Goldman Sachs Asset Management

FIXED INCOME OUTLOOK 3Q2025

Decoding Dispersion and Divergence

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“The global fixed income opportunity set is richer than it has been in a long time, driven by macro dispersion and divergent central bank policies. This environment presents relative value interest rate strategies in developed markets. We also favor select emerging market local bond markets that benefit from high real rates, further disinflation, and a weaker dollar.”

“As we move into the second half of the year, our attention is on evaluating the impact of tariffs on inflation, jobs, spending, and earnings. For now, solid credit fundamentals continue to support income potential across fixed income sectors. We prefer securitized and high-yield credit for income, but active security selection is key."

CIO Perspectives

The first half of 2025 was marked by significant market volatility and rapid shifts in sentiment due to a series of catalysts, including US tariffs, rising long-end government bond yields, and geopolitical uncertainties. Despite initial sell-offs driven by heightened uncertainty and fears of economic deterioration, the outlook improved, leading to a recovery in financial asset performance. This recovery was supported by tariff de-escalation, a resilient US economy, a Fed willing to respond to labor market weakness, stabilization of long-end bond market volatility, and the avoidance of worst-case geopolitical scenarios. Enthusiasm for AI-related capital expenditure has also buoyed broader risk sentiment. In the second half of 2025, the focus shifts towards discerning the tangible consequences of tariffs on inflation, employment, company earnings, and consumer spending. In addition, while fiscal and geopolitical risks have receded for the moment, they remain potential sources of future market volatility.

In our clients' fixed income portfolios, we stay focused on generating income and delivering total return. We have increased our relative value interest rate exposures to capitalize on divergent central bank actions, as the tariff shock generally reinforces disinflation and dovish policies outside the US. We are also positioned for yield curves to steepen in several markets, including Europe and the US. Additionally, we see opportunities in emerging market (EM) local rates, benefiting from high real rates, dollar weakness, stabilized energy prices, continued disinflation, and monetary easing, particularly in Asia and Central and Eastern Europe (CEE). We supplement our discretionary exposures with systematic strategies to capitalize on short-term market dislocations. Despite sound credit fundamentals, historically tight spreads and potential cyclical weakness, lead us to maintain moderate overall exposure to fixed income spread sectors, with a preference for securitized and high yield credit

The dollar remains a notable exception to the year-to-date rebound seen in most other assets and is a subject of much debate. We anticipate a more nuanced path forward. Regional asset allocation diversification and rising hedge ratios on US asset holdings by global investors may exert downward pressure on the dollar. However, we expect the dollar to retain its status as a safe-haven asset during risk-off events, especially those originating outside the US, and its position as the world's reserve currency. Consequently, we hold an underweight stance on the dollar but use currency options to position for potential episodes of upside. Overall, our approach is deliberate in assessing risks, disciplined in capturing income and relative value, and dynamic in leveraging systematic strategies and active management to modulate our exposures.

Summary of Investment Views

	Underweight	Neutral	Overweight	Investment Perspectives
Sovereign Bonds				
US		●		Neutral but stay tactical to position for anticipated Fed easing.
Euro Area			●	Moderately overweight and positioned for a steepening yield curve, driven by reduced long-end bond demand from Dutch pension funds.
Japan	●			Underweight and positioned for a flattening yield curve given wage-price dynamics support the case for further BoJ rate hikes, contingent on stable global financial conditions.
UK			●	Overweight, expecting that softening labor market dynamics, weaker growth, and slowing inflation will prompt the BoE to accelerate its easing.
Other G10			●	Overweight rates in Sweden, Norway, Canada, New Zealand; domestic macroeconomic factors and global growth risks stemming from trade tensions are expected to reinforce dovish actions by central banks in these economies.
Currencies				
US Dollar	●			Underweight, reflecting expected downward pressure from regional asset allocation diversification and increased hedging of US assets by global investors.
Euro		●		Neutral, in alignment with our currency signals.
Japanese Yen			●	Overweight as informed by our currency signals and expectations of continued BoJ rate hikes, as well as safe-haven demand.
British Pound		●		Tactically neutral, based on our currency signals, but acknowledging that fiscal concerns and further BoE easing could contribute to weakness.
Chinese Yuan			●	Overweight, in alignment with our currency signals.
EM (ELMI)			●	Overweight, in alignment with our currency signals.
Fixed Income Spread Sectors				
IG Credit	●			Moderately underweight in multi-sector portfolios due to tight spreads.
HY Credit			●	Overweight, with a preference for B-rated bonds from companies with strong or improving business fundamentals.
Bank Loans			●	Moderately overweight, attracted by income potential, but selective due to potential stress among borrowers with significant short-term and floating-rate debt.
Agency MBS		●		Neutral given short-term headwinds from interest rate volatility and potential increases in prepayment activity as rates decline.
Securitized Credit			●	Overweight various sectors including CLOs and RMBS, supported by strong fundamentals and attractive carry.
External EMD			●	Moderately overweight, favoring investment-grade bonds BB-rated issuers.
Local EMD			●	Moderately overweight given tailwinds from dollar weakness, stabilized energy prices, continued disinflation, and monetary easing, particularly in Asia and Central and Eastern Europe.

Source: Goldman Sachs Asset Management. As of July 4, 2025. Based on representative exposures in a global multi-sector fixed income portfolio. Currency Signals: We systematically derive investment signals based on analysis of carry prospects, macro fundamentals, and market sentiment. Our portfolio managers then exercise discretion to adjust or override these signals based on fundamental economic research, market intelligence and risk analysis, ensuring a risk-aware approach to optimizing returns.

The economic and market forecasts presented herein are for informational purposes as of the date of this document. There can be no assurance that the forecasts will be achieved. Please see additional disclosures at the end of this document.

Top of Mind

1. Fiscal Flashpoints

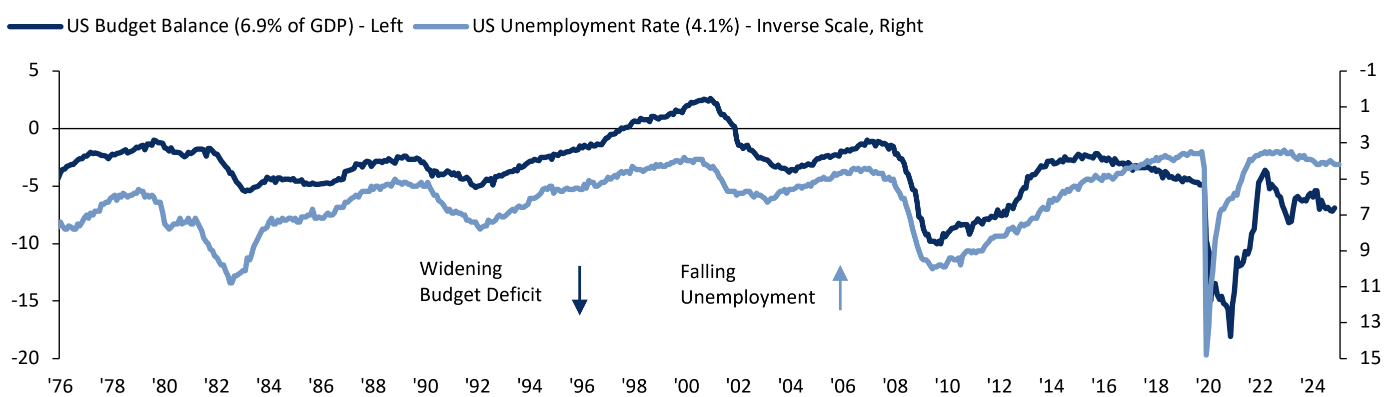
Bottom line: The convergence of higher interest rates, budget deficits, elevated debt levels, slowing nominal growth, and demographic aging pose headwinds to long-term fiscal sustainability globally.

