

# Q3 2025 CORPORATE BOND MARKET OUTLOOK



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## Key Drivers For The Quarter

- Investment grade (IG) corporate bond spreads tightened 11 basis points (bps), ending the second quarter at an option-adjusted spread (OAS) of 83 bps.<sup>1</sup>
- Spreads retraced most of the first quarter widening and are just 3bps wider year-to-date (YTD), as worst-case tariff risks receded and an equity market rebound drove improved sentiment.<sup>2</sup>
- The yield-to-worst (YTW) for the Index was 4.99 percent on June 30, down from 5.15 percent at the end of the first quarter of 2025. We believe an IG YTW in the 83rd percentile, based on Bloomberg (BBG) data, may support demand.<sup>3</sup>
- IG gross bond supply was \$426 billion in the second quarter, an increase of 5 percent over the prior year. On a net basis, after heavy redemptions, issuance was just \$32 billion.
- After \$44 billion in outflows in April, \$66 billion flowed into taxable bond funds in May and \$38 billion in the second quarter.<sup>4</sup> Foreign investor net corporate purchases were \$109 billion YTD through April.<sup>5</sup>
- IG credit metrics are stable. Leverage is steady, while margins are at a record high.<sup>6</sup> Capital relief and deregulation may drive earnings and mergers and acquisitions (M&A) in the U.S. bank sector.
- Tight credit spreads, solid demand, stable credit fundamentals, and tariff-related uncertainty drive a modest overweight to corporate bonds with a defensive posture.

1. The Bloomberg U.S. Corporate IG Bond Index, Breckinridge, 6/30/25.

2. Ibid.

3. Ibid.

4. Investment Company Institute (ICI), Statistics, Combined Estimated Long-Term Flows and ETF Issuance, 7/2/25.

5. U.S. Treasury International Capital Data for April 2025, June 18, 2025.

6. Bloomberg Intelligence, North America Credit Strategy Dashboard, Trimmed Mean (Bottom/Top 10 percent), 6/30/25.



## INVESTMENT REVIEW & OUTLOOK

### Tight Spreads, Favorable Technicals, and Stable Fundamentals Drive a Modest Overweight

During the second quarter, volatility was the name of the game. On April 2, 2025, the U.S. announced a broad package of import duties and reciprocal tariffs, which were higher than expected.<sup>7</sup> The “shock-and-awe” of the Executive Order pushed equities sharply lower and credit spreads materially wider. For a brief time in mid-April, spreads touched 120bps or the 40th percentile. A 90-day pause for reciprocal tariffs was announced on April 9, 2025, which drove a steady recovery in equities and credit. At June 30, after 35bps of tightening from the wides, spreads were back to the 3rd percentile.

The pause on tariffs is set to expire on July 9, driving more negotiations, the possibility of another extension, or implementation. Depending on where tariffs shake out, it is reasonable to expect volatility in the corporate market although not as acute. Spreads are tight and quality spreads have narrowed compared to history. Credit picking is still key, with our view that a slower growth, inflationary environment may emerge, driving dispersion in valuations and performance across sectors and issuers.

IG corporate new issuance began the quarter sluggishly, as some deals were tabled during the early part of April due to market conditions. However, after strong May and June tallies, gross issuance of \$426 billion end 2Q25 up 5 percent year-over-year (Y/Y).

In terms of flows, it was a choppy quarter. After \$47 billion of taxable bond fund outflows in April, \$66 billion flowed back in during May and \$38 billion for 2Q25. Still, after \$107 billion in net inflows in the first quarter and \$77 billion in the prior year, the second quarter’s tally represented a material slowdown compared with the first quarter and the prior year. Fortunately, other sources of demand were steady, with foreign investors’ net corporate purchases of \$109 billion through April, per Treasury.<sup>8</sup> Overall, we consider the supply/demand or technical backdrop as a modest positive for corporate bonds.

