Fixed Income Insights

NORTH AMERICA
US & CANADA EDITION

MONTHLY REPORT | **OCTOBER 2025**

Credit still in a sweet spot after Fed & BoC policy shift

Both the Fed and BoC re-focussed on weaker labour markets in Q3, easing rates. Looser financial conditions & lower rates drove risk asset gains, including credit, despite growth downgrades. HY & financials outperformed. Curves steepened in longs, but 10s/2s curves have stabilised. Credit, munis & provis, all outperformed Canadian govts. as spreads fell.

Macro and policy backdrop – Fed and BoC rate cuts signal labour market concerns

Recent labour market softening drove September easing moves, although US GDP growth remains robust in Q3. Lower inflation gives the BoC more policy options. (pages 2-3)

US IG & HY credit – Banks perform strongly in IG. Fallen angels becoming rarer?

Banks and asset-backed lead IG returns. Fallen angel share in HY at 23 yr low. (pages 4-5)

Canadian govt bonds, provis & munis – Curve steepens in longs, but not mediums

Signs emerge of 10s/2s stabilising in Q3. Muni spreads tighten again. (page 6)

Canadian IG & HY credit – Credit remains in sweet spot after BoC rate cut

Greater yield protection in Canadian credit, as share of overall yield. (page 7-8)

Performance – Treasuries rallied in Q3, on the Fed rate cut, credit still robust

The Fed rate cut boosted longer Treasuries, but shorts and mediums mostly outperformed in G7. Canadian credit, munis and provis outperformed govt bonds YTD. (pages 9-11)

Appendix (from page 11) Global bond market returns, historical bond yields, bond market durations and market values and foreign exchange returns.

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Chart 1: Long-dated yields fell in Canada and the US in Q3, relative to the Eurozone and UK, where yields increased, despite a BoE rate cut. Debt issuance weighed on European govt markets, led by France.

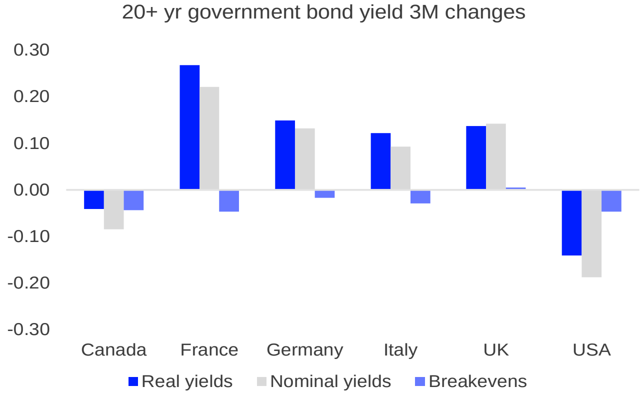
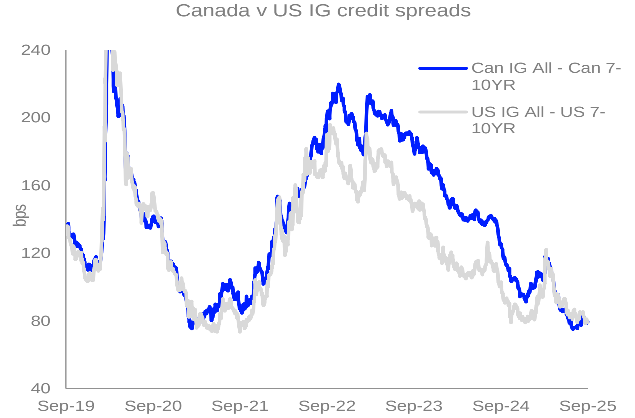


Chart 2: Canadian IG credit spreads have fallen more than US, since 2022-23, despite Canadian 7-10 yr govt yields falling more than US. So Canadian spreads still offer more protection versus risk-free rates.



Source: FTSE Russell and Datastream. Other data as of September 30, 2025. Past performance is no guarantee of future results. This report should not be considered 'research' for the purposes of MIFID II. Please see the end of the report for important legal disclosures. Bond market data is derived from FTSE Fixed Income Indices. See Appendix for list of indices used for each market.

Macroeconomic Backdrop – Growth and Inflation Expectations

Consensus growth forecasts have priced in tariffs of 15-20%, though some economies are more resilient than others, and the impact will be cushioned by ongoing G7 rate cuts, relatively easy fiscal policy and easier financial conditions (see page 3). The Atlanta Fed Nowcast still projects US Q3 growth at 3.8%. With central banks switching focus to weaker growth, above target inflation is less of a market concern, provided inflation expectations remain stable.

Higher tariffs are now priced into weaker consensus growth, and slightly higher inflation forecasts for 2025-26 (Chart 1). Labour markets may be slowing, particularly in the US and Canada, with unemployment now above 7% in Canada, but the Atlanta Fed Nowcast projects Q3 GDP growth at 3.8%, helped by a recovery in consumption and investment. Eurozone growth benefitted from the recovery in southern Europe, and an improved labour market. Chinese growth forecasts carry the highest uncertainty.

Canadian inflation remains closer to target than the US at 1.9% y/y in August, giving the BoC the chance to cut rates in September (Chart 2). The BoC estimates underlying inflation to be 2.5%, even if preferred core measures are nearer 3% y/y. US inflation remained stickier than Canadian, due to shelter and services, and service sector inflation is still at 3.8% y/y, even if lower goods inflation means the targeted PCE is at 2.9% y/y. Core inflation measures remain around 2.5% in Japan, above the 2% target.

Structural changes impact US and Canadian labour markets, with labour force participation rates now much lower amongst prime age workers of 25-54 yrs, in the US, as Chart 3 shows. The difficulty here is that prime age workers are the biggest cohort, so overall participation rates have fallen. The Canadian labour force has also been boosted by higher labour migration. This extra labour supply plus tariff related drop in demand explains the sharp increase in Canadian unemployment in 2025.

Short term US inflation breakevens have stabilized, though they have exceeded the Fed's 2% inflation target since mid-2024. Stable breakevens allowed a Fed rate cut in September, after pivoting to growth and employment, though they require monitoring.

Chart 1: Consensus GDP forecasts carry higher uncertainty than usual because of tariff effects, and big swings in Quarterly GDP data on trade flows. Despite a weaker labour market, US Q3 GDP is projected at nearly 4% in Q3.

Latest Consensus Real GDP Forecasts (Median, %, September 2025)

	2024	**2025**	**2026**
US	2.8	**1.7**	**1.7**
UK	0.9	**1.3**	**1.2**
Eurozone	0.7	**1.2**	**1.1**
Japan	0.8	**0.9**	**0.7**
China	4.9	**4.6**	**4.2**
Canada	1.3	**1.3**	**1.3**

Chart 2: US service inflation remains at 3.8% y/y, keeping core PCE inflation at close to 3% y/y, but the Fed switched focus to the labour market. Canadian inflation dipped below the 2% target in August data.

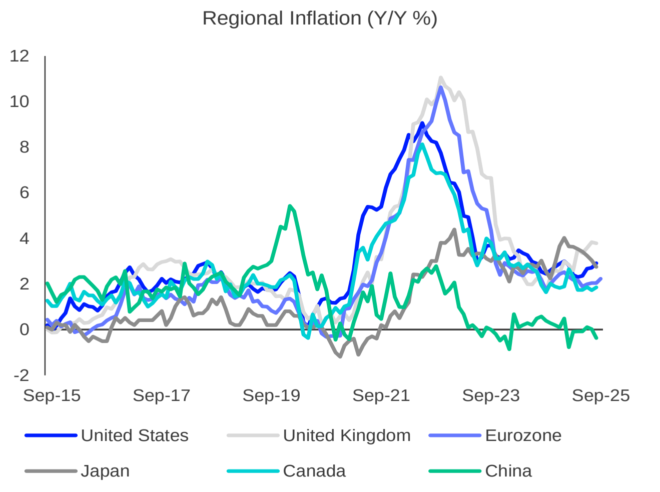


Chart 3: Tale of two labour markets ? Structural change continues to impact the US and Canadian labour markets. The US 25-54 yrs worker participation rate is now a full 4% below the Canadian rate.

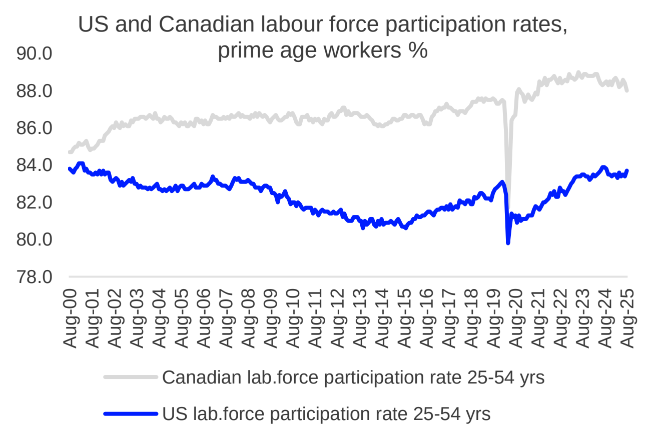
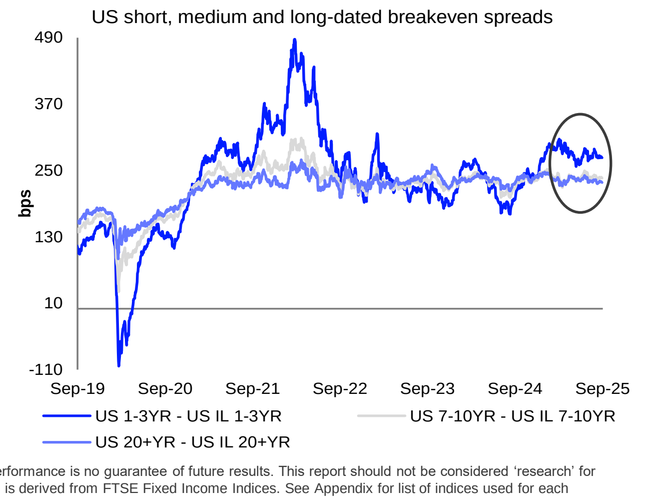


Chart 4: Inflation breakevens have stabilised after the tariff spike in April, though they are above the Fed's inflation target. Longer dated breakevens have remained near 2.5% since 2021 and are more stable.