Fiscal sustainability is a recurring concern for investors (see here and here) and focus on this issue has sharpened in 2025, due to events like the Trump Administration's "One Big Beautiful Bill Act (OBBBA)" and increased European defense spending. Gilt market volatility in early July serves as a reminder of the market's sensitivity to fiscal trajectories.

Government debt-to-GDP levels are elevated across major economies, propelled higher in recent years by pandemic-related spending. The path ahead is marked by increasing government spending needs driven by global fragmentation, geopolitical uncertainties, defense spending, green energy initiatives, energy security, and AI infrastructure development. Additionally, many economies, especially in Europe, face demographic challenges. Aging populations lead to higher healthcare and pension costs, coupled with a declining workforce and reduced tax revenues, further straining fiscal positions. History suggests no maximum public debt threshold as a percentage of GDP.[1] The UK saw debt-to-GDP ratios exceed 200% in the 18th, 19th, and 20th centuries due to major wars, and Japan's debt-to-GDP currently stands above 250%. However, conditions surrounding fiscal dynamics, such as weak growth, policy shocks, and rising rates, can create problems. In the post-financial crisis cycle, low interest rates and quantitative easing helped manage debt servicing costs. Today, higher interest rates and the absence of central bank bond-buying have significantly increased debt servicing costs, potentially crowding out productive long-term spending.

In the US, the fiscal deficit has been notably large relative to the economic state and unemployment levels for several years, and this situation does not appear to be changing soon. The renewal of the 2017 tax cuts in OBBBA, only somewhat offset by spending cuts and tariff revenue, suggests a sustained and substantial budget deficit of 6-7% of GDP for the remainder of the decade. We believe the risks are skewed towards wider budget deficits, considering many of the temporary consumer tax cuts may be extended, and tariff revenues may fall short of expectations if tariff de-escalation continues.

Exhibit 1: The US Fiscal Deficit is Notably Large Relative to the Current Economic State and Unemployment Levels



Source: Goldman Sachs Asset Management, Macrobond, U.S. Department of Treasury, U.S. Bureau of Economic Analysis. Unemployment rate as of June 2025, Budget balance as of 1Q 2025.

In Europe, concerns have shifted from peripheral nations to core economies. Italy and Spain continue to benefit from the European Recovery Fund, and a minority government in Spain has restrained fiscal expansion. Conversely, political instability in France following the 2024 snap elections, which resulted in a hung parliament and a fragile coalition, could lead to renewed political volatility, sharpening investor focus on France's fiscal outlook as soon as this summer. The UK has limited room to maneuver against its deficit target, making the Autumn budget a crucial test of fiscal sustainability. China, despite high domestic savings, faces challenges from local government indebtedness, which continues to weigh on growth prospects. Interestingly, many other EM economies, where fiscal

[1] See Goldman Sachs Global Investment Research Top of Mind US fiscal worries: Is this time different? (June 12, 2025) discussion with historian Sir Niall Ferguson.

worries are usually centered, exhibit lower debt levels compared to developed market peers and have seen improvements in external fundamentals in recent years, reducing near-term risks.

There are various strategies to improve fiscal sustainability, but each presents its own challenges. The most optimistic scenario envisions a surge in productivity, driven by widespread AI adoption, which would enable economies to grow out of their debt issues, like the impact of the Industrial Revolution on the UK. However, doubts remain about whether this will occur rapidly or smoothly enough to make a significant near-term difference. Other solutions include running a fiscal surplus, but political will for this appears limited. Less favorable solutions include default (which we believe is unlikely in major economies), unexpected inflation (at the expense of savers), and financial repression, which can discourage saving and investment, hindering growth. US Treasury Secretary Scott Bessent appears focused on debt dynamics and aims to achieve a 3% budget deficit by 2028 through a 3% real GDP growth target, driven by deregulation, energy expansion, and supply-side reforms. While ambitious, the specific steps to achieve these targets remain undefined.

The investment implications of this fiscal environment for government bonds vary by economy. The likely outcome is a continued expansion in term premium, a rise in longer-dated government bond yields, and steeper yield curves. Policy interventions, such as Japan's shift to shorter-dated bond issuance and similar discussions in the US, have temporarily quelled long-end bond market volatility. However, underlying trends in major economies' fiscal positions remain a concern, potentially leading to more periods of volatility as fiscal considerations gain prominence. Pinpointing a precise trigger for fiscal concerns to peak is challenging. Markets could enforce discipline, as seen in the UK in 2022, and arguably earlier this year in the US. This backdrop emphasizes the importance of diversification in fixed income portfolios and a deep understanding of fiscal positions.

SPOTLIGHT ON US TREASURY MARKET MICROSTRUCTURE

The US Treasury (UST) market, the world's largest and most liquid, benefits from well-developed funding (repo) and derivatives markets. These markets allow investors to hedge risks effectively, which, in theory, should result in lower yields compared to markets lacking such depth. However, understanding the market's evolving demand base and evolving microstructure is crucial for identifying potential sources of volatility in the UST market.

The composition of UST demand has changed in recent years. While demand from traditional, long-term investors—such as central banks, insurance companies, pension funds, and sovereign wealth funds—remains significant, it has decreased relative to other investor types. Furthermore, primary dealers, who are authorized to transact directly with the Fed, now hold fewer USTs than in the past. This is partly due to regulatory changes like Basel III, which imposes capital requirements that make holding large inventories of assets like USTs more expensive.

Conversely, the role of leveraged investors, including hedge funds and private funds, has increased. These entities often use USTs for liquidity risk management. However, their demand tends to be less stable than that of traditional investors. They react more quickly to price changes and may rapidly unwind positions during periods of market volatility to manage risks in other parts of their portfolios. The UST market also experiences frequent relative value trading strategies. Examples include:

- **Basis Trades:** Exploiting price discrepancies between similar assets trading in different markets (e.g., cash USTs vs. UST futures).
- **Swap Spread Trades:** Taking positions in interest rate swaps and USTs to profit from changes in the spread between swap rates and government bond yields of similar maturities.

The combination of these shifts in demand and market structure can contribute to periods of heightened volatility. For instance, in 2020 and early 2025, the market saw forced selling of USTs due to factors such as increased market volatility and margin calls in the repo market. Participants in the repo market are primarily concerned with liquidity risk (the ability to quickly sell assets) rather than credit risk (the risk of default).

Policymakers have responded with measures like the Reverse Repurchase Agreement (RRP) facility, the Standing Repo Facility, and adjustments to the Supplementary Leverage Ratio (SLR) to strengthen market stability and increase dealer capacity to hold USTs. However, the bond market volatility in April—when the 30-year US Treasury yield exceeded 5%, and the Japanese equivalent reached a record high—highlights the importance of understanding technical market dynamics and the potential for sudden deleveraging of popular investment strategies. This episode underscored the need for diversified exposures and swift de-risking in the face of acute uncertainty.

2. Dollar Dynamics—Cyclical and Strategic Shifts

Bottom line: Dollar depreciation may extend due to regional asset allocation diversification, a potential increase in hedge ratios on US asset holdings by global investors and narrowing growth and rate differentials but we don't expect the downtrend to be linear.

