

# FIXED INCOME MUSINGS

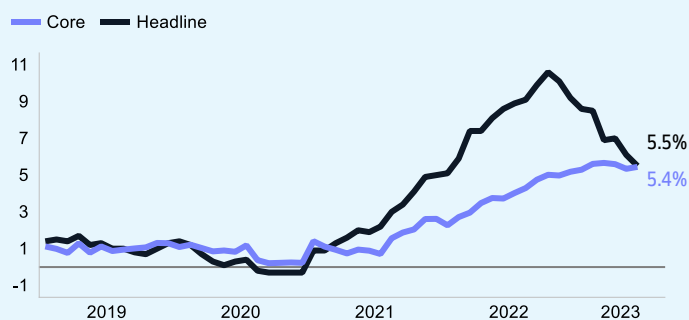
## MACRO AT A GLANCE

**Mixed disinflation progress in the Euro area.** Slowing energy and food prices continued to temper annual headline inflation (see Chart). Notably, annual headline inflation in Spain fell below the ECB’s 2% target for the first time since April 2021. That said, core inflation climbed higher, largely due to strength in core services, a development we expect to extend the ECB’s hiking cycle.

**US housing data support the soft landing narrative.** The Case-Shiller national home price index increased by the fastest rate since May 2022 while new home sales surprised sharply to the upside, rising 12.2% on the month. A turnaround in the housing market before the Fed’s hiking cycle has ended is supportive of a soft landing scenario, though it also likely reflects structurally low housing supply and may present hawkish implications for monetary policy.

### Euro area headline inflation eased further in June

Annual Euro area inflation (%)



Source: Goldman Sachs Asset Management, Macrobond. As of June 2023.

## POLICY PICTURE

Officials struck a hawkish tone at the ECB’s Forum on Central Banking in Sintra, Portugal:

- **Fed** – Elevated inflation and a tight labor market led Chair Powell to suggest hiking rates “at consecutive meetings is not off the table.” We expect the Fed to deliver a final 25bps hike in July but acknowledge risks are skewed towards further tightening.
- **ECB** – The central bank suggested rates will remain elevated “for as long as necessary” given second-round inflation effects and elevated wage growth. We have raised our terminal rate projection from 3.75% to 4.0%.
- **BoE** – Governor Bailey hinted interest rates could remain higher for longer than market-implied terminal rate pricing, posing upside risks to our terminal rate forecast.

### Higher-for-longer policy rates

	Latest hike (basis point)	Expected hike at next meeting (basis point)	Current policy rate (%)	Expected terminal rate (%)
<b>Fed</b>	-	25	5.0-5.25	5.25-5.5
<b>ECB</b>	25	25	3.5	4.0
<b>BoE</b>	50	25	5.0	5.5

Source: Goldman Sachs Asset Management, Macrobond. As of June 30, 2023. Based on forecasts from our economists.

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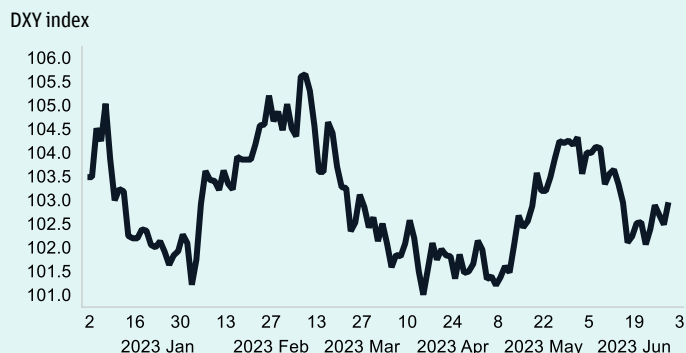
## NAVIGATING FIXED INCOME

**US dollar maintains upward trajectory.** The outperformance of US economic data compared to its peers have supported the dollar (see Chart). We maintain our overweight position on the US dollar (USD) but note a risk-on sentiment tends to weigh on it's appeal as a perceived safe-haven asset.

**Mutiny in Russia met with a muted market response.**

Political volatility has the potential to generate market turbulence and short-term fluctuations in asset prices. While swift de-escalation of the Wagner uprising – combined with no impact to oil production – resulted in a muted response by global financial markets to last weekend's events in Russia, significant uncertainty remains. Another key development this past week was resumed settlement of certain Russian bonds by Euroclear, reversing a suspension that had been in place since November 2022.

