

Views from our Alpha Pods

February 2026

Macroeconomic outlook

US Treasury yields continue to fluctuate, reflecting multiple tensions.

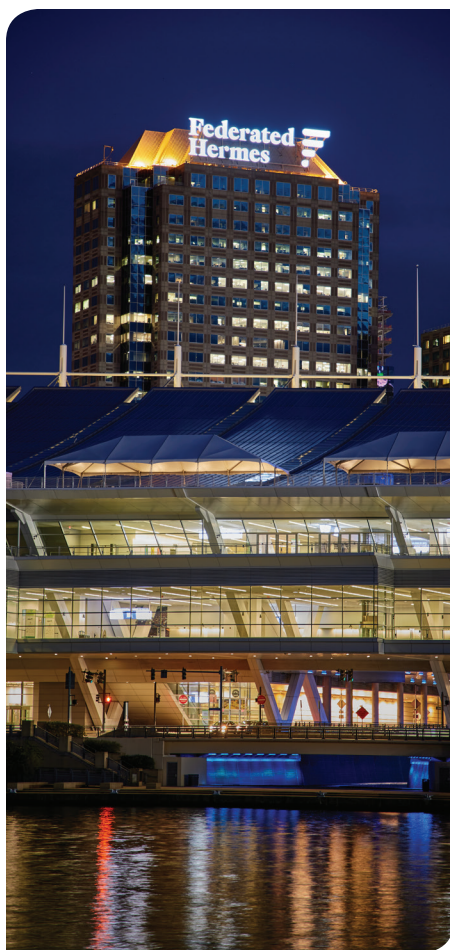
Signs of underlying economic strength are balanced with ongoing concerns about labor-market softening (despite a recent jump in employment) and the impending leadership transition at the Federal Reserve. Current fiscal policy remains supportive as markets await details of a new administration housing initiative aimed at improving affordability without undermining home prices.

Fed Chair nominee Kevin Warsh may change the Federal Reserve's focus.

This could include how the Fed communicates and implements policy frameworks. Warsh has previously spoken against interest on excess reserves and may lighten the Fed's long-term holdings. If he gets all that he wants, markets may see steeper yield curves and lower short rates in the medium term of one to two years.

A number of factors could steepen the yield curve this year.

These include questions of Fed independence, federal deficit worries and delays in Fed rate cuts. With Japanese bond yields pushing higher, the relative value realm is shifting. Overall, even if the front of the curve moves little, the longer end may be firm to pushing ever so slightly higher because of the balance of risks.



By the numbers

Key fixed income stats and our directional expectations for the next 3 to 6 months.

	Prior data	Current data	Directional change from prior period	Our expectations
Unemployment rate*	4.50%	4.40%	▼	–
Inflation (Core PCE YOY)**	2.70%	2.80%	▲	▼
Real US GDP Growth***	3.80%	4.40%	▲	▼
Federal Funds rate range upper bound****	3.75%	3.75%	–	–
2-year Treasury yield****	3.47%	3.52%	▲	▼
10-year Treasury yield****	4.18%	4.26%	▲	▲

*Bloomberg current as of 12/31/25, prior as of 11/30/25.

**Bloomberg current as of 11/30/25, prior as of 10/31/25.

***Bloomberg current as of 9/30/25, prior as of 6/30/25.

****Bloomberg current as of 1/31/26, prior as of 12/31/25.

PCE is Personal Consumption Expenditures.

Past performance is no guarantee of future results.

Alpha Pod overview

Federated Hermes' fixed income investment committees, the Alpha Pods, guide our firm's bond market views and positioning.

- Four independent pods (Duration, Sector, Yield Curve, Currency)
- Consists of portfolio managers, analysts and traders
- Monthly meetings with votes and recommendations
- Aimed at generating alpha from active management
- Security selection by portfolio managers combines bottom-up analysis with the top-down Alpha Pod input

Opportunities in fixed income

There is a range of return opportunities within fixed income that can be sourced from a variety of risk exposures such as sector, duration and quality. Fixed income investors vary with respect to risk tolerances, investment goals and time horizons.

Summary investment views

Based on lively committee discussions, the below themes summarize the views our Alpha Pods are using when making investment decisions.