The DXY index declined by 10.7% in the first half of the year, deviating from the uptrend seen in recent years.[2] The dollar's weakness reflects improving prospects outside the US, such as optimism over German fiscal expansion, Euro area defense spending, and Chinese AI model development, as well as concerns over US policymaking, equity market concentration, and valuations. Although US financial assets have largely recovered April's losses, dollar weakness during the drawdown in US equities earlier this year amplified losses for non-US investors with low or no currency hedges on their non-US asset allocations. This has led investors to reassess hedging strategies. While obtaining hedge ratio data for institutional investors in real-time is difficult, we have observed an increase in hedge ratios among Danish insurers and pension funds, as well as Dutch pension funds, with evidence of smaller increases across Latin American investors.[3] This may have also contributed to the dollar's weakness this year.

Looking ahead, we are mindful that hedge ratios among other global investors, including those in Europe, have room to expand based on our anecdotal client engagements. Slowing US growth relative to the rest of the world and Fed easing may also reinforce dollar depreciation, as these are key factors behind prior periods of sustained dollar weakness. However, any downtrend in the dollar is unlikely to be linear. The dollar can still rally during risk-off episodes, especially if driven by developments outside the US, or during periods of US growth outperformance — a dynamic known as the dollar smile. We think the "smile" dynamic still holds, but it is flatter than before, meaning it now takes significantly more negative news or much stronger positive US growth outperformance for the dollar to rally.

Additionally, we don't believe the dollar is on the verge of losing its status as the global reserve currency, mainly because no alternative matches its scale and liquidity. There will be an increase in high-quality euro-denominated assets given German fiscal expansion, but even after considering this, the supply is modest relative to demand and the size of the US Treasury market. Meanwhile, digital currencies remain in early stages of deployment and are not yet scalable, while policy uncertainty and capital controls remain key constraints on the Chinese currency. Considering the myriad of cyclical and structural dynamics, we are underweight the US dollar but employ currency options to position from potential episodes of appreciation. Read more in [The Dollar's Shifting Landscape: From Dominance to Diversification].

Arnab Nilam
Head of Currency

"My over 20 years of experience trading currencies have shown me that currency valuations are more of an art than a science. While the dollar may seem expensive compared to certain Asian currencies, its valuation against other currencies can largely be justified by relative growth, productivity and interest rate differentials. Although these differentials may be narrowing in favor of other currencies, and a rise in hedging ratios can prolong the dollar's weakness, we caution that the path won't be linear. Growth and rate differentials can still shift in favor of the dollar, which remains dominant as the global reserve currency and benefits from its perceived safe-haven status in times of stress."

3. Germany's Fiscal Push

Bottom line: Germany's announced fiscal push has pulled forward optimism in European assets, but execution challenges could alter the path ahead.

Germany's ambitious 2025 budget, approved in June, represents a significant fiscal expansion. The plan dramatically increases defense spending — targeting 3.5% of GDP by 2029 (up from 2.4% in 2025) — by exempting spending above 1% of GDP from debt brake restrictions. Investment spending will surge to over €115 billion in 2025, a 55% increase from 2024, focusing on areas like rail infrastructure, education, social housing, digitization, and climate protection.

We project this fiscal stimulus to boost economic growth, forecasting 0.5% growth in 2025 (exceeding the consensus forecast of 0.2%) and stronger growth in 2026, a marked improvement over the contractions of 2023 and 2024. The accelerated investment spending will likely increase German Bund issuance in the third and fourth quarters of 2025, potentially steepening the European yield

[2] Source: Macrobond, Goldman Sachs Asset Management. As of June 30, 2025.
[3] Source: Danish Central Bank, Dutch Central Bank, BNP Paribas. As of June 12, 2025. For Latin America, Standard Chartered. As of April 17, 2025.

curve due to higher term premium on longer-dated bonds. However, we anticipate a limited impact on the short end of the German Bund yield curve, with further ECB easing remaining a possibility.

This fiscal expansion, combined with Europe's military build-up, has already fueled optimism over investment potential in the region, lifting the euro, European equities, and European bonds. The euro's 9% appreciation against the dollar in 2Q 2025 marked its second-largest quarterly gain in a decade.

Despite this positive outlook, we identify several key execution risks. Legislative approval in September could result in amendments and Germany's political fragilities could delay approval. Moreover, historical trends suggest that actual investment may fall short of planned levels due to execution delays caused by capacity constraints, material shortages and skills gaps. It's also important to note that a 0.5% growth rate remains modest in a global context.

GERMAN FISCAL FIGURES IN FOCUS

€1tn

Significant Fiscal Expansion[4]
Expected spending over the next 10-12 years, equivalent to ~21% of GDP, including €500bn on infrastructure and €300bn on defense.

€150bn

Increased Bund Issuance[5]
Estimated net German bund issuance in 2026, up from €80bn in 2024 and a projected €102bn in 2025.

0.5%

Front-Loaded Growth Uplift[6]
Estimated German growth in 2025, a sizeable improvement on -0.2% contractions in 2023 and 2024.

Macro at a Glance

Growth: Steady Deceleration

US economic growth data from early 2025 has been distorted by anticipatory behavior related to expected tariffs. Importers front-loaded imports and built-up inventories to avoid tariffs, which artificially depressed 1Q GDP growth figures. A corresponding reversal of these effects is expected to boost 2Q data. While the US One Big Beautiful Bill Act (OBBBA) may appear substantial, its impact on growth is projected to be limited. This is because the bill primarily prevents fiscal policy tightening by extending the 2017 tax cuts. In addition, the structure of the OBBBA's tax cuts favors higher-income individuals, who are likely to save a portion of any additional income, especially if they perceive the tax changes as temporary. In contrast, the bill's proposed cuts to social safety net programs like SNAP (Supplemental Nutrition Assistance Program) and Medicaid could significantly affect spending by lower-income consumers.

Concurrently, the US labor market, a key determinant of consumer spending, is gradually slowing. Evidence includes downward revisions to payroll data, narrower job gains, slower private sector growth, elevated jobless claims, and declining consumer confidence in the job market. The decrease in the unemployment rate to 4.1% in June was mainly due to a reduction in labor force participation rate, rather than robust job creation. This decline in participation could be a sign that tighter immigration controls are beginning to take effect. The revocation of work visas for certain immigrant workers may reinforce this trend in the coming months. Overall, we expect slower US economic activity due to the impact of tariffs, which will only be partially offset by fiscal policies. However, we anticipate slower growth, not an outright economic contraction.

Europe is currently exhibiting positive economic momentum and China has experienced a temporary boost to its economy due to accelerated exports ahead of the anticipated tariffs. However, both the European and Chinese economies remain susceptible to adverse effects from the implemented tariffs and any significant deceleration in US economic growth. Despite tariff headwinds, fundamental

[4] Source: Goldman Sachs Asset Management, UBS German fiscal: A large spending increase ahead (June 25, 2025), Morgan Stanley, Goldman Sachs Global Investment Research Germany—Budget Announcement Suggests a More Frontloaded Fiscal Boost (June 25, 2025), J.P.Morgan Germany: A big fiscal ease now, return to caution later (June 26, 2025).

[5] Source: Goldman Sachs Global Investment Research. As of June 27, 2025.

