



A Note from the AB Fixed Income Trading Desk

Thoughts from Our Senior Portfolio Managers

Sell America, or Buy Bonds?

“Chance fights ever on the side of the prudent.”—Euripides

For decades, US markets were the anchor for global investors—reliable, resilient, and seen as the best of the best. But now, with a shifting policy backdrop, trade disputes and persistent budget worries, that foundation is being put into question. Investors are rightly reassessing whether the same rules will carry them forward. The market isn’t in panic mode; it’s reassessing if long-held capital-market assumptions still hold in an environment where conviction trades are lacking. In a world where the range of potential outcomes is wide, and the interplay of trade, fiscal and monetary forces is more complex than ever, complacency can be the easy option for many investors. However, in a world where there are more questions than answers, chance always fights on the side of the prudent—and the active.

Key Takeaways

- The range of outcomes remains wide—markets are pricing in possibilities in both directions, not just the downside.
- We expect volatility as market narratives shift, but underlying economic fundamentals and technicals are supportive.
- Active management is best poised to capture opportunity in range-bound but shifting environments.

What Happened

What’s been feeding the “Sell America” narrative in recent weeks? Economic and policy data have painted a mixed picture, reinforcing a sense that markets are in a holding pattern until the hard data suggest otherwise.

Trade Policy: A US trade court ruled that President Trump’s tariffs exceeded his authority under the International Emergency Economic Powers Act, which reserves such powers for Congress. However, an appeals court granted a stay, temporarily keeping the tariffs in place. Meanwhile, the administration announced plans to double tariffs on steel and aluminum imports to 50%, effective June 4, aiming to support the domestic steel industry amid the U.S. Steel–Nippon Steel deal. Concurrently, trade negotiations with the EU remain tense, with the bloc preparing countermeasures should talks break down. All the while, the US trade deficit narrowed 55.5% in April, due to a record 16.3% decline in imports and a 3% increase in exports (*Display 1*).

Economic Data: The second estimate for the 1Q 2025 GDP indicated a 0.2% annualized contraction, marking the first decline in three years. Notably, consumer spending growth was revised downward to 1.2%, the weakest pace in nearly two years, highlighting softer final consumption (*Display 2*).

Manufacturing and Services: The ISM Manufacturing PMI fell to 48.5 in May, indicating a contraction in the manufacturing sector for the third consecutive month. However, underlying components such as new orders and employment showed pockets of resilience.

Global Perspective: In the eurozone, headline inflation undershot forecasts in May at 1.9%, with core inflation easing to 2.3%. The ECB followed through by cutting the policy rate by 25 basis points (bps), in line with consensus (*Display 3*). In Japan, the Ministry of Finance signaled potential reductions in superlong bond issuance following weak demand in recent auctions, leading to a decline in yields on 30-year Japanese government bonds. This development provided some support to the global rates complex, particularly at the long end (*Display 4*).

Fiscal and Geopolitical Backdrop: The “One Big Beautiful Bill Act,” currently under Senate review, proposes significant tax cuts alongside substantial spending reductions, particularly targeting Medicaid. While the bill aims to stimulate economic growth, it is projected to add approximately \$3 trillion to the national debt over the next decade, raising concerns among fiscal conservatives and contributing to volatility in US term premiums (*Display 5*).

Federal Reserve Commentary: Recent statements from Federal Reserve officials indicate a cautious approach amid economic uncertainties. Dallas Fed President Lorie Logan emphasized the need for patience in monetary policy, noting that while inflation is slightly above target, the full impact of recent tariffs is yet to be seen. Atlanta Fed President Raphael Bostic echoed the need for patience, suggesting that the current economic conditions should be carefully monitored before interest rates are adjusted. Meanwhile,

Fed Governor Christopher Waller expressed openness to rate cuts later in the year, provided that core inflation trends toward the Fed's 2% goal and the labor market remains strong.

Jobs: The US economy added 139,000 jobs in May, which combined with downward revisions to past months, is in line with the consensus forecast. Unemployment remained unchanged at 4.2%.

