



## A Note from the AB Fixed Income Trading Desk

Thoughts from Our Portfolio Management Team

# A New Playbook for the Fed

*"What we've given markets is a new chapter for the central bank, some fresh thinking."*—Federal Reserve Chair Kevin Warsh

The arrival of sweltering summer temperatures caps off a red-hot first half for asset returns in 2026. Despite June being a relatively lackluster month, the second quarter produced banner returns for risk assets. The S&P 500 returned 15% in the second quarter after selling off in March, resulting in its strongest quarterly performance in six years (*Display 1*). Credit markets also produced healthy returns in the quarter, with spreads now hovering around where they were at the beginning of the year (*Display 2*). Rates ended higher on the back of higher real yields and expectations of a higher neutral policy rate. The drivers for the rally in the second quarter can be described as "optimism" on both a global and local level.

In June, the US and Iran signed a Memorandum of Understanding. Though substantial uncertainty remains and attacks have sporadically continued, market participants are more optimistic about a near-term resolution now than they were a month ago. This is most evident in the price of crude oil, which has now fallen to near pre-conflict levels, bringing with it lower inflation expectations (*Display 3*). Optimism domestically is also drawing from robust data concerning the labor market, US consumer spending and corporate earnings. SpaceX brought the largest IPO in history in June, while hyperscalers looked far and wide for capital markets to provide financing for their AI data-center build-out needs (*Display 4*). Against this backdrop, we received a dramatic shift in tone from the Fed: particularly, that markets should expect less commentary and guidance from the central bank. The overarching message: investors should do their own homework. In this note, we review the round trip in geopolitics and look ahead at what higher yields and the new Fed framework means for fixed-income markets.

## Recent Market Events and Data Releases (June 2026)

**The Fed and Chair Warsh's First Meeting:** From a headline perspective, the Fed's June meeting went as expected. The central bank left its target interest rate unchanged, and the dot plot showed that governors project that hikes are now more likely than cuts in the coming months—which had already been priced in by markets. As a result, the Treasury yield curve continued to flatten over the first half of 2026 (*Display 5*).

Under the surface, there were much bigger changes. Chair Warsh used his first meeting to shorten and simplify the Fed's statement, remove forward guidance, decline to submit his own Summary of Economic Projections (SEP) and launch task forces in five areas: communications, the balance sheet, data sources, productivity/jobs and the inflation framework. Less forward guidance represents a change in the trend of increasing transparency from Fed governors over the last few decades, and the launch of task forces mean more changes are likely forthcoming.

**Other Major Central Banks Turning Hawkish:** The ECB raised rates by 25 basis points (bps), taking the deposit rate to 2.25%, citing inflation pressures from the Middle East conflict and higher energy prices. The Bank of England held its policy rate at 3.75%, but the vote was 7 to 2, with two members favoring a hike to 4.00%. The Bank of Japan also continued normalization, guiding the overnight call rate to around 1.0% and signaling that underlying inflation was approaching its 2% objective.

**The Strait Is Open (Conditionally):** The US and Iran reached an initial agreement to reopen the Strait of Hormuz and extend a ceasefire, reducing the immediate left-tail risk to global energy markets despite tit-for-tat attacks challenging the agreement's durability. Oil prices fell on this news, with Brent and West Texas Intermediate reaching prewar levels. While the current agreement alleviates the blockade and returns a portion of traffic to the Strait of Hormuz, both sides exchanged strikes in recent weeks and there is uncertainty around the conditions for a longer-term agreement.

**The Labor Market Shows Signs of Strength:** Recent payroll data has highlighted the continued resilience of the US labor market. Although June payrolls came in below expectations, they were on the heels of better-than-expected prints in recent months. Additionally, the unemployment rate, at 4.2%, remains healthy, though falling labor force participation is becoming an increasingly bigger factor in maintaining that level. Despite headlines and concerns about tail risks, there have yet to be signs of cracks in the US labor market.

