July 2024

BlackRock

Fixed Income Strategy Macro Deck

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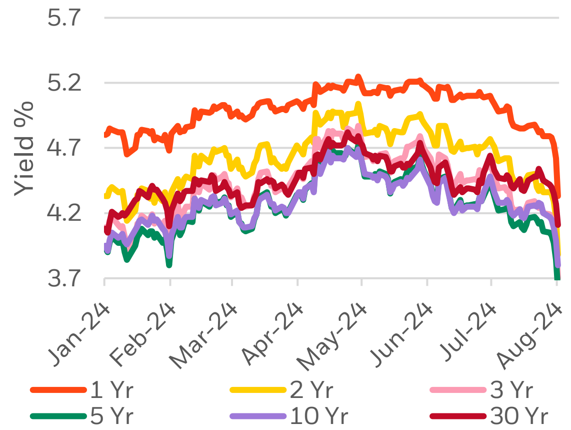
Table of contents

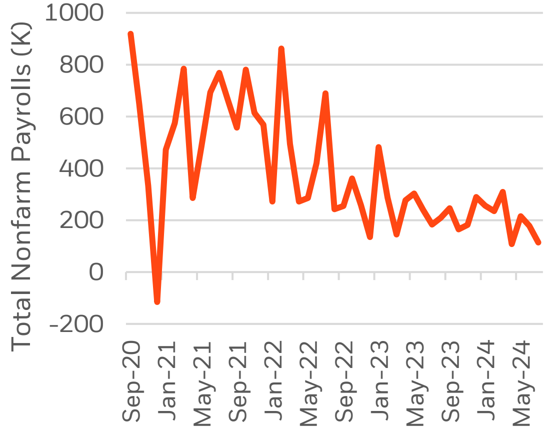
July 2024: Ushering in August with Escalating Volatility

Rates steadily rallied with declining inflation, but plunged post non-farm payrolls (NFP)



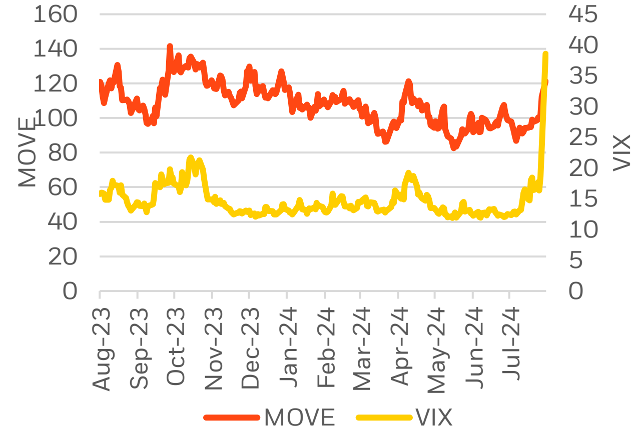
Source: The US Treasury as of August 2, 2024.

Below consensus July NFP following a somewhat dovish FOMC sparked recession concerns



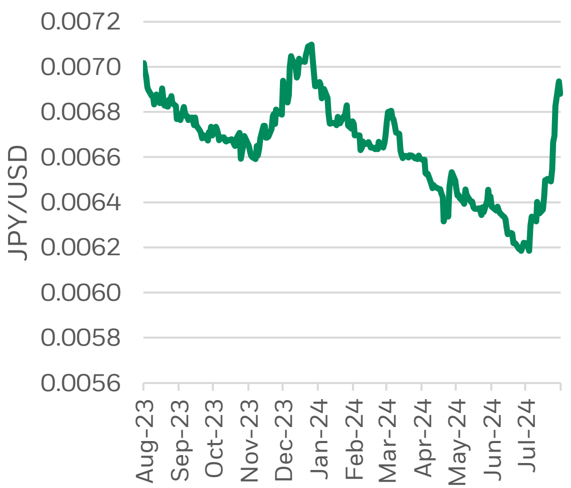
Source: BEA. Data as of August 2, 2024. NFP= Nonfarm Payrolls.

Interest rate (MOVE) and equity (VIX) volatility spiked, with VIX reaching highs since 2020



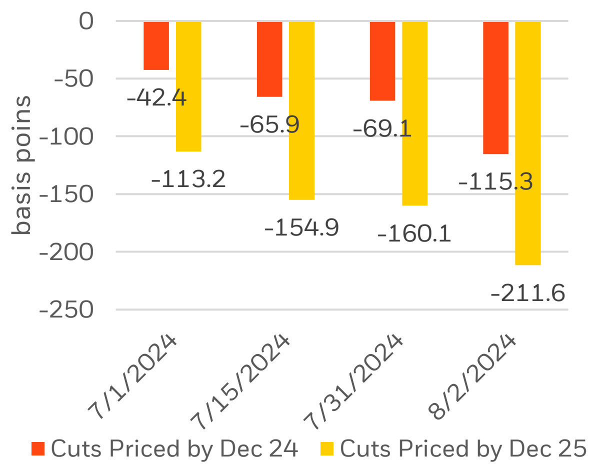
Source: Bloomberg as of August 5, 2024.

The JPY appreciated against USD as investors unwound carry trades as BOJ raised rates



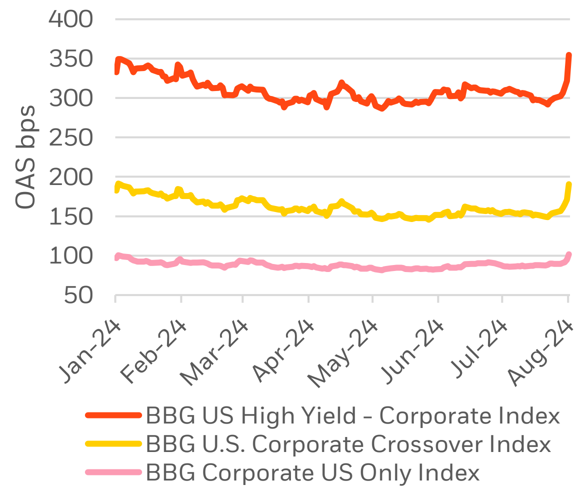
Source: Bloomberg. Data as of August 6, 2024.

Worries of a hard landing caused markets to aggressively price in monetary policy easing



Source: Bloomberg as of August 2, 2024.