### USD moves higher on higher for longer rate expectations



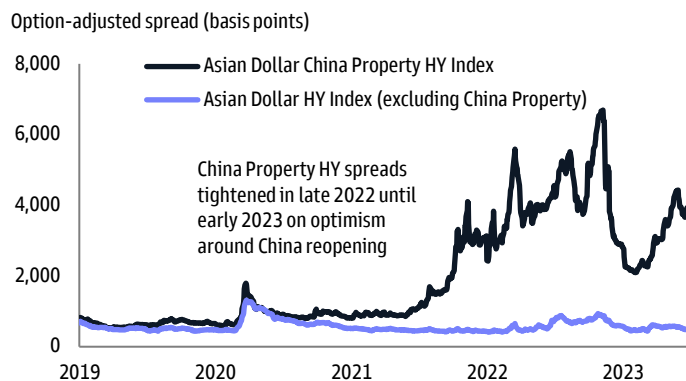
Source: Goldman Sachs Asset Management, Macrobond. As of June 29, 2023. The DXY index is a benchmark for the international value of the US dollar, tracking moves in the value of the US dollar relative to a basket of other currencies.

## CREDIT CHECK-IN

We expect default activity in Asia high yield (HY)—beyond the structurally challenged China HY property sector—to remain contained, similar to our outlook for [US](#) and [European](#) HY markets.

**Asia HY credit – still a tale of two.** Performance in Asia HY credit beyond the China property sector has been relatively resilient year-to-date. We expect downgrade and default activity beyond the China HY property sector (which is in the process of a multi-year adjustment) will remain contained. We see scope for selective policy easing in China considering recent weakness in activity. We expect policy stimulus in response to recent activity to be moderate, though any support delivered has potential to help stabilise the property sector. Overall, we continue to see investment potential in Asia HY credit beyond the China property sector, for example, among Indian issuers that are well positioned for the country's decarbonisation efforts.

### Asia HY credit – resilient beyond China property



Source: Goldman Sachs Global Investment Research, ICE-BAML. As of June 29, 2023.

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## CENTRAL BANK SNAPSHOT

	Interest Rate Policy	Balance Sheet Policy	Outlook	Our outlook relative to market-implied pricing
<b>Fed</b>	<p><b>Federal funds rate: 5.0-5.25%</b></p> <p>Prior changes: May, March, February 2023 (+25bps) December 2022 (+50bps) June, July, September and November 2022 (+75bps) May 2022 (+50bps) March 2022 (+25bps)</p>	<p>The monthly pace of net asset purchases was reduced from November 2021 and ended in March 2022. Since June 2022, the Fed has engaged in balance sheet runoff.</p>	<p>We expect another hike in July should inflation and the labor market remain firm.</p> <p><b>Expected terminal rate: 5.25-5.5%</b></p>	Neutral
<b>ECB</b>	<p><b>Deposit facility rate: 3.5%</b></p> <p>Prior changes: June, May 2023 (+25bps) March, February 2023 and December 2022 (+50bps) September and October 2022 (+75bps) July 2022 (+50bps), the first hike since 2011</p>	<p>The ECB's balance sheet unwind began on March 1, 2023. The decline will amount to EUR 15bn per month on average until the end of the second quarter of 2023 and its subsequent pace will be determined over time. The anti-fragmentation tool, the Transmission Protection Instrument (TPI), unveiled in July 2022 will be used to ensure monetary policy is transmitted smoothly across all euro area countries.</p>	<p>We expect the ECB to reach a terminal rate of 4% given elevated inflation, a tight labor market and sticky wage growth.</p> <p><b>Expected terminal rate: 4.0%</b></p>	Neutral
<b>BoE</b>	<p><b>Bank Rate: 5.0%</b></p> <p>Prior changes: June 2023 (+50bps) May, March 2023 (+25bps) February 2023 and December 2022 (+50bps) November 2022 (+75bps) August and September 2022 (+50bps) February, March, May, June 2022 (+25bps) December 2021 (+15bps)</p>	<p>In September/October 2022, the BoE temporarily purchased long-dated UK gilts and postponed active gilt sales; in November 2022 the BoE commenced active sales and an unwind of the temporary purchases.</p>	<p>We expect recent data momentum to keep the BoE on a hiking path and expect a terminal rate of 5.5%.</p> <p><b>Expected terminal rate: 5.5%</b></p>	Dovish
<b>BoJ</b>	<p><b>Policy deposit rate: -0.10%</b></p> <p>Prior changes: January 2016, when the Bank introduced its negative interest rate policy (NIRP) 10-year JGB yield target: ~0%, with tolerance band of +/-50bps (yield curve control policy)</p>	<p>Following the December 2022 meeting, the BoJ has stepped up their defence of the new +0.5% YCC upper band by significantly increasing regular and ad-hoc Japanese Government Bond purchases along the yield curve. Targets for ETF, corporate bond and other risk asset purchases remain in place but in practice there have been limited recent buying.</p>	<p>Absent a turn in the global economic cycle, we expect YCC to be tweaked further or abandoned. We also see potential for a rate rise this year.</p>	Hawkish

Source: Goldman Sachs Asset Management. As of June 30, 2023. The economic and market forecasts presented herein are for informational purposes as of the date of this presentation. 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	6 months ago	12 months ago
US 2 Year	4.9	4.4	2.9
US 10 Year	3.9	3.9	3.0
US 2-10 Slope	-1.0	-0.5	0.1
US Treasury 10-Year Inflation-Protected	1.7	1.6	0.7
Germany 2 Year	3.2	2.7	0.7
Germany 10 Year	2.4	2.6	1.4
Japanese 10 Year	0.4	0.4	0.2
UK 10 Year	4.4	3.7	2.3
Chinese 10 Year	2.6	2.8	2.8

Source: Macrobond, Goldman Sachs Asset Management. As of 30 June 2023.