Duration	Sector	Yield curve	Currency
Moved to a lean short as intermediate to longer rates seem poised to move higher on solid momentum in US growth	We continue to be sensitive to value as spreads across many sectors are within striking distance of historically tight levels	Re-entered the steepener trade as that trend seems poised to reaccelerate, on either bullish or bearish sentiment	The US dollar continues to be under pressure. We continue to hold few currency trades as we wait for trends away from the US Dollar to emerge

Overall, fixed income continued to deliver fairly steady returns and, in our opinion, fulfill its role within diversified portfolios. Our view remains unchanged: active management and valuation are paramount. High-grade, liquid instruments have met our expectations and we believe they remain an attractive option for fixed income across any time period.

Alpha Pod positioning and rationale

Portfolio construction and management are the responsibility of portfolio management teams; however, the Pods provide tactical direction to each team. The below reflects the Pods' positioning following their regularly scheduled meetings, occasionally the Pods change positioning intra-meeting.

Duration management Moved to a lean short (97.5%) benchmark duration from neutral	With the move shorter, the Pod recognized the solid momentum in US growth, continued fiscal and AI-driven investment, supportive financial conditions, stubborn inflation, and a difficult to forecast jobs construct. At the same time, we remain mindful of risks to a larger short position—ranging from potential Fed balance-sheet reductions to elevated real rates, shifting investor flows, geopolitical uncertainty, and China's ongoing export of deflation—which tempered the degree of our move.
Sector allocation Overweight: Treasuries Neutral: MBS Underweight: IG; HY; CMBS; EMD	The Pod remains constructive on economic fundamentals but continues to focus on the lack of value across most sectors, with spreads to UST remaining toward historically tight levels. With potential catalysts for spread widening, notably significant new issue supply, we remain disciplined toward valuation but poised to move on IG. Our active positioning in MBS, IG, HY, EM, and CMBS leaves a residual overweight in Treasuries and agencies, which serves as funding for attractive out-of-index opportunities in our most flexible strategies.
Yield curve analysis Re-established the Steepener	The Pod recommends a steepener, expressed in 2/10 and 2/30 curves at a total of 0.2 KRD. The group sees room for additional curve steepening from here—whether driven by a bullish move if risk-off dynamics intensify, or a bearish move should above-potential growth lift inflation and term premiums before AI-related productivity gains begin to moderate price pressures. The primary risk to this view is the potential announcement of an Operation Twist, which tempers the positioning at the 0.2 KRD level rather than the max of 0.5 KRD.
Currency management Underweight: USD	The Pod concluded last year by noting that “2026 will prove less exciting for the USD than it was in 2025.” Boy, did that comment not work in January. However, the FX volatility of the last few days of January proved fleeting and most exchanges have since fallen back into their preexisting ranges. We envisage a mostly stable USD environment in 2026, but with an ongoing downward skew.

As of 2/6/26.

Mortgage-backed securities (MBS). Emerging markets debt (EMD). Investment-grade corporates (IG). High yield (HY). Commercial mortgage-backed securities (CMBS).

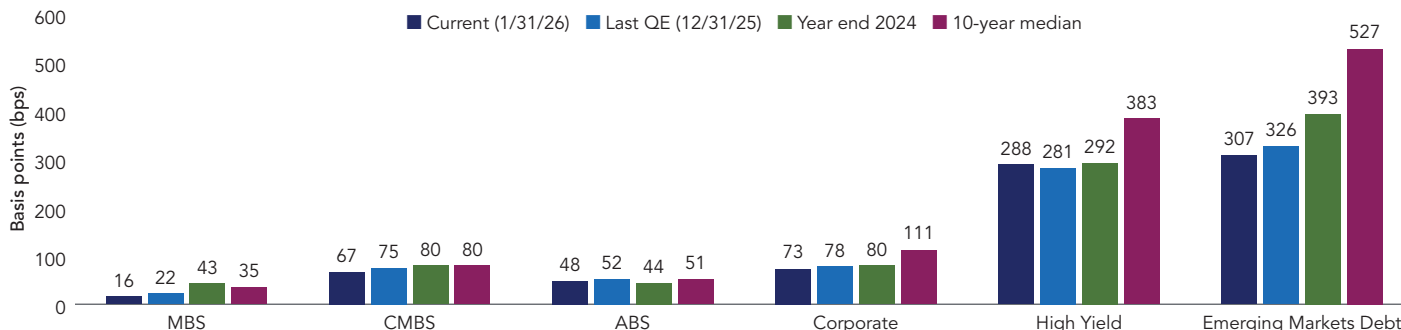
Sector snapshot

Spreads

MBS rallied hard into year end as the steepening yield curve pulled in more buyers. ABS continued to perform well, but spreads ended the year wider than they started. We are looking forward to potential opportunities in IG as more supply forecasted in 2026 could restore value given the continued solid fundamentals.

