

MacKay Shields Fixed Income Quarterly Outlooks

April 2026



Investment
Management

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Global Fixed Income & Macro 2Q2026

Stay the course

Executive summary

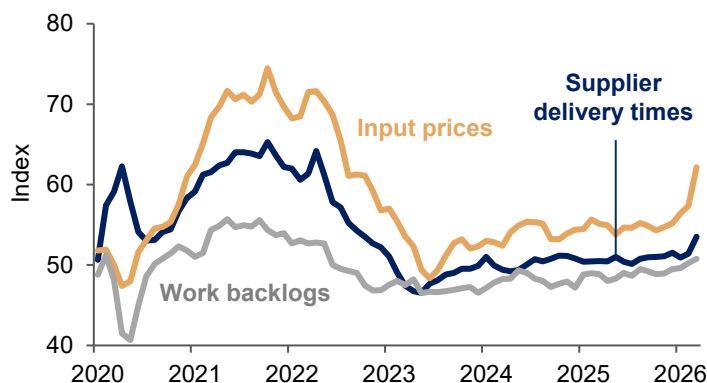
- The war in Iran represents a broad-based supply shock that is likely to slow global growth and push inflation higher, though the direct impact on the U.S. economy should remain manageable.
- Against a backdrop of elevated inflation and moderating growth, the Federal Reserve is likely to remain on hold, as policymakers balance upside risks to inflation against a gradual softening in activity.
- For fixed income markets, higher yields, increased volatility, and modest spread widening have improved forward return potential, with income remaining the primary driver of returns.
- We maintain a neutral to modestly long duration stance, favor intermediate maturities, and emphasize higher-quality credit and securitized assets, as dispersion across sectors reinforces the importance of selectivity and disciplined portfolio construction.

Macroeconomic outlook

The war in Iran poses meaningful downside risks to the global economy, particularly for oil-importing economies in Asia and Europe that are most vulnerable to disruptions in flows through the Strait of Hormuz. Beyond energy markets, the conflict represents a broader supply shock with potential spillovers into key industrial inputs, including fertilizer, plastics, aluminum and segments of the semiconductor supply chain. While the scale of disruption is unlikely to approach that seen during the pandemic, the war nonetheless introduces a stagflationary impulse, constraining output while placing upward pressure on global prices.

For the U.S. economy, the macroeconomic impact should remain manageable provided the conflict does not escalate further and shipping through the Strait begins to normalize in the coming weeks. Recent developments on this front have been mixed, however, and pricing in prediction markets reflects expectations that a return to more typical vessel traffic may not occur until early summer. Against this backdrop, we have lowered our US growth forecast for this year by 50 basis points, to two percent. The revision reflects both higher energy prices and the drag from tighter global supply conditions. The state of the U.S. consumer also factors into this adjustment.

Figure 1: Global manufacturing PMIs are already reflecting increased supply chain stresses



Source: S&P Global. Readings above 50 indicate that a greater share of responding firms report rising input prices, longer supplier delivery times, or increasing backlogs of work

Compared with the 2022 energy price spike, household resilience appears more limited, with a softer labor market, higher debt servicing burdens, and reduced savings all suggesting less capacity to absorb an external shock.

While the impact on headline inflation is likely to be meaningful, the effect on core inflation should be more limited and mainly reflecting higher transportation costs, increased input prices for goods such as plastics, and broader supply chain frictions. Assuming inflation expectations remain anchored, we expect core PCE inflation to end the year roughly where it began, at around three percent, for a second consecutive year. (see Figure 2)

Figure 2: Beyond the next year, inflation expectations remain anchored



Source: Barclays

Global Fixed Income & Macro 2Q2026

(cont'd)

We continue to expect monetary policy to remain on hold this year. While markets have at times priced in the possibility of a rate hike by year-end, we remain skeptical of such an outcome. As long as inflation expectations remain contained, policymakers are likely to look through a temporary energy-driven increase in inflation, particularly given the associated drag on growth and labor demand. We expect incoming Fed Chair Kevin Warsh to take a similar approach, remaining focused on underlying inflation dynamics and requiring clearer evidence of second-round effects before considering any tightening of policy.

