TD Global Investment Solutions

Talking Points

Commentary | Jul 2025

For the month ended July 2025

Fixed Income Outlook

TD Asset Management emphasizes capital preservation in our active fixed income portfolios while seeking to maintain a yield advantage relative to the benchmark. We expect U.S. growth (real GDP) will slow to below trend in 2025 with a slight uptick in 2026 due to a fiscal policy boost. The height of policy uncertainty has passed as trade agreements/frameworks continue to be realized, mitigating the more extreme tariffs, and the signing of the One Big Beautiful Bill into law. Economic survey data indicate a broad-based slowdown with above-target inflation. The U.S. labor market continues to be resilient but is expected to weaken during 2025. The Federal Open Market Committee (FOMC) will reduce its policy rate during the latter part of 2025 and into 2026 as the pass-through impact of tariffs is better understood, and the labor market weakens further. We remain constructive, and very selective toward corporate credit and are comfortable with our strategic credit positioning. Corporate bonds continue to offer some value over government bonds; thus, we maintain our preference for high-quality investment grade corporates. We continue to be positioned with an emphasis on liquidity and quality.

Focal Points

- Initial reading of 2Q 2025 U.S. GDP is 3.0% (-0.5% in 1Q 2025). Tariff front-running which detracted -2.0% from 1Q growth boosted 2Q growth by 1.8%. Net exports was the largest positive contributor as imports plunged, while inventories was the largest negative contributor. Domestic demand continues to slow and suggests below trend economic growth.

- The current federal funds target range is 4.25%-4.50%. The FOMC's median federal funds forecast for year end 2025 is 3.875%. Amid the uncertainty, the FOMC expects, above-target inflation, a weakening labor market, and below trend economic growth in 2025 and 2026.

- Treasury yields increased, and the yield curve flattened. Most hard economic data continue to indicate a resilient U.S. economy. Tariff uncertainty and tariff-related price hikes will negatively impact household and business spending into 2H 2025. This may allow interest rates to move lower from current levels.

- Corporate bond spreads narrowed month over month as investors continue to find value in the sector during a benign macroeconomic environment and reduced tariff uncertainty.

Investment Professionals:

Dennis Woessner, CFA, CAIA
Vice President & Director

Russell Wald, CFA
Vice President

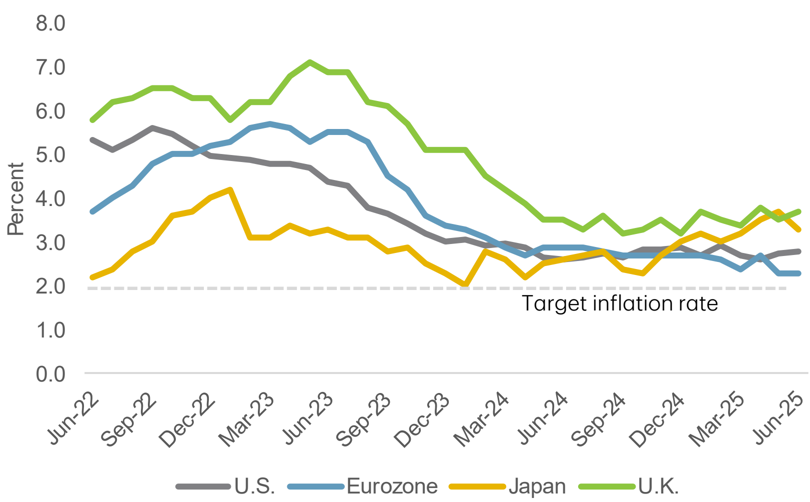
Macro Update

- U.S. real GDP increased 3.0% in 2Q 2025 (-0.5% in 1Q 2025). The whipsaw in trade balance as imports plunged last quarter (opposite to tariff front-running in 1Q) caused net exports to contribute almost 5 ppts to GDP. Conversely, the slowdown in inventory growth detracted 3.2% ppts from GDP. Domestic demand continues to weaken, ending the quarter at its weakest level since 4Q 2022.
- We expect tariff policy to crimp household spending. This will slow U.S. growth (real GDP) to below trend (~2.0%) in 2025 and 2026. We believe inflation will remain elevated and the labor market will weaken during the remaining part of this year.