Our View

Markets are always uncertain—some days more so than others. Today's backdrop is far from the upheaval of the global financial crisis or the eurozone debt crisis, but it's also a far cry from the confidence and vigor of the post-pandemic recovery. We're in the mid-to-late innings of this cycle, with trade, fiscal and monetary regimes all shifting in ways that leave markets more exposed to policy risk and sentiment-driven swings than we've seen in some time. Against this backdrop, investors are rightly asking whether the pillars of past playbooks are the right moves going forward.

Trade Policy and Growth: The recent court ruling that President Trump's tariffs overstepped Constitutional authority—though paused for now—likely extends the timeline for final clarity on trade policy. That uncertainty complicates negotiations and clouds federal budget revenue assumptions, potentially delaying the resolution of the broader fiscal outlook. In the meantime, businesses and consumers are showing caution, delaying discretionary investment and spending as the path forward remains murky. All told, this suggests a near-term drag on growth as we move through mid-year.

Macro Outlook: Hard data remain relatively firm, with labor markets still strong and final demand softening only gradually. However, the "strong consumer" regime that powered the early post-pandemic recovery has faded, and we believe the economy is more sensitive to labor market conditions and shifting sentiment than it was even a year ago. Outside the US, the risk is tilted firmly to the downside: Europe faces real recession risk, and China will have to lean more heavily than usual on fiscal and monetary intervention to offset trade disruptions and maintain growth stability.

Fiscal and Term Premiums: The One Big Beautiful Bill Act leans expansionary and highlights the absence of fiscal restraint in Washington. Moody's downgrade wasn't a surprise, but it underscores that markets are no longer giving the US a free pass on fiscal sustainability. The result is higher term premiums and a more discerning bond market—particularly at the long end of the curve. De-dollarization concerns and larger-than-expected deficits would only reinforce this dynamic.

Valuations: Rates markets have likely tested the near-term lows and highs, with the US curve oversold and Europe relatively overbought. Globally, we expect yield curves to continue steepening on the back of easing monetary policy and persistent term premium concerns—except in Japan, where flattening is likely to continue. Meanwhile, risk assets no longer look cheap, with little downside priced in. We continue to see better relative value in credit markets versus equities, given the strong fundamental and technical backdrop that has supported credit spreads and all-in yields so far this year.

Investment Implications

In an environment characterized by economic and policy uncertainty, conviction is understandably low, and markets are likely to continue oscillating within ranges until a clear narrative emerges. While markets are always messy, this backdrop makes active management not just valuable but essential. Here's how—

- **Strategic Portfolio Construction:** Active managers can design portfolios that outperform through the cycle by focusing on durable risk-adjusted returns rather than short-term index moves or near-term market gyrations.
- **Cross-Sector Capabilities:** The flexibility to allocate across governments, corporates and securitized markets means active managers can identify and take advantage of relative value across different sectors—recognizing that policy and economic shifts impact these areas differently.
- **Quantitative Research:** A robust quantitative and technology architecture enables the identification of relative value opportunities and mispricings across broad sets of securities and issuers, as well as evolving risk compositions.
- **Fundamental Research:** The ability to avoid weaker credits, while focusing on those with strong fundamentals and technicals, is crucial. Actively navigating shifting credit cycles and seizing on technical imbalances can create meaningful alpha opportunities and provide a critical cushion against drawdowns.
- **Duration Management:** Active managers can tactically adjust interest-rate exposure—capturing value when it emerges, managing risks associated with changing global rate paths, and recognizing that not all yield curves are created equal. We continue to see attractive opportunities in global duration positioning, particularly in the UK and US, which look increasingly cheap relative to other developed market peers. Curve steepeners also remain a compelling way to express these views—by capitalizing on the likelihood that curves will steepen in the face of slowing growth, sticky inflation and shifting central bank policies. In Japan, by contrast, we continue to expect flattening despite monetary policy staying relatively accommodative.
- **Risk Management:** Thoughtful risk management remains foundational: taking more risk when markets dislocate and pulling back when complacency or exuberance pushes valuations too far. In today's environment, that also means prioritizing liquidity and maintaining a higher-quality bias within fixed-income allocations—two levers that offer both flexibility and protection when the path forward is murky.