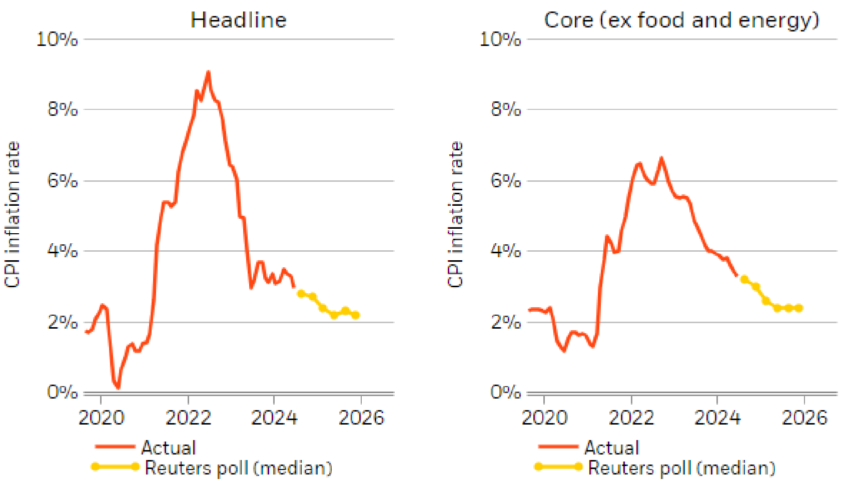
Following months of spread stability, credit spreads widened in tandem with a sell-off in equities



Source: Bloomberg. Data as of August 2, 2024.

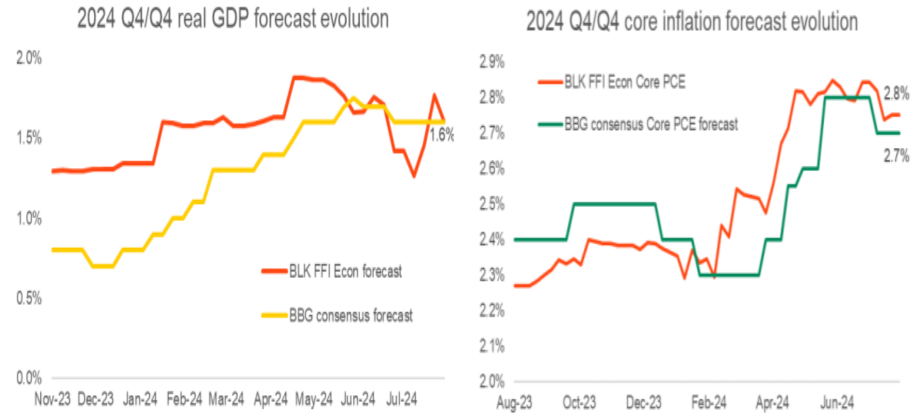
US Macro Overview

Core inflation has made significant improvement on the back of moderating services inflation



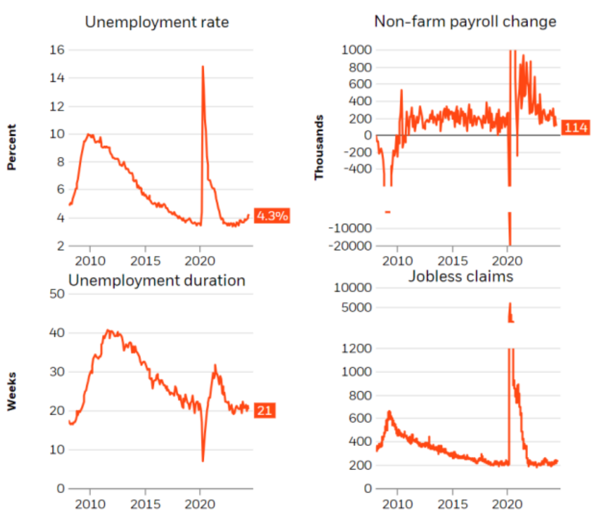
Source: Bureau of Labor Statistics and Haver Analytics, Charts by BlackRock as of August 7th, 2024

We expect real GDP to print below historical trend level by YE 2024 and core inflation to be above Fed's 2% target



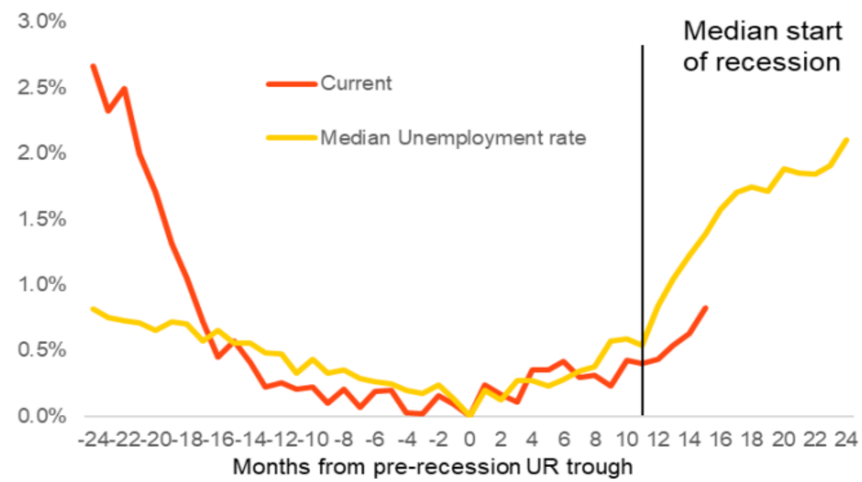
Source: Bloomberg as of August 6th, 2024

The US labor market is beginning to show signs of softening



Source: Bureau of Labor Statistics and Haver Analytics, Chart by BlackRock as of August 6th,, 2024

