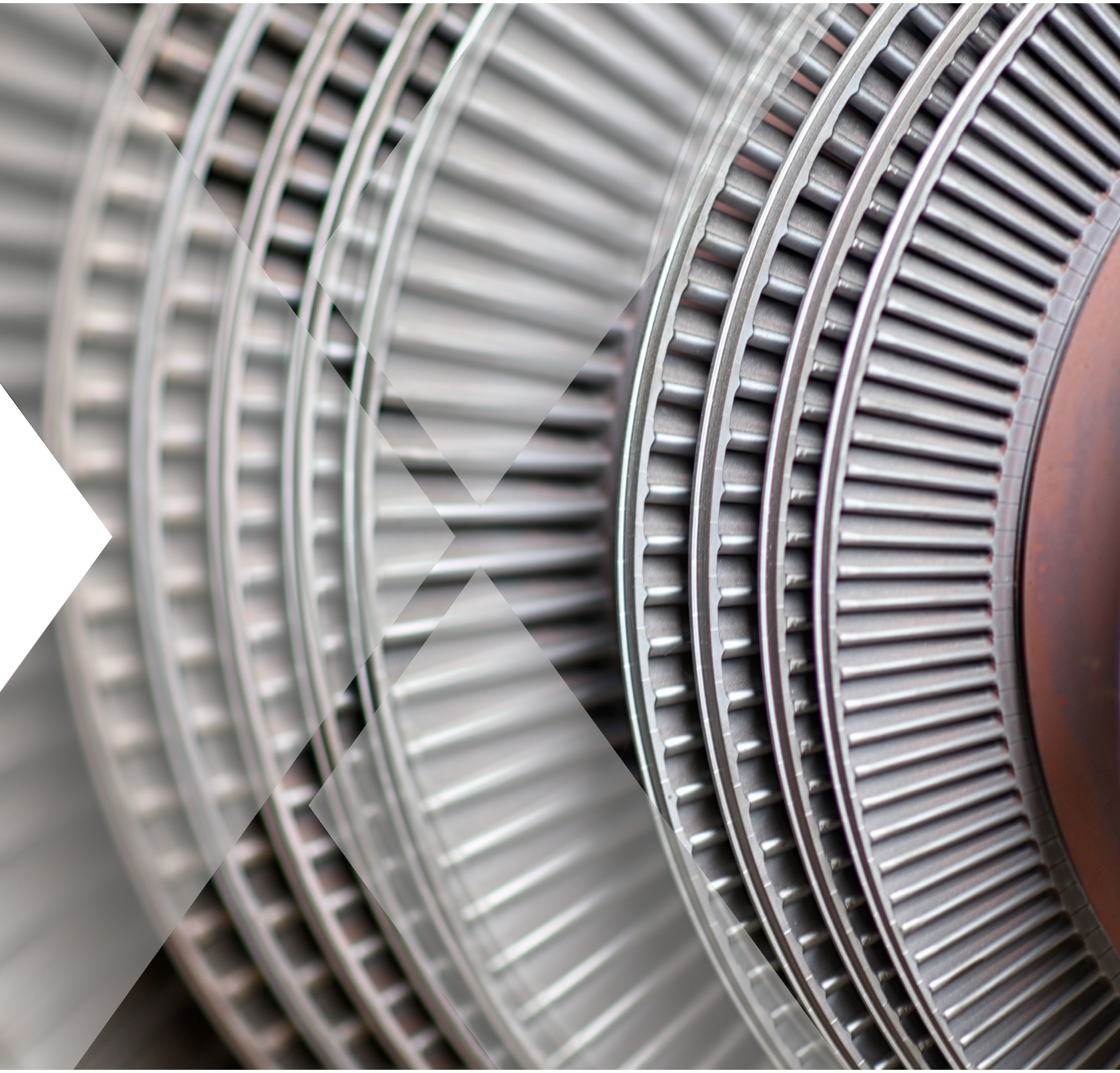
# Mid-Year Credit Outlook 2026

June 2026



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# Introduction

## Coming into 2026, our central thesis was one of continued resilience in global fixed income markets.

This expectation was predicated on a stable macroeconomic backdrop of above-trend US growth, supported by fiscal stimulus and AI-related investment, with the Federal Reserve (Fed) delivering two or three US interest rate cuts to take the policy rate towards 3.25% by mid-year. Europe was framed as steady. We anticipated long-end yields reflecting fiscal deficit concerns, and credit spreads remaining broadly rangebound with modest near-term widening pressure from heavy issuance.