Market and portfolio implications

A macroeconomic backdrop characterized by slowing growth, persistent inflation near three percent, and a Federal Reserve on hold creates an environment in which fixed income returns are increasingly driven by income, selectivity, and careful sector allocation than in recent years. The stagflationary nature of the current shock, combined with elevated uncertainty, has contributed to higher volatility and a more uneven performance across sectors. At the same time, higher starting yields and recent spread widening have improved forward return potential, reinforcing the role of fixed income as both an income-generating and diversifying asset class. In this environment, carry may continue to be a significant driver of returns, while episodic volatility may create opportunities for selective positioning.

Rates outlook: rangebound with a mild steepening bias

We expect the 10-year Treasury to remain in a relatively broad range of roughly 4.0% to 4.5% in the near term. Slower growth and the potential for eventual policy easing once inflation stabilizes may limit upward pressure on yields, while elevated fiscal deficits and Treasury supply concerns argue for continued caution around the long end of the curve. In this environment, duration is unlikely to be the primary source of return, and we favor intermediate maturities and curve positioning over aggressive long-end exposure.

Return profile: income still dominates

The first quarter reinforced a simple but important point: in a higher-rate world, fixed income does not need a large rally to generate attractive returns. Income remains the foundation of the asset class. At the same time, the market weakness late in the quarter improved the entry point in several sectors, increasing the potential for capital appreciation.

This is also an environment in which dispersion is increasing. Broad market exposure is less attractive than it was when spreads were tighter and volatility was lower. In our view, returns from here are more likely to come from careful sector selection, structural advantages, and security-specific opportunities than from broad beta exposure alone.

Credit outlook

Corporate credit fundamentals remain broadly stable, but the picture is becoming more uneven. In investment grade, balance sheets are still generally healthy, and all-in yields remain attractive. However, margins are no longer improving across the board, and weaker credits are beginning to show more strain than stronger issuers. That argues for maintaining a quality bias, particularly within BBB-rated credit and more cyclical industries.

In high yield, higher-quality segments continue to offer a more attractive risk-reward tradeoff than lower-quality credit. Wider spreads have improved compensation, but not all parts of the market have repriced equally. We continue to favor the upper tier of high yield, where carry remains compelling and refinancing risk is more manageable.

We remain more cautious on leveraged loans. Their floating-rate structure provided relative support in the quarter, but that same feature continues to pressure weaker borrowers. In our view, loans remain more vulnerable in a slowing growth environment, especially where issuers face margin pressure, elevated leverage, or business-model uncertainty. That caution extends to parts of the market adjacent to private credit, where transparency, valuation discipline, and refinancing flexibility may prove increasingly important as the year progresses.

Global Fixed Income & Macro 2Q2026

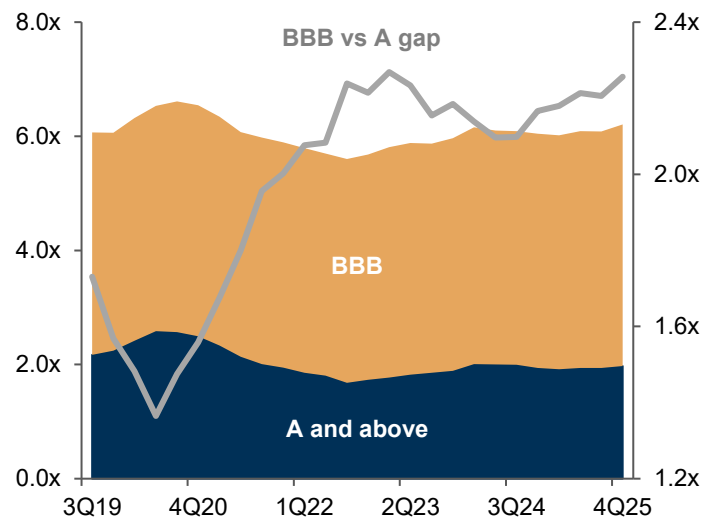
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While a sharp deterioration in credit is not our base case, spread widening risk has increased, particularly in lower-quality segments and in sectors where refinancing needs are rising into a still-restrictive funding backdrop.

Conclusion

The first quarter of 2026 did not undermine the case for fixed income. It refined it. The environment remains favorable for income generation, but the path forward is likely to be less forgiving for lower-quality credits and broad beta exposure. In our view, public fixed income has regained its role as a meaningful source of income and portfolio diversification, but the market is increasingly rewarding selectivity, liquidity, and balance-sheet strength. Accordingly, we believe that maintaining a focus on income, quality, and liquidity remains critical as markets navigate a more uncertain macroeconomic and policy landscape.