Long-Term Views:

- U.S. growth will be positive, at the margin, while global economic growth remains relatively weak, especially in the Eurozone. Short-term interest rates are moving lower in many developed markets as growth and inflation moderate.
- Federal Reserve policy will focus on economic growth if inflation moves toward its target rate and the unemployment rate rises. Nominal and real interest rates may remain elevated as U.S. economic growth remains positive.
- Additional disinflation in developed markets may find some resistance due to higher wages, higher food prices, and geopolitical events such as tariffs and on-going conflicts.

Inflation



Source: Bloomberg Financial L.P.; July 31, 2025

Headline inflation in the U.S. and other major economies remain above target levels. US inflation is consolidating above the FOMC's target. We expect inflation to be biased upward in the US and remain elevated over the next twelve months due implementation of tariff and trade-related policies.

Achieving and remaining at the FOMC's two-percent target rate on a sustained basis may be a challenge.

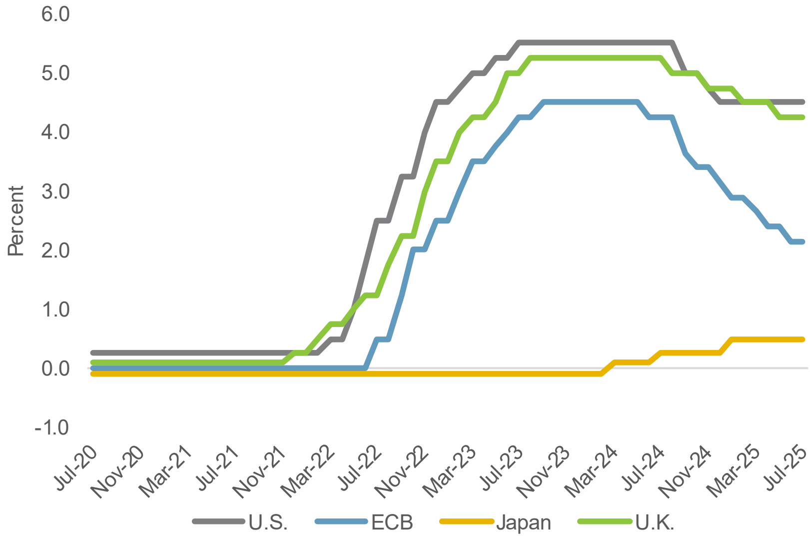
U.S. Central Bank Update

- The current federal funds target range is 4.25%-4.50%. The pace of rate cuts will slow in 2025 due to above-target inflation, a slightly weaker labor market, and a less restrictive policy rate. The FOMC is mindful of heightened uncertainty within its economic outlook and indicated a willingness to look through tariff-impacted inflation they view as one-off if growth meaningfully weakens.
- The FOMC's summary of economic projections report shows below-trend growth, higher-for-longer inflation, a slightly weaker labor market, and a declining federal funds rate, to 3.875% by year end 2025. Uncertainty in the FOMC's economic outlook has diminished but remains elevated due to tariffs.

Long-Term Views:

- The federal funds effective rate will become less restrictive as the FOMC continues decreasing interest rates. We expect a shallower federal funds rate cut path in 2025; however, this outcome is highly uncertain due to the current administration's tariff and fiscal policy agenda.
- The FOMC is committed to its monetary policy framework and market facilities to support price stability, labor markets, and financial market liquidity.

Central Bank Policy Rates



Source: Bloomberg Financial L.P.; July 31, 2025

Most major Central Banks are lowering policy rates as data are showing moderating growth even as inflation remains sticky. Central Banks remain data dependent when determining future policy decisions.

The Federal Reserve reduced the federal funds rate by 1.0 ppt in the latter third of 2024. The trajectory of rate cuts in 2025 will likely be shallower than forecast due to uncertain trade and economic policies. The upper bound of FOMC's policy range has been held at 4.50% since last December (as shown in graph).