In this context, our preference had been for higher-quality credit, shorter-to-intermediate duration, and selective exposure across sub-asset classes, with strains in the private credit market flagged as a key contagion risk.

The path so far in 2026 has been more disruptive than our base case. The outbreak of conflict in Iran in late February has driven Brent oil prices above US$100 a barrel, raising headline inflation and so forcing the Fed into holding interest rates – markets now price no further cuts in 2026. While credit spreads have remained remarkably resilient and stay at cycle tights, long-end core yields have risen.

New Fed chair Kevin Warsh arrives with a stated ‘regime change’ agenda – a smaller balance sheet, less forward guidance, fewer Fed speakers and tighter coordination with the Treasury – and a clear preference for lower interest rates. This will be harder to deliver than at any point in the past 18 months as Warsh inherits an energy-driven inflation shock that monetary policy cannot directly address.

US consumer price inflation (CPI) rose to 3.8% in April, the highest since 2023 and up from 3.3% in March, with core inflation at 2.8%.[1] The Iran conflict is the proximate cause: gasoline prices are up nearly 50% since February.[2] Inflationary pressure is also visible in shelter, food and airfares. Rates futures are now assigning some probability that interest rates will go up, not down, and real wages have turned negative.[3] The outlook for US interest rates is unusually difficult to judge, and Fed credibility will be tested in real time.

In this mid-year outlook, we share our perspectives on each of the main sub-asset classes that we focus on within fixed income and identify key watch items for the second half of 2026.


1 Bloomberg, as at 30 April 2026
2 Bloomberg, as at 22 May 2026
3 Bloomberg, as at 22 May 2026



# High yield credit

## The benign growth-and-disinflation story that anchored our initial 2026 outlook for high yield bonds has been disrupted by the inflationary spillover of the Iran conflict. Yet the structural case for high yield remains firmly intact, in our view.

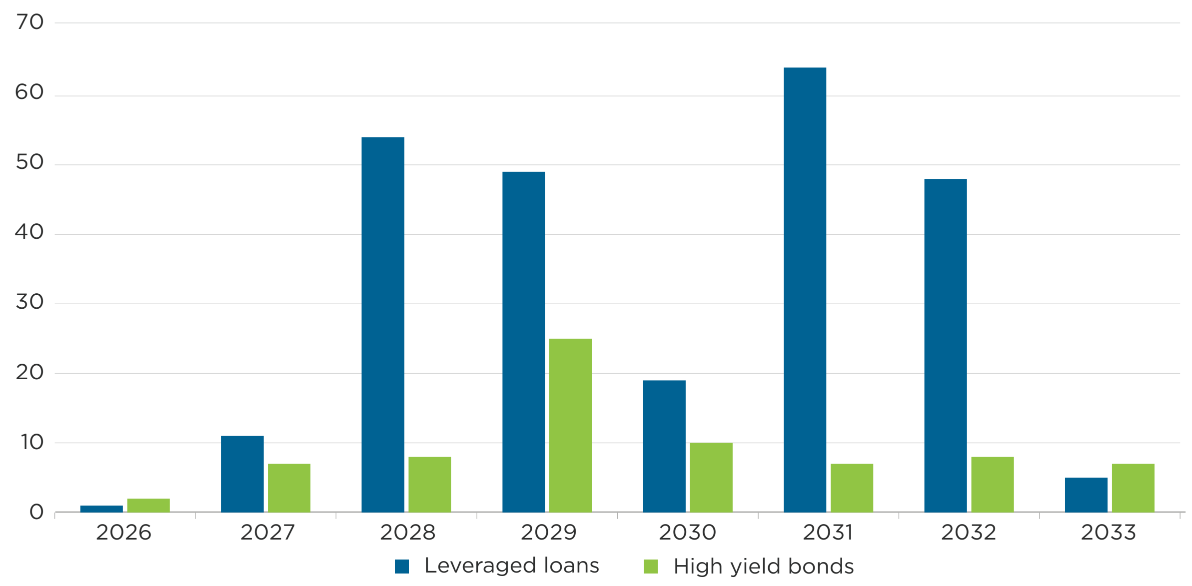
Absolute yields are elevated (see chart below), providing meaningful carry and a substantial breakeven cushion. Default rates remain low and credit failures are mostly idiosyncratic, rather than reflecting sector-wide stress.[4]

