

## January 2026

The December payroll report showed nonfarm jobs rising just 50k, capping a notably weak year for hiring and confirming the labor market has cooled materially from the post-pandemic expansion. Job growth in 2025 averaged well below prior years, with most gains front-loaded early in the year and momentum fading into year-end. The unemployment rate edged down to 4.4%, but that improvement masks a clear loss of hiring strength beneath the surface.

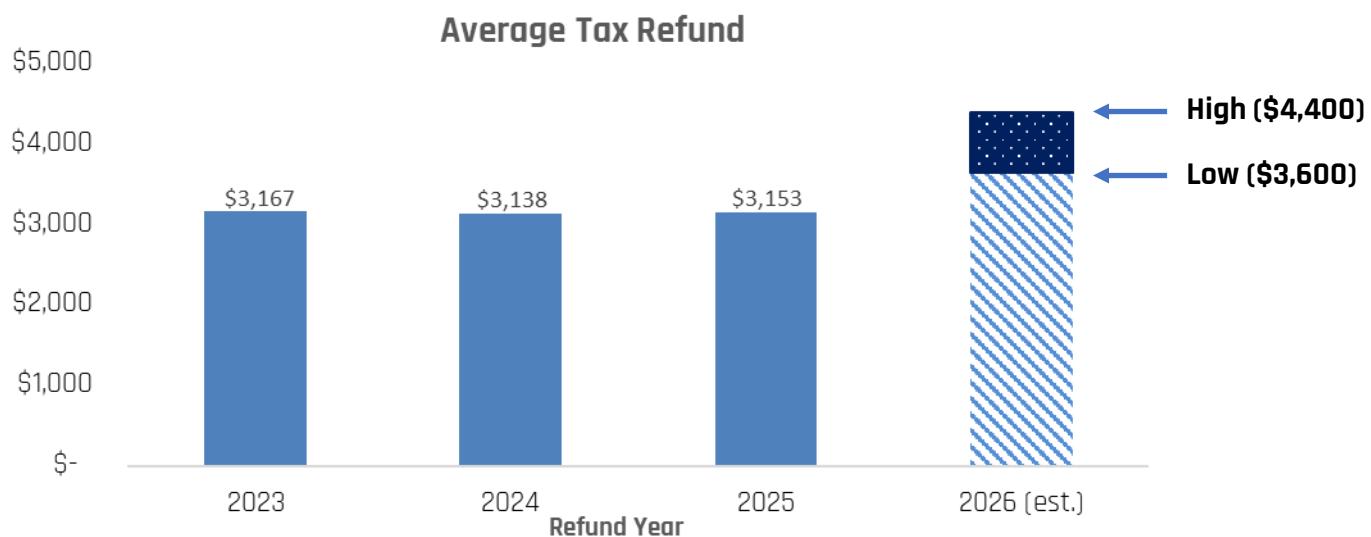
Despite that softness, 2026 is shaping up to be supported on the growth side. First, recent tax law changes are likely to generate a relatively strong refund season: withholding tables did not fully reflect 2025 tax cuts, so many households appear on track for larger-than-usual refunds that could bolster spending in the first half of 2026. Second, major technology firms continue to push forward with large-scale AI-related capital expenditures, which should keep investment and related activity elevated even as questions grow about the ultimate return on this spending.

The administration is also leaning into a consumer-centric agenda heading into the 2026 midterms. President Trump has directed Fannie Mae and Freddie Mac to purchase roughly \$200 billion in mortgage-backed securities in an effort to lower mortgage rates and improve housing affordability, a move that has already boosted housing-linked financial stocks. Additionally, he has called for a one-year cap on credit-card interest rates at 10%, signaling a willingness to intervene more directly in consumer finance costs, even though the implementation path may require additional legislative or regulatory steps. Additional proposals under discussion focus on limiting institutional purchases of single-family homes and expanding access to lower-cost refinancing for existing borrowers.

On inflation, the key risk is that an economy supported by refunds, policy stimulus, and AI-driven investment could re-ignite price pressures just as the Federal Reserve is trying to guide inflation back toward 2%. If growth re-accelerates without a corresponding productivity surge from AI, there is potential that easier monetary policy could re-stoke inflation.

Equity markets, for now, are firmly embracing the optimistic scenario. The Dow and S&P 500 set new record highs in the first week of 2026, while the Nasdaq and small-cap benchmarks have rallied as investors price in tax-driven consumer strength, AI optimism, and a Fed that ultimately tilts more supportive rather than restrictive.

Market pricing currently reflects roughly 50 basis points of Fed cuts over 2026, with investors skeptical of a rapid easing cycle given still-elevated inflation. We continue to hold the view that a more dovish Committee composition later this year, combined with growing concern about labor-market slack, will lead the FOMC to deliver 100 basis points of easing this year. That divergence between current pricing and the potential policy path is likely to be an important theme as the year unfolds.



## Product Views

**Rates:** Over the past year, the Treasury curve has steepened as the Fed eased policy. The 2-year yield is roughly 75 basis points lower, the 10-year is down about 50 basis points, while the 20- and 30-year tenors are largely unchanged. With markets pricing only 50 bps of cuts in 2026 versus our expectation of 100 bps, we see value in targeting duration in the front end and belly of the curve. We remain cautious on the long end, where markets may view aggressive easing as potentially reflationary and term premium could rise as fiscal sustainability and budget deficits move back into focus. Depending on the outcome of the Supreme Court decision around tariffs, this dynamic could change.

As noted last month, housing affordability and elevated mortgage rates are key priorities for the current administration, and recent actions this week reinforce our view. We do not believe these efforts are complete and could ultimately include measures such as an "Operation Twist 2.0" to provide targeted relief to the long end and help lower mortgage rates.

**Credit:** Investment-grade credit returned 7.77% in 2025 and spreads continue to hover near all-time tights, led by financials, valuation remains challenging. Accordingly, we maintain an underweight allocation, focusing selectively on higher-quality names while keeping an up in credit bias.

**Securitized:** MBS returned 8.58% in 2025, roughly in line with high yield (8.62%) while delivering a more attractive risk-adjusted profile and outperforming investment-grade credit. MBS has also started 2026 on solid footing following the administration's announcement of renewed MBS purchases. While opportunities across securitized assets are becoming more limited, we continue to expect policy support to remain consumer-focused and maintain a preference for MBS over credit. Selective opportunities exist in other securitized asset, though careful security selection and detailed collateral analysis is increasingly important.