[6] Source: Goldman Sachs Asset Management forecast as of July 3, 2025. 2023, Macrobond for 2023 and 2024 growth.

strengths within the global economy, such as healthy private sector balance sheets in many major economies, suggest that global economic expansion is likely to persist, although at a more moderate pace than previously observed.

Inflation: Country Divergence

Recent US inflation data shows disinflation in the services sector, including rents, and only a limited initial pass-through of tariff costs to consumer goods prices. We expect the impact of tariffs on inflation to become more evident in the coming months. However, the fluctuating nature of tariff rates may delay price adjustments as businesses await greater clarity, and the large stock of inventory built up in advance of tariffs could also contribute to this delay. That said, we believe the inflationary impact of tariffs in the US will be less severe and shorter-lived compared to the inflation surge in 2021-2022. Several factors support this view:

- We anticipate a peak inflation rate of 3-4%, much lower than the 9% peak during the pandemic. This reflects a narrower breadth of inflation, contained supply chain stress, and continued services disinflation.
- The labor market is not as tight as it was during the previous inflationary period, reducing wage pressures.
- Unlike 2021-2022, household spending power is not being boosted by government stimulus checks.
- 1Q earnings season commentary suggests that companies are mitigating tariff-driven input cost increases through supply chain diversification, cost reductions, and inventory stockpiling, rather than solely passing on costs to consumers (though some pass-through is still anticipated).
- Long-term inflation expectations remain well-anchored

We would become more concerned about persistent tariff-driven inflation if country-specific tariffs rose back to prohibitive rates or if tariff revenue is used to provide broad-based stimulus checks for consumers. Outside the US, we generally expect tariffs to reinforce disinflationary trends. The Euro area has achieved its 2% inflation target, while the UK is experiencing disinflationary pressure due to a slowing labor market and reduced economic activity. In China, manufacturing overcapacity, weak domestic demand, and demographic challenges are expected to continue to contribute to deflationary pressures. Conversely, an upswing in domestic demand and wage growth are expected to sustain inflationary pressures in Japan.

Policy Picture

Steady Easing

Although the Fed has maintained a steady policy stance this year, recent communications indicate low tolerance for labor market weakness. We anticipate two rate cuts in 2025, one in September and another in December, contingent on steadily rising unemployment and a temporary inflation boost from tariffs. Outside the US, the tariff shock supports easing paths across smaller DM and EM economies, although easing actions may slow as policy rates approach neutral. We expect the BoE to resume rate cuts in August, followed by consecutive reductions starting in 4Q, ultimately lowering the Bank Rate to 3.25%. This forecast is based on expectations of slower growth and continued labor market loosening. We also foresee further easing in Europe, though German fiscal plans, which imply a more front-loaded growth uplift than previously anticipated, may slow the ECB down. Meanwhile, we believe global financial stability and domestic price pressures will pave the way for the BoJ to resume rate hikes. Additionally, we expect further easing among smaller DM central banks, such as those in Sweden and Canada. Easing actions are also expected to continue in EM economies, particularly across Asia and Central Eastern Europe, with the recent pullback in oil prices and dollar weakness alleviating inflation risks.

What We're Watching

Tariffs & Trade

The coming months will be pivotal in assessing the true economic impact of the implemented tariffs. Drawing from the 2018 trade war experience, we expect a 3–4-month delay before tariffs significantly influences consumer prices, suggesting the impact will become more noticeable this summer. However, this timeline could be extended due to the current volatility in tariff rates. It will also be crucial to monitor the job market's health and its capacity to sustain consumer spending, as the tax-like effects of tariffs begin to weigh on disposable incomes. Additionally, we are closely watching the progress of ongoing trade negotiations, with sector-specific tariffs on pharmaceuticals, semiconductors, and critical minerals remaining a possibility.

Corporate Earnings

Corporate bond investors have found reassurance in the continued resilience of credit fundamentals, as reflected in 1Q earnings season. Recent company guidance in the US points towards slower hiring (influenced by both tariffs and the rise of AI), constrained capital expenditure beyond AI-related investments, below-potential economic growth (though not a recession), and a one-time inflationary effect. As we move into 2Q earnings season, a central question is whether the strong earnings performance earlier this year was driven by pulled-forward activity or genuine, sustainable resilience. Our research analysts will be closely assessing how tariffs are impacting corporate profit margins: Are companies successfully passing increased costs onto consumers, or are profit margins being negatively affected? We will also focus intently on forward guidance, particularly regarding hiring plans and capital expenditure forecasts.

Geopolitical Risks

The recent escalation in geopolitical tensions in the Middle East serves as a stark reminder that fresh shocks can emerge unexpectedly. However, unless the worst-case scenarios materialize, the impact on financial markets tends to be short-lived. While recent geopolitical tensions have subsided, a more transactional approach to security alliances and global trade suggests that flare-ups may become more frequent. The most critical factor for investors to monitor is the potential economic impact on energy supply and prices. However, it is equally important to assess which economies are more reliant on or resilient to energy price volatility.

Asset Class Views

Interest Rates

Outlook

We anticipate the Fed will maintain a "wait-and-see" approach this summer, but recent signals suggest a low tolerance for a weakening labor market. We continue to forecast two rate cuts in 2025 (September and December), contingent on a steady rise in unemployment and the tariff impact on inflation being narrow, primarily affecting goods, and short-lived. However, the risks lean towards a later start to easing, given recent strong jobs data. Importantly, the Fed's decisions will be data-dependent, not solely based on the dot plot projections, which still indicated two cuts at the June meeting.

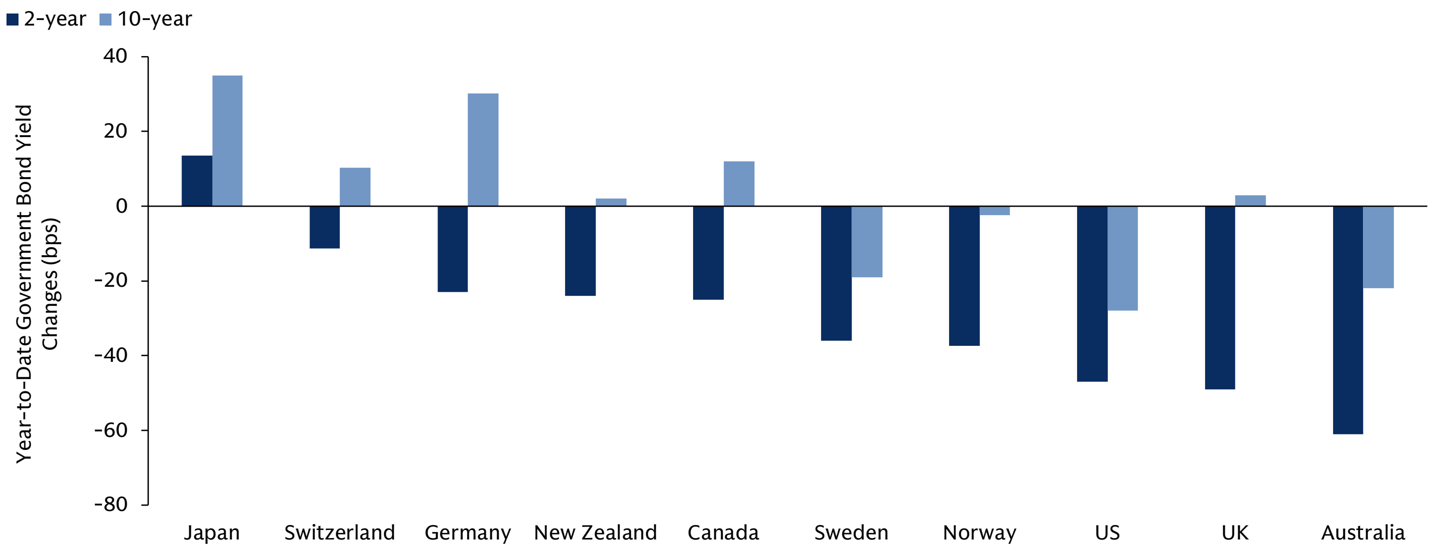
Regarding the ECB, given recent activity momentum, reduced uncertainty around tariff policy, and front-loaded German fiscal easing, we now only expect one more cut down from two previously, likely in September, bringing the policy rate down to 1.75%. We expect the BoE to resume rate cuts in August, followed by consecutive reductions starting in November, ultimately lowering the Bank Rate to 3.25%. This forecast is based on expectations of slower growth, reduced wage growth, and a continued loosening of the labor market.

