ALLIANCEBERNSTEIN®

June 24, 2025

A Note from the AB Fixed Income Trading Desk

Thoughts from Our Senior Portfolio Managers

Safe Havens and Shaky Assumptions

“In investing, what is comfortable is rarely profitable.”—Robert Arnott

Investors aren’t short on information; they’re short on conviction. Over the past two weeks, softer inflation, weaker retail sales and rising geopolitical tensions have all challenged the usual playbook. When conflict escalated in the Middle East on June 13, traditional safe havens like Treasuries didn’t initially respond as expected. Rates eventually rallied the following week, but that moment of hesitation reflects a broader theme: historical relationships are under pressure, and economic intuition isn’t always rewarded.

In this note, we explore what’s driving that part of that disconnect—and where we still see clarity in an increasingly uncertain landscape.

Key Takeaways

- Hard data weakened, soft data improved, central banks stayed firm and geopolitical tensions increased.
- Concerns over foreign selling of US Treasuries are overdone, but curve positioning remains critical.
- The combination of short-term credit, intermediate duration and global diversification is still our preferred approach to managing asymmetric risks.

What Happened

Despite a relatively light macro calendar, markets were far from quiet. Shifting trade rhetoric, geopolitical tensions and central bank decisions gave market participants plenty to digest.

Hard Data: Labor markets continued to show signs of orderly rebalancing. Continuing jobless claims reached new cycle highs, reinforcing a slow grind toward a softer employment backdrop but reflective of a labor market in balance (*Display 1*). Inflation data surprised to the downside for a fourth straight month: May’s CPI and Producer Price Index prints fell short of expectations. May retail sales fell 0.9%, the sharpest drop year-to-date, with broad-based weakness across categories.

Soft Data: Consumer sentiment rebounded in June, breaking a three-month slide, according to a University of Michigan survey. The improvement was driven by falling short-term inflation expectations, which dropped by1.5% (*Display 2*). Consumers remain highly reactive to headline risks—particularly around energy and food—but the latest uptick likely reflects a temporary reprieve from aggressive trade rhetoric.

Central Banks: There was a flurry of central bank activity last week, including policy rate decisions from the Bank of Japan, Federal Reserve and Bank of England. As expected, all policymakers left rates on hold, while the Fed maintained its median forecast for two more rate cuts by year-end (*Display 3*). Meanwhile, speculation around Chair Jerome Powell’s successor is gaining traction. Treasury Secretary Scott Bessent is being floated as a potential nominee, raising market concerns over future Fed independence and policy direction under the second Trump administration.

Trade Policy: President Donald Trump reiterated plans to reset US tariff rates by June 25, ahead of the expiration of current reciprocal delay agreements. While Secretary Bessent has floated temporary exemptions for “good faith” partners, the legal framework remains unclear. A tentative US–China agreement to ease restrictions on rare earths and tech exports emerged from London talks—possibly laying the groundwork for a Trump–Xi meeting later this year.

Geopolitics: Tensions in the Middle East escalated on June 13 following Israeli air strikes on Iranian military and nuclear infrastructure, reportedly eliminating senior Islamic Revolutionary Guard Corps leadership. Iran responded with a barrage of more than 200 missiles, and the US is weighing the decision of whether or not to engage with military action. Oil and gold rallied, and the US dollar firmed, but Treasuries failed to rally in the immediate aftermath—raising fresh questions about their role as the default risk-off asset.

Fiscal Policy: The One Big Beautiful Bill Act continued to evolve in the Senate, with tax and Medicaid provisions dominating both the deficit-increasing and deficit-reducing elements. The proposed changes offer an early read on the potential fiscal trajectory heading into autumn.

Our View

Uncertainty may be the most consistent market force this year, but that doesn't mean investors should sit on their hands. If anything, the muted response in Treasuries following a major geopolitical event highlights how traditional assumptions about safe havens are being reevaluated in real time.

We've written previously about the "Sell America" narrative. It remains more theory than reality, but the conversation is gaining volume. While there's little concrete evidence of foreign flight from US assets, persistent questions around fiscal sustainability, trade fragmentation and central bank independence are reshaping long-end risk premiums. That said, there are early signs that domestic retail buyers are reallocating from core US exposures to globally diversified strategies (*Display 4*).

Treasuries: Despite shifting narratives, the structural case for Treasuries remains intact. Auction data show healthy demand, and TIC flows confirm steady foreign participation (*Display 5*). April data show that private investors net-sold $53 billion whereas the foreign official and private investors communities added $12 billion. However, rolling demand thus far still shows above-average net-buying prior to April. Still, with deficits rising and term premiums elevated, investors are increasingly sensitive to auction sizes, debt-management policy and shifting narratives on global flows.