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Financial conditions and economic policy

Loosening in financial conditions has been an important driver of risk assets in 2025, and our indicators show US FCIs have not eased as much as other G7 members and China. FCIs are generally back to 2021 levels. The USD stabilised in Q3, though remains sharply lower YTD, while the Canadian dollar has returned to mid-2024 levels, after the BoC slowed the pace of rate cuts in recent months. The Fed pivot to easier policy appears driven by the weaker labour market.

The FTSE Russell FCIs are shown in Chart 1*. They show the relative loosening in FCs is greater in the Eurozone than the US, reflecting greater policy loosening at the ECB, and the high level of the US dollar, despite recent weakness. US and Canadian financial conditions have both eased substantially since the tariff-related tightening spike in conditions in April. Such easing in FCs is often correlated with stronger risk asset performance, and is consistent with equity market gains in the US and Canada in 2025.

The US dollar stabilised in Q3, but remains sharply lower YTD, reflecting the administration's preference for a less strong dollar. After the 2024 decline, in response to nearly 200bp of rate cuts, the Canadian dollar has returned to mid-2024 levels, as Chart 2 shows, with rate differentials less negative. A stable exchange rate gives the BoC room to ease rates further in Q4 if required.

The BoC and Fed reduced rates in September, with both central banks citing labour market weakness as a key factor in the easing of rates (Chart 3). The Fed has pivoted away from inflation as its main policy concern to growth and employment, judged by the FOMC statement, and the BoC also cited downside risks to growth and employment after cutting rates in September.

After slowing balance sheet contraction to $40bn monthly in April (with $35bn in MBS and $5bn in Treasuries) the Fed preferred to cut rates in September to ease policy, and continues with its QT programme. In contrast, the BoC has effectively ended QT, and normalised its balance sheet, though it is larger than pre-Covid (Chart 4). Short rates remain the dominant policy instrument.

* Building the FTSE Russell financial conditions indicator | LSEG, September 2025.

Chart 1: US financial conditions have not eased as much as other G7 members and China, reflecting higher policy rates and bond yields and the dollar's valuation. Financial conditions generally eased to 2021 levels.

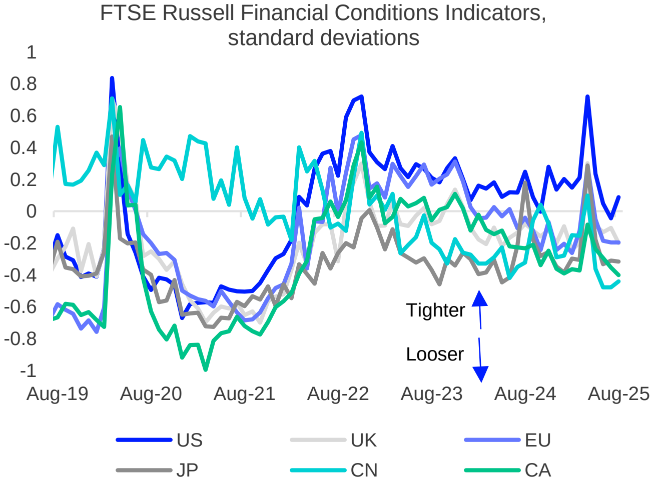


Chart 2: Pronounced weakness in the yen versus the dollar broadly tracked short rates and yield differentials since Covid. Differentials have moved more in favour of the yen after the Fed's September rate cut.

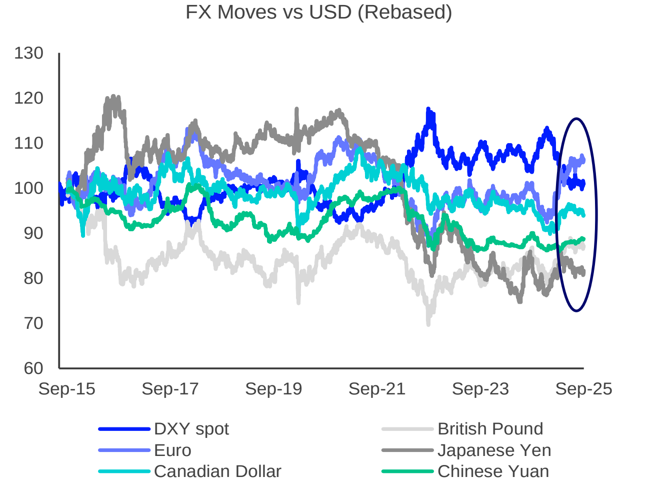


Chart 3: The BoC and US Fed took out some recession protection in September by easing policy 25bp, though the speed of BoC easing remains slower in 2025, with only 50bp of easing versus 200bp in 2024.

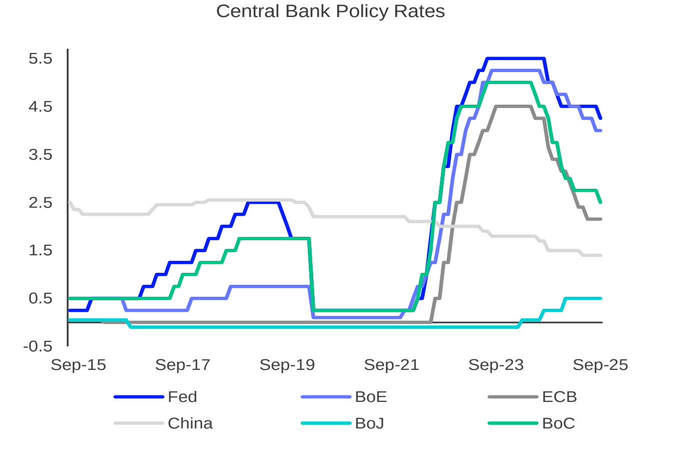
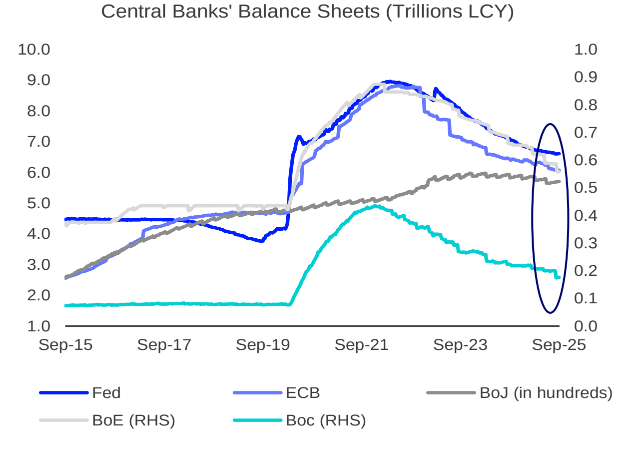


Chart 4: The BoC has largely normalised its balance sheet and ended QT, though it intends to maintain a larger balance sheet than pre-Covid, as it moves to a floor system for settlement balances.



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US Credit : Investment Grade Credit and RMBS analysis

Chart 1: Higher grade US credit yields were pulled below UK yields by the rally in Treasuries, after the Fed reduced rates in September. Canadian IG yields also fell further, helped by the BoC’s rate cut.

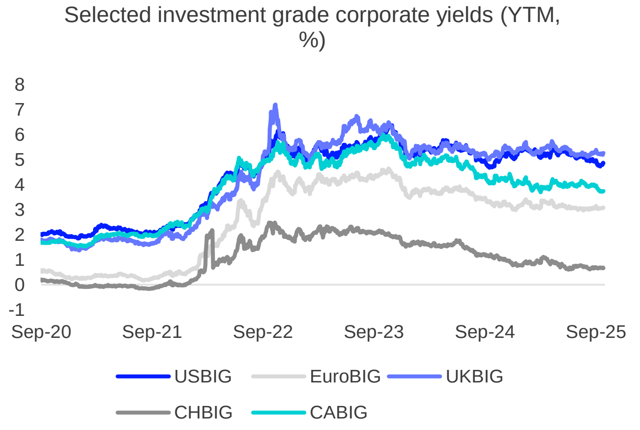


Chart 2: Yield per unit of duration risk remains higher than pre-Covid, due to the combination of higher yields and lower duration, which shortened across all major markets, partly due to lower prices.

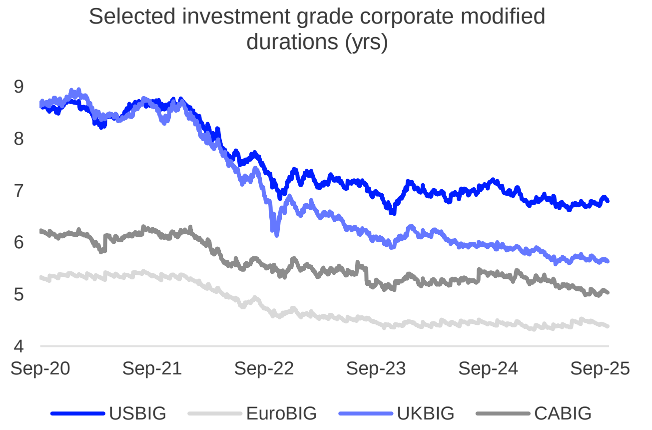


Chart 3: Although 1-3 yr IG credits have delivered stronger returns than longer maturity credits, and particularly 10+ yr maturities since 2022, 7-10 yr credits rallied on the Fed’s September rate cut, closing the gap.

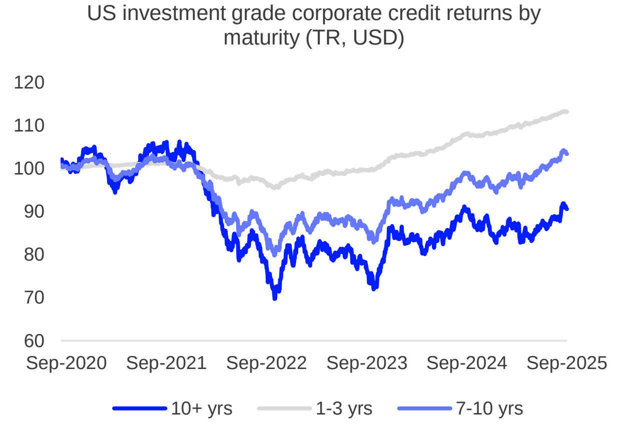


Chart 4: US banks continued their strong IG performance in Q3, helped by strong net interest income, and the steeper yield curve in 2024-25. Asset backed issues continue to show the best risk/return. .

