

# 2026 Mid-Year Outlook

Macro, Equities, Retail, Funds, Agency RMBS,  
Non-Agency RMBS, CMBS, and CLO insights

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# Contents

## [Executive Summary](#)

### [Section 1 – Macro Outlook: An oil shock - but when inflation is lower than 2022](#)

Author: Robin Marshall, MA, MPhil, Director of Global Investment Research, FTSE Russell

### [Section 2 – Equities Outlook: Record-High Earnings Expectations and Returns on AI Investment](#)

Author: Tajinder Dhillon, CFA, Head of Earnings and Equity Research

### [Section 3 – Retail Consumer Outlook: “Pricing Power, Promotions, and Consumer Priorities”](#)

Author: Jharonne Martis, Head of Consumer Research

### [Section 4 – Funds Outlook: Triumph of the optimists?](#)

Authors: Dewi John, Head of Research, LSEG Lipper, Europe

Detlef Glow, Head of Lipper ETF Research

### [Section 5 – Agency RMBS Outlook: Agency RMBS in 2026: Mid-Year Review of Prepayment Trends and Housing Market Developments](#)

Author: Irene Shi, Senior Manager, Agency RMBS Research and Modeling

### [Section 6 – Non-Agency RMBS Outlook: Strong growth and resilient performance](#)

Author: Plamen Mitkov, Head of Global RMBS Quantitative Research

### [Section 7 – CMBS Outlook: Record paced issuance but high rates continue to pressure maturities](#)

Author: Luke Lu, Head of Credit Research and Quantitative Modelling

Loy Weng, Director, CMBS Research and Quantitative Modelling

Hank Qian, CMBS Quantitative Researcher

### [Section 8 – CLO Outlook: Holding up despite software and private credit stress](#)

Authors: Luke Lu, Head of Credit Research and Quantitative Modelling

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## Executive Summary

### Macro

Although the oil shock arising from the Middle East conflagration in Q1 has been described as “the worst ever oil shock” by the IEA, the timing of the shock is much less damaging than the Ukraine shock in 2022.

Lower inflation in the G7 in 2026 compared with 2022, and weaker domestic demand growth, means there is less pressure on central banks to raise rates, not least because energy supplies are beyond central bank control, and 2nd round effects on inflation expectations are muted. So financial conditions are near longer term means in the major economies, after some initial tightening after the March weakness in equity and bond markets.

Structural changes in the oil market mean both oil supply and demand elasticity has risen sharply, beyond the very short term, reducing the impact of Gulf supply disruption on prices, even if high net energy importers from the Middle East are more exposed. With more diverse oil supplies globally, and shorter capital cycles in production, exposure to geo-political shocks in the energy market has fallen, compared to the 1970s and 1980s.

Both nominal and real government bond yields remain near post-GFC highs, despite easing back since April, and yield curves now carry a higher term premium in longer maturities. This may reflect a regime shift to more active fiscal policy for the green transition and infrastructure development, leading to higher government debt/GDP ratios.

The Goldilocks period in the early 2000s proved equity markets can still progress with govt bond yields in the 3-5% range, provided inflation remains modest and earnings growth robust.

### Equities

U.S. large-cap equities remain resilient following one of the strongest earnings seasons on record, with consensus forecasting one of the strongest earnings expansions in decades. This has kept equities near all-time highs despite higher oil prices, renewed inflation concerns and a more hawkish Federal Reserve, with markets now pricing two rate hikes over the next 12 months compared with two rate cuts at the start of the year.

The earnings outlook remains highly concentrated, with the Mag-7 (particularly Nvidia) driving a disproportionate share of index earnings growth, although leadership is expected to broaden to the S&P 493 throughout the year. Another notable feature of this earnings cycle is the increasingly blurred distinction between core and non-core earnings, as hyperscalers expand their AI investment portfolios and mark-to-market investment gains become a more meaningful contributor to reported earnings.

Concerns over AI-related capital spending have weighed on the Mag-7, which has underperformed the S&P 493 year-to-date. Hyperscaler capex is forecast to approach \$1 trillion by 2029, placing significant pressure on free cash flow and leverage, although the pace of spending growth is expected to peak this year. Despite these concerns, most hyperscalers continue to generate returns on incremental invested capital above their cost of capital, suggesting the current investment cycle remains economically justified.

### Retail

The LSEG Retail & Restaurant Index delivered a strong start to 2026, with first-quarter earnings growth reaching 27.2%, supported by a resilient labor market, a historic tax refund season, and continued consumer spending aided by higher-than-usual promotional activity. While 74% of companies exceeded earnings expectations, the magnitude of earnings surprises remained below historical averages, suggesting earnings momentum is beginning to normalize.

Looking ahead to the second half of 2026, the retail landscape is expected to become increasingly challenging. Consensus forecasts for second-quarter earnings growth have been revised sharply lower as retailers contend with moderating consumer spending, persistent inflationary pressures, higher fuel costs, tariffs, and growing geopolitical uncertainty. Consumer behavior is also becoming more polarized across income groups. Higher-income households continue to support premium retailers, while middle- and lower-income consumers are increasingly prioritizing value, benefiting off-price retailers and essential consumer categories.

Despite the broader slowdown, several areas of the consumer sector continue to demonstrate resilience. Hotels, Restaurants & Leisure, Leisure Products, Consumer Staples, and Personal Care Products are expected to deliver solid earnings growth throughout 2026, reflecting consumers' continued willingness to spend on experiences and everyday necessities. At the company level, retailers with differentiated brands, pricing power, and strong value propositions, including luxury and off-price operators, remain best positioned to outperform.

Pricing remains a critical theme entering the second half of the year. Rising consumer and producer prices indicate that inflationary pressures are continuing to build across retail supply chains. Retailers have responded by increasing promotional activity, with discount penetration reaching its highest level in six years. However, average markdowns have remained historically low, suggesting retailers are adopting a more disciplined promotional strategy designed to stimulate demand while preserving margins.

LSEG research shows a widening divide in same-store sales performance. Fewer than half of retailers in the LSEG Same-Store Sales Index are expected to generate positive comparable sales growth in 2026, underscoring the uneven nature of consumer demand. E-commerce continues to provide a modest tailwind, although online sales growth has stabilized at a sustainable pace and brick-and-mortar stores continue to account for the majority of U.S. retail spending.

Overall, the outlook for the remainder of 2026 points to a more selective operating environment. Retailers with strong balance sheets, disciplined inventory management, pricing power, and differentiated customer propositions should be best positioned to navigate ongoing macroeconomic headwinds. Conversely, companies with limited pricing flexibility, weaker consumer demand, or heavy reliance on promotional activity are likely to face continued pressure on margins and earnings as the year progresses.

## Funds

Recent global fund flows indicate a market where investor enthusiasm for artificial intelligence overshadows concerns over geopolitics, particularly in the US.

While money market and bond funds initially dominated inflows in late 2024, investors shifted back toward equities following market volatility triggered by US tariff announcements in 2025, often using market corrections as buying opportunities.

US and non-US investors, however, have taken different paths. Throughout 2024 and 2025, US investors were distinctly 'risk-on', rotating from equity funds to money market and bond funds. By contrast, investors outside the US continued allocating strongly to equities alongside maintaining liquidity buffers.

That changed in 2026, as US investors became significantly more bullish, driving strong inflows into US large-cap and information technology funds despite heightened geopolitical tensions. This optimism appears closely linked to enthusiasm for AI-related investments. Fund flow data suggests that confidence in AI-driven growth has increasingly outweighed concerns over tariffs, wars and other geopolitical risks, particularly among US investors.

## Agency RMBS

The Agency RMBS market has remained resilient through the first half of 2026, supported by stable issuance, improving housing inventory, and moderating home price appreciation. Existing home sales have stabilized near 4 million units, while inventory has increased from year-end levels, helping to ease some of the supply constraints that have weighed on the housing market in recent years.

Mortgage rates have remained relatively stable, though affordability challenges and the mortgage rate lock-in effect continue to restrain housing activity. Prepayment speeds increased during early 2026, driven primarily by seasonal turnover and refinancing activity among higher-coupon borrowers. Looking ahead, interest rates, housing supply, labour market conditions, and ongoing housing policy developments will remain key drivers of prepayment behaviour and overall Agency RMBS performance through the remainder of 2026.

## Non-Agency RMBS

Non-agency RMBS enters mid-2026 with strong issuance momentum. Public Non-QM issuance reached approximately \$37.6bn in Jan–Apr 2026, up from \$20.1bn in Jan–Apr 2025, while Jumbo 2.0 issuance rose to approximately \$20.2bn, up from \$12.2bn.

Non-QM AAA spreads tightened materially from the 2022/23, reaching the low-110 bps area in early 2026 before widening in March and partially retracing in April–May. Jumbo 2.0 mortgage rates have also remained close to conforming rates.

Collateral performance differs meaningfully across sectors. Jumbo 2.0 borrowers generally have higher FICO scores and materially lower early delinquencies, while Non-QM loans carry higher coupons and more borrower / documentation complexity. Still Non-QM have proven credit risk stability and lower expected losses.

Prepayment behaviour remains a major risk. Across non-agency fixed-rate cohorts, prepayments are well below the 2020/2021. In the 2025 cohorts, Jumbo 2.0 prepayments picked up more sharply than Non-QM, suggesting that prime jumbo borrowers remain more refinance- and mobility-sensitive, while Non-QM borrowers may face greater refinancing friction. At the same time Jumbo 2.0 prepayments have been dropping and we expect this trend to continue.

Issuer call behaviour is now a major duration and extension-risk theme for Non-QM and several Jumbo 2.0 deals. There is a strong relationship between call activity and the economics of refinancing existing securitization liabilities into new deals. Deals originated in the low-rate period remain much less likely to call, while selected higher-coupon 2022–23 deals may become callable earlier if market execution improves.

The key question for the rest of 2026 is durability. There has been issuance growth, spread tightening and low cumulative losses. The next test is whether the sector can maintain performance, liquidity and structural discipline as recent vintages season and issuance continues to scale.

## CMBS

### Agency CMBS

Agency CMBS had a strong 1H2026 despite heightened geopolitical tensions, higher oil prices, and renewed inflation concerns. Issuance reached \$71.4 billion (+34.0% YoY). Spreads recovered quickly from a brief March-April widening episode. Credit performance improved on steady multifamily fundamentals. And prepayments remained subdued due to limited refinancing incentives and strong call protection.

Looking into 2H 2026, we expect agency CMBS to remain supported by strong market demand and agency liquidity, despite ongoing macroeconomic uncertainties. We therefore frame our outlook under three scenarios:

Base case: Stabilizing inflation and gradual improvement in multifamily fundamentals support strong issuance, stable-to-tighter spreads, and resilient credit performance.

Stress case: Elevated inflation and Fed's pivoting to tighten lead to wider spreads, slower issuance, and increased pressure on property fundamentals and credit performance.

Some of the forecasts for the agency CMBS market in 2026 are summarized below:

Base case: \$170 billion total issuance; spreads tighten by 2-3 bps; GNPL delinquency remains in the 0.6-0.8% range, DUS delinquency at 0.20-0.30%, and Freddie MF delinquency at 0.50-0.55%.

Stress case: \$130 billion issuance; spreads widen by 15-35 bps; GNPL, DUS, and Freddie MF delinquency rate rise to 1.0%, 0.40-0.55%, and 0.60%, respectively.

For prepayments, we expect activity to remain broadly subdued. GNPL prepayments should stay low overall, with occasional healthcare-related CPR spikes driven by operator transitions and industry consolidation. Fixed-rate DUS and Freddie K loans are expected to maintain low and stable CPRs given strong call protection, while floating-rate loans remain the primary source of prepayment volatility due to refinancing opportunities, cap expirations, and business plan completions.

### Non-Agency CMBS

Despite renewed inflation pressure and Fed rate hike risk, we remain cautiously constructive on the outlook for 2H2026 and beyond. Capital markets remain open and investor demand for securitized CRE debt has been resilient, but high rates continue to limit refinance proceeds and keep maturity risk elevated.

Non-agency CMBS issuance totalled \$96.1 billion in 1H2026, nearly 20% above 1H2025, driven by healthy SASB volume and a stronger-than-expected recovery in CRE CLO. We would keep our 2026 full-year SASB issuance forecast unchanged at \$110 billion, raise our CRE CLO forecast from \$35 billion to \$55 billion, and lower our conduit forecast from \$35 billion to \$30 billion, as conduit loan availability remains constrained.

Credit performance remained broadly stable in 1H2026 with signs of stabilization in office, although lack of purchase transactions slowed price discovery and liquidation of troubled properties. We maintain our YE2026 projection of 7% delinquency rate overall (vs. 6.66% currently) and 11% for office (vs. 10.43% currently). We would reduce our YE2026 CRE CLO delinquency forecast from 4% to 3%, reflecting solid sector performance and improved market liquidity.

Maturity performance of conduit CMBS loans weakened in 1H2026, while SASB and CRE CLO outperformed as capital availability shifted toward large single-asset transactions and transitional lending. We also find conduit CMBS maturities in 2H2026 may continue to be under pressure with only 57.2% of balance likely to refinance upon maturity.

In conclusion, we expect continued non-agency CMBS market growth in 2H2026, led by SASB and CRE CLO, while cautioning that higher-for-longer rates, inflation uncertainty, and refinancing pressure remain the key risks.

## Collateralized Loan Obligations (CLO)

As we move into the second half of 2026, the CLO market remains resilient, but it faces major headwinds including tighter arbitrage margins, limited new loan supply, software-sector weakness amid AI disruption concerns, and macro volatility driven by rate path and geopolitical uncertainty. While sustained investor demand continues to support CLO liabilities, compressed asset spreads and volatile loan prices have reduced equity profitability and made new-issue economics more challenging. Refi/reset activity should remain active where liability savings are meaningful, but resets are likely to become more collateral-dependent as managers face greater difficulty cleaning up portfolios and preserving par.

In our updated forecast, we project 2026 CLO new issuance of \$172bn, including \$136bn of BSL CLO issuance and \$36bn of Private Credit CLO issuance, down from our beginning-of-year total forecast of \$192bn. Refi/reset/reissue volume is expected to reach \$267bn, below the exceptional 2025 pace but still supported by tight liability spreads and a meaningful pool of deals exiting non-call or approaching the end of reinvestment. We expect liability spreads to tighten modestly by YE with BSL AAA spreads at 125bps and BB spreads at 525bps, reflecting lower supply and strong demand.

Credit fundamentals are expected to remain steady in 2H2026, with Caa-or-lower exposure at 5.50% and the TTM default rate at 2.25% by YE. For CLO performance, we maintain our Junior OC cushion forecast at 3.25%, while lowering our equity cash-on-cash forecast to 12.00% to reflect tighter arbitrage, weaker par build, and lower equity distributions in 1H2026.

Overall, we maintain a constructive but more cautious outlook for the CLO market in 2026. Active primary and capital markets provide a solid backdrop, but elevated inflation and rate hike concern will keep pressuring market sentiment. Credit dispersion will remain a key theme, with risks concentrated in software and other weaker borrowers with cash flow and refinancing stress. As such, collateral quality, software exposure management, par preservation, and manager selection remain critical for CLO performance in the second half of the year.

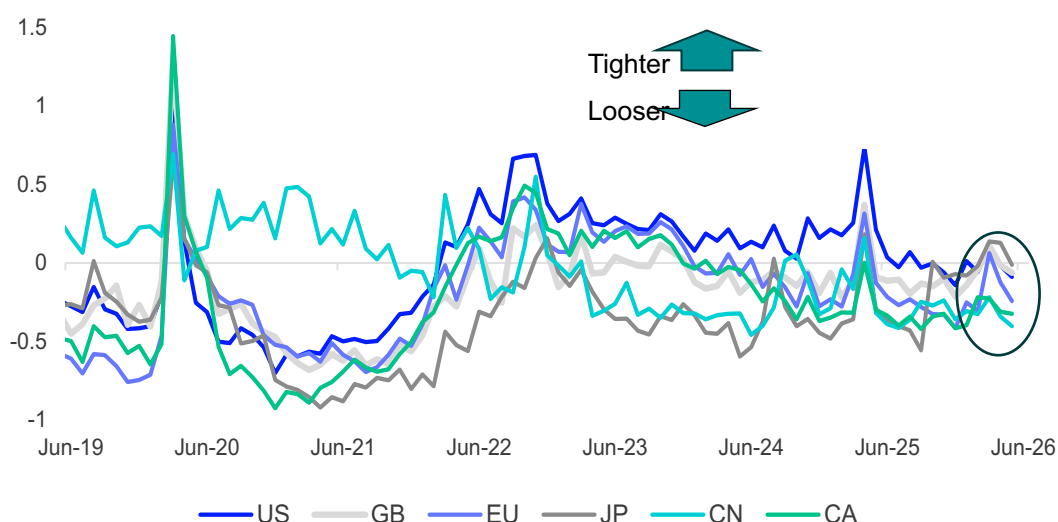
## Section 1 – Macro Outlook

### An oil shock - but when inflation is lower than 2022

The global economy and financial markets began 2026 in a relatively benign environment, with inflation rates generally close to target levels, and modest but positive growth, helped by policy easing in 2024-25, and despite US tariff turbulence in 2025. Oil prices were near the lower end of the \$60 to \$80 range prevailing since 2024, equity markets at, or near all-time highs, and corporate credit spreads at 10-year lows. We pointed out in our 2026 Outlook<sup>1</sup> that recession risks appeared relatively low, despite the uncertainty of tariff effects, excluding economies hit hard by sizeable trade exposures to the US (i.e., Canada). But this outlook was adversely affected by the conflagration in the Middle East, from February 26th onwards, and associated oil price shock. The IEA described this as the “worst ever oil shock”, given the scale of the potential energy supply disruption through the Straits of Hormuz of up to 20mb/d<sup>2</sup>, or about 20% of global production, though actual supply loss appears to have been significantly less at 10-12mb/d<sup>3</sup>, or about 11% of global supply in March.

Financial conditions in major economies deteriorated in March 2026, as stagflation and central bank tightening fears grew, but the moves were relatively modest compared to both the tariff turbulence in Q2 2025, and the Ukraine and monetary tightening shock in 2022-23. Thus, the FTSE Russell Financial Conditions indicators shown in Exhibit 1 remain near longer term means.

**Exhibit 1: FTSE Russell Financial Conditions indicators (stand.dev.from long term mean)**



Source: FTSE Russell, data to May 31, 2026.

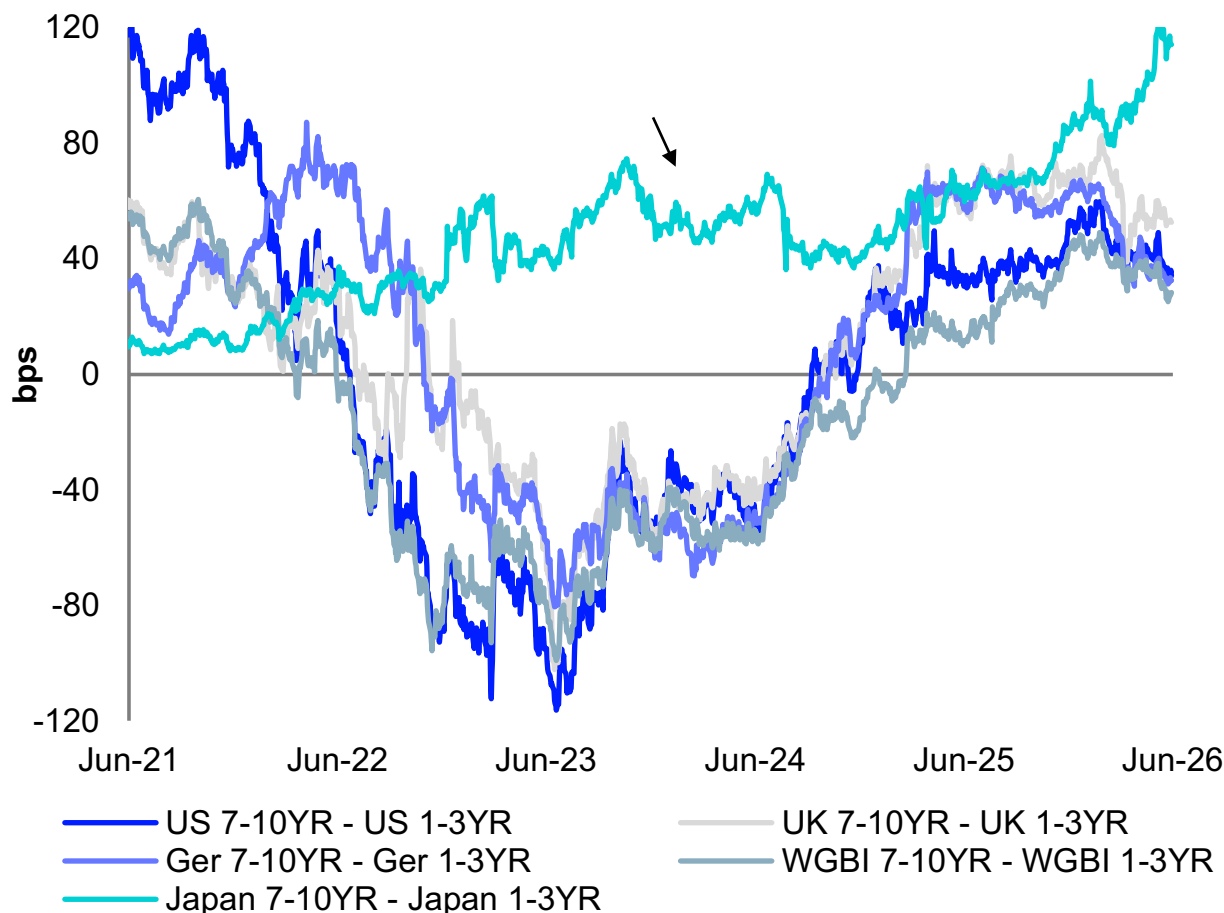
### Although the 2026 energy shock worsens growth/inflation trade-offs ...

The initial financial market sell-off in March, was driven by a combination of stagflation fears, concern about a long-lasting increase in oil prices, and the risks of central banks raising rates to preserve inflation targets. As a result, government bond yield curves bear flattened, with short yields rising relative to medium and longer dated maturities, as bond markets discounted a higher profile for central bank policy rates, as Exhibit 2 shows.

<sup>1</sup> See [2026-year-ahead-outlook.pdf](#) LSEG, January 2026.

<sup>2</sup> Dallas Fed, IEA estimates

<sup>3</sup> IEA, Reuters estimates, March 2026.

**Exhibit 2: Selected G7 and global yield curve spreads**

Source: FTSE Russell, data to June 2026.

#### ....there are quite different macro settings for the 2022 and 2026 energy and inflation shocks

This severe government bond market reaction in March/early April, and bear flattening (yields rising more in short maturities than longs) may reflect the scale of the monetary tightening and inflation shock that followed the Ukraine energy shock in February 2022, and the stagflationary outcomes after the oil shocks in the 1970s and 1980s. In 2022-23, rates then rose by up to 525 bp in the G7 nations, comfortably exceeding initial bond market expectations. But the macro-economic setting for the twin shocks was, and is, substantially different. The Ukraine energy shock coincided with a strong rebound in global growth, domestic demand and inflation, after Covid Lockdowns ended, and some central banks already tightening policy.

#### Demand-pull inflation shocks traditionally last longer...

Indeed, the 2022-23 episode was reminiscent of the kind of demand-pull inflation seen in the 1970s and 1980s, when inflation expectations and wage settlements often de-stabilised causing higher inflation to persist for some years. *Ceteris paribus*, demand-pull inflations carry higher risks of persistence, since excess demand growth means price increases to consumers are easier to pass on<sup>4</sup>. Cost-push inflation pressures, facing weaker final demand, are more likely to be dissipated in supply chains with some contraction in corporate margins. The 2021-23 inflation shock was particularly difficult because the Ukraine energy shock was superimposed on economies with strong demand growth, and cost-push pressures in tradeable goods particularly, after dislocation of supply-chains during Covid.

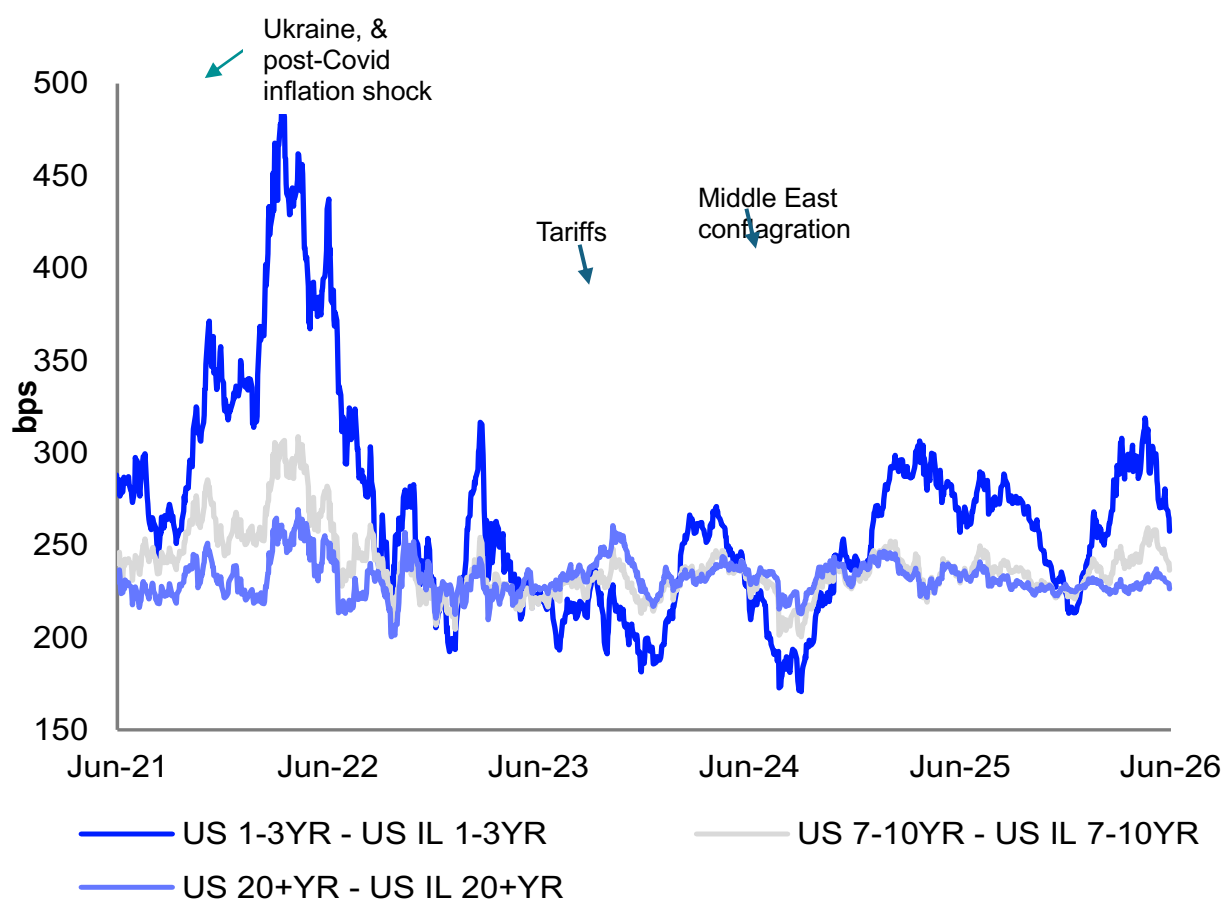
<sup>4</sup> See – “Retrospectives: Cost-Push and Demand-Pull Inflation: Milton Friedman and the “Cruel Dilemma” “, Johannes A. Schwarzer, Journal of Economic Perspectives, Winter 2018.

In contrast, the 2026 Middle east conflagration caused a negative energy supply shock, beyond the control of central banks. This in turn has driven some cost-push (headline) inflation but has occurred in a more subdued growth and inflation environment, even if some economies have experienced inflation target overshoots, ie, US and UK.

### ...and more benign macro setting explains muted response in inflation expectations

The more benign macroeconomic setting in 2026 also helps explain the muted reaction in inflation expectations compared to 2022, measured by inflation breakevens<sup>5</sup>, and largely confined to short-term expectations, easing central bank fears of 2<sup>nd</sup> round effects from the increase in headline inflation. Exhibit 3 shows movements in inflation breakevens since Covid and the impact of recent shocks.

**Exhibit 3: Selected US inflation breakevens since 2021.**



Source: FTSE Russell, data to June 12, 2026.

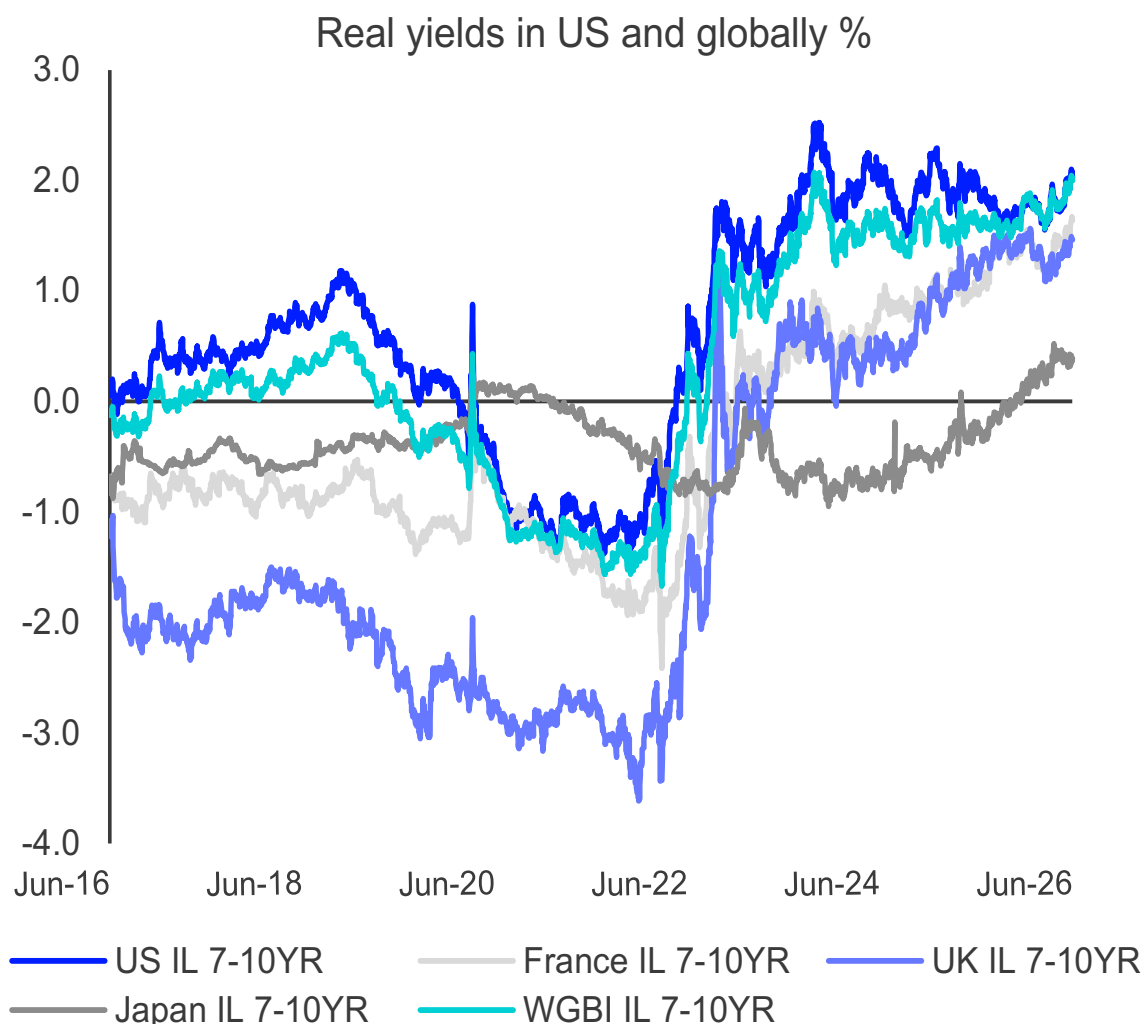
<sup>5</sup> Measured by the difference between nominal yields and real yields on government bonds of the same maturity.

### Markets reacted differently to the energy shock unwinding, though bond yields also fell

Government bond yields have fallen modestly since the April peaks, and Middle East ceasefire, but the sharp decline in oil prices and the strong outperformance by equities relative to government bonds remains a feature, even if US equity market gains are concentrated in a small number of stocks and dominated by the AI boom <sup>6</sup>. Energy price increases will take some months to work through inflation indexes, though G7 central banks have, in the main, been prepared to look through increases in headline inflation, on the view this is a transitory increase in inflation, driven by a negative energy supply shock, unless 2<sup>nd</sup> round effects become evident in inflation expectations <sup>7</sup>. Remember also that a one-off increase in energy price levels does not translate into a permanent increase in inflation rates, unless it becomes embedded in higher inflation expectations, which is why 2<sup>nd</sup> round effects are critical for central banks.

This raises the more fundamental question of why nominal and real yields on G7 government bonds remain near post-Global Financial Crisis highs, as Exhibit 4 and Exhibit 5 show, and whether this reflects more resilience in global growth to the energy shock than initially assumed?

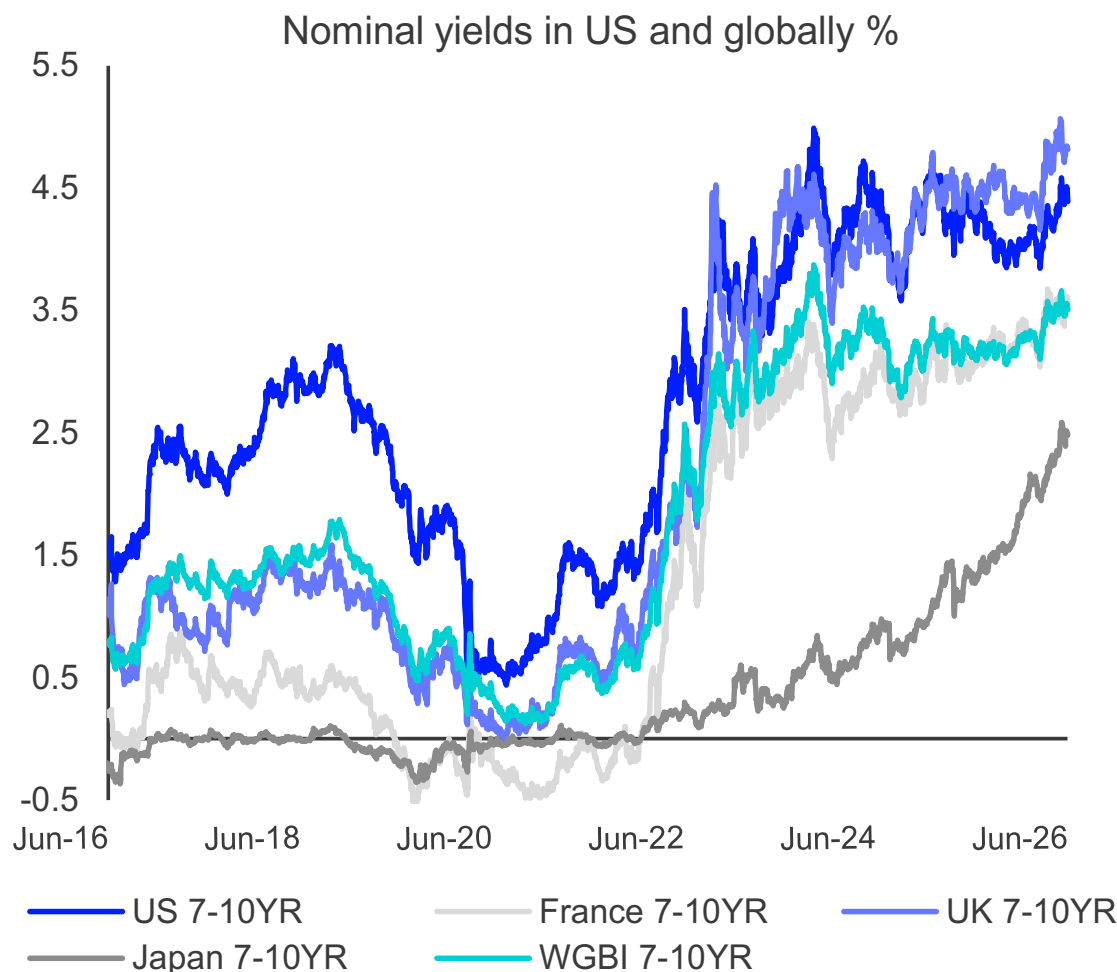
#### Exhibit 4: Real yields in US and globally



Source: FTSE Russell, data to June 2026.

<sup>6</sup> See June Performance Report, FTSE Russell

<sup>7</sup> See US Fed FOMC June statement.

**Exhibit 5: Nominal yields in US and globally**

Source: FTSE Russell, data to June 2026.

**A different type of oil shock than the 1970s & 1980s, with reduced impact?...**

In that regard, it is notable the IMF's April GDP forecasts for 2026-27 changed only modestly, and that the net impact of the oil shock varies considerably, depending on the net energy status of individual economies (ie, importer or exporter). Since Europe relies far less on Middle East oil supplies than APAC, and the US and Canada are significant net energy exporters, the 2026 oil supply shock is also largely an APAC energy shock. Although much depends on the duration and scale of the 2026 energy and geopolitical shock, and whether equilibrium oil prices settle in higher ranges, several factors suggest both oil supply and demand elasticity, beyond the short term, are higher than in the 1970s and 1980s.

These factors range from OPEC's lower share of global production (from about 50% to about 35% now <sup>8</sup>), to a higher share of US, Canadian, Norwegian and Brazilian production, to deeper oil markets, allowing more hedging of price risks, to greater strategic oil reserves, and floating storage, to faster capital cycles in oil production. Financially viable reserves have also surged due to technology improvements in fracking, etc. All of which suggest oil supply elasticity is notably higher now, globally. Meanwhile, demand elasticity has been boosted by more alternative fuels and lower energy coefficients in GDP.