Cash/Short-term Market Update

- Short-end Treasury yields increased during the month as the labor market remained resilient, and inflation remains elevated. Tariff uncertainty will negatively impact household and business spending into 3Q 2025 which will contribute to a softening macro economic setting.
- Short-term credit spreads narrowed 5 bps, to 47 bps, during July. Decreased trade-related uncertainty was the main factor in the spread move. Solid fundamentals, attractive yields, and durable growth have supported credit spreads.
- Prime money fund assets increased $50.1 billion during the 3-month period ending July 2025. Total assets are $1.18 trillion (up 12.4% YoY).

Current Positioning:

- Short and Short/Intermediate Government/Credit models prefer high-quality investment grade corporate bonds and have a similar duration profile relative to their respective benchmark.

Number of Hikes/Cuts Priced into Market

Source: Bloomberg Financial L.P.; July 31, 2025

Fewer rate cuts are expected in 2025 as the FOMC's updated projections indicate that inflation will remain higher for longer. It expects the PCE price index to reach the 2.0% target by year-end 2027.

The implied policy rate reached a peak rate of 5.3% in 2024. This rate is now expected to decline along a much shallower path in 2025 due elevated inflation, slightly below-trend economic growth, and the uncertain economic impact from trade and economic policies.

1-3 Year Corporate Option-Adjusted Spread (OAS)

Source: Bloomberg Financial L.P.; July 31, 2025

At 47 bps, the index OAS is 5 bps tighter from last month end. Year-over-year, the index OAS is 9 bps tighter. Factors which may benefit spreads are trend GDP growth outlook, solid fundamentals, and an easing FOMC policy framework. Uncertainty pertaining to trade and fiscal policies are negatively affecting corporate bond spreads.

Corporate fundamentals are expected to weaken from a strong base as growth slows to below trend. Financial conditions are not overly restrictive as the FOMC is easing policy restriction and spreads remain near multiyear tight levels.

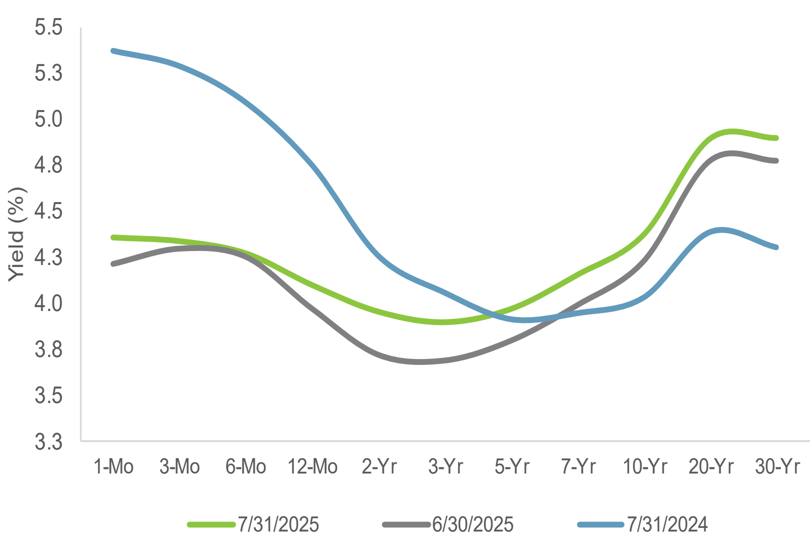
U.S. Treasury Market Update

- U.S. Treasury yields increased, and the yield curve flattened. Some pullback in household and business spending is expected to reduce economic growth during the next couple quarters. Hard economic data continue to indicate a resilient U.S. economy with limited impact from tariff-related policies.
- The scale and scope of the Trump administration's trade, tax, immigration, and regulatory policies to expected real economic growth, inflation, and fiscal deficits remains uncertain. Overall, these policies have elevated short-term implied inflation rates.

Current Positioning:

- Government models have similar duration profiles relative to their respective benchmark. We expect interest rates to be more volatile during this period of uncertain fiscal- and trade-related policies.

