FIXED INCOME MUSINGS

MACRO AT A GLANCE

US Economy, Fed Response, and the US Dollar

In this edition of Musings, we highlight views from our recently published 2Q 2025 Fixed Income Outlook: Risk-Aware, Return-Ready. For the quarter ahead, we are focused on key market dynamics including: the outlook for the US economy, the Fed's reaction to a policy-induced downturn, the portfolio properties of the US dollar in a world of trade decoupling.

Tariffs and Their Effects on the US Economy

Assessing the precise economic impact of tariffs and their indirect effects through sentiment channels is incredibly complex due to the rapid pace of developments. The extent to which reciprocal tariffs will return after July 9 or whether retaliation will escalate remains uncertain. Qualitatively, we expect the tariffs to lead to higher inflation and lower growth in the US. Quantitatively, estimates suggest the tariffs will boost core PCE inflation by 1.7% to just under 4% and lower GDP by 0.9-2.6%. However, the confidence intervals around these estimates are wide, depending on retaliation and any use of tariff revenues to provide fiscal support to households and businesses.

Thinking Like the Fed

With trade policy changing rapidly, it will be challenging for Fed officials to incorporate the tariff shock into economic models. While incoming data will help us understand the US economy's starting point, the signal will be outdated relative to the new environment. Therefore, we expect the Fed will focus on engaging with businesses to understand their responses. Specifically, they will look at whether firms plan to negotiate with suppliers or pass on higher prices to consumers. If companies face limitations in exercising pricing power, they may absorb some of the increased input costs but aim to recover the impact on profit margins gradually through persistent price rises. This consideration is crucial for Fed officials as it will determine whether tariffs cause a one-time price level reset, or a sustained rise in inflation.

US Dollar – Diminished, Not Finished

Despite short-term weakness due to trade wars and policy uncertainty, the US dollar remains dominant in global trade and finance. We acknowledge that the US dollar's weakness may persist in the near term due to trade wars and policy uncertainty affecting US growth. Notably, the breadth of tariffs suggests the dollar may need to weaken to adjust supply chains if demand cannot be redirected quickly. However, we caution against extrapolating this trend to broad-based, sustained weakness, despite negative trends in US governance and institutions. It is unlikely that the US economy will weaken without impacting the global economy, making it hard to see a weaker dollar versus all other currencies. Moreover, policy shifts that reduce uncertainty could lead to resumed dollar appreciation.

NAVIGATING FIXED INCOME

Here's a snapshot of our latest investment views on Investment Grade Credit, High Yield Credit and Bank Loans, Securitized Credit, and Emerging Market Debt.

Investment Grade Credit

Despite the increase in volatility driven by US economic and policy uncertainty, we believe that investment grade credit will continue to demonstrate resilience compared to riskier asset classes such as US high yield and US equities. We are moderately underweight in multi-sector fixed income portfolios, while moderately overweight in single-sector fixed income portfolios as well as multi-sector fixed income portfolios that do not invest in high yield credit. Given the sound fundamentals, we may add exposure to high conviction views if risk premiums are attractive, while staying alert to risks from tariffs and slower growth.

High Yield Credit and Bank Loans

We are moderately positioned across US high yield (HY) credit, bank loans, and European high yield credit. The financial consequences of efforts to improve US government efficiency are challenging to predict precisely, as there is no historical precedent for such measures. However, we are aware of potential implications for the aerospace, defense, and healthcare sectors. For instance, lower Medicaid reimbursements could impact certain healthcare facilities. These considerations, combined with tariff headwinds, have led us to reduce our exposure to the healthcare and defense sectors in the US market, where we were already underweight. We continue to believe that our fundamentals-focused, active approach will enable us to identify opportunities while avoiding potential pockets of stress, especially in the context of the evolving tariff situation.

Securitized Credit

While tariffs present downside risks to growth, we expect the credit fundamentals for securitized sectors to remain resilient. Corporate and consumer balance sheets are healthy, and the labor market remains strong, with wages running slightly above historic levels. However, we are mindful of managing convexity risk and the impact of tariffs on consumer and corporate credit fundamentals. We are overweight securitized credit sectors but have rotated our exposures to higher quality assets. We remain overweight CLOs due to negative net supply and strong demand from both institutional and retail investors, which provide a positive technical backdrop.

Emerging Market Debt

We view EMD as an attractive source of income and alpha potential given high dispersion within the asset class. With valuations becoming more attractive and the expected easing of global financial conditions, EMD may outperform in the medium term for investors who can ride out near-term volatility. Given the US-centric nature of the current economic shock, EM credit can also provide valuable diversification benefits. Among EM sovereign bonds, we favor IG issuers that provide attractive income potential as well as BB-rated issuers, including those that we think are candidates for upgrade into the high yield market such as Morocco, Oman, Serbia, and Paraguay. We also expect large, domestically-oriented economies such as India and Brazil to prove resilient even as global trade slows.