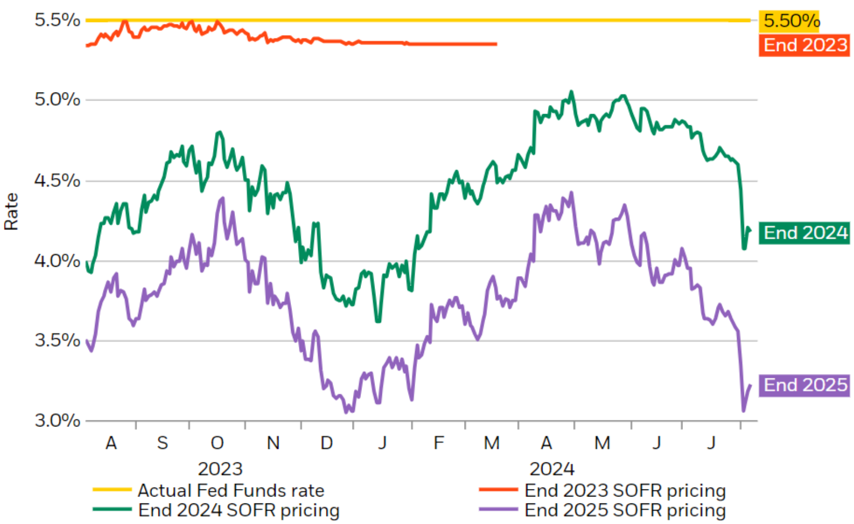
The unemployment rate has followed a more gradual path relative to historical median, but recent uptick is notable



Source: Bloomberg as of August 6th, 2024

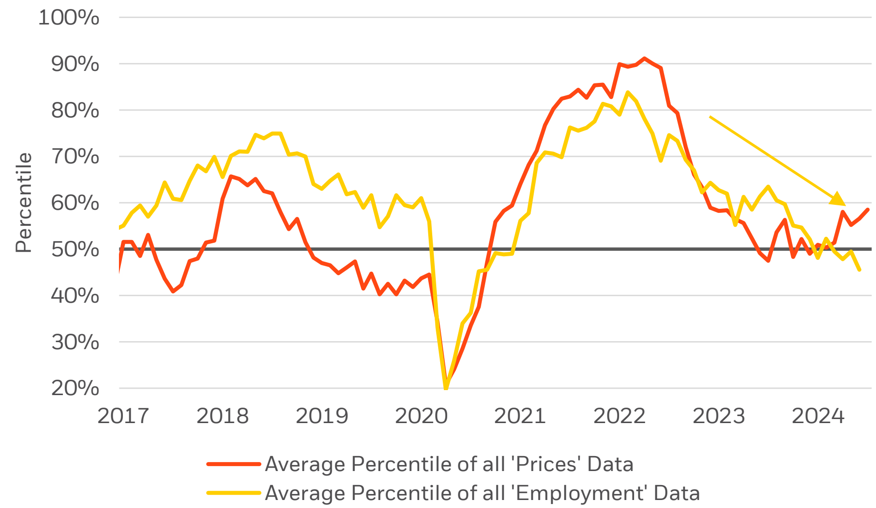
Fed and US Rates Overview

The market has increased the probability of a hard landing and raised the Fed cut to around four by end of 2024



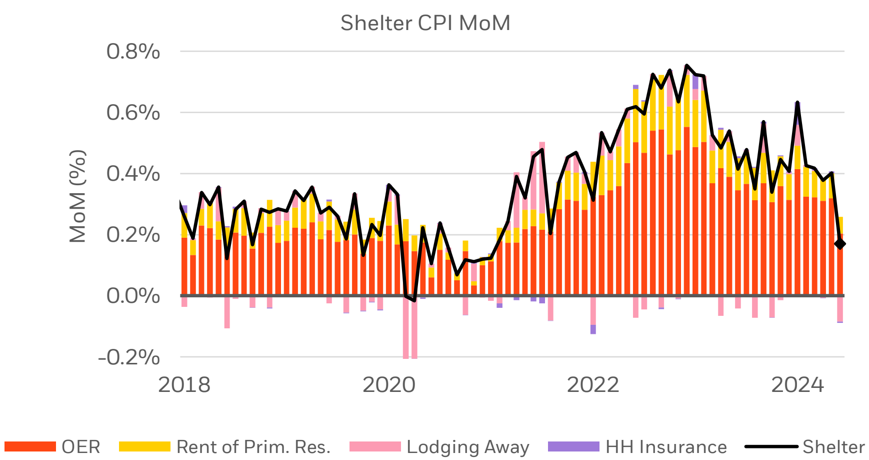
Source: Bloomberg as of August 7th, 2024

With inflation in a better place, the labor market is likely to capture more of the market attention as a downside risk factor



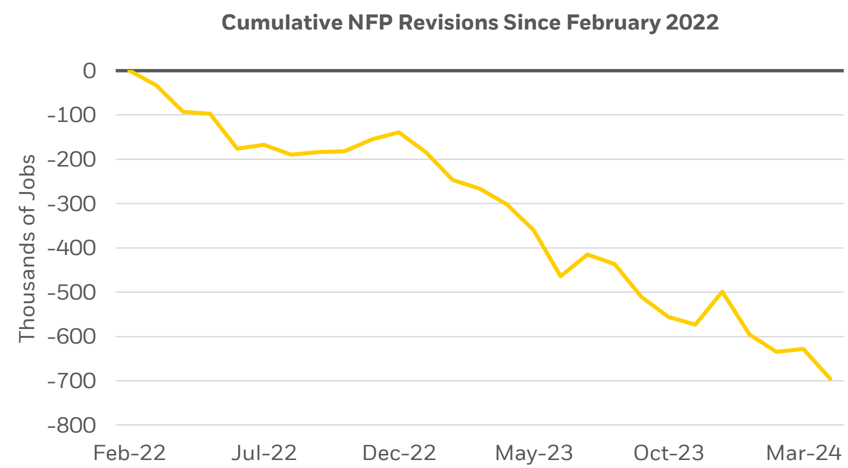
Source: Bloomberg, as of July 31stt, 2024

Compelling signs that June shelter slowdown is just the beginning



Source: Bloomberg as of July 31st, 2024

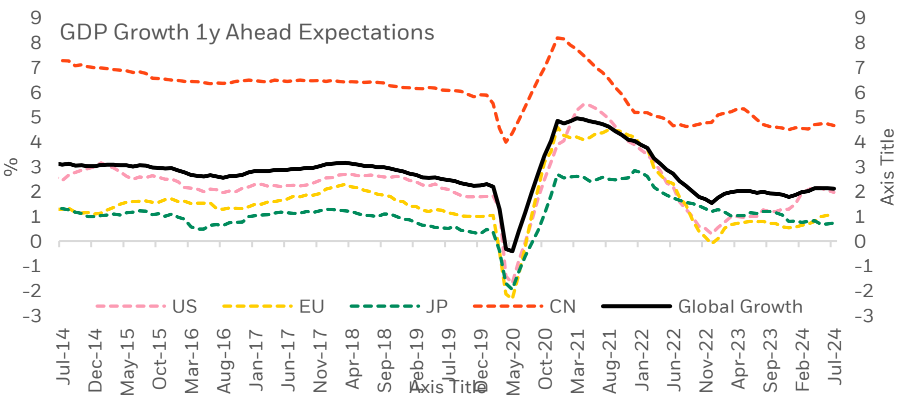
There are inkling of a labor market slowdown with 700,000 jobs being 'revised down' since Feb 2022



