

April 10, 2026

## **Q1 2026 Bond Market Update: Fixed Income for Unpredictable Markets**

By Bill Smith, Fixed Income Trader and Portfolio Manager

Quarter one of 2026 was marked by rising geopolitical tensions. The conflict with Iran added significant uncertainty to the global growth and inflation outlook. What appeared to be a relatively straightforward path toward further easing has become more ambiguous with rate cut expectations fluctuating widely in recent weeks.

At its March meeting, the Federal Reserve (Fed) held rates steady and continued to signal one rate cut this year, while emphasizing the growing uncertainty around both sides of its mandate. Markets have turned more conservative with the probability of a single cut by year-end falling to about 25%, according to Bloomberg's interest rate probability model, compared with two cuts fully priced in at the beginning of the year.

Against this backdrop, yields have drifted higher as markets balance a still-resilient U.S. economy against fears of rising inflation. U.S. mortgage, Treasury and agency indices performed well this quarter, while high-yield corporate and emerging market bonds, last year's performance leaders, lagged in the first quarter amid risk-off sentiment.

The charts below summarize the yield and performance of select fixed income tenors and indices as of March 31, 2026:

**U.S. Treasury Yield Curve**

Maturity	Yield	Change (Basis Points)	
		Q1 2026	Year-to-date
2-year	3.80	32.1	32.1
5-year	3.94	21.8	21.8
10-year	4.32	15.0	15.0
30-year	4.91	6.7	6.7

Source: Bloomberg, 31 March 2026 (US On/Off The Run Sovereign Curve)

**U.S. Corporate (Investment Grade) Yield Curve**

Maturity	Yield	Change (Basis Points)	
		Q1 2026	Year-to-date
2-year	4.37	36.6	36.6
5-year	4.76	32.6	32.6
10-year	5.30	26.0	26.0
30-year	5.93	15.4	15.4

Source: Bloomberg, 31 March 2026 (USD US Corporate IG BVAL Yield Curve)

**Municipal (AAA) Yield Curve**

Maturity	Yield	Change (Basis Points)	
		Q1 2026	Year-to-date
2-year	2.41	-3.1	-3.1
5-year	2.60	20.3	20.3
10-year	3.08	35.1	35.1
30-year	4.50	31.1	31.1

Source: Bloomberg, 31 March 2026 (BVAL Muni AAA Yield Curve)

**Index Characteristics and Returns**

Index	Yield (Worst)	Modified Duration	Returns (%)	
			Q1 2026	Year-to-date
U.S. Treasury	4.16	5.96	0.09	0.09
U.S. Agency	4.14	3.97	0.36	0.36
U.S. Corporate Investment Grade	5.15	6.46	-0.42	-0.42
U.S. Corporate High Yield	7.44	3.27	-0.55	-0.55
U.S. Mortgage Backed Securities	4.84	5.73	0.58	0.58
U.S. Broad Market	4.60	5.91	0.06	0.06
Global Broad Market	4.05	6.06	-0.36	-0.36
Emerging Market Corporate	5.81	4.93	-0.70	-0.70
Municipal Investment Grade	3.81	6.17	-0.18	-0.18
Municipal High Yield	5.23	7.08	0.80	0.80
Municipal Taxable	4.99	7.47	0.55	0.55

Source: ICE DATA INDICES, LLC ("ICE DATA"), 31 March 2026. Past performance is no guarantee of future results. U.S. Treasury = ICE BofA US Treasury Index, U.S. Agency = ICE BofA US Agency Index, U.S. Corporate Investment Grade = ICE BofA US Corporate Index, U.S. Corporate High Yield = ICE BofA US High Yield Index, U.S. Mortgage Backed Securities = ICE BofA US Mortgage Backed Securities Index, U.S. Broad Market = ICE BofA US Broad Market Index March 2020 Regular Rebalance, Global Broad Market = ICE BofA Global Broad Market Index, Emerging Market Corporate = ICE BofA Emerging Markets Corporate Plus Index, Municipal Investment Grade = ICE BofA US Municipal Securities Index, Municipal High Yield = ICE US High Yield & Non-Rated Municipal Securities Index, Municipal Taxable = ICE BofA Broad US Taxable Municipal Securities Index.