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POLICY PICTURE: EUROPE

The euro area's near-term growth prospects are currently weak due to tariff headwinds. However, economic prospects are expected to improve from 2026 onwards as the region enhances its domestic defence capabilities and Germany undergoes a significant fiscal regime shift.

ECB: A Sixth Successive Cut

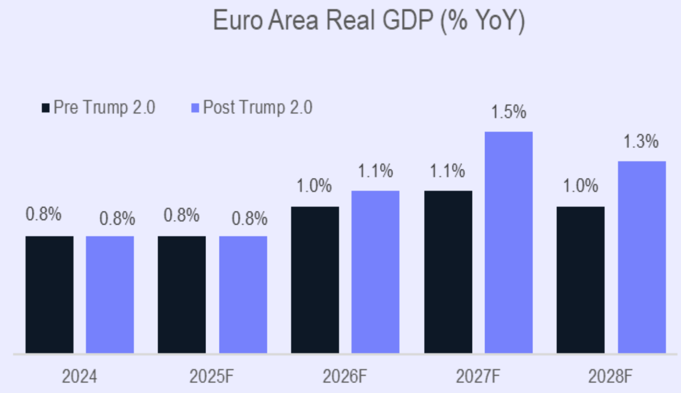
The European Central Bank cut its policy rate for the sixth successive time on April 17, delivering a further 25bps rate cut and taking its benchmark rate to 2.25%, in line with our expectations. ECB officials signalled rising concerns around growth due to global trade tensions, noted a "marked" decline in services inflation and stated that the impact of trade tensions on inflation was "less than clear" (a shift from prior communication). In general, the statement and press conference that followed the release struck a dovish tone.

The Governing Council removed its reference to policy restriction and kept its meeting-by-meeting and data-dependent approach. We expect near-term growth risks to reinforce disinflation and prompt the ECB to cut rates below 2%, despite improved growth prospects from 2026 onwards due to German fiscal and region-wide defence spending.

Policymakers Monitoring Downside Risks to Growth

The post-meeting ECB communication has mirrored rising concerns around growth, with Vice President de Guindos noting that downside risks to growth are "materialising." While President Lagarde repeated at the IMF Spring Meetings in Washington that the net impact of tariffs on inflation remains to be seen, she pointed to headline inflation of 2.1% in 2025 (vs 2.3% in the March projections) and French governor Villeroy argued that "inflation risks are currently on the decline".

European Growth Prospects Pre and Post Trump 2.0



Source: Goldman Sachs Global Investment Research as of April 02, 2025

What We're Watching

We are closely monitoring the progress of implementing German fiscal ambitions and the increase in defence spending region-wide. We are also mindful that the capacity for additional fiscal stimulus to offset the tariff shock may be limited, especially in high-debt, high-deficit economies like France and Italy, suggesting near-term risks to growth in the region are tilted to the downside. However, we continue to believe that the medium-term outlook in Europe looks brighter, which may yield attractive income opportunities across European credit markets over time.

ECB Speaker and Date	Comment
de Guindos, April 22, 2025	"Downside risks to growth are materializing. […] Policy transmission may be partly curbed by uncertainty."
Lagarde, April 22, 2025	"We don't see a recession in the euro area. […] We will either cut or pause [in June] but we will be data-dependant to the extreme."
Villeroy, April 22, 2025	"This inflation risk seems rather low. It is even quite likely that inflation risks are on the decline."

Source: ECB, Goldman Sachs Global Investment Research. As of April 23, 2025.
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CENTRAL BANK SNAPSHOT

