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 tight levels.

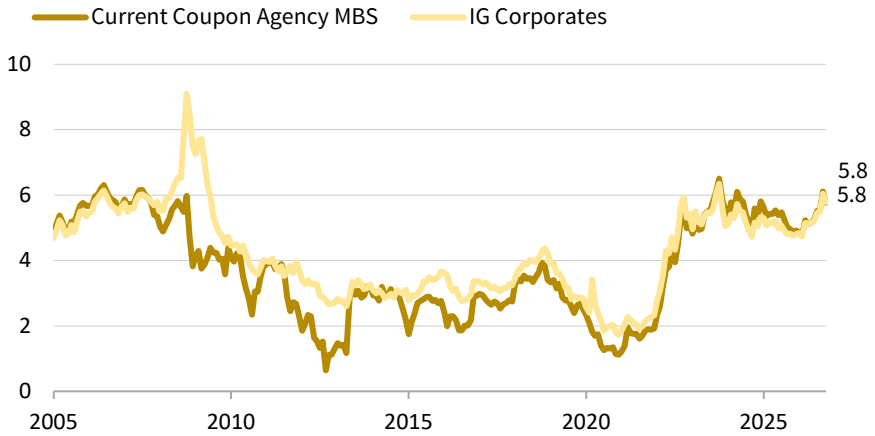
Key support 1: For the first time since 2007–08, current coupon yields have routinely matched or exceeded those of corporates. Historically, from these levels, current coupons have outperformed corporates 62% of the time over the next two years, with excess returns ranging from -3% to 11%. As a AAA-rated 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 given elevated AI-related issuance, concerns about the AI outlook, and ongoing geopolitical conflicts.

Key support 2: While corporate spreads are near historical tights, current coupon MBS spreads to Treasuries are less extreme—currently in the 39th percentile over the past 20 years. Spreads have widened in recent months alongside a sharp increase in Treasury yields and rate volatility. Another meaningful move higher in yields and volatility seems less likely from these levels, while ongoing GSE purchases of MBS and rising issuance of corporate debt support 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.

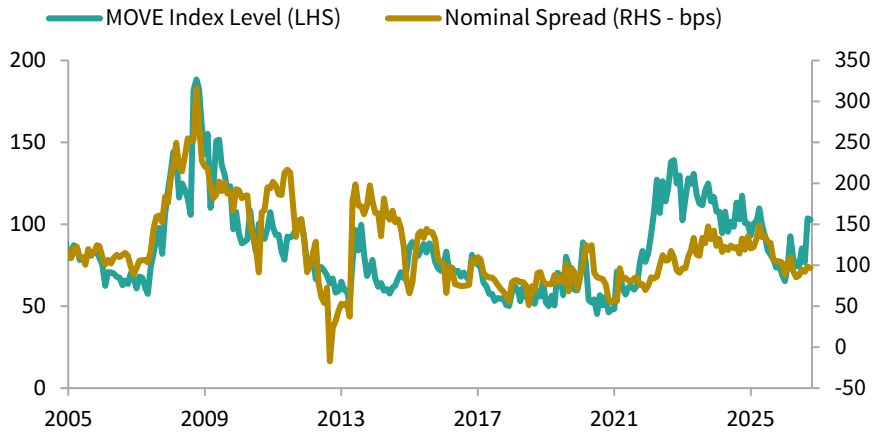
US bond yields

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



Rate volatility and CC Agency MBS vs Treasury nominal yield spread

January 31, 2005 – October 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.

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