Figure 3: Rising leverage gap between AAA-a and BBB issuers | gross leverage



Source: JP Morgan

Emerging Markets 2Q2026

War and peace

The war involving Iran has unleashed a sharp supply shock that extends well beyond oil and gas. Disruptions now affect a broad range of petrochemical products, from fertilizers to helium, compounding pressure across global production chains. Prices reacted swiftly: Brent crude traded well above \$100¹, while freight rates surged as shipping routes adjusted to constrained passage through the Strait of Hormuz.

More recently, however, markets have responded positively to the agreement on a two-week ceasefire and the reopening of the Strait of Hormuz. Brent crude has fallen back below \$95¹, while sovereign credit, rates, and FX markets have rallied sharply as investors unwind some of the geopolitical risk premium that had built up during the conflict. That said, it is still too early to conclude that the shock has fully reversed. Much will depend on whether the ceasefire holds, whether shipping flows normalize in practice, and whether negotiations continue to move toward a more durable de-escalation.

The macro impulse from Iran war is stagflationary. Rising input costs threaten to slow growth just as inflationary pressures begin to re-emerge, placing policymakers in an increasingly uncomfortable position. However, the economic fallout is far from uniform. The shock is reinforcing a familiar fault line between net energy exporters and net energy importers, a divergence that is particularly pronounced across emerging markets.

The rally in oil prices inevitably revives memories of 2022, when Russia's invasion of Ukraine triggered a sharp spike in energy prices and a broad-based sell-off across emerging market assets. That episode exposed vulnerabilities in external balances, pushed inflation sharply higher, and coincided with rapid tightening in global financial conditions. Market stress was swift and indiscriminate: sovereign spreads widened by roughly 140bp¹ within weeks as investors reassessed risk across the asset class.

1. JP EMBIG Index, via Bloomberg

So far, the reaction has been notably more restrained. Since the start of the current conflict, emerging market sovereign debt spreads at the time of writing roughly 25bp wider compared with the end February. This more measured response reflects a fundamentally different starting point. Global interest rates are already much higher, fundamentals have been on the mend, and investor positioning is less crowded.

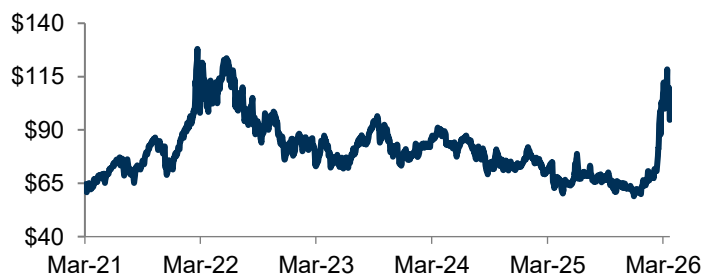
Market pressure has also been more selective. Stress has concentrated in countries with direct exposure to the conflict and among structurally vulnerable energy importers. In contrast, oil exporting economies, particularly those outside the immediate theater of conflict, have generally outperformed.

Figure 1: EM sovereign debt spread



Source JPM EMBIG Index, via Bloomberg

Figure 2: Crude oil price | Price per barrel



Source JPM EMBIG Index, via Bloomberg

Taken together, these dynamics argue for caution rather than alarm. While geopolitical uncertainty and elevated energy prices warrant close monitoring, current conditions do not point to a repeat of the broad-based emerging market dislocation seen in 2022. This adjustment is more targeted, reflecting both the nature of the shock and a markedly different global macro and market backdrop.

Emerging Markets 2Q2026 (cont'd)

Emerging markets show increased fundamental resilience

Emerging markets were once among the most vulnerable segments of the global economy, prone to sudden stops in capital flows that triggered currency collapses, inflation spikes, and painful policy tradeoffs. Over time, however, the asset class has evolved. Stronger monetary frameworks, more credible fiscal policies, more flexible exchange rates, and tighter financial regulation have materially improved resilience.

The stress tests of recent years, from the pandemic to the global rate shock of 2022, exposed weaknesses but also forced adjustment. Many sovereigns responded by tightening policy, allowing greater exchange rate flexibility, rebuilding foreign exchange reserves, and strengthening balance sheets, often through IMF led programs. As a result, a number of emerging markets enter the current shock with meaningfully stronger buffers than in the past.