	INTEREST RATE POLICY	BALANCE SHEET POLICY	OUTLOOK	OUR OUTLOOK RELATIVE TO MARKET-IMPLIED PRICING
Fed	**Federal funds rate**: 4.25-4.5% **Last change**: December and November 2024 (-25bps), September 2024 (-50bps) **Hiking cycle duration**: 17 months **Rate at the start of latest hiking cycle**: 0.25%	The Fed decided to slow the pace of QT at the March FOMC meeting, with plans to slow its pace of US Treasury runoff from $25bn a month to $5bn a month from April 2025, while the pace of reduction in its MBS holdings remained unchanged at $35bn.	We expect rate cuts to resume provided that second-round impacts of tariff inflation are avoided once negative impact on growth from tariff becomes clearer. **Expected rate at end-2025**: 3.75-4.0% **Neutral rate estimate**: 2.75-3.5%	Slightly hawkish
ECB	**Deposit facility rate**: 2.25% **Last change**: April (-25bps), March and January 2025 (-25bps) December, October, November and September 2024 (-25bps) **Hiking cycle duration**: 15 months **Rate at the start of the latest hiking cycle**: -0.5%	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.	We anticipate further rate reductions based on growth headwinds from US tariffs, if they are maintained. We do not expect the economic effects of German fiscal spending to be felt until 2026 and beyond. **Expected rate at end-2025**: 1.5% **Neutral rate estimate**: 2.0-2.25%	In line
BoE	**Bank Rate**: 4.5% **Last change**: February 2025 (-25bps), November and August 2024 (-25bps) **Hiking cycle duration**: 21 months **Rate at the start of the latest hiking cycle**: 0.1%	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 anticipate quarterly easing from the BoE with a rate cut in May. However, the pace of easing may accelerate due to tightening financial conditions and tariff-related headwinds to global growth. **Expected rate at end-2025**: 3.5% **Neutral rate estimate**: 2.5-3.5%	Slightly dovish
BoJ	**Policy deposit rate**: 0.5% **Last change**: January 2025 (+25bps), July 2024 (+15bps), March 2024 (+20bps) **Duration of negative rates**: 98 months **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 will initially concentrate on intermediate maturity bonds.	We anticipate ongoing policy normalization in 2025 as robust data and inflationary pressures remain, provided the global economy does not enter a recession. **Expected rate at end-2025**: 0.75% **Neutral rate estimate**: 1.0-1.5%	Hawkish

Source: Goldman Sachs Asset Management. As of April 24, 2025. Abbreviations: Pandemic Emergency Purchase Program (PEPP). 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. 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.

SOVEREIGN BOND YIELDS (%)

	Latest (%)	Year-to-date Change (bps)	1-Year Change (bps)	Last 10-year Percentile
US 2 Year	3.8	-44	-116	75
US 10 Year	4.4	-18	-22	94
US 2-10 Slope	0.6	26	94	59
US Treasury 10-Year Inflation-Protected	2.1	-13	-10	95
Germany 2 Year	1.8	-33	-122	75
Germany 10 Year	2.5	14	1	93
Japanese 10 Year	1.3	25	48	98
UK 10 Year	4.6	1	36	97
Chinese 10 Year	1.7	-1	-58	2

Source: Macrobond, Goldman Sachs Asset Management. Based on data available as of 24 April 2025.

EXCHANGE RATES

	Latest	Year-to-date Change (%)	1-year Change (%)
Euro (€ per $)	0.88	-8.3	-6.2
British Pound (£ per $)	0.75	-5.5	-7.1
Japanese Yen (¥ per $)	142.65	-9.1	-7.8
Chinese Yuan Renminbi (CNY per $)	7.31	0.2	0.9

Source: Macrobond, Goldman Sachs Asset Management. Based on data available as of 24 April 2025.

FIXED INCOME SECTOR YIELDS (%)

	Latest (%)	Last 10 year average (%)	Year-to-date change (bps)	Last 10 year Percentile
US Investment Grade	5.4	3.8	1	86
European Investment Grade	3.1	1.7	-8	74
UK Investment Grade	5.5	3.4	1	86
US High Yield	7.9	6.7	46	77
European High Yield	5.8	4.5	32	74
EM External	8.0	6.4	12	79
EM Corporate	6.6	5.4	17	82
US Agency MBS	5.2	3.1	-5	95
US ABS	5.1	3.1	2	79
US Munis	4.3	2.5	54	98
US CMBS	5.1	3.3	-20	77

Source: Macrobond, Goldman Sachs Asset Management, ICE BofAML and J.P. Morgan. Based on data available as of 24 April 2025.

FIXED INCOME SECTOR SPREADS (BASIS POINTS)

	Latest (bps)	Last 10 year average (bps)	Year-to-date change (bps)	Last 10 Year Percentile
US Investment Grade	108	126	26	31
European Investment Grade	105	123	4	30
UK Investment Grade	117	147	26	21
US High Yield	375	429	83	40
European High Yield	358	399	47	41
EM External	8	6	0	42
EM Corporate	258	328	32	10
US Agency MBS	57	38	15	83
US ABS	111	97	30	74
US CMBS	109	97	14	62

Source: Macrobond, Goldman Sachs Asset Management, ICE BofAML and J.P. Morgan. Based on data available as of 24 April 2025.