Treasury Yields

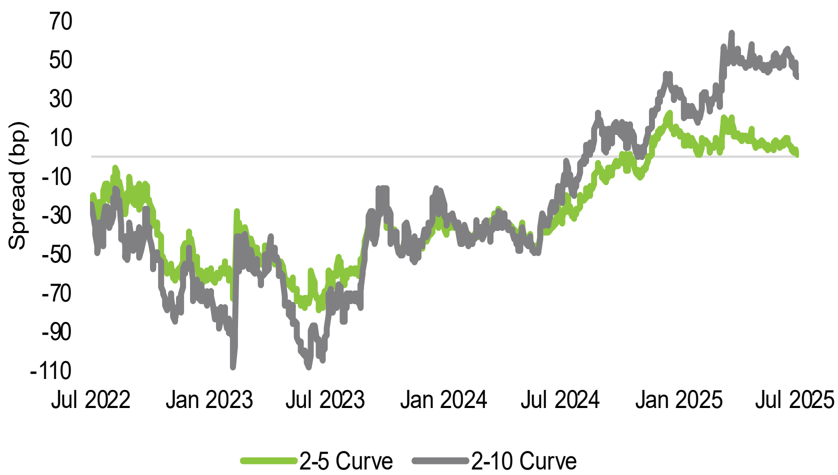


Source: Bloomberg Financial L.P.; July 31, 2025

Treasury yields increased during July. The spread between 2- and 30-year maturities decreased 11 bps, to 94 bps. The yield gap between the 3-month T-Bill and 10-year Treasury is 4 bps, 11 bps steeper since last month end.

We expect yields to move lower from current levels as labor demand weakens, and economic growth slows. Stimulative fiscal policy will contribute to growth later this year and through 2026 which may push yields higher. The FOMC's policy framework is still restrictive. We expect interest rates to be more volatile during this period of uncertain fiscal- and trade-related policies.

Treasury Curves



Source: Bloomberg Financial L.P.; July 31, 2025

The belly of the Treasury curve bear flattened during the month as markets discounted near-term interest rate cuts. Higher fiscal deficits may pressure term premiums higher over the medium and longer term. Investors maintain focus on indicators pointing to weaker economic growth and sticky inflation outlooks. The 2s10s curve decreased 9 bps, to 42 bps. The 2s5s curve, at 2 bps, decreased 6 bps.

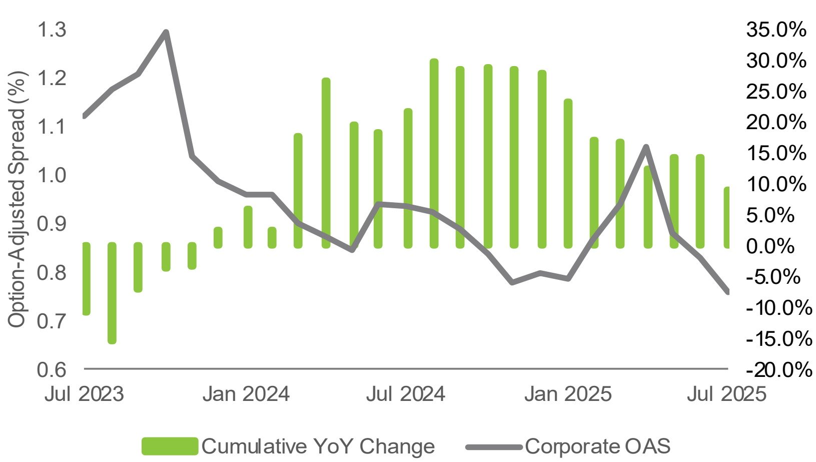
Investment Grade Credit Market Update

- Corporate bond spreads narrowed 7 bps, to 76 bps, and the credit curve flattened relative to last month. Mostly-firm economic data, and reduced uncertainty regarding trade and economic policies were positive factors. Corporate bond yields moved higher during the month.
- Investors are monitoring U.S. trade policy and potential retaliatory measures as it relates to economic growth and corporate earnings.
- Looking forward, corporate fundamentals should remain solid but will continue to weaken from very strong levels as the economy enters a period of below trend growth.

Current Positioning:

- Government/Credit models remain overweight the corporate sector, mostly in the banking industry, and have similar duration profiles relative to their respective benchmark.