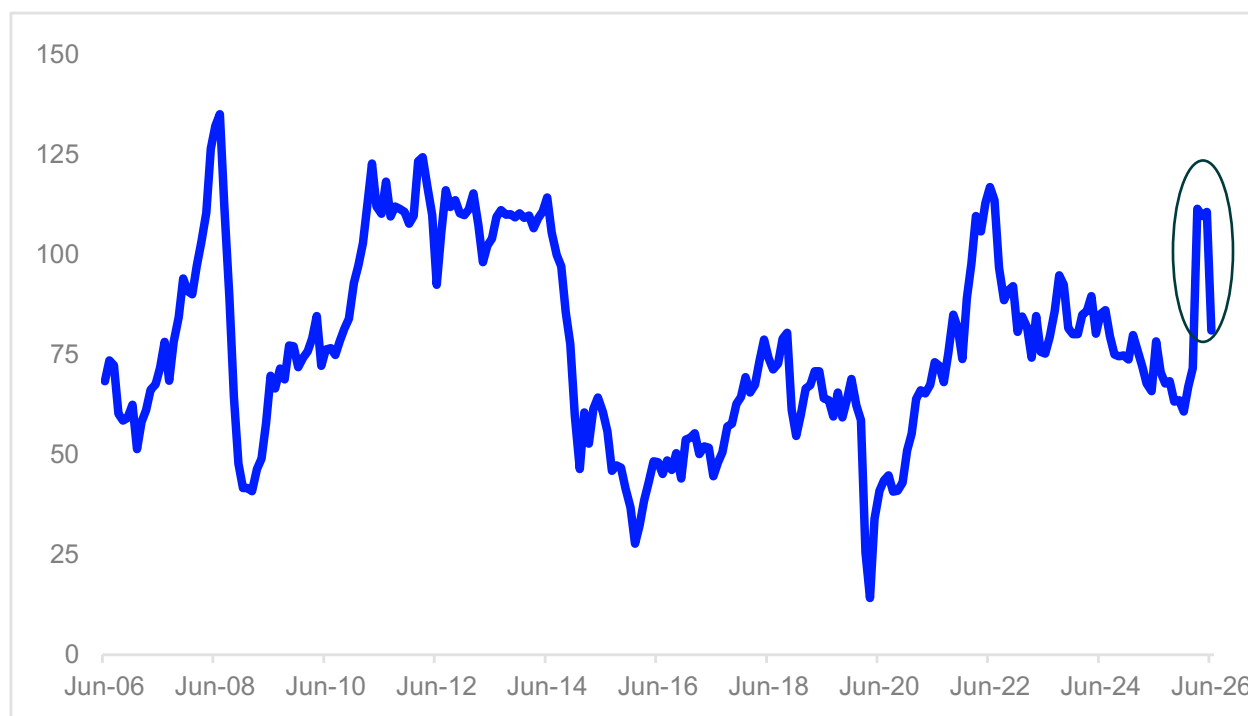
<sup>8</sup> IEA data.

Thus, some estimates of the world economy's oil intensity – the oil required to produce a single unit of GDP – are roughly 70% lower due to increased fuel efficiency compared with the 1970s.<sup>9</sup> In addition, the global economy faced significant excess supply in oil markets when the Middle East conflagration began, which the IEA estimates at 3.6 mb/d for 2026 as a whole.<sup>10</sup>

#### ....and a possible glut in the medium term?

The other possibility that increases in oil supply elasticity raise is more price instability, and even a divergent cobweb in dynamic pricing, whereby oil prices fall sharply in response to a renewed supply glut. Given the increased role of futures contracts, this may explain why reactions to the Middle East ceasefire and Memorandum of Understanding have been so pronounced in oil markets, as Exhibit 6 shows.

**Exhibit 6: Crude oil, Brent spot price US\$/barrel**



Source: LSEG, data to June 24, 2026.

Recent falls in oil prices, evidence of a more benign oil shock in 2026, and central bank caution on raising rates all suggest government bond yields near post-Global Financial Crisis highs are likely driven by other factors, and that there has been a regime shift to higher rates and yields. These factors include (1) higher government debt issuance, due to more active, and stimulative fiscal policy, (2) a rise in the term premia, as inflation uncertainty has increased, and perhaps (3) the impact of the AI boom in raising productivity and the marginal product of capital.<sup>11</sup> As a result, even though there has been some bear flattening since the energy shock occurred, yield curves now have significant gradients out to longer maturities.

A financial regime in which 10 yr US Treasuries are in a 3 to 5% range, whilst equities perform robustly, powered by strong earnings growth and new technology, occurred during the Goldilocks era in the early-2000s, before the GFC, so the current regime is not unique. There remain macro-economic risks, notably in higher government debt issuance, and geo-politically, but structural changes in energy markets reduce the risk from oil shocks, even if the inflation shock delays further policy easing.

<sup>9</sup> See "The changing impact of fossil fuel shocks on the UK economy ", UK Office for Budget Responsibility, July 2022.

<sup>10</sup> See "How global oil supplies have readjusted to help fill the huge gap left by the Strait of Hormuz shock ", IEA, June 2026.

<sup>11</sup> See [AI and government bond yields – onwards and upwards? | LSEG](#), June 2024.

## Section 2 – Equities Outlook

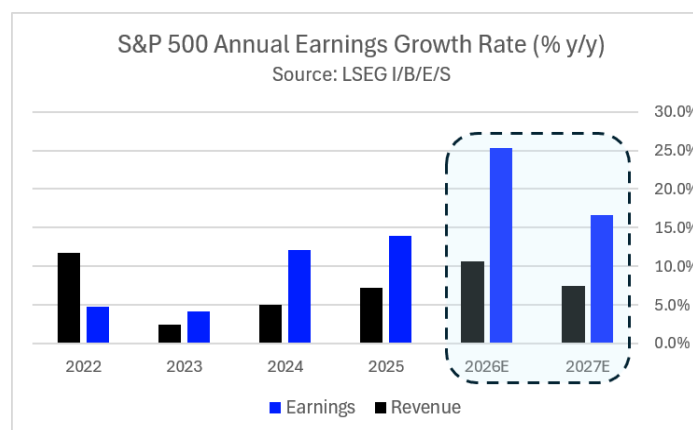
### Record-High Earnings Expectations and Returns on AI Investment

#### Starting 2026 Off with A Bang: Highest Annual Growth in Two Decades

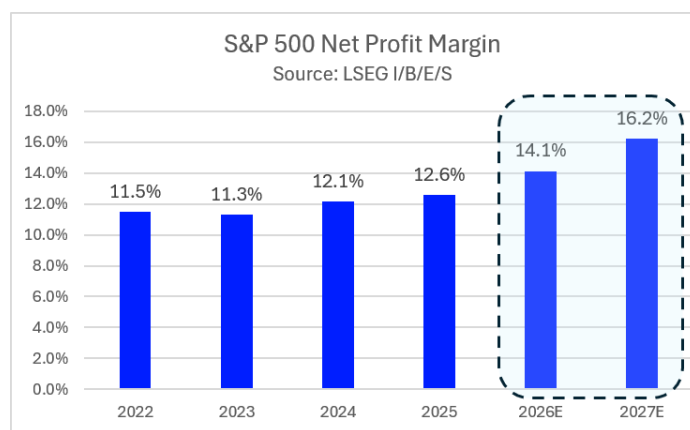
Consensus forecasts imply earnings growth of 25.4% this year, which marks the strongest non-recessionary, non-pandemic growth rate in more than two decades and is expected to grow by a further 16.6% increase in 2027 (Exhibit 7). Technology remains the primary engine of growth, accounting for roughly half of total S&P 500 earnings growth in both years.

With earnings expected to grow at more than twice the pace of revenue, net margins have reached record highs at 14.1% this year and 16.2% in 2027, with Technology and Energy seeing the largest improvements in margin expectations (Exhibit 8).

**Exhibit 7: S&P 500 Annual Growth Rates**



**Exhibit 8: S&P 500 Net Profit Margin Forecasts**



Source: LSEG I/B/E/S

#### Q1 Earnings Season: Stronger Than Headlines Suggest

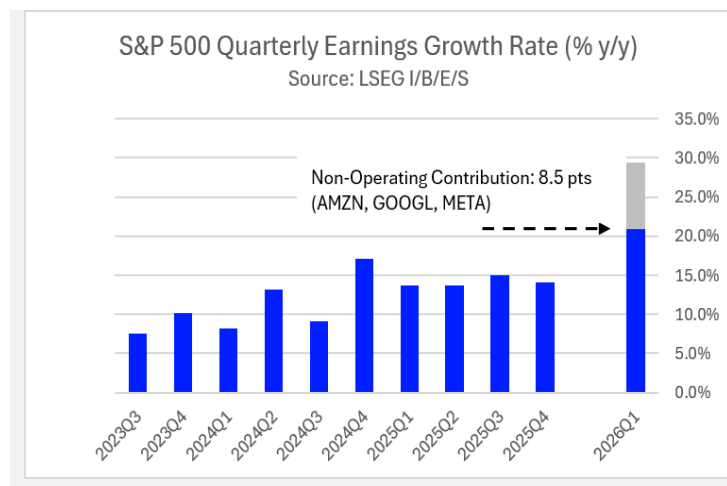
Q1 delivered one of the strongest earnings seasons on record, with earnings growth of 29.4%. Aggregate earnings rose to a record \$684 billion, increasing 8.8% sequentially, while revenue growth accelerated to 11.4% year-over-year, the strongest pace since 2022.

Information Technology and Communication Services accounted for roughly two-thirds of total earnings growth. Analyst forecasts proved too pessimistic heading into the quarter, with 10 of 11 sectors posting earnings beat rates above their prior four-quarter average, led by Information Technology, which recorded an all-time high beat rate of 98.6%.

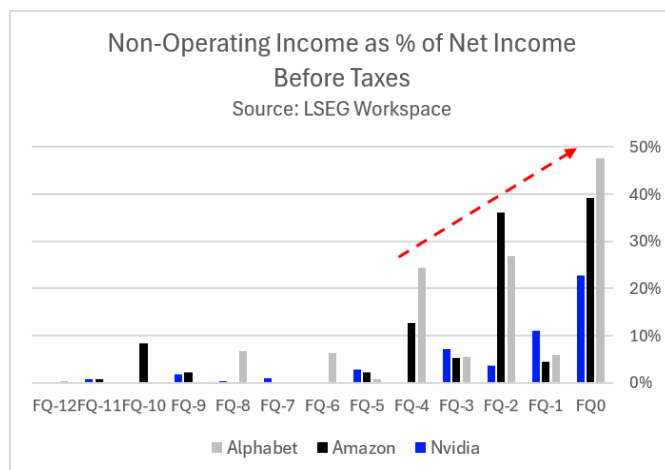
A defining feature of the Q1 earnings season was that a meaningful portion of earnings growth was driven by non-operating investment gains from Alphabet and Amazon. Mark-to-market (MTM) gains in Anthropic provided a \$53 billion tailwind for the two companies and accounted for 48% of pre-tax income at Alphabet and 39% at Amazon. Nvidia also saw a large MTM gain in its public investment portfolio. This dynamic is likely to persist as several mega-cap technology companies hold sizeable investment portfolios across both private and publicly listed companies, making unrealized gains and losses a more meaningful contributor to reported earnings (Exhibit 10).

To demonstrate the impact, Consumer Discretionary earnings growth fell from 40.5% to 11.8% in Q1 when adjusting for non-operating gains, while Communication Services growth declined from 51.0% to -0.5% after additionally adjusting for Meta's one-time tax benefit.

At the index level, headline growth fell from 29.4% to 20.9%, yielding an 8.5 percentage point impact from non-operating items (Exhibit 9). Although non-operating gains had a meaningful impact, the adjusted Q1 growth rate of 20.9% still marks the highest quarterly growth rate since 2018 when excluding the pandemic recovery period.

**Exhibit 9: S&P 500 Quarterly Earnings Growth Rate**

Source: LSEG I/B/E/S

**Exhibit 10: Non-Operating Income as Percentage of Total Income**

## Earnings Breadth is Improving, but Concentration Persists

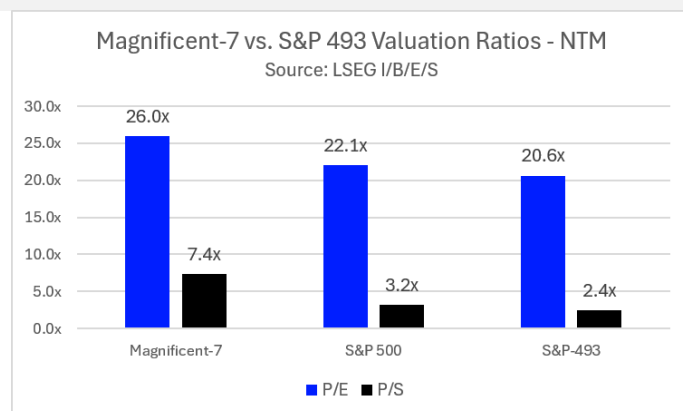
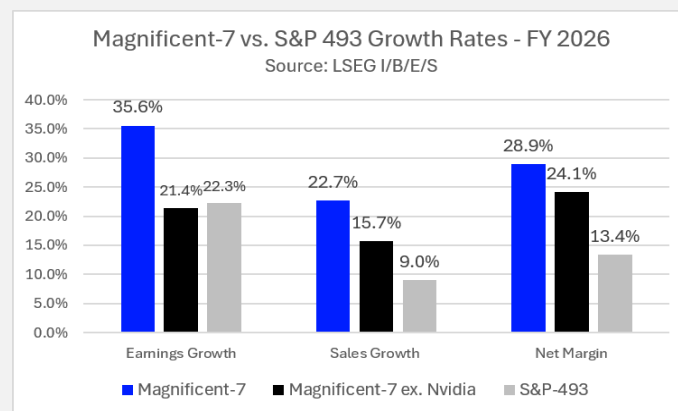
While the Magnificent-7 (Mag-7) has been the primary engine of earnings growth for the last few years, leadership has gradually broadened to the S&P-493, who has significantly outperformed the Mag-7 year to date, compressing the valuation gap to a multi-year low (Exhibit 11).

This reflects two important developments. First, the benefits of AI are beginning to extend beyond the hyperscalers to a broader set of companies, including suppliers of AI infrastructure such as memory, networking, storage, power and cooling. Second, greater emphasis is being placed on the substantial capital required to build that infrastructure, as Mag-7 hyperscalers continue to shoulder most of the investment, placing increasing pressure on free cash flow despite a robust earnings outlook.

Mag-7 grew earnings by 61.2% in Q1, or 32.9% when adjusting for non-operating gains. Importantly, consensus estimates indicate a narrower spread between the two groups, where the S&P-493 is expected to grow Q4 earnings at a faster rate than the Mag-7, a feat not seen since 2022.

Part of this rotation can be explained by the concentration within the Mag-7, specifically Nvidia, who is driving over half of the group's growth. Mag-7 earnings are expected to rise by 35.6% in 2026 and 20.8% in 2027, with Nvidia contributing 53% and 61% of total growth in both years.

Excluding Nvidia, the adjusted "Mag-6" earnings growth rate falls to 21.4% in 2026, slightly below the 22.3% growth expected from S&P 493 (Exhibit 12).

**Exhibit 11: Magnificent-7 Valuation Ratios – P/E & P/S****Exhibit 12: Magnificent-7 Earnings, Sales, Margins**

Source: LSEG I/B/E/S

The concentration within the Mag-7 also extends to the broader index, both on a market-cap and earnings basis. While market-cap concentration is well understood, earnings concentration receives far less attention despite having important implications for the durability of aggregate earnings forecasts.

Communication Services exhibits the highest level of earnings concentration, with its two largest earnings contributors accounting for 63% of total sector earnings. Consumer Discretionary, Energy and Information Technology also remain highly concentrated, while Industrials, Real Estate and Utilities are considerably more diversified (Exhibit 13).

Much of this concentration within Communication Services, Consumer Discretionary and Information Technology reflects the ongoing AI investment cycle, where hyperscalers account for both the majority of capital spending and a disproportionate share of earnings growth. Understanding whether that investment continues to generate attractive economic returns is critical to assessing the sustainability of the current earnings outlook.

**Exhibit 13: Earnings and Market-Cap Concentration**

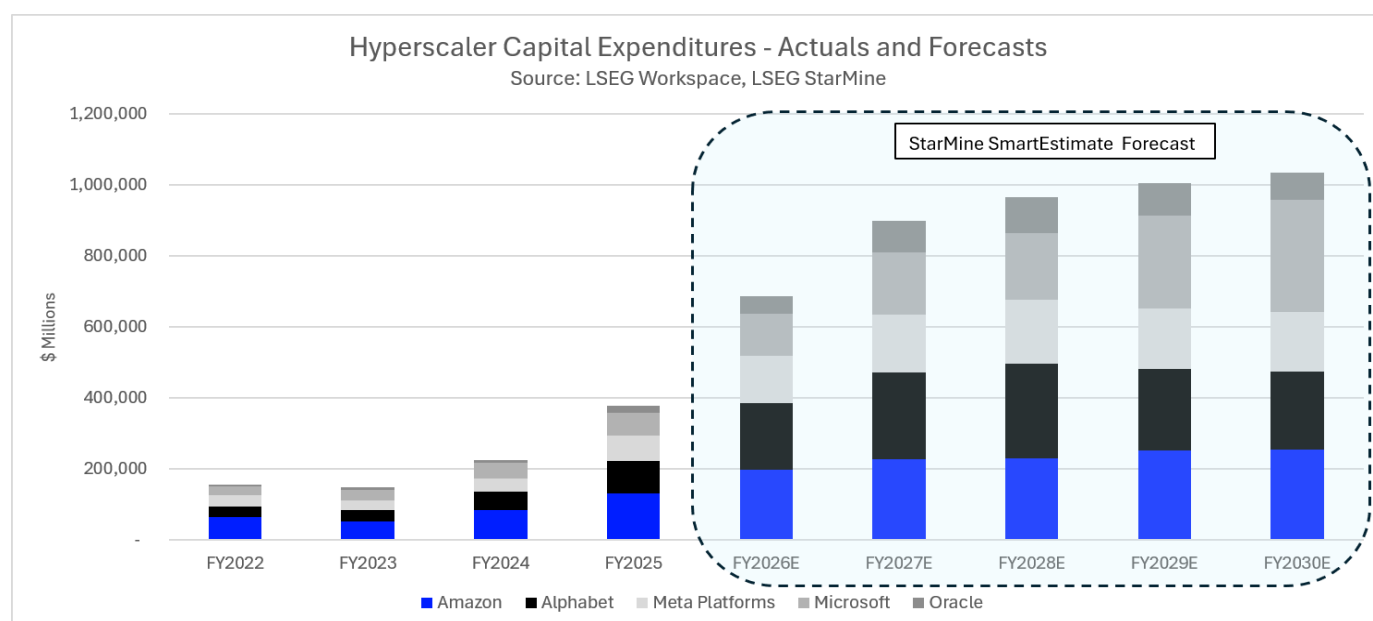
Source: LSEG I/B/E/S

## The AI Capex Cycle: Peak Growth, Not Peak Spending

AI infrastructure spending continues to accelerate, with aggregate capex across Amazon, Alphabet, Meta, Microsoft and Oracle forecast to reach approximately \$730 billion in 2026, up 40% from the start of the year based on StarMine SmartEstimates (Exhibit 14).

Although spending is expected to surpass \$1 trillion by 2029, growth is likely to peak in 2026, with capex growth slowing from 82% this year to mid-single digits by 2028. This marks a key inflection point, as 2026 is likely to represent peak capex growth rather than peak spending in dollar terms. The focus should shift from how much companies are spending to whether that investment is generating attractive economic returns.

**Exhibit 14: Aggregate Capital Expenditures – Actuals and StarMine Forecasts**



Source: LSEG Workspace, LSEG StarMine

While hyperscalers largely remain capable of funding capex through operating cash flow (with Oracle the notable exception), the investment cycle has materially compressed free cash flow generation. Capex as a percentage of free cash flow has climbed to roughly 75% in 2026, while aggregate Net Debt/EBITDA has turned positive for the first time in eight years, indicating that hyperscalers are drawing on their balance sheet strength to support AI infrastructure spending (Exhibit 15).

While market attention has centered on rising leverage and weaker free cash flow, the overlooked point is that AI investment remains economically justified for most hyperscalers today. Measured by the three-year change in Return on Incremental Invested Capital (ROIIC) relative to the current Weighted Average Cost of Capital (WACC), Meta generates the greatest value creation, with a spread of 34%, followed by Alphabet at 21%. Both companies have a high degree of capex intensity yet generate economic returns well-above their cost of capital. Microsoft remains the most capital-efficient operator in the group, with the lowest capex intensity at 67% (Exhibit 16).

Exhibit 15: Aggregate Net Debt/EBITDA vs. Capex/ FCF

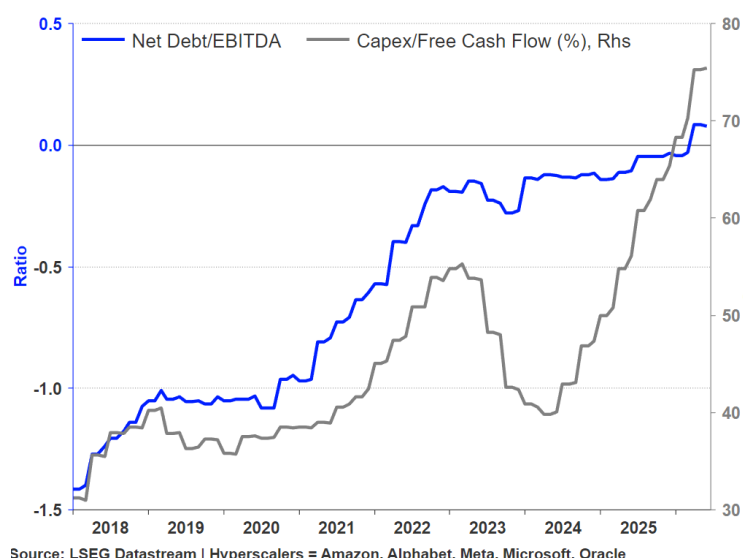
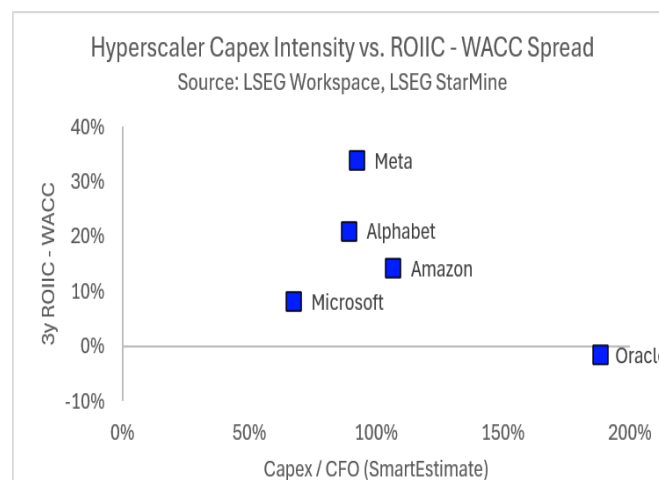


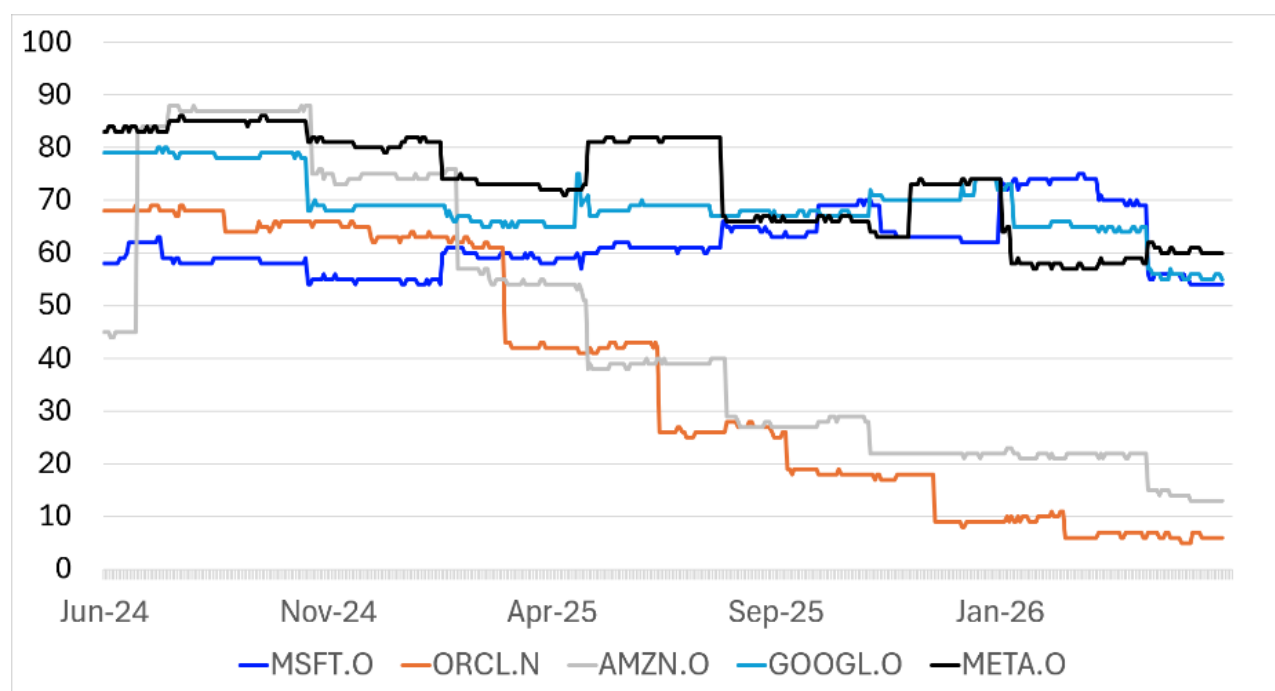
Exhibit 16: ROIIC and WACC vs. Capex Intensity



Amazon's capex now exceeds operating cash flow but continues to generate positive economic returns. Oracle remains the notable exception, with capex approaching 200% of operating cash flow but a ROIIC-WACC spread of -2%, indicating that incremental investments have yet to generate returns sufficient to cover their cost of capital.

This distinction is also reflected in the StarMine Earnings Quality (EQ) model, which measures the sustainability of earnings using accruals, cash flows, operating efficiency, and one-time exclusions. Both Amazon and Oracle have seen a sharp deterioration in EQ score over the past year and sit in the bottom decile, in sharp contrast to their hyperscaler peers (Exhibit 17).

Exhibit 17: StarMine Earnings Quality Score for Hyperscalers



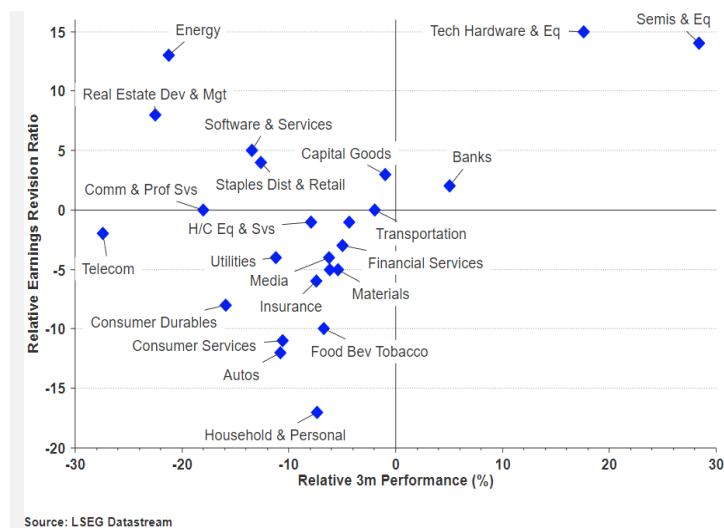
Despite the sharp increase in capital spending, analysts remain broadly constructive on the hyperscaler group. StarMine's Analyst Revision Model (ARM), which measures analyst sentiment using earnings estimate revisions and recommendation changes, assigns Amazon the highest score of 89 (1=bearish, 100=bullish), followed by Alphabet (84), Meta (78), Oracle (73), and Microsoft (69).

Optimism extends across the AI supply chain—including Semiconductors and Semiconductor Equipment—who have experienced the strongest improvement in earnings revisions relative to the broader market (Exhibit 18).

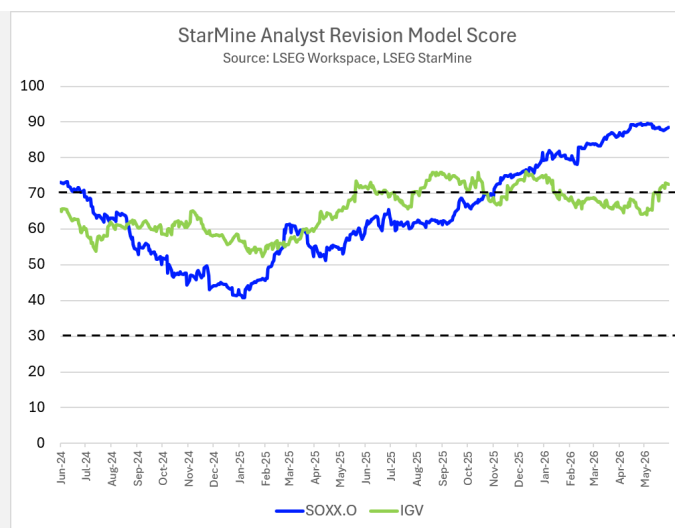
In contrast, Software & Services experienced a sharp sell-off since Q4 2025 and remains approximately 30% below its recent peak amid concerns that large language models will disrupt traditional software subscription models. Yet, the correction has been entirely valuation-driven, as earnings estimates have remained broadly stable and relative earnings revisions continue to outperform the broader index, as shown in the upper-left quadrant.

This view is reinforced by StarMine's Analyst Revision Model (ARM), which shows that analyst sentiment remained broadly constructive throughout the SaaS sell-off. While the Semiconductor ETF (SOXX) has seen sentiment rise sharply over the last year, both SOXX and the Expanded Software ETF (IGV) carry bullish ARM scores above 70 (1=bearish, 100=bullish) (Exhibit 19). The resilience in IGV's ARM score suggests analysts do not view AI as a broad threat to the entire software sector. It is likely that we will see differentiation in sentiment between companies with proprietary data, scalable AI-enabled platforms and pricing power, and those that struggle to defend their competitive position or demonstrate a clear path to AI monetization.

**Exhibit 18: Relative Earnings and Price Performance vs. S&P 500**



**Exhibit 19: StarMine Analyst Revision ETF Scores**



## Valuation: PEG Ratio Falls Below 1

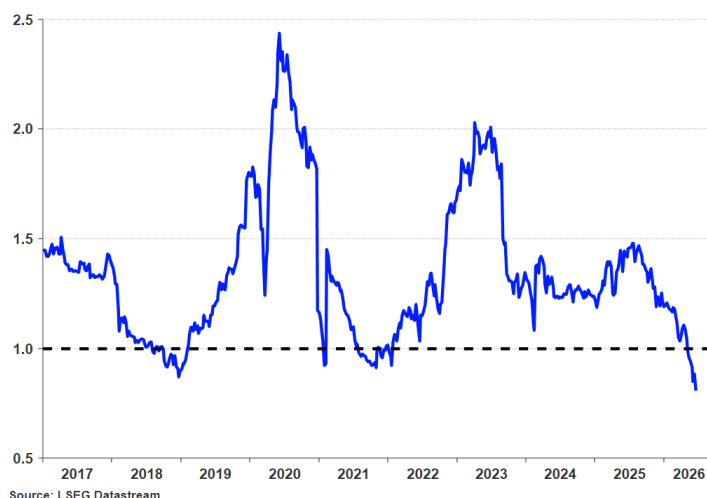
The strength of the earnings outlook is reflected in bottom-up consensus estimates, with FY2027 EPS increasing by nearly \$50 over the past seven months to a record \$400 per share, outpacing S&P 500 price appreciation by more than five percentage points (Exhibit 20).

As a result, the forward P/E has compressed by one turn to 18.4x, despite the index remaining near all-time highs. This is also reflected in the PEG ratio, which has fallen below 1 for the first time in five years as long-term growth expectations have risen to record highs (Exhibit 21). Unlike the internet bubble of 2000, today's market is characterised by rising growth expectations alongside lower valuation multiples. This suggests that markets are looking for further evidence that current growth expectations can be sustained before assigning higher valuation multiples.

Should these growth expectations prove durable over the medium-term, current valuations appear considerably less demanding than headline P/E multiples imply. Technology is particularly notable, trading on a PEG ratio of just 0.51x despite long-term earnings growth expectations approaching 45%.

**Exhibit 20: S&P 500 Valuation Table**

|           | Nov 28, 2025 | Jun 25, 2026 | Change |
|-----------|--------------|--------------|--------|
| S&P 500   | 6,812.61     | 7,357.49     | 8.0%   |
| 2027 EPS  | 351.74       | 400.24       | 13.8%  |
| P/E       | 19.4x        | 18.4x        | -1.0x  |
| LTEG      | 18.2%        | 25.5%        | 7.3%   |
| PEG Ratio | 1.06x        | 0.72x        | -0.34x |

**Exhibit 21: S&P 500 PEG Ratio**

## Conclusion

Corporate fundamentals remain exceptionally strong. Earnings expectations and profit margins are at record highs, earnings leadership is broadening beyond the Magnificent-7, and earnings have outpaced share-price appreciation, leaving valuations more attractive than at the start of the year despite a more hawkish monetary policy outlook. Markets continue to demand evidence that AI-driven earnings growth can be sustained before assigning higher valuation multiples.

Much of the market debate has centred on the scale of hyperscaler AI investment and its impact on free cash flow. However, the data suggests the current investment cycle remains economically justified, with most hyperscalers continuing to generate returns on incremental invested capital above their cost of capital. The next phase of the AI cycle is therefore likely to be defined less by the pace of capital spending and more by the companies capable of consistently converting that investment into durable earnings growth and economic value creation.

## Section 3 – Retail Consumer Outlook

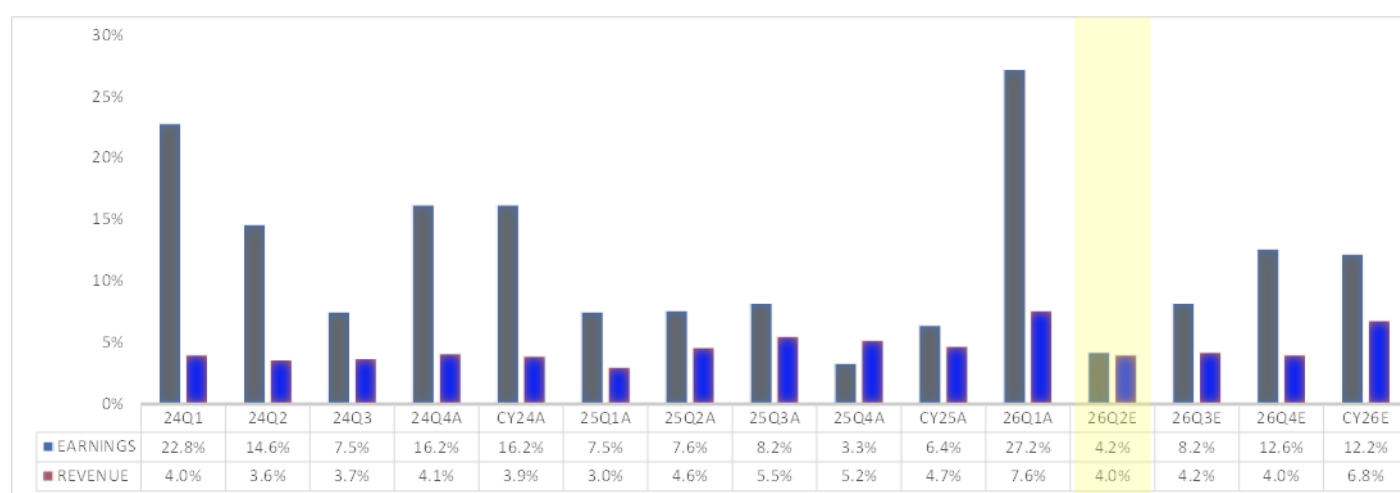
### “Pricing Power, Promotions, and Consumer Priorities”

#### Retail Earnings Outlook

The LSEG Retail/Restaurant Index reported Q1 2026 earnings growth of 27.2% (Exhibit 22). Among the companies that have reported, 74.0% exceeded analyst earnings expectations, 4% met expectations, and 22% fell short. This compares with a typical quarter, when 71% of companies beat estimates, 3% meet expectations, and 26% miss. Over the past four quarters, an average of 70% of companies exceeded estimates, 4% met expectations, and 26% missed.

In aggregate, Q1 earnings were 4.0% above consensus estimates, below both the long-term average earnings surprise of 11.4% and the 6.0% average surprise recorded over the previous four quarters.

**Exhibit 22: The LSEG Retail/Restaurant Earnings Index: Q1 2024 Act – Q4 2026 Est.**



Source: LSEG I/B/E/S

Retail earnings in the first quarter of 2026 received a significant boost from a historic tax refund season, reinforcing consumer spending at a time when the labor market remained resilient. However, recent earnings reports suggest that spending momentum is beginning to moderate and that consumer behavior is becoming increasingly segmented across income cohorts.

Higher-income consumers continue to spend freely on premium merchandise, supporting strong results at retailers such as Williams-Sonoma and Ralph Lauren. Both companies highlighted robust demand for full-price products, underscoring the resilience of affluent shoppers despite ongoing economic uncertainty.

By contrast, middle-income consumers are becoming more selective with discretionary purchases. Best Buy reported continued weakness in appliance sales, while Home Depot and Lowe's noted that customers are delaying larger home improvement projects. At the same time, these consumers remain willing to purchase premium brands when offered at attractive prices, benefiting off-price retailers such as TJX Companies, Ross Stores and Burlington.

Among lower-income households, value remains the dominant purchasing consideration. Dollar Tree reported a 4.5% increase in average ticket size, partially offset by a 1.0% decline in customer traffic, suggesting that budget-conscious consumers are consolidating purchases into fewer shopping trips as higher gasoline prices and other living expenses continue to pressure household budgets.

Looking ahead, consumer sentiment has softened. The LSEG/Ipsos Consumer Sentiment Index declined for the third time in the past four months, reflecting weaker expectations for local economic conditions and reduced confidence in making major household purchases. Consumers' perceptions of both current economic conditions and the outlook have deteriorated since the onset of geopolitical unrest in the Middle East earlier this year. Rising gasoline prices and persistent cost-of-living pressures remain key concerns, leaving overall consumer confidence subdued.