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INSIGHT HIGHLIGHTS

[Fixed Income Musings]

Weekly Insight

[Fixed Income Outlook 2Q 2025]

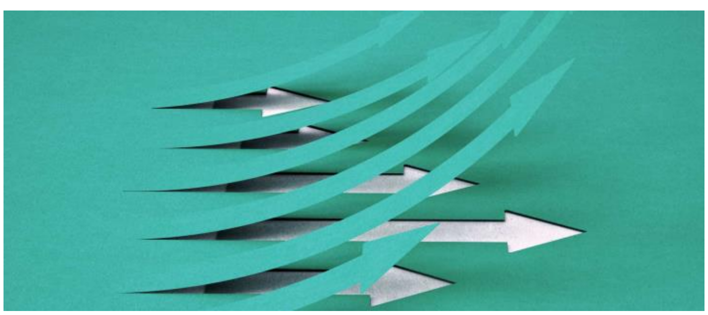
April 23, 2025

[CIO Digest: What's on the Minds of Our CIOs?]

April 10, 2025

[Market Brief: Taking Stock of the Tariff Shock]

April 3, 2025



[Market Brief: Level Setting on the Forces Shaping Markets]

March 14, 2025

[Income Generation: Seeking Steady Streams in Unstable Times]

March 7, 2025

Risk Consideration

Investments in fixed income securities are subject to the risks associated with debt securities generally, including credit, liquidity, interest rate, prepayment and extension risk. Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can result in the decline in the bond's price. The value of securities with variable and floating interest rates are generally less sensitive to interest rate changes than securities with fixed interest rates. Variable and floating rate securities may decline in value if interest rates do not move as expected. Conversely, variable and floating rate securities will not generally rise in value if market interest rates decline. Credit risk is the risk that an issuer will default on payments of interest and principal. Credit risk is higher when investing in high yield bonds, also known as junk bonds. Prepayment risk is the risk that the issuer of a security may pay off principal more quickly than originally anticipated. Extension risk is the risk that the issuer of a security may pay off principal more slowly than originally anticipated. All fixed income investments may be worth less than their original cost upon redemption or maturity.

The risk of foreign currency exchange rate fluctuations may cause the value of securities denominated in such foreign currency to decline in value. Currency exchange rates may fluctuate significantly over short periods of time. These risks may be more pronounced for investments in securities of issuers located in, or otherwise economically tied to, emerging countries. If applicable, investment techniques used to attempt to reduce the risk of currency movements (hedging), may not be effective. Hedging also involves additional risks associated with derivatives.

Emerging markets investments may be less liquid and are subject to greater risk than developed market investments as a result of, but not limited to, the following: inadequate regulations, volatile securities markets, adverse exchange rates, and social, political, military, regulatory, economic or environmental developments, or natural disasters.

Collateralized loan obligations ("CLOs") involve many of the risks associated with debt securities, including interest rate risk, credit risk, default risk, and liquidity risk. The risks of an investment in a CLO also depend largely on the quality and type of the collateral and the class or "tranche" of the CLO. There is the possibility that the strategy may invest in CLOs that are subordinate to other classes. CLOs also can be difficult to value and may be highly leveraged (which could make them highly volatile). The use of CLOs may result in losses.

When interest rates increase, fixed income securities will generally decline in value. Fluctuations in interest rates may also affect the yield and liquidity of fixed income securities.

International securities may be more volatile and less liquid and are subject to the risks of adverse economic or political developments. International securities are subject to greater risk of loss as a result of, but not limited to, the following: inadequate regulations, volatile securities markets, adverse exchange rates, and social, political, military, regulatory, economic or environmental developments, or natural disasters.

High-yield, lower-rated securities involve greater price volatility and present greater credit risks than higher-rated fixed income securities.

Mortgage-related and other asset-backed securities are subject to credit/default, interest rate and certain additional risks, including extension risk (i.e., in periods of rising interest rates, issuers may pay principal later than expected) and prepayment risk (i.e., in periods of declining interest rates, issuers may pay principal more quickly than expected, causing the strategy to reinvest proceeds at lower prevailing interest rates).

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Sector Spread Indexes

US Investment Grade Corporates: ICE BofAML US Corporate Index

US High Yield Corporates: ICE BofAML US Corporate High Yield Index

European Investment Grade Corporates: ICE BofAML Euro Corporate Index

European High Yield Corporates: ICE BofAML Euro High Yield Index

US Municipals: ICE BofAML Municipal Securities Index

ABS: ICE BofAML US Fixed Rate Asset-Backed Securities Index

MBS: ICE BofAML US Agency Mortgage-Backed Securities Index

CMBS: ICE BofAML Fixed Rate AAA Rated CMBS Index

EM External Debt: J.P. Morgan, EMBI Global Diversified Face Constrained Index

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), Quantitative Easing (QE), Quantitative Tightening (QT), Pandemic Emergency Purchase Program (PEPP), Consumer price index (CPI), producer price index (PPI), developed markets (DM), emerging markets (EM), Japanese Government Bond (JGB). Mortgage-backed securities (MBS), Asset-backed securities (ABS).