That said, a new test is now taking shape. Governments across emerging markets are moving to cushion the impact of higher energy costs through subsidies, tax cuts, and other interventions that provide near term relief but risk slowing fiscal consolidation. Measures to curb energy demand may help limit inflation in the short run, but if sustained, they could weigh on productivity and medium term growth.

As a result, even though fundamentals are stronger, we believe a prolonged shock would still revive familiar pressures: strained public finances, draws on foreign exchange buffers, and higher costs of external borrowing, all against the backdrop of debt burdens that remain elevated relative to pre pandemic levels.

The longer the conflict persists, the greater the drag on fiscal accounts

If the shock were to persist, fiscal risks across emerging markets would inevitably rise. For now, however, the impact appears contained. Many EM countries enter this episode with stronger fiscal frameworks than in the past, providing useful safeguards against abrupt deterioration.

The main areas of vulnerability lie among net energy importing economies with a history of intervening in fuel, electricity, and other energy related markets, where subsidies and tax relief can quickly erode public finances if elevated prices endure. These risks are amplified in countries with weaker external positions, particularly where subsidy reform remains incomplete or political constraints complicate adjustment.

By contrast, fiscally stronger economies are better placed to absorb temporary intervention, while net energy exporting emerging markets remain relatively well insulated. In parts of Latin America, Africa, and Asia, higher commodity revenues provide a meaningful offset, helping to contain the fiscal cost of support measures. This divergence underscores a broader reality: resilience across emerging markets is no longer uniform, but increasingly shaped by energy exposure, policy credibility, and the willingness to prioritize medium term stability over near term relief.

That said, a new challenge is beginning to emerge. Governments across emerging markets have already begun deploying measures to cushion the impact of higher energy prices: steps that carry a fiscal cost. Fuel subsidies and tax cuts may offer short term relief, but they weigh on budgets at a time when fiscal consolidation remains challenging for many sovereigns. As a result, even with stronger fundamentals and energy prices still below the extremes of 2022, a prolonged shock would bring familiar pressures back into focus: widening fiscal strains, increased reliance on foreign exchange buffers to smooth currency weakness, and higher external financing costs, all against a backdrop of debt burdens that remain elevated relative to pre pandemic levels.

Markets turn hawkish, but central banks remain in “wait and see” mode

The current supply disruptions pose a risk of a synchronized tightening of monetary policy across emerging markets, as central banks move to anchor inflation expectations and shore up financial stability. That risk cannot be dismissed should energy disruptions persist. For now, however, EM central banks are more likely to adopt a largely “wait and see” approach rather than risk responding to the supply driven shock prematurely.

Emerging Markets 2Q2026 (cont'd)

This is supported by the elevated real policy rates across emerging markets providing room to assess the fallout before adjusting monetary policy.

In addition, demand pressures are far more contained than in 2022, reducing the risk of second round effects that were a key driver of inflation during that episode. Back then, energy price shocks coincided with post pandemic reopening, strong fiscal support, high accumulated savings and strong wage growth. Today's environment is very different, with softer labor dynamics and tighter financial conditions limiting pass through into wage-inflation cycle.

Both factors suggest that current market pricing overstates both the likelihood and the scale of EM policy tightening. Recent moves in rates markets appear driven more by positioning and short term dislocations than by a realistic assessment of central bank reaction functions. Provided the shock does not prove long lasting, fiscal deterioration should also remain manageable, limiting the risk of a sustained need in monetary policy tightening.

Alpha opportunities in EM sovereigns

Amid heightened market volatility driven by geopolitical risks and sharp swings in commodity markets, our focus is on countries where fundamentals are improving and where political developments, market access, and rating trajectories offer asymmetric upside. In this context, we hold a constructive view on Ecuador and Argentina.

In both cases, strong political commitment to reform under IMF programs is reinforced by constructive relations with the United States, providing an important external anchor. As commodity exporters, both countries also stand to benefit from higher prices, improving the macro backdrop.

We are similarly encouraged by recent polling in Hungary, which suggests that the opposition has a credible chance of winning next year's elections. We believe markets appear to underprice the probability of a favorable political outcome that could unlock EU fund flows and materially improve the outlook for local assets, creating asymmetric upside potential. We also see value in Suriname, where recent liability management efforts have addressed key investor concerns and offer attractive compensation for investors willing to support a multi-year reform agenda.