Against this backdrop, analysts surveyed by LSEG have become increasingly cautious on the retail sector's near-term earnings outlook. Consensus forecasts for second-quarter earnings growth have been revised down from 8.1% at the start of the year to 4.2%, reflecting concerns over moderating consumer spending, higher fuel costs, and evolving trade and tariff-related pressures. If achieved, second-quarter earnings growth would represent a sharp slowdown from the 27.2% growth reported in the first quarter (Exhibit 22).

Q2 2026 earnings are currently expected to mark the weakest growth rate of 2026, with consensus forecasts calling for a gradual improvement during the second half of the year. Nevertheless, retailers continue to prepare for an operating environment characterized by cautious consumers, persistent inflationary pressures, geopolitical uncertainty, evolving trade policies, and ongoing tariff-related disruptions. While consumer spending has remained resilient, the margin for error is narrowing as households become increasingly focused on value and affordability.

## Sector Outlook

A closer look at the data shows that, despite this year's broader slowdown, pockets of strength remain concentrated in three consumer categories. The Hotels, Restaurants & Leisure sector is expected to deliver consistently strong earnings growth throughout 2026, suggesting consumers continue to prioritize experiences over goods (Exhibit 23).

The Leisure Products category also posted a sharp 130.9% earnings growth rate in Q1 2026, consistent with recent U.S. retail sales data showing strong year-over-year growth in the hobby and sporting goods segment. This may reflect a shift among increasingly value-conscious consumers toward lower-cost recreational activities. The Consumer Staples and Personal Care Products sectors are also on track to report positive earnings growth in 2026, underscoring the relative resilience of essential and everyday categories while discretionary spending remains under pressure.

**Exhibit 23: The LSEG Retail Index Sectors: Q1 2026 Act – Q4 2026 Est.**

| GICS Industry                          | Q1 2026 Act. | Q2 2026 Est. | Q3 2026 Est. | Q4 2026 Est. |
|----------------------------------------|--------------|--------------|--------------|--------------|
| Distributors                           | -5.6%        | -5.7%        | 2.4%         | 18.9%        |
| Hotels, Restaurants & Leisure          | 14.2%        | 9.7%         | 28.8%        | 16.7%        |
| Household Durables                     | -25.0%       | -19.4%       | -5.3%        | 5.6%         |
| Household Products                     | 4.5%         | -4.7%        | 1.3%         | 1.2%         |
| Consumer Staples Distribution & Retail | 12.5%        | 10.5%        | 10.3%        | 9.9%         |
| Leisure Products                       | 130.9%       | 1.8%         | 28.8%        | 34.7%        |
| Broadline Retail                       | 73.3%        | 8.2%         | -2.1%        | 21.1%        |
| Personal Care Products                 | 21.1%        | 15.6%        | 12.8%        | 10.1%        |
| Specialty Retail                       | 6.8%         | 2.8%         | 8.6%         | 5.0%         |
| Textiles, Apparel & Luxury Goods       | 35.3%        | -4.9%        | 6.1%         | 10.6%        |
| <b>TOTAL</b>                           | <b>27.2%</b> | <b>4.2%</b>  | <b>8.2%</b>  | <b>12.6%</b> |

Source: LSEG I/B/E/S

Despite broader discretionary sector challenges, there are pockets of optimism. Looking ahead to Q2 earnings, analysts surveyed by LSEG are already constructive on Dillard's Inc. The consensus estimate for Dillard's Q2 2026 EPS stands at \$4.31. Notably, a highly rated five-star analyst has issued a Bold Estimate of \$4.58, above the consensus. This positive divergence between the Bold Estimate and consensus suggests the potential for an earnings beat and a favorable surprise when the company reports.

The StarMine SmartEstimate is a weighted average of analyst estimates, with more weight given to more recent estimates and more accurate analysts. Our studies have shown that when the SmartEstimate differs from the consensus (I/B/E/S mean) by more than 2%, the company is likely to post subsequent earnings surprises directionally correct 70% of the time.

This percentage difference is referred to as the Predicted Surprise (PS%) (Exhibit 24).

#### Exhibit 24: Dillard's Inc. StarMine Predicted Surprise %: Q2 2026 Est.

| Earnings Per Share, Q2 Jul-26 (This QTR)            |               |
|-----------------------------------------------------|---------------|
| ▼ EARNINGS PER SHARE - Consolidated USD Per Share ⓘ |               |
| Custom Calculated Mean                              | \$ 4.31       |
| SmartEstimate®                                      | \$ 4.46       |
| Mean                                                | \$ 4.31       |
| Predicted Surprise %                                | 3.38%         |
| Median                                              | \$ 4.18       |
| Low: \$ 4.17                                        | High: \$ 4.58 |

Source: LSEG Workspace

More broadly, the companies listed below have LSEG Predicted Surprise values exceeding 2.0% for Q2 2026, Q3 2026, and/or the current fiscal year (Exhibit 25). Elevated Predicted Surprise scores indicate that earnings expectations may still be too conservative, increasing the likelihood that these companies outperform consensus estimates and deliver positive earnings surprises.

#### Exhibit 25: Strongest StarMine Predicted Surprise %: 2026 Est.

|            |                           | Earnings Per Share - Predicted Surprise PCT |                  |                  |
|------------|---------------------------|---------------------------------------------|------------------|------------------|
| Identifier | Company Name              | Current Qtr (FQ1)                           | Next Qtr - (FQ2) | Current FY (FY1) |
| LGIH.OQ    | LGI Homes Inc             | 16.3%                                       | 0.8%             | 2.1%             |
| RRGB.OQ    | Red Robin Gourmet Burgers | 6.4%                                        | 1.4%             | 14.3%            |
| HELE.OQ    | Helen of Troy Ltd         | 4.0%                                        | 11.7%            | 0.8%             |
| DDS.N      | Dillard's Inc             | 3.4%                                        | 3.0%             | 6.6%             |
| CRI.N      | Carter's Inc              | 3.2%                                        | 2.7%             | 1.1%             |

Source: LSEG Workspace

Conversely, the companies listed below have a negative Predicted Surprise of less than -2.0% for Q2 2026, Q3 2026, and/or the current fiscal year; indicating they are likely to miss earnings expectations and deliver negative surprises.

#### Exhibit 26: Weakest StarMine Predicted Surprise %: 2026 Est.

|            |                  | Earnings Per Share - Predicted Surprise PCT |                  |                  |
|------------|------------------|---------------------------------------------|------------------|------------------|
| Identifier | Company Name     | Current Qtr (FQ1)                           | Next Qtr - (FQ2) | Current FY (FY1) |
| WHR.N      | Whirlpool Corp   | -127.2%                                     | -10.3%           | -13.1%           |
| RH.N       | RH               | -10.7%                                      | -3.4%            | -2.6%            |
| SHAK.N     | Shake Shack Inc  | -8.5%                                       | -5.1%            | -4.0%            |
| WYNN.OQ    | Wynn Resorts Ltd | -6.7%                                       | -11.5%           | -3.2%            |
| COTY.N     | Coty Inc         | -2.9%                                       | -2.1%            | -1.0%            |

Source: LSEG Workspace

Inflation & Pricing Trends

According to the U.S. Bureau of Labor Statistics, the Consumer Price Index rose a sharp 0.5% month over month in May 2026 and 4.2% year over year. The acceleration was largely driven by energy prices, which increased 23.5% from a year earlier. The latest CPI data underscores the pressure consumers continue to face from higher costs for essentials, including food, electricity, and transportation. For retailers, this reinforces ongoing headwinds from weak consumer sentiment and increasingly value-conscious shoppers managing elevated living expenses.

In collaboration with Centric Market Intelligence, LSEG is tracking weekly average original prices across selected categories in U.S. mall stores. From December 2024 through June 2026, Backpacks recorded the steepest increase among the tracked categories, with average prices rising 5.6% ahead of the back-to-school season. Accessories followed with a 5.3% increase, while Footwear prices rose 2.6% (Exhibit 27).

Meanwhile, men’s apparel increased a more modest 1.3%. Women’s apparel saw the smallest price increase, edging up just 0.4%. Overall, the data suggests consumers are facing the greatest pricing pressure in travel-related and accessory categories, while core apparel inflation has remained subdued amid softer demand and heightened promotional activity as retailers compete aggressively for value-conscious shoppers.

Exhibit 27: Average Price Changes: December 2024 – June 2026 Est

|                 | Women's Apparel | Men's Apparel | Footwear | Accessories | Backpacks |
|-----------------|-----------------|---------------|----------|-------------|-----------|
| % Price Changes | 0.4%            | 1.3%          | 2.6%     | 5.3%        | 5.6%      |

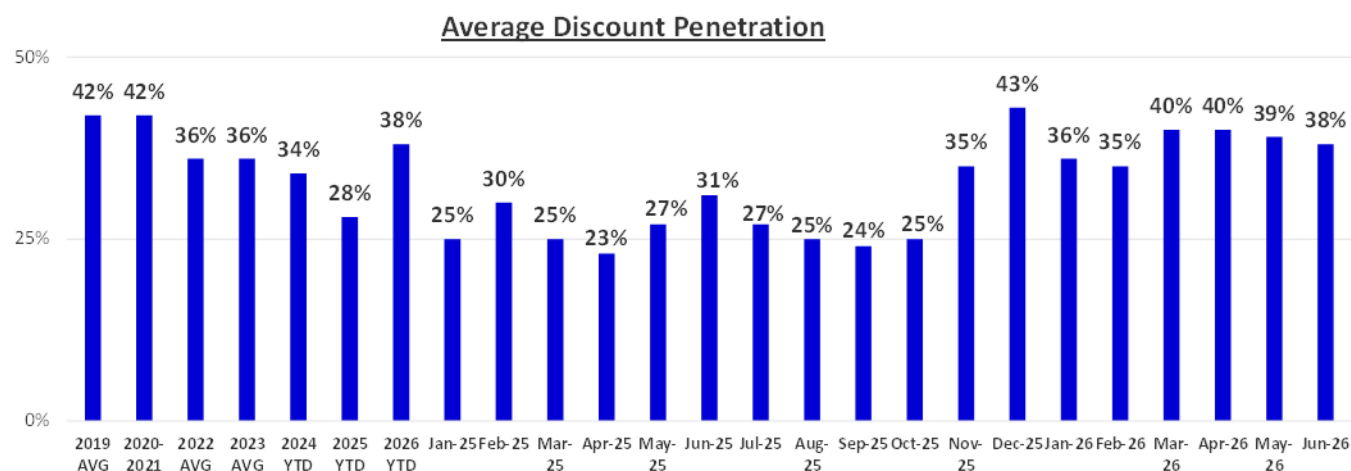
Source: Centric Market Intelligence.

Despite the recent resilience in consumer spending, the latest Producer Price Index (PPI) data, which measures price changes before they reach consumers, suggests inflationary pressures may be building beneath the surface. Over the past year, consumer prices have remained relatively contained, partly due to strategic actions by importers and retailers, including preordering inventory and absorbing tariff-related costs to shield consumers in the near term. However, that buffer may be fading. The latest PPI data indicates that higher costs are increasingly moving through the supply chain, driven in part by persistent tariff and transportation pressures. As these upstream costs continue to accumulate, consumers may soon begin to feel the impact more directly.

Promotional Activity

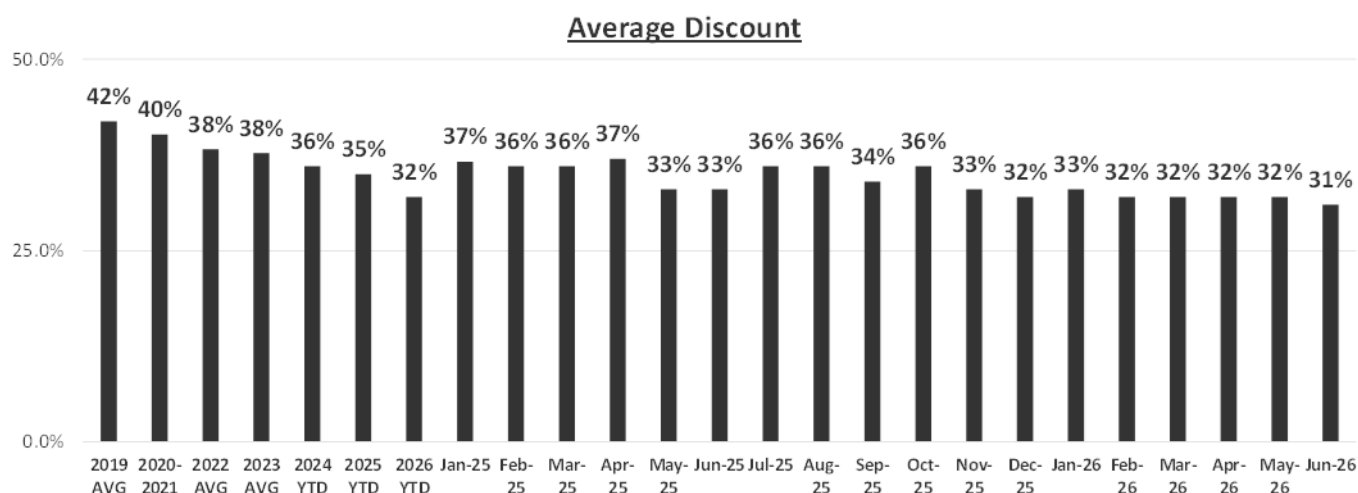
One factor supporting stronger first-quarter retail sales was an increase in promotional activity. The discount penetration, defined as the percentage of merchandise on sale, rose to its highest level in six years (Exhibit 28). Average discount penetration reached 40% in March and April, up from a year-to-date average of 38% in 2026 and above levels recorded a year earlier.

The increase in promotional activity reflects retailers' efforts to stimulate demand in an environment where consumers remain highly value-conscious. As elevated living costs continue to pressure household budgets, retailers are relying more heavily on discounts to drive store traffic and maintain sales momentum. Entering the second quarter, discount penetration remains elevated, holding above its long-term average of 37%, suggesting promotional intensity is likely to remain a defining feature of the retail landscape through the remainder of the year.

**Exhibit 28: Average Discount Penetration: U.S. Online Retailers**

Source: Centric Market Intelligence

However, the average percentage discount has remained near 32%, making it the lowest year-to-date average since LSEG began tracking the data in 2019 (Exhibit 29). This suggests that while retailers are expanding the breadth of promotional activity by placing more merchandise on sale, they have largely resisted offering deeper discounts. The trend points to a more disciplined pricing environment, with retailers using targeted promotions to drive traffic and appeal to value-conscious consumers while helping to preserve margins.

**Exhibit 29: Average Discount: U.S. Online Retailers**

Source: Centric Market Intelligence.

**Retail Same Store Sales Outlook**

In the retail sector, approximately 42% of companies in our SSS index are on track to deliver positive same-store sales growth in 2026. Aritzia leads the group with the strongest first-quarter SSS estimate and is expected to sustain robust comparable sales throughout the year (Exhibit 30). Ralph Lauren continues to benefit from demand among high-end consumers, while TJX and Ross Stores are also projected to deliver consistently healthy same-store sales growth, supported by strong value-seeking behavior in 2026.

**Exhibit 30: Retail Strongest SSS estimates: Q1 2026 – Q4 2026**

|                            |        |              | Same Store Sales Estimates |         |         |
|----------------------------|--------|--------------|----------------------------|---------|---------|
| Retailer                   | Ticker | Q1 2025 Act. | Q2 2025                    | Q3 2025 | Q4 2025 |
| Aritzia Inc                | ATZ    | 30.8% Est.   | 17.9%                      | 9.1%    | 10.8%   |
| Ross Stores Inc.           | ROST   | 17.0%        | 6.5%                       | 3.1%    | 2.6%    |
| Ralph Lauren Corp          | RL     | 17.0%        | 5.9%                       | 5.5%    | 5.4%    |
| Costco Wholesale Corp      | COST   | 9.8%         | 7.7%                       | 6.6%    | 6.6%    |
| TJX Companies Incorporated | TJX    | 6.0%         | 3.3%                       | 3.1%    | 3.3%    |

Source: LSEG I/B/E/S

At the other end of the spectrum, Destination XL Group is expected to post consistently negative same-store sales throughout 2026. Overall, approximately 58% of retailers in our SSS Index are projected to report negative comparable sales this year, highlighting the challenging operating environment facing much of the sector. Kohl's reported a 1.1% decline in comparable sales in Q1 2026. Although consensus estimates call for continued negative comparable sales over the next two quarters, they also point to a gradual sequential improvement in performance (Exhibit 31).

**Exhibit 31: Retail Weakest SSS estimates: Q1 2026 – Q4 2026**

|                                          |        |              | Same Store Sales Estimates |         |         |
|------------------------------------------|--------|--------------|----------------------------|---------|---------|
| Retailer                                 | Ticker | Q1 2025 Act. | Q2 2025                    | Q3 2025 | Q4 2025 |
| J.Jill Inc                               | JILL   | -8.7%        | -3.2%                      | 0.3%    | 2.2%    |
| Destination XL Group Inc. (Consolidated) | DXLG   | -3.8%        | -5.5%                      | -2.0%   | -0.7%   |
| Caleres Inc.                             | CAL    | -2.3%        | -5.0%                      | -2.0%   | -1.0%   |
| Lululemon Athletica                      | LULU   | -2.0%        | -4.7%                      | -3.4%   | -3.4%   |
| Kohl's Corp                              | KSS    | -1.1%        | -0.8%                      | -0.5%   | 0.1%    |

Source: LSEG I/B/E/S

**Restaurant Same Store Sales Outlook**

In the restaurant sector, approximately 65% of the companies in our SSS index are on track to deliver positive same-store sales (SSS) results for 2026. Texas Roadhouse led the group with the strongest SSS performance in Q1 and is expected to maintain robust comps throughout the year. Starbucks is also projected to post consistently healthy same-store sales in 2026. Most remaining restaurant operators are expected to report low single-digit comparable sales growth.

**Exhibit 32: Restaurant Strongest SSS estimates: Q1 2026 – Q4 2026**

|                                        |        |              | Same Store Sales Estimates |         |         |
|----------------------------------------|--------|--------------|----------------------------|---------|---------|
| Restaurant                             | Ticker | Q1 2025 Act. | Q2 2025                    | Q3 2025 | Q4 2025 |
| Texas Roadhouse Inc (Company)          | TXRH   | 7.1%         | 6.0%                       | 5.5%    | 5.7%    |
| Starbucks Corp (Consolidated)          | SBUX   | 6.2%         | 5.6%                       | 4.3%    | 4.9%    |
| El Pollo Loco Holdings Inc             | LOCO   | 5.8%         | 3.6%                       | 2.9%    | 1.1%    |
| Darden Restaurants Inc. (Consolidated) | DRI    | 4.6%         | 3.1%                       | 2.9%    | 2.9%    |
| YUM Brands Inc (Worldwide)             | YUM    | 3.0%         | 3.0%                       | 2.7%    | 2.8%    |

Source: LSEG I/B/E/S

Meanwhile, Wingstop is on track to report consistently negative comps over the next two quarters in 2026. In fact, about 35% of the restaurants in our SSS Index are on track to report negative comps this year.

### Exhibit 33: Restaurant Weakest SSS estimates: Q1 2026 – Q4 2026

| Restaurant                            | Ticker | Q1 2025 Act. | Same Store Sales Estimates |         |         |
|---------------------------------------|--------|--------------|----------------------------|---------|---------|
|                                       |        |              | Q2 2025                    | Q3 2025 | Q4 2025 |
| Wingstop Inc                          | WING   | -8.7%        | -5.2%                      | -0.1%   | 2.4%    |
| Wendys International (Systemwide)     | WEN    | -6.8%        | -4.3%                      | -0.4%   | 2.8%    |
| Dave Busters Entertainment In (Total) | PLAY   | -5.4%        | -2.4%                      | -1.1%   | -0.5%   |

Source: LSEG I/B/E/S

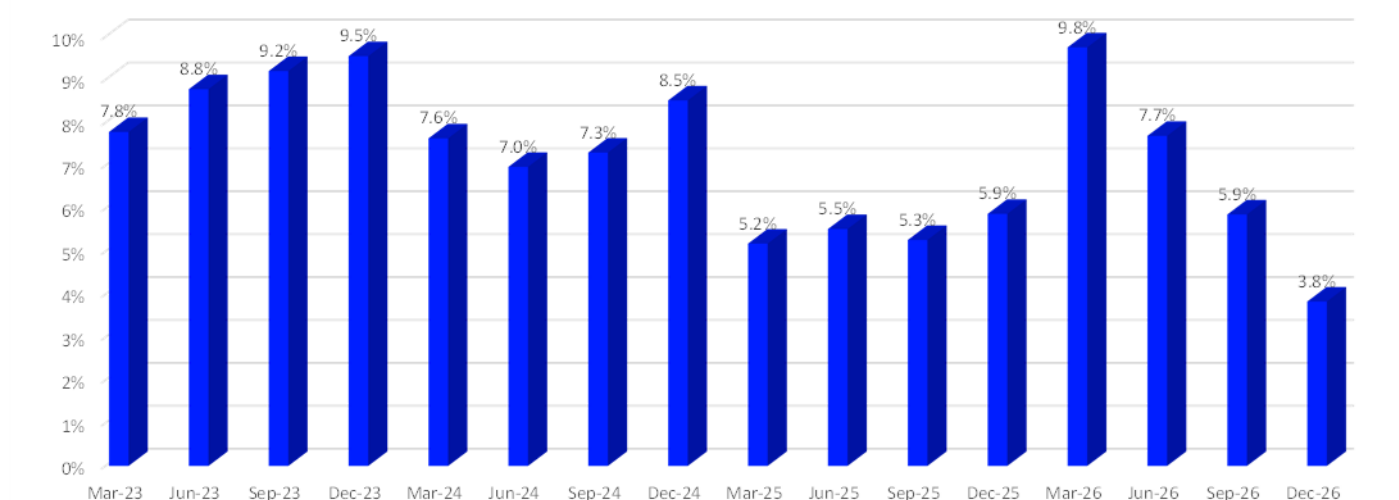
## E-Commerce Outlook

According to the latest U.S. Census Bureau e-commerce report, online retail sales reached \$326 billion in the first quarter of 2026, a robust increase of 9.8% from a year earlier (Exhibit 34). Looking ahead, LSEG IFR expects e-commerce growth to remain within the 4% – 8% range that has prevailed over the past three years. This outlook is consistent with recent U.S. retail sales data, which continue to show solid year-over-year growth in the nonstore retail segment.

Steady online sales growth may also reflect changing consumer behavior. As gasoline prices remain elevated, consumers appear to be placing greater value on the convenience of home delivery and digital shopping, reducing the need for discretionary trips to physical stores.

Despite this steady growth, e-commerce still accounts for only about 16% of total U.S. retail sales, underscoring the continued dominance of brick-and-mortar retail. While online penetration continues to expand gradually, a substantial portion of U.S. retail spending remains outside the reach of even the largest e-commerce platforms, including Amazon.

### Exhibit 34: E-commerce growth data: 2023 – 2026



Source: LSEG IFR

## Consumer Outlook

Retailers have now concluded reporting first-quarter 2026 earnings, with roughly half of companies citing tariffs and rising fuel prices during their earnings calls, underscoring the growing influence of both on the sector. While large retailers such as Walmart possess the scale, balance sheet strength, and pricing power to absorb or mitigate these pressures, smaller retailers remain considerably more exposed, with limited flexibility to offset rising costs and supply chain disruptions. Still, during its last earnings' call, CEO Doug McMillon warned that higher tariffs and transportation expenses could eventually lead to higher prices.

Recent increases in both the Consumer Price Index (CPI) and Producer Price Index (PPI) suggest that cost pressures are continuing to build across the retail value chain. At the same time, consumer sentiment has deteriorated as households contend with higher prices, elevated gasoline costs, and growing concerns about the labor market. The shift in consumer focus from long-term economic uncertainty to immediate affordability highlights a more cautious spending environment heading into the second half of the year.

Apparel remains one of the clearest examples of these competing forces. Despite persistent inflation across much of the economy, apparel prices have remained subdued as retailers prioritize demand over pricing power. Faced with higher input costs and softer consumer spending, many brands have expanded promotional activity rather than fully passing through price increases. According to the LSEG Retail & Restaurant Index, the apparel sector is expected to report one of the weakest earnings growth rates in the second quarter, at -4.9%, illustrating the pressure on both margins and profitability.

Looking ahead, the retail landscape is likely to remain defined by cautious consumers, elevated input costs, and continued geopolitical and trade-related uncertainty. Retailers with differentiated brands, pricing power, strong balance sheets, and disciplined inventory management should be best positioned to navigate this environment, while retailers lacking pricing power or relying heavily on promotional activity are likely to face continued pressure on both margins and earnings through the remainder of 2026.

## Section 4 – Funds Outlook

### Triumph of the optimists?

Global fund flows over the past couple of years indicate a market where artificial intelligence overshadows concerns over geopolitics, particularly for US investors.

We looked at global flows over the 24 months, from June 2024 to May 2026, then split these by US and ex-US.

In the last seven months of 2024, money market funds attracted the largest share of global flows (+\$964bn), followed by bonds (+\$534bn), then equities (+\$350bn). In contrast, mixed-asset funds experienced sizeable redemptions (-\$202bn), suggesting that investors were increasingly unwilling to rely on blended allocations and instead preferred to make more explicit choices between cash, duration and equity risk.

This pattern carried into the opening phase of 2025, but then we see a directional shift in the spring of that year—most specifically April's heavy sell-off in bonds (-\$67nbn) and spike in equity sales (+\$74bn).

Linking fund flows to macro events, especially over shorter time periods, can often be as scientific as reading the entrails of a chicken. But the shift here is fairly obvious, given the timing: President Trump's announcement of the most comprehensive tariffs since the 1930s. This led to a drop in equity indices that fund investors seem to have taken advantage of tactically, by "buying on the dips". Nevertheless, the longer-term effect was the dampening of the animal spirits of equity markets, as 2026's flows for the asset class were +\$245bn: lower than for both the last seven months of 2024 (+\$350bn) and the first five of 2026 (+\$439bn).

**Exhibit 35: Monthly fund flows by asset type, US market, June 2024-July 2026 (\$bn)**



Source: LSEG Lipper

**Exhibit 36: Monthly fund flows by asset type, ex-US, June 2024-July 2026 (\$bn)**

Source: LSEG Lipper

This was most keenly felt by US fund investors, who had in any case been negative on equities over the back end of 2024, when \$15bn was redeemed. US fund flows were dominated by money market inflows of \$656bn, with bond funds taking in \$228bn. That defensive bias intensified into 2025, as equity outflows in the US fell to \$289bn, while bond inflows rose to \$459bn and money market inflows reached \$714bn. Rather than rotating into equity markets elsewhere, US investors opted for yield, liquidity and capital preservation.

Outside the US, the tone was more supportive of risk assets over 2024 and 2025. In 2024, ex-US investors allocated across all three major asset buckets, with \$365bn into equities, \$306bn into bonds and \$308bn into money market products.

Over 2025, equity inflows from non-US investors were \$535bn, ahead of bond flows (+\$493bn). This is an important distinction: in ex-US markets, large money market balances did not translate into an outright retreat from equities. Instead, investors appeared willing to maintain liquidity buffers alongside risk assets exposure.

If we take equity exposure as a proxy for market or broader economic optimism, US investors were markedly more downbeat than their global peers. That, however, changed in 2026. Over the first five months of the year, US investors—through an undoubted spike in geopolitical risk—have deployed \$178bn into equity funds, or 36.5% of the market's total net flows, in comparison to \$261bn (32.2%) for their global peers.

This does, of course, even out fluctuations, not least around February and March, with the escalating conflict in the Middle East. It was not surprising that money market funds were one of the winners of the risk off move. However, as disruptions of the closure of the Strait of Hormuz seemed to be less impactful than expected, investors returned in to risk-on.

## Keep on dancing

Having survived 'SaaSmageddon' and the logjam in the Straits of Hormuz, investors have decided that "while the music plays, you have to keep dancing". This, however, conceals a rather different dynamic between US and ex-US markets.

US investors have been getting increasingly bullish over the year. Equity fund flows in the US for April and May have been the largest for the past 24 months and concentrated on Equity US (US large cap) and Equity Theme – Information Technology. Over the first five months of 2026, these two have taken more than \$105bn, or 60% of total US equity flows.

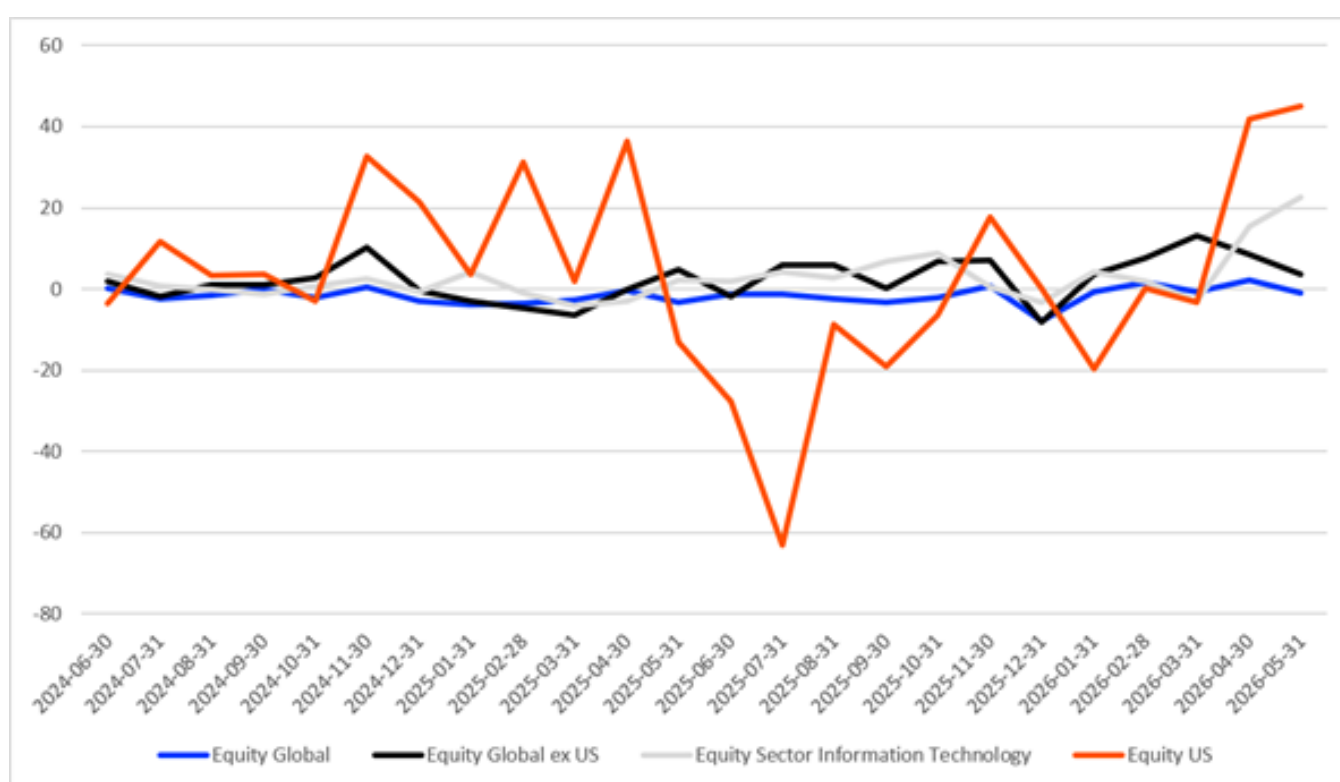
In contrast, US Smid is still seeing significant outflows, and the classification has consistently seen the heaviest redemptions over the past 24 months. Even when US investors were at their most negative on equities generally, and US equities in particular—2025—Equity US Small & Mid Cap redemptions were more than four times higher than for Equity US, the classification with the second worst outflows over 2025.

Meanwhile, although still positive on equities, ex US investors are preferring the broader allocation to Equity Global (\$119bn out of \$260bn total equity YTD) compared to Equity US (\$42.37bn) and Equity Sector – IT (\$32.23bn).

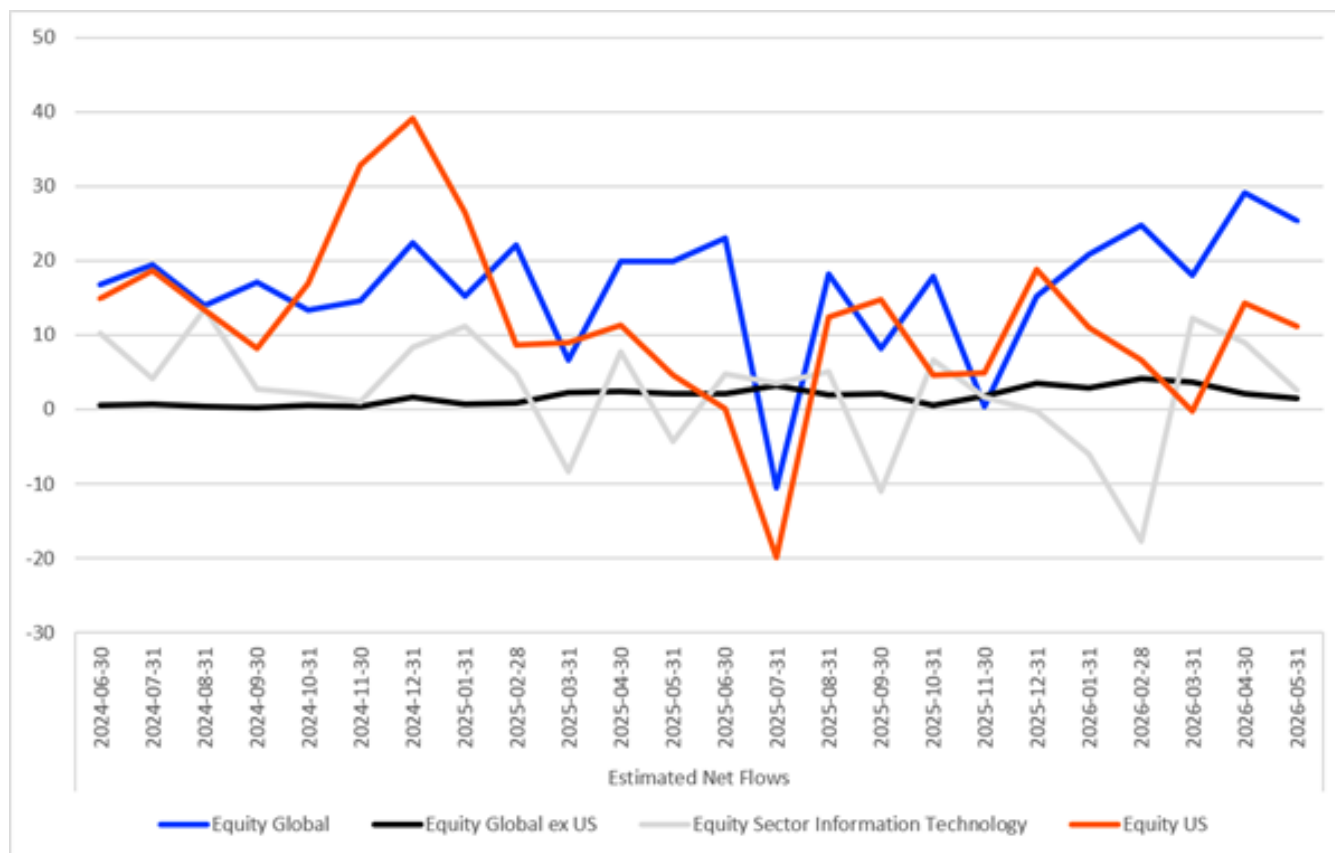
The contrast between US (Exhibit 37) and ex-US (Exhibit 38) equity preferences can be seen by comparing US, Global, Global ex US and IT sector flows over the period. There are some common characteristics, not least the largest Equity US redemptions in July 2025, with the announcement of a swathe of further tariffs and the Fed holding rates as inflation expectations ground upwards. But the charts also highlight the differences, with the ex-US appetite for Equity US peaking in November 2024, and equity Global gaining increasing favour from the end of last year. Meanwhile, US investors' appetite for Equity US and IT has increased sharply over the spring.

In addition, it is interesting to see that the demand for Equity US from US investors has strongly increased over the course of the past three months and is now higher than during the former peak, while the appetite for Equity US from investors outside the U.S. is still rather low.

**Exhibit 37: Equity Global, Global ex-US, Information Technology and US: US domicile (\$bn)**



Source: LSEG Lipper. June 2024-May 2026.

**Exhibit 38: Equity Global, Global ex-US, Information Technology and US: ex-US domicile (\$bn)**

Source: LSEG Lipper. June 2024-May 2026.

## From 'what' to 'why'

The overall fund flow trends for ETFs and mutual funds globally over the course of 2026 shows that investors globally may have different asset class preferences when it comes to their investments in risk-on and risk-off mode. Nevertheless, the trend also shows they can act swiftly to potentially negative economic, geopolitical, or political events. But it also shows that estimated net flows are somewhat resilient, since global investors continued investing once they had evaluated the possible impacts of the closure of the Strait of Hormuz on the global economies.

What's stands out from the recent US data is the relationship between Equity US and Information Technology flows. Over the 24-month period, Equity US (+\$83.75bn) and IT (+\$66.78bn) are the two most popular classifications. Given this, and that AI-themed stocks have dominated both market narrative and returns, you might expect the monthly flows to these classifications to be highly correlated. They are not: in 16 of the 24 months, they run in opposite directions. That bifurcation was particularly stark over 2025, where IT was the most popular equity sector (+\$20.19bn) and Equity US the second least popular (-\$46.89bn), only worsted by US Smid (-\$198bn) (Exhibit 39).

So, from this data, when US investors were most negative on equities, it seems that it was not predominantly because of fears over AI bubbles, as IT funds continued to attract cash. Where we do see them move together is April and May 2026: the only time these two classifications occupy the top two slots. While two data points don't make a trend, it's at least an interesting coincidence.