All of this reinforces our conviction in fixed income as a compelling source of risk-adjusted returns. In a world where the outlook for equities and illiquid alternatives remains uncertain, high-quality bonds and credit strategies can help both income and resilience. The opportunity set for active fixed-income investing is as strong as it has been in years—especially for managers prepared to cut through the noise and adapt to changing market signals.

Wishing you continued success in your investment journey,

Scott DiMaggio, Gershon Distenfeld, Matt Sheridan, Fahd Malik, Will Smith, John Taylor, Serena Zhou, Tim Kurpis, Christian DiClementi, Sonam Dorji and AJ Rivers

To learn more about AB's fixed-income solutions and access other market insights, visit [Fixed-Income Investments | AB](#).

US Economic Scenarios

Economic Outcome	Description	Probability (Percent)
Hard Landing/Deep Contraction	Either an external shock occurs or business-cycle dynamics deteriorate sharply. Growth slows rapidly, and central banks have to act aggressively to support growth.	20
Soft Landing/Mild Contraction	Growth slows, labor markets weaken, and central banks hurry to get back to neutral. The magnitude of the slowdown defines the terminal rate, and inflation expectations determine the speed with which it is reached.	35
Rebalancing	Both inflation and growth approach trend levels only slowly, leaving the Fed comfortable easing policy slowly and remaining restrictive well into 2025: 25-bps cuts at some, but not all, meetings until the policy hits neutral in late 2025 or 2026.	35
Stagflation	The economy slows, but inflation expectations rise, trapping the Fed between a rock and a hard place.	5
No Landing	The economy performs despite headwinds, and inflation stays elevated enough to keep the Fed on hold for some time to come.	5

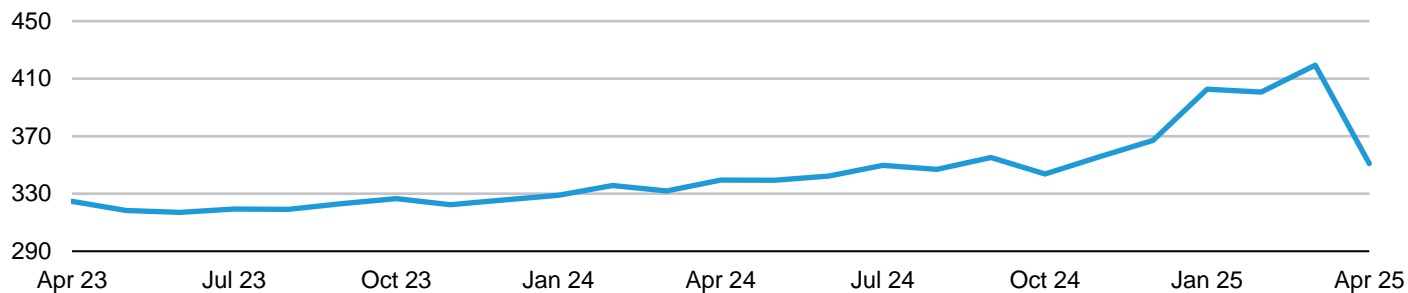
European Tariff Scenarios

2025 Forecasts	Counterfactual No Tariffs at All (Percent)	Upside No Universal Tariffs (Percent)	Current Situation 10% Universal Tariffs (Percent)	April 2nd–9th 20% Universal Tariffs (Percent)	Downside 30% Universal Tariffs (Percent)
Growth (YoY)	1.10	0.80	0.06	0.30	−0.60
Inflation (Annual)	2.00	1.80	1.60	1.70	1.40
ECB Deposit Rate (Year-End 2025)	2.00	1.75	1.75	1.75	1.00
Recession Probability	30.00	40.00	60.00	70.00	90.00

There is no guarantee that any estimates or forecasts will be realized.