Beyond these cases, we expect continued rating improvements in Ivory Coast, supported by robust economic growth and improved macro stability. We also believe in the relative value in oil exporting economies such as Angola and Nigeria, where higher energy revenues provide a buffer, and where Nigeria in particular, is showing encouraging progress on fiscal reforms and tax collection. Finally, in Romania, while downgrade risks persist, current valuations more than compensate investors for this uncertainty, offering what we believe is an attractive risk reward profile at current levels.

High Yield 2Q2026

After positive returns in January and February, it seemed all but certain that the ICE BofA US High Yield Index would extend its streak of 13 consecutive positive quarters, its longest since 1997. The outbreak of war in Iran put an abrupt end to this. The Index posted a negative 1.2% return in March alongside most asset classes, including a 5.1% loss for the S&P 500. (ICE BofA US High Yield Index has since recouped this loss in April, gaining 1.8% through April 14).

Before the outbreak of conflict took center stage, leveraged credit markets were focused on another risk: the disruptive potential of AI. Fears that AI could displace traditional Software as a Service (SaaS) companies has already been recognized by the markets, and many SaaS companies experienced significant declines in their valuation in 2025; for example, cloud-based software company Salesforce, Inc.’s shares declined about 21% in 2025.¹

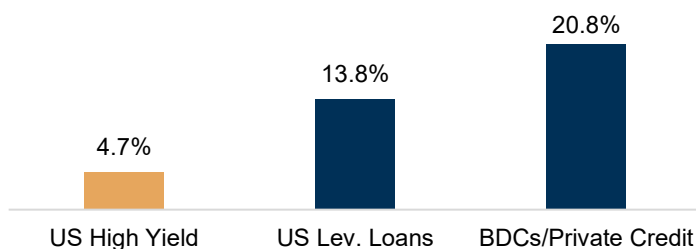
In 2026, the AI fears have intensified and spread beyond the “SaaSocalypse”. Every recent release of new AI tools by Anthropic or ChatGPT seems to have sparked a new wave of fear in industries beyond software and information technology. For example, the February release of Insurify, a ChatGPT app that enables users to easily compare insurance quotes, triggered fears of disintermediation of insurance brokers and selling in their bonds.

Financial sponsors have long been drawn to software and IT services companies due to their recurring revenues, high margins, and fragmented nature of those industries. These companies proved to be more resilient during the pandemic and tariffs, which has added to their appeal. As a result, technology, software, and IT services represent a much higher portion of the leveraged loan and private credit markets compared to high yield, as seen in Figure 2.

1. Source: Bloomberg 2. Source: JP Morgan 3. ICE BofA Indices

The leveraged loan market’s exposure is more than twice that of high yield; private credit’s nearly four times.

Figure 1: Technology/software weight % of market

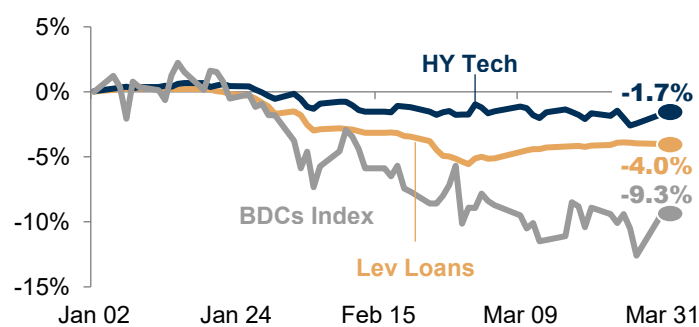


Data as of January 31, 2026
Source: J.P. Morgan Research

Software companies with high yield bonds have stronger credit profiles than their leveraged loan counterparts. 42% of software high yield bonds are rated BB, compared to just 10% of loans. Meanwhile, 47% of software loans are rated B-, compared to just 19% of bonds.² The credit profiles of the software companies in the private credit markets are likely weaker. As a result, high yield technology bonds performed much better than loans and the Business Development Company Index as seen in the chart below.