Growth: While growth has held up so far, the momentum is fading. We expect a deceleration in the second half of 2025 as tariffs impact supply chains and consumption patterns become more erratic. The bounce in sentiment data is encouraging, but given the data's decline in explanatory power, we are cautious about overinterpreting this movement.

Rates: While the market typically focuses on the median dot in the Fed's *Summary of Economic Projections*, the median dot is all but irrelevant now because the distribution of the dots is bimodal. It is not yet clear whether the inflation or the growth impact will be larger. Our view is that the growth impact will ultimately motivate the Fed to act, and thus we expect two cuts later this year. But if the labor market doesn't slow, the Fed could easily choose not to cut rates at all. We will need to watch the data carefully—especially labor-market data and inflation expectations—before we can be confident about the Fed's path.

Therefore, we continue to favor global steepeners as the clearest way to express duration views—particularly in the US and UK, where curves remain exposed to inflation and fiscal risks. In the US, the Fed may be patient. But if labor markets weaken and inflation expectations remain anchored, cuts may come faster than markets currently expect.

Credit: Despite high-yield spreads breaking below 300 basis points (bps) again, credit still offers one of the best combinations of income and resilience. Crossover and high-quality high yield remain attractive. Issuers have adapted to higher rates through shorter tenors and floating-rate issuance—especially within financials. Additionally, there are attractive opportunities in European high yield, as hedged-dollar yields remain elevated. On a forward-looking basis, we believe credit is still positioned better than equities.

Fallen Angels: The downgrade of Warner Bros. to high yield could be the first of several large investment-grade downgrades. In prior cycles, these reratings caused disruption, but today's market appears more balanced. An "up-in-quality" rotation in high yield is underway and may help absorb new entrants more smoothly. We are therefore positioned to act quickly on further migrations.

Volatility: We expect elevated volatility to persist, but this creates opportunity for active managers. In this environment, curve positioning, relative value and security selection can materially enhance outcomes. Portfolios should stay flexible, diversified and grounded in fundamentals.

Investment Implications

Against a backdrop of rising fiscal uncertainty, evolving central bank dynamics and unexpected market behavior, we continue to emphasize fixed-income strategies that balance income generation with structural resilience.

Short-Duration High Yield: This segment remains a core allocation for investors seeking to balance risk and return. Yields continue to hover near multi-decade highs, offering equity-like return potential with less exposure to credit volatility and interest-rate risk. Importantly, shorter spread duration and a higher average-credit quality profile provide meaningful downside mitigation relative to traditional high yield. In our view, short duration high yield remains one of the most efficient ways to preserve income while reducing exposure to the long end of the curve and broader macro uncertainty.

Belly of the Yield Curve: The belly continues to offer the most attractive balance of yield, convexity and volatility management. It avoids the sensitivity of the long end—where budget dynamics and term premium repricing have created pockets of instability—while still delivering income that outpaces cash and short-duration bonds. We see the belly of the yield curve as the most effective hedge against a slowing growth environment or dovish shift in policy, especially in the US and UK, where central banks are still weighing the risks of doing too much versus too little.

Global Bonds: In today's environment, we believe geographic and sector diversification adds incremental value—particularly when interest-rate paths and inflation pressures are diverging across regions. Global mandates allow for dynamic allocation across sovereigns, currencies and credit sectors—an important toolset as US policy becomes less predictable. We are not abandoning US duration, but we see merit in complementing it with exposures where fundamentals and policy conditions remain more stable. The ability to allocate across multiple opportunity sets enhances both flexibility and potential resilience.