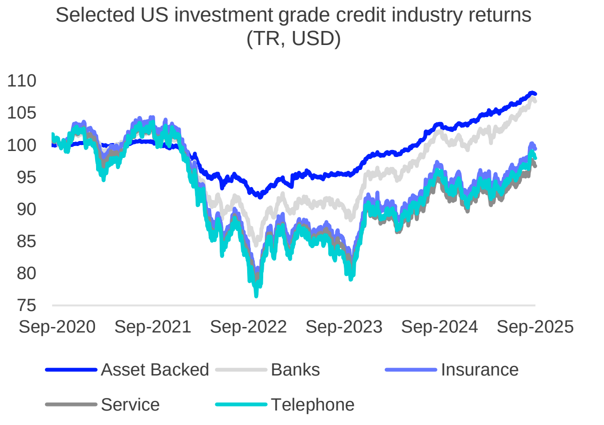


Chart 5: A fall in IG credit spreads relative to agency-MBS spreads continues. This is mostly driven by IG credit spreads narrowing v US govts. in 2024-25. Possible privatisation of the US MBS agencies may also be a factor?

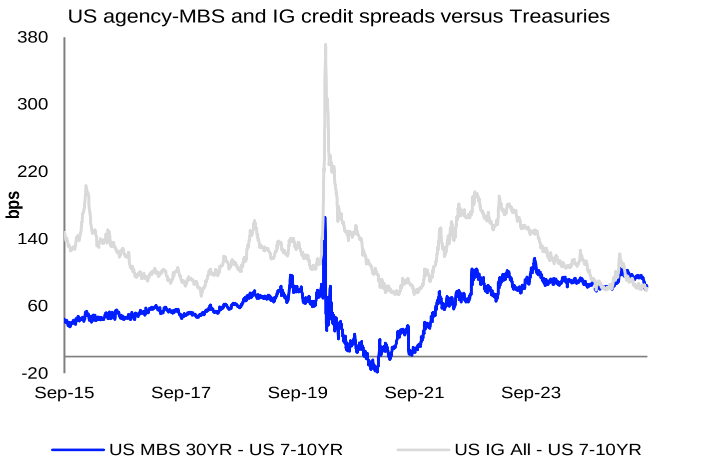
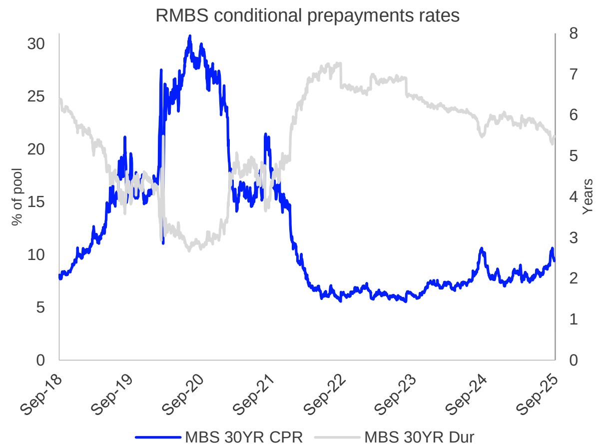


Chart 6: The Fed rate cut in Sept. increased mortgage prepayments a little, but most mortgages have coupons < current mortgage rates. 2-3% Fed funds may be needed to drive a sharper increase in refis.



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US Credit : High Yield Credit Analysis

Chart 1: Sterling HY returns still exceed US HY, helped by sterling FX gains for a US dollar-based investor. HY generally remains in a sweet spot, with rates slowly falling, and strong correlation to the equity rally.

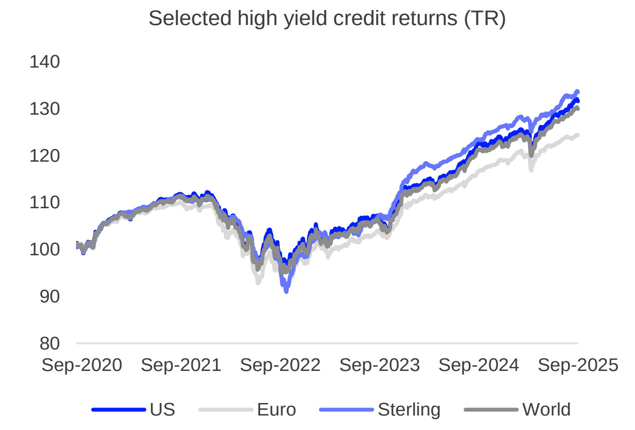


Chart 2:.The share of fallen angels in US HY remains close to a 23 yr low, and has falling from13.5% after Covid struck in 2020, to the current level just above 3%, reflecting improved financial metrics in credit in this cycle.

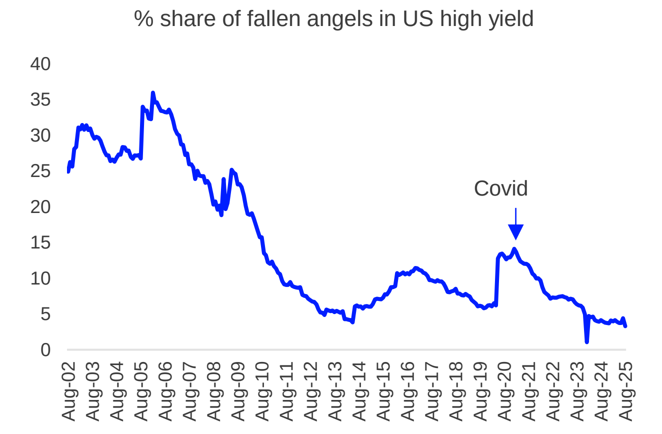


Chart 3: HY index weights show the dominance of services, which includes Technology and healthcare. Energy issues are lower weighted than often assumed (10.5%), and financials a much higher IG weight.

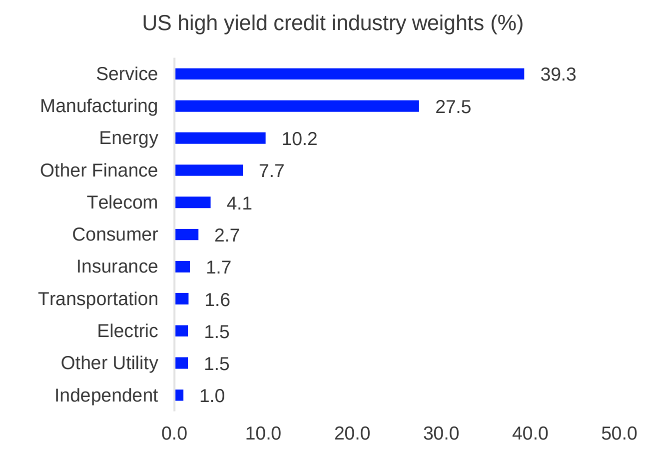


Chart 4: Energy remains the strongest HY sector since Covid, of the larger industry weights, though financials have recovered strongly. All sectors have recovered the losses suffered in the 2022 tightening.

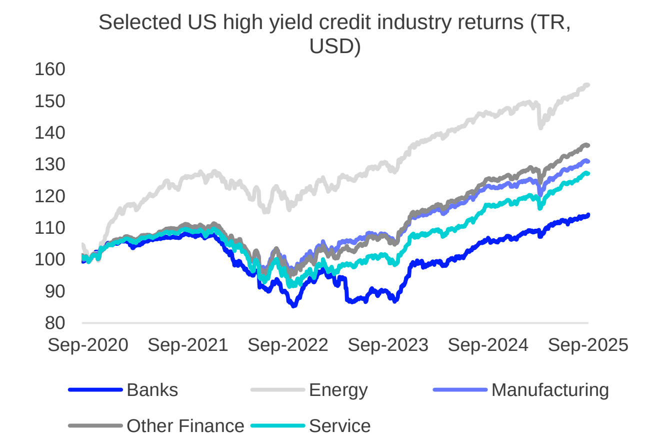


Chart 5: CCC spreads have yet to unwind the tariff-related spike in April, and are more sensitive to risk appetite, with less access to pools of capital & higher default rates. BB spreads are at multi-year lows.

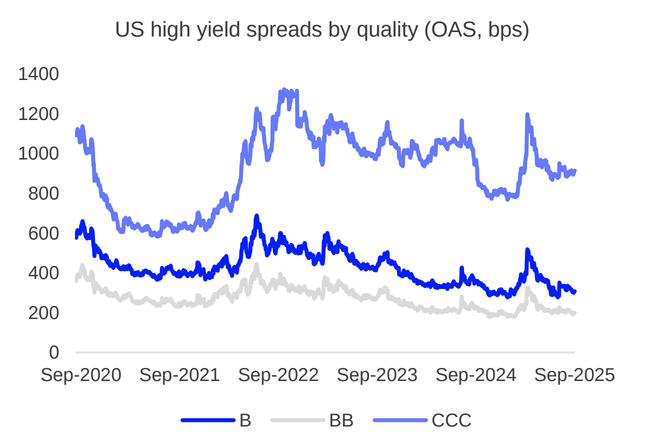
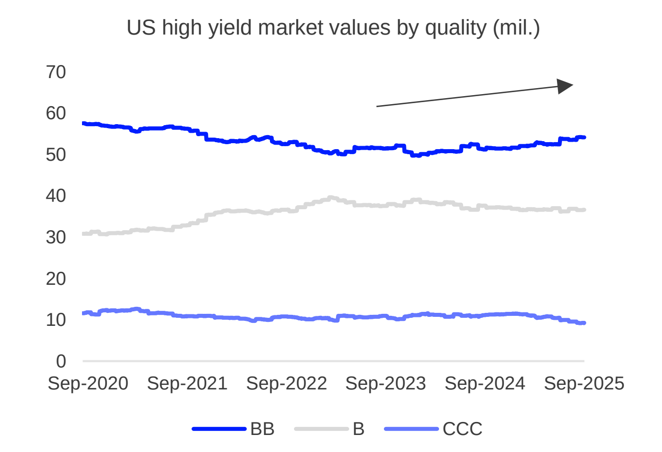


Chart 6: BB remains the biggest quality bucket in the HY market, and now comprises 53.5% of the index, reflecting improved credit quality. CCC issues are only 9.6% of the HY index, compared with over 12% in 2021.



