2026 Outlook: Fixed Income

Perspectives from the Impax Fixed Income team

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Fixed income outlook

The resilience that global fixed income markets exhibited in 2025 looks set to continue into 2026.

A relatively stable macroeconomic environment should help underpin risk assets. The US economy enters 2026 with above-trend growth expectations, supported by expansionary fiscal policy, continued investment in artificial intelligence (AI) related infrastructure and the prospect of two or three additional interest rate cuts, bringing the policy rate towards 3.25% by mid-year and concluding the final phase of the easing cycle that began in late 2025. Lower mortgage rates should underpin the real estate market while corporate earnings are expected to remain robust. Against this, slowing labour markets and sticky inflation will continue to weigh on the US consumer. Meanwhile companies will look closely at potential efficiency savings through the use of AI, which further clouds the employment outlook.

European growth meanwhile should remain stable in 2026, with Germany's push for additional infrastructure and defence spending offsetting the ongoing challenges facing its automotive industry. The Eurozone benefits from the lower interest rate environment, but the need for budgetary consolidation in many countries (including the UK, too) limits potential for fiscal expansion.

Large fiscal deficits in countries such as the US, UK, France and Japan, together with high debt-to-GDP ratios and worsening demographics, will increasingly be factored into long-term government bond yields. This is one of the drivers behind negative interest rate swap spreads. We recently made the case that swaps now represent the risk-free rate as illustrated by selected high-quality corporates accessing the market through government bond yields.[1]

Cautious optimism for credit

We think credit markets will likely prove resilient in 2026, overall. We expect credit spreads to remain rangebound, albeit with modest widening pressure in the near term due to rising issuance by the technology sector to finance capital expenditure and an anticipated increase in borrowing related to mergers and acquisitions (M&A).[2,3] Given our views on the yield curve, we prefer shorter to intermediate credit duration.

Increased supply of debt is likely to be seen not only in investment grade credit, but also across high yield and leveraged loans. Against this backdrop, we generally favour more highly-rated credits, particularly in high yield where single-name selection remains critical to generating competitive risk-adjusted returns.

Recent defaults in private credit appear to be idiosyncratic in nature but also serve to highlight the need for stronger underwriting of credit risk. Notwithstanding the strength of the high yield market, the risk of contagion cannot be entirely dismissed.

Credit investors – public and private alike – would do well to listen carefully to the warning and focus on the fundamentals.

1 Impax, October 2025: Five reasons why swaps should be the benchmark for US credit spreads – not Treasuries
2 Barbuscia, D., 21 November 2025: Jitters over AI spending set to grow as US tech giants flood bond market. *Reuters*
3 KPMG, 8 December 2025: M&A market expects clear upward trend in 2026

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Key convictions for credit in 2026

Short to intermediate duration:

- Lock in elevated corporate bond yields before further interest rate cuts

Quality over beta:

- Be rigorous in credit selection, especially in high yield, given tight spreads
- Keep duration and risk modest in technology on expected surge in supply
- Position in sectors that will benefit from a lower interest rate environment: financials (larger diversified banks), telecommunications and property
- Favour securitised assets: collateralised loan obligations (CLOs), collateralised mortgage obligations (CMOs) and collateralised mortgage-backed securities (CMBS)

Diversify globally:

- Look to exploit policy divergence and relative value across regions
- Assess relative value versus swaps and government bonds on a currency neutral basis

Sustainability matters:

- Sustain focus on issuer resilience and sustainability factors, which remain central to credit risk assessment and opportunity identification

Past performance is not indicative of future returns.

Below, we share our perspectives on each of the main sub-asset classes that we focus on within fixed income.

1 US investment grade

Resilient economic growth, decent earnings and strong technical factors buoyed US investment grade credit in 2025. This was despite historically stretched valuations.

We do not anticipate that investment grade spreads will tighten materially in 2026. Instead, we believe that it will be a 'carry' environment in which current yield is all-important.

Credit quality continues to remain strong within investment grade. Corporate balance sheets are healthy, overall, but remain vigilant to the risks posed by potential re-leveraging of corporate balance sheets. With higher issuance, technical factors could present a rising headwind in 2026.

Credit spreads continue to trade at historically tight levels...
Spread to worst by asset class (basis points)

Source: Bloomberg data, 18 December 2025. 'US High Yield' = ICE BofA US High Yield Index. 'Euro High Yield' = ICE BofA Euro High Yield Constrained Index. 'Sterling High Yield' = ICE BofA Sterling High Yield Index. 'Emerging Market Corporate' = JPMorgan Corporate Emerging Market Bond Index Broad Diversified. 'US Corporates' = ICE BofA US Corporate Index. Indexes are unmanaged and not available for direct investment.