The structure of the high yield market has also improved materially over past decades: the ICE BofA Global High Yield Index is now tilted towards ‘BB’-rated bonds (the highest non-investment grade rating), duration sits near historic lows (at around three years) and the debt maturity wall has been pushed out to 2028 and beyond.[5]

The bifurcation between disciplined public credit and stressed private credit – where defaults were estimated to be 9% in 2025 – has widened more starkly than anticipated.[6] The collapse of First Brands and Tricolor, and subsequent fraud indictments brought against executives in both US businesses, lends support to ‘mark to myth’ valuation concerns. Since then, the non-traded business development company (BDC) structure for US private credit investments has been tested by redemption requests that have forced some managers to restrict withdrawals. Structural guardrails have functioned as designed, but the liquidity expectation embedded in the non-traded BDC wrapper has been meaningfully re-rated.

### A looming maturity wall adds to software concerns in loans

**Value of US software sector debt maturing by year (US$bn)**




Source: JP Morgan data, March 2026

4 JPMorgan Default Monitor, May 2026
5 Bloomberg, April 2026
6 Fitch Ratings, March 2026

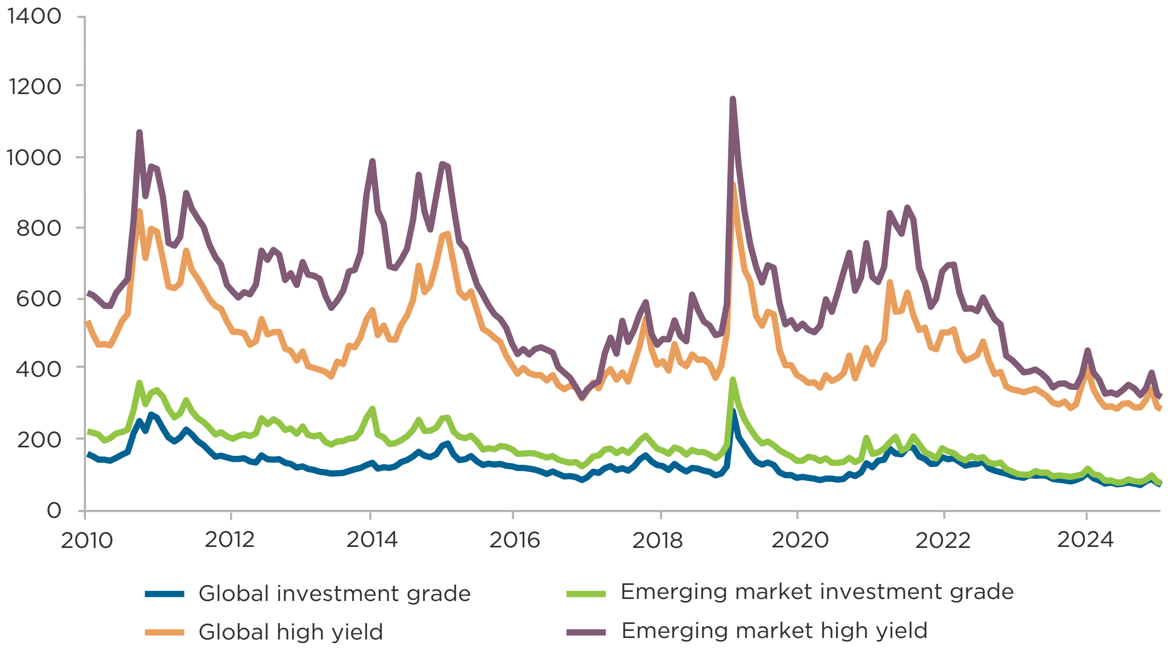
**Past performance is not indicative of future returns.**