Exhibit 39: Largest equity in- and outflows by Lipper Global Classification (\$bn)

| Rank       | 2024-06-30                      | 2024-07-31                        | 2024-08-31                        | 2024-09-30                       | 2024-10-31                        | 2024-11-30                      | 2024-12-31                        | 2025-01-31                        | 2025-02-28                       | 2025-03-31                        | 2025-04-30                        | 2025-05-31                        | 2025-06-30                        | 2025-07-31                       | 2025-08-31                        | 2025-09-30                       | 2025-10-31                      | 2025-11-30                       | 2025-12-31                        | 2026-01-31                        | 2026-02-28                       | 2026-03-31                        | 2026-04-30                       | 2026-05-31                        |
|------------|---------------------------------|-----------------------------------|-----------------------------------|----------------------------------|-----------------------------------|---------------------------------|-----------------------------------|-----------------------------------|----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|-----------------------------------|----------------------------------|-----------------------------------|----------------------------------|---------------------------------|----------------------------------|-----------------------------------|-----------------------------------|----------------------------------|-----------------------------------|----------------------------------|-----------------------------------|
| Inflow 1   | Information Technology<br>3,709 | US<br>11,608                      | US<br>3,478                       | US<br>3,655                      | China<br>6,981                    | US<br>32,528                    | US<br>21,536                      | Information Technology<br>4,286   | US<br>31,173                     | Europe<br>5,959                   | US<br>36,244                      | Global ex US<br>4,761             | Emerging Markets Global<br>2,204  | Global ex US<br>5,780            | Global ex US<br>5,919             | Information Technology<br>6,763  | Information Technology<br>8,865 | US<br>17,845                     | Industrials<br>2,535              | Emerging Markets Global<br>15,153 | Emerging Markets Global<br>9,419 | Global ex US<br>13,071            | US<br>41,827                     | US<br>45,044                      |
| Inflow 2   | US Sm&Mid Cap<br>2,895          | Financials<br>3,510               | Real Estate US<br>1,435           | Emerging Markets Global<br>1,406 | Global ex US<br>2,828             | Global ex US<br>10,209          | US Income<br>1,204                | Financials<br>3,744               | Europe<br>2,284                  | US<br>2,030                       | US Income<br>1,813                | Information Technology<br>2,275   | Information Technology<br>2,026   | Information Technology<br>4,268  | Information Technology<br>2,748   | Industrials<br>3,208             | Global ex US<br>6,684           | Global ex US<br>7,214            | Materials<br>1,655                | Industrials<br>7,577              | Global ex US<br>7,590            | Natural Resources<br>6,117        | Information Technology<br>15,516 | Information Technology<br>22,630  |
| Inflow 3   | Global ex US<br>1,803           | Utilities<br>1,278                | Global ex US<br>1,009             | Real Estate US<br>1,266          | Greater China<br>1,681            | US Sm&Mid Cap<br>8,500          | Industrials<br>379                | US<br>3,635                       | Canada<br>1,037                  | Germany<br>1,089                  | Canada<br>1,182                   | Industrials<br>2,157              | Industrials<br>1,219              | Financials<br>3,448              | Industrials<br>1,574              | Canada<br>1,549                  | Europe<br>3,748                 | Emerging Markets Global<br>4,948 | Gold & Precious Metals<br>1,439   | Materials<br>4,778                | Industrials<br>4,915             | Industrials<br>4,092              | Emerging Markets Global<br>9,053 | Global ex US<br>3,739             |
| Inflow 4   | India<br>1,008                  | Industrials<br>824                | Utilities<br>786                  | Global ex US<br>1,110            | Canada<br>1,616                   | Financials<br>7,550             | Argentina<br>199                  | Industrials<br>1,909              | Communication Services<br>1,004  | Utilities<br>999                  | Global Income<br>359              | Europe<br>1,309                   | Korea<br>1,011                    | Industrials<br>2,536             | Canada<br>1,277                   | Emerging Markets Global<br>1,431 | Industrials<br>1,951            | Healthcare<br>2,961              | Real Estate US<br>963             | Natural Resources<br>4,771        | Natural Resources<br>3,893       | Korea<br>1,561                    | Global ex US<br>8,436            | Infrastructure<br>1,654           |
| Inflow 5   | Financials<br>674               | Information Technology<br>816     | Financials<br>674                 | Canada<br>732                    | Real Estate US<br>1,379           | Industrials<br>2,647            | Financials<br>105                 | Consumer Discretionary<br>1,364   | Materials<br>602                 | Consumer Staples<br>541           | Utilities<br>325                  | Canada<br>945                     | Communication Services<br>896     | Global ex US Sm&Mid Cap<br>1,449 | Gold & Precious Metals<br>964     | Gold & Precious Metals<br>880    | Materials<br>1,410              | Canada<br>925                    | Consumer Discretionary<br>937     | Financials<br>4,403               | Japan<br>3,261                   | Utilities<br>1,548                | Industrials<br>2,788             | Real Estate US<br>1,346           |
| Inflow 6   | Utilities<br>575                | Energy<br>227                     | Consumer Staples<br>462           | Greater China<br>511             | Financials<br>1,378               | Information Technology<br>2,551 | Greater China<br>76               | Energy<br>746                     | Infrastructure<br>584            | Global Income<br>428              | Japan<br>316                      | Global Income<br>928              | Consumer Discretionary<br>855     | Infrastructure<br>937            | Utilities<br>801                  | Infrastructure<br>867            | Healthcare<br>1,241             | Global ex US Sm&Mid Cap<br>907   | Infrastructure<br>602             | Information Technology<br>4,149   | Korea<br>2,962                   | Infrastructure<br>528             | Japan<br>2,655                   | Industrials<br>956                |
| Inflow 7   | Global Sm&Mid Cap<br>256        | India<br>197                      | India<br>269                      | Consumer Staples<br>476          | Industrials<br>1,195              | Consumer Discretionary<br>1,531 | Communication Services<br>64      | Communication Services<br>672     | Emerging Markets Global<br>475   | Greater China<br>372              | Mexico<br>237                     | Taiwan<br>756                     | Canada<br>813                     | Emerging Markets Global<br>753   | Infrastructure<br>658             | Alternative Energy<br>763        | Utilities<br>1,067              | Alternative Energy<br>736        | Europe<br>386                     | Global ex US<br>3,510             | Materials<br>1,970               | Energy<br>438                     | Global<br>2,249                  | Alternative Energy<br>945         |
| Inflow 8   | Europe<br>245                   | Consumer Discretionary<br>144     | UK<br>107                         | Infrastructure<br>434            | Information Technology<br>669     | Canada<br>566                   | Consumer Staples<br>54            | Japan<br>489                      | Utilities<br>399                 | Frontier Markets<br>87            | Brazil<br>220                     | Brazil<br>649                     | Infrastructure<br>789             | Global Income<br>705             | Consumer Discretionary<br>637     | Global Income<br>735             | Infrastructure<br>924           | Infrastructure<br>702            | Korea<br>363                      | Gold & Precious Metals<br>3,012   | Information Technology<br>1,888  | Canada<br>371                     | Real Estate Global<br>1,925      | Consumer Discretionary<br>728     |
| Inflow 9   | Emerging Markets Global<br>159  | UK<br>112                         | Taiwan<br>86                      | Gold & Precious Metals<br>371    | Taiwan<br>545                     | Global<br>535                   | Australia<br>50                   | Utilities<br>340                  | Financials<br>364                | China<br>84                       | Germany<br>116                    | Infrastructure<br>625             | India<br>707                      | Alternative Energy<br>589        | Global Income<br>591              | Consumer Discretionary<br>668    | Alternative Energy<br>909       | Global<br>611                    | Alternative Energy<br>250         | Healthcare<br>1,731               | Global Income<br>1,728           | Brazil<br>247                     | Infrastructure<br>1,784          | Consumer Staples<br>708           |
| Inflow 10  | Mexico<br>71                    | Natural Resources<br>90           | Netherlands<br>25                 | Mexico<br>281                    | Consumer Discretionary<br>544     | Communication Services<br>468   | South Africa<br>40                | Mexico<br>292                     | Energy<br>171                    | Australia<br>81                   | Frontier Markets<br>106           | Communication Services<br>549     | Global Income<br>585              | Utilities<br>573                 | Other<br>538                      | Consumer Staples<br>504          | Gold & Precious Metals<br>851   | Information Technology<br>601    | Utilities<br>233                  | Korea<br>1,730                    | Global<br>1,675                  | UK<br>216                         | Materials<br>1,774               | Natural Resources<br>541          |
| Outflow 1  | Infrastructure<br>-290          | Materials<br>-716                 | Consumer Discretionary<br>-826    | Global ex US Sm&Mid Cap<br>-567  | Europe<br>-413                    | Global Income<br>-480           | Global Income<br>-893             | Gold & Precious Metals<br>-797    | Consumer Discretionary<br>-1,028 | Financials<br>-1,547              | Consumer Discretionary<br>-988    | Gold & Precious Metals<br>-476    | Financials<br>-818                | Consumer Discretionary<br>-226   | Europe<br>-548                    | Japan<br>-272                    | Other<br>-323                   | Natural Resources<br>-267        | Japan<br>-1,293                   | Asia Pacific<br>-138              | Italy<br>-65                     | Global<br>-789                    | Gold & Precious Metals<br>-503   | Utilities<br>-832                 |
| Outflow 2  | Japan<br>-307                   | US Income<br>-836                 | Europe<br>-928                    | Real Estate Global<br>-894       | Asia Pacific ex Japan<br>-563     | Japan<br>-499                   | Real Estate Global<br>-1,263      | Global ex US Sm&Mid Cap<br>-859   | Gold & Precious Metals<br>-1,056 | Natural Resources<br>-1,886       | Industrials<br>-1,262             | Materials<br>-665                 | Asia Pacific<br>-902              | Real Estate US<br>-244           | India<br>-841                     | Utilities<br>-466                | Consumer Discretionary<br>-513  | Other<br>-361                    | Global ex US Sm&Mid Cap<br>-1,338 | Communication Services<br>-393    | Utilities<br>-98                 | Communication Services<br>-1,784  | Utilities<br>-632                | Global ex US Sm&Mid Cap<br>-923   |
| Outflow 3  | Communication Services<br>-318  | Healthcare<br>-838                | US Income<br>-983                 | Industrials<br>-930              | Natural Resources<br>-955         | Greater China<br>-637           | Consumer Discretionary<br>-1,270  | India<br>-1,034                   | Information Technology<br>-1,088 | US Income<br>-2,184               | China<br>-1,922                   | Natural Resources<br>-1,185       | Global ex US Sm&Mid Cap<br>-1,037 | Asia Pacific<br>-264             | Japan<br>-1,054                   | Germany<br>-481                  | Greater China<br>-563           | Energy<br>-397                   | Global Sm&Mid Cap<br>-1,665       | Real Estate US<br>-451            | Global Sm&Mid Cap<br>-123        | India<br>-2,149                   | India<br>-882                    | Europe<br>-989                    |
| Outflow 4  | Industrials<br>-621             | Real Estate US<br>-1,055          | Japan<br>-1,188                   | Information Technology<br>-1,242 | Real Estate Global<br>-1,087      | Consumer Staples<br>-705        | Japan<br>-1,506                   | US Income<br>-1,222               | Natural Resources<br>-1,310      | Healthcare<br>-2,335              | Global ex US Sm&Mid Cap<br>-2,371 | Financials<br>-1,608              | Natural Resources<br>-1,175       | Natural Resources<br>-428        | Natural Resources<br>-1,490       | Europe<br>-732                   | Financials<br>-683              | Materials<br>-595                | Healthcare<br>-2,198              | Global<br>-792                    | Gold & Precious Metals<br>-435   | Gold & Precious Metals<br>-2,701  | Consumer Staples<br>-1,352       | Global<br>-1,067                  |
| Outflow 5  | Consumer Discretionary<br>-639  | China<br>-1,127                   | Global ex US Sm&Mid Cap<br>-1,391 | Healthcare<br>-1,336             | Global ex US Sm&Mid Cap<br>-1,274 | Global ex US Sm&Mid Cap<br>-909 | Natural Resources<br>-2,222       | Natural Resources<br>-2,371       | Industrials<br>-1,970            | Consumer Discretionary<br>-2,547  | Financials<br>-2,808              | US Income<br>-2,142               | Global<br>-1,353                  | Natural Resources<br>-428        | Emerging Markets Global<br>-2,047 | Natural Resources<br>-968        | Real Estate US<br>-803          | Consumer Staples<br>-684         | Emerging Markets Global<br>-2,839 | Global Sm&Mid Cap<br>-942         | Consumer Discretionary<br>-545   | Emerging Markets Global<br>-2,792 | Healthcare<br>-1,502             | Healthcare<br>-1,315              |
| Outflow 6  | Global Income<br>-865           | Global ex US<br>-1,707            | Healthcare<br>-1,523              | Japan<br>-1,342                  | Global<br>-2,156                  | Real Estate Global<br>-926      | Global<br>-2,964                  | Emerging Markets Global<br>-2,460 | Healthcare<br>-2,195             | Global<br>-2,759                  | Information Technology<br>-3,021  | Healthcare<br>-2,210              | Global ex US<br>-1,970            | Global<br>-1,228                 | US Income<br>-2,308               | Healthcare<br>-2,378             | Emerging Markets Global<br>-917 | Gold & Precious Metals<br>-850   | Information Technology<br>-3,278  | Utilities<br>-1,291               | Communication Services<br>-701   | Information Technology<br>-3,106  | Europe<br>-1,725                 | Gold & Precious Metals<br>-1,319  |
| Outflow 7  | Healthcare<br>-1,284            | Emerging Markets Global<br>-1,736 | Global<br>-1,602                  | US Income<br>-1,453              | Healthcare<br>-2,299              | Real Estate US<br>-1,069        | Europe<br>-4,153                  | Healthcare<br>-2,895              | Global<br>-3,646                 | Emerging Markets Global<br>-2,877 | Healthcare<br>-3,142              | Emerging Markets Global<br>-2,585 | Healthcare<br>-2,709              | US Income<br>-1,613              | Global<br>-2,355                  | Global<br>-3,256                 | Global<br>-2,021                | Consumer Discretionary<br>-1,436 | US Income<br>-4,385               | Consumer Discretionary<br>-1,472  | Asia Pacific<br>-798             | Financials<br>-3,130              | Natural Resources<br>-1,753      | Financials<br>-1,950              |
| Outflow 8  | Natural Resources<br>-2,709     | Europe<br>-2,022                  | Emerging Markets Global<br>-1,808 | Natural Resources<br>-2,480      | US<br>-2,907                      | Europe<br>-1,991                | Healthcare<br>-4,308              | Global ex US<br>-3,033            | Global ex US<br>-4,581           | Information Technology<br>-4,251  | Natural Resources<br>-3,580       | Global<br>-3,403                  | US Income<br>-3,294               | Healthcare<br>-3,743             | Healthcare<br>-2,551              | US Income<br>-3,501              | US Income<br>-3,439             | US Income<br>-2,174              | Global<br>-7,884                  | US Income<br>-2,386               | Healthcare<br>-885               | US<br>-3,186                      | Global Sm&Mid Cap<br>-1,861      | Korea<br>-2,810                   |
| Outflow 9  | US<br>-3,429                    | Global<br>-2,418                  | Natural Resources<br>-2,278       | Financials<br>-3,336             | Emerging Markets Global<br>-3,363 | China<br>-3,005                 | Emerging Markets Global<br>-5,868 | Global<br>-3,923                  | US Income<br>-4,662              | Global ex US<br>-6,430            | Emerging Markets Global<br>-3,843 | US Sm&Mid Cap<br>-11,074          | US Sm&Mid Cap<br>-19,679          | US Sm&Mid Cap<br>-55,555         | US<br>-8,830                      | US Sm&Mid Cap<br>-12,842         | US<br>-6,302                    | Financials<br>-3,107             | Global ex US<br>-8,194            | US Sm&Mid Cap<br>-18,214          | US Sm&Mid Cap<br>-4,481          | Healthcare<br>-3,610              | Real Estate US<br>-3,122         | Emerging Markets Global<br>-2,841 |
| Outflow 10 | US Income<br>-4,880             | US Sm&Mid Cap<br>-3,745           | US Sm&Mid Cap<br>-6,380           | US Sm&Mid Cap<br>-10,534         | US Sm&Mid Cap<br>-9,043           | Healthcare<br>-3,521            | US Sm&Mid Cap<br>-10,504          | US Sm&Mid Cap<br>-8,869           | US Sm&Mid Cap<br>-8,960          | US Sm&Mid Cap<br>-9,295           | US Sm&Mid Cap<br>-15,974          | US<br>-13,107                     | US<br>-27,836                     | US<br>-62,953                    | US Sm&Mid Cap<br>-11,305          | US<br>-18,983                    | US Sm&Mid Cap<br>-20,154        | US Sm&Mid Cap<br>-9,306          | US Sm&Mid Cap<br>-15,056          | US<br>-19,640                     | Financials<br>-5,574             | US Sm&Mid Cap<br>-8,556           | US Sm&Mid Cap<br>-9,151          | US Sm&Mid Cap<br>-4,722           |

Source: LSEG Lipper. June 2024-May 2026. The 20 largest flows by classification are colour coded

## Section 5 – Agency RMBS

### Agency RMBS in 2026: Mid-Year Review of Prepayment Trends and Housing Market Developments

#### Policy and Macroeconomic Developments

##### Restrictions on Institutional Investment in Single-Family Housing

Since the publication of our original 2026 outlook, efforts to limit institutional ownership of single-family homes have advanced significantly. On January 20, 2026, the Administration issued an executive order directing federal agencies and housing-related government entities to restrict support for acquisitions of single-family homes by large institutional investors and to prioritize sales to owner-occupants where legally permissible.

More recently, Congress approved the 21st Century ROAD to Housing Act, which includes restrictions on purchases of single-family homes by large institutional investors. The legislation generally applies to investors controlling at least 350 single-family homes while providing several exceptions, including certain build-to-rent and housing supply related activities. The bill represents one of the most significant federal policy efforts in recent years aimed at limiting institutional participation in the single-family housing market and increasing opportunities for owner-occupant homebuyers. As of June 2026, the legislation has been passed by both chambers of Congress and has been presented to the President for final action.

If implemented, these measures could reduce investor demand in selected markets where institutional ownership is concentrated, potentially improving access for first-time and owner-occupant buyers. However, because institutional investors represent a relatively small share of the overall U.S. housing stock, the impact on nationwide housing affordability is likely to be modest. Mortgage rates, housing inventory, and new housing construction are expected to remain the primary drivers of housing affordability and market activity.

##### Macroeconomic Policy and Geopolitical Considerations

Macroeconomic and geopolitical developments have become increasingly important factors shaping the outlook for the Agency RMBS market in 2026. While housing market fundamentals have remained relatively stable, investors continue to face uncertainty surrounding inflation, fiscal policy, monetary policy, and geopolitical risks.

Core inflation pressures have remained more persistent than previously anticipated, complicating the Federal Reserve's path toward policy easing. Although headline inflation has moderated, underlying inflation measures continue to reflect resilient consumer demand and elevated service-sector prices. As a result, expectations for rapid interest-rate cuts have diminished, contributing to a higher-for-longer rate environment.

At the same time, increased geopolitical tensions in the Middle East, particularly the conflict involving Iran, have contributed to periodic spikes in market volatility. Escalating tensions have increased uncertainty around energy prices, global economic growth, and investor risk sentiment, leading to broader fluctuations across fixed income and housing-related markets.

Fiscal policy has also emerged as an important consideration. Expanding federal deficits and increased Treasury borrowing needs have resulted in a significant rise in Treasury supply, particularly at longer maturities. The combination of elevated issuance and persistent inflation concerns has placed upward pressure on long-term interest rates, contributing to a steeper yield curve and higher mortgage borrowing costs.

Meanwhile, the federal funds rate remains elevated relative to pre-pandemic norms. Although additional policy easing remains possible, the Federal Reserve continues to balance inflation risks against signs of moderating economic growth. Consequently, financing conditions are expected to remain restrictive compared with the low-rate environment that prevailed during much of the previous decade.

## Housing Finance Reform and Mortgage Market Policy

### Adoption of VantageScore 4.0 and Credit Reporting Transition

Since our original outlook, the FHFA has accelerated the implementation of modernized credit scoring for Agency mortgages. On April 22, 2026, FHFA announced an interim framework allowing approved lenders to deliver loans to Fannie Mae and Freddie Mac using either the traditional Classic FICO model or VantageScore 4.0. The initiative is intended to increase competition in credit scoring, expand access to mortgage credit, and provide lenders with greater flexibility while the broader modernization effort continues.

Early adoption is already beginning to appear in Agency collateral. As of June 2026, newly originated loans underwritten using VantageScore 4.0 have started to enter Fannie Mae and Freddie Mac pools through the approved lender rollout process. While these loans currently represent only a small fraction of overall Agency issuance and remain significantly outnumbered by traditional FICO-scored production, their presence marks the first meaningful introduction of VantageScore-based collateral into the Agency RMBS market. As issuance volumes increase, investors and modelers will be able to monitor the performance characteristics of these loans and better assess their implications for prepayment and collateral behavior.

VantageScore 4.0 incorporates trended credit data and may consider additional sources of credit information, including rental payment history, enabling the model to score borrowers with limited or nontraditional credit histories. As a result, the transition has the potential to expand mortgage eligibility for certain first-time homebuyers and younger borrowers while increasing origination opportunities for the Agency market.

At the same time, implementation of FICO 10T remains ongoing. FHFA and the GSEs have indicated that historical FICO 10T loan-level data is expected to be published during the summer of 2026, providing lenders, investors, and modelers with additional information to evaluate the model's performance. However, FICO 10T has not yet been adopted for general loan delivery, and its implementation timeline remains subject to further operational readiness and industry testing.

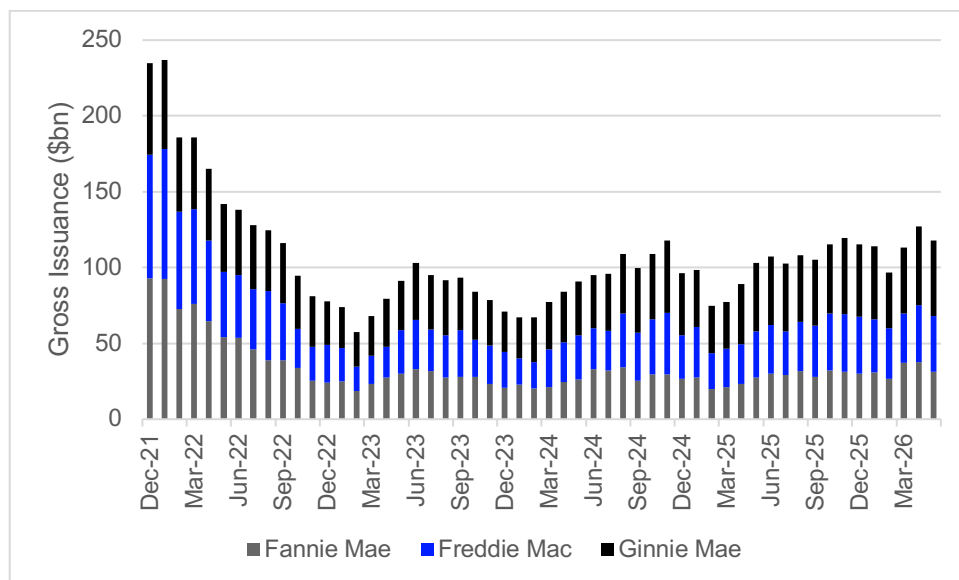
### Issuance

Agency RMBS issuance through the first half of 2026 has continued the recovery that began in 2025, with volumes tracking above year-ago levels and remaining materially stronger than the lows observed in 2023 and early 2024. Based on issuance through June 2026, gross issuance remains consistent with our expectation of a gradual normalization in mortgage origination activity, supported by stable housing demand, improving market liquidity, and a modest increase in refinance opportunities for select borrower cohorts.

Throughout the first half of the year, issuance across Fannie Mae, Freddie Mac, and Ginnie Mae has remained healthy. Fannie Mae and Freddie Mac continued to benefit from stronger conventional origination activity, while Ginnie Mae issuance remained relatively stable, reflecting sustained demand for FHA and VA lending programs. The improvement has been broad-based rather than concentrated in a single issuer, suggesting that origination conditions have become more supportive across both government and conventional channels.

Compared with the same period in 2025, issuance levels are modestly higher and exhibit greater consistency month-to-month. While volumes remain well below the refinancing-driven peak experienced in 2021, the market has continued its transition from a period of historically depressed issuance toward a more normalized environment. Incremental improvements in borrower affordability, a gradual easing of the mortgage rate lock-in effect and increased turnover activity have contributed to stronger production volumes.

The first half of 2026 also shows continued momentum in conventional agency issuance. Fannie Mae and Freddie Mac production has increased as purchase activity stabilizes, and refinancing becomes incrementally more attractive for higher-coupon borrowers. At the same time, Ginnie Mae issuance continues to provide an important source of market stability, supported by FHA and VA borrowers who remain active despite ongoing affordability challenges.

**Exhibit 40: Agency RMBS Gross Issuance by Month**

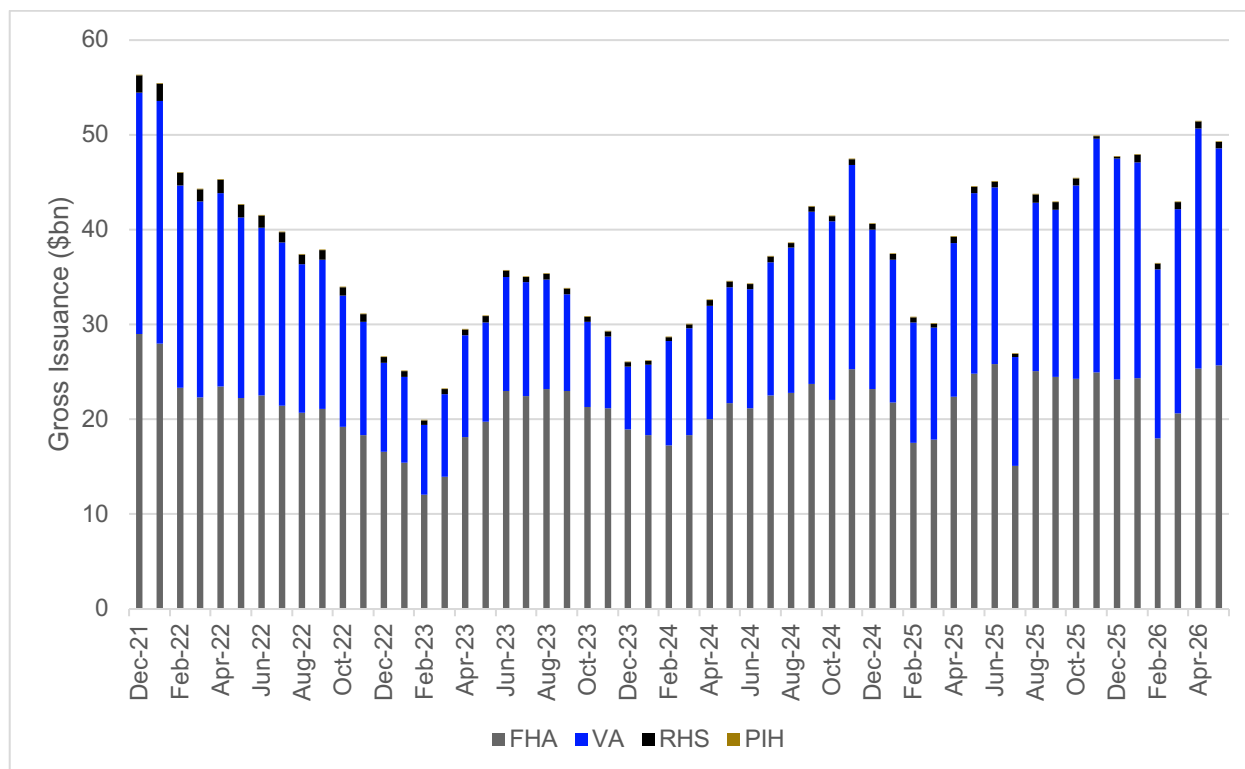
Source: eMBS

Through the first half of 2026, GNMA issuance continues to be dominated by FHA and VA programs, which together account for nearly all Ginnie Mae production. Through the first half of the year, both programs remain on track to exceed 2025 issuance levels, reflecting continued strength in government-backed lending and improving mortgage origination activity. FHA issuance remains the largest contributor to GNMA volume, while VA issuance has maintained the strong momentum that emerged during 2025. As a result, total GNMA issuance through mid-year is running above comparable periods in both 2024 and 2025.

FHA-backed issuance continues to benefit from affordability challenges facing first-time homebuyers and borrowers with limited down payment capacity. Despite elevated home prices and financing costs, FHA lending remains an important source of mortgage credit availability due to its flexible underwriting standards and lower down payment requirements. Issuance volumes have generally remained stable throughout the year, supporting a consistent baseline level of GNMA production.

VA issuance has exhibited particularly strong growth during the first half of 2026. Monthly issuance volumes have remained near recent highs and noticeably above levels observed in 2024. The continued appeal of VA loan features, including low or no down payment requirements and competitive financing terms, has supported sustained borrower demand. This trend has allowed VA loans to capture an increasing share of total GNMA issuance and has been a meaningful driver of overall government-backed mortgage production.

In contrast, RHS and PIH issuance continue to represent only a very small portion of total GNMA volume. While issuance from these programs has increased modestly alongside broader market activity, their contribution remains limited and consistent with their targeted borrower bases and policy mandates.

**Exhibit 41: Ginnie Mae RMBS Gross Issuance by Guarantor**

Source: eMBS

Looking ahead, we continue to expect agency RMBS issuance to remain on an improving trajectory through the remainder of 2026. Assuming moderate economic growth, stable labor market conditions, and continued normalization in housing market activity, issuance should benefit from both purchase and refinance activity. While housing supply constraints and affordability challenges are likely to prevent a return to historically elevated issuance levels, current trends remain broadly consistent with our previously projected range of approximately \$1.5 trillion to \$1.7 trillion in total agency RMBS issuance for 2026.

## Existing Home Sales and Inventory

Existing home sales have remained relatively stable through the first four months of 2026, continuing to operate within the narrow range that has characterized the housing market over the past two years. Sales reached a seasonally adjusted annual rate of 4.02 million in April 2026, modestly below the 4.27 million pace recorded in December 2025. While transaction activity remains subdued by historical standards, the market has shown signs of stabilization despite ongoing affordability challenges.

In the current environment of elevated home prices and mortgage rates that remain high relative to pre-pandemic levels, modest sales activity is not unexpected. Affordability constraints continue to limit buyer demand, particularly among first-time homebuyers, while the lingering mortgage rate lock-in effect continues to discourage some existing homeowners from listing their properties. Nevertheless, sales have remained remarkably resilient, generally holding near the 4 million annualized pace observed throughout 2025.

On the supply side, inventory conditions have improved gradually since the beginning of the year. Total existing home inventory increased from 1.23 million homes in December 2025 to 1.47 million in April 2026, representing the highest inventory level observed since mid-2025.

Despite these improvements, inventory remains low by longer-term historical standards. While the recent increase in listings may reflect a modest easing of the lock-in effect and improving homeowner's willingness to transact, available supply remains insufficient to generate a significant acceleration in housing sales. As a result, housing market activity continues to be characterized by limited inventory, subdued transaction volumes, and moderate competition for available homes.

Overall, the housing market appears to be gradually normalizing. Inventory has improved and sales activity has stabilized at a relatively low but sustainable level. While affordability challenges remain a key constraint, the combination of increasing supply and stable demand suggests that the housing market is moving toward a more balanced environment than that observed during the past several years.

Exhibit 42: Existing Home Sales and Inventory by Month

|                          | 04/26 | 03/26 | 02/26 | 01/26 | 12/25 | 11/25 | 10/25 | 09/25 | 08/25 | 07/25 | 06/25 | 05/25 | 04/25 |
|--------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Existing Home Sales (M)  | 4.02  | 4.01  | 4.13  | 4.02  | 4.27  | 4.09  | 4.11  | 4.08  | 4.03  | 4.03  | 3.98  | 4.04  | 4.02  |
| Inventory (of homes) (M) | 1.47  | 1.39  | 1.32  | 1.26  | 1.23  | 1.44  | 1.52  | 1.53  | 1.53  | 1.55  | 1.54  | 1.54  | 1.45  |
| Inventory (of months)    | 4.4   | 4.2   | 3.8   | 3.8   | 3.5   | 4.2   | 4.4   | 4.5   | 4.6   | 4.6   | 4.6   | 4.6   | 4.3   |
| Median Sales Price (\$K) | 417.7 | 409.1 | 398.0 | 395.0 | 405.1 | 410.0 | 414.9 | 412.3 | 422.4 | 425.7 | 432.7 | 423.7 | 414.0 |

Source: National Association of Realtors

House Price Index

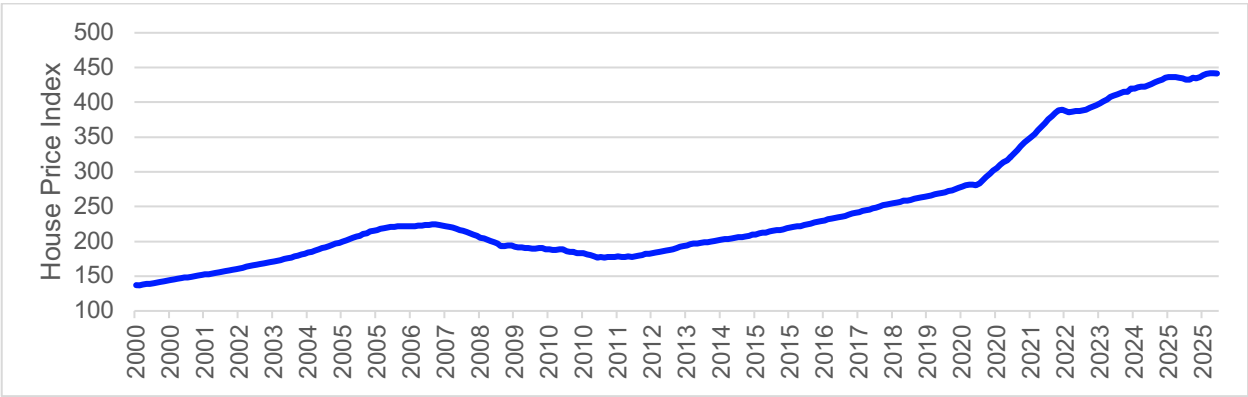
The FHFA House Price Index has remained near record highs through the first half of 2026, though the pace of appreciation continues to moderate relative to the rapid gains observed during 2020–2022. The index reached approximately 442 in recent months, compared with levels near 437 at the end of 2025, indicating continued but modest home price growth.

While home prices continue to increase, appreciation has slowed significantly from the post-pandemic period. House prices remain substantially above pre-pandemic levels, with the index roughly 58% higher than its January 2020 level. However, recent price growth has been considerably more restrained as elevated mortgage rates, affordability constraints, and subdued housing turnover have limited demand.

In the current production prepayment model version v26.1, Yield Book assumes annualized HPA of 2% for 2026, 2.5% for 2027, and 3% thereafter.

Overall, the combination of moderating home price appreciation, gradual improvements in housing inventory, and ongoing housing finance reforms contributes to a cautiously optimistic outlook for the housing market in 2026. Buyers may benefit from modest improvements in inventory availability and expanded credit access resulting from initiatives such as the adoption of VantageScore 4.0. However, affordability remains a significant challenge, as home prices continue to sit near record highs and mortgage rates remain elevated relative to pre-pandemic levels. The labor market has remained resilient through the first half of 2026, supporting household formation and housing demand, though uncertainty surrounding economic growth, AI-driven automation, productivity shifts, and potential workforce reductions across certain sectors could weigh on employment expectations and consumer confidence. While increased inventory and slower house price growth should help ease affordability pressures at the margin, a more meaningful improvement in housing activity will likely require either lower borrowing costs or a larger increase in housing supply. Overall, the housing market is expected to continue its gradual normalization through the remainder of 2026, characterized by modest home price appreciation, improving inventory conditions, and stable, but historically subdued, sales activity.

Exhibit 43: US Monthly FHFA House Price Index (Purchase Only)



Source: Federal Housing Finance Agency

## Mortgage Rates

Mortgage rates have remained relatively stable through the first half of 2026, following the gradual decline observed during 2025. The 30-year fixed mortgage rate averaged approximately 6.5% in recent months, while the 15-year fixed mortgage rate remained near 5.8%. Although rates remain elevated relative to the historically low levels observed during 2020 and 2021, they have generally traded within a narrower range than in prior years, providing greater certainty for both borrowers and lenders.

By comparison, mortgage rates experienced significant volatility during 2023 and 2024 as markets adjusted to changing inflation expectations and monetary policy. The 30-year fixed rate peaked above 7% several times during 2024 before declining modestly in late 2024 and throughout 2025. In contrast, the first half of 2026 has been characterized by more stable rate conditions, with mortgage rates fluctuating within a relatively limited range despite ongoing uncertainty surrounding inflation, economic growth, and Federal Reserve policy.

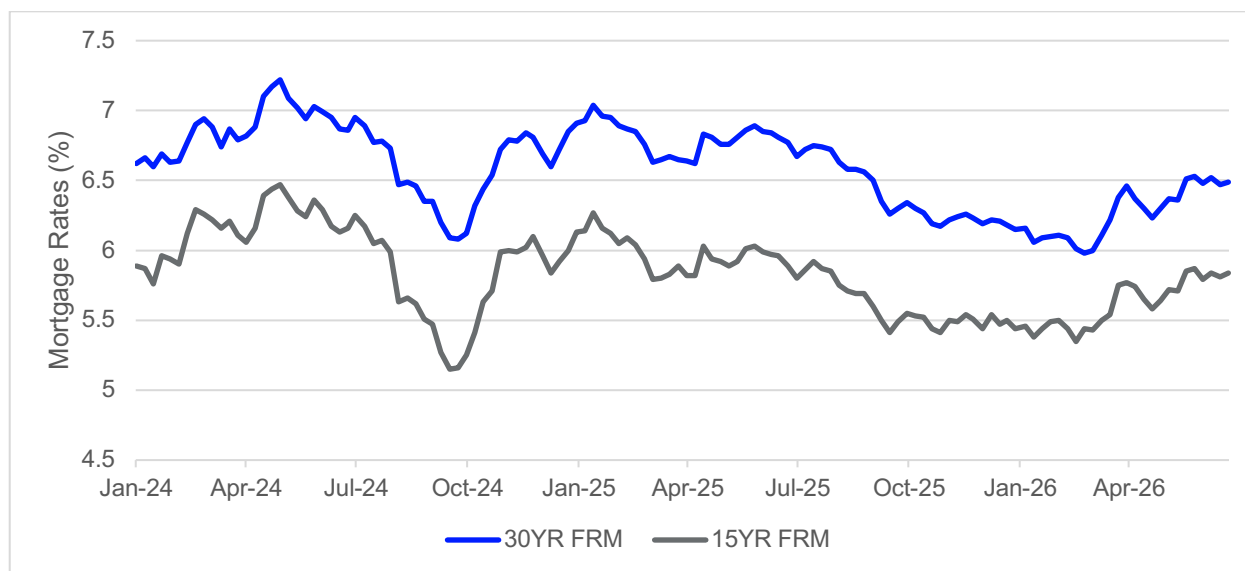
The persistence of mortgage rates near current levels continues to weigh on housing affordability and transaction activity. While rates are below the peaks reached during the recent tightening cycle, they remain substantially higher than the mortgage rates held by many existing homeowners. As a result, the mortgage rate lock-in effect continues to limit housing turnover, although gradually improving inventory levels suggest that its impact may be moderating.