We also foresee further easing among smaller G10 economies. The Riksbank in Sweden, for instance, signaled greater openness to further easing after a 25bps cut to 2% at its June meeting. This, combined with our expectation that the impact of trade policy will become apparent in upcoming activity data, leads us to expect a further rate cut from the Riksbank in September. The Norges Bank in Norway surprised with a 25bps rate cut to 4.5% in June, initiating its easing cycle three months earlier than anticipated. We expect a gradual easing path ahead, with two further rate cuts expected this year. Reflecting the divergence in the global economic landscape, the SNB in Switzerland recently lowered its policy rate to 0%, and a return to negative rates seems plausible, while the BoJ appears set to continue moving away from ultra-low policy rates.

Opportunities

Global macro dispersion and central bank divergence strengthens the case for diversified duration exposures and creates a rich opportunity set for relative value interest rate views. We believe the market is underpricing future easing by the BoE, creating a favorable environment to be overweight UK rates. Overweight opportunities also exist in smaller G10 markets like Sweden and Norway, where inflation momentum has slowed, and in New Zealand and Canada, where market expectations for monetary easing appear insufficient. We are also positioned for a steepening of the European yield curve, driven by diminished demand for long-end bonds from Dutch pension funds and an increase in German bund issuance. Conversely, we are underweight Japanese rates and positioned for a flatter Japanese yield curve as higher inflation supports further rate hikes by BoJ. While we maintain a neutral stance on US rates, we believe the Fed's readiness to respond to labor market weakness will help preserve the diversification benefits of US Treasuries in multi-asset or multi-sector fixed income portfolios, particularly in the event of unexpected economic downturns. Recognizing the complexities of the investment environment, we also see opportunities to complement active interest rate views with systematic strategies driven by various disaggregated factors influencing asset prices and returns. These data-informed strategies are grounded in a deep understanding of market structure and fundamental return drivers. These drivers encompass macro factors like inflation dynamics, statistical relationships such as mean reversion, market dynamics including new issuance activity, and security-level characteristics, notably curve steepness, which can generate carry and roll opportunities. Read more in Asset Management Mid-Year Outlook 2025: Broader Equity Horizons and Income Generation.

Exhibit 2: A World of Diverging Rate Moves Presents Relative Value Opportunities



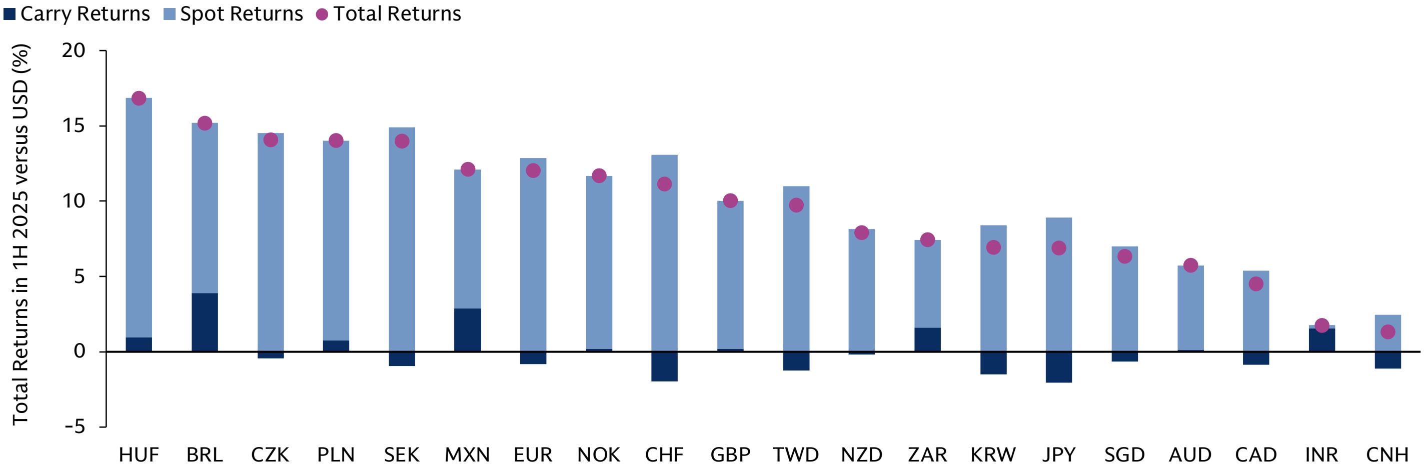
Source: Macrobond, Goldman Sachs Asset Management. New Zealand and Japan as of July 3, 2025. Other markets as of July 2, 2025.

Currencies

Outlook

The first half of 2025 saw negative total returns for the US dollar across major currency pairs. European currencies, particularly those in Central and Eastern Europe, showed the strongest year-to-date total returns. The euro notably appreciated 9% against the dollar in 2Q 2025, its second-largest quarterly gain in a decade. Looking forward, we anticipate that trade-related uncertainties and geopolitical tensions will take a backseat in driving currency moves compared to the relative economic performance of the US versus the rest of the world. While currency flow and hedging strategies remain relevant, we expect US economic data to become the primary driver of currency movements. US jobs data will be crucial in determining the Fed's policy path and will remain a key area of attention. Nonfarm payroll (NFP) surprises tend to have asymmetrical effects on DM and EM currencies. A weaker-than-expected NFP report offers less support to DM currencies compared to the pressure stemming from a stronger-than-expected report. Conversely, EM currencies, such as the Mexican Peso (MXN) and South African Rand (ZAR), tend to outperform more significantly in response to a weak NFP print compared to their reaction to a strong one.

Exhibit 3: Most Currencies Gained Ground Versus the Dollar in 1H 2025



Source: Goldman Sachs Global Investment Research, Goldman Sachs FIC and Equities GS FX Morning Notes: Looking back, looking ahead. As of July 2, 2025. Spot return arises from changes in spot exchange rates which can arise from economic variables, market sentiment and risk appetite, and technical factors. Carry return comes from the interest rate differential between two currencies.

Opportunities

We are underweight the US dollar due to downward pressure from regional asset allocation diversification and rising hedge ratios on US asset holdings by global investors. However, we believe the dollar can still rally during risk-off episodes, especially if these are driven by developments outside the US. We also expect the dollar to maintain its status as the world's reserve currency, as no other currency matches its scale and liquidity. Accordingly, we use currency options to position for potential episodes of dollar upside. Elsewhere, we are overweight the Japanese yen in anticipation of further BoJ rate hikes and considering its perceived safe-haven status. We are also overweight commodity-oriented currencies such as the Canadian and Australian dollars, as well as Asia currencies running positive net international investment positions such as the Korean won and Singaporean dollar.