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Canadian Governments, Provinces and Municipalities

Chart 1: The Canadian yield curve renewed steepening at the long end in September, partly due to the BoC's 25bp rate cut pulling short dated yields lower. The 10s/2s curve stabilised in Q3.

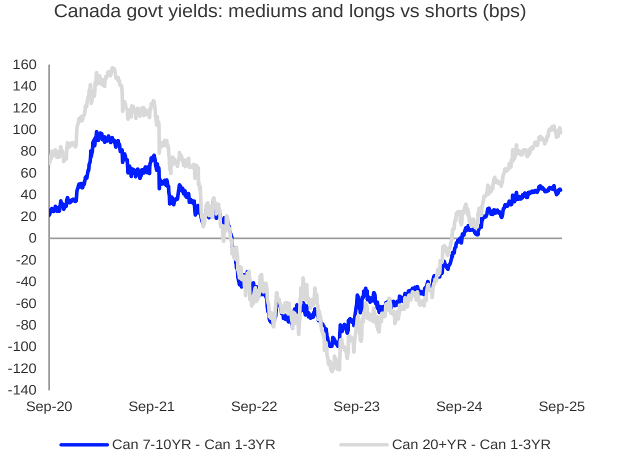


Chart 2: Canadian breakevens remain relatively stable, near the 2% inflation target, even if short dated breakevens have oscillated with tariff negotiations in recent months.

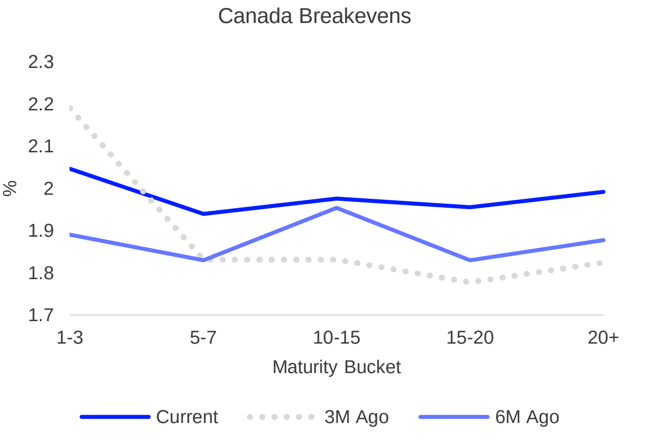


Chart 3:.Canadian sovereign spreads fell further versus JGBs in Q3, as the BoJ edged towards raising rates again in Q4. Spreads versus gilts also fell, helped by lower relative inflation in Canada versus the UK.

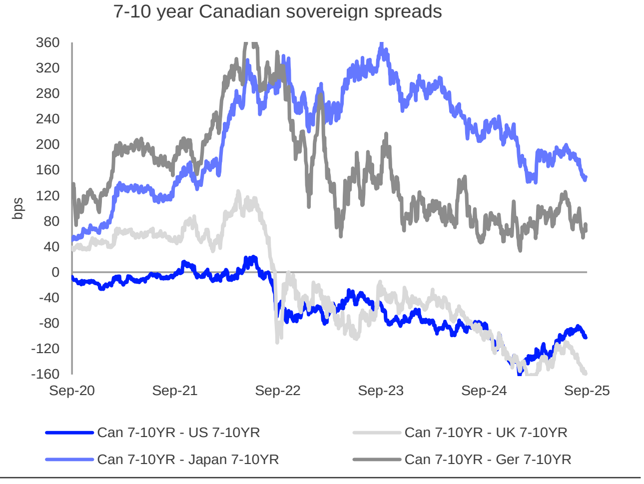


Chart 4: Long-dated Canadian spreads moved back out versus the US, after the Fed's rate cut. Spreads versus gilts fell, as the gilt market braced for higher issuance in 2025-26, and remain near multi-year lows.

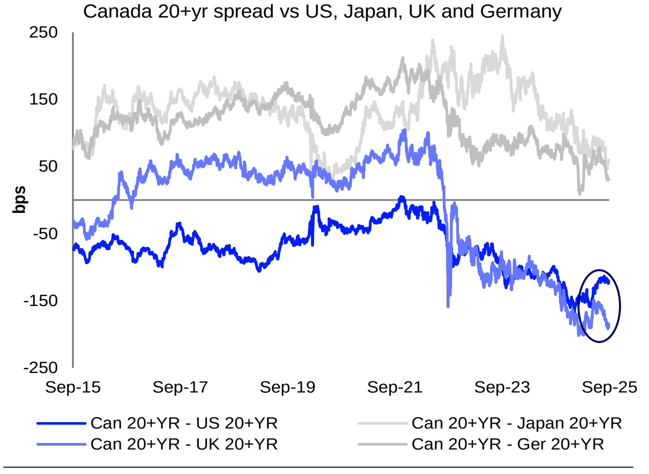


Chart 5: 20+ yr Canadian breakevens rose sharply versus other markets in 2024-25, despite inflation stabilizing near 2%. This may be due to a demand/supply imbalance in long Canada real return bonds.

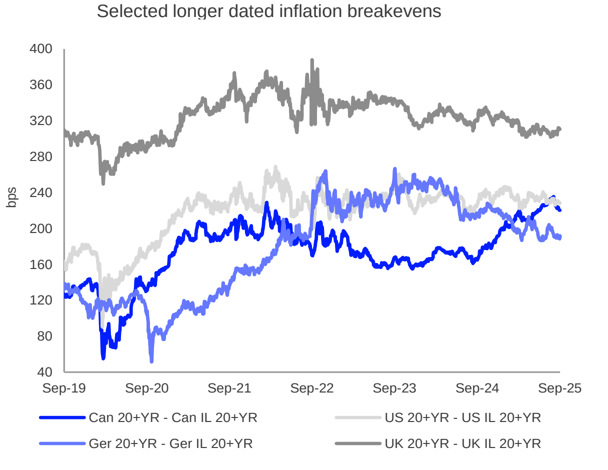
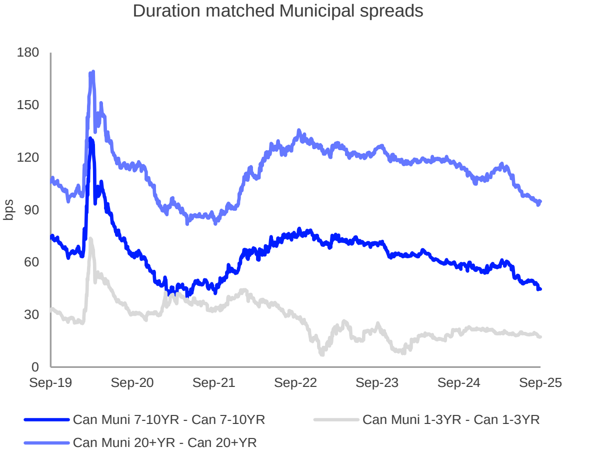


Chart 6: Municipal spreads have generally tightened in the BoC rate-cutting cycle since mid-2024. Investors were attracted by attractive valuations relative to provincial credits, and stable credit ratings.



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Canada : Investment Grade Credit Analysis

Chart 1: Canadian IG yields fell further in September, pulled lower by the BoC rate cut. Canadian IG yields have gone from being some of the highest in the G7 in 2021-22 to near the lowest in 2025.

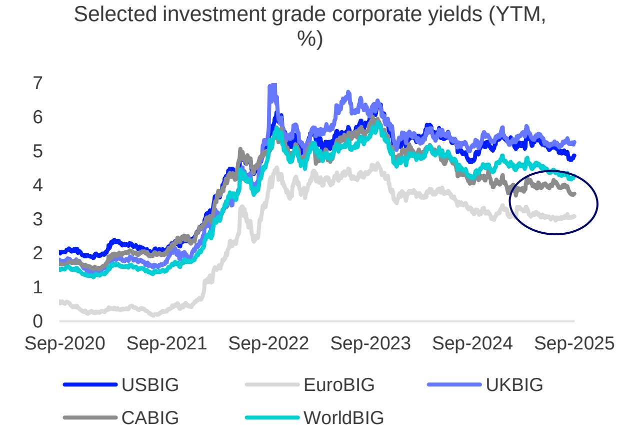


Chart 2: Like other markets, the duration of Canadian credit fell steadily since 2020, as yields rose. With duration now shorter, credit markets are less sensitive to changes in govt yields than in 2021-22.

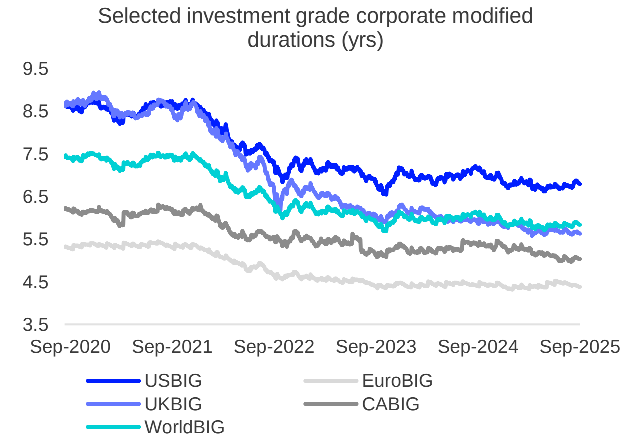


Chart 3: BBB credits have generally outperformed during the strong credit rally in 2023-25. Conservative financial management during this cycle may explain this outperformance, and low issuance.