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

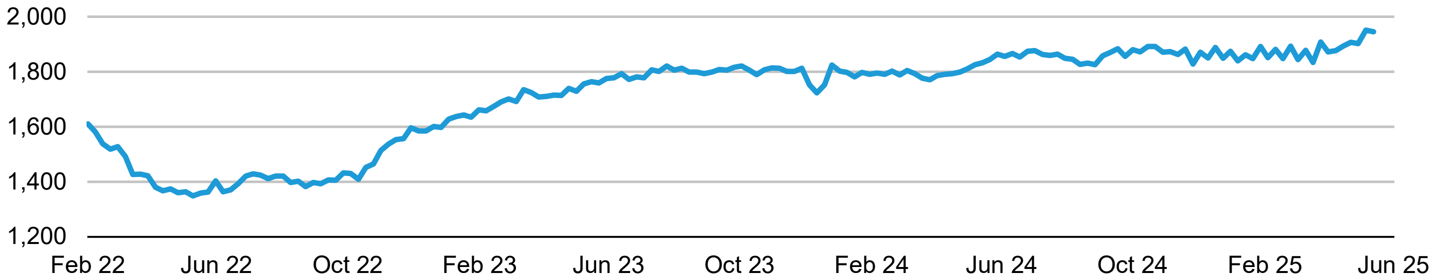
Economic Outcome	Description	Probability (Percent)
Hard Landing/ Deep Contraction	Either an external shock occurs or business-cycle dynamics deteriorate sharply. Growth slows rapidly, and central banks have to act aggressively to support growth.	20
Soft Landing/ Mild Contraction	Growth slows, labor markets 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 long-term trend levels only slowly, leaving the Fed comfortable with 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.	5

European Tariff Scenarios

2025 Forecasts	Counterfactual: No Tariffs at All (Percent)	Upside: No Universal Tariffs (Percent)	Current Situation: 10% Universal Tariffs (Percent)	April 2–9: 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

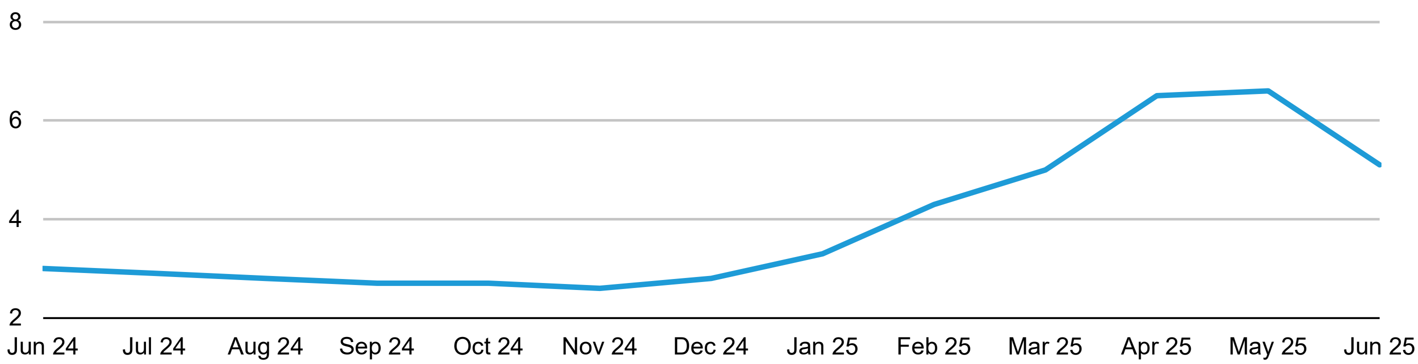
There is no guarantee that any estimates or forecasts will be realized.

Display 1: Continuing Jobless Claims Have Hit a New Cycle High
US Continuing Jobless Claims



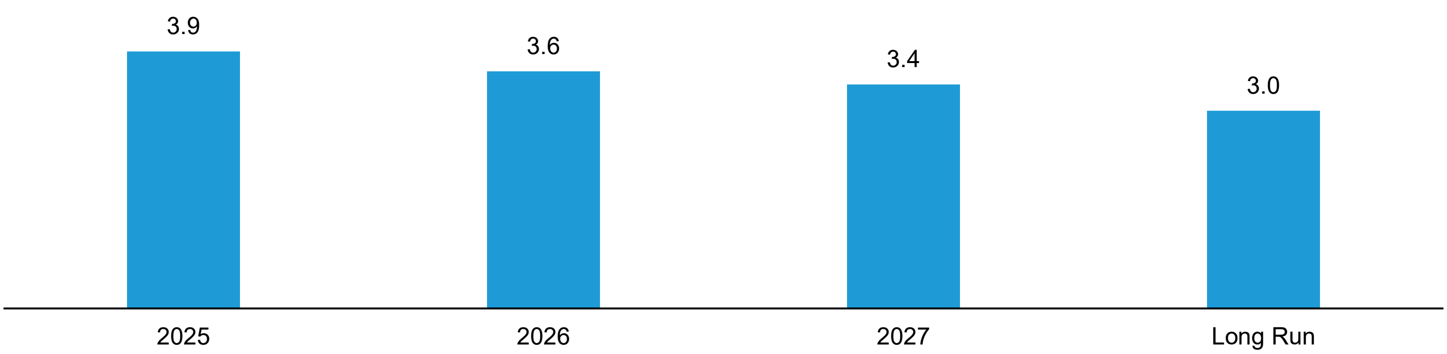
As of June 20, 2025
Source: Bloomberg and US Department of Labor