Spread levels by sector (bps)

Compared to similar maturity US Treasuries



Source: Bloomberg indices (MBS, CMBS, ABS, Corporate EMD), ICE BofA (High Yield).

A deeper dive

The Sector Pod focuses primarily on the sectors included in the Bloomberg US Universal Index. Additionally, underlying teams and portfolio managers weigh in on out of index sectors that could be used. The below provides some additional context to our overall views.

MBS

Neutral: We maintain our neutral position to MBS with valuations now at multi-year tight, similar to spread sector alternatives. The Trump administration’s announcement of \$200B in Fannie/Freddie purchases will take out a meaningful share of expected origination for 2026 and probably puts a backstop bid on spreads. Nominal and option-adjusted spreads (OAS) have reached the lowest levels since 2022. Volatility is already low and has continued to fall, but there may be less room for further declines in implied volatility.

CMBS

Underweight: We maintain our underweight positioning due to overall weak Commercial Real Estate (CRE) fundamentals, weakness in the office sector, and tight valuations. The growth rate of new CRE supply slowed, which should help lead to 1-2% net operating income (NOI) growth in 2026. The Fed’s Senior Loan Officer Survey indicates most banks are no longer tightening CRE lending standards, but a weak labor market is a headwind for CRE rent growth. The CMBS (60+ day) delinquency rate rose to 8%, and the index OAS of +67bps is 18bps tighter than the long term median.

Treasuries

Residual overweight: The process of our active sector decisions imply a suggested overweight to US Treasuries. In practice, this allocation serves as a funding source for out of index sector holdings such as trade finance, Treasury Inflation-Protected Securities (TIPS), asset backed securities and more in our most flexible strategies. Treasury yield curves were stable to start 2026 but show signs of steepening.

IG

Underweight: We maintain our underweight to IG with a bias to move to neutral on spread widening. We are seeing robust and increasingly broad-based revenue and earnings growth and the US macroeconomic picture appears resilient. There is strong demand for new issues with deals multiple times oversubscribed and impact of fiscal tax changes are positive for earnings and capital expenditures. However, valuations remain stretched but range-bound since June 30, 2025. Rising animal spirits and a more lax regulatory environment may lead to more M&A and debt financing.

HY

Underweight: We maintain an underweight primarily on stretched valuations. The big technical tailwind continued with more demand than supply. The economy generated solid GDP numbers and tax refunds should help on the consumer side. Redemptions across leveraged finance are modest given the weakness. We believe risk of contagion from loans and private credit into high yield is probable if pressure continues. The data center building boom is benefiting the economy, but could the boom turn into an overbuilding bust?

EMD

Underweight: Overall, we are constructive, but with historically rich valuations, we look for better entry points. Broad fundamentals have not changed much, but uncertainty is increasing. While the imminent threat of conflict involving Iran has eased, risks for escalation remain high. In China, the anti-involution initiative gained some traction. Through measures such as supply constraints and stricter environmental standards, prices in key inputs—coal, steel, and cement—have stabilized. Despite the US dollar losing substantial ground in January, we envisage a mostly stable US dollar in 2026, but with an ongoing downward skew.


Overweight/underweight calls are relative to Bloomberg US Universal Index. Mortgage-backed securities (MBS). Emerging markets debt (EMD). Investment-grade corporates (IG). High yield (HY). Commercial mortgage-backed securities (CMBS). Asset-backed securities (ABS).