Looking ahead, mortgage rates are expected to remain sensitive to inflation trends, labor market conditions, Federal Reserve policy decisions, and broader macroeconomic developments. While markets continue to anticipate additional monetary policy easing over time, the timing and magnitude of future rate declines remain uncertain. As a result, mortgage rates are likely to remain elevated relative to pre-pandemic norms, though modest declines remain possible if inflation continues to moderate and economic growth slows.

Overall, the mortgage rate environment in 2026 appears more stable than in recent years, reducing one source of uncertainty for borrowers and housing market participants. However, rates remain high enough to constrain affordability and limit refinancing incentives for most borrowers. Consequently, mortgage rates will continue to play a central role in shaping housing demand, mortgage origination activity, and prepayment behavior throughout the remainder of 2026.

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### Exhibit 44: US Weekly Primary Mortgage Market Survey



Source: Freddie Mac

## Prepayment

Prepayment speeds for both conventional and GNMA securities remained elevated through the first five months of 2026, extending the pickup that began during the second half of 2025. While speeds moderated somewhat from the seasonal highs observed in March, prepayment activity remained generally above the levels recorded during most of 2025, reflecting a combination of housing turnover, seasonal factors, and refinancing activity among higher-coupon borrowers.

For conventional securities, prepayment activity accelerated during the first quarter of 2026 before moderating in April and May. FNMA 30-year speeds increased from 8.8 CPR in December 2025 to a peak of 11.0 CPR in March before declining to 8.2 CPR in May. FHLMC 30-year speeds followed a similar pattern. Although speeds retraced from their seasonal highs, they remained elevated relative to levels observed during much of early 2025.

Conventional 15-year products exhibited a similar but more muted pattern. FNMA 15-year speeds peaked at 8.6 CPR in March and May, while FHLMC 15-year speeds reached 9.4 CPR in March before declining modestly to 8.9 CPR in May. The relatively stable performance of these cohorts reflects the greater refinancing sensitivity typically associated with shorter-term mortgages.

GNMA securities continued to prepay faster than their conventional counterparts. GNMA II 30M speeds rose from 12.1 CPR in December 2025 to 14.6 CPR in March before moderating to 11.4 CPR in May, while GNMA II 30C speeds increased from 13.2 CPR to 14.2 CPR during the same period before easing to 12.5 CPR. The stronger prepayment performance of GNMA collateral continues to be supported by borrower characteristics, streamlined refinance programs, and greater turnover relative to conventional pools.

The increase in prepayment activity during early 2026 occurred despite mortgage rates remaining elevated relative to historical norms. While current rates continue to limit refinancing opportunities for deeply out-of-the-money borrowers, at-the-money and in-the-money cohorts remain responsive to changes in financing conditions. At the same time, gradually improving housing inventory and stable home sales activity have continued to support turnover-related prepayments across both conventional and government-backed collateral.

Overall, prepayment activity through the first half of 2026 remains consistent with our expectation that turnover will continue to be the primary driver of prepayments for out-of-the-money borrowers, while refinancing activity remains concentrated among higher-coupon cohorts. Mortgage rates, housing turnover, and the pace of housing market normalization will continue to be key determinants of prepayment performance through the remainder of 2026.

#### Exhibit 45: Actual Prepayment Speed by Product

|            | RPB(\$B) | 05/26 | 04/26 | 03/26 | 02/26 | 01/26 | 12/25 | 11/25 | 10/25 | 09/25 | 08/25 | 07/25 | 06/25 | 05/25 |
|------------|----------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| FNMA 30    | 2,908.5  | 8.2   | 9.2   | 11.0  | 9.0   | 7.6   | 8.8   | 8.4   | 10.5  | 7.9   | 7.2   | 7.4   | 7.1   | 7.4   |
| FNMA 15    | 287.4    | 8.6   | 8.5   | 8.6   | 7.4   | 7.6   | 8.0   | 7.1   | 8.8   | 8.1   | 7.9   | 8.1   | 7.8   | 7.8   |
| FHLMC 30   | 2,594.8  | 8.6   | 9.9   | 12.0  | 9.9   | 8.2   | 9.5   | 9.2   | 11.5  | 8.4   | 7.4   | 7.6   | 7.3   | 7.6   |
| FHLMC 15   | 245.7    | 8.9   | 9.1   | 9.4   | 8.0   | 8.2   | 8.8   | 7.7   | 9.9   | 8.7   | 8.5   | 8.5   | 8.2   | 8.0   |
| GNMAII 30M | 1,923.4  | 11.4  | 12.9  | 14.6  | 11.9  | 10.5  | 12.1  | 12.1  | 14.7  | 10.9  | 9.4   | 8.9   | 8.7   | 10.3  |
| GNMAII 30C | 627.7    | 12.5  | 13.9  | 14.2  | 12.4  | 11.0  | 13.2  | 11.8  | 13.4  | 11.1  | 9.6   | 9.2   | 8.9   | 10.2  |
| GNMAII 15M | 13.1     | 13.2  | 13.4  | 13.8  | 11.8  | 12.2  | 11.7  | 10.2  | 13.0  | 11.2  | 11.7  | 11.3  | 11.4  | 11.2  |
| GNMA 30    | 39.0     | 7.1   | 7.0   | 6.7   | 5.8   | 6.0   | 6.5   | 5.9   | 6.7   | 6.5   | 6.6   | 6.9   | 6.6   | 6.7   |

Source: eMBS

#### Exhibit 46: Projected Prepayment under Different Rate Scenario (% of Mortgage Paying Off in 1 Year)

| Rate Change | FNM Refinance | FNM Home Sale | GNII Refinance | GNII Home Sale |
|-------------|---------------|---------------|----------------|----------------|
| -3.00%      | 22.27%        | 4.59%         | 39.66%         | 5.11%          |
| -2.00%      | 17.23%        | 4.50%         | 29.68%         | 5.03%          |
| -1.00%      | 8.93%         | 4.40%         | 17.07%         | 4.94%          |
| Current     | 2.41%         | 4.20%         | 3.63%          | 4.77%          |
| 1.00%       | 1.05%         | 3.81%         | 1.34%          | 4.29%          |
| 2.00%       | 0.70%         | 3.30%         | 1.10%          | 3.61%          |
| 3.00%       | 0.56%         | 2.84%         | 0.98%          | 3.02%          |

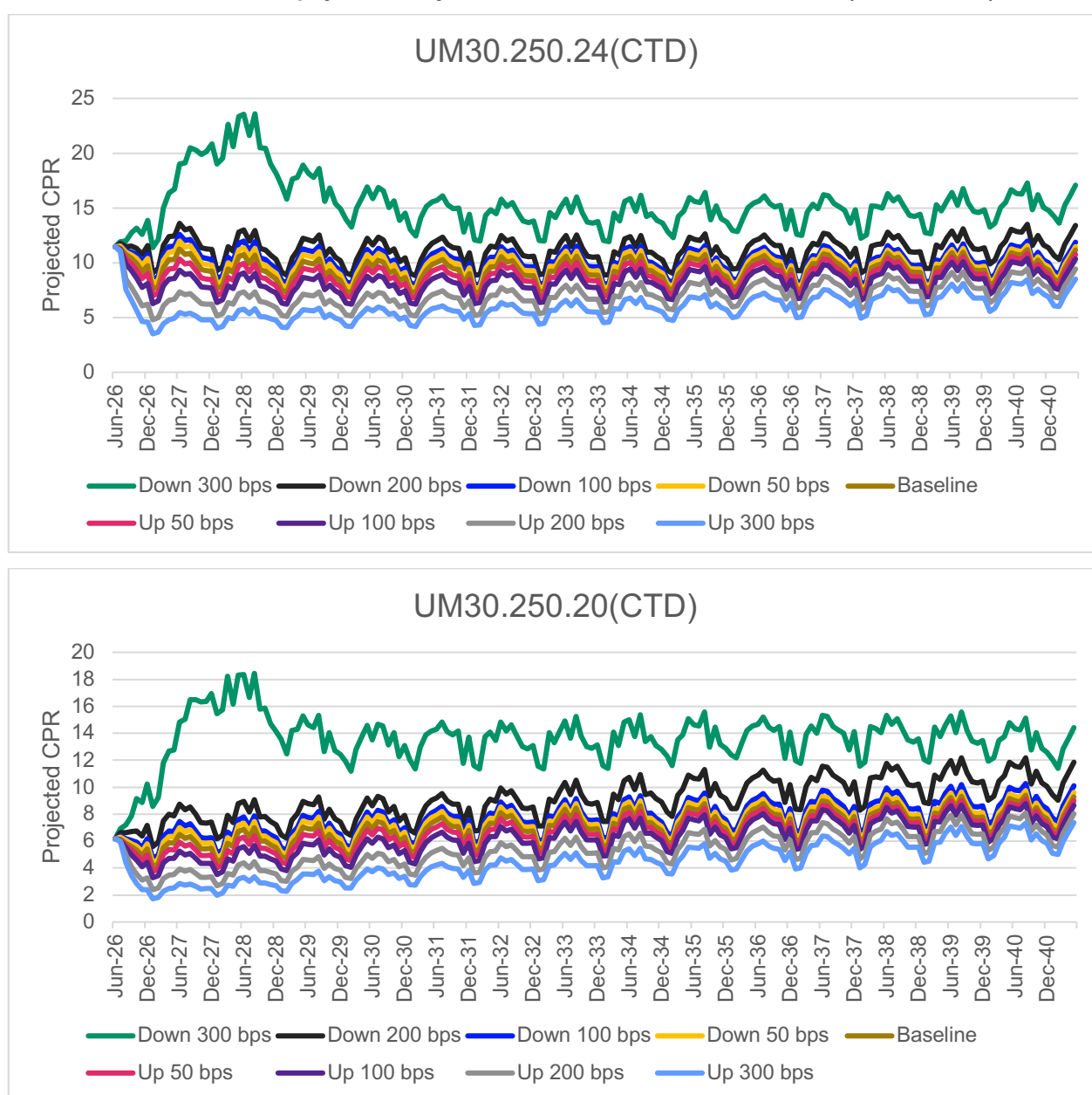
Source: LSEG Yield Book

For out-of-the-money (OTM) agency RMBS, turnover prepayments are expected to remain the primary source of prepayment activity in 2026, as elevated mortgage rates continue to limit refinancing incentives for most borrowers. Under the current rate environment, projected home sale activity accounts for approximately 4.2% of annual prepayments for Fannie Mae and 4.8% for Ginnie Mae, while refinance activity remains comparatively muted.

If mortgage rates decline, refinancing activity is expected to increase significantly, particularly for borrowers that move closer to at-the-money status. A 100-bps rate decline increases projected refinance activity to 8.9% for Fannie Mae and 17.1% for Ginnie Mae collateral, while a 200-bps decline raises projected refinance activity to 17.2% and 29.7%, respectively. Conversely, in a higher-rate environment, refinance activity falls below current levels, while turnover activity remains the primary driver of prepayments.

Exhibit 47 presents projected prepayment speeds across various interest rate scenarios for the deeply OTM UMBS 30-year cheapest-to-deliver (CTD) cohort originated in 2024 and 2020 with a 2.5 coupon.

**Exhibit 47: Yield Book Prepayment Projections for Different Rate Scenarios (OTM Cohort)**

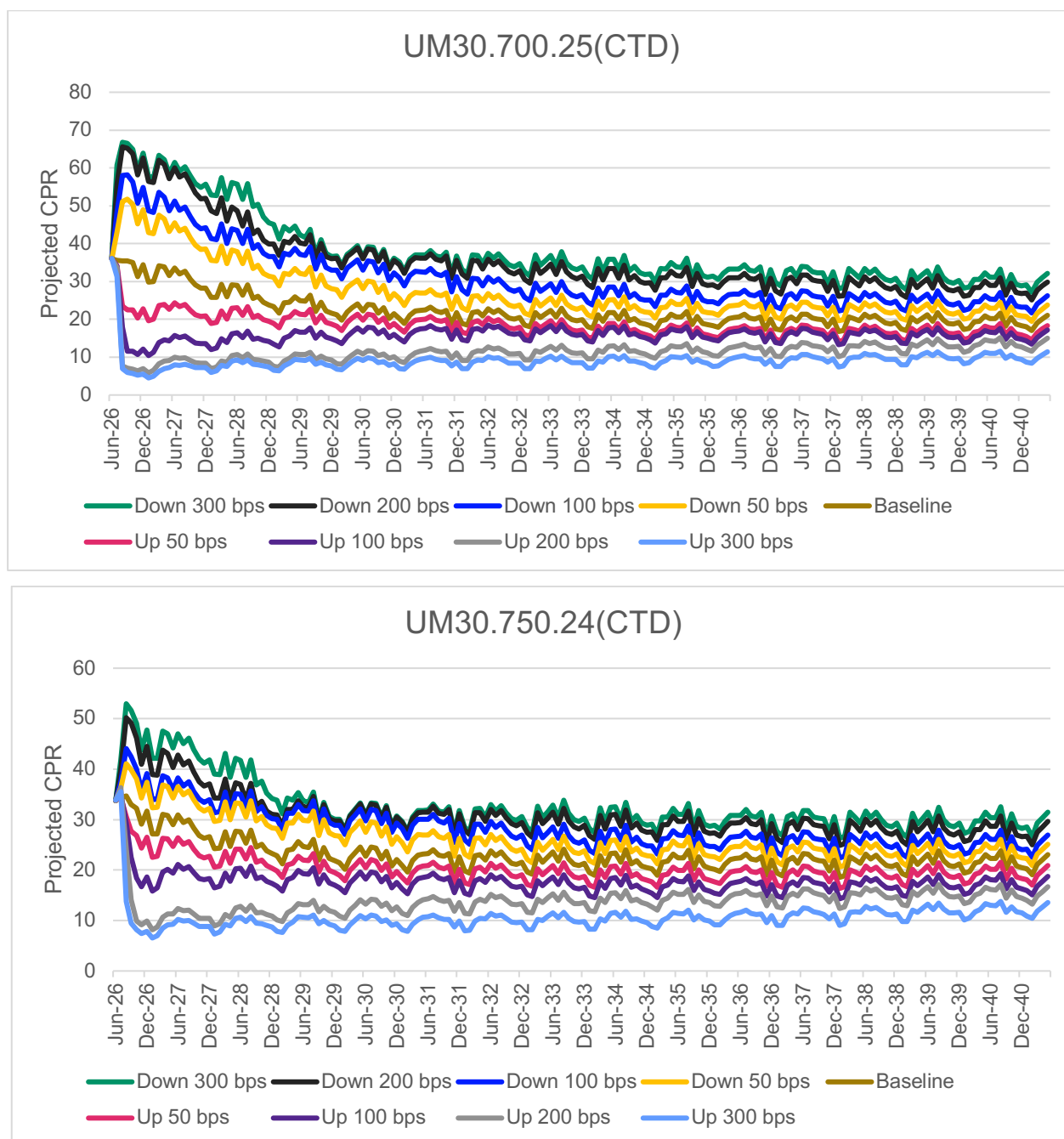


Source: LSEG Yield Book

For in-the-money (ITM) cohorts, prepayment activity is expected to accelerate in 2026 if mortgage rates continue to decline, as borrowers become increasingly incentivized to refinance or move. The responsiveness is likely to be particularly pronounced in newer vintages, where lower prevailing rates relative to existing loan coupons create the strongest financial incentive. Media coverage and heightened borrower awareness of refinancing options may further amplify prepayment activity, potentially resulting in a surge in prepayment speeds compared with 2025 levels.

Exhibit 48 illustrates projected prepayment behavior for two deeply in-the-money (ITM) UMBS 30-year cheapest-to-deliver (CTD) cohorts with 7.0% coupons, originated in 2025 and 2024.

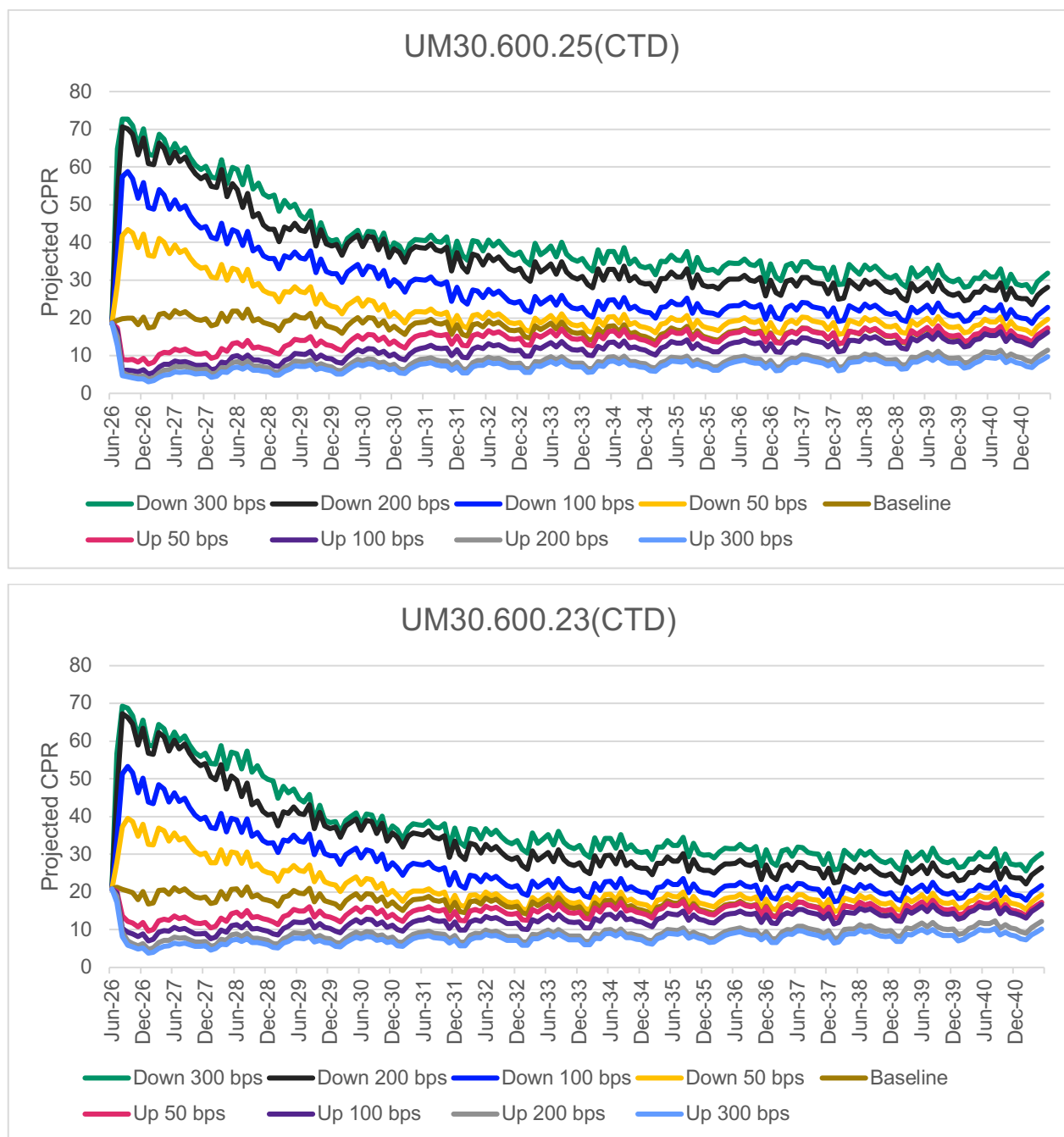
**Exhibit 48: Yield Book Prepayment Projections for Different Rate Scenarios (ITM Cohort)**



Source: LSEG Yield Book

Exhibit 49 presents projected prepayment speeds under various interest rate scenarios for the at-the-money (ATM) UMBS 30-year cheapest-to-deliver (CTD) cohorts with 6.0% coupons, originated in 2025 and 2023. In both newer and older vintages, prepayment rates are projected to increase sharply in response to declining interest rates.

**Exhibit 49: Yield Book Prepayment Projections for Different Rate Scenarios (ATM Cohort)**



Source: LSEG Yield Book

## Conclusion

The Agency RMBS market has remained resilient through the first half of 2026, supported by stable issuance, gradually improving housing inventory, and moderating home price appreciation. While mortgage rates have remained elevated relative to pre-pandemic levels, housing market activity has stabilized and prepayment speeds have increased modestly, driven primarily by turnover and refinancing activity among higher-coupon borrowers.

Recent policy developments, including progress on restrictions targeting institutional ownership of single-family homes, ongoing GSE reform discussions, the rollout of VantageScore 4.0, and continued evaluation of mortgage portability initiatives, may influence housing affordability, credit availability, and mortgage market liquidity. At the same time, persistent inflation pressures, elevated federal deficits, and geopolitical uncertainty continue to present risks to the interest-rate outlook.

Market participants should continue to monitor interest rates, housing supply, federal housing policies, and broader macroeconomic conditions, which will remain key drivers of mortgage origination activity, prepayment behavior, and overall Agency RMBS performance through the remainder of 2026.

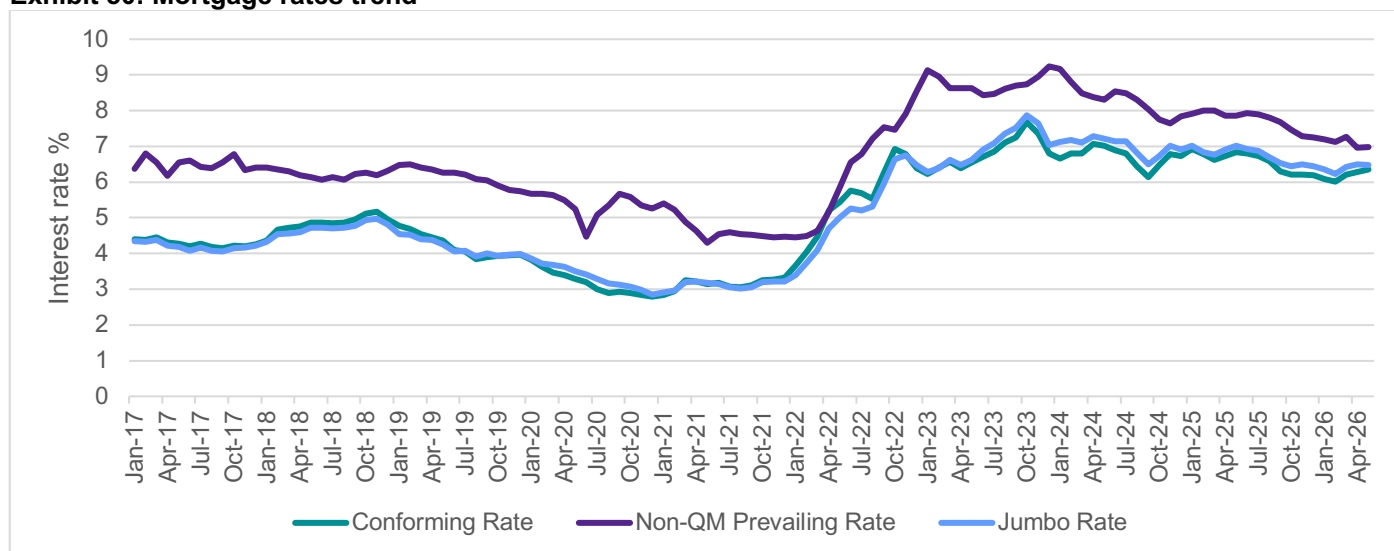
## Section 6 – Non-Agency RMBS

### Strong growth and resilient performance

#### Mortgage rates

Mortgage rates rose sharply after 2021 and remain well above pre-pandemic levels. Non-QM rates continue to carry a premium versus conforming and jumbo rates; however, the spread has narrowed as the Non-QM market has become more competitive, with no recent indication of widening.

**Exhibit 50: Mortgage rates trend**



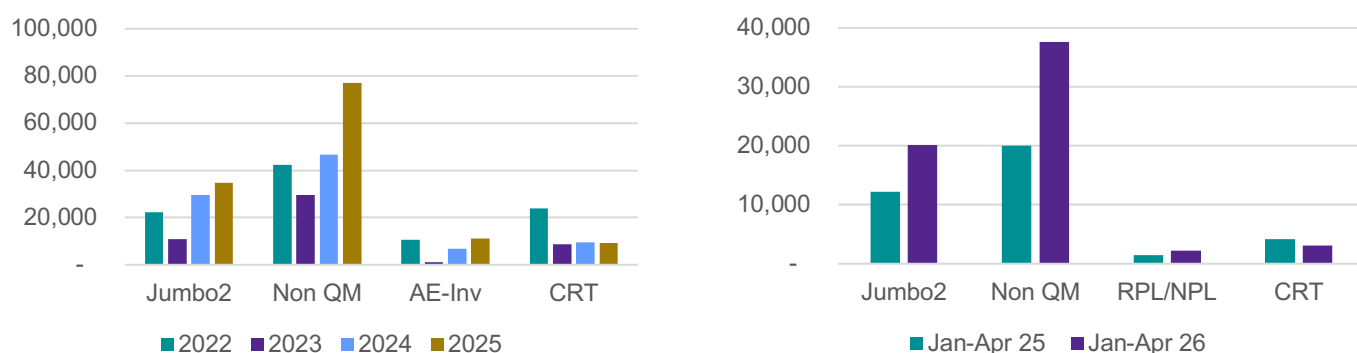
Source: LSEG Yield Book, Optimal Blue

#### Non-Agency Securitization Issuance

Public Non-QM RMBS has been the standout sector within private-label mortgage credit. Non-QM issuance increased from approximately \$46.7bn in 2024 to \$77.2bn in 2025, followed by a further acceleration in early 2026. In Jan–Apr 2026, public Non-QM issuance reached approximately \$37.6bn, compared with \$20.1bn in Jan–Apr 2025, representing growth of about 87.1%. This suggests that Non-QM is benefiting not only from collateral supply, but also from improved securitization execution, repeat issuer programmes, and broader investor acceptance.

This growth outpaced Jumbo 2.0 over the same Jan–Apr period and contrasts with weaker CRT issuance trend. At the same time, Jumbo 2.0 issuance has also been strong in 2026 and is trending for another strong year.

**Exhibit 51: Non-agency securitization volumes**

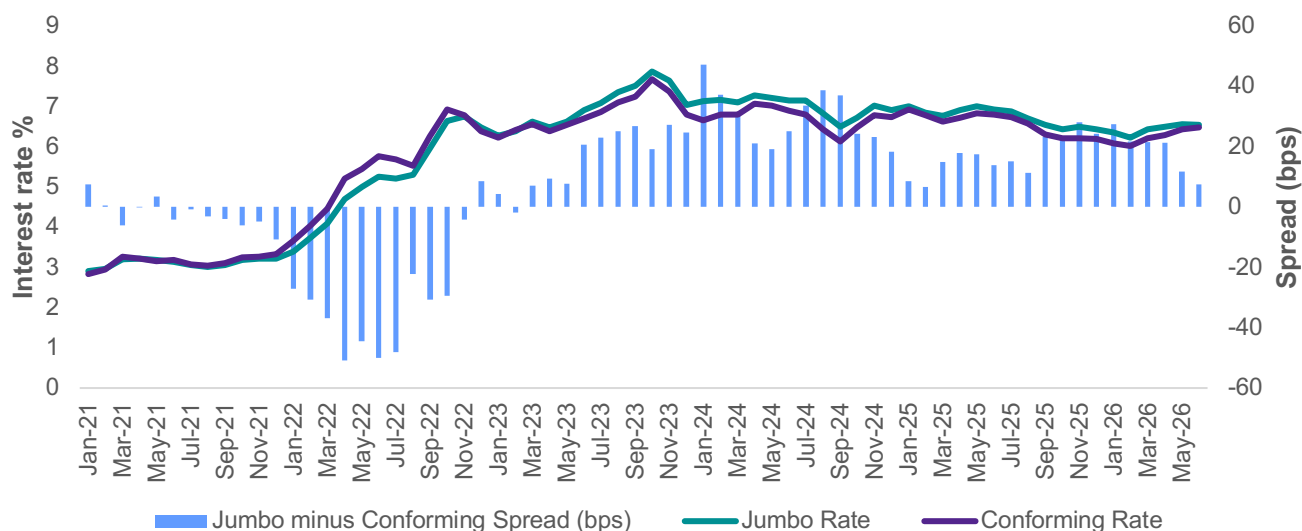


Source: LSEG Yield Book

## Spreads

Jumbo 2.0 rates have remained close to conforming rates in recent months, with a modest positive spread rather than the negative spread seen in parts of 2022. The persistence of a positive jumbo premium is consistent with elevated rate volatility and tighter bank balance-sheet discipline, even as prime jumbo credit remains strong.

**Exhibit 52: Jumbo 2.0 interest rates compared to conforming**

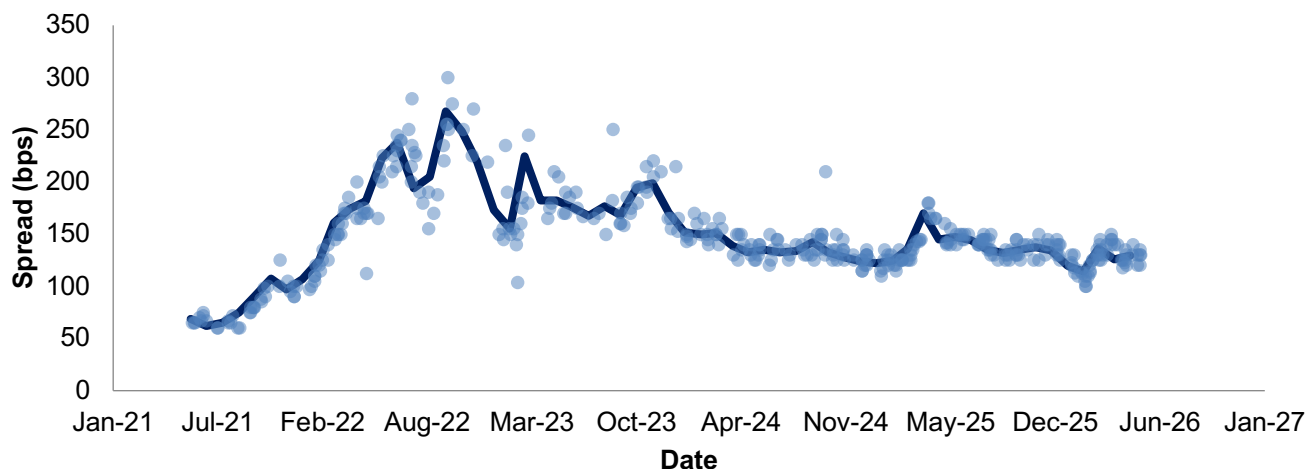


Source: Federal Reserve Bank of St. Louis (Provided by Optimal Blue's OBMMI)

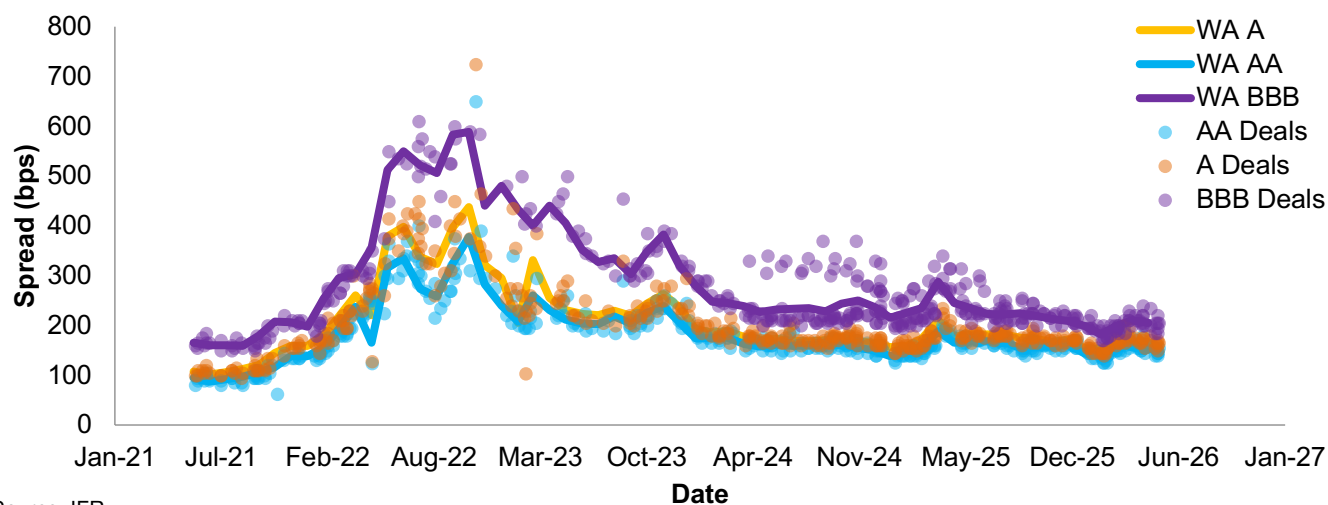
Non-QM spreads to the I-Curve have tightened materially from the 2022 and 2023. The AAA spreads on certain deals reached levels into the low-110s in early 2026 before widening in March as a result of the Iranian conflict and partially retracing in April–May.

The tightening trend in the past year reflects several factors: stronger credit performance than expected, attractive value of the Non-QM asset class. The recent Iran-related volatility affected oil prices, inflation expectations, Treasury yields, mortgage rates, and broader risk appetite, which all feed into Non-QM execution.

**Exhibit 53: Non-QM AAA rated spreads over I-Curve**



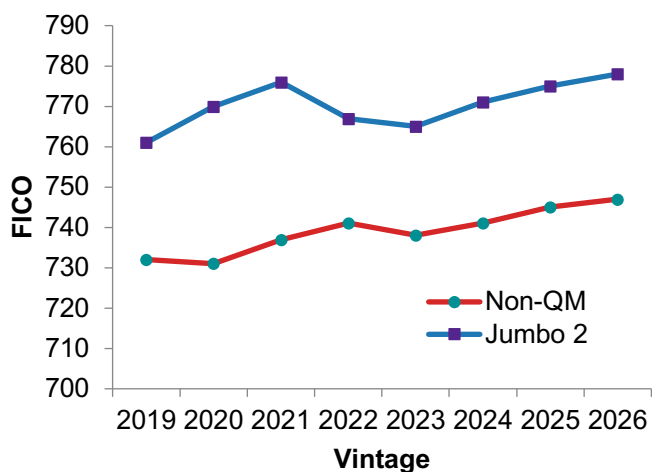
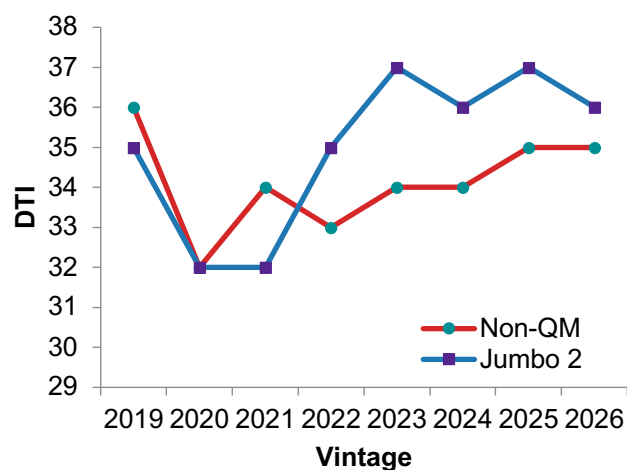
Source: IFR

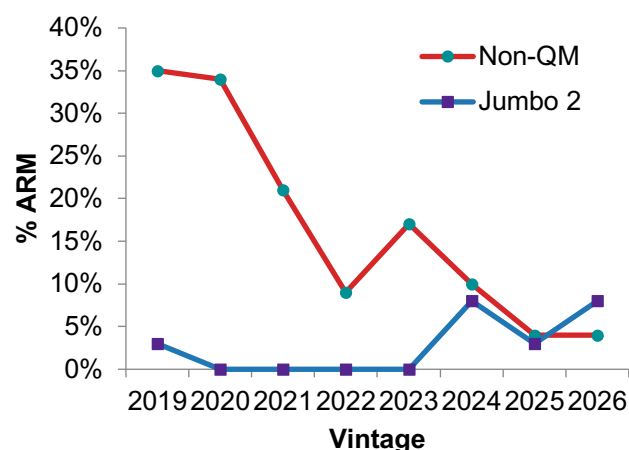
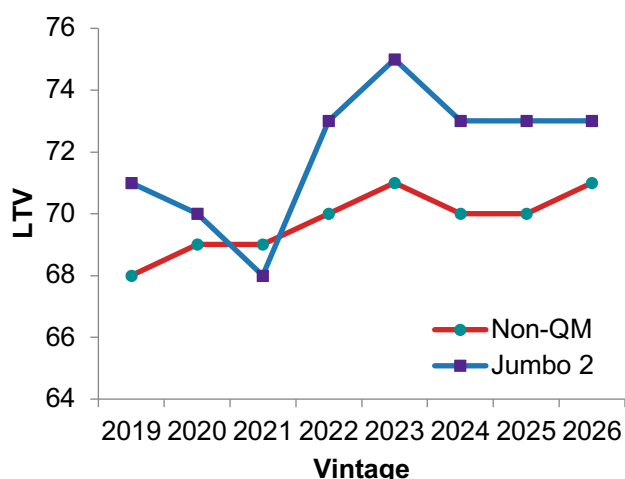
**Exhibit 54: Non-QM AA/A/BBB rated spreads over I-Curve**

Source: IFR

## Collateral Characteristics

Non-QM and Jumbo collateral show clear differences across vintages. Jumbo borrowers generally have higher credit scores, while Non-QM loans carry higher coupons. Leverage and DTI remain broadly stable, with Jumbo showing slightly higher CLTV and DTI in recent vintages.