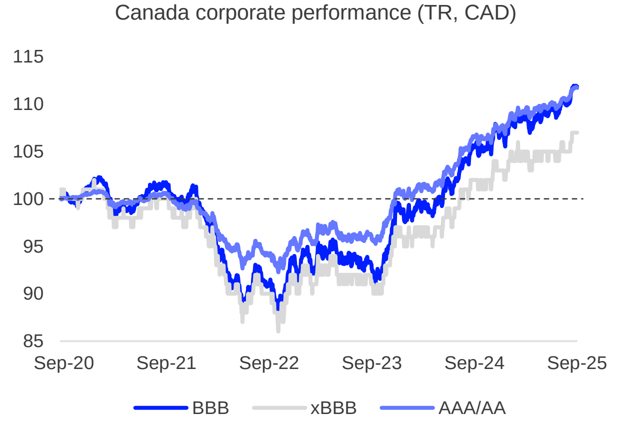


Chart 4: As a result, Canadian credit spreads have fallen by 120-100 bp since 2023, helped by lower corporate leverage in this cycle, and the surge in govt borrowing, relative to the private sector.

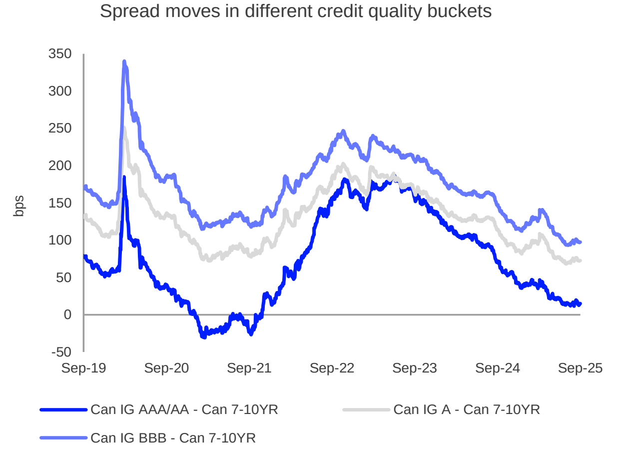


Chart 5: Canadian IG credits remain dominated by energy (38% weight) and infrastructure (24% weight), reflecting the underlying structure of the economy, and the substantial energy sector.

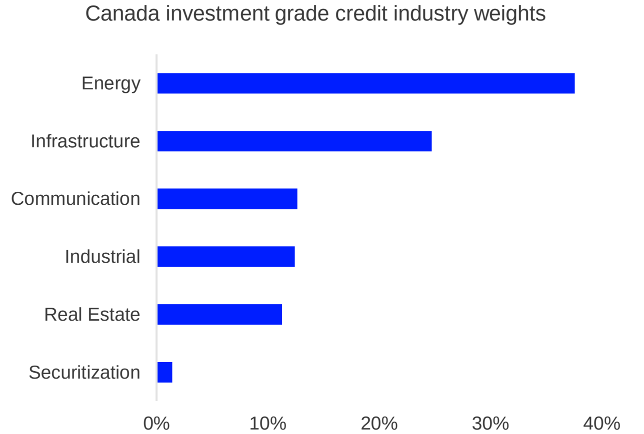
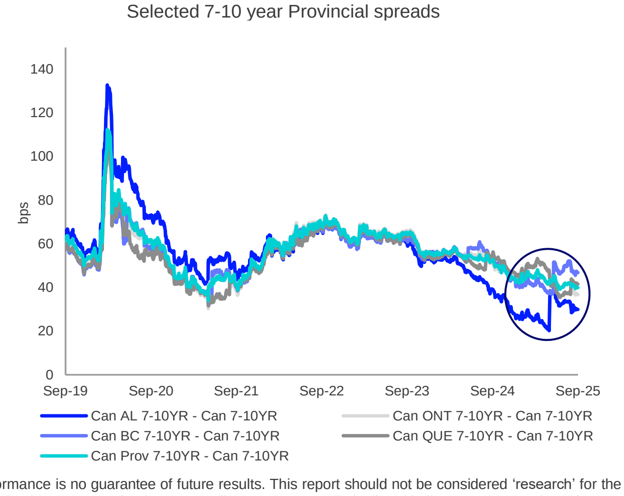


Chart 6: Alberta spreads stabilized after the spike on fears of an independence referendum earlier in 2025. Other provincial spreads have remained stable in 2025, after the sharp move lower in 2024.



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Canada : High Yield Credit Analysis

Chart 1: The level of Canadian credit yields remains attractive, benchmarked against the last 10 yrs, and even though Canadian yields have been pulled lower by 250bp of BoC rate cuts in 2024-25.

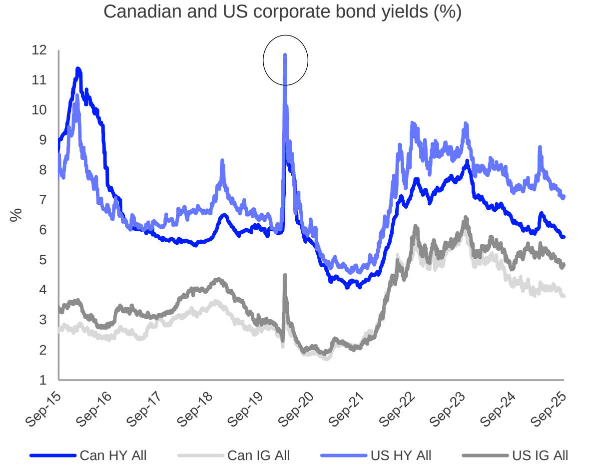


Chart 2: Investors get higher protection in Canadian HY, than US, since the proportion of yield that is risk-free is lower in Canada, after the fall in Canadian govt yields versus the US (also see Chart 2 on page 1).

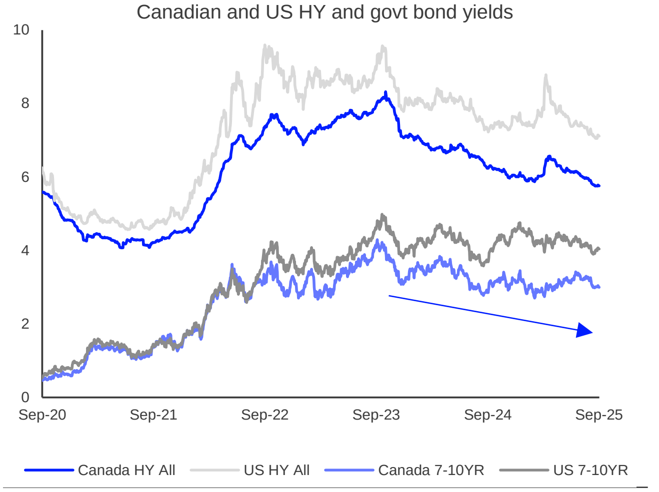


Chart 3: Energy issues dominate the Canadian HY credit market, and have a much higher weight (45%) than US energy issues in the US HY market (only about 11%). Financials have close to zero weight.

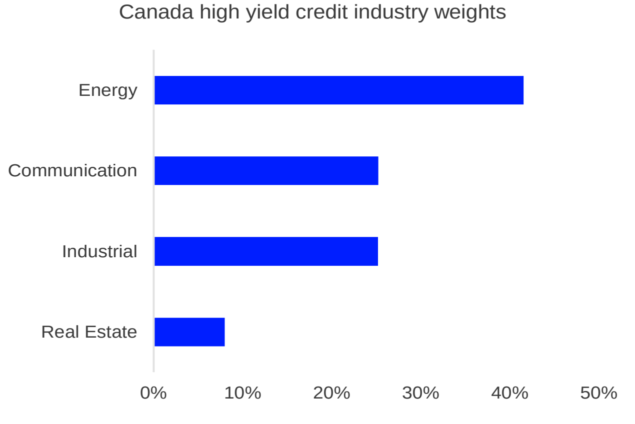


Chart 4: Canadian HY credits outperformed again in Q3, and shrugged off tariff-related risks to growth and profit margins in 2025. With curves steepening in 2024-25, the longer duration advantage of IG was offset.

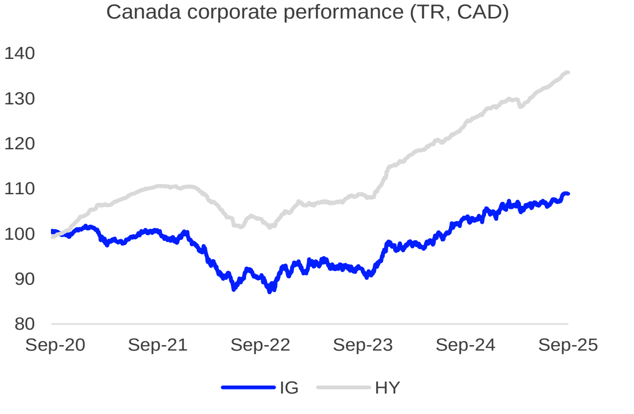


Chart 5: Canada's high yield Energy sector has outperformed, despite oil prices drifting lower in 2025. The Communication industry has stabilised and is improving. Real estate has benefitted from BoC easing.

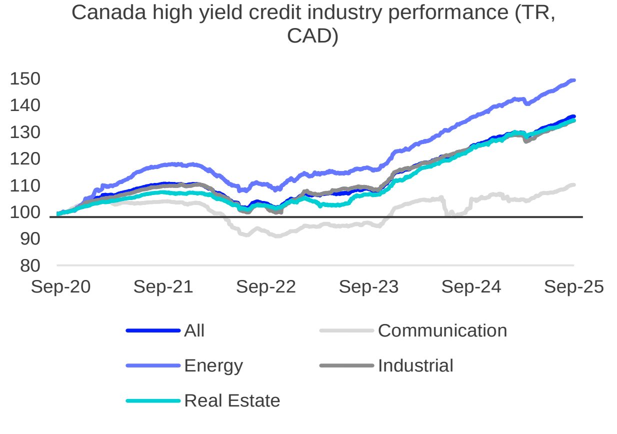
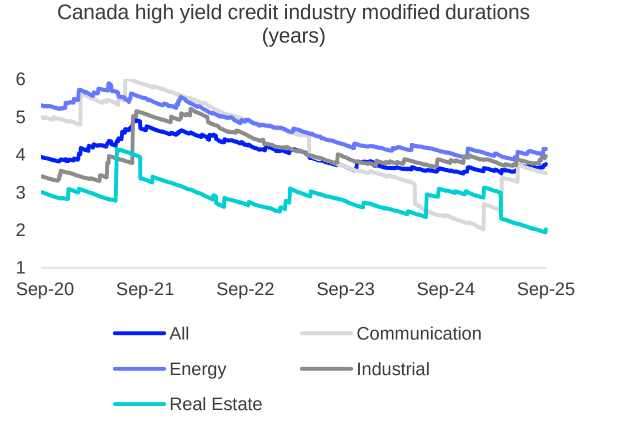


Chart 6: Energy issues, which represent near 45% of the Canadian high yield universe, have the highest level of duration, at about 4 years, followed by Industrial at 3.7 years.