Display 2: Consumer Expectations of Inflation Have Fallen Since "Liberation Day"
Expected Changes in Inflation Rates (In 2026, Percent)



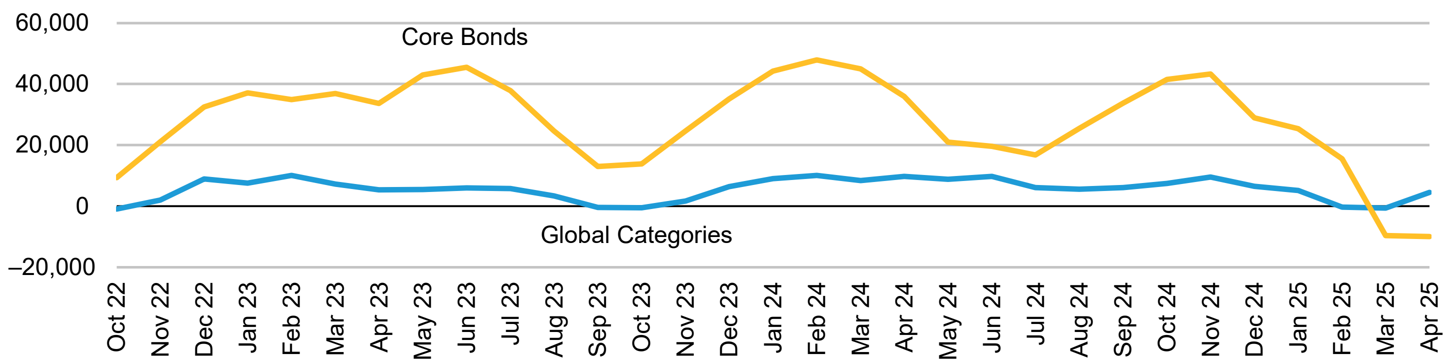
As of June 20, 2025
Source: University of Michigan Consumer Survey

Display 3: The Median Dot Shows That the Federal Reserve Expects to Cut Interest Rates Twice by Year-End
Implied Federal Funds Rate (Percent)



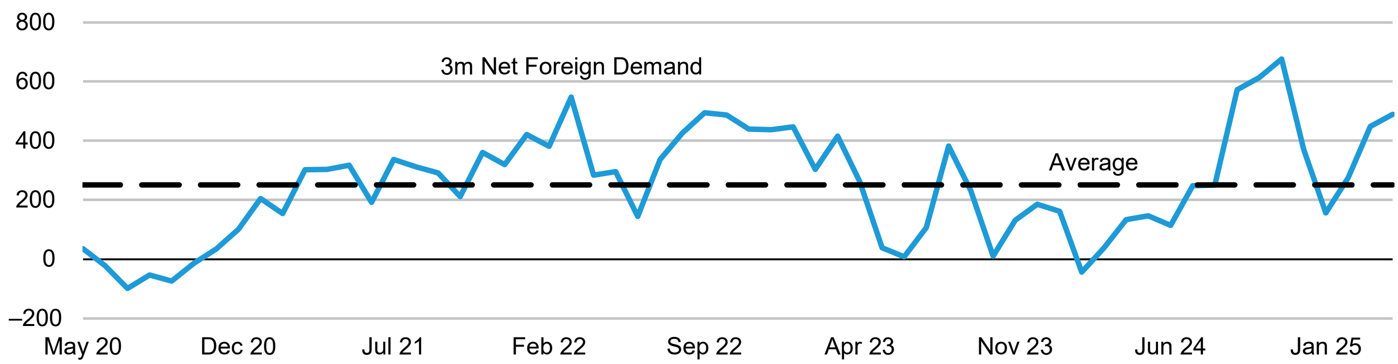
As of June 20, 2025
Source: Federal Open Market Committee *Summary of Economic Projections*

Display 4: US Consumers Are Selling Core Bonds, While Demand for Global Bonds Is Increasing
Trailing Three-Month Category Net Flow (USD Thousands)



As of April 30, 2025
Source: Simfund and AB

Display 5: Foreign Demand for US Treasuries Remains Robust Despite Market Conjecture
Trailing Three Months (Percent)



As of June 20, 2025
Source: Bloomberg and Treasury International Capital (TIC) System

Investment Risks to Consider

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