In our view, credit fundamentals remain stable with solid earnings growth and high operating margins. For now, a pause in tariffs has softened potential negative credit risks. After higher-than-forecast 13 percent growth in 1Q25, earnings growth is projected to slow to 5 percent in 2Q25.<sup>9</sup> Capital relief and deregulation may drive earnings growth, less long-term debt issuance, and further consolidation in the U.S. bank sector.<sup>10,11</sup> Agency corporate credit rating upgrades exceeded downgrades by about 2:1 in 2Q25.<sup>12</sup> We view corporate credit fundamentals as supportive for the IG market.

The Breckinridge Investment Committee’s base case is for sub-par economic growth due to a slowdown in consumer spending, a softer job market, and the risk of reimposition of delayed tariffs. With baseline tariffs slowing economic growth and the labor market, we believe the Federal Reserve (Fed) will reduce interest rates twice in 2H25. Our positioning is defensive with tight spread valuations in most corporate sectors. Attractive all-in yields continue to bring inflows from yield-based buyers and drive demand for IG corporates.

7. “Regulating Imports with a Reciprocal Tariff to Rectify Trade Practices that Contribute to Large and Persistent Annual United States Goods Trade Deficits,” Presidential Actions, Executive Orders, The White House, 4/2/25.

8. Financial Accounts of the United States, Flow of Funds Report, Federal Reserve System, First Quarter, 2025.

9. Bloomberg Earnings Analysis, S&P 500 Index Consensus Earnings Growth [% Y/Y], 6/30/25.

10. Board of Governors of the Federal Reserve System, Agencies Request Comment on Proposal to Modify Certain Regulatory Capital Standards, 6/27/25.

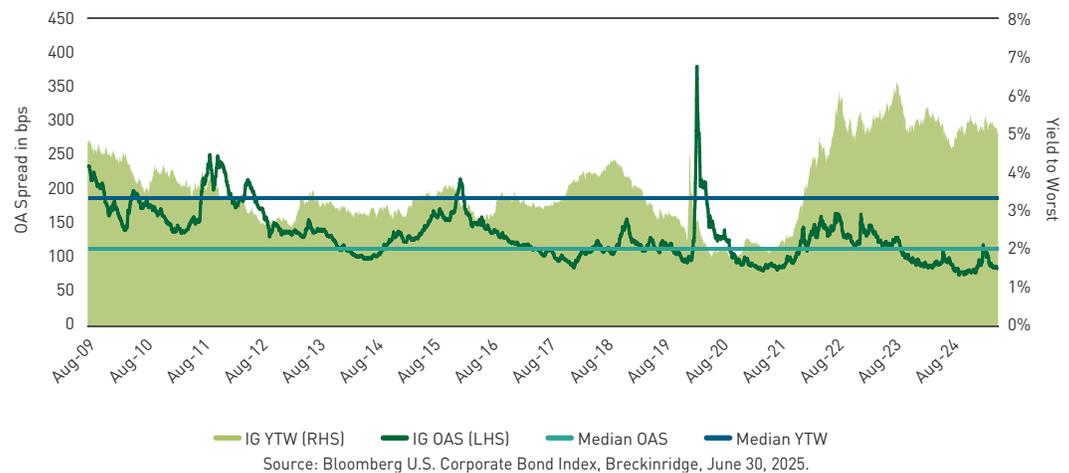
11. Bloomberg Law, *Trump Signs Repeal of OCC Rule Tightening Bank Merger Reviews*, Evan Weinberger, 6/21/25.