Display 1: A Record 16.3% Decline in Imports Cut the Monthly Trade Deficit in Half

US Trade Balance of Imports (USD)

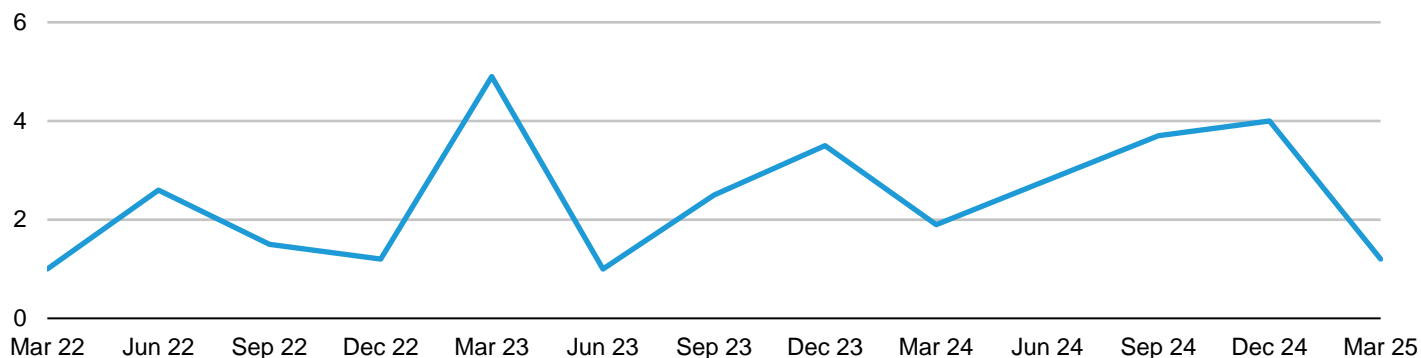


As of June 6, 2025

Source: Bloomberg

Display 2: Consumer Spending Growth Was Revised Downward to the Weakest Pace in Nearly Two Years

GDP US Personal Consumption (QoQ)