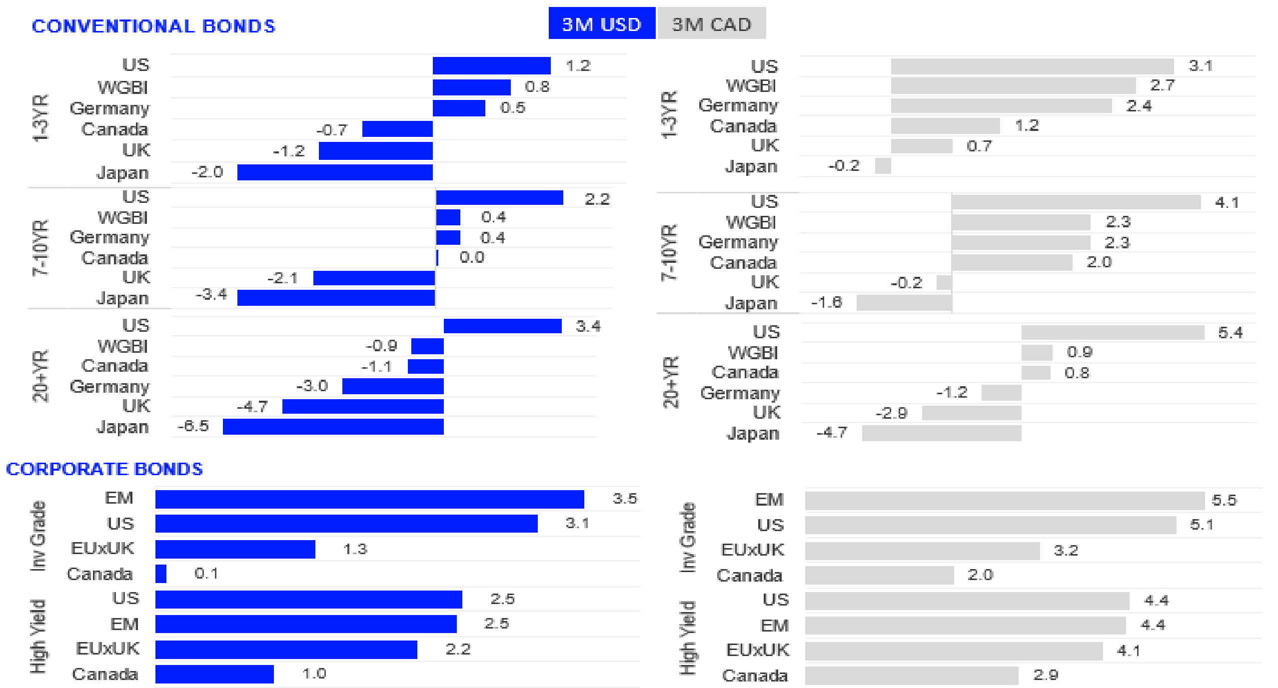
Source: FTSE Russell and LSEG. All data as of September 30, 2025, unless indicated otherwise. Past performance is no guarantee of future results. This report should not be considered 'research' for the purposes of MIFID II. Please see the end of the report for important legal disclosures. Bond market data is derived from FTSE Fixed Income Indices. See Appendix for list of indices used for each market.

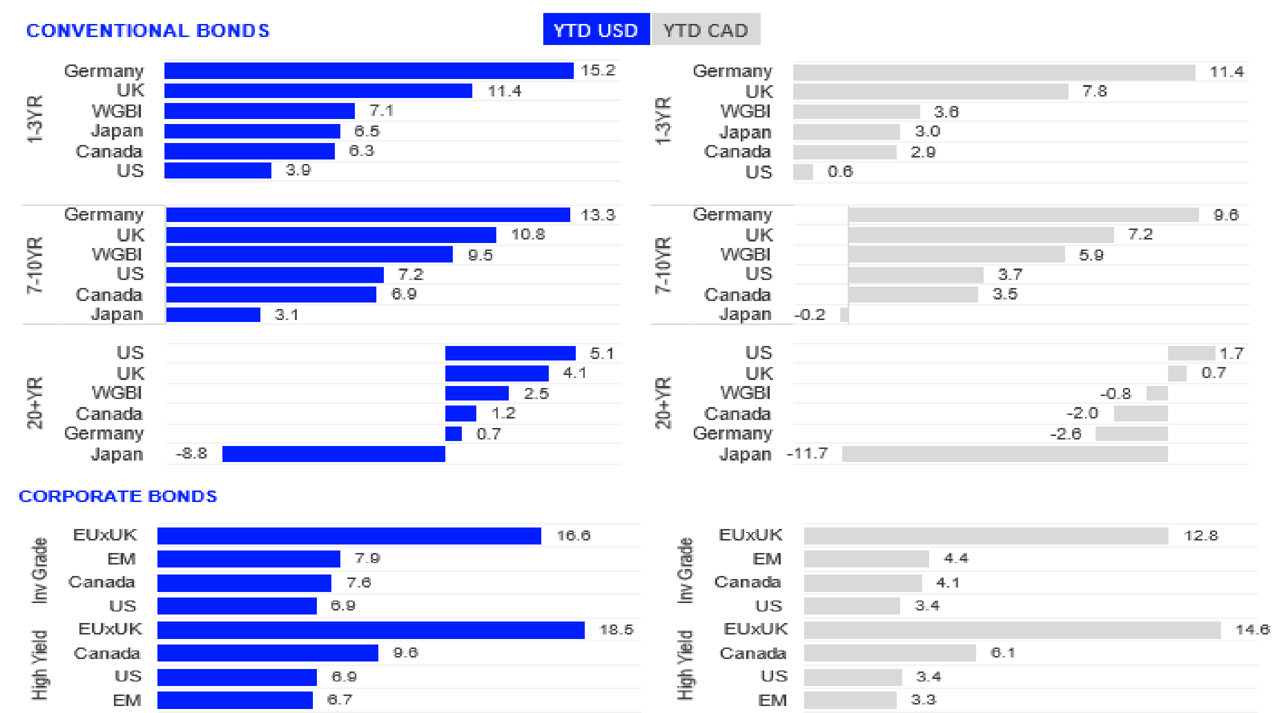
Conventional Government Bond Returns − 3M & YTD % (USD, CAD, TR)

Treasuries rallied in Q3, as the Fed pivoted to growth concerns. With the US dollar recovering, Treasuries delivered returns of 3-5% in Canadian dollar terms, with long US outperforming, though elsewhere, shorter maturities mostly outperformed. Short and medium Bunds gained 10-11% YTD in CAD, and 13-15% in USD. Credit again performed well.

Canadian govt bonds lacked lustre in Q3, with the BoC on hold until the rate cut in mid-September though shorts and mediums delivered 6-7% YTD returns in US dollars, helped by the rally in the currency.

Both IG and HY credit showed further gains in Q3, led by EM, with gains of 3-6% in Euro, US and EM IG credits in CAD, and up to 15% YTD, and 19% in USD. Canadian credit shows solid gains of 8-10% YTD, in USD, helped by the correlation to equities.