**Inflation Printed In-Line with Expectations, but the Trend Is Uncomfortable:** Headline CPI rose 4.2% year over year in May, while core CPI rose 2.9% year over year. Energy drove the uptick: gasoline prices were up sharply on a year-over-year basis, reflecting the pass-through from higher oil prices. The Fed's June SEP also marked inflation materially higher, with the 2026 median personal consumption expenditures (PCE) inflation forecast revised to 3.6% from 2.7% in March and core PCE revised to 3.3% from 2.7%. That said, oil prices have fallen close to pre-conflict levels and inflation expectations are at their lows for the year, indicating that the market does not view it likely that today's inflation pressures will persist or that second order impacts will materialize.

## Portfolio Manager Perspectives

**Central Banks:** We expect central banks to remain more cautious than markets hoped for at the start of the year with the Fed on hold and central banks outside the US also less supportive. While the most recent Fed projections lean hawkish, the round trip in energy prices that occurred following the Fed's meeting and well-anchored inflation expectations give the Fed room to be patient. The ECB's 25 bps hike, the hawkish split at the Bank of England and the Bank of Japan's continued normalization all point to policymakers who are focused on staving off the persistence of the most recent bout of inflation, even as growth has been more challenged in England and Japan than in the US.

We do not see a strong case for materially tighter monetary policy through 2026 unless inflation broadens meaningfully beyond energy prices. June data weakened the near-term case for cuts: payrolls remain positive, Institute for Supply Management readings are firmly expansionary, and the Fed's own inflation forecasts moved higher. At the same time, hikes are not our base case, as much of the recent inflation pressure is tied to energy and supply-sensitive categories, and additional tightening could weigh on rate-sensitive sectors without necessarily addressing the underlying sources of price pressure. That leaves us expecting a higher-for-longer range, with the Fed on hold until it has clearer evidence that price pressures are either feeding into core inflation and expectations or fading as energy markets normalize. Rather than trying to preempt the Fed's next step, investors should position portfolios for a higher-for-longer rate environment where yields are attractive for income seekers and active management of curve positioning, and global diversification is crucial.

**Growth and Inflation:** Can the US economy continue to defy expectations around growth? We think so, but the bifurcation of the economy and the US consumer warrants monitoring. Despite higher interest rates, elevated energy prices and geopolitical uncertainty, the US economy has remained remarkably resilient. This has been true not just for 2026, but for most of the post-COVID period. Strong consumer spending and continued corporate investment—particularly in AI infrastructure—have sustained the momentum in economic growth most recently. A key question for the remainder of the year is whether AI spending can continue to be a boon to business investment, employment and economic growth at the pace currently priced in.

The caveat is that economic resilience now cuts both ways. Stronger activity is constructive for earnings and risk assets, but it also reduces the urgency for policy support and makes elevated price components harder to ignore. A continued ceasefire between the US and Iran would be disinflationary at the margin, likely reducing market pricing of policy rate hikes, but significantly reduce tail risk for both growth and inflation—a welcome development for bonds and risk assets alike.

**Application for Rates:** Treasury yields are higher on the year, despite inflation breakevens and market-implied inflation expectations, falling to year-to-date lows. In effect, real yields have cheapened and present a more compelling entry point to own duration. Our expectation of fewer hikes than the market has priced in, along with reduced forward guidance from the Fed supporting higher-term premiums, signal a steeper curve. This reinforces our preference for the belly of the curve, where roll and carry is attractive and downside protection is most valuable should growth risks reassert themselves. Cautious position sizing is warranted, as the Fed's communications framework is being reset and geopolitical risk has eased but not disappeared. However, we believe investors are being properly compensated for owning duration in many parts of the world today.

**Application for Credit:** We remain constructive on investment-grade and high-yield credit, primarily because of attractive yields and consistently strong demand despite tight spreads. All-in yields remain attractive, fundamentals are still solid, corporate earnings have held up well, and moderate inflation can support earnings growth. Defaults should remain manageable if growth stays positive, and even in a weaker macro scenario, we expect the first impact to show up through valuations before it becomes a broader credit-cycle problem.

That said, tight spreads leave less room for error. We would not add credit beta indiscriminately. We believe the better approach is to use credit deliberately: emphasize income, quality, diversification and structures that can withstand a wider range of outcomes. For investors, we continue to think credit can be funded from both sides of the traditional 60/40 portfolio. From cash, credit can improve income potential. From equities, high yield and short-duration high yield can reduce reliance on equity upside while keeping clients invested in a constructive growth environment.