Unsurprisingly, riskier bonds underperformed meaningfully given intra-quarter volatility. CCC and below bonds declined 2.1%, compared to modest losses of 0.4% for BBs and Single-Bs.³

Figure 2: Q1 2026 performance



As of March 31, 2026.
BDC Index is The MVIS® US Business Development Companies Index (MVBDC) - tracks the performance of the largest and most liquid Business Development Companies that are listed and incorporated in the United States. This is a modified market cap-weighted index, and only includes companies that qualify as a Business Development Company.
Source: Bloomberg US Leveraged Loans Index, Bloomberg US Corporate High Yield Index

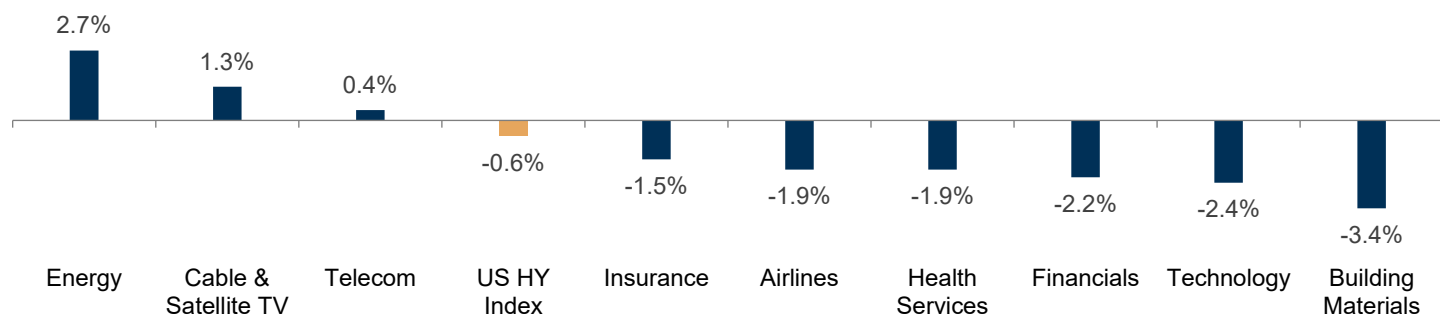
High Yield 2Q2026 (cont'd)

Sector dispersion remained elevated, driven by AI, the Middle East conflict, and sector specific weakness. As seen in the chart below, Energy was the best performing high yield sector as a direct beneficiary of war-induced higher oil prices, which also negatively impacted Airlines. AI disruption fears not only pressured Technology, but also companies within Insurance and Health Services. Outside of AI and war, Financials were lower as certain

consumer financing companies were hit by both regulatory concerns and charge-offs due to bad loans. Building Materials companies declined on continued softness in end-market demand.

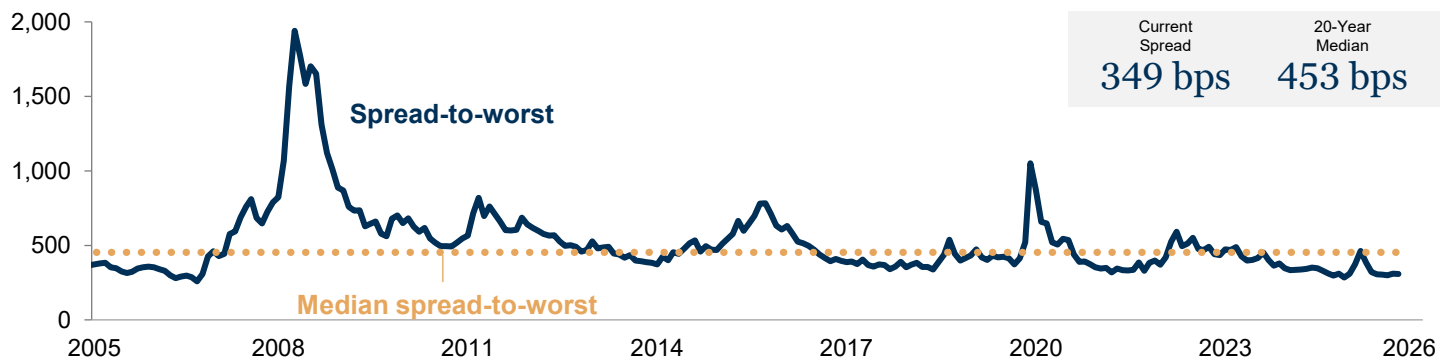
High yield valuations remain elevated. The spread to worst of the ICE BofA US High Yield Index finished Q1 2026 at 349 bps within the post-GFC “non-panic” range of 325-525 bps. (See Figure 4)

Figure 3: Q1 2026 performance by sector



Data as of March 31, 2026 Index: ICE BofA US High Yield Index. Source: ICE Data.

Figure 4: US high yield market spreads



Data as of March 31, 2026. Index: ICE BofA US High Yield Index. Source: ICE Data.