Investment Grade

Outlook

Even though US investment grade (IG) spreads are near their tightest levels in 15 years (6th percentile), IG credit offers attractive income and total return potential due to elevated yields. Solid underlying fundamentals suggest that credit spreads should remain well-behaved, even amid an expected deceleration in US economic growth stemming from the effects of tariffs. We are carefully monitoring the impact of tariffs on 2Q corporate earnings to ascertain whether the robust 1Q performance was driven by accelerated activity or genuine underlying strength. We are encouraged by the financial conservatism exhibited by companies, particularly those rated BBB, who continue to allocate less than 100% of their operating cash flow to capital expenditures, dividends, and share repurchases. While we anticipate a rise in fallen angels (companies downgraded to high yield) this year relative to the unusually low levels of recent years, we expect downgrade volumes to remain below the peak levels observed during the pandemic, the 2016 energy crisis, and the global financial crisis. We observe similar positive trends in the European market.

Opportunities

In multi-sector fixed income portfolios, we are slightly underweight IG credit, favouring high-yield (HY) credit and securitized sectors instead. However, within dedicated IG portfolios, we are moderately overweight, capitalizing on market volatility to increase exposure to our high-conviction ideas at attractive levels, including participating in new bond issuances. We maintain an overweight position in BBB-rated bonds that exhibit strong credit fundamentals, anticipating limited fallen angel activity. However, we are closely monitoring the lower end of the BBB rating spectrum. We also favour European and US banks. Our preference is for senior debt issued by large, systemically important banks that possess sufficient capital to withstand a normalization in asset quality (i.e., a potential increase in loan delinquencies). Conversely, we are cautious about the global auto sector due to slowing demand, declining profit margins, and tariff-related challenges, though see selective opportunities. We are also wary of US utilities, as investments related to the energy transition has led to weaker credit metrics and increasing bond supply. Within Euro utilities, we prefer the electric sub-sector due to its defensive characteristics, domestic European focus, and strong regulatory oversight.

High Yield Credit and Bank Loans

Outlook

We anticipate continued strong total returns from HY credit and bank loans in the second half of the year, driven by robust fundamentals, supportive market dynamics, and attractive yields. 1Q earnings season reinforced our positive view of credit fundamentals, with 75% of the companies we monitor reporting revenue and EBITDA growth that met or exceeded expectations. Furthermore, over 80% of companies provided forward guidance that was in line with or better than expected, despite anticipated concerns related to the uncertain impact of tariffs. From a technical perspective, high single-digit yields continue to draw investor interest, with demand surpassing supply. In fact, the leveraged loan and, particularly, the high-yield bond market have contracted in recent years due to rating upgrades to investment-grade credit and reduced gross new bond issuance. This partly reflects a shift among lower-quality issuers to private credit markets, where they can secure more tailored lending arrangements. Within the leveraged loan market, strong gross issuance has primarily been driven by repricing and refinancing activities, with the remaining portion largely allocated to CLO formation, which has become a structural source of demand for the asset class. We expect these favorable trends to persist.

Opportunities

Despite recent spread compression, we continue to see attractive income and total return potential in the HY credit and leveraged loan markets, particularly in B-rated bonds issued by companies exhibiting strong or improving business fundamentals. We favor companies in the industrials and capital goods sectors with diversified revenue streams and robust order pipelines, including those involved in data center infrastructure and aerospace production, benefiting from increased global infrastructure spending. We also maintain a constructive outlook on select technology companies characterized by pricing power, recurring demand, conservative capital management, and diversified exposures, including those in the software-as-a-service (SaaS) space, and favor companies in the insurance broker sector, which benefit from high policy renewal rates, consistent organic growth, and strong free cash flow generation. Conversely, we are cautious on homebuilders, building products, autos, chemicals, oilfield services, and other consumer-oriented sectors, as these are more vulnerable to a potential slowdown in consumer spending, rising interest rates, higher input costs, and tariff-related headwinds, though we are selectively identifying opportunities within the consumer cyclical sector where valuations appear compelling. Within the energy sector, we hold a favorable view on select companies in the Liquefied Natural Gas (LNG) space, as well as issuers focused on renewable energy infrastructure, benefiting from long-term contracts and increasing demand for clean energy solutions. Lastly, we remain underweight in the media and communications sectors due to ongoing digital disruption, and the healthcare sector, given high leverage, elevated labor costs, limited free cash flow, and increasing government budget scrutiny.

Agency MBS

Outlook

While the sector is generally insulated from concerns about slower economic growth and has the potential to outperform other fixed-income spread sectors in in a decelerating growth environment, we are mindful of short-term challenges posed by increased interest rate volatility stemming from trade policy uncertainty and the potential for elevated prepayment risks in a declining interest rate environment. From a technical perspective, recent fund outflows represent a near-term headwind, as banks and non-US investors have remained largely inactive. However, we continue to anticipate that demand from domestic banks will become a positive market factor later in the year. While we expect policy rates to trend downward, we anticipate that intermediate bond yields and mortgage rates will remain higher than in the previous economic cycle. This, coupled with constrained housing affordability, will likely moderate housing market activity and, in turn, limit the supply of agency MBS. We remain constructive on mortgages and believe improving technicals later in the year should benefit the sector.

Opportunities

Given recent interest rate volatility and macroeconomic uncertainty, we currently hold a neutral position in agency mortgage-backed securities. We favour higher and lower coupon mortgages, while holding an underweight position in intermediate ("belly") coupon mortgages, as higher coupons offer more attractive valuations and belly coupons exhibit weaker market support. Within specified pools, we are overweight higher coupon and loan balance pools, which we believe should offer some protection against prepayment risk in the event of a rate rally.

Securitized Credit

Outlook

The securitized credit market offers a diverse range of sub-sectors, each presenting compelling investment opportunities. We believe its total return and income potential makes this asset class attractive, both as a standalone allocation and within a multi-sector fixed income portfolio. Many assets are floating rate with low duration, potentially leading to outperformance in a sustained high-interest-rate environment. From a fundamental perspective, stronger levels of credit enhancement should provide sufficient protection against an increase in delinquencies as the cycle extends. Furthermore, declining interest rates should support risk assets and specific sectors like CMBS valuations, improving refinancing ability. The structural protections built into securitized assets' capital structures can also help protect investors from losses, depending on their position within the structure. From a technical standpoint, investor demand remains robust. While gross supply in sectors like CLOs remains elevated, net supply remains constrained, ultimately being a positive for spreads in the sector. We expect these favorable dynamics to persist throughout the year.

Opportunities

We currently see value in Collateralized Loan Obligations (CLOs) and Residential Mortgage-Backed Securities (RMBS), while maintaining a neutral stance on Asset-Backed Securities (ABS). CLOs offer attractive income and return potential relative to our assessed risks, underpinned by our expectation of continued robust loan fundamentals. We have capitalized on recent underperformance in RMBS to increase our exposure at compelling valuations, particularly in the US where the housing sector remains strong and consumer balance sheets are healthy. Within RMBS, we favor AAA-rated securities due to their valuations and robust credit support. In the Commercial Mortgage-Backed Securities (CMBS) sector, we have shifted our allocation towards A- and AAA-rated securities, reducing our exposure to BBB-rated securities in response to recent market dynamics and the more attractive income and return potential we see in higher-rated securities relative to their underlying risks.