Source: Bloomberg, as of August 6th, 2024

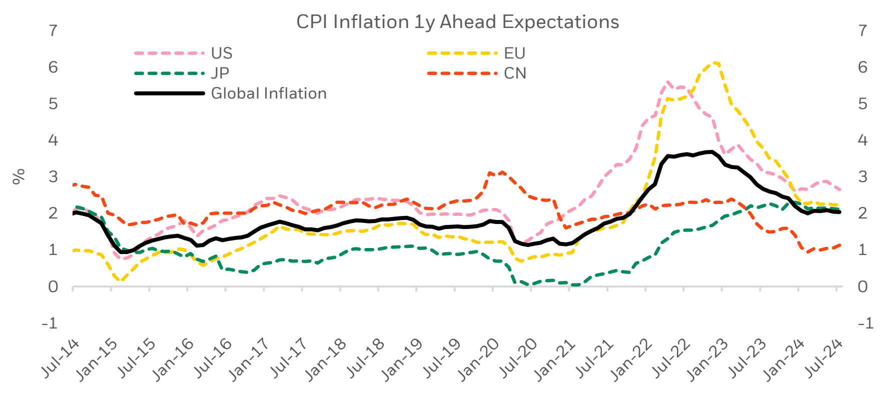
Global Macro Backdrop

GDP Growth: US and China growth expectations weaken as Japan and EU improve



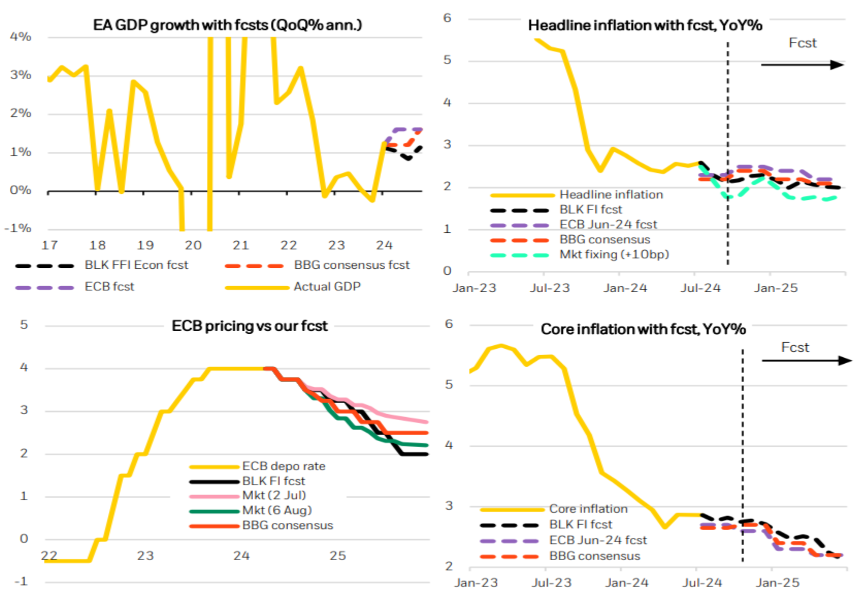
Source: Bloomberg as of July 31st, 2024

CPI Inflation: Disinflationary trend returns across major economies, Japan above 2%



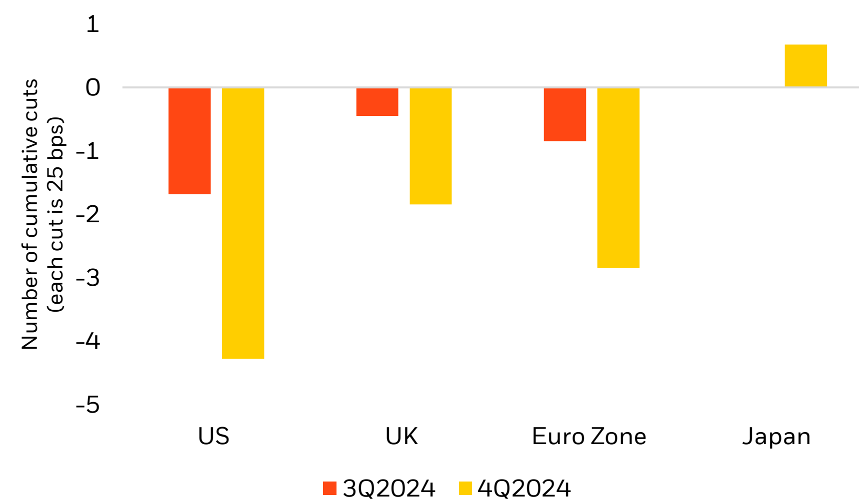
Source: Bloomberg as of July 31st, 2024

Along with the moderate growth, inflation is expected to decline to 2% by early 2025, prompting the ECB to cut rates to 2% by end 2025



Source: Bloomberg, as of July 31st,, 2024

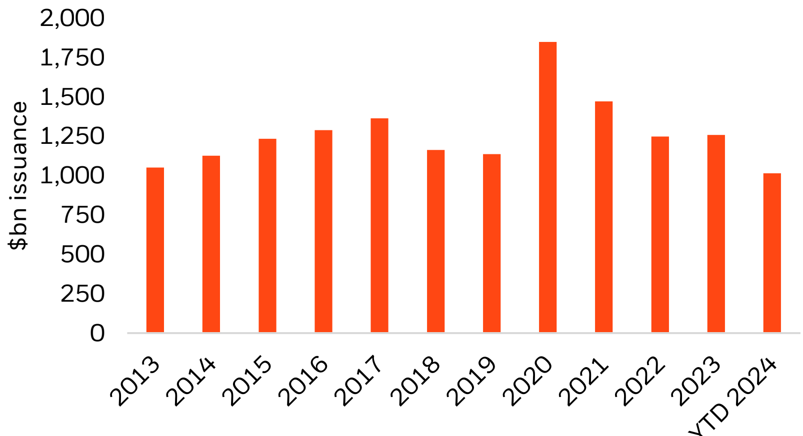
The market's expectation of DM central banks' rate policy has materially shifted over the year