A second narrative that we are watching is the potential for AI-driven disruption to software-as-a-service (SaaS) business models (the so-called 'SaaSpocalypse'). High yield exposure to software is comparatively modest: while the sector accounts for only 4.5% of the US high yield universe, its share of the US leveraged loans market is three times greater.[7]

The more material concern is a looming wall of debt maturing in 2028 and 2029 – much of it underwritten at low coupons and elevated leverage – that will require substantial refinancing (see chart below).[8] We continue to see selective opportunities, particularly within AI infrastructure, while remaining cautious on SaaS issuers where terminal economics appear inadequately priced.

### Credit spreads continue to trade at historically tight levels...

Option-adjusted spread to worst by asset class, Jan 2010 to May 2026 (basis points)




Source: Bloomberg, ICE BofA indices. 22 May 2026. ICE BofA Global Investment Grade Index; Global High Yield Index; Emerging Markets Corporate Investment Grade Index; Emerging Market Corporate High Yield Index.

7 JP Morgan data, March 2026
8 JP Morgan data, March 2026



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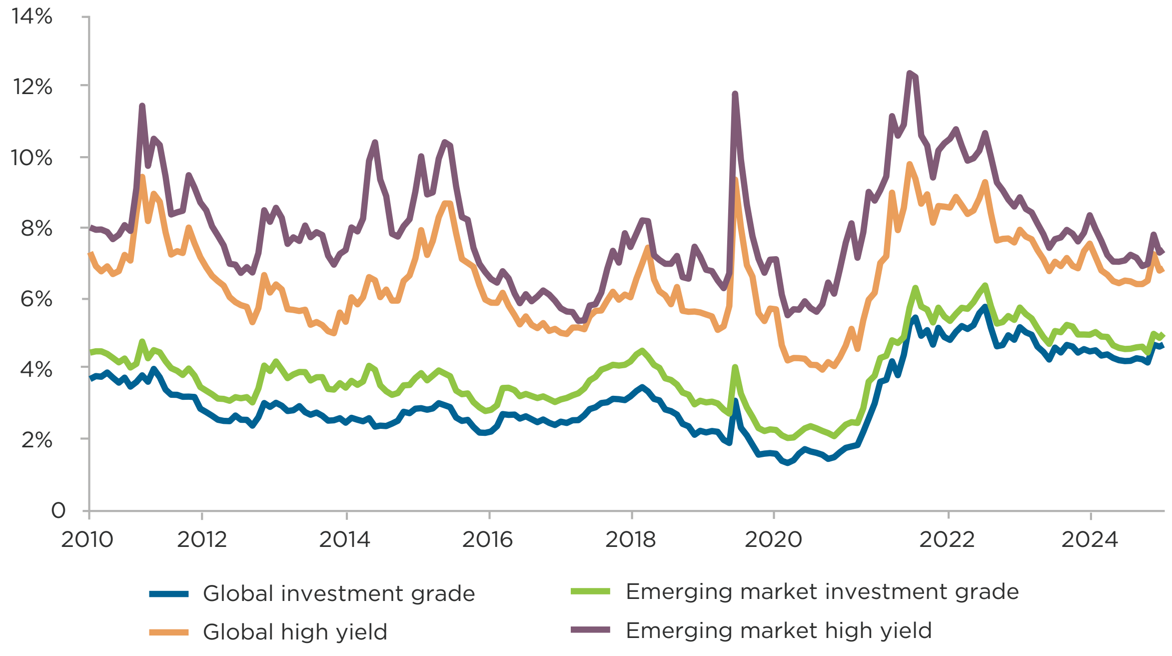
This is not a moment for high yield investors to be complacent. Dispersion is rising and contagion risk from private markets remains. Spreads – which are close to multi-decade tights – do not offer a generous margin of safety.

While the warning signs flagged at year-end are growing louder in private credit, public high yield fundamentals so appear resilient. Investors are also compensated for risks with what we believe to be relatively compelling yields. This supports our constructive, if increasingly selective, stance on the asset class.