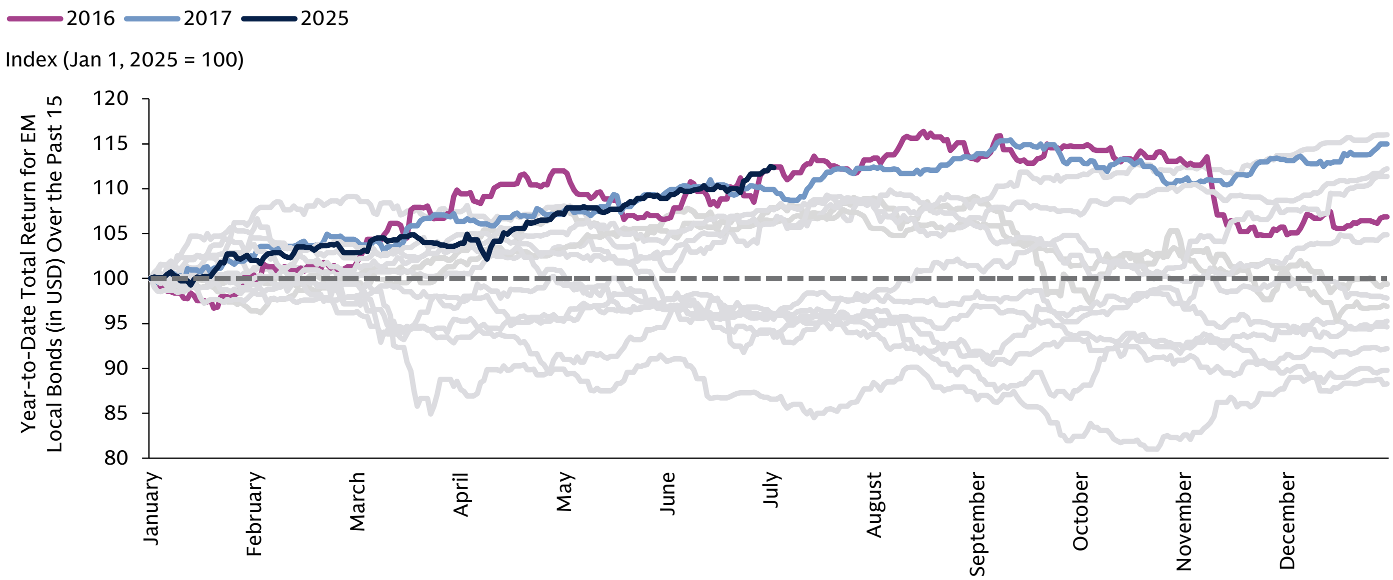
Emerging Market Debt

Outlook

Emerging market debt delivered robust positive total returns in the first half of the year, spearheaded by EM local rates (12.3%), benefiting from a weaker US dollar and declining EM rates, followed by EM external sovereign debt (5.6%) and EM corporate bonds (4%).[7] Looking ahead to the second half of 2025, we anticipate this strong performance will continue, driven by renewed Fed easing, potential inflows into the asset class, and a projected EM-DM growth differential of 2.4% in 2025.[8] Reduced trade policy uncertainty and a shift towards trade deals versus tariff escalation should further bolster growth prospects. Despite a slowing pace of disinflation, high real rates, easing energy price pressures, and a weaker dollar should facilitate further monetary easing across EM economies, supporting EM local bond gains, EM currency resilience, and steeper yield curves. We expect the positive ratings momentum observed across sovereigns and companies since 2024 to persist, with rising stars from high yield to investment grade and upgrades among lower-rated cohorts. EM corporate fundamentals are also expected to remain robust, demonstrating continued financial discipline. While persistent outflows have been a headwind, recent months have shown stabilization and signs of renewed inflows, which we believe could continue. Low starting allocations to EM assets suggest strong performance may attract further inflows. Overall, we expect carry, tailwinds from Fed easing, and a weaker dollar to support EMD returns in the second half of the year, with positive ratings actions contributing to spread tightening. Key risks include slower-than-expected deceleration in the US or renewed dollar strength, as well as heightened geopolitical volatility.

[7] Source: J.P.Morgan. As of June 2025.
[8] Source: Goldman Sachs Global Investment Research. As of June 30, 2025.

Exhibit 4: EM Local Bonds Posted One of Their Strongest H1 Performances in Recent History



Source: Goldman Sachs Global Investment Research The EM Trade: The Upside in H2, Bloomberg. As of July 2, 2025. Based on the Bloomberg EM Local Currency Government 10% Country Capped Total Return Index Unhedged USD.

Opportunities

We view EMD as an attractive source of income and alpha potential, driven by high dispersion within the asset class. Given the US-centric nature of recent economic events, EMD offers valuable diversification benefits, and improving technical factors support a positive outlook. Within EM sovereign bonds, we favor investment-grade credits for their income potential, as well as BB-rated issuers like Morocco, Serbia, and Paraguay, which we believe are candidates for upgrades to investment grade. We also expect resilience in large, domestically-oriented economies such as Brazil. Select frontier countries offer investment potential due to positive reform momentum and commitment to addressing economic imbalances. In EM local bond markets, we anticipate a tailwind from central bank easing, particularly in markets with high real rates, and expect resilient currency performance. While the correlation between EM local rates with US 5-year Treasury yields has trended lower, we remain vigilant regarding potential currency weakness linked to a weaker Chinese currency or a stronger US dollar if Fed rate cuts are delayed. In EM corporate bonds, we are overweight BB- and BBB-rated issuers, favoring non-cyclical sectors like Food & Beverages due to their strong brand recognition, global operations, and customer loyalty. Select airport issuers in Mexico and Panama are attractive due to limited competition and resilient passenger numbers. Conversely, we are underweight financials across Asia and the Middle East due to valuation concerns in the higher-quality segments. Overall, we maintain a nimble approach, expecting EM corporates to demonstrate financial flexibility and preserve their credit metrics. We are also monitoring fiscal concerns, particularly in Latin American, Central and Eastern European countries, and lower-rated frontier economies.

Municipal Bonds

Outlook

Elevated new bond supply, driven partly by concerns regarding potential changes to tax exemption rules, has been a significant headwind for the municipal bond market over the past 18 months and is expected to continue into the coming quarter. However, we anticipate a moderation in supply volumes compared to the strong pace observed in the first half of the year. Despite the increase in new issuance and the subsequent rise in yields, credit spreads have remained relatively stable, reflecting the generally sound financial health of municipal issuers, a trend we expect to continue. We are closely monitoring sectors such as higher education and hospitals, where careful credit selection is crucial due to potential financial pressures. While headlines regarding credit deterioration warrant attention, the actual impact on credit fundamentals has been limited thus far, though we continue to monitor this dynamic. As we enter the summer reinvestment season, we anticipate strong demand across various investment vehicles—SMAs, mutual funds, and ETFs—as investors

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reinvest capital and proceeds from maturing securities. While elevated new supply may temper potential outperformance, we still expect reasonable performance in the third quarter, supported by strong demand and attractive starting yields.