Source: Bloomberg, as of August 8th, 2024

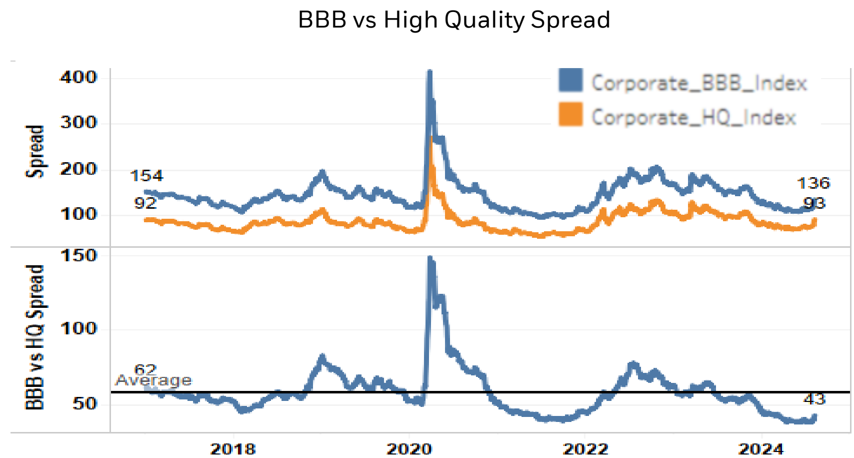
Global Investment Grade Credit

US IG supply remained strong over July bringing total issuance to north of $1 trillion for the year at its fastest pace since 2020



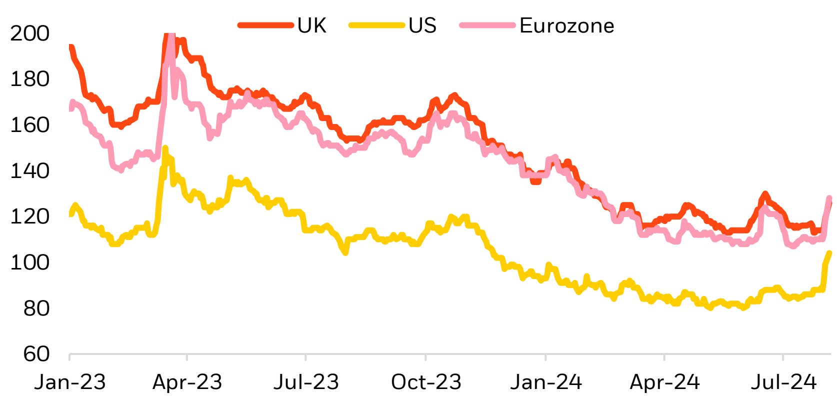
Source: SIFMA. Data as of July 31, 2024.

Amidst broader market volatility, BBB-rated and high-quality IG credit are at its tightest spreads since 2022



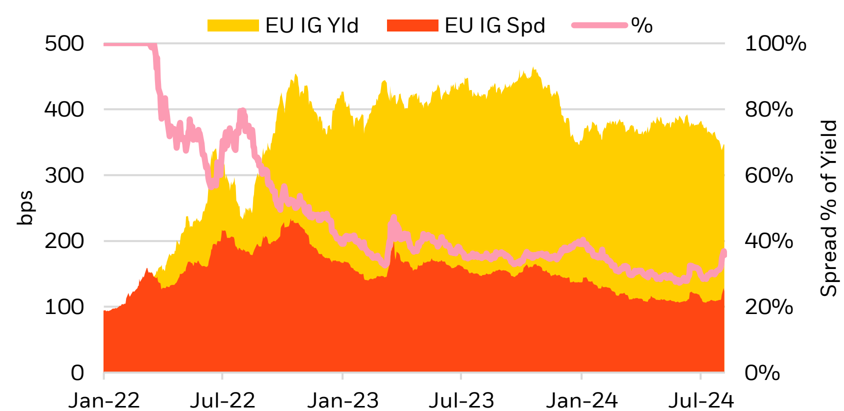
Source: BlackRock. Data as of August 6, 2024.

US credit spreads compressed in July but widened early August after a weaker jobs report prompted a rates sell-off



Source: BlackRock . Data as of August 6, 2024.

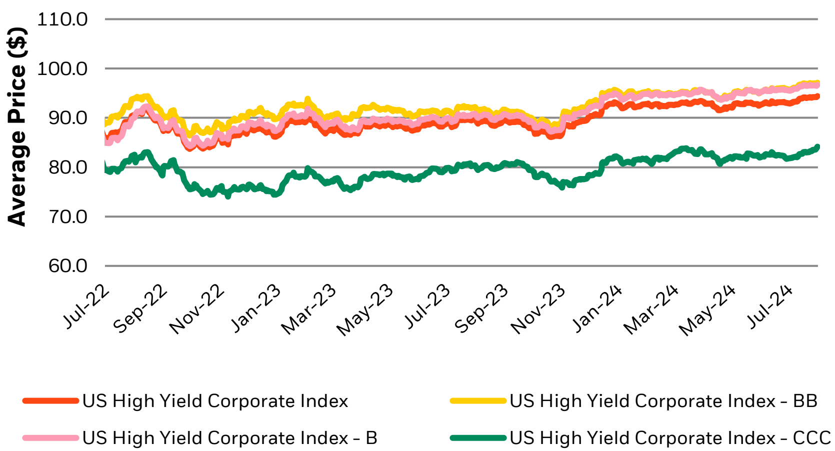
Woth the recent widening in spreads, European credit all-in-yields have corrected meaningfully



Source:: Bloomberg, BlackRock. Data as of August 6, 2024.