## Investment Implications

We continue to prefer a balanced fixed-income posture with a global tilt. Markets have rallied on the back of AI enthusiasm or potential euphoria. Tech-sensitive markets have driven the semiconductor sector in the S&P up 33% year to date. However, tighter credit spreads, elevated Treasury yields and a more cautious central-bank backdrop argue for portfolios that are diversified by region, rate cycle and credit exposure. For advisors, this is a good time to review whether client portfolios are overly concentrated in US duration, US corporate credit or cash-like exposures.

- **Global Bond—USD Hedged:** A USD-hedged global bond strategy can be a practical complement to core bond allocations. Central banks are no longer moving in lockstep, creating opportunities across global yield curves as policy paths diverge by region. A hedged global approach allows investors to maintain high-quality, intermediate-duration exposure while giving portfolio managers

the flexibility to shift between US and non-US markets as conditions change. For clients who still need ballast against equity volatility but want more flexibility than a traditional US-only core bond allocation provides, a global bond allocation can broaden the opportunity set without abandoning quality. We are not convinced that central banks will ultimately raise rates as high as markets are pricing in—and even if they did, central banks would likely need to soon return to easing, as underlying economic growth does not support such restrictive rates. Either way, this supports owning global duration.

- **Global High Yield:** Credit fundamentals remain supported by healthy earnings and a demand for income, but with US high-yield spreads already tight, we believe the next step should be broader rather than simply bigger. A global high-yield allocation can expand the opportunity set beyond US corporate credit by adding exposure to European high yield, emerging-market corporates and select securitized credit. We believe that a broader mix can provide additional sources of income, regional diversification and exposure to different economic and credit cycles. For advisors, the key message is that clients who already own high yield may not need more US high yield; they may need a more diversified version of the exposure.
- **Short-Duration High Yield:** For clients who believe the economy can hold together, but are not ready to take a full step into broad high yield, short-duration high yield remains a useful middle ground. These strategies typically focus on higher-quality high-yield issuers, carry less spread duration than the broad high-yield market, and sit in a part of the curve that still offers attractive income. Yields above 6% can help improve portfolio income, while the shorter-duration profile can help reduce sensitivity to rate volatility and limit drawdown risk if market sentiment weakens. This is not risk-free, but it can be a more measured way to add credit exposure for clients who want more income without taking on the full volatility of the broader high-yield market.

**Bottom line:** The strength of today's economic activity, along with higher real yields, creates pockets of opportunity. We believe that global bonds, global high yield and short-duration high yield each offer a different way to help clients stay invested, increase income and manage risk in a market where both rates and spreads require staying the course.

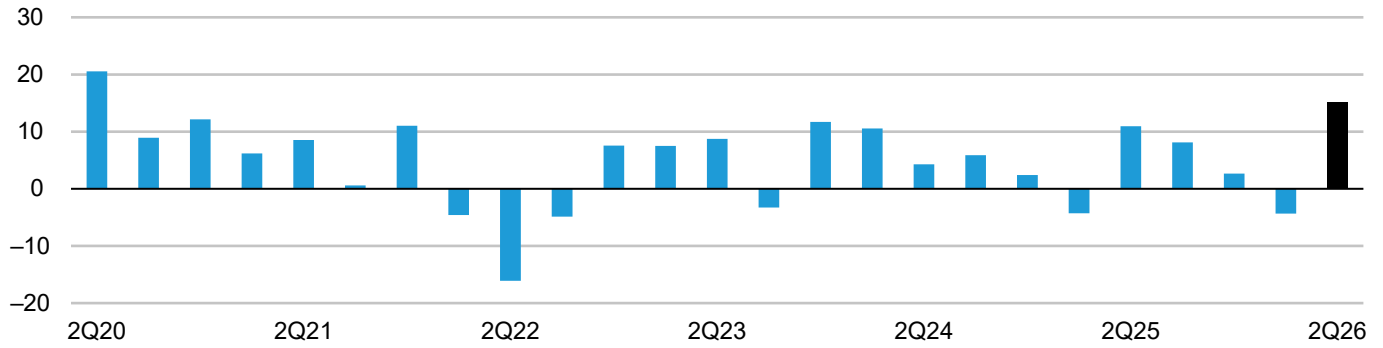
Wishing you success in your continued investment journey,

