R0A0. JPMorgan: JPM CLOIE AAA Post-Crisis Index; JPM CLOIE BBB Post-Crisis Index. LSTA/ Morningstar Leveraged Loans Index. Yield data is presented as an asset class characteristic, it is not intended to represent or imply any projected return of any investment, strategy or fund, and does not take into account any applicable fees or expenses, which would reduce returns otherwise achieved by the portfolio. **Past performance is no guarantee of future results.**

5. Areas of Opportunity in Credit

Despite broadly narrow credit spreads, some areas continue to provide appealing relative value. These include collateralized loan obligations (below) and hybrid securities, which continue to offer a yield advantage over other fixed income assets of comparable credit quality. Although emerging markets face headwinds over the strong dollar and elevated U.S. rates, we see pockets of opportunity, including in non-investment grade corporates, where default rates are easing (also below); in particular, Latin American high yield offers option-adjusted spread of about 100 basis points over U.S. counterparts, roughly in line with its historical average.

CLOS' YIELD ADVANTAGE



[1] Source: Bloomberg and JP Morgan as of December 31, 2024. Data shown represents CLO yield to maturity inclusive of forward rate curve, loan yield to maturity, bond yield to worst. Benchmarks used were the JPM Morgan CLO Index, ICE BofA AA U.S. Corporate Index, ICE BofA Single-A U.S. Corporate Index, Bloomberg U.S. Aggregate Bond Index and ICE BofA Single-A U.S. Municipal Securities Index. You cannot invest directly in an index. Excludes defaulted issuers. Above index data is intended to solely reflect observations relating to the asset classes noted. Nothing reflected above relates to the performance or yields of any specific investment strategy, product or fund.

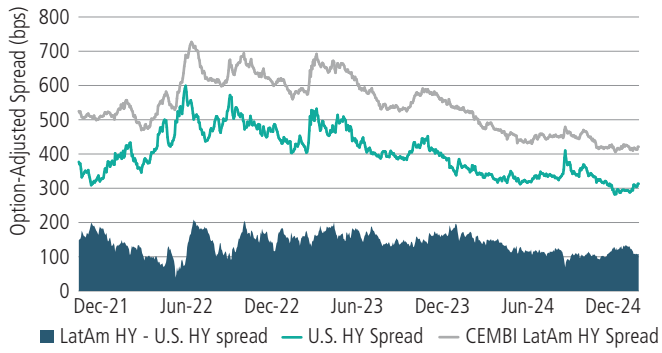
[2] Generic 7-year U.S. Treasury Yield.

[3] Source: Bloomberg, JP Morgan and S&P/LSTA Leveraged Loan Index as of December 31, 2024. Data shown represents CLO yield to maturity bond yield to worst. Benchmarks used were the BofA Corporate Bond Indices and JP Morgan CLO Index. Hedge Benefit to USD is 1.61%, based on annualized benefit of a 3M USD/EUR Forward. You cannot invest directly in an index. Excludes defaulted issuers.

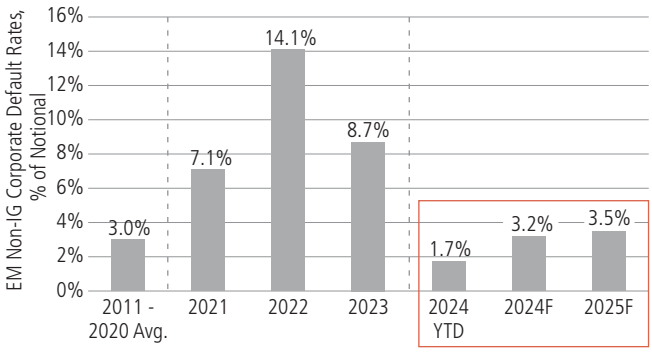
[4] Source: Bloomberg, JP Morgan and S&P/LSTA Leveraged Loan Index as of December 31, 2024. Data shown represents CLO yield to maturity bond yield to worst. Benchmarks used were the BofA Corporate Bond Indices and JP Morgan CLO Index.

EMERGING MARKETS: HIGH YIELD OPPORTUNITY

LatAm Spread Pickup Is Significant



EM Defaults Are Normalizing



Source: Left: Bloomberg, JPMorgan as of December 31, 2024; Right: JPMorgan and NB estimates as of July 31, 2024. NB FY 2024 default rate estimate does not include Russian corporates, as those are no longer part of the investable EM corporate universe.