12. Bloomberg Credit Rating Trends, Long Term Investment Grade Rating Changes (Moody’s, S&P, Fitch), 6/30/25.



## VALUATIONS

**FIGURE 1: SPREADS ARE TIGHT, YIELDS ARE WELL ABOVE AVERAGE**



Corporate spreads were 11bps tighter in 2Q25, closing at an OAS of 83bps. IG corporates widened about 20bps in the first five trading days of April. A 90-day pause on reciprocal tariffs fueled a rebound in equities and improved sentiment in IG credit. The IG OAS stayed over 100bps until the first week of May and has narrowed steadily since then. An IG yield at 5 percent, in the 83rd percentile, may support demand. Quality spreads have narrowed with the gap between As and BBBs at 32bps for a Z-score<sup>13</sup> of negative 1.5 compared to the average over the last five years.<sup>14</sup>

## TECHNICALS

**FIGURE 2: MODEST NET SUPPLY STILL ABSORBED BY LIGHTER INFLOWS**



IG gross supply was \$426 billion in 2Q25, up 5 percent Y/Y. April issuance (\$125 billion) was down 12 percent from the prior year. However, May (\$152 billion) and June (\$149 billion) were up double-digits compared to the prior year. On a net basis after redemptions, issuance was just \$32 billion. After \$47 billion of outflows in April, \$66 billion flowed into taxable bond funds in May and \$38 billion for 2Q25. Foreign investor net corporate purchases were \$109 billion YTD through April, per the U.S. Treasury Department. That is on pace to approximate the 2024 (\$264 billion) and 2023 (\$270 billion) amounts, indicating solid demand.<sup>15</sup> This is subject to change depending on tariffs and the resiliency of the U.S. dollar, but foreign buying of corporates has been sticky over the last few years and has helped offset some of the variability in domestic fund flows.

13. A z-score is a statistical measurement that indicates how far away a data point is from the mean of a dataset, measured in terms of standard deviations. It essentially standardizes a raw score, allowing for comparisons between different datasets or populations.

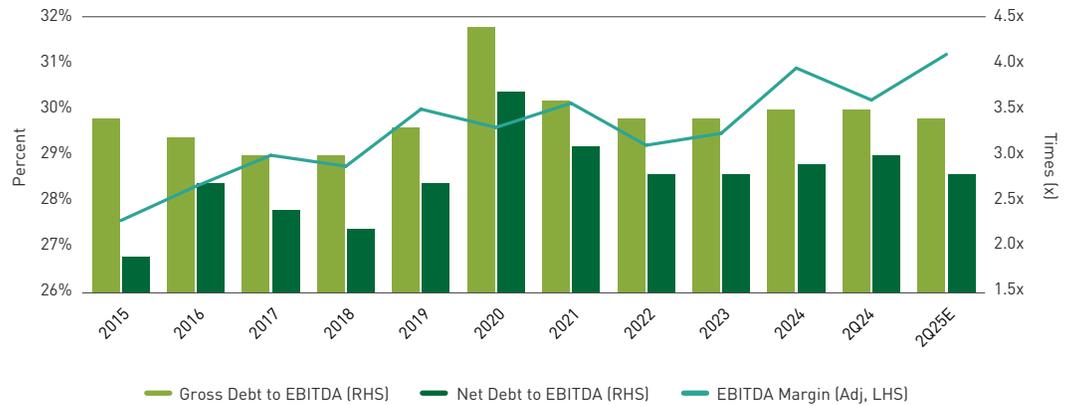
14. The Bloomberg U.S. Corporate IG Bond Index, Breckinridge, 6/30/25.

15. U.S. Treasury International Capital Data for April 2025, June 18, 2025.



## FUNDAMENTALS

**FIGURE 3: LEVERAGE IS STEADY, MARGINS ARE AT A RECORD**



Source: Bloomberg Intelligence, North America Credit Strategy Dashboard, Trimmed Mean (Bottom/Top 10%), June 30, 2025.

IG credit metrics are stable and have improved slightly. A pause in tariffs has softened potential negative credit implications, although risks remain. Leverage is steady at around 2.8 times, on a net basis, while operating margins are at a record high at 31 percent. Spread-per-turn of net leverage at 30bps is below its 10-year average of 44bps.

Regulators are softening their stance towards Banks. Congress recently passed a resolution to roll back the Office of the Comptroller of the Currency (OCC) merger review rule and the Federal Deposit Insurance Corporation (FDIC) rescinded a policy update meant to toughen merger scrutiny. Regulatory relief is accelerating, which may boost revenues and reduce compliance costs.