The AllianceBernstein Fixed Income Team

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

**Display 1: The Second Quarter of 2026 Produced the Strongest Equity Returns in Six Years**

S&P 500 Quarterly Returns (Percent)

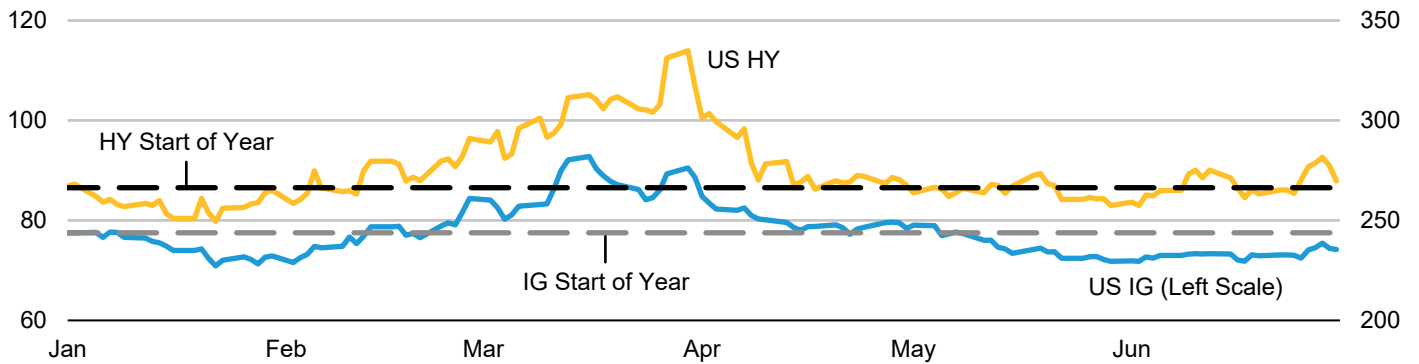


As of June 30, 2026

Source: Bloomberg

**Display 2: Credit Spreads Are Close to Start-of-Year Levels**

Option-Adjusted Spreads (Basis Points)



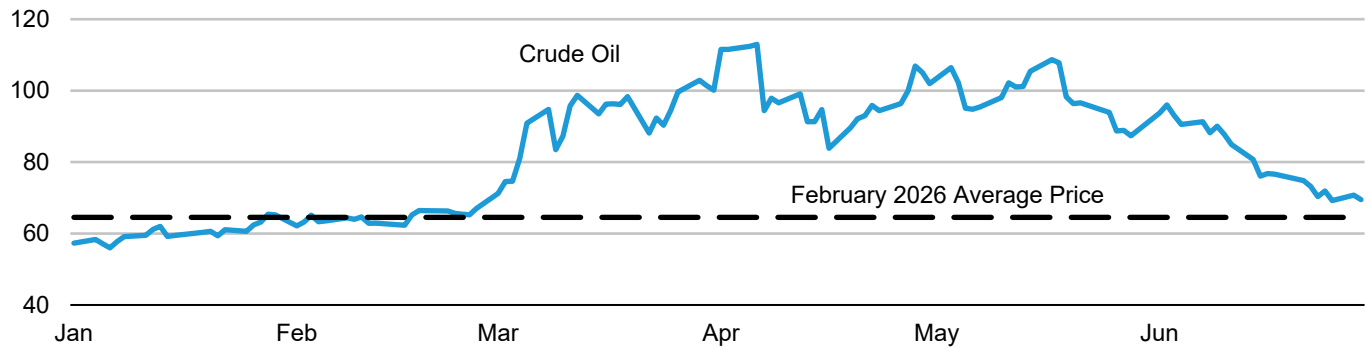
HY: high-yield; IG: investment-grade

As of June 30, 2026

Source: Bloomberg

**Display 3: Crude Oil Prices Have Fallen to Levels Similar to Where They Were Before the Iran Conflict**

Price (USD)