**Exhibit 55: Non-QM vs. Jumbo collateral profile****FICO score by origination year****DTI by origination year****Combine LTV by origination year****% ARMS mortgages by origination year**



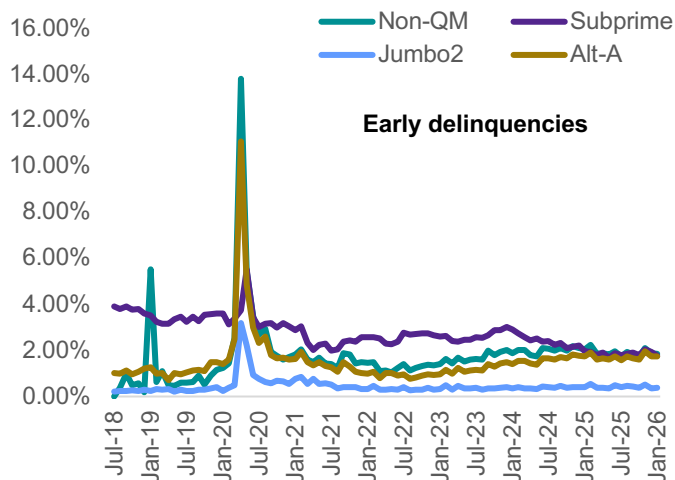
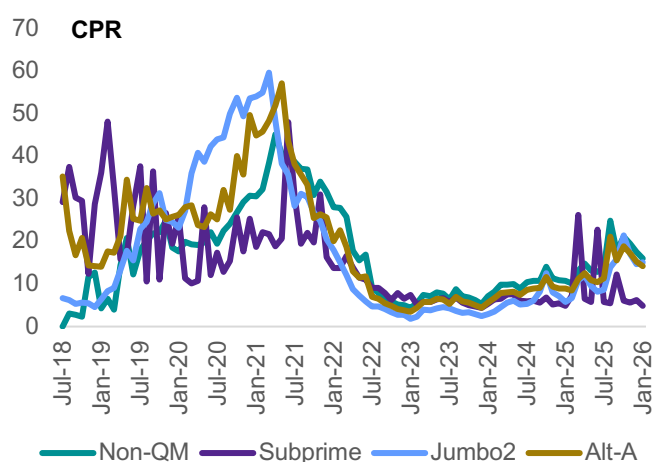
Source: LSEG Yield Book, Cotality

As debt servicing costs have increased, DTI has naturally increased over the last several years.

## Prepayments

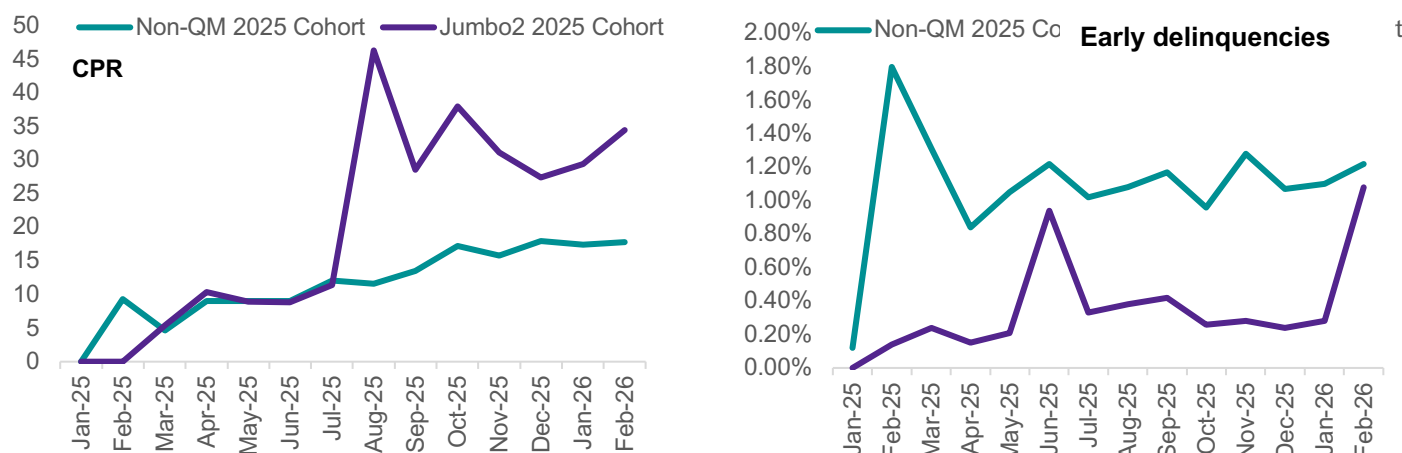
Across all Non-Agency RMBS fixed cohorts, prepayment speeds have fallen from the high levels seen in 2020–2021. Early Delinquency rates have remained fairly stable, with Non-QM generally in line with Alt-A and well below the spike seen during the 2020 stress period.

### Exhibit 56: Prepayments and early delinquencies of all non-agency RMBS fixed cohorts



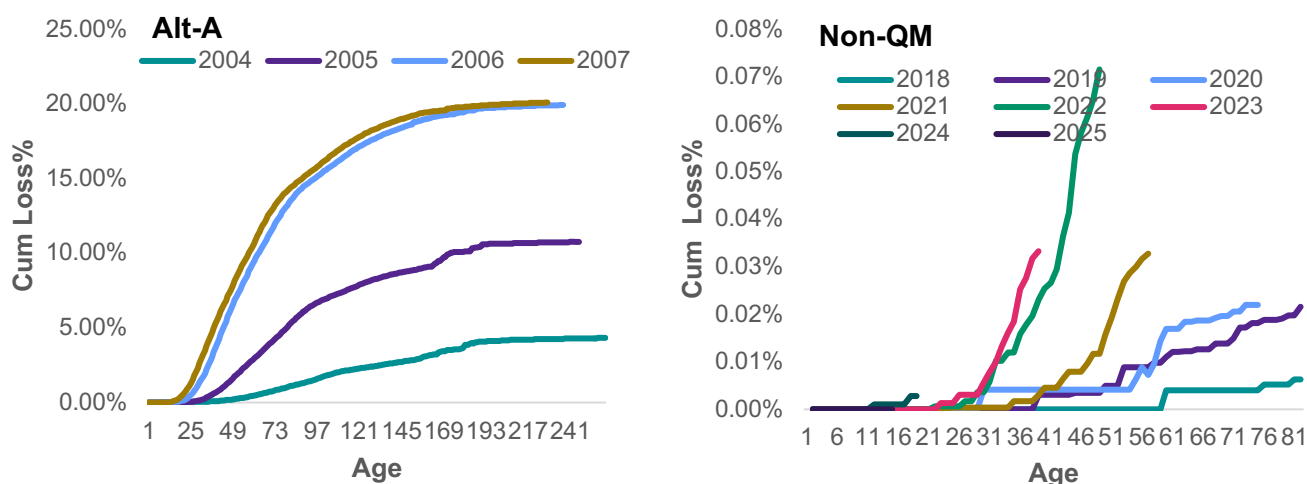
Source: LSEG Yield Book, Cotality

For the latest cohorts, prepayment speeds picked up in 2025 year, with Jumbo 2.0 increasing more sharply than Non-QM. Early Delinquency rates remained low despite some volatility in the Non-QM cohort. In recent months, Jumbo 2.0 prepayment speeds have calmed down from the heights in Q3 2025, and we expect them to continue trending down.

**Exhibit 57: Prepayments and early delinquencies of 2025 Non-QM and Jumbo fixed cohorts**

## Credit Risk

Non-QM cumulative losses remain very low across vintages, but there are some recent increases. In contrast, older Alt-A vintages show much higher loss levels. This supports the argument that post-crisis underwriting, diligence and structures have performed well so far. Jumbo 2 cohort have had almost 0 losses so we will not report on them in the Exhibit 58 below.

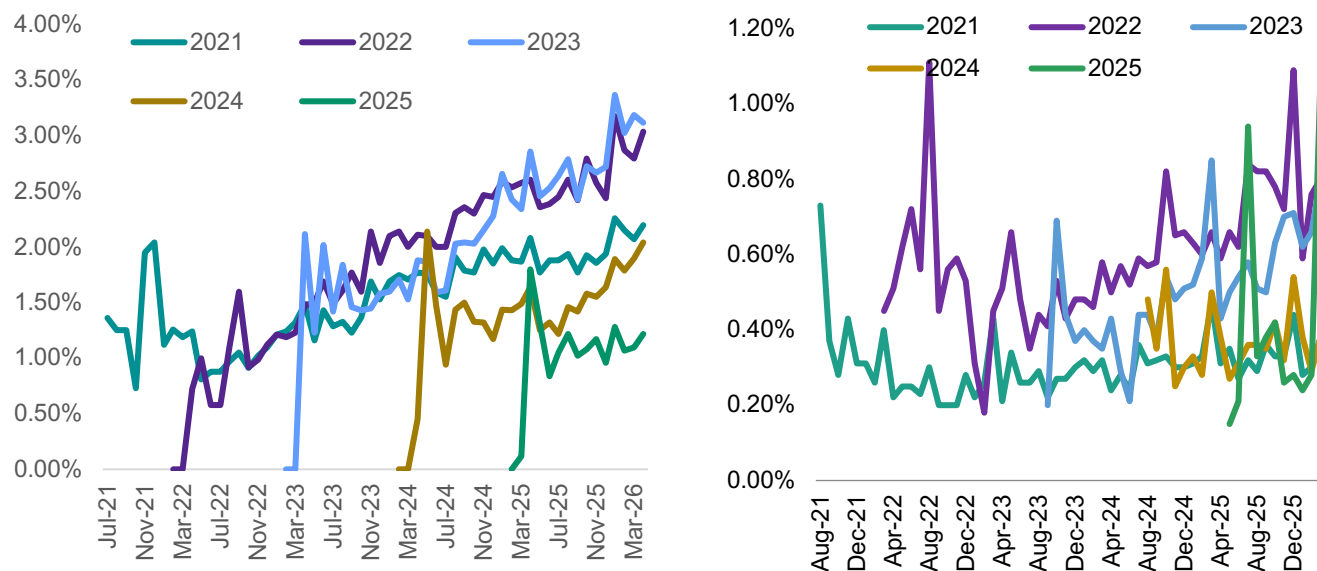
**Exhibit 58: Cumulative losses comparisons between non-agency cohorts**

Source: LSEG Yield Book, Cotality

Source: LSEG Yield Book, Cotality

Early delinquency rates have increased for several recent Non-QM vintages, especially the 2022 and 2023 cohorts. By segment, Bank Statement/Self-Employed and Prime Non-QM show higher delinquency levels, while Jumbo Non-QM remains the strongest performer.

**Exhibit 59: Early delinquency rates for Non-QM and Jumbo 2 cohorts**

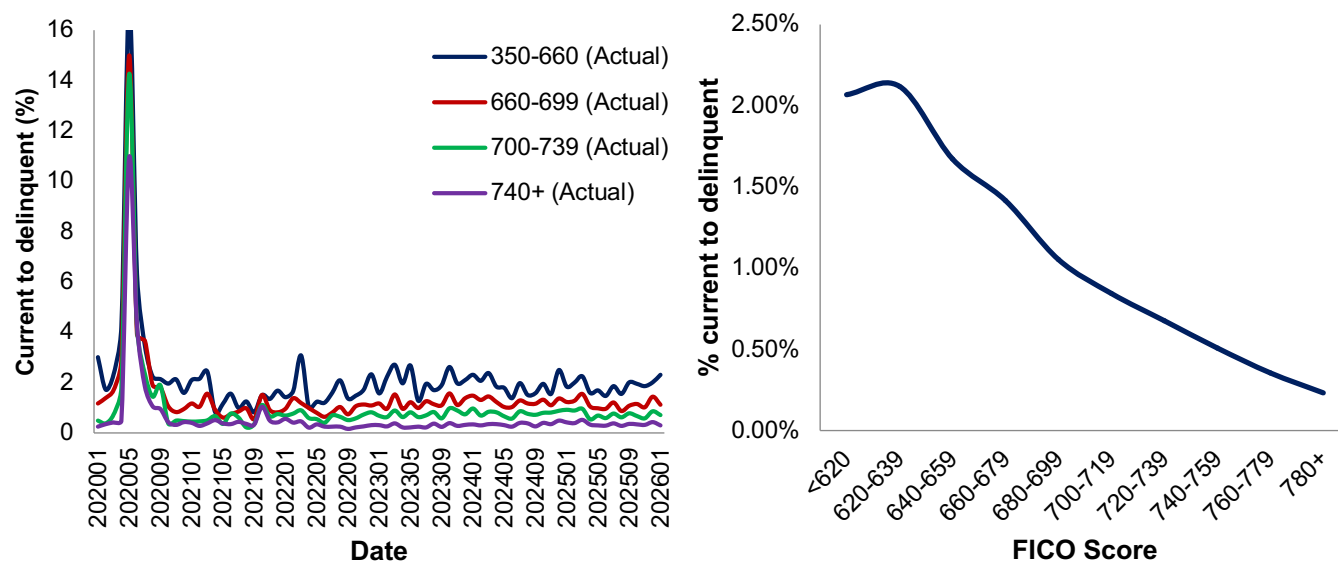


Source: LSEG Yield Book, Cotality

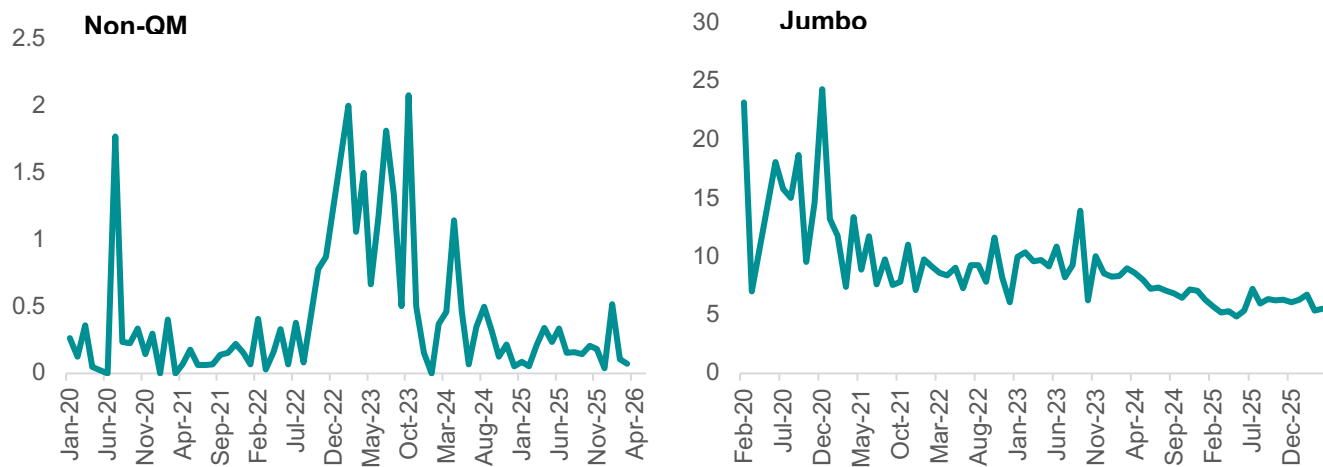
## Drivers of Credit Risk

FICO remains an important driver of credit performance. Credit risk is clearly higher for lower FICO borrowers, while higher FICO groups show lower and more stable default rates.

**Exhibit 60: FICO impact on Non-QM**

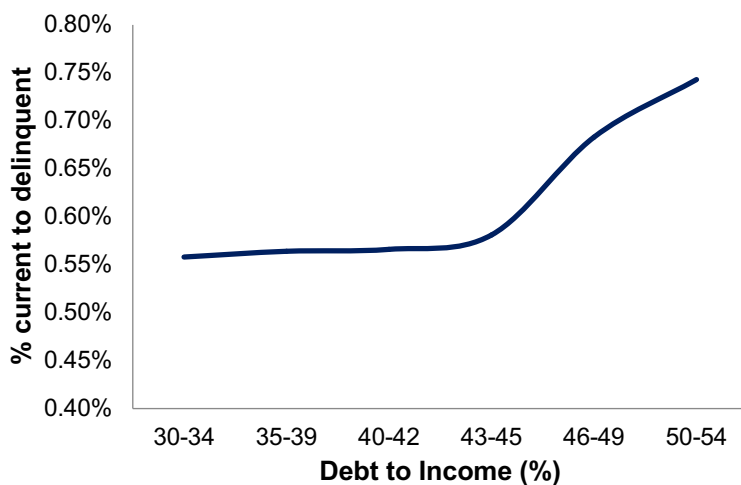


Source: LSEG Yield Book, Cotality

**Exhibit 61: Non-QM and Jumbo 2: % of FICO<680 by origination date**

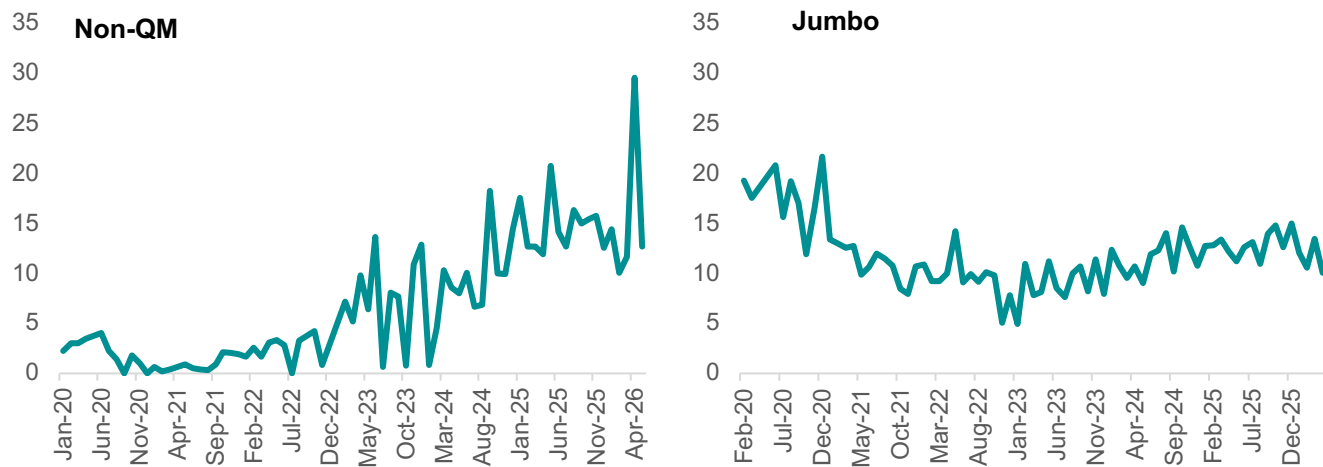
Source: LSEG Yield Book, Cotality

Delinquency risk is generally similar across most DTI groups, but it increases more noticeably at higher DTI levels. Borrowers with DTI above 46% show higher transition rates, which reflects that elevated DTI remains an important credit risk factor.

**Exhibit 62: DTI Impact – Non-QM**

Source: LSEG Yield Book, Cotality

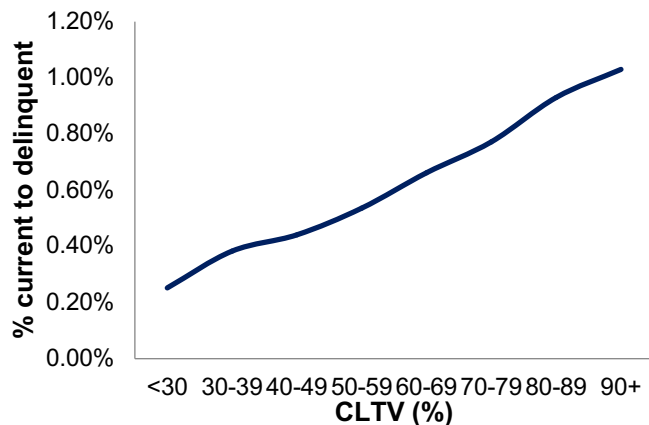
**Exhibit 63: Non-QM and Jumbo 2: % DTI > 45 by origination date**



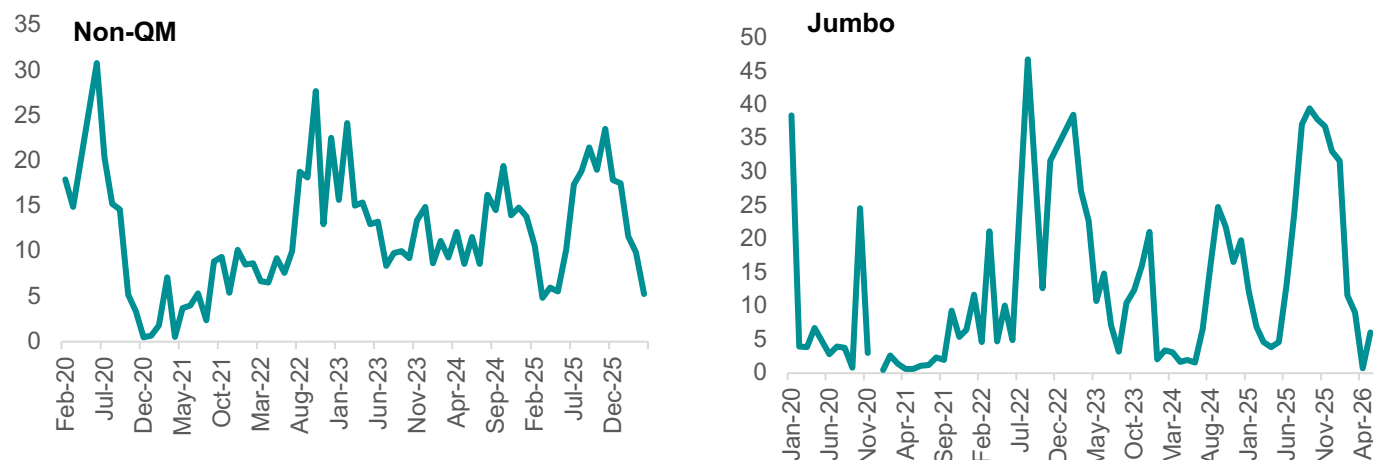
Source: LSEG Yield Book, Cotality

Loan to Value remains a first-order risk driver. The current-to-delinquent transition rate rises steadily as Combined Loan to Value increases, confirming that borrower equity remains an important mitigant, particularly if home-price appreciation slows.

**Exhibit 64: Loan to value impact**

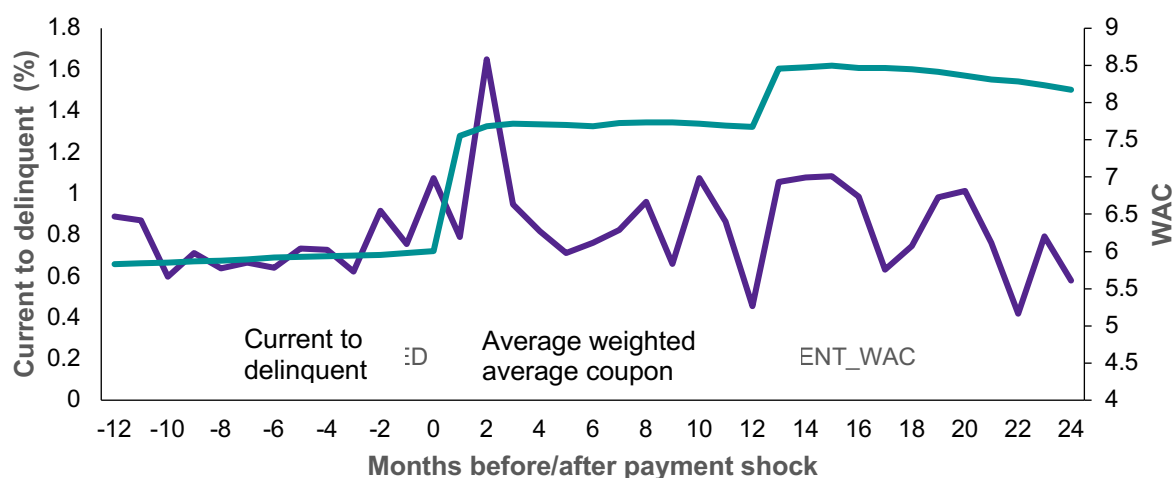


Source: LSEG Yield Book, Cotality

**Exhibit 65: Non-QM and Jumbo 2: % LTV > 80 by origination date**

Source: LSEG Yield Book, Cotality

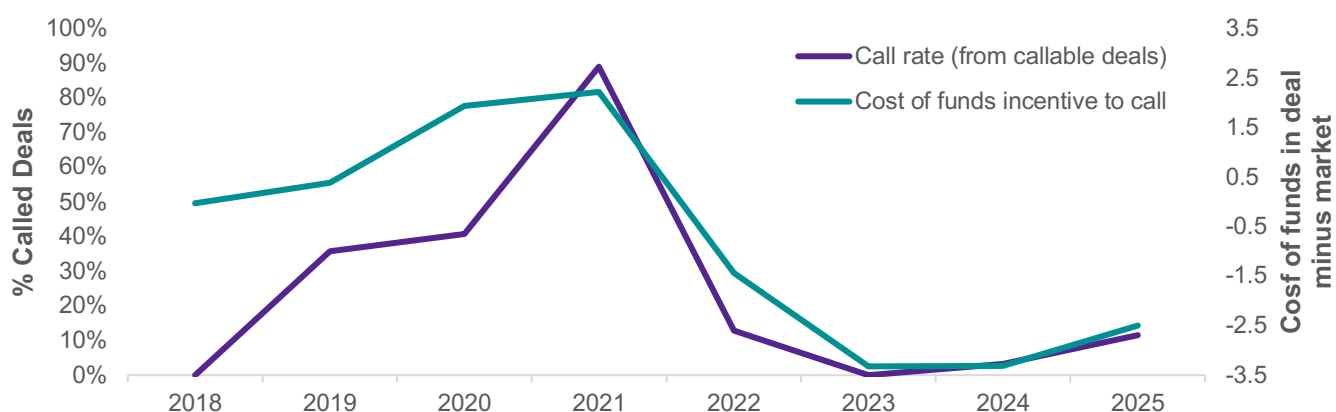
Delinquencies rise around the payment reset period, as some borrowers struggle with higher monthly payments. After the initial spike, delinquencies decline even though rates stay high. This points to credit burnout, as weaker borrowers are impacted early and the remaining pool performs more steadily afterward.

**Exhibit 66: Payment shock for Non-QM ARM Cohorts**

Source: LSEG Yield Book, Cotality

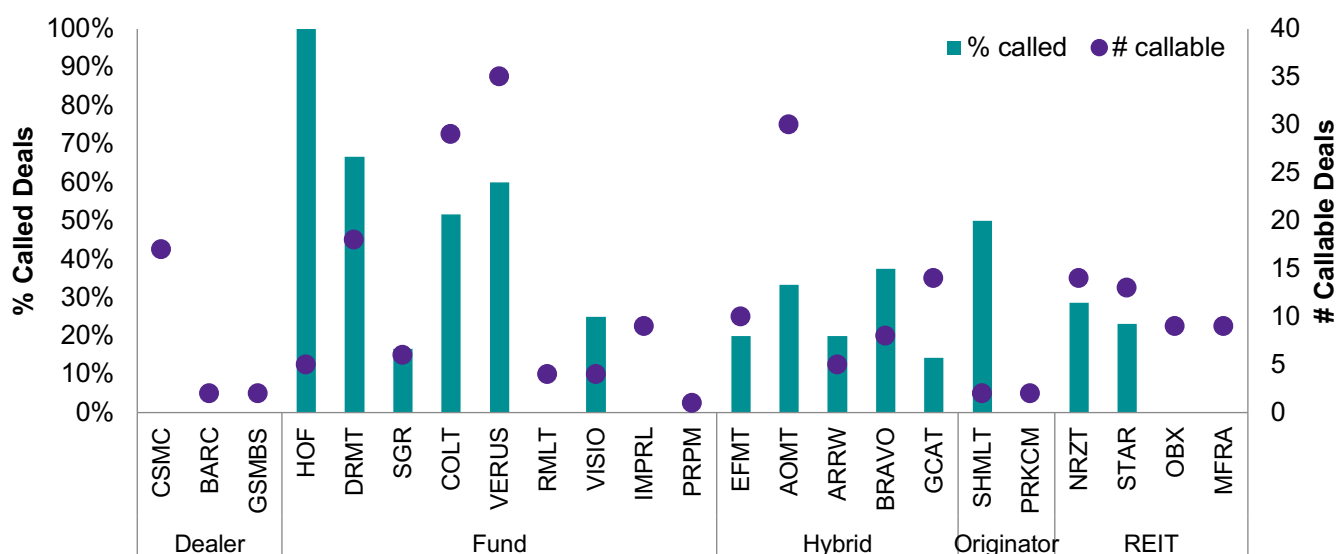
## Deal call Activity

There is a historical relationship between the percentage of call options triggered from all callable deals each year and the average difference between the cost of funds in the deal compared to re-securitising the assets. 2021 was the year with the lowest primary market rates on the Non-QM bonds while the cost of funds in the securitization was much higher, triggering very high activity in executing the call options. By contrast, in 2023 and 2024 the cost of funds of the seasoned deals was lower than the cost of funds in new securitizations, which decreased the rate of calling to nearly 0%. Subsequently in 2025 we have seen slight increase in call activity, driven mainly by securitizations originated in the higher interest rate regime.

**Exhibit 67: Correlation between call rates and cost of funds in the deal compared to issuing a new deal**

Source: LSEG Yield Book

We can also observe differences in call activity across issuer types of Sponsors such as alternative asset managers or private credit funds have traditionally called deals more frequently, regardless of the incentive to call, while permanent capital vehicles such as REITs have exhibited lower call activity. The exhibits below show differences between issuer groups in both lower and higher interest rate regime environments.

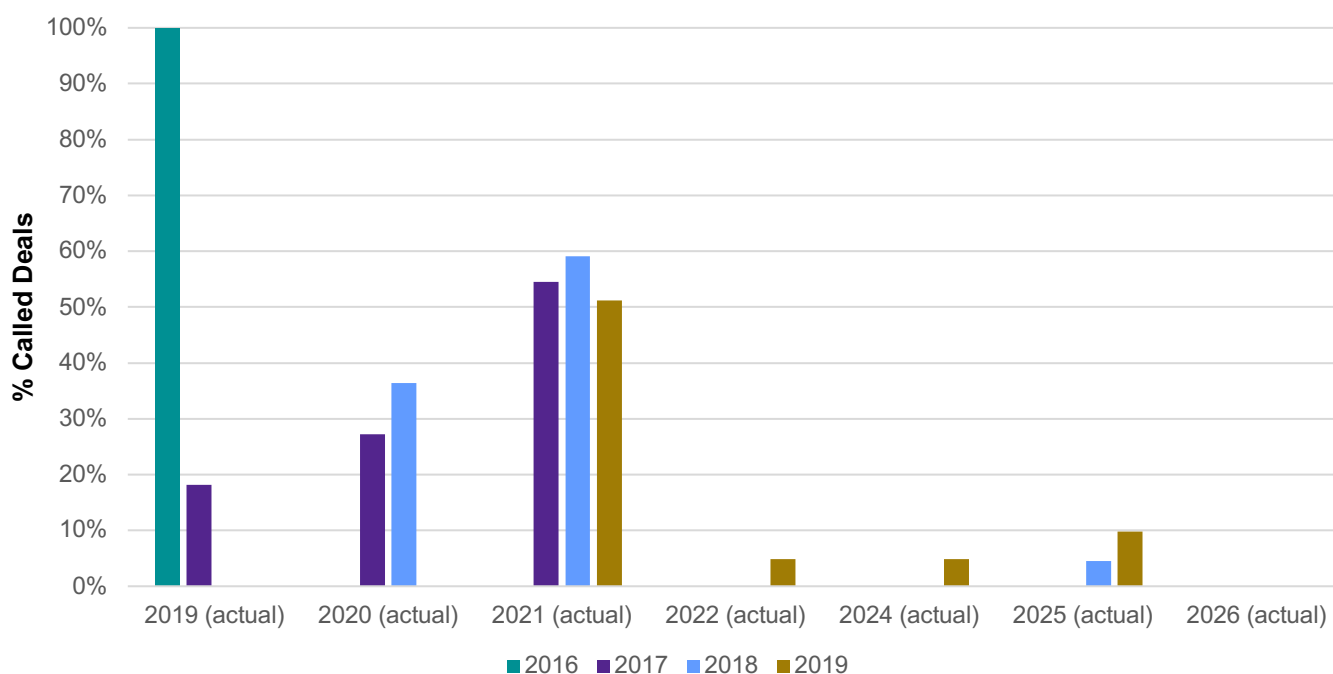
**Exhibit 68: Call rates by sponsor for originations before H2 2022**

Source: LSEG Yield Book

**Exhibit 69: Call rates by sponsor for originations after H2 2022**

Source: LSEG Yield Book

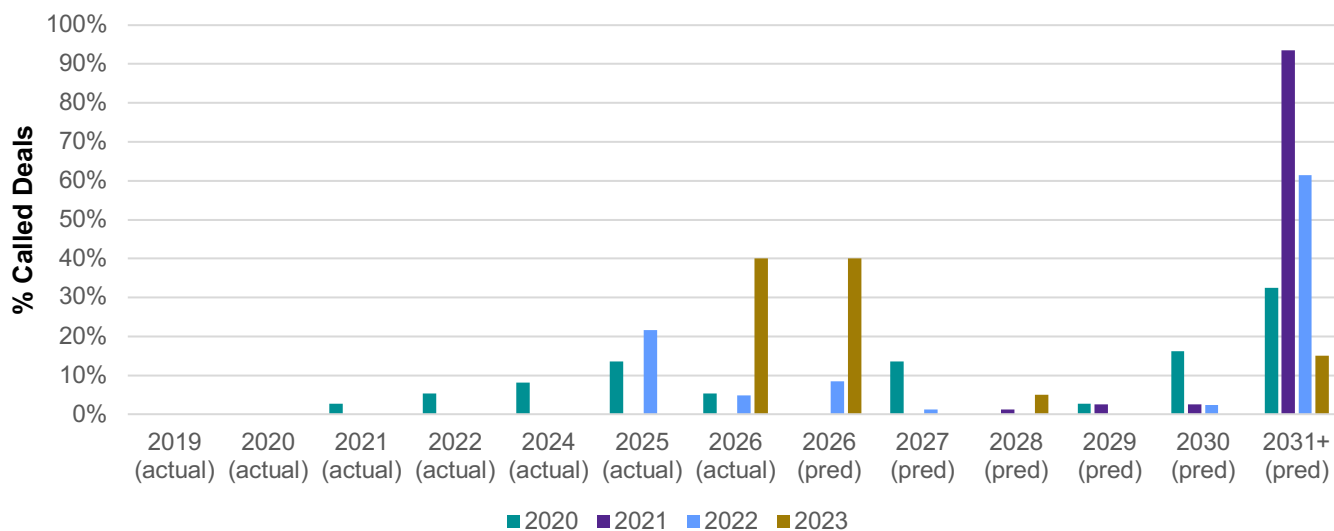
For vintages originated during the low and declining interest rate environment, most RMBS securitizations were called at or shortly after their optional redemption date, reflecting the strong economic incentive created by the embedded step-up and lower refinancing costs.

**Exhibit 70: Actual call rates for Non-QM deals originated 2016-2019**

Source: LSEG Yield Book

In Exhibit 71 below, many securitizations originated during the low-rate environment of 2020-2022 have remained uncalled. Our call model indicates the incentive to call that is low, pushing the expected call date beyond 2030 for many deals, especially for the 2021 cohort, which were originated with very low coupons.

**Exhibit 71: Actual and predicted call rates for Non-QM deals originated 2020-2023**



Source: LSEG Yield Book

## Section 7 – CMBS Outlook

### Record paced issuance but high rates continue to pressure maturities

#### Agency CMBS

##### 1H 2026 Recap

1H 2026 saw outperformance of agency CMBS against a volatile macro backdrop. The Iran war and escalating geopolitical tensions pushed oil prices higher and reignited inflation concerns, weighing on risk assets and fixed income markets. Yet agency CMBS market was largely insulated from these pressures. Issuance kept strong momentum across all three agency programs, spreads tightened following a brief episode of volatility in March and April, and credit performance generally improved as multifamily vacancy and rent stabilized. Meanwhile, prepayment activity remained subdued as strong call protection and limited refinancing incentives continued to constrain loan turnovers.

This divergence reflects several structural factors unique to the sector. First, agency CMBS is driven more by policy-supported lending and refinancing demand than by cyclical investment flows, limiting its sensitivity to broader risk-off sentiment. Second, the agencies continue to serve as a critical liquidity backstop for multifamily housing at a time when many traditional lenders remain cautious, supporting both origination and securitization activity. Third, the sector benefits from a combination of high credit quality, stable cash flows, and strong investor demand for agency-backed products, which helped keep spreads well anchored even as other fixed-income sectors experienced greater volatility. As a result, agency CMBS has continued to exhibit characteristics of a defensive, liquidity-driven segment of the structured credit market, with performance increasingly decoupled from the broader macroeconomic uncertainty that dominated the first half of 2026.