Corporate Spread & Issuance

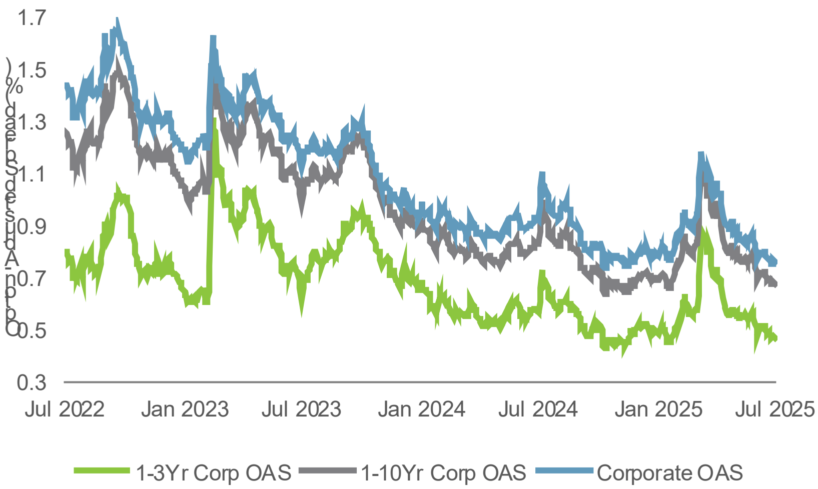


Source: Bloomberg Financial L.P.; July 31, 2025

In July, corporate bond issuance was $88.5 billion, a 29% decrease from the same period last year. The cumulative 12-month change is 9%. The spread on the corporate bond index, at 76 bps, is 7 bps tighter on the month.

YTD issuance is $1.045 trillion. Expected corporate bond issuance for 2025 is $1.55 trillion; therefore, we expect a slowdown in issuance for the remainder of 2025.

Corporate Spreads by Maturity



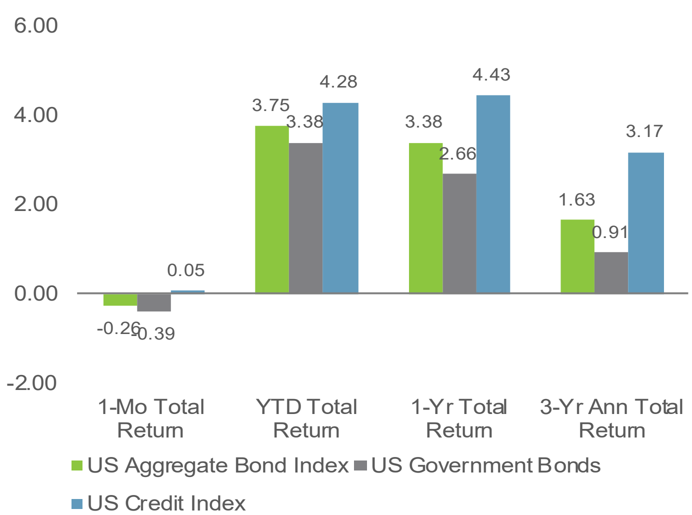
Source: Bloomberg Financial L.P.; July 31, 2025

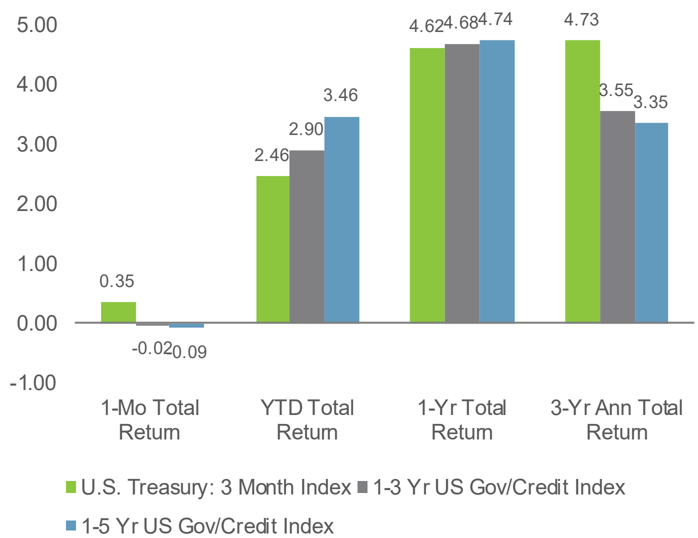
The Bloomberg U.S. Corporate Bond Index spread is 18 bps tighter during the past 12-month period. There has been strong investor demand during a period of relatively higher yields and record issuance. Factors which may benefit future spreads are trend GDP growth outlook, solid fundamentals, and an easing FOMC policy framework. Uncertainty from tariff and fiscal policies is negatively impacting spreads.