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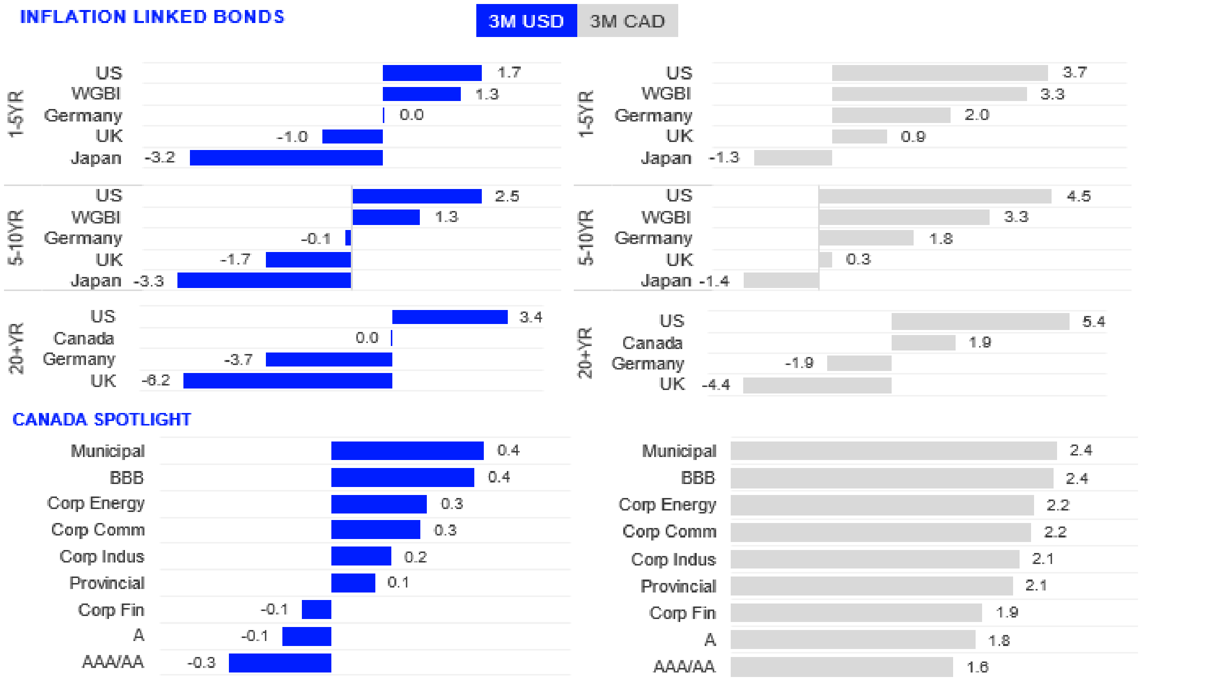
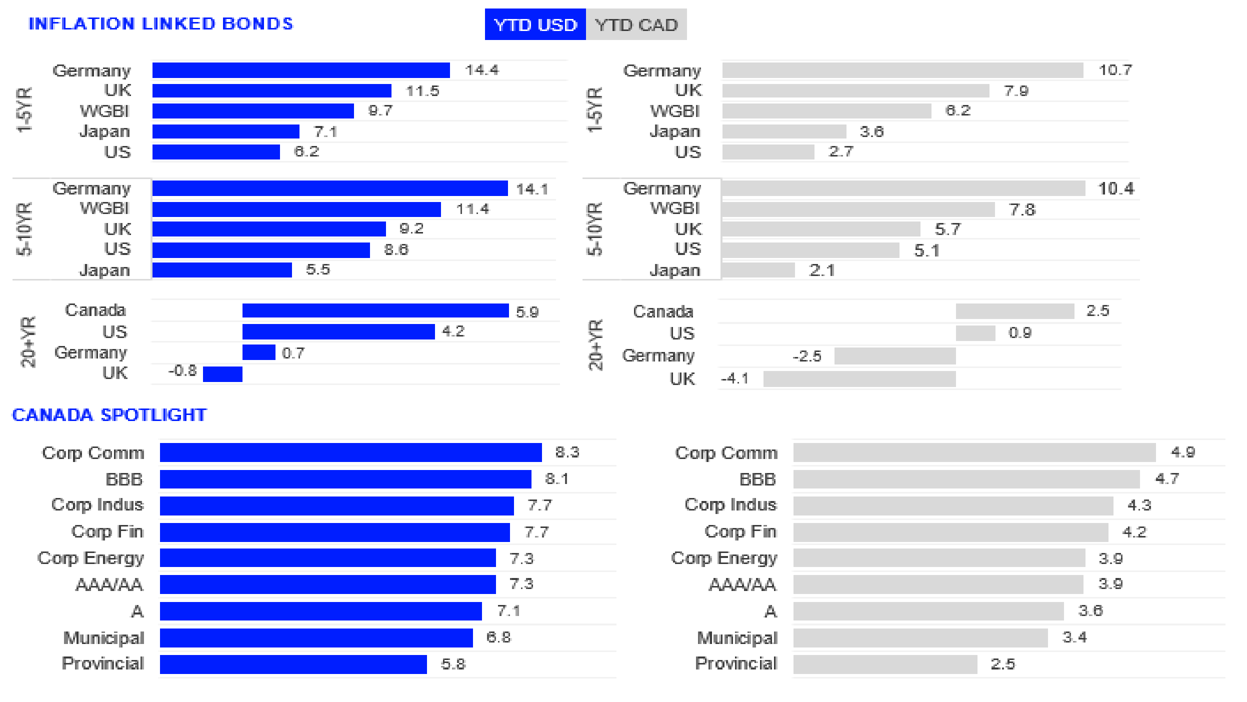
Global Inflation-Linked Bond Returns – 3M & YTD % (USD, CAD, TR)

Inflation-linked government bonds broadly matched the moves in conventionals in Q3, with breakevens stable, and longs weakening, exc. US Tips. Tips showed the strongest gains in CAD terms of 4-5% in Q3. Canadian Munis and BBB credit led Canadian returns in Q3 with gains of 2%, but near zero in USD. Credit also led YTD Canadian returns.

Ultra-long duration weighed on long UK linkers in Q3, with losses of 4-6% in USD and CAD. Long Bund linkers fell back 2-4% as the German govt unveiled higher spending plans for 2025-29.

Short and medium linkers all benefitted from G7 rate cuts, YTD, with gains of 5-14% in Bunds, WGBI, UK and US Tips, YTD, in USD and CAD terms.





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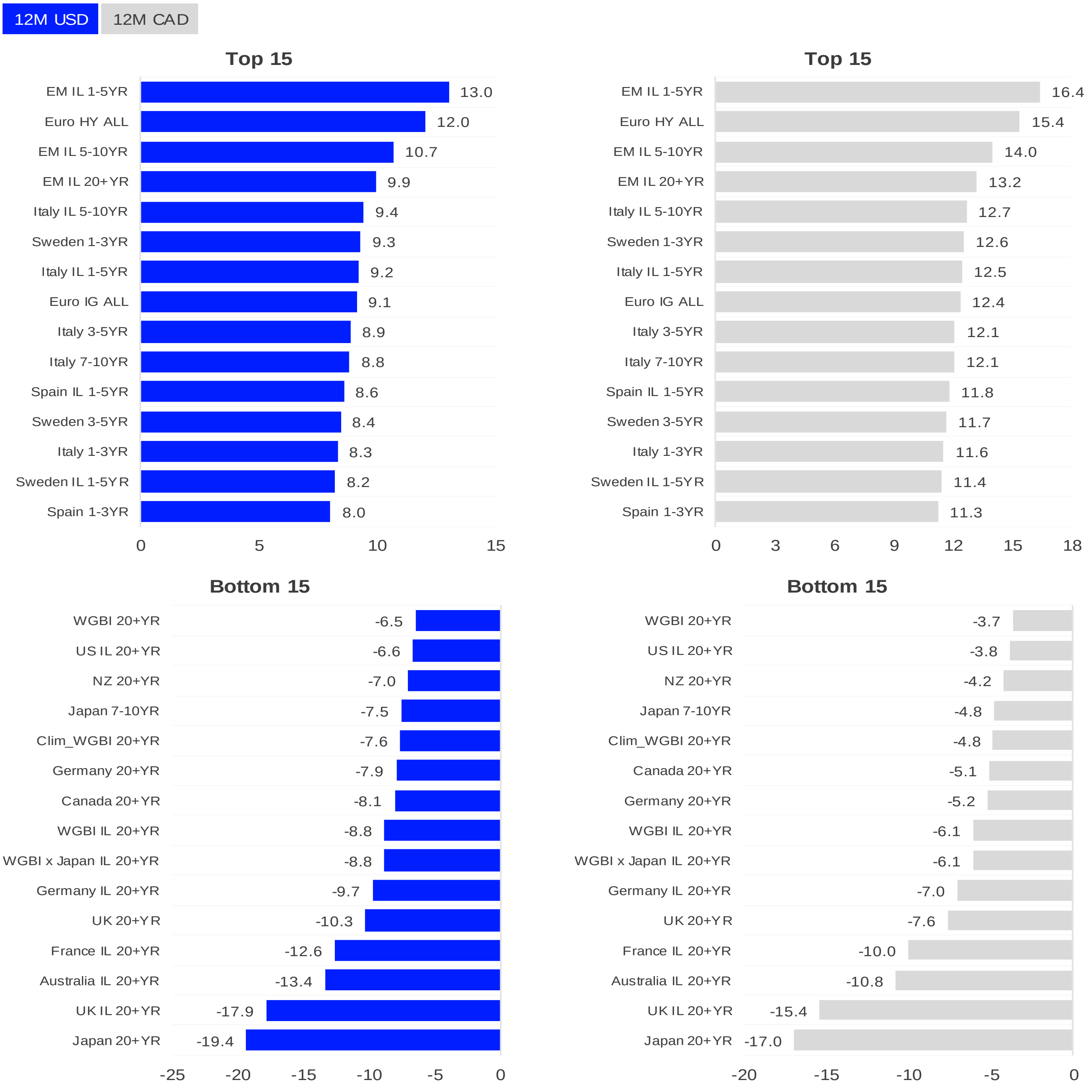
Top and Bottom Bond Returns − 12M % (USD, CAD, TR)

EM inflation-linked led 12M returns in USD and CAD, with gains of 13-16%. Strong Latam currencies were a big driver of returns, given the high Mexican and Brazilian weights in EM inflation-linked. On 12M, Euro credits were up 12-15% in USD and CAD terms, buoyed by currency strength and credit’s correlation to the equity market rally in 2024-25. Tariff fears proved short-lived.

Convergence trades in the peripheral Eurozone markets drove strong returns, as yields fell in Spain and Italy, with gains of 8-9% in USD and 11-13% in CAD terms on 12M. Swedish bonds were boosted by the Skr,and gained 13% on 12M in CAD terms.

Currency weakness and curve steepening after BoJ yield curve control was suspended, meant JGBs were the weakest market on both 1M and 12M, with losses of 17-19% on 12M in longs. Long gilts and linkers were weak, losing 15-18% in CAD & USD.

Long Australian and French bonds suffered from the RBA’s reluctance to reduce rates after the inflation overshoot, and political difficulty in agreeing fiscal deficit reductions in France, so the two markets lost 10-13% in CAD and USD terms. Bunds were also weak on 12M, after the German govt announced plans to increase fiscal deficits, infrastructure and defence spending in 2025-29.