Our leadership in fixed income

<p>more than</p> <h1>55 years</h1> <p>managing fixed income products</p>	<p>team of over</p> <h1>100</h1> <p>fixed income professionals</p>	<p>our portfolio managers average</p> <h1>28 years</h1> <p>in the investment industry</p>	<p>our portfolio managers average</p> <h1>20 years</h1> <p>at Federated Hermes</p>
--	--	---	--

Alpha Pods are chaired by seasoned leaders

Duration management	Sector allocation	Yield curve strategy	Currency management
11 voting members including Chair	10 voting members including Chair	10 voting members including Chair	7 voting members including Chair
Chaired by: R.J. Gallo <i>Deputy Chief Investment Officer, Global Fixed Income</i> Outlook based on: Business cycle analysis, Valuation indicators, Global attractiveness	Chaired by: Mark Durbiano <i>Co-Head of Domestic High Yield Group</i> Outlook based on: Historical spread analysis, volatility analysis	Chaired by: Donald Ellenberger <i>Head of Multi-Sector Strategies Group</i> Outlook based on: Federal Reserve policy, inflation expectations, proprietary multi-factor model	Chaired by: Ihab Salib <i>Head of International Fixed Income Group</i> Outlook based on: US current account/fiscal conditions, interest rate differential, expectations for growth



For dedicated municipal bond or short duration thought leadership from our team, reach out to your Federated Hermes representative.

Forward-looking statements or projections are subject to certain risks and uncertainties. Actual results may differ from those expressed or implied.

Views are as of the date above and are subject to change based on market conditions and other factors. These views should not be construed as a recommendation for any specific security or sector. Material has been prepared using sources of information generally believed to be reliable, but its accuracy is not guaranteed.

Bond prices are sensitive to changes in interest rates, and a rise in interest rates can cause a decline in their prices.

High-yield, lower-rated securities generally entail greater market, credit/default and liquidity risks, and may be more volatile than investment grade securities.

International investing involves special risks including currency risk, increased volatility, political risks, and differences in auditing and other financial standards. Prices of emerging markets securities can be significantly more volatile than the prices of securities in developed countries and currency risk and political risks are accentuated in emerging markets.

The value of some mortgage-backed securities and asset-backed securities may be particularly sensitive to changes in prevailing interest rates, and although the securities are generally supported by some form of government or private insurance, there is no assurance that private guarantors or insurers will meet their obligations.

Investment-grade securities are securities that are rated at least "BBB" or unrated securities of a comparable quality. Non-investment-grade securities are securities that are not rated at least "BBB" or unrated securities of a comparable quality. Credit ratings are an indication of the risk that a security will default. They do not protect a security from credit risk. Lower-rated bonds typically offer higher yields to help compensate investors for the increased risk associated with them. Among these risks are lower creditworthiness, greater price volatility, more risk to principal and income than with higher-rated securities and increased possibilities of default.

2s/10s and 5s/30s spread: The difference in yield between the 2-year and 10-year and the 5-year and 30-year Treasury bonds, respectively, is a measure of yield curve steepness.

2s/30s steepener: Refers to the environment or expectation that the difference between 2-year Treasury and 30-year Treasury yields is widening. Investors employing this strategy aim to benefit from their expectation that the 30-year rate will rise more than the 2-year rate or that the 2-year rate will fall more than the 30-year rate.

Alpha: Measures the excess returns of a fund relative to the return of a benchmark index.

Duration: A measure of a security's price sensitivity to changes in interest rates. Securities with longer durations are more sensitive to changes in interest rates than securities of shorter durations.

Key Rate Duration (KRD): A measure of the sensitivity of a security or the value of a portfolio to a 1% change in yield for a given maturity.

Yield Curve: Graph showing the comparative yields of securities in a particular class according to maturity. Securities on the long end of the yield curve have longer maturities.

Yield Spread: The difference between the quoted rate of return on different debt instruments.

Yield to Maturity (YTM): Used to determine the rate of return an investor would receive if a long-term, interest-bearing investment, such as a bond, is held to its maturity date. It takes into account purchase price, redemption value, time to maturity, coupon yield and the time between interest payments.

Bloomberg US Aggregate Bond Index: Is an unmanaged index composed of securities from the Bloomberg Government/Corporate Bond Index, Mortgage-Backed Securities Index and the Asset-Backed Securities Index. Total return comprises price appreciation/depreciation and income as a percentage of the original investment. Indices are rebalanced monthly by market capitalization.

Bloomberg US Universal Index: Is an index that represents the union of the US Aggregate Index, US Corporate High-Yield, Investment-Grade 144A Index, Eurodollar Index, US Emerging Markets Index and the non-ERISA eligible portion of the CMBS Index. The index covers USD-denominated, taxable bonds that are rated either investment grade or below investment grade.

Indexes are unmanaged and cannot be invested in directly.

Past performance is no guarantee of future results.