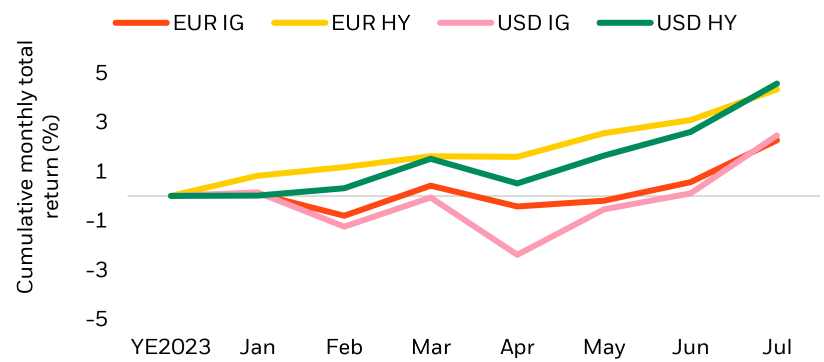
High Yield (HY) Credit

The HY Index was up +1.9%, led by the outperformance of CCCs against BBs and Bs



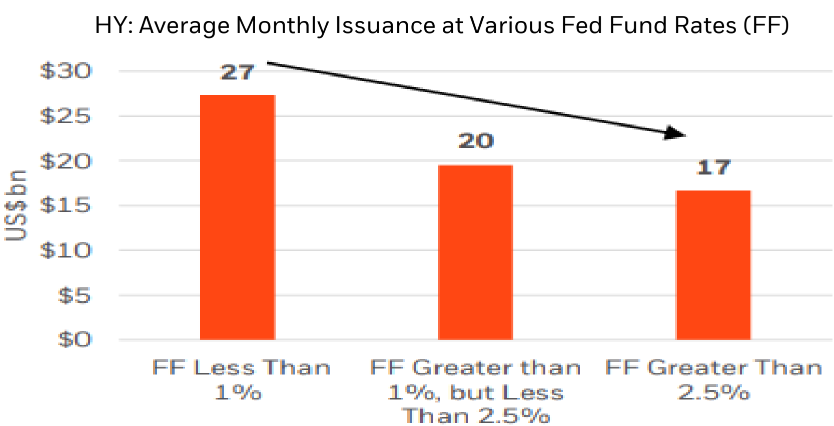
Source: Barclays Live. Data as of July 31, 2024. **Past performance is not indicative of future results.**

Despite cooling economies in the US and Eurozone, High Yield continued to outperform IG



Source: Bloomberg, ICE –BofA, BlackRock. Data as of July 31, 2024. **The figures shown relate to past performance. Past performance is not a reliable indicator of current or future results.** Index performance returns do not reflect any management fees, transaction costs or expenses. Indices are unmanaged and one cannot invest directly in an index.

Given higher financing rates, US HY issuers have reduced their overall supply and debt growth….



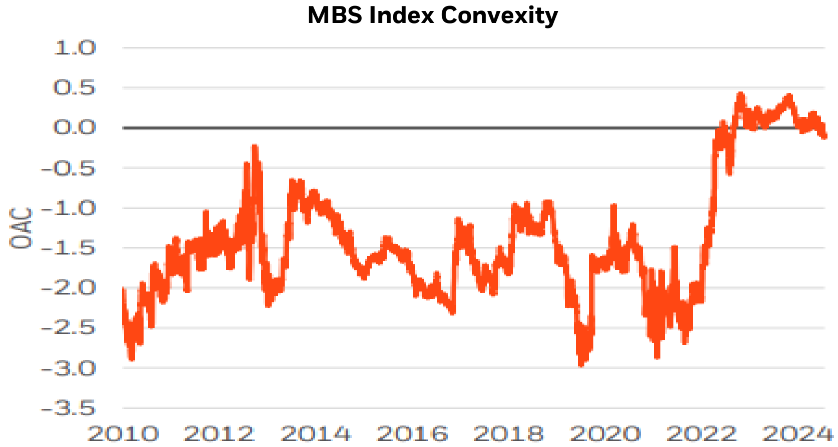
Source: BlackRock . Data as of June 30, 2024.

…consequently, there is a higher quality mix of HY than in the past, with BBs making up ~50% of the market

Source: Morgan Stanley. Data as of June 28, 2024.

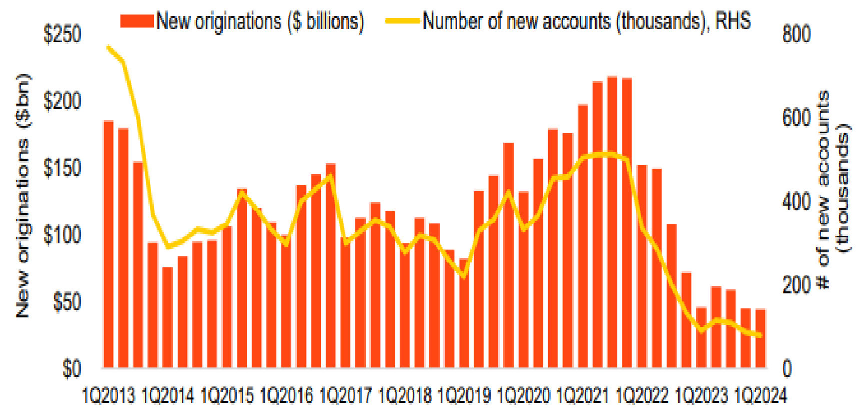
Agency MBS

MBS currently has a muted convexity profile, providing potential opportunity to perform better than credit in a growth slowdown



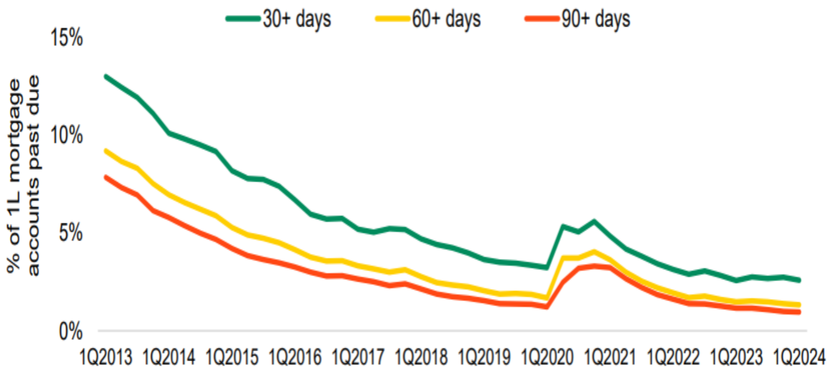
Source: Bloomberg. Data as of July 19, 2024