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2 Securitised products

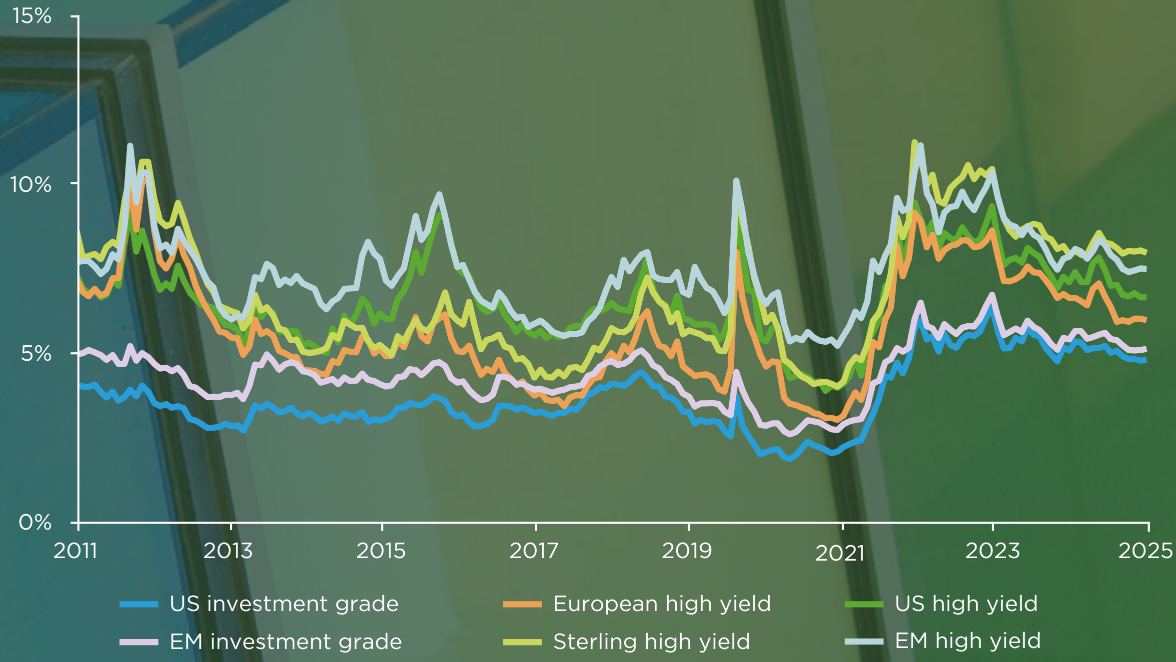
It is our view that there are compelling relative value opportunities within securitised products as we look into 2026.

Consumer credit performance is broadly stable, with loan delinquencies levelling off despite a 'K-shaped' recovery – characterised by divergent outcomes and prospects for high and low-income workers – and weakness within the sub-prime segment. Mortgage credit benefits from resilient home prices and tightened underwriting standards.

Overall, we favour adding exposure to residential credit and non-agency collateralised mortgage-backed securities (CMBS) while maintaining high-quality duration exposure in agency MBS.

... but yields continue to provide a reasonable entry point

Yield to worst by asset class



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3 US high yield

After a volatile but strong year for US high yield, low spreads continue to be offset by relatively high absolute yields.

Looking into 2026, we remain on high alert for potential weakness emanating from private credit markets. This notwithstanding, we remain comfortable with the larger, higher quality companies that the US high yield universe offers, accompanied by greater transparency and liquidity.

4 European high yield

Positive economic growth, accommodative monetary and fiscal policy, and limited inflation all point to a constructive macroeconomic outlook for European bond issuers in 2026.

In terms of company fundamentals, European high yield issuers do not face imminent refinancing needs.

Although spreads are tight, we think this can persist in a higher-quality market. Besides, all-in yields remain elevated, providing investors with the prospect of reasonable returns from carry.

5 Emerging market credit

2025 was a volatile year for emerging market credit, primarily driven by uncertainties concerning trade tariffs. We expect this to subside in 2026 as trade relations between the world's two largest economies, China and the US, show signs of de-escalation. Growth dynamics still appear favourable, particularly outside of China.

Company fundamentals also continue to look robust: defaults are low and expected to stay below their long-term historical average.[4] Corporate leverage is also low relative to previous periods – and is lower than in developed markets.[5]

These strong fundamentals are reflected in tight spreads, which show limited room for further compression.

6 Labelled bonds

We expect issuance of labelled bonds to be flat globally in 2026, having fallen in the first three quarters of 2025 after years on an upward trajectory.[6]

The reversal stems from the US, where corporate issuance of labelled bonds has roughly halved in 2025.[7] There are few catalysts for this trend to reverse in the near term, given the current US political environment and heightened regulatory scrutiny surrounding labelled issuance.

4 JPMorgan, November 2025: Emerging Market Credit Outlook & Strategy 2026
5 JPMorgan, November 2025: Emerging Market Credit Outlook & Strategy 2026
6 Sustainable Fitch, October 2025: Labelled Bond Issuance Slows Further, Transition and Nature Themes Gain
7 Barclays, November 2025: Global Outlook

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