

Overweight Current Coupon Agency MBS/Underweight Investment-Grade Corporates

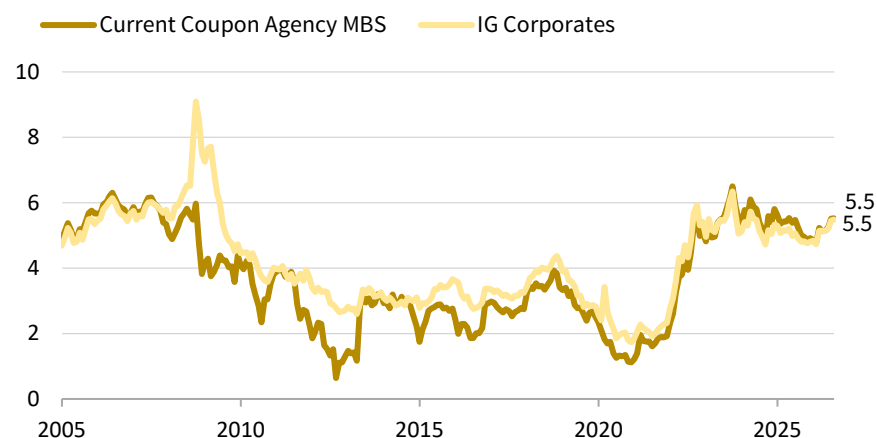
Recommended since October 31, 2025

Investment thesis: US current coupon agency MBS—recently issued, higher-yielding securities—represent a high-quality, attractively valued segment of the investment-grade bond universe. With yields currently competitive with US corporates, they offer compelling relative value and are well positioned to outperform, providing defensive characteristics without sacrificing yield if credit spreads widen from historically tight levels.

Key support 1: For the first time since 2007–08, current coupon yields have routinely matched or exceeded those of corporates. Historically, from these levels, current coupons have outperformed corporates 62% of the time over the next two years, with excess returns ranging from -3% to 11%. As a AAA-rated sector, agency MBS provide better protection against risk asset sell-offs that pressure credit spreads. Corporate spreads remain historically tight and appear vulnerable to widening amid increased issuance and elevated geopolitical risk.

US bond yields

January 31, 2005 – August 31, 2026 • Percent (%)

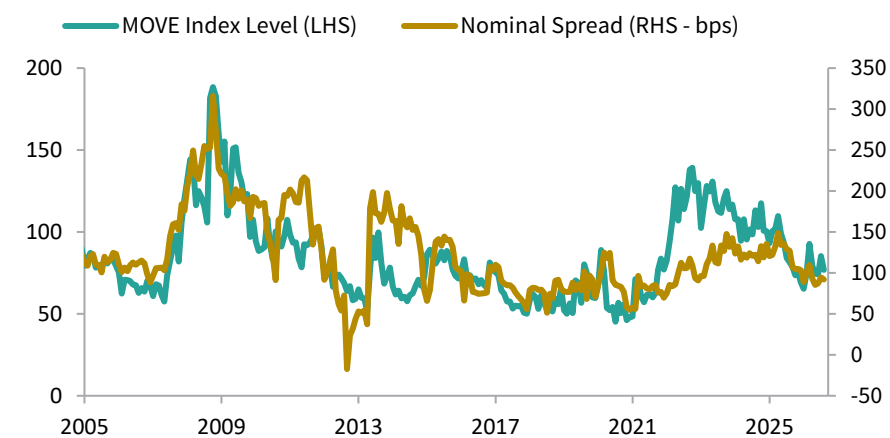


Key support 2: While corporate spreads are near historical tight, current coupon MBS spreads to Treasuries are less extreme—currently in the 35th percentile over the past 20 years. Spreads have tightened over the last year driven by Fed easing, lower rate volatility, and the Trump Administration’s directive for Government-Sponsored Enterprises (GSEs) to purchase \$200B in MBS. Although further upside from declining spreads and volatility is likely now more limited, ongoing GSE purchases may provide a backstop, supporting a more favorable risk/reward profile relative to corporates.

Key risks: While the Fed’s ongoing MBS portfolio reduction has been a headwind, it is likely priced in. However, higher rate volatility remains a risk given uncertainty around inflation and Fed policy. Policy changes also introduce uncertainty, but measures to improve housing affordability have so far been net positive for agency MBS. Prepayment risk could rise if affordability boosts housing activity, though the overall impact should remain limited due to structural hurdles and elevated mortgage rates.

Rate volatility and CC Agency MBS vs Treasury nominal yield spread

January 31, 2005 – August 31, 2026



Sources: Bloomberg Index Services Limited, Intercontinental Exchange Inc., and Thomson Reuters Datastream.

Notes: The MOVE Index is a key indicator of expected volatility in the US Treasury market. Yield spread is calculated versus the Bloomberg US Treasury Index.