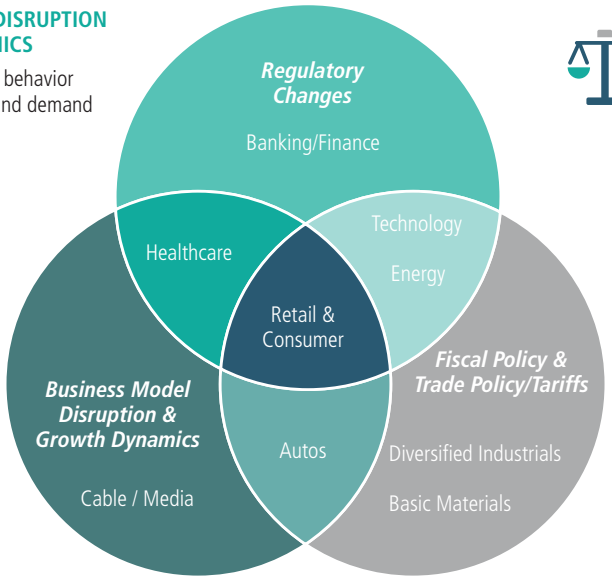
6. Be Prepared for Policy-Driven Volatility

2024 was a time of historic elections affecting over 70 countries. Whether the Labour victory in Britain, electoral gains by the far left and right in France or legislative losses by India's ruling party, the stories together painted a picture of populist shifts and a willingness to cast out incumbents to foment change. Among all the contests, few were as significant as Donald Trump's victory in the U.S., with the potential for impacts across the country's regulatory environment, tax structure and trade, as well as globally.

We will be considering all of these trends as the year progresses, assessing impacts on inflation, rates, geographies and issuers. In our view, it seems likely that the policy environment will be eventful in the coming year and beyond—potentially generating price volatility, but also opening up opportunities for those with the ability and desire to capitalize through the timely use of capital.

CHANGES UNDER TRUMP COULD HAVE FAR-REACHING CONSEQUENCES

BUSINESS MODEL DISRUPTION & GROWTH DYNAMICS
- Changing consumer behavior
- Changes to supply and demand dynamics



REGULATORY CHANGES
- Increased scrutiny of high-profile industries
- Deregulation
- Potential health policy changes
- New antitrust leadership

FISCAL POLICY & TRADE POLICY/TARIFFS
- Trade wars
- Tariffs impacting supply chains
- Corporates impacted by retaliatory behavior

Source: Barclays, Bloomberg.

Market Views

Next 12 Months

	UNDER −−	−	NEUTRAL ◇	+	OVER ++	CHANGE NOTES
GOVERNMENT BOND MARKETS						
United States	○	○	●	○	○	
United Kingdom	○	○	○	●	○	
Germany	○	●		○	○	
France	○	○	●	○	○	
Italy	○	○	●	○	○	
Spain	○	○	○	●	○	
Japan	○	○→	●	○	○	Path of policy normalization (hikes) in line with our outlook. Offers value on a hedged basis.
Canada	○	○	●	○	○	
New Zealand	○	○	○	●	○	
Australia	○	○→	●	○	○	Rates structure in line with other G10 markets; downside economic risk rising as China struggles.
U.S. TIPS	○	○	○	●	○	
INVESTMENT GRADE SECTOR						
U.S. Agencies	○	○	●	○	○	
U.S. Agency MBS	○	○	○	●	○	
U.S. CMBS	○	○	○	●	○	
U.S. ABS	○	○	○	●	○	
U.S. Mortgage Credit	○	○	○	●	○	
U.S. Credit	○	○	○	●	○	
Europe Credit	○	○	○	●	○	
U.K. Credit	○	○	●	○	○	
Hybrid Financial Capital	○	○	○	●	○	
Municipals	○	○	●	○	○	

Market Views (continued)