Opportunities

We see attractive income potential across the investment universe, particularly after the recent yield increases in intermediate and longer-dated bonds. Intermediate-maturity bond valuations appear fair relative to historical levels, with yields on high-grade municipal bonds in that segment of the curve now exceeding their decade average by more than 100bps. Long-end maturities are particularly appealing, given their relative underperformance due to the yield curve steepening observed in the prior quarter, although this underperformance could persist through year-end. The risks associated with potential tax policy changes appear to be diminishing, and the elevated new issue volumes seen recently are unlikely to continue for the rest of the year, potentially providing positive momentum in the coming months. Furthermore, given the wide dispersion of opportunities within the high-yield market, active credit selection is crucial. Our outlook anticipates that income will be the primary driver of returns in the near term, with credit spreads expected to remain range-bound. Therefore, incorporating high-yield exposure has potential to enhance overall portfolio performance for the year.

Responsible Investing

Outlook

Global issuance of green, social, and sustainability bonds rebounded in 2Q, bringing year-to-date issuance to levels comparable to 2024, a record year.[9] Sentiment towards sustainability has become more positive in Europe and Asia, with new issuers continuing to finance green, social, and sustainability capital expenditures through initial issuances of labeled bonds. With spreads having tightened to levels similar to the start of the year, yields remain at favorable income levels, making them attractive for investors. Given the Euro's dominance, anticipated rate cuts from the ECB before year-end are likely to support the performance of sustainable fixed income for the remainder of the year, contingent on market volatility. Demand for sustainable fixed income funds and separately managed accounts (SMAs) is increasing in Asia as the cost of dollar hedging rises and sustainability ambitions grow, driving increased allocations.

Opportunities

Green bonds have continued to outperform conventional investment-grade bonds year-to-date. With duration increasingly correlated with conventional bonds, this asset class offers advantages for investors rebalancing back into fixed income following the equity rally after April's market volatility. Given the challenges of assessing the true green, social, or sustainable nature of a bond, active selection with a focus on evaluating the ESG attributes of both issuers and bonds remains crucial.

Liquidity Solutions

Outlook

Market expectations for Fed easing currently exceed the median projections outlined in the June Summary of Economic Projections (the "dot plot"), which indicated two rate cuts this year. However, the Fed's actions will be driven by incoming economic data, particularly labor market outcomes, rather than the dot plot itself. Greater clarity on trade policy and potential fiscal changes will also be important for shaping US monetary policy. We believe there is a case for a couple of rate cuts later this year, contingent on a gradual increase in the unemployment rate and a short-lived inflationary impact from tariffs.

Opportunities

We believe money market funds offer investors stability and liquidity amid near-term market volatility. For investors who can segment their cash allocation and are willing to extend duration, short-duration strategies provide a high-quality source of income that can complement existing fixed income strategies, while exhibiting lower volatility. These strategies can offer higher income relative to cash, while maintaining reasonable liquidity.

[9] Source: Goldman Sachs Asset Management, Bloomberg. As of June 30, 2025.

Central Bank Snapshot

	INTEREST RATE POLICY	BALANCE SHEET POLICY	OUTLOOK	NUMBER OF CUTS EXPECTED FOR THE REMAINDER OF 2025	OUR OUTLOOK VERSUS MARKET-IMPLIED PRICING
Fed	**Federal funds rate:** 4.25-4.5% **Last change:** December 2024 (-25bps) **Start of the cutting cycle:** September 2024 **Rate at the start of the cutting cycle:** 5.25-5.5%	At the March FOMC meeting, the Fed decided to slow the pace of QT, lowering the cap on Treasury runoff from $25bn/month to $5bn/month effective April, while keeping the MBS cap of $35bn/month unchanged.	If the economy avoids second-round inflation effects and unemployment rises steadily from 4.1% to around 4.4-4.5%, two Fed rate cuts seem plausible. **Expected rate at end-2025:** 3.75-4.0% **Neutral rate estimate:** 3.0%	**Our outlook:** 2 **Market-implied pricing:** 2	Neutral
ECB	**Deposit facility rate:** 2.0% **Last change:** June 2025 (- 25bps) **Start of the cutting cycle:** June 2024 **Rate at the start of the cutting cycle:** 4.0%	The ECB started reducing its balance sheet in March 2023 and ceased reinvestments from its APP in July 2023. The reinvestment of proceeds from maturing securities under the PEPP decreased, which started in July 2024 and concluded in December 2024.	Further disinflation progress and export headwinds from a stronger euro may prompt a further rate cut in September. **Expected rate at end-2025:** 1.75% **Neutral rate estimate:** 2.0-2.25%	**Our outlook:** 1 **Market-implied pricing:** 1	Neutral
BoE	**Bank Rate:** 4.25% **Last change:** May 2025 (-25bps) **Start of the cutting cycle:** July 2024 **Rate at the start of the cutting cycle:** 5.25%	The BoE has actively been reducing its balance sheet since November 2022. At the September 2024 meeting, the MPC voted to maintain the pace of gilt stock reduction at £100bn. Given higher redemptions, this implies a notable reduction in the pace of active sales.	We expect the BoE to maintain its quarterly easing pace, potentially accelerating to consecutive meetings from November, especially if inflation momentum decreases and global growth risks from tariffs persist. **Expected rate at end-2025:** 3.5% **Neutral rate estimate:** 2.5-3.5%	**Our outlook:** 3 **Market-implied pricing:** 2	Dovish
BoJ	**Policy deposit rate:** 0.5% **Last change:** January 2025 (+25bps) **Start of the hiking cycle:** March 2024 **Rate at start of the latest hiking cycle:** -0.1%	The gradual reduction plan for JGB purchases will be from around ¥6tn per month to around ¥3tn over 18 months. Reduced bond buying is focused on intermediate maturity bonds.	Domestic activity remains stable, but inflation is reaccelerating and above target. If tariffs are rolled back and market stability continues, we expect the BOJ to resume hiking later this year. **Expected rate at end-2025:** 0.75% **Neutral rate estimate:** 1.0-1.5%	**Our outlook:** 1 **Market-implied pricing:** 0 – 1	Slightly hawkish

Source: Goldman Sachs Asset Management, Bloomberg for market-implied pricing. As of July 4, 2025. Abbreviations: Quantitative Tightening (QT). The neutral rate estimates come with a degree of uncertainty. They are derived from a combination of fundamental, market, and model-based assessments. The ranges for the Fed, BoE and BoJ reflect the diversity of these estimates. For the ECB, the range represents the spectrum of policymakers' estimates, which has been adjusted based on our discretionary perspective. Estimated neutral rates by central banks are as follows: BoE 2-3%, BoJ 1-2.5%, Fed 2.4-3.8%, ECB 1.5-3%. The economic and market forecasts presented herein have been generated by Goldman Sachs Asset Management for informational purposes as of the date of this presentation. They are based on proprietary models and there can be no assurance that the forecasts will be achieved. Please see additional disclosures at the end of this presentation.

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GLOSSARY

Sustainability bonds are use-of-proceeds instruments, as defined by ICMA Sustainability Bond Guidelines). Sustainability-linked bonds are tied to an issuer's overall sustainability performance.

ABBREVIATIONS

US Federal Reserve (Fed), European Central Bank (ECB), Bank of England (BoE), Bank of Japan (BoJ), Swiss National Bank (SNB), Central Bank of Sweden (Riksbank), Reserve Bank of New Zealand (RBNZ), Central Bank of Norway (Norges Bank), Bank of Canada (BoC), Reserve Bank of Australia (RBA).

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