Mortgage originations have reached their lowest levels in over a decade as rates have risen past their post-GFC lows



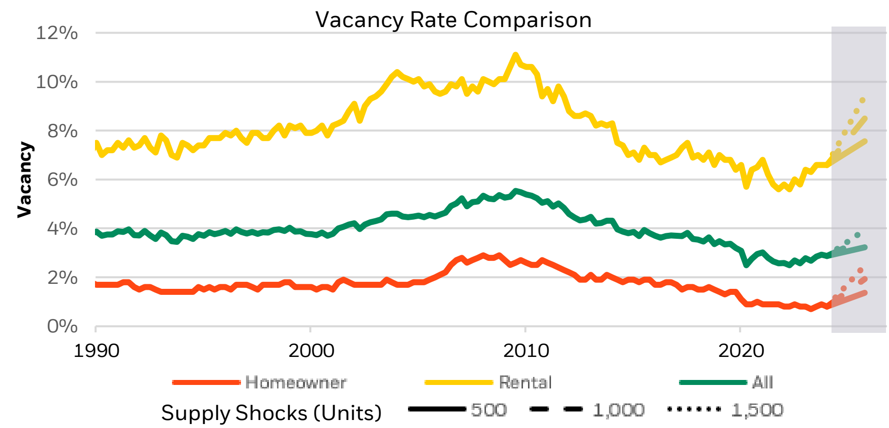
Source: Federal Reserve Y-14M Data, Federal Reserve Bank of Philadelphia, BlackRock. Data as of Q1 2024, March 31, 2024.

Mortgage delinquency rates remain near record lows supported by strong home price appreciation and a resilient US consumer



Source: Federal Reserve Y-14M Data, Federal Reserve Bank of Philadelphia, BlackRock. Data as of Q1 2024, March 31, 2024. Note: 1L stands for first lien mortgage account

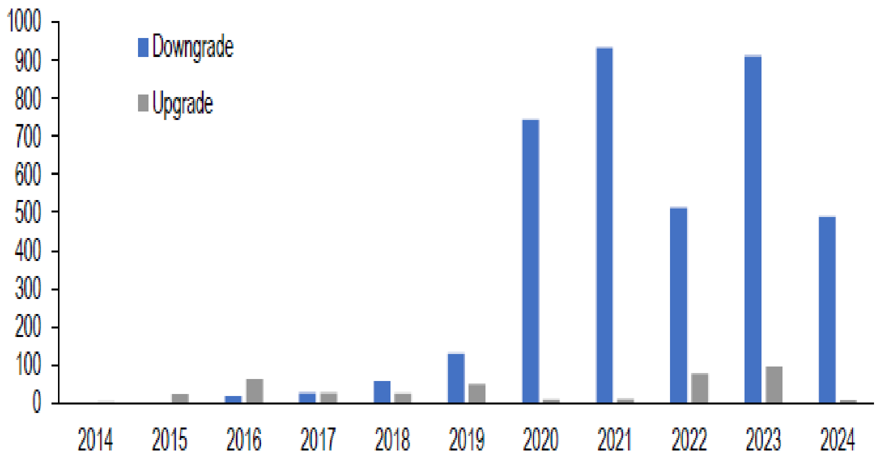
Though housing starts and completions have risen, the supply will likely not be able to help address the historic housing shortage



Source: U.S. Census Bureau as of 06/30/2024. Grey shaded area highlights hypothetical scenarios.

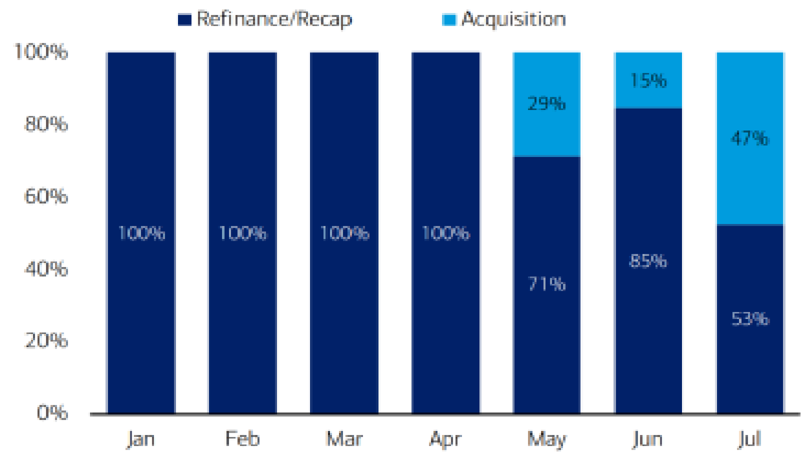
Securitized Assets

Downgrades in conduit CMBS has continued due to structural challenges in the office space and high rates



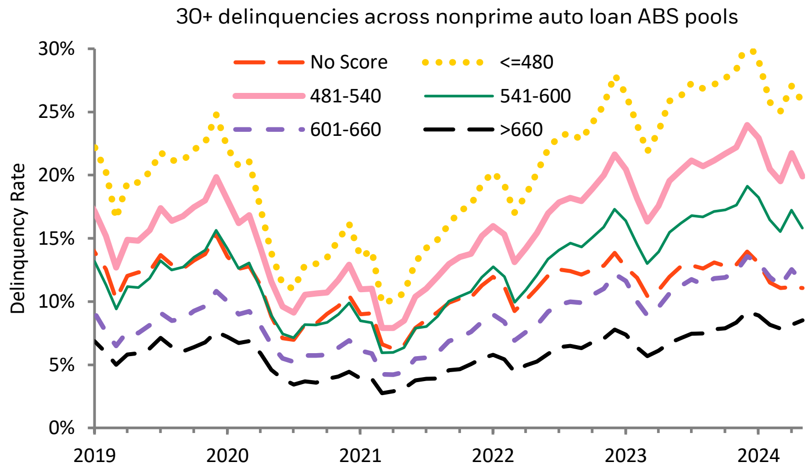
Source: JP Morgan, Bloomberg Finance. Data as of July 26, 2024.