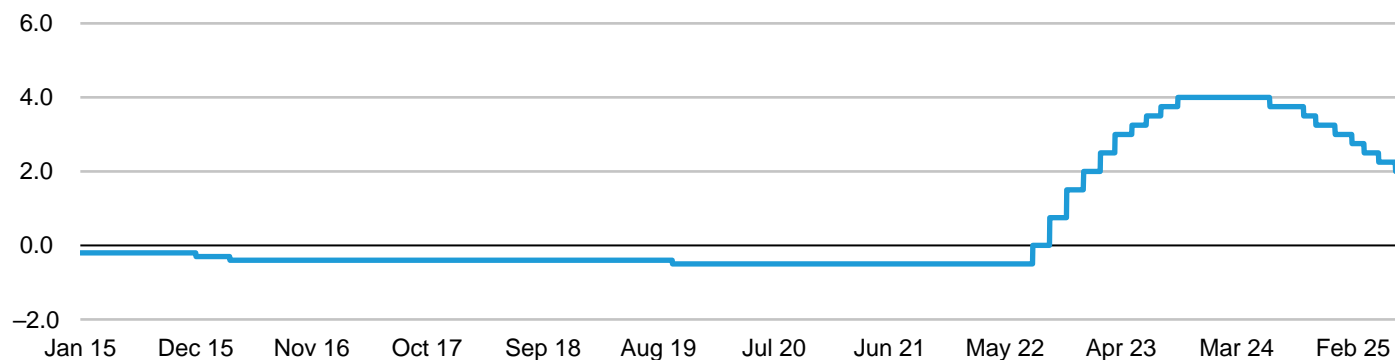


June 6, 2025

Source: Bloomberg

Display 3: The ECB Cut 25 Basis Points, In Line with Consensus Forecasts

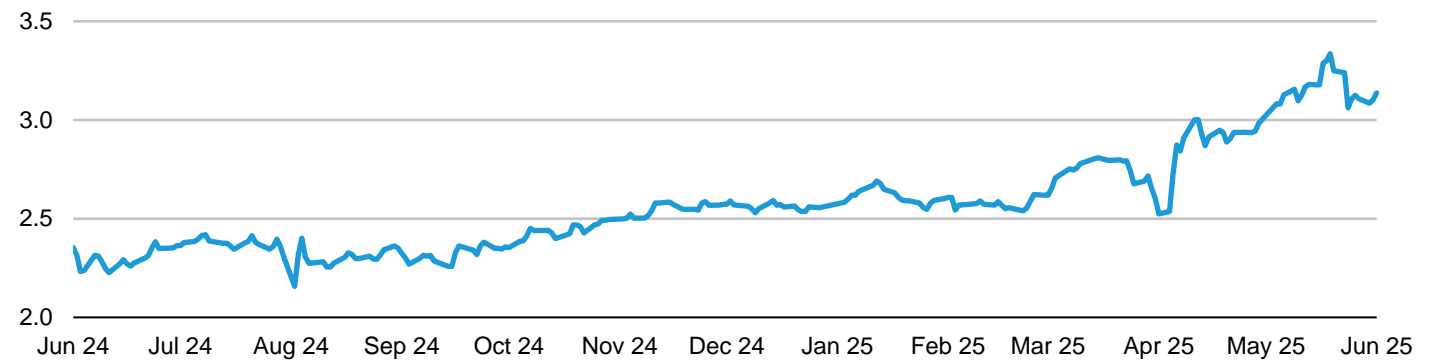
ECB Deposit Facility Announcement Rate (Percent)



As of June 6, 2025

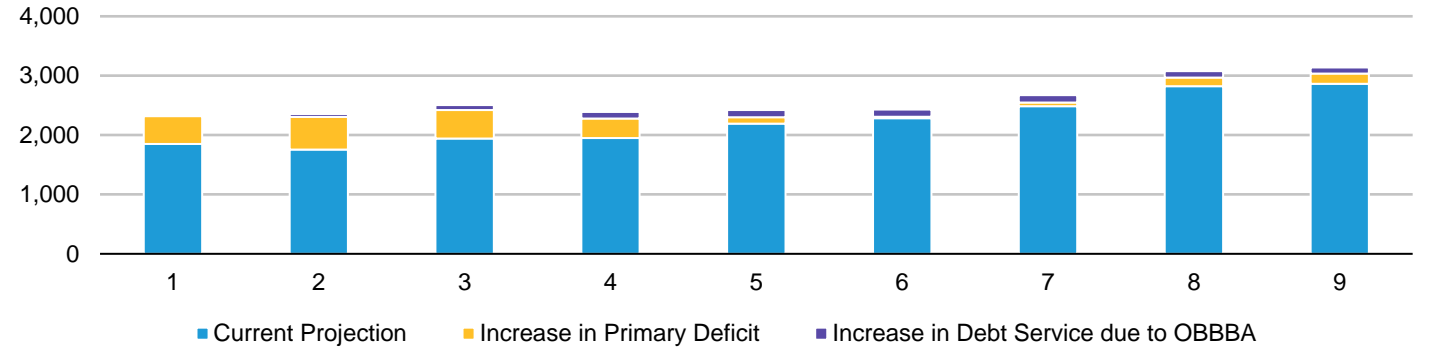
Source: Bloomberg

Display 4: The Japan Ministry of Finance Signaled Potential Reductions in Superlong Bond Issuance, Calming Markets
Japan Government Bond 40-Year Compound Yield (Percent)



As of June 6, 2025
Source: Bloomberg

Display 5: One Big Beautiful Bill Act to Increase the Budget Deficit by Approximately \$3 Trillion
US Federal Budget Deficit (USD Billion)



Past performance does not guarantee future results.
OBBBA: One Big Beautiful Bill Act
As of June 6, 2025
Source: Bloomberg

Investment Risks to Consider

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