Convertibles 2Q2026

Performance

The U.S. convertible market finished the first quarter of 2026 with a remarkable performance. What made the performance noteworthy was the benchmark's 3.72% rise despite not only a decline in equity markets but also a coincident rise in interest rates and a corresponding drop in the high yield and Treasury bond markets. Generally, a drop in both equity and bond markets would make a decline in convertible securities a near certainty. However, several unusual occurrences in the first quarter allowed convertibles to outperform nearly every other asset class, a continuation of the trend we experienced in 2025. For the first quarter, the ICE BofA U.S. Convertibles Index's 3.72% advances compared to the 4.35% decline in the S&P 500 and the 6.96% loss in the NASDAQ. The smaller cap Russell 2000 posted a small gain of .92% for the quarter which provided a small tailwind to the convertible market, as many convertible securities in the Index emanate from small and mid-cap issuers. The main driver of convertible performance, however, was the sharp rise in several large Index constituents seen as beneficiaries of the buildout of A.I. data centers. The Index's largest constituent, Lumentum Holdings, a manufacturer of optical equipment used in data transmission, rose 90% in the first quarter alone after gaining more than 300% in 2025. In addition, data storage companies, Seagate Technologies and Western Digital, two other large Index constituents, rose 42% and 57% respectively, in the first quarter following very strong advances in 2025 as well. In addition, the U.S. convertible market was not burdened by the weak performance of the so-called Magnificent Seven stocks which have an outsized impact on the large cap equity indices. The stocks of all seven companies posted first quarter declines and enhanced the relative performance of the U.S. convertible market versus equity indices such as the S&P 500 and the NASDAQ Composite.

While the first quarter gains versus equities are remarkable, they have been relatively concentrated in the bonds of a few companies tied to the buildout of data centers, data storage, and power demand related to the needs of AI infrastructure. It may be difficult for those gains to broaden out in an environment of high energy prices, higher interest rates, and concerns related to private credit investments.

*(performance data from Bloomberg)

However, if the war in the Middle East can be ended relatively quickly on terms seen as favorable to the U.S., a broad rally in equities and equity-linked securities such as convertibles is likely.

Issuance

For the first quarter of 2026, new issuance totaled \$26.0 billion (*from Bank of America data*), ahead of last year's \$15.8 billion of new issuance for the same period. Issuance totals in the first quarter were impacted by Oracle Corporation's \$5 billion convertible preferred share issue, the proceeds of which will be used to fund its buildout of AI computing and data storage facilities. Additional issuance came from companies seeking to refinance existing convertible debt. We expect the pace of new issuance to remain strong through the balance of the year as numerous bonds that came to the market during the pandemic-fueled issuance spree of 2020-2021 approach maturity and need to be refinanced. However, a prolonged slump in equities may dampen issuance somewhat from other companies.

Positioning and Outlook

We are surprised by the convertible market's strong performance so far this year, particularly within the backdrop of falling stock and bond markets. Surprised but pleased. Despite the narrow scope of the convertible market's advance, we have kept pace with the Index even with our relatively conservative portfolio positioning which outperformed the Index on most down days. Some of our large data center and storage holdings were benchmark winners, which rose by avoiding anything linked to cryptocurrency such as MicroStrategy and Coinbase, which continue to fall in value even after last year's very poor performance. We remain overweight in the Healthcare, Consumer Staples, Information Technology sectors, market-weighted the Communication, Consumer Discretionary, Real Estate, Energy sectors, and underweight Financials, and Utilities. We believe that in the absence of a prolonged spike in energy prices, the economy can maintain its pace of low single-digit GDP growth combined with relatively low, sub-5% unemployment. We continue to believe that our process, which emphasizes strong company fundamentals and reasonable valuation, will outperform over a complete market or economic cycle.

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INDEX DEFINITIONS

The ICE BofA All U.S. Convertibles Index is an unmanaged index that consists of convertible bonds traded in the U.S. dollar denominated investment grade and non-investment grade convertible securities sold into the U.S. market and publicly traded in the United States. The Index constituents are market value weighted based on the convertible securities prices and outstanding shares, and the underlying index is rebalanced daily.

JMP EMBIG Index — The J.P. Morgan Emerging Markets Bond Index (EMBI) is a family of benchmark indices tracking liquid, U.S. dollar-denominated debt instruments issued by emerging market sovereign and quasi-sovereign entities. They measure total return performance, including Brady bonds, Eurobonds, and traded loans, acting as a standard for portfolio management in this sector



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