**Federal Open Market Committee (FOMC)**

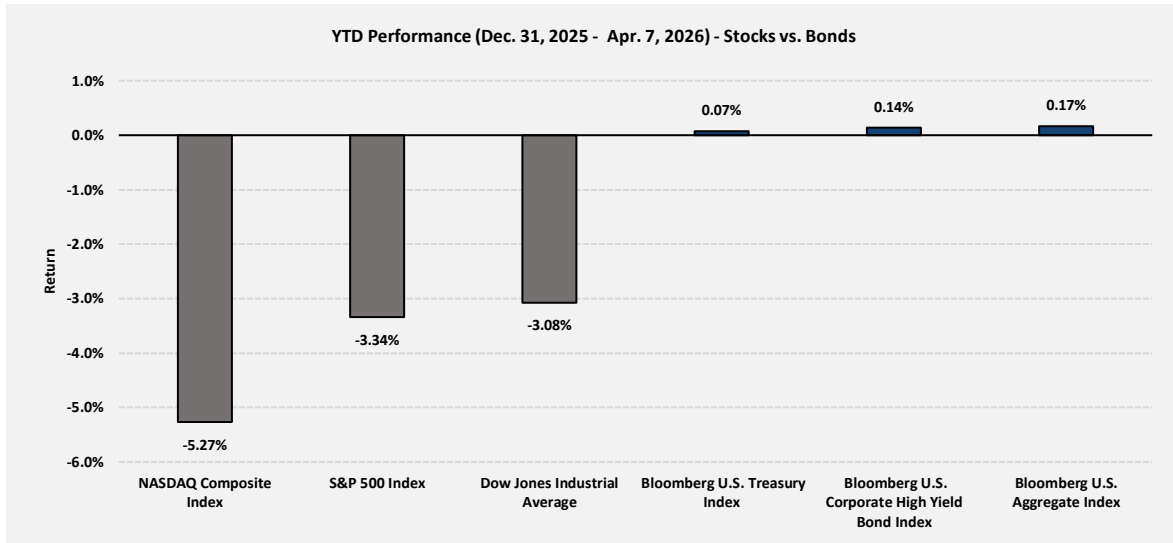
Fed Funds Rate - Upper Bound	3.75	Last FOMC Meeting	18-Mar-26
Fed Funds Rate - Lower Bound	3.50	Next FOMC Meeting	29-Apr-26
Fed Funds Effective Rate	3.64		
Discount Rate	3.75		

Source: Bloomberg, 7 April 2026

*Past performance is not a guarantee of future results.*

## Stock/Bond Correlation

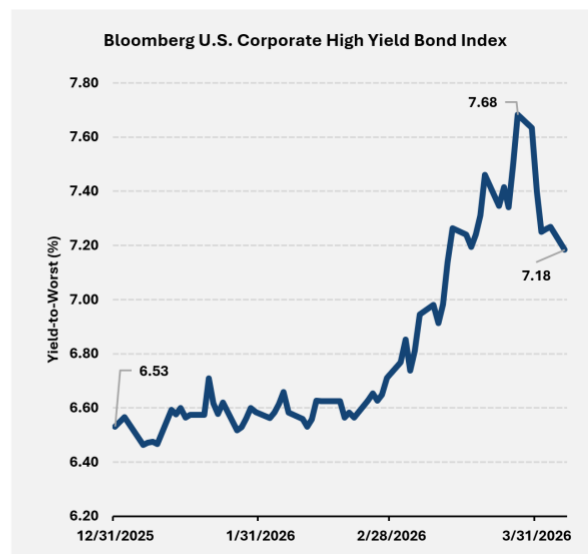
Total returns for stocks and bonds moved in opposite directions to start the year, with equity indices declining and many fixed income indices posting modest gains. For example, the S&P 500 index was down more than 3.30% from Dec. 31, 2025, to April 7, 2026, while the Bloomberg U.S. Aggregate Bond Index was up 0.17% over that same period, as illustrated in the chart below. This contrast underscores how bonds can provide stability during periods of equity market volatility, even when gains are limited.



Source: Bloomberg. Past performance is not a guarantee of future results.