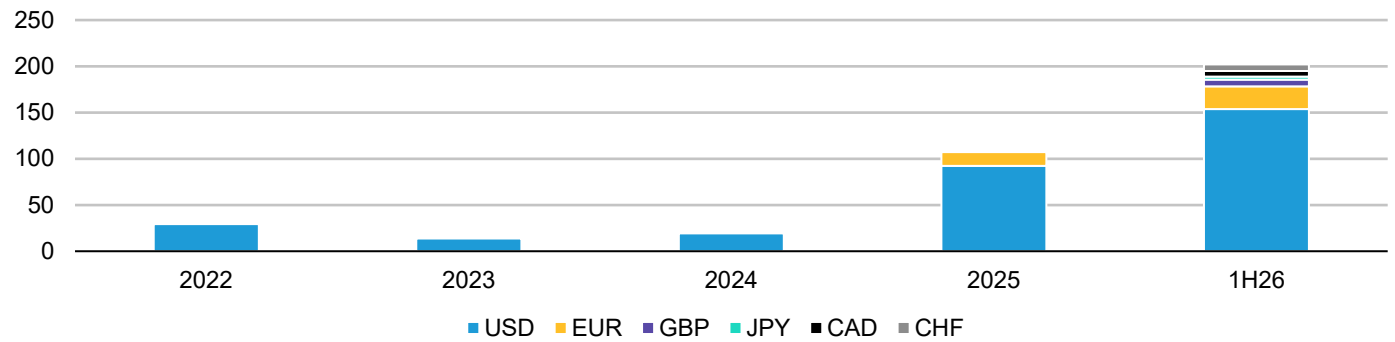


As of June 30, 2026

Source: Bloomberg

**Display 4: Hyperscalers Have Turned to a Variety of Debt Markets for Financing Data Center Capital Needs**

Investment-Grade Debt Issued (USD Billions)



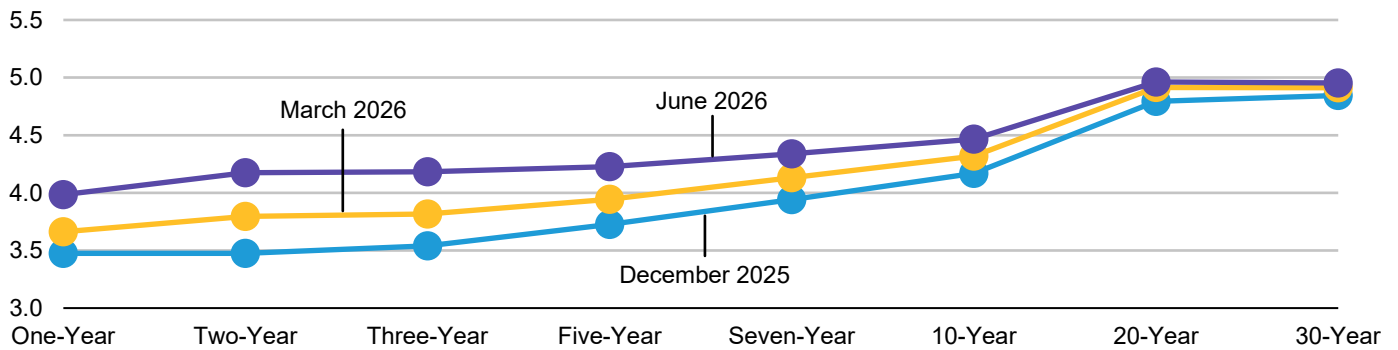
Hyperscalers defined as Google, Meta Platforms, Microsoft, Amazon, SpaceX and Oracle.

As of June 30, 2026

Source: Bloomberg

**Display 5: The Treasury Yield Curve Has Flattened in the First Half of 2026**

Yield (Percent)



As of June 30, 2026

Source: Bloomberg

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## Investment Risks to Consider

**The value of an investment can go down as well as up, and investors may not get back the full amount they invested. Capital is at risk. Past performance does not guarantee future results.**

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IMA-961828-2026-07-06