The corporate bond index OAS is 7 bps tighter since last month end, currently 76 bps. The 1-10-year index OAS, at 68 bps, is 8 bps tighter for the month.

Charts & Tables

Fixed Income Indices





Economic Figures & Short-term Rates

Description	Current	3-mo Ago	1-yr Ago	Next Release
Fed Funds (%)	4.50	4.50	5.50	9/17/2025
CPI (YoY %)	2.70	2.40	3.00	8/12/2025
PCE (YoY %)	2.60	2.30	2.40	8/29/2025
Unemployment Rate (%)	4.10	4.20	4.10	8/1/2025
GDP (YoY %)	2.00	2.00	2.90	8/28/2025
Retail Sales (YoY %)	3.90	5.10	2.30	8/15/2025
Leading Indicators (YoY %)	-4.00	-3.50	-4.50	8/21/2025
Housing Starts (000s)	1,321	1,355	1,327	8/19/2025

Description	Current	3-mo Ago	1-yr Ago
Fed Funds (%)	4.50	4.50	5.50
3-Mo U.S. Treasury Bill	4.34	4.29	5.29
6-Mo U.S. Treasury Bill	4.28	4.18	5.09
USD O/N Govt. Repo	4.40	4.52	5.46
U.S. 30-Day Comm Paper*	4.31	4.37	5.32
U.S. 90-Day Comm Paper*	4.35	4.38	5.29