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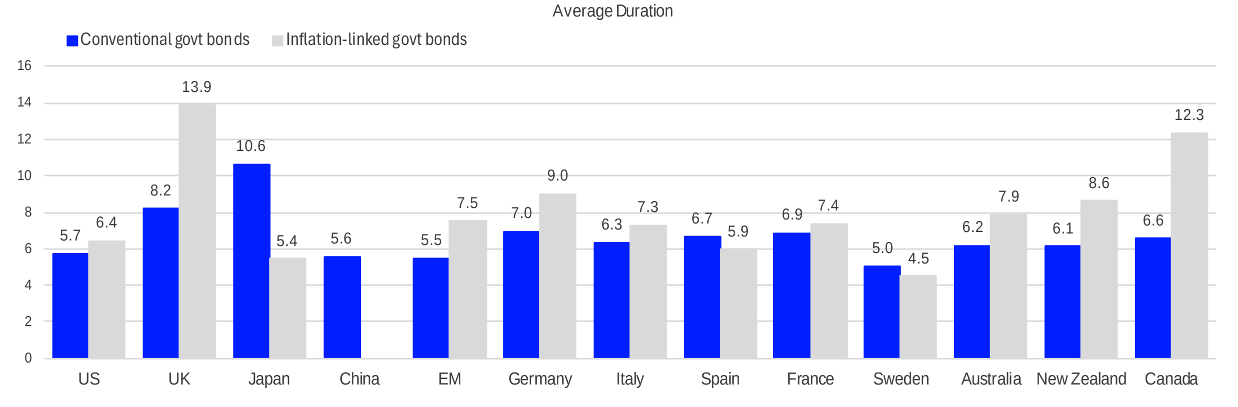
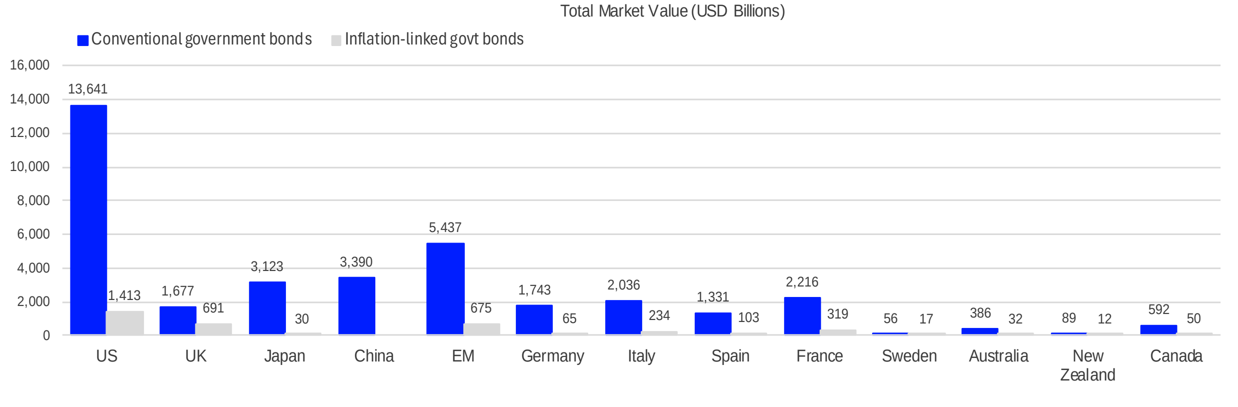
Appendix – Duration and Market Value (USD, Bn) as of September 30, 2025

	Conventional government bonds								Inflation-linked government bonds					
	Duration				Market Value				Duration			Market Value		
	3-5YR	7-10YR	20+YR	Overall	3-5YR	7-10YR	20+YR	Total	5-10YR	20+YR	Overall	5-10YR	20+YR	Total
US	3.6	7.0	16.0	**5.7**	3,068.1	1,298.8	1,540.1	**13,641.1**	7.0	20.9	**6.4**	466.1	115.0	**1,413.5**
UK	3.5	7.3	16.9	**8.2**	203.7	276.7	328.8	**1,676.6**	7.3	25.5	**13.9**	143.8	207.7	**690.9**
Japan	3.9	8.1	21.9	**10.6**	402.7	521.2	561.8	**3,122.9**	7.9		**5.4**	15.9		**29.8**
China	3.7	7.7	17.8	**5.6**	770.4	602.7	354.4	**3,389.7**						
EM	3.5	7.1	15.9	**5.5**	1,190.3	1,000.4	507.2	**5,437.1**	6.1	13.4	**7.5**	161.0	162.8	**674.7**
Germany	3.7	7.6	20.0	**7.0**	359.6	297.0	198.1	**1,742.6**	7.3	19.6	**9.0**	14.6	17.0	**65.3**
Italy	3.7	7.1	16.3	**6.3**	394.7	324.0	167.0	**2,035.8**	6.9	23.0	**7.3**	55.0	9.4	**233.5**
Spain	3.6	7.2	17.5	**6.7**	270.0	237.6	112.0	**1,331.5**	6.3		**5.9**	60.5		**102.7**
France	3.6	7.1	18.4	**6.9**	502.9	450.7	230.7	**2,216.2**	6.4	22.8	**7.4**	73.1	21.3	**319.1**
Sweden	4.0	7.9		**5.0**	9.2	12.6		**56.1**	6.5		**4.5**	3.7		**17.2**
Australia	3.6	7.1	15.9	**6.2**	65.4	107.4	20.8	**386.0**	6.6	20.7	**7.9**	18.4	2.7	**31.7**
New Zealand	3.7	7.0	15.4	**6.1**	18.3	22.3	5.4	**88.5**	4.6		**8.6**	3.4		**12.3**
Canada	3.7	7.4	18.7	**6.6**	117.1	130.5	81.8	**591.9**	5.5	21.3	**12.3**	8.3	12.9	**49.8**

	Investment grade bonds										High Yield	
	Duration					Market Value					Duration	MktVal
	AAA	AA	A	BBB	Overall	AAA	AA	A	BBB	Overall		
US	10.2	8.2	6.9	6.4	6.8	76.1	466.6	3078.5	3725.8	7347.1	3.7	1192.4
Europe	6.0	4.9	4.5	4.1	4.4	27.1	249.7	1430.2	1787.5	3494.5	3.3	407.1
EM		6.3	5.5	5.5	5.6		72.4	177.8	249.5	499.7	3.5	189.7





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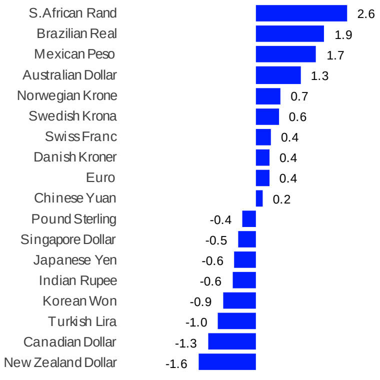
Appendix − Foreign Exchange Returns % as of September 30, 2025

1M vs USD

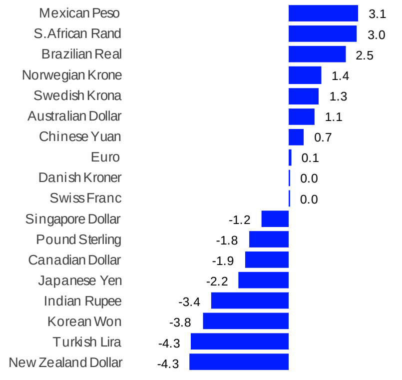
3M vs USD

12M vs USD

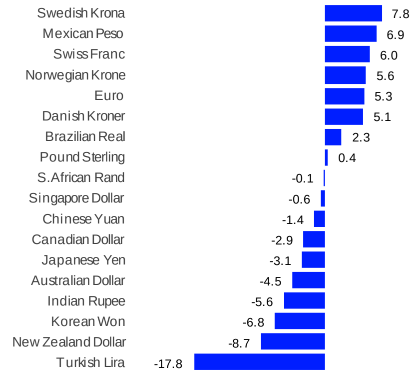
FX Moves vs USD - 1M



FX Moves vs USD - 3M



FX Moves vs USD - 12M

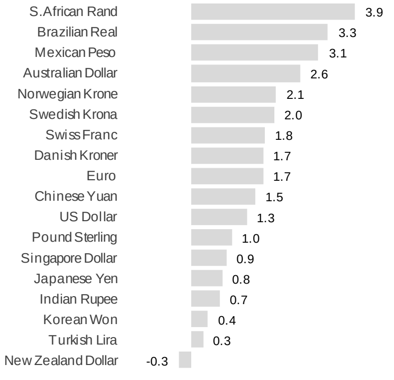


1M vs CAD

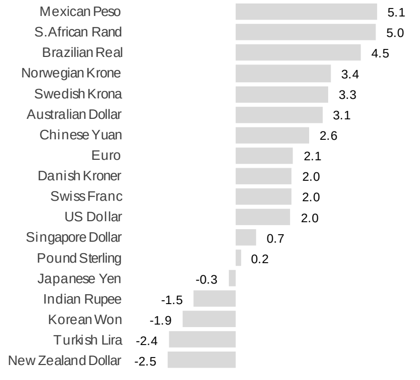
3M vs CAD

12M vs CAD

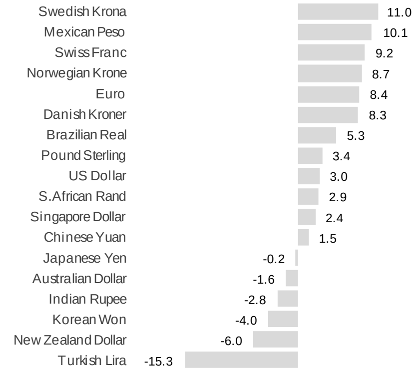
FX Moves vs CAD - 1M



FX Moves vs CAD - 3M



FX Moves vs CAD - 12M



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Appendix − Glossary

Bond markets are based on the following indices:

FTSE World Government Bond Index (WGBI) for all global government bond markets

FTSE World Inflation-Linked Securities Index (WorldILSI) for all global inflation-linked bond markets

FTSE US Broad Investment-Grade Bond Index (USBIG®) for the US corporate bond market

FTSE US High-Yield Market Index for the US high yield bond market

FTSE Euro Broad Investment-Grade Bond Index (EuroBIG®) for the Euro-denominated corporate bond market

FTSE European High-Yield Market Index for the European high yield market

FTSE Chinese Government and Policy Bank Bond Index (CNGPBI) for the Chinese government bond market

FTSE Emerging Markets Inflation-Linked Securities Index (EMILSI) for the emerging markets inflation-linked bond market

FTSE Emerging Markets Government Bond Index (EMGBI) for the emerging markets government bond market. Please note that over 50% of this index is invested in China

FTSE Emerging Markets Broad Bond Index (EMUSDBBI) for the emerging markets corporate bond market

FTSE ESG World Government Bond Index for the global government bond markets with an ESG tilt

FTSE Climate Risk-Adjusted World Government Bond Index (Climate WGBI) and FTSE Advanced Climate Risk-Adjusted World Government Bond Index (Advanced Climate WGBI) for each country’s relative exposure to climate risk, with respect to resilience and preparedness to the risks of climate change

List of Abbreviations used in charts:

IL = Inflation-linked bonds

IG = Investment-grade bonds

HY = High-yield bonds

BPS = Basis points

EM = Emerging market

LC = Local currency

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