## EXCHANGE RATES (BASIS POINTS)

	Latest	6 months ago	12 months ago
Euro (€ per \$)	0.92	0.94	0.96
British Pound (£ per \$)	0.79	0.83	0.82
Japanese Yen (¥ per \$)	144.61	131.94	135.84
Chinese Yuan Renminbi (CNY per \$)	7.25	6.90	6.70

Source: Macrobond, Goldman Sachs Asset Management. As of 30 June 2023.

## FIXED INCOME SECTOR YIELDS (%)

	Latest	Last 10 year average	Last 10 year Percentile
US Investment Grade	5.6	3.3	98.4
European Investment Grade	4.3	1.3	99.5
UK Investment Grade	6.5	3.0	99.4
US High Yield	8.6	6.3	92.6
European High Yield	7.4	4.1	96.5
EM External	8.4	6.0	92.1
EM Corporate	7.1	5.2	97.2
US Agency MBS	4.8	2.7	98.9
US ABS	6.2	2.3	99.9
US Munis	3.6	2.3	96.0
US CMBS	4.8	2.4	98.9

Source: Macrobond, Goldman Sachs Asset Management, ICE BofAML and J.P. Morgan. As of 30 June 2023.

## FIXED INCOME SECTOR SPREADS (BASIS POINTS)

	Latest	12 months ago	Last 10 Year Percentile
US Investment Grade	131	158	53.1
European Investment Grade	160	202	88.2
UK Investment Grade	174	202	79.5
US High Yield	414	562	48.8
European High Yield	442	601	68.2
EM External	436	535	78.7
EM Corporate	316	372	81.9
US Agency MBS	55	36	37.4
US ABS	135	145	85.4
US CMBS	53	54	87.0

Source: Macrobond, Goldman Sachs Asset Management, ICE BofAML and J.P. Morgan. As of 30 June 2023.

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## ADDITIONAL FIXED INCOME INSIGHTS

### Musings

[June 23, 2023](#)

[June 16, 2023](#)

[June 9, 2023](#)

[June 2, 2023](#)

### Navigating Fixed Income

[Navigating Opportunities in Investment Grade Credit](#)

[Navigating External EM Debt](#)

[Navigating The EM Corporate Bond Market](#)

[Navigating Short Duration Opportunities](#)

[Staying Overweight MBS Through Macro Volatility](#)

[Navigating Fixed Income in 2023](#)

### Fixed Income Outlook

[Q2 2023 Outlook: Quality Control](#)

[Q1 2023 Outlook: Bring on Bonds](#)

### Asset Management Insights

[Asset Management Perspectives: Finding Footholds for Growth](#)

#### Fixed Income Highlights:

- [Commercial Real Estate: Into the Headwinds](#)
- [Bear \(Market\) Necessities: The Case for Core Fixed Income](#)
- [All About Alpha: Portfolio Construction in a New Reality](#)
- [China's Next Chapter: Reopening, Recovery and Beyond](#)
- [Green Bonds: Connecting Fixed Income Capital to the Global Climate Transition](#)

[Asset Management Perspectives: Inflection Points](#)

#### Fixed Income Highlights:

- [Europe: Recovering into a New Regime](#)

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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.

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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.

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## MUSINGS

### **Index Benchmarks**

Indices are unmanaged. The figures for the index reflect the reinvestment of all income or dividends, as applicable, but do not reflect the deduction of any fees or expenses which would reduce returns. Investors cannot invest directly in indices.

The indices referenced herein have been selected because they are well known, easily recognized by investors, and reflect those indices that the Investment Manager believes, in part based on industry practice, provide a suitable benchmark against which to evaluate the investment or broader market described herein. The exclusion of "failed" or closed hedge funds may mean that each index overstates the performance of hedge funds generally.

### **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

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

**MBS:** ICE BofAML US Agency Mortgage-Backed Securities Index

**CMBS:** ICE BofAML US Fixed Rate Commercial Mortgage-Backed Securities Index

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

**Past performance does not guarantee future results, which may vary.** The value of investments and the income derived from investments will fluctuate and can go down as well as up. A loss of principal may occur.

**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).

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