## CORPORATE TRENDS DASHBOARD

**KEY DRIVERS:** Favorable rating trends and regulatory relief are offset by high geopolitical risk and full valuations

TRENDS	Weakness			Strength		
Credit Ratings			X			U.S. IG Agency corporate credit rating upgrades exceeded downgrades by about 2:1 in 2Q25.
Regulatory			X			Regulatory relief seems to be accelerating, which may boost revenues and reduce compliance costs.
Supply/Demand			X			IG supply of \$426B in 2Q25 up 5% Y/Y. Net supply of \$32B was easily absorbed by inflows.
Central Bank Policy		X				Per median projections in the Fed's June SEP, officials expect two interest rate cuts in 2025.
Economy		X				Weak U.S. consumer surveys are offset by a de-escalation of tariffs and resilient hard data.
Financial Leverage		X				Leverage metrics are steady while spread-per-turn of net leverage is below its ten-year average.
Operating Trends		X				After higher-than-forecast 13% growth in 1Q25, earnings growth is projected to slow to 5% in 2Q25.
Corporate Event Risk	X					Global M&A values were up 18% in 2Q25 Y/Y with the highest increase in North America (+24%).
Valuations		X				At +83bps, spreads are in the 3rd percentile of the 15-Year range while yields are in the 83rd percentile.
Geopolitical Risk	X					Geopolitical risks are high with global trade tensions and wars in the Middle East and Ukraine.

Sources: Breckinridge Capital Advisors, Federal Reserve, Morgan Stanley, Barclays, Bloomberg, ICI, FactSet, Rating Agencies, June 30, 2025.



## STATISTICAL SUMMARY

	As of 6/30/2025		OAS Change (bps)		
	Yield to Worst (%)	OAS (bps)	Month to Date	Quarter to Date	Year to Date
<b>Bloomberg U.S. Corporate Index</b>	4.99	83	-5	-11	3
<b>Corporate Credit Curves</b>					
Corporate 1-3 Year	4.34	52	-4	-6	0
Corporate 1-5 Year	4.43	63	-4	-6	3
Corporate 5-10 Year	4.98	93	-5	-10	8
Corporate 10+ Year	5.71	100	-6	-16	2
<b>Corporate Quality Spreads</b>					
AAA Corporate	4.75	34	1	-7	1
AA Corporate	4.70	47	0	-7	2
A Corporate	4.86	71	-3	-9	2
BBB Corporate	5.18	102	-7	-12	5
<b>Corporate Sector Spreads</b>					
Banking	4.77	79	-5	-10	0
Basic Industry	5.17	93	-7	-11	1
Capital Goods	4.86	71	-3	-11	0
Communications	5.21	92	-10	-21	-5
Consumer Cyclical	4.92	84	-5	-9	12
Consumer Non-Cyclical	4.99	74	-2	-10	0
Energy	5.27	101	-8	-8	9
Insurance	5.23	94	-6	-9	6
REITS	4.86	85	-6	-12	4
Technology	4.84	67	-2	10	2
Transportation	5.19	82	-4	-10	7
Utility	5.22	93	-4	-10	10
<b>Supply/Demand (\$Billions)</b>					
	<b>1Q25*</b>	<b>1Q24*</b>	<b>2024</b>	<b>2023</b>	<b>2022</b>
Net Corporate Supply	1272	1071	729	508	389
Net Purchases (Foreigners)	363	428	356	202	161
Net Purchases (Funds)	464	650	461	179	127
Net Purchases (Households)	-123	-672	-357	4	-301
Net Purchases (Insurance)	171	238	213	140	208
Net Purchases (Other)	397	427	56	-17	194

\* Note: Quarterly figures are seasonally adjusted annual rates.

Sources: Bloomberg Barclays, Fed Flow of Funds, as of June 30, 2025.



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