##### Key Drivers for 2H 2026

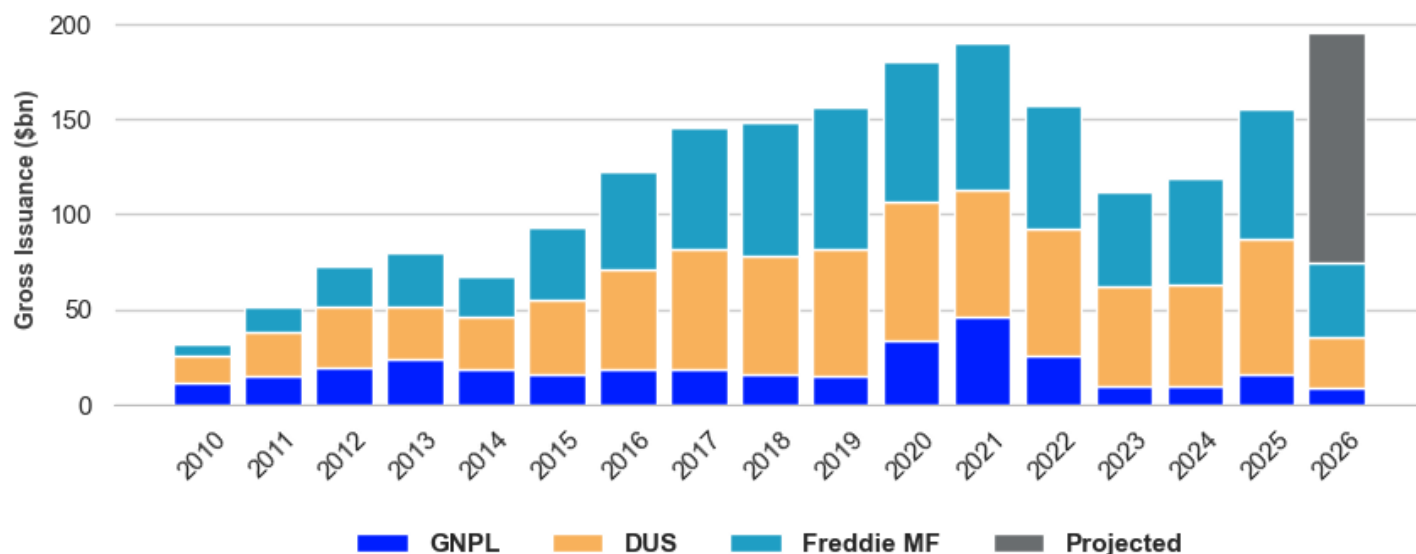
A key uncertainty for 2H 2026 is the path of Federal Reserve policy. While inflation has moderated, persistent price pressures and a resilient labor market could prompt the Fed to maintain a restrictive stance or even start rate hikes. Such an outcome would likely drive Treasury yields higher, increase rate volatility, and tighten financial conditions. For agency CMBS, higher rates could weigh on refinancing activity, borrowing demand, and spread performance, although the sector should remain relatively resilient given its policy-driven lending framework and agency support.

While markets generally anticipate stable or lower rates over time, the risk of additional tightening remains. If inflation reaccelerates during the second half of the year, the Fed could be forced to raise rates further, creating headwinds for fixed-income markets and risk assets. Although agency CMBS may be less directly affected than other credit sectors, a prolonged higher-rate environment could indirectly pressure performance through weaker credit fundamentals, slower originations, and greater spread volatility. Geopolitical uncertainties around the ceasefire deal poses as a secondary risk, primarily to the extent that they contribute to inflationary pressures and reinforce a more hawkish Fed stance.

##### Issuance

Agency CMBS issuance had a strong first half of 2026 despite heightened geopolitical uncertainty and inflation concerns. Total issuance reached \$71.4 billion, up 34.0% year-over-year, with all three agency programs running ahead of last year's pace. GNPL issuance increased 49.2% to \$8.3 billion, while Fannie Mae DUS and Freddie Mac Multifamily issuance rose 17.8% and 44.8% to \$26.2 billion and \$36.8 billion, respectively. The strong production underscores the sector's resilience and the continued importance of agency financing as a reliable source of liquidity for multifamily and healthcare borrowers.

The robust first-half performance puts agency CMBS on track for another strong year after total issuance reached \$155.5 billion in 2025. Under our base case, issuance is on track to reach approximately \$170 billion in 2026, supported by refinancing demand, agency liquidity, and continued lender discipline. On the other hand, persistent inflationary pressure and potential rate hikes could reduce issuance to approximately \$130 billion in the stress scenario.

**Exhibit 72: Agency CMBS Gross Loan Issuance by Year**

Source: GNMA, FNMA, FLHMC, LSEG Yield Book (June 2026)

**Market Spreads**

Agency CMBS spreads remained resilient through the first half of 2026 despite heightened geopolitical tensions and renewed inflation concerns. After tightening steadily through late 2025, senior K-Series and DUS spreads experienced only modest widening during the March-April volatility episode and subsequently retraced most of the move by May. In contrast, agency RMBS spreads reacted much more sharply, with FNMA 30-year current-coupon Z-spreads widening from 99 bps in January to 121 bps in March before recovering. The divergence suggests investors viewed agency CMBS as relatively insulated from the macro uncertainty and rate volatility that affected other fixed-income sectors.

Looking ahead, we expect agency CMBS spreads to stay broadly range-bound with a modest tightening bias in our base case scenario, supported by stable credit performance and continued investor demand. However, if the stress scenario materializes due to run-away inflation, we may see 15-35 bps of spread widening.

**Exhibit 73: Market Spreads for DUS, K and FNMA RMBS CC bonds**

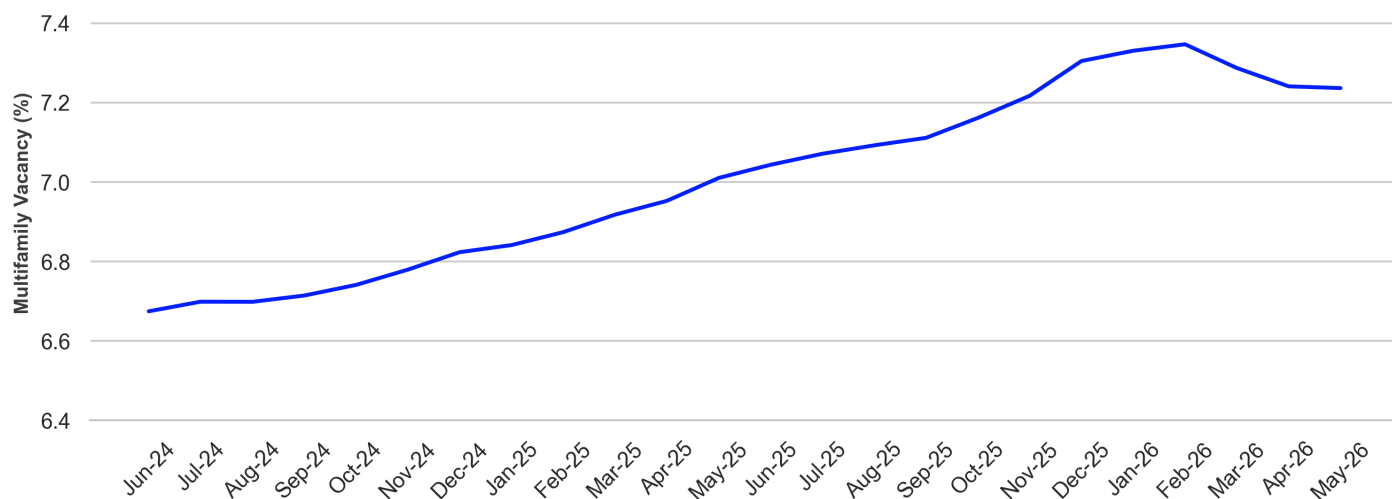
| Agency | Bond         | Jun 25 | Jul 25 | Aug 25 | Sep 25 | Oct 25 | Nov 25 | Dec 25 | Jan 26 | Feb 26 | Mar 26 | Apr 26 | May 26 |
|--------|--------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| FHLMC  | K - A1       | 48     | 48     | 48     | 44     | 45     | 46     | 46     | 36     | 37     | 38     | 37     | 37     |
| FHLMC  | K - A2       | 42     | 40     | 40     | 37     | 38     | 40     | 38     | 31     | 32     | 34     | 31     | 30     |
| FHLMC  | K - AM       | 46     | 44     | 45     | 41     | 42     | 44     | 44     | 33     | 35     | 39     | 35     | 34     |
| FHLMC  | K - AS       | 60     | 60     | 58     | 58     | 58     | 61     | 60     | 56     | 54     | 58     | 56     | 57     |
| FNMA   | DUS - 10/9.5 | 47     | 48     | 46     | 44     | 49     | 49     | 46     | 37     | 36     | 38     | 35     | 33     |
| FNMA   | DUS - SARM   | 62     | 58     | 57     | 58     | 58     | 61     | 61     | 56     | 55     | 59     | 60     | 60     |
| FNMA   | 30Yr - CC    | 139    | 132    | 123    | 124    | 123    | 121    | 105    | 99     | 108    | 121    | 108    | 103    |

Source: CMA, LSEG Yield Book (June 2026)

## Multifamily Fundamentals

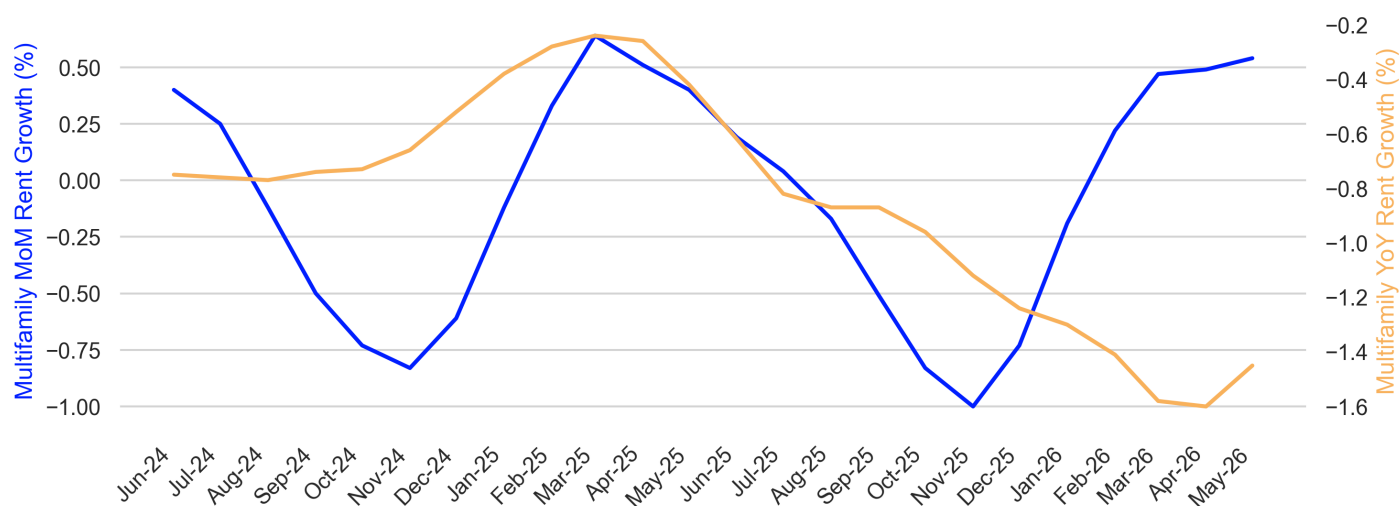
Multifamily fundamentals showed early signs of stabilization during the first half of 2026 after several years of supply-driven pressure. Vacancy rates continued to rise into early 2026, reaching a peak of approximately 7.4% in February, before declining modestly in subsequent months as new deliveries slowed and absorption improved. Rent conditions remained challenging, with annual rent growth staying negative throughout the period. However, monthly rent growth rebounded sharply from late-2025 lows and turned positive during the spring, suggesting that the market may be approaching an inflection point as supply-demand imbalances gradually ease.

### Exhibit 74: Multifamily Vacancy Rate



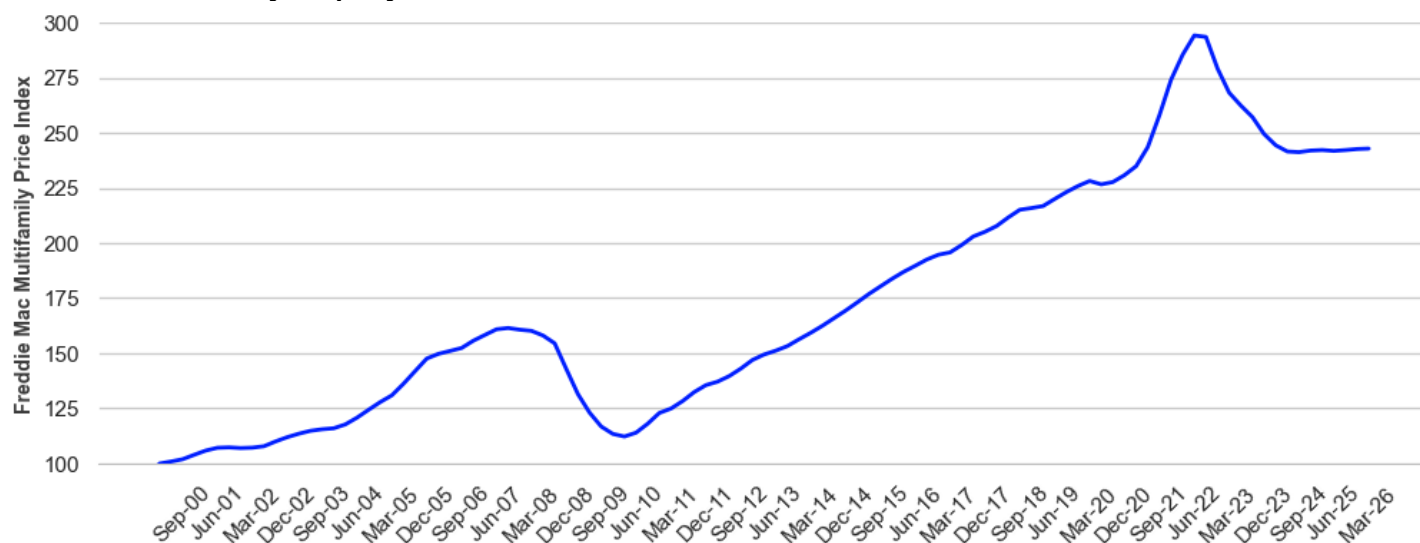
Source: Apartment List, LSEG Yield Book (June 2026)

### Exhibit 75: Multifamily Rent Growth Rate



Source: Apartment List, LSEG Yield Book (June 2026)

Property valuations have been steady in 2026. After recovering from the 2022-2023 downturn, multifamily prices have largely moved sideways over the past year, reflecting a balance between higher financing costs and improving expectations for future fundamentals.

**Exhibit 76: Multifamily Property Price Index**

Source: FHLMC, LSEG Yield Book (June 2026)

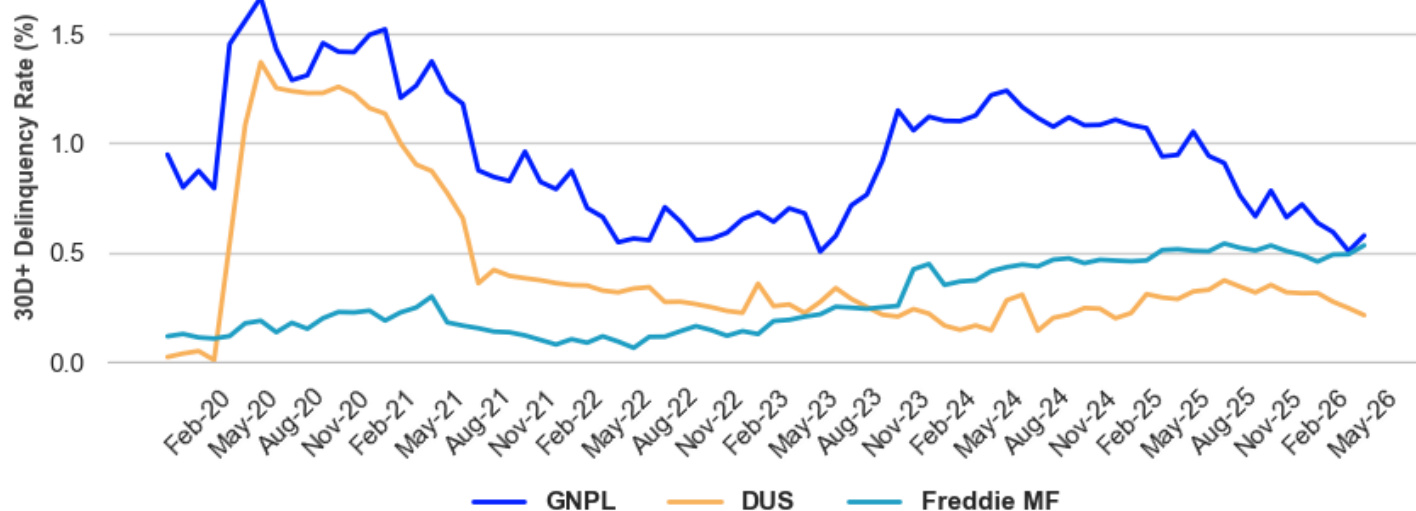
For 2H 2026, under our base case, vacancy rates would gradually decline from recent highs, rent growth may turn modestly positive, and property values may improve modestly as new supply moderates. The stress scenario envisions Fed tightening to rein inflation, leading to higher vacancy, weaker rent growth, and renewed pressure on property valuations.

**Credit Performance**

Credit performance remained positive through the first half of 2026 despite elevated vacancy rates and negative rent growth.

- GNPL delinquency declined from 0.72% in January to 0.56% in May, driven primarily by continued improvement in the nursing home sector, where delinquency fell from 1.22% to 0.87% amid strong demand for senior housing and long-term demographic tailwinds from an aging population. In contrast, GNPL residential multifamily performance was more mixed, with delinquency fluctuating during the period and ending at 0.48% in May.
- Fannie Mae DUS continued to exhibit the strongest credit performance among the agency programs, with delinquency declining to approximately 0.22%.
- Freddie Mac Multifamily delinquency was largely stable near 0.5%, though with dispersion across lending programs. The core K-Series book had steady delinquency rate around 0.35%, reflecting the strong credit quality of the underlying assets. However, deterioration continued in SB loans, where delinquency rose above 4.5%, while multi-PC loans also experienced a gradual increase in delinquency rates from very low levels at the beginning of year.

Entering 2H 2026, our base case assumes steady delinquency rates through year-end, with GNPL in the 0.6-0.8% range, DUS near 0.20-0.30%, and Freddie MF around 0.50-0.55%, while the stress scenario could push delinquencies of GNPL, DUS, and Freddie MF toward 1.0%, 0.40-0.55%, and 0.60%, respectively.

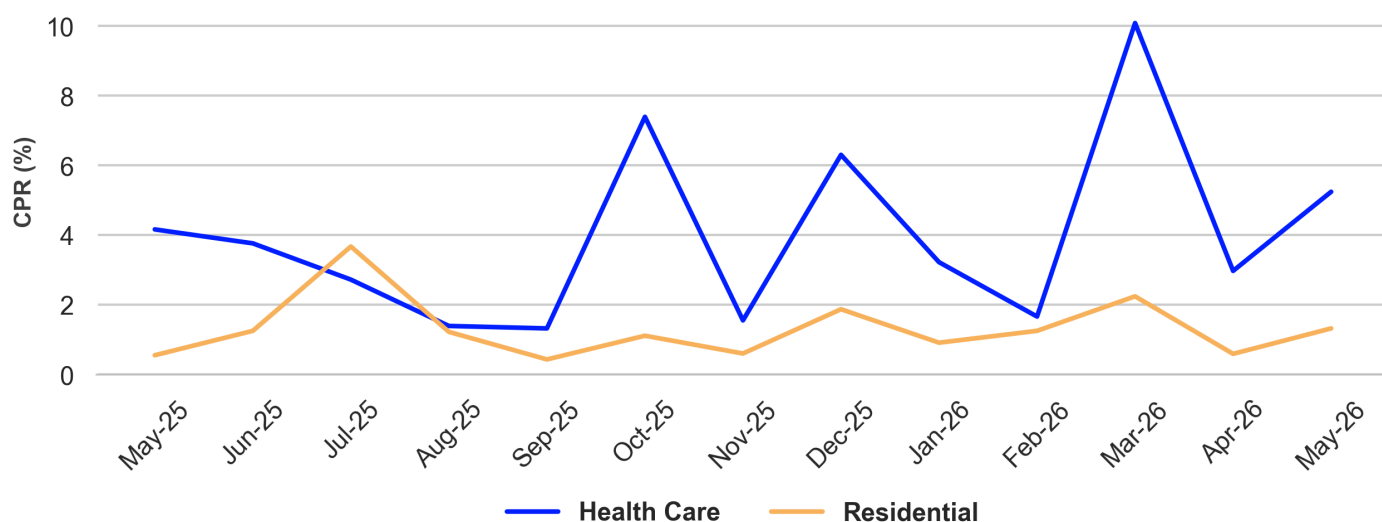
**Exhibit 77: Agency CMBS 30D+ Delinquency Rates**

Source: GNMA, FNMA, FHLMC, LSEG Yield Book (June 2026)

### Prepayments

Agency CMBS prepayment activity was generally subdued through 1H 2026 despite strong issuance and improving credit performance, as refinancing incentives stayed constrained amid still-elevated borrowing costs, stable property valuations, and robust call protection across most agency loan programs.

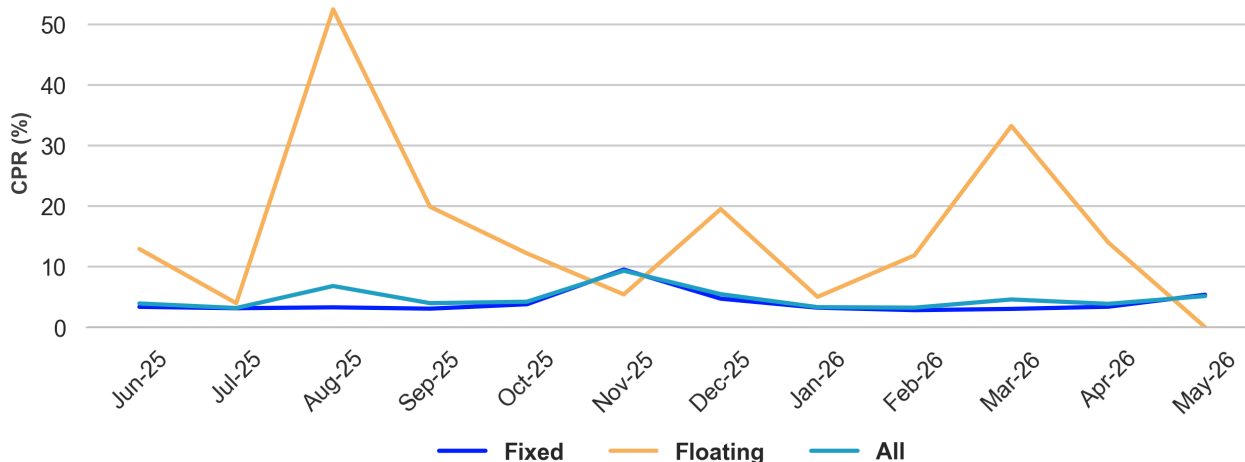
Prepayment activity for GNPL was muted overall during the first half of 2026, reflecting limited refinancing incentives for the fixed-rate collaterals. Residential multifamily CPRs generally remained in the 1–2% range, while healthcare loans exhibited greater volatility, with occasional spikes driven by operator transitions and industry consolidation. Looking ahead, we expect GNPL prepayments to remain tempered, although healthcare collateral will likely continue to experience episodic refinancing waves that create temporary CPR spikes.

**Exhibit 78: GNPL Actual Prepay Speeds By Property Type**

Source: GNMA, LSEG Yield Book (June 2026)

For Fannie Mae DUS, prepayment behavior continued to diverge sharply between fixed- and floating-rate loans. Fixed-rate loans, which account for more than 95% of outstanding balances, maintained stable prepayment speeds in the 3–5 CPR range due to strong yield-maintenance provisions. In contrast, floating-rate loans experienced significantly higher and more volatile CPRs, with speeds fluctuating widely as borrowers responded to cap expirations, refinancing opportunities, and business plan completions. Given the dominance of fixed-rate collateral, we expect aggregate DUS prepayment speeds to stay modest through year-end, with most variability driven by the relatively small floater segment.

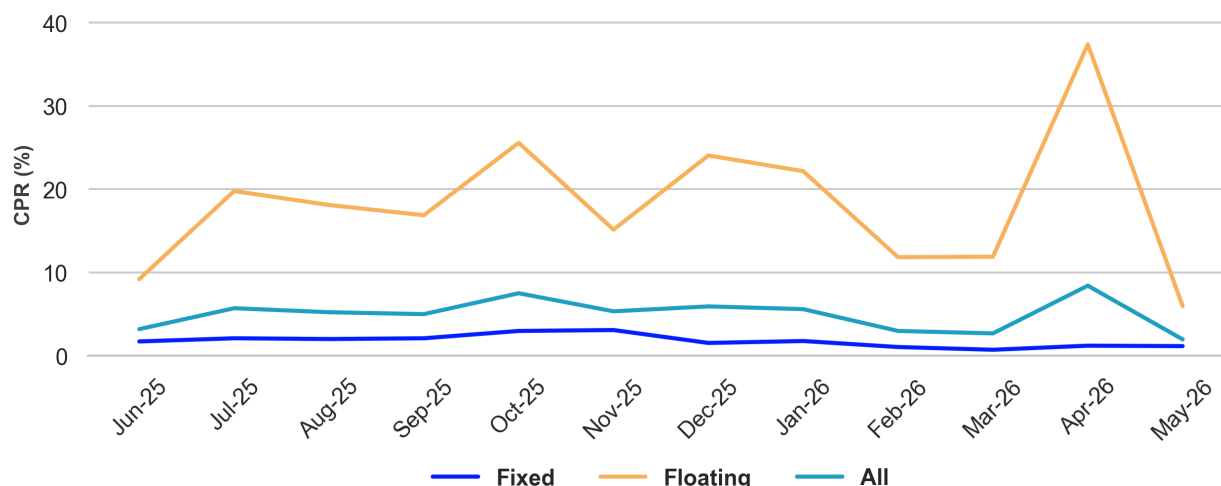
**Exhibit 79: DUS Actual Prepay Speeds by Coupon Type**



Source: FNMA, LSEG Yield Book (June 2026)

A similar pattern was observed for Freddie Mac Multifamily. Fixed-rate K-loans continued to prepay slowly, generally in the 1–3 CPR range, reflecting strong call protection. Floating-rate loans prepaid at substantially higher speeds, causing volatility in overall CPRs. Since floating-rate loans represent a larger share (14%) of the Freddie Mac portfolio than in DUS, aggregate Freddie prepayment speeds were somewhat more volatile. For 2H 2026, we expect fixed-rate collateral to remain firmly anchored at low CPR levels, while floating-rate prepayments continue to fluctuate with financing conditions and borrower execution strategies.

**Exhibit 80: Freddie K Actual Prepay Speeds by Coupon Type**



Source: FHLMC, LSEG Yield Book (June 2026)

## Non-Agency CMBS

### Summary of 1H2026

The year 2026 started with continued momentum in CMBS markets, broadly in line with expectations set at the end of 2025. SASB issuance remained healthy, while conduit issuance softened amid market volatility. CRE CLO issuance surged in the first half of the year, driven by investor demand and market liquidity for transitional multifamily financing. Spreads stayed range-bound despite macro volatility and geopolitical concerns. Property fundamentals were mostly steady, as signs of stabilization emerged in office sector.

However, the inflation backdrop became more challenging in the first half of 2026 as the Iran war triggered an energy-price shock and renewed concern that inflation could remain above the Fed's target for longer. While oil prices have retreated post ceasefire deal, the impact from the conflict will linger and pressure the inflation outlook. This keeps investors cautious despite continued liquidity in capital markets.

More importantly, the interest-rate path has become less supportive of CRE during 1H2026. As treasury yields stay elevated and Fed pivots to tightening to rein inflation, it would keep borrowing costs high and limit takeout proceeds, aggravating the refinancing risk for maturing loans.

### Issuance

1H2026 non-agency CMBS issuance totaled \$96.1 billion, nearly 20% higher than 1H2025. The growth was driven by SASB issuance, which totaled \$56.0 billion and represented 58.2% of private-label CMBS issuance, and CRE CLO issuance which surged to \$25.1 billion, up 45.1% from the same period last year. Conduit issuance came in weak, totaling \$14.9 billion, or 15.5% of the market. If the pace continues in 2H2026, we expect 2026 non-agency CMBS issuance to exceed 2025 volume and set a new post-GFC annual record.

We expect SASB deal flows to remain robust in 2H2026, although the pace may moderate from the very strong first half. We would keep our 2026 full year issuance forecast unchanged at \$110 billion for SASB, as refinancing needs and borrower demand continue to support transaction volume. For CRE CLO, we would raise our 2026 full year issuance forecast from \$35 billion to \$55 billion, as more alternative lenders have tapped the securitization market for leverage and issuance activity has rebounded meaningfully from 2025 levels. On the other hand, we would lower the forecast for conduit issuance from \$35 billion to \$30 billion, as conduit loan availability remains constrained. Borrower preference has shifted toward shorter-duration executions after benchmark rates rose, with more than three-quarters of conduit issuance being five-year deals, up from roughly 70% during the same period last year.

In total, our updated projection for 2026 full year non-agency CMBS issuance grows to \$195 billion, compared to \$163.5 billion in 2025 and our original projection of \$180 billion for 2026.

We saw office exposure rose slightly to 27.3% in SASB deals so far this year, compared with 26.1% in 1H2025. In conduit deals, office exposure continued to grow steadily to 17.2% from 16.4%, while multifamily exposure declined to 21.2% from 23.8%. On the other hand, CMBS loan leverage appears to be on the rise this year, with LTVs up across all three segments: 58.2% vs. 57.0% for conduit, 66.4% vs. 64.3% for SASB, and 67.3% vs. 65.7% for CRE CLO, suggesting a modest loosening in lender underwriting.

### Exhibit 81: Non-Agency CMBS Issuance Forecast

|                | 2025 FY (\$bn) | 1H 2026 (\$bn) | 2026 proj. (\$bn)<br>original | 2026 proj. (\$bn)<br>updated mid-year |
|----------------|----------------|----------------|-------------------------------|---------------------------------------|
| <b>Conduit</b> | 33.7           | 14.9           | 35                            | 30                                    |
| <b>SASB</b>    | 99.2           | 56.0           | 110                           | 110                                   |
| <b>CRE CLO</b> | 30.6           | 25.1           | 35                            | 55                                    |
| <b>Total</b>   | 163.5          | 96.1           | 180                           | 195                                   |

Source: Trepp, LSEG Yield Book (June 2026)

## CRE Fundamentals

Despite continued maturity pressure, CMBS credit performance was broadly stable in 1H2026, as the 30+ day delinquency rate of conduit and SASB loans increased only by 5 bps to 6.66% from 6.61% at YE2025. With elevated maturity default risk and slow pace of resolution of distressed loans, we think delinquency rate remains on track to reach the 7% level by YE2026, consistent with our earlier forecast.

Office remains the weakest sector among conduit and SASB collaterals, but the sector has shown early signs of stabilization. The office delinquency rate increased only modestly to 10.43% in May 2026 from 10.36% in December 2025, despite continued refinancing challenges and maturity pressure. We are comfortable maintaining our YE2026 office delinquency rate projection at 11%, as the limited increase so far this year suggests that credit deterioration has been more contained than headline risks might imply.

We are also comfortable with our projections for most other property types. Multifamily delinquency increased modestly to 5.55% from 5.39%, while retail improved slightly to 6.39% from 6.54% and lodging declined to 5.25% from 5.73%, reflecting generally steady property fundamentals. Industrial delinquency rose to 1.11% from 0.72%, prompting us to adjust our YE2026 forecast to 1% from 0.5%; however, we view the increase more idiosyncratic risk driven instead of evidence of broad sector deterioration.

CRE CLO credit performance was significantly stronger than expected in 1H2026, with the 30+ day delinquency rate declining by 213 bps to 2.56% from 4.69% at YE2025. The improvement is consistent with booming CRE CLO issuance activity and better performance among transitional multifamily assets. As a result, we would reduce our YE2026 CRE CLO delinquency rate forecast to 3% from 4% originally.

### Exhibit 82: Non-Agency CMBS 30 day+ Delinquency Rate Forecast

|                                  |                | Dec 2025 | May 2026 | YE2026 proj. - original | YE2026 proj. - updated mid-year |
|----------------------------------|----------------|----------|----------|-------------------------|---------------------------------|
| <b>Conduit and SASB combined</b> | Industrial     | 0.72%    | 1.11%    | 0.5%                    | 1%                              |
|                                  | Lodging        | 5.73%    | 5.25%    | 6%                      | 6%                              |
|                                  | Multifamily    | 5.39%    | 5.55%    | 7%                      | 7%                              |
|                                  | Office         | 10.36%   | 10.43%   | 11%                     | 11%                             |
|                                  | Retail         | 6.54%    | 6.39%    | 7%                      | 7%                              |
|                                  | <b>Overall</b> | 6.61%    | 6.66%    | 7%                      | 7%                              |
| <b>CRE CLO</b>                   |                | 4.69%    | 2.56%    | 4%                      | 3%                              |

Source: Trepp, LSEG Yield Book (June 2026)

CMBS liquidation speed in 2026 has been below our expectation, with YTD monthly average disposition volume at \$265 mm, compared to the 2025 level of \$325 mm. Meanwhile, loss severity from dispositions rose to 66% in 2026 YTD from 60% in 2025. Loss severity may remain elevated in 2H2026 as liquidations continue to be concentrated on the most troubled loans that have experienced severe cashflow deterioration and valuation impairment.

We have been projecting more sales transactions and speedier resolutions for distressed properties in 2026, but it looks like the progress of property/loan liquidation may still take more time as buyers and sellers try to close gap in clearing levels in face of elevated cap rates. Hence, we are expecting a delayed property value recovery in general even though CRE prices have mostly stabilized in the last few quarters.

### Exhibit 83: Non-Agency CMBS Loan Disposition

|                                       | 2025 | 2026 YTD |
|---------------------------------------|------|----------|
| Monthly Avg Disposition Volume (\$mm) | 325  | 265      |
| Avg Loss Severity                     | 60%  | 66%      |

Source: Trepp, LSEG Yield Book (June 2026)

## Maturity Performance

Maturity performance of conduit CMBS loans weakened in 1H2026, while SASB and CRE CLO performed better as capital availability shifted toward large single-asset transactions and transitional lending. Conduit CMBS maturity payoff dropped to 55.4% in 2026 YTD from 69.7% in 2025, while maturity delinquency rose to 27.7% from 19.3% and extensions increased to 16.9% from 10.9%. The deterioration reflects continued refinancing friction and stymied conduit deal flow.

SASB and CRE CLO maturity performance improved overall. SASB payoff increased modestly to 13.6% from 10.6%, while CRE CLO payoff rose to 42.7% from 31.5%. We expect the trend to continue in 2H2026, as SASB and CRE CLO benefit from stronger issuance, better liquidity, and more refinancing options.

Office maturity performance diverged by deal type. Conduit office weakened significantly, with payoff dropping to 32.3% from 45.2% and delinquency rising to 44.0% from 37.9%, highlighting persistent refinancing challenges for smaller and weaker office loans. In contrast, SASB office payoff improved to 49.0% from 22.1%, suggesting that refinancing remains available for larger institutional-quality office assets with better sponsorship and cash flow.

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### Exhibit 84: Non-Agency CMBS Maturity Performance

| Deal Type/Year | 2025       |       |             | 2026 YTD   |       |             |
|----------------|------------|-------|-------------|------------|-------|-------------|
|                | paid off % | dlq % | extension % | paid off % | dlq % | extension % |
| Conduit        | 69.7%      | 19.3% | 10.9%       | 55.4%      | 27.7% | 16.9%       |
| Conduit Office | 45.2%      | 37.9% | 16.9%       | 32.3%      | 44.0% | 23.7%       |
| SASB           | 10.6%      | 3.3%  | 86.1%       | 13.6%      | 3.4%  | 83.0%       |
| SASB Office    | 22.1%      | 5.4%  | 72.5%       | 49.0%      | 27.5% | 23.5%       |
| CRE CLO        | 31.5%      | 7.8%  | 60.7%       | 42.7%      | 5.6%  | 51.7%       |

Source: Trepp, LSEG Yield Book (June 2026)

## Maturity Wall of 2H2026

Maturity refinancing is likely to remain a key pressure point in 2H2026, with \$41.8 billion of hard maturities coming due across conduit, SASB, and CRE CLO. Conduit has the largest and most granular maturity wall, with \$21.1 billion across 1,223 whole loans, followed by SASB at \$19.1 billion across 15 large loans and CRE CLO at \$1.6 billion. While most of the 2H2026 hard-maturity cohort is currently performing, the refinancing test could still be challenging given elevated rates, tighter debt proceeds, and continued valuation pressure.

For conduit, the 2H2026 maturity wall is concentrated in retail and office, which account for 31.1% and 26.6% of the maturing balance, respectively. This could keep conduit maturity performance under pressure, especially as conduit office payoff already weakened meaningfully in 1H2026. For SASB, lodging, office, and mixed-use make up nearly all of the 2H2026 hard-maturity balance. Although the performance of SASB cohort has held up in general, the low count of large loans means outcomes could be more idiosyncratic and sponsor/property specific. CRE CLO has a much smaller 2H2026 hard-maturity balance, and the maturity pressure could be relatively manageable as long as CRE CLO issuance and refinancing liquidity remain open.

**Exhibit 85: Non-Agency CMBS Conduit Maturity Wall by Property Type (2H2026)**

| Property Type | Balance (\$B) | Balance % |
|---------------|---------------|-----------|
| Retail        | 6.6           | 31.1%     |
| Office        | 5.6           | 26.6%     |
| Mixed Use     | 2.8           | 13.3%     |
| Lodging       | 2.7           | 12.7%     |
| Other         | 1.2           | 5.9       |
| Multifamily   | 1.1           | 5.4%      |
| Industrial    | 1.1           | 5.1%      |
| Total         | 21.1          | 100%      |

Source: Trepp, LSEG Yield Book (June 2026)

Elevated interest rates and potential rate hikes are pressing refinancing for 2H2026 CMBS maturities as many legacy fixed-rate conduit and fixed-rate SASB loans were originated at much lower rates and now need to refinance into a materially higher-rate market. To estimate refinancing stress, we use the coupon rates on recent new CMBS issuance (2Q2026) as a proxy for the coupon rates borrowers would face if they refinance today. We then recalculate each maturing loan's DSCR by assuming net operating income stays the same, but debt service rises in line with the higher refinancing rate. If the recalculated DSCR is above 1.20x, the loan is treated as refinaneable; if it falls below that threshold, the loan is considered at risk of failing to refinance (i.e., it may end up in default outright when DSCR is too low or in extension if special servicer deems there's still a chance for turnaround).