Elevated SASB new issuance is due to a pick up in acquisitions, while the prospect of lower rates could boost overall origination



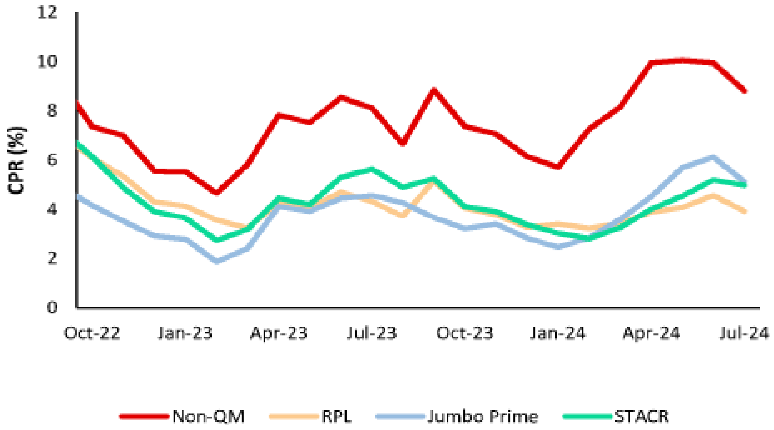
Source: BofA Global Research. July 31, 2024.

Within ABS, lower credit borrowers saw more notable deterioration versus high quality borrowers



Source: JP Morgan, ABS-EE via 1010data as of 7/8/24.

A moderation in prepayments across Non-Agency RMBS could be explained by higher rates, which are expected to reverse upon a rally



Source: Nomura. Data as of July 31, 2024.

Fixed Income sector views

August 2024

Sector views

U.S. Rates

Market movement over the month of July was widely driven by anticipation of the Federal Open Markets Committee (FOMC) meeting which took place over the last two days of the month. As expected, the FOMC maintained its target policy rate at 5.25 – 5.5% at its July meeting. While the Committee suggested that an initial rate cut is on the table for September, its statement fell short of providing direct guidance for a future cutting cycle as members continue their data dependent posture in all rate decisions. Noticeably, the FOMC's statement turned attention to both the labor market and inflation, as Powell noted the Fed is continuing to monitor both deflationary pressures and labor market stability.

Bearish **Bullish**

Global Inflation Linkers

We like TIPS on a relative value basis against nominal treasuries. Recent inflation prints have established a deceleration trend, and we believe it will continue to moderate over the next several months with shelter inflation leading the way. We believe there are pockets of opportunity in the intermediate portion of the curve to be long inflation expectations (breakevens). Wage growth may moderate further but consumer spending remains above trend as consumers dip further into their pandemic savings and use credit to support their consumption. We see core CPI remaining above the Fed's 2% target over 2024.

Bearish **Bullish**

Global Rates

The European Central Bank (ECB) held rates at 3.75%, describing upcoming data prints as supportive of its prior medium-term outlook. The incoming September decision was still seen as "wide open", with a few dovish tweaks that increased confidence in continued rate cuts. Over the month, UK yields continued to trend lower with a steepening bias, as 2-year yields fell 9bps more than the 10-year, and 16bps more than the 30-year. The Bank of England cut its benchmark rate by 25bps to 5.0%, a decision that followed an expansionary Purchasing Managers Index reading for the UK for the month of July. JGB yields rose in the front end, with the yield curve twist flattening. JGB 10y ended the month 0.015% higher at 1.055%. The Bank of Japan, contrary to widespread expectations, decided to raise the policy rate to 0.25% at the end-of-month policy meeting.

Bearish **Bullish**

US Agency MBS

The Bloomberg MBS Index outperformed similar duration Treasuries by 42bp in June, bringing year-to-date excess performance to 22bp. June's CPI data released on 7/11 showed signs of continued cooling in the economy; the long-awaited moderation in shelter inflation increased investor confidence that the Fed would move the overnight rate lower in H2. This dovish development put downward pressure on implied rate vol, which in turn benefitted MBS performance vs. Treasury hedges. The 30yr MBS par coupon tightened 8bps to 129bps over Treasuries and the Option Adjusted Spread of the Bloomberg MBS Index finished 7bps tighter at 38bps.

Bearish **Bullish**

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IG Corporates

In contrast to the events of June, where a dip in Treasury yields led to a widening of IG corporate spreads, July saw a relative stability in spreads despite a significant rally in the Treasury market. Within the spectrum of ratings, the outperformance of AA bonds could suggest a shift in investor sentiment towards favoring quality, likely influenced by the emergence of softer economic indicators.. Against this backdrop, the US Investment Grade Credit Index was unchanged in July, resulting a monthly excess return of 7bps.

Bearish Bullish

Municipals

Municipal bonds maintained their summer strength and posted a second-consecutive month of positive performance in July. Falling interest rates provided leadership as continued weakening of economic data and an increasingly dovish tone from the Federal Reserve solidified expectations for a September rate cut. However, rich valuations amid a persistent onslaught of issuance acted as a drag and prompted underperformance versus comparable Treasuries. We believe that some near-term caution is warranted, especially given the magnitude of the recent rally in interest rates and corresponding boost to performance.

Bearish Bullish

HY Corporates

In July, the High Yield Index produced total returns of +1.94%. Lower-quality bonds outperformed. We see more room for downside but think the market should remain relatively well supported in the intermediate to long-term given the strong fundamental backdrop and attractiveness of yields near current levels. We believe that going forward, as economic uncertainty persists and growth slows, dispersion in High Yield will increase and provide opportunity for increased alpha generation through strong credit selection rather than owning generic risk at all levels.

Bearish Bullish

Emerging Markets

July was a positive month for Emerging Markets Debt. The asset class was supported by a fall in US Treasury yields as US data pointed to a slowing in hiring and a steady uptrend in unemployment which, combined, kept the Fed on track for a rate cut in September. That said, the fundamental backdrop for EM remains mixed given how resilient the global economy has been to monetary adjustment and technicals continue to be supportive given a net negative supply and extreme levels of cash on the sidelines. We hold a cautiously convicted long position while remaining closer to home in spreads within both sovereigns and corporates as well as FX.

Bearish Bullish

Securitized Assets

We continue to be selective across the securitized asset complex, focusing on higher quality assets with strong levels of protection. Within CMBS, we favor multi-family up the capital stack, as well as high quality industrials. In addition, we hold a decent allocation to CLOs, particularly at the top of the capital structure, while being cautious in Non-Agency RMBS given weaker market tone.

Bearish Bullish

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Important Notes Cont'd

Index
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