### ... but yields remain elevated - and have ticked up

Yield to worst by asset class, Jan 2010 to May 2026 (%)




Source: Bloomberg, ICE BofA indices. 22 May 2026. ICE BofA Global Investment Grade Index; Global High Yield Index; Emerging Markets Corporate Investment Grade Index; Emerging Market Corporate High Yield Index.

# US investment grade credit

## The US economy remains resilient, corporate earnings are strong, balance sheets look fundamentally healthy and technical factors remain generally supportive, despite minor signs of weakening.

While this environment has been supportive of credit, two major shifts have emerged: a massive surge in AI-related data centre issuance and conflict in the Middle East.

Data centre financing is booming: it is estimated that investment grade debt issuance from the 'hyperscale' cloud computing providers will exceed US$200bn this year, up from US$120bn in 2025.[9] While the market has largely digested this supply, some deals, such as Meta's recent US$25bn offering, have required borrower concessions.[10] We are monitoring this trend closely, remaining highly selective in the primary market for bonds issued by 'hyperscalers', to whom we maintain an underweight stance.

Meanwhile, geopolitical events have raised the possibility of a US interest rate hike. While this materially raises the risk profile for investment grade credit, the market has largely looked past the conflict after the initial shock, focusing instead on stable economic data and strong corporate earnings. Indeed, investment grade credit spreads are slightly tighter than at the start of the year.[11]

Given this backdrop, we retain our preference for high-quality corporate issuers with strong cash flow generation. We remain highly vigilant regarding elevated geopolitical risks and softening technical indicators, though.


9 Barbuscia, D., 21 May 2026: Big Tech's AI Debt Binge Tests High-Grade Market, Barclays Says. *Bloomberg*
10 Mutua, C., Gambale, M. & Gurumurthy, G., 30 April 2026: Meta Sells $35 Billion of Debt as Investor Worry, Fatigue Builds. *Bloomberg*
11 Bloomberg data, as at 22 May 2026

# Securitised products

## In the context of tight investment grade credit spreads, we believe that securitised products offer a compelling, but increasingly selective opportunity set heading into the second half of 2026.

Despite a subdued US housing market constrained by lack of affordability, mortgage market fundamentals remain resilient. Residential mortgage-backed securities (RMBS), in particular, continue to provide stable income levels. Commercial mortgage-backed securities (CMBS) meanwhile appear to offer compelling carry as fundamentals improve, in our view, although the recovery is uneven across sectors and further spread tightening potential is limited.

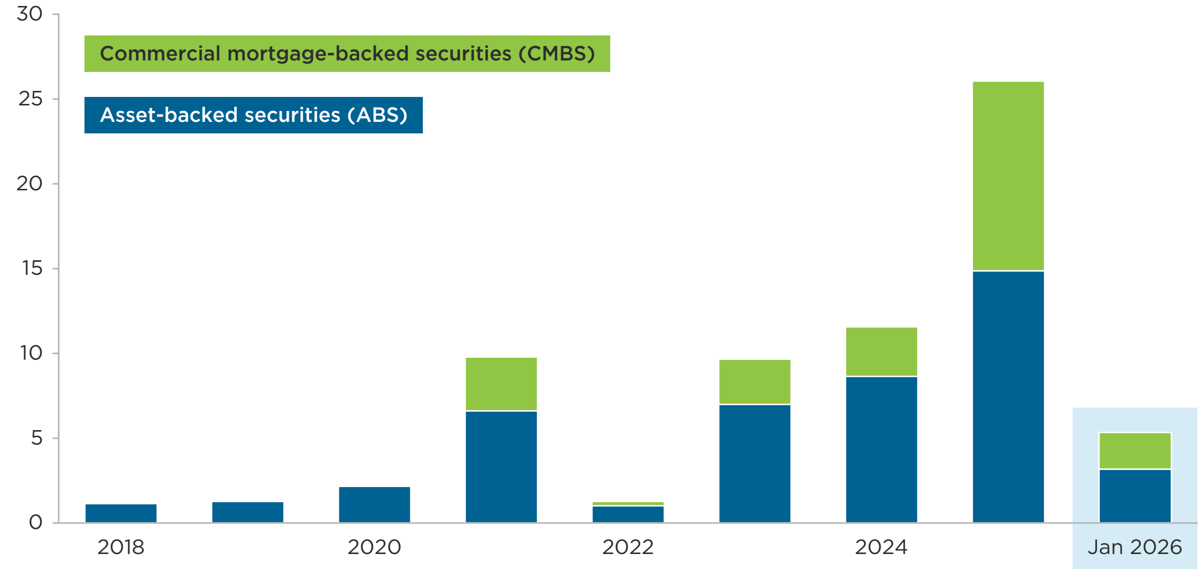
A divergence is emerging within asset-backed securities (ABS). Digital infrastructure ABS and CMBS are benefiting from strong secular demand tied to the AI buildout (see rising issuance in the chart below), while consumer ABS is increasingly pressured by inflation and weaker lower-income borrowers. A similar split characterises the market for collateralised loan obligations (CLOs): senior 'AAA'-rated tranches are supported by strong demand, due to their attractive carry and structural protections, while lower-rated tranches face challenges from increased credit dispersion and potential AI-driven credit deterioration.