The coupon reset is significant as conduit maturing loans carry coupons mostly in the low-4% range, while current new-issuance coupons are in the low-to-mid-6% range. This higher debt-cost burden drives a sharp DSCR decline from 2.1x to 1.3x on average for 2H2026 maturities. Our calculation indicates 57.2% of conduit maturity balance with effective DSCR at or above 1.2x, 17.9% with DSCR between 1.0x and 1.2x, and 24.9% with DSCR falling below 1.0x, which is roughly in line with the 55.4% maturity payoff rate, 16.9% extension rate, and 27.7% delinquency rate we've observed YTD in 2026 for maturity conduit loans. Unless rates decline or property cash flows improve, elevated refinancing coupons are likely to keep maturity payoff rate contained in 2H2026.

**Exhibit 86: Non-Agency CMBS Conduit Loans Coupon Rate by Property Type**

| Property Type | WtAvg Coupon Rate% of 2Q2026 New Issuance | WtAvg Coupon Rate% of 2H2026 Maturities |
|---------------|-------------------------------------------|-----------------------------------------|
| Lodging       | 6.6                                       | 4.6                                     |
| Office        | 6.5                                       | 4.1                                     |
| Retail        | 6.6                                       | 4.2                                     |
| Multifamily   | 6.2                                       | 4.4                                     |
| Industrial    | 6.2                                       | 4.3                                     |

Source: Trepp, LSEG Yield Book (June 2026)

**Exhibit 87: Non-Agency CMBS Conduit Loans (2H2026 Maturity) Effective DSCRs Based on Current Market Rate**

| WtAvg Current DSCR | WtAvg Effective Refi DSCR | Effective DSCR $\geq 1.2x$ | Effective DSCR [1.0, 1.2) | Effective DSCR $< 1.0x$ |
|--------------------|---------------------------|----------------------------|---------------------------|-------------------------|
| 2.1x               | 1.3x                      | 57.2%                      | 17.9%                     | 24.9%                   |

Source: Trepp, LSEG Yield Book (June 2026)

**Spreads**

CMBS spreads remained resilient in 1H2026 despite middle-east conflicts and AI trade volatility, as improving risk sentiment and strong investor demand offset concerns around inflation, rates, and geopolitical uncertainty. Conduit LCF AAA spreads tightened modestly to 79 bps for 5-year deals and 77 bps for 10-year deals in June 2026, from 83 bps and 79 bps at YE2025, respectively. BBB- spreads also tightened to 443 bps from 452 bps, suggesting that investor appetite for lower-rated conduit classes improved.

We are comfortable keeping our YE2026 spread projections unchanged. Under our base scenario, we expect conduit AAA spreads to remain near current levels or compress slightly, reaching 80 bps for 5-year deals and 75 bps for 10-year deals. BBB- spreads could tighten further to around 400 bps if rate uncertainty recedes and investors continue to move down the credit stack for yield. However, we expect spreads to remain vulnerable to renewed macro volatility in 2H2026, especially if inflation pressure, elevated Treasury yields, or maturity refinancing stress persist. In a downside scenario, lower-rated conduit classes would likely come under pressure first, especially for deals exposed to weaker collaterals, while senior AAA spreads should remain better supported by strong liquidity and demand for high-quality bonds.

**Exhibit 88: Conduit CMBS New Issue Spreads Forecast**

| Period                  | LCF AAA spreads (bps) |             | BBB- spreads (bps) |
|-------------------------|-----------------------|-------------|--------------------|
|                         | 5-yr deals            | 10-yr deals |                    |
| Dec 2025                | 83                    | 79          | 452                |
| June 2026               | 79                    | 77          | 443                |
| YE2026 proj. (original) | 80                    | 75          | 400                |
| YE2026 proj. (updated)  | 80                    | 75          | 400                |

Source: Trepp, LSEG Yield Book (June 2026)

**Outlook**

Entering the second half of the year, the key question is whether the recent energy shock will prove temporary or whether it will keep inflation elevated for longer. While some initial price pressure has eased, the inflation outlook remains less predictable, raising the risk of Fed tightening.

Capital markets remain open, and securitization activity has generally held up despite macro volatility and geopolitical risk. However, liquidity alone will not solve the refinancing challenge, as elevated rates continue to weigh on borrowing costs and property valuation.

Despite these uncertainties, we remain cautiously constructive on the outlook for 2H2026 and beyond. Our baseline assumption is that rate hikes (if any) will be measured and economic growth will remain intact, allowing market liquidity to support continued CRE and CMBS activity. In conclusion, we are positive on CMBS prospects in 2026, but would caution on the risk of sticky inflation, Fed tightening, and persistent maturity refinancing pressure.

## Section 8 – CLO Outlook

### Holding up despite software and private credit stress

#### Market Overview

##### A resilient market facing multifaceted challenges

The CLO market entered mid-2026 strong but on an unsure footing. Issuance and refinancing/resets were active through bouts of macro volatility, supported by sustained investor demand, broadly stable credit fundamentals, and a functioning primary market. However, the tone became more defensive as sticky inflation, higher-for-longer rate expectations, and geopolitical uncertainty weighed on risk appetite. Liability tranches, particularly senior notes, remained well supported, while lower rated notes and equity were more sensitive to shifts in macro sentiment and credit dispersion.

Key market developments in 1H26 include the software selloff and private credit concern, driven by AI disruption fear and vulnerable business-models/worse liquidity/elevated leverage. While near-term fundamentals remain generally intact as defaults stay idiosyncratic for now, future refinancing risk is looming with heavy debts set to mature starting 2028. On the leveraged loan side, new loan supply remained limited and new loan spreads touched multi-year lows despite broader market volatility, pressuring CLO deal economics and softening equity returns.

Against this backdrop, CLO performance in 2H26 will rely more heavily on collateral selection, software exposure management, par preservation, and managers' ability to mitigate tail risk.

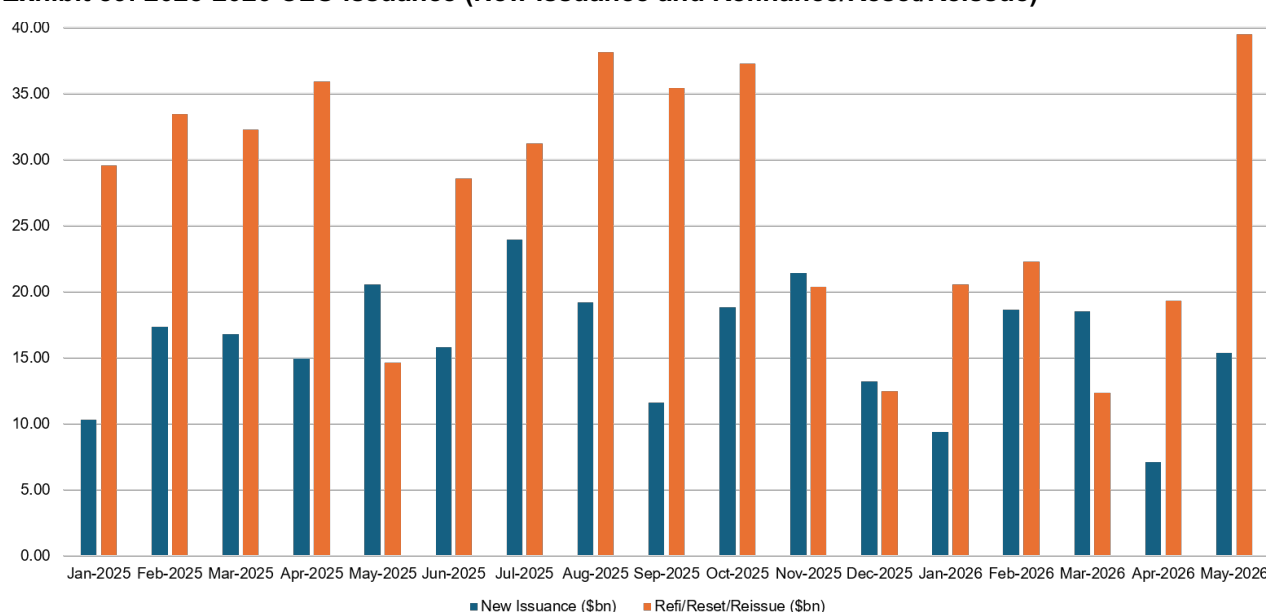
#### Issuance, Spreads, and Refi/Reset

##### New issuance down modestly from 2025 and 2H2026 volume may also be contained due to tight arbitrage

Through May, total US CLO new issuance YTD reached \$68.50bn, down 14% YoY from \$79.97bn in 2025. The decline was driven primarily by weaker BSL volume, which fell 16% YoY to \$54.07bn, while PC CLO issuance edged up 3% YoY to \$13.94bn. Static issuance was muted at \$0.50bn, down from \$2.39bn in YTD 2025.

Refinancing and reset activities also underperformed the exceptional pace set in 2025. Total US CLO refi/reset/reissue volume through May was \$113.95bn, down 21% YoY, with the shortfall driven by resets which fell 37% YoY to \$62.51bn. Refinancing rose 12% YoY to \$50.99bn as managers continued to capture available liability savings amid tighter spreads. Looking into 2H2026, activity should remain supported for deals with significant spread savings and clean credit profiles, but volumes are likely to stay more measured than 2025 given constrained arbitrage, software-related par concerns, and the risk of renewed spread volatility.

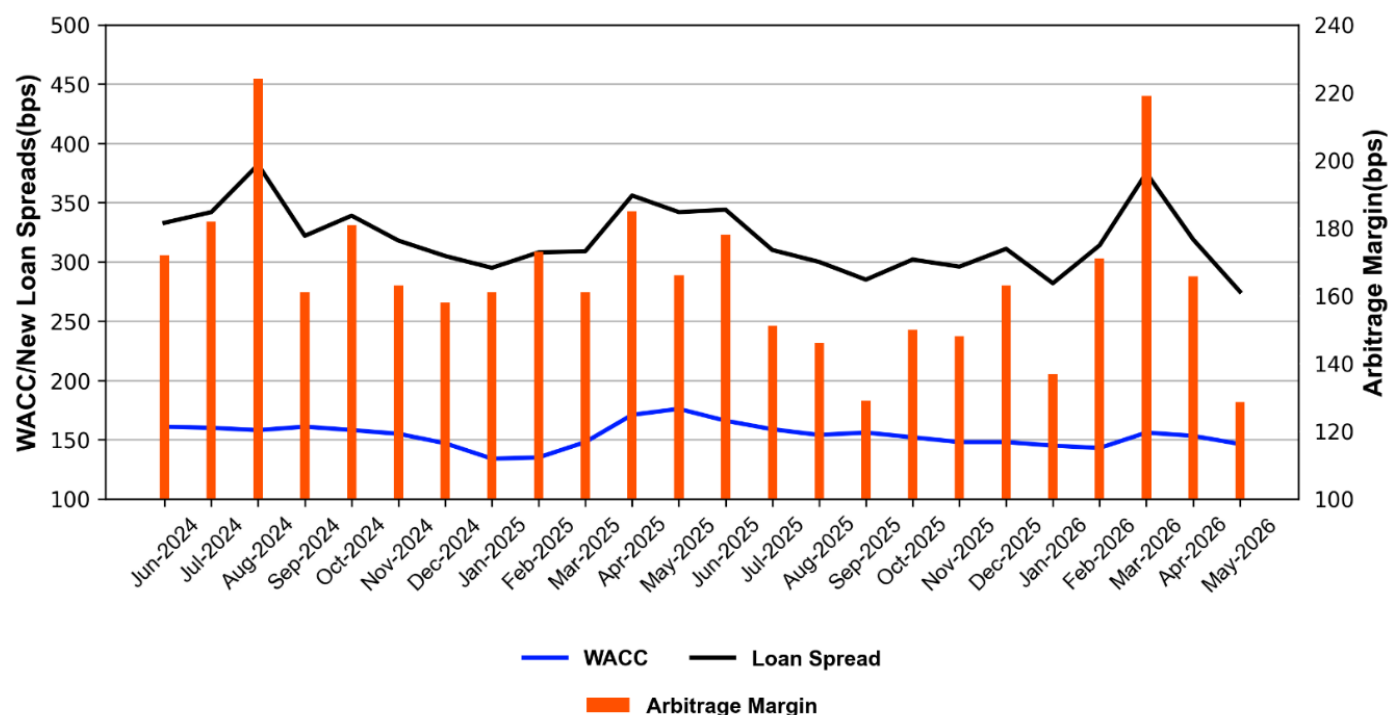
**Exhibit 89: 2025-2026 CLO issuance (New Issuance and Refinance/Reset/Reissue)**



Source: Green Street, Yield Book (June 2026)

CLO arbitrage was volatile through 1H2026, tightening to 137bps in January followed by a surge to 219bps in March and a slump back to 129bps by May, driven by new loan supply constraints, repricing activities, and liability spread volatilities.

**Exhibit 90: CLO WACC, new loan spreads and CLO arbitrage margin (new issues)**



Source: Green Street, LSEG LPC, Yield Book (June 2026)

Given the volatile market backdrop and tight arbitrage conditions, we are lowering our 2026 BSL CLO new issuance forecast to \$136bn, down from our \$154bn projection at the beginning of the year. The revision reflects limited new loan supply, tighter asset spreads, and episodic liability-spread volatility, all of which have made new-issue economics more challenging. While the CLO primary market has remained open, issuance has become more dependent on favorable market windows, with managers facing greater difficulty sourcing collateral at attractive spreads amid continued loan repricing activity and limited new-money formation.

We maintain our Private Credit CLO issuance forecast at \$36bn, broadly in line with our beginning-of-year expectation, as the sector has shown relative stability despite continued scrutiny around private credit fundamentals, software exposure, and fund-level liquidity pressure.

In total, we now project \$172bn of 2026 CLO new issuance, approximately 16% below the 2025 level of \$203bn. Looking into 2H26, sustained deal flow will likely depend on either a meaningful pickup in new-money loan supply that supports wider asset spreads, or further liability tightening sufficient to offset asset-spread compression.

**Exhibit 91: 2026 CLO New Issuance Forecast**

| Year                           | BSL (\$bn) | Private Credit (\$bn) | Total New Issue (\$bn) | Refinance/Reset/Reissue (\$bn) |
|--------------------------------|------------|-----------------------|------------------------|--------------------------------|
| Full Year 2025                 | 161        | 35                    | 203                    | 289                            |
| YTD through May                | 54         | 14                    | 68                     | 114                            |
| Original Proj. for 2026        | 154        | 38                    | 192                    | 338                            |
| Midyear Updated Proj. for 2026 | 136        | 36                    | 172                    | 267                            |

Source: Yield Book, Green Street (June 2026)

### Refi/resets forecast also revised down with resets under pressure from portfolio cleanup

CLO refinancing volume reached \$51bn through May, 12% above the YTD 2025 level, as managers continued to capture liability-cost savings amid a generally constructive tightening trend in senior and mezzanine spreads. On the other hand, reset activities slumped 37% to \$63bn from \$99bn over the same period last year, reflecting the difficulty managers faced in cleaning up portfolios and preserving par amid continued software weakness.

Based on current spread levels, we estimate \$121bn of deals that exited non-call by YE2026 are in the money for refinancing, defined as deals with AAA spreads of 133bps or wider, or 10bps above the current new-issue AAA level. We also estimate \$42bn of deals are prime reset candidates, defined as deals with WACC of 156bps or higher, or 10bps above the current new-issue WACC level. However, with software loans still trading at deep discounts, reset execution remains more constrained than refinancing. As a result, we subtract \$10bn from the projected reset opportunity, bringing the adjusted reset candidate pool to \$32bn and total projected full year 2026 refinance/reset/reissue volume to \$267bn.

### Liability spreads may tighten in 2H2026 on lower supply and sustained demand

Strong CLO demand, healthy collateral fundamentals, and still-low default rates kept liability spreads well supported through 1H2026 despite intermittent market volatility. BSL AAA spreads were basically unchanged at 123bps in June 2026 (vs. 124bps at YE2025), underscoring persistent demand for senior CLO paper. While we initially expected modest widening to 128bps by YE2026, the resilience of senior demand amid lower supply and a stable credit backdrop support a tighter forecast of 125bps.

Lower-rated tranches were more sensitive to volatility around software loans, macro uncertainty, and collateral dispersion, but spread performance has also been firm with BSL BB spreads largely unchanged in 1H2026 (536bps in June vs. 535bps at YE2025). Given continued investor demand for CLO carry and the absence of broad-based credit deterioration, we now expect BB spreads to tighten modestly to 525bps by YE2026.

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### Exhibit 92: 2026 CLO New Issue Spreads Forecast

| Year                             | BSL AAA spread (bps) | BSL BB spread (bps) |
|----------------------------------|----------------------|---------------------|
| YE2025                           | 124                  | 535                 |
| June 2026                        | 123                  | 536                 |
| Original Proj. for YE2026        | 128                  | 550                 |
| Midyear Updated Proj. for YE2026 | 125                  | 525                 |

Source: LSEG Yield Book, Green Street (June 2026)

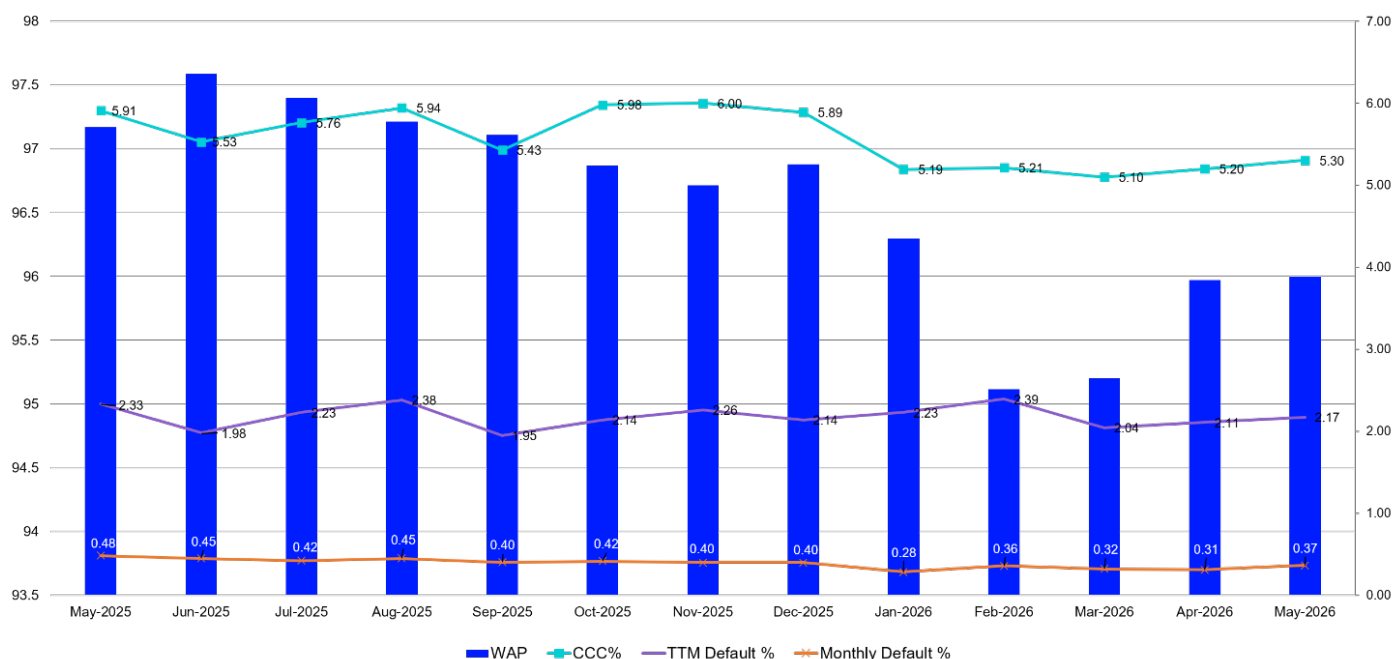
## Credit Fundamentals

### Overall stable but increasingly dispersed credit fundamentals highlighted by software distress

Credit fundamentals remained broadly stable through 1H26, though dispersion increased as macro volatility and sector-specific weakness widened the gap between stronger and weaker borrowers. CLO collateral metrics generally held up with low default rates, limited Caa/CCC exposure, and robust loan-market technicals. Reinvesting deals continued to show solid junior OC cushions with contained downgrade and default risk. This helped keep CLO performance stable despite volatility in liability spreads and loan prices.

CLO collateral Weighted Average Price (WAP) declined from 96.88 at YE2025 to 95.45 in February on software selloff, before recovering and stabilizing at 96.00 in May.

CCC exposure improved from 5.89% at YE2025 to 5.30% in May 2026. Default metrics were also steady: the trailing 12-month default rate only edged up from 2.14% at YE2025 to 2.17% by May 2026, while monthly defaults ticked down from 0.40% at YE2025 to 0.37% in May 2026.

**Exhibit 93: Key credit metrics remained stable in the last 12 months**

Source: LSEG LPC, Trepp, Yield Book (June 2026)

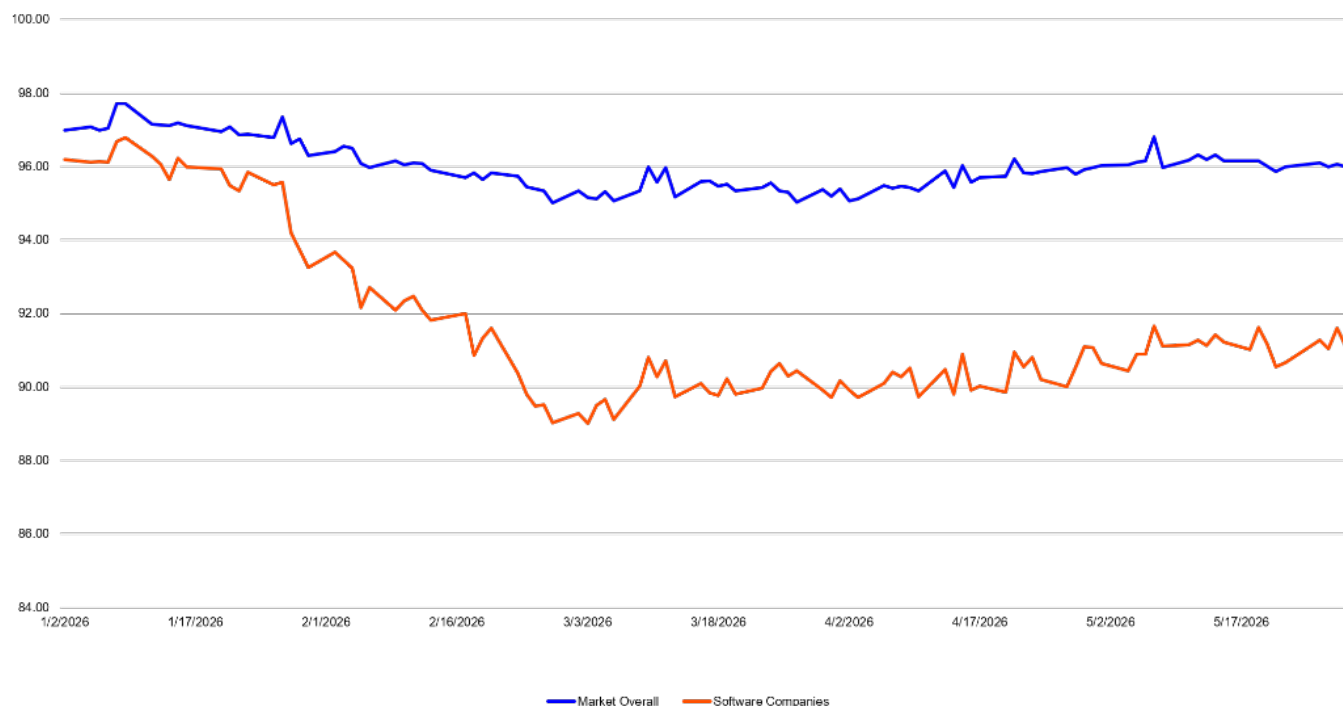
However, credit outlook has become cloudier as sticky inflation, elevated rates, and technology revolution pressure industries and issuers with weaker business model, tight cash flow, or refinancing pressure. We see Wholesale, General Manufacturing, and Services leading in Caa-rated exposure, while Wholesale, Healthcare, and Chemicals report the highest default rates. From a tail-risk perspective, Technology and Business Services carry the largest concentration of assets priced below 80, as both are victims of sharp software selloff this year.

We note some CLO managers have used the selloff to add discounted loans with stable fundamentals for par-build upside, while others reduced exposure to issuers viewed as structurally vulnerable to AI disruption or refinancing pressure, leading to further tiering among software or business service loans.

**Exhibit 94: BSL CLO collateral performance of the top 10 industries by CLO exposure**

| Industry                     | CLO Exposure (%) | Caa or below (%) | CCC or below (%) | Defaulted (%) | Price<80 (%) |
|------------------------------|------------------|------------------|------------------|---------------|--------------|
| Technology                   | 14.60            | 4.77             | 4.93             | 0.09          | 13.36        |
| Financial Services           | 14.41            | 1.93             | 1.72             | 0.00          | 2.06         |
| Healthcare                   | 8.32             | 6.89             | 3.96             | 0.57          | 3.60         |
| Business Services            | 8.04             | 6.39             | 6.85             | 0.02          | 9.08         |
| Services                     | 6.10             | 7.23             | 6.33             | 0.06          | 3.85         |
| General Manufacturing        | 5.76             | 8.87             | 8.21             | 0.21          | 5.71         |
| Leisure and Entertainment    | 3.70             | 1.93             | 3.56             | 0.26          | 0.97         |
| Transportation               | 3.39             | 2.52             | 0.02             | 0.01          | 2.18         |
| Wholesale                    | 3.27             | 14.83            | 8.98             | 1.04          | 5.19         |
| Chemicals, Plastics & Rubber | 3.21             | 3.24             | 6.12             | 0.48          | 1.69         |
| Overall Market Average       |                  | 5.34             | 4.58             | 0.38          | 5.35         |

Source: LSEG LPC, Yield Book (June 2026)

**Exhibit 95: Weighted average price for software sectors vs. overall market in 2025**

Source: LSEG LPC, Yield Book (June 2026)

In terms of YE2026 credit forecast, we maintain our estimate of 5.50% Caa-or-lower-rated CLO assets, slightly higher than the 5.34% midyear 2026 level, reflecting contained downgrade pressure in near term. Meanwhile, we are raising our TTM default forecast to 2.25% at YE2026 (vs. 2.00% in the original forecast), compared to the 2.17% midyear 2026 level as credit dispersion may lead to more default events in the 2<sup>nd</sup> half.

**Exhibit 96: 2026 Forecast of Caa% and Default Rate**

| Year                              | Caa%  | TTM Default % |
|-----------------------------------|-------|---------------|
| Midyear 2026                      | 5.34% | 2.17%         |
| Original YE2026 Projection        | 5.50% | 2.00%         |
| Midyear Updated YE2026 Projection | 5.50% | 2.25%         |

Source: Trepp, LSEG Yield Book (June 2026)

**Private Credit CLOs: weaker credit metrics mitigated by healthy structural cushions**

Private Credit (PC) CLOs have been under increased investor scrutiny since last year, as several high-profile credit events heightened market caution around private credit fundamentals, valuation transparency, and liquidity risk. BDCs have also faced rising redemption pressure and declining market-value NAVs, reinforcing concerns around weaker/smaller borrowers and less liquid assets.

Looking at the fundamentals, PC CLOs do show weaker credit quality metrics than BSL CLOs, with CCC exposure standing at 9.19%, more than double the 4.18% level for BSL CLOs, while PC WARF was also higher at 3690 versus 2740, reflecting a riskier underlying borrower profile. Default rates were also elevated, with PC CLOs reporting 0.88% defaults compared with 0.38% for BSL deals.

On the other hand, PC CLOs have stronger deal-level structural protection to mitigate the risk from their weaker credits. The average Junior OC cushion for PC CLOs was 7.62%, compared with 3.56% for BSL CLOs, while the share of deals failing Junior OC tests was lower at 6.08% versus 6.74% for BSL. Thanks to the higher CCC% threshold, PC deals also showed a lower share of CCC test failures, 8.33% compared with 15.51% for BSL.

Despite broader market concerns around private credit, we remain constructive on PC CLO performance but would emphasize the importance of manager selection, underwriting discipline, valuation transparency, and close monitoring of borrower-level credit deterioration.

#### Exhibit 97: Private Credit CLO vs. BSL CLO

| Metrics                       | Private Credit CLO | BSL CLO |
|-------------------------------|--------------------|---------|
| CCC% (based on reported test) | 9.19%              | 4.18%   |
| Deals Failing CCC test        | 8.33%              | 15.51%  |
| WARF                          | 3690               | 2740    |
| Junior OC Cushion             | 7.62%              | 3.56%   |
| Deals Failing Junior OC       | 6.08%              | 6.74%   |
| Default Rate                  | 0.88%              | 0.38%   |

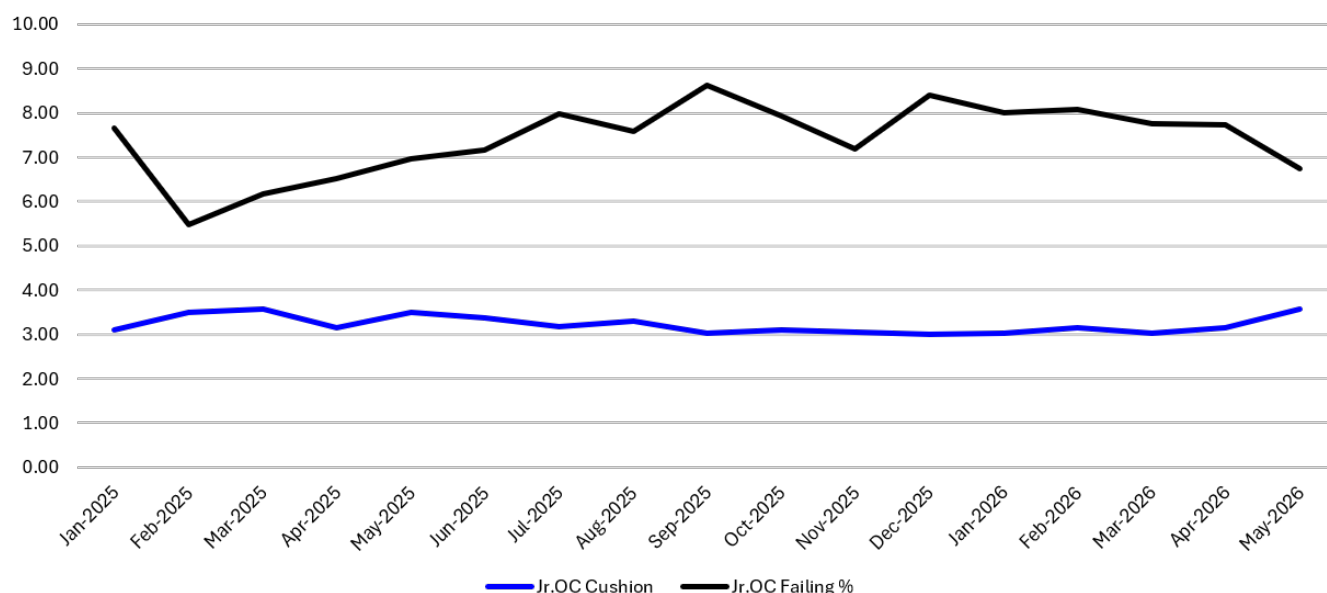
Source: Trepp, LSEG Yield Book (June 2026)

## CLO Performance

### Solid structural performance but eroded equity return

In 1H2026, CLO Junior OC cushions held broadly steady despite software-sector weakness and periodic loan-price volatility. The recovery in collateral prices from February lows, contained CCC exposure, and low default rates helped prevent a broad deterioration in OC cushions. Junior OC test failing rates remained manageable, averaging 6.74% in May, while the average Junior OC cushion also improved to 3.56% in May, up from 3.01% at YE2025. Overall, CLO structural performance remained generally stable, with stronger aggregate cushion levels, though test pressure stayed concentrated in seasoned deals and portfolios with weaker collateral flexibility.

#### Exhibit 98: Market average Junior OC cushion and Junior OC test failing rate



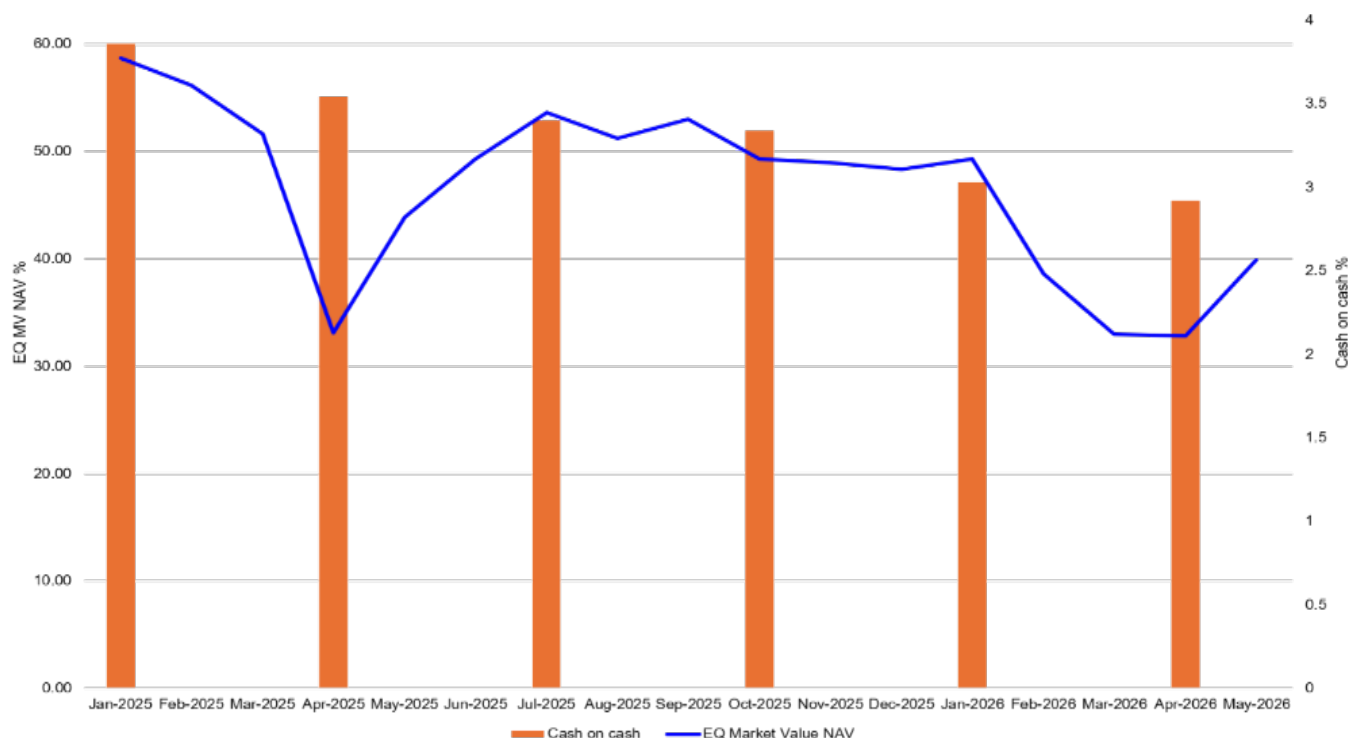
Source: Trepp, Yield Book (June 2026)

While senior and mezzanine liabilities remained well supported, equity returns were more exposed to the compression in asset spreads and the uneven collateral backdrop. Equity performance weakened in 1H2026, with cash-on-cash returns dropping as tighter loan spreads, constrained arbitrage, and weaker collateral trading levels weighed on excess spread. The cumulative cash-on-cash return stood at 5.95% in the first half of 2026, 20% down from the YTD 2025 level.

Equity NAV was also highly volatile through 1H26, reflecting large swings in leveraged loan prices as NAVs recovered from February low to 39.9% in May, below the 48.3% level at YE2025.

Par build was another headwind, with many deals facing negative par formation as managers navigated discounted loan positions and limited opportunities to source higher-spread collateral at attractive prices. Software weakness complicated this dynamic further, as managers sought to reduce exposure or clean up portfolios for resets often had to sell loans at depressed market prices, taking losses and limiting par recovery. As a result, equity performance in 1H2026 became more manager-dependent, with stronger outcomes tied to collateral selection, disciplined trading, and the ability to preserve par while maintaining sufficient spread income.

#### Exhibit 99: CLO Equity market value NAV and Cash-on-Cash Return



Source: Trepp, LSEG Yield Book (June 2026)

Looking into 2H26, CLO performance should remain robust if defaults stay low and managers continue to proactively manage distressed assets. However, weaker software loans, higher-for-longer financing costs, and idiosyncratic downgrades could increase pressure for deals with thinner cushions or less flexibility to trade out problem credits.

For the Junior OC cushion, we maintain our year-end forecast at 3.25%, unchanged from our original projection despite the improvement in the mid-year level, as software-related dispersion, negative par build, and potential downgrade pressure could weigh on cushions in 2H26.

For the equity cash-on-cash return, we lower our 2026 forecast to 12.00%, down from the original 14.50% projection. While the May level likely reflects a period of elevated market stress and should improve if loan prices stabilize and liability spreads remain supportive, full-year equity returns are now expected to fall below the strong 2025 level.

#### Exhibit 100: 2026 CLO Junior OC Cushion and Equity Cash-on-Cash Forecast

| Period                        | Junior OC Cushion | Equity Cash on Cash |
|-------------------------------|-------------------|---------------------|
| December 2025                 | 3.01%             | 14.16%              |
| May 2026                      | 3.56%             | 5.95%               |
| Original 2026 Forecast        | 3.25%             | 14.50%              |
| Midyear Updated 2026 Forecast | 3.25%             | 12.00%              |

Source: Trepp, LSEG Yield Book (June 2026)

### **Cautiously constructive outlook amid challenging macros**

Overall, we remain cautiously constructive for 2H2026. The market has shown resilience through macro volatility, supported by sustained investor demand, stable credit fundamentals, and continued access to the primary market. However, tighter arbitrage, limited new loan supply, and episodic market volatility are likely to keep new issuance measured, while refi/reset activities remain dependent on liability spread level and collateral credit profile.

Fundamentals have been broadly stable, but with credit dispersion highlighted by software weakness. CLO liabilities should remain well supported by strong demand with spreads likely to stay tight amid lower supply, though equity return is pressured by compressed arbitrage, volatile loan price actions, and par burn. Ultimately, all eyes are on inflation/jobs data and Fed rate path as the CLO market navigates the second half of the year.

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