### Yields Opportunities Abound

Yields have increased in 2026. The yield to worst on the Bloomberg U.S. Corporate Bond Index, for example, has risen nearly 30 basis points in 2026, while the Bloomberg U.S. High-Yield Index is up more than 65, reflecting both market caution and policy uncertainty. Elevated yields continue to enhance the income profile of fixed income portfolios, providing investors with attractive carry while maintaining defensive characteristics amid ongoing market volatility.

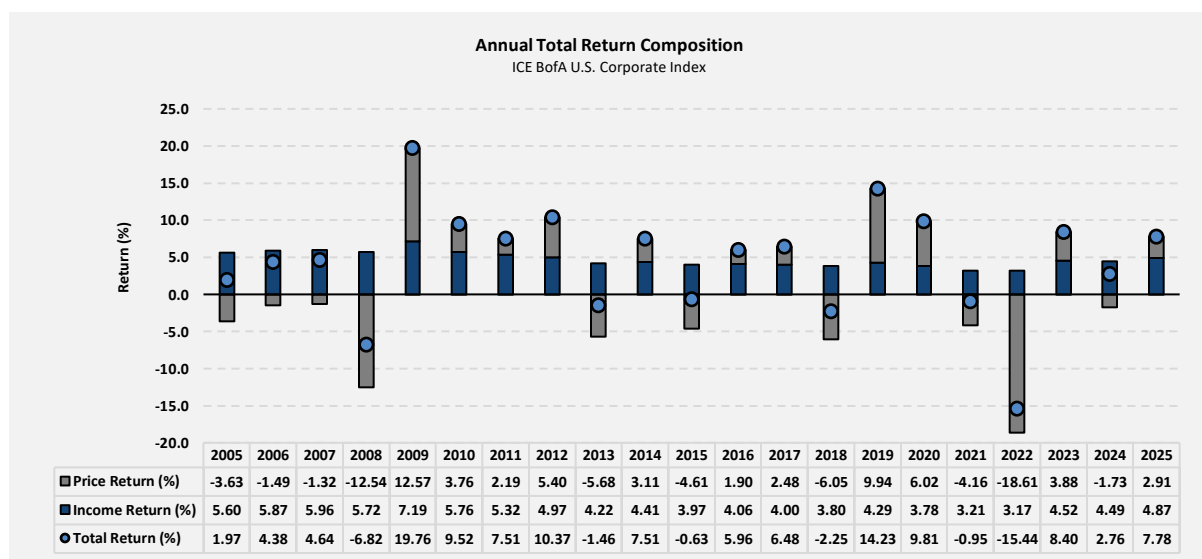


Source: Bloomberg data as of Apr. 7, 2026. Past performance is not a guarantee of future results.

## The Case for Fixed Income in Volatile Markets

With yields elevated, monetary policy uncertain and volatility likely to persist, it’s important to remember two key principles that help fixed income investors navigate choppy markets:

1. **Bonds Mature at Par:** One of the most important aspects of fixed income is also the simplest. Bonds mature at par (face value). For buy-and-hold investors, unrealized gains and losses due to shifting interest rates can largely be ignored. Barring a default or bond call, no matter the price volatility experienced over the life of a bond, investors’ principal is returned at maturity.
2. **Income Returns are Always Positive:** While prices fluctuate over the life of a bond, one aspect of fixed income remains constant: Income returns are always positive. Barring a default or bond call, you know how much you’re going to make, and you know when you’re going to get paid. The chart below, “Annual Total Return Composition,” helps to illustrate this point. Regardless of the direction of bond prices in any given year, coupon payments are always a positive contributor to total returns.



Source: ICE DATA INDICES, LLC (“ICE DATA”). Past performance is not a guarantee of future results.

Despite geopolitical tensions and inflation fears, fixed income has provided much needed portfolio ballast in 2026, highlighting the value of diversification in a shifting macro environment. While volatility is likely to remain high, attractive yields continue to create compelling opportunities across fixed income sectors.

*Fixed income. Flexible thinking.*



A prudent approach to fixed income investing calls for diversification across both credit and duration exposure. As always, Dynamic recommends staying balanced, diversified and invested. Despite short-term market pullbacks, it's more important than ever to focus on the long-term, improving the chances for investors to reach their goals.

*Bill Smith serves as president, Portfolio Management & Trading, of Harmont Fixed Income in Phoenix.*

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