Overall, supportive technical factors for securitised products – including deregulation, strong investor demand and elevated yields – are offset by headwinds from persistently high interest rates and emerging AI-related disruption risks.

In this context, we maintain a preference for higher-quality assets and emphasise disciplined, bottom-up credit selection as macroeconomic and geopolitical uncertainties continue to shape market direction through the remainder of 2026.

**Securitising the engine rooms of AI**

**Issuance of data centre ABS and CMBS (US$bn)**




Source: BofA Global Research, February 2026

# Emerging market credit

The structural case for emerging market credit remains intact, in our view. Around 60% of the hard-currency universe is investment grade, leverage multiples sit below developed market peers, and default rates are expected to remain subdued.

Further, high-quality corporate issuers trade wider than their fundamentals warrant as valuations are typically capped, in effect, by those of local government bonds. Combined with negative net supply and – in many emerging markets – supportive structural growth dynamics and easing monetary policy, we believe the asset class offers a compelling carry profile, overall.

As we highlighted earlier this year, emerging markets' return to favour is reflected in renewed investor interest: investment flows into emerging market fixed income strategies were positive in 2025 after three years of net outflows.

The picture for the rest of 2026 is nuanced. Spreads are close to their tightest since 2007 with all-in yield, rather than spread compensation, doing most of the work in supporting investor demand. Nonetheless, in our view underlying credit quality is healthy, with strong bank and insurer results across the Middle East and Asia as well as manageable 2026 refinancing needs.

The dominant near-term risk facing emerging market credit, overall, remains the Middle East conflict. The longer the Strait of Hormuz remains effectively closed, the more second-order effects surface; fertiliser supply chains, petrochemical margins and food-price transmission all bear monitoring.

Also, monetary policy across emerging markets is more mixed than it appeared at the start of 2026 as elevated oil prices complicate the disinflationary path. Oil-exporting Colombia has raised interest rates twice this year, for example. We still expect further interest rate cuts in Brazil, Turkey and selected other markets, however.

In this context, we continue to favour high-quality credits and, given tight spreads, believe there is value in protecting against widening spreads. Regional dispersion remains wide, supporting opportunities for active, bottom-up selection in our view.

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**Important Information, continued**

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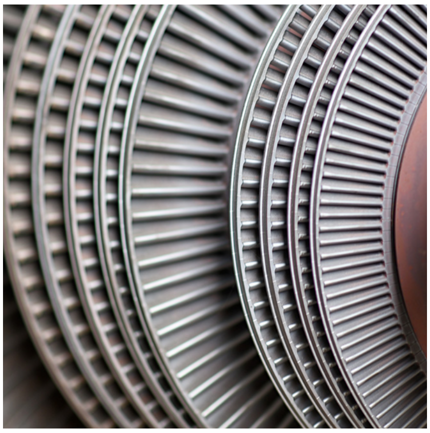

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