*A1/P1/F1 rated U.S. Commercial Paper

Source for all charts and tables: Bloomberg Financial L.P.; July 31, 2025

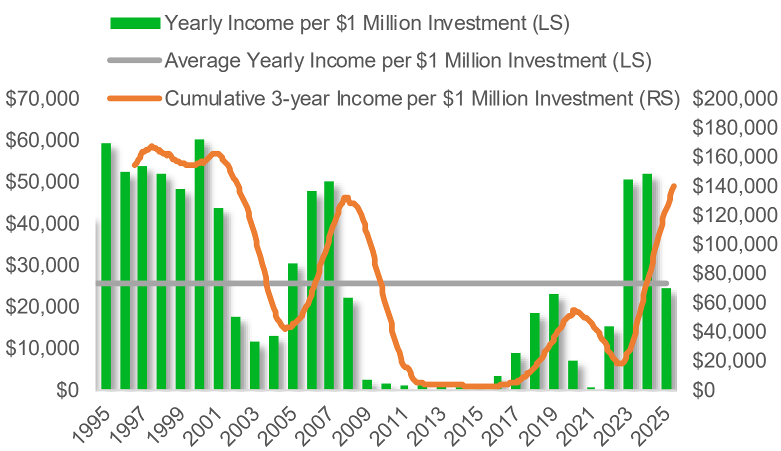
Charts & Tables - continued

Treasury Market

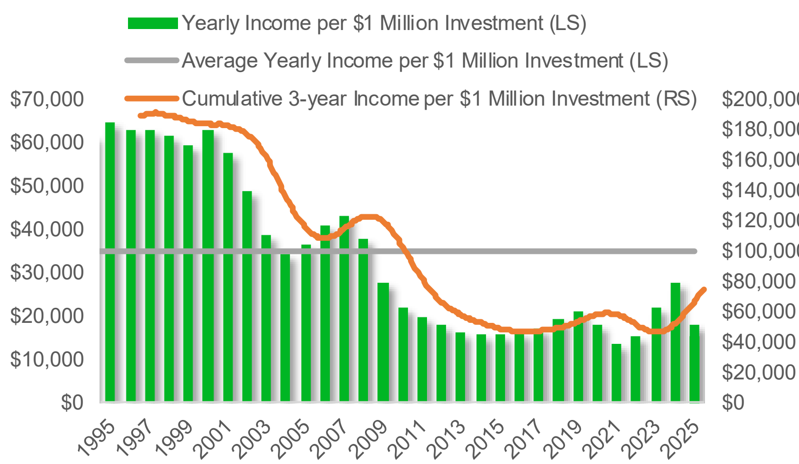
Maturity	Yield Curve (%)	Change in Yield Curve (basis points) 1-Mo Ago	3-Mo Ago	1-Yr Ago
1-Mo	4.36	15	6	-101
3-Mo	4.34	4	5	-95
6-Mo	4.28	2	10	-81
12-Mo	4.10	13	25	-65
2-Yr	3.96	24	35	-30
3-Yr	3.90	21	31	-16
5-Yr	3.97	18	25	6
7-Yr	4.16	17	22	21
10-Yr	4.38	15	21	34
20-Yr	4.90	12	20	51
30-Yr	4.90	13	22	60

Investment Income per $1 Million Invested in Index (No reinvestment of income)

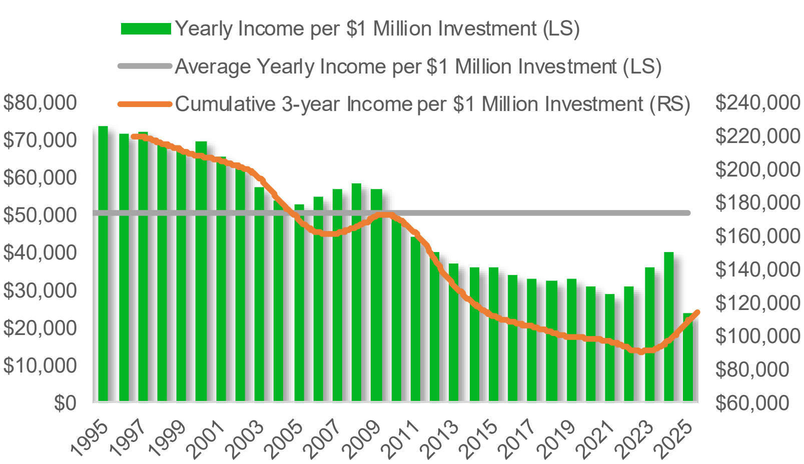
Bloomberg U.S. 3 Month Treasury Bill Index



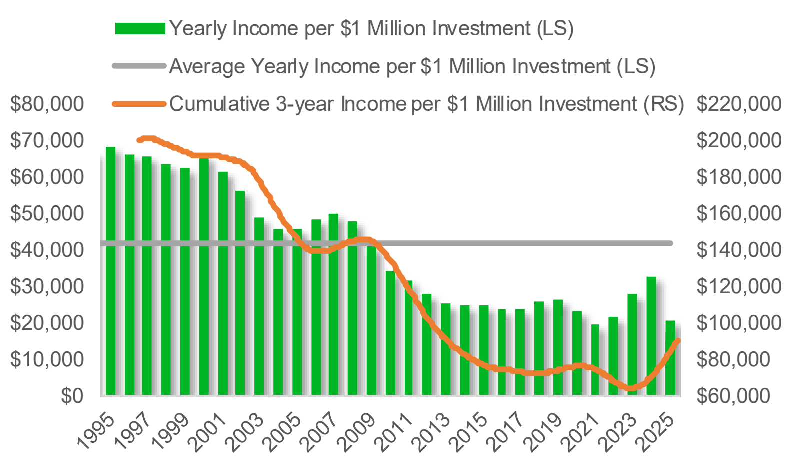
Bloomberg U.S. Treasury 1-5 Year Index



Bloomberg U.S. Corporate Bond 1-5 Year Index



Bloomberg U.S. Intermediate Government/Credit Index



Source for all charts and tables: Bloomberg Financial L.P.; July 31, 2025

Talking Points

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