Next 12 Months

	UNDER −−	−	NEUTRAL ◇	+	OVER ++	CHANGE NOTES
HIGH YIELD & EMERGING MARKETS						
U.S. Full-Market High Yield	○	○	●	○	○	
U.S. Short-Duration High Yield	○	○	○	●	○	
Pan-Euro High Yield	○	○	○	●	○	
Floating-Rate Loans	○	○	●	○	○	
U.S. CLO	○	○	○	●	○	
EM Hard-Currency Sovereigns	○	○	○	●	○	
EM Hard-Currency Corporates	○	○	●	○	○	
EM Hard-Currency Short Duration	○	○	○	●	○	
EM Local-Currency Sovereigns	○	○	○	●	○	
CURRENCY*						
U.S. Dollar	○	○	●	○	○	
Euro	○	○	●	○	○	
Pound	○	●	○	○	○	
Yen	○	○	●	○	○	
Swiss Franc	○	○	●	○	○	
Australian Dollar	○	○	○	●	○	
Swedish Krona	○	○	●	○	○	
Norwegian Krone	○	○	●	○	○	
Canadian Dollar	○	○	●	○	○	
Mexican Peso	○	○	○ →	●	○	Trade risk appears to be adequately priced based on available information; the government is showing a willingness to maintain a good relationship with Trump, which could help prevent harsher tariffs.
South African Rand	○	○	○	●	○	
Brazilian Real	○	○	○	●	○	
Chinese Yuan	○	●	○	○	○	

Views expressed herein are generally those of the Neuberger Berman Fixed Income Investment Strategy Committee and do not reflect the views of the firm as a whole. Neuberger Berman advisors and portfolio managers may make recommendations or take positions contrary to the views expressed. Nothing herein constitutes a prediction or projection of future events or future market behavior. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed. See additional disclosures at the end of this material, which are an important part of this presentation.

*Currency views are based on spot rates, including carry.

Talk to Neuberger Berman

For more information, please contact your Neuberger Berman representative or visit www.nb.com.

FIRM HEADQUARTERS

New York
+1 800 223 6448

REGIONAL HEADQUARTERS

Hong Kong
+852 3664 8800

London
+44 20 3214 9000

Shanghai
+86 21 5203 7700

Tokyo
+81 3 5218 1930

PORTFOLIO MANAGEMENT CENTERS

Atlanta
Boston
Buenos Aires
Chicago
Dallas
Hamilton
Hong Kong
London
Los Angeles
Milan
New York
Paris
Philadelphia
Redwood City
Shanghai
Singapore
The Hague
Taipei
Tokyo
Toronto
West Palm Beach

OFFICES

AMERICAS

Atlanta
Bogota
Boston
Buenos Aires
Chicago
Dallas
Hamilton
Los Angeles
Morristown
New York
Philadelphia
Redwood City
San Francisco
São Paulo
Tampa
Toronto
West Palm Beach
Wilmington

EUROPE, MIDDLE EAST & AFRICA

Dubai
Dublin
Frankfurt
London
Luxembourg
Madrid
Milan
Paris
Stockholm
Tel Aviv
The Hague
Zurich

ASIA PACIFIC

Hong Kong
Melbourne
Mumbai
Seoul
Shanghai
Singapore
Sydney
Taipei
Tokyo

This material is provided for informational purposes only and nothing herein constitutes investment legal accounting or tax advice or a recommendation to buy sell or hold a security. This material is general in nature and is not directed to any category of investors and should not be regarded as individualized a recommendation investment advice or a suggestion to engage in or refrain from any investment-related course of action. Neuberger Berman is not providing this material in a fiduciary capacity and has a financial interest in the sale of its products and services. Neuberger Berman as well as its employees does not provide tax or legal advice. You should consult your accountant tax adviser and/or attorney for advice concerning your particular circumstances. Information is obtained from sources deemed reliable, but there is no representation or warranty as to its accuracy completeness or reliability. All information is current as of the date of this material and is subject to change without notice. Any views or opinions expressed may not reflect those of the firm as a whole. Neuberger Berman products and services may not be available in all jurisdictions or to all client types. Investing entails risks including possible loss of principal. Investments in hedge funds and private equity are speculative and involve a higher degree of risk than more traditional investments. Investments in hedge funds and private equity are intended for sophisticated investors only. Indexes are unmanaged and are not available for direct investment. **Past performance is no guarantee of future results.**

The views expressed herein are those of the Neuberger Berman Fixed Income Investment Strategy Committee. Their views do not constitute a prediction or projection of future events or future market behavior. This material may include estimates, outlooks, projections and other "forward-looking statements." Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed. This material is being issued on a limited basis through various global subsidiaries and affiliates of Neuberger Berman Group LLC. Please visit www.nb.com/disclosure-global-communications for the specific entities and jurisdictional limitations and restrictions.
The "Neuberger Berman" name and logo are registered service marks of Neuberger Berman Group LLC.

NEUBERGER | BERMAN

Neuberger Berman
1290 Avenue of the Americas
New York, NY 10104-0001

www.nb.com

S0026 01/25 2070600 ©2025 Neuberger Berman Group LLC. All rights reserved.