Fixed Income Perspectives

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The big story

"Who is the real Warsh?"

During his debut press conference in June, Chair Kevin Warsh presented a convincingly hawkish message that helped ease concerns over weakened Fed independence. The market took his message as credible with front-end yields rising, while the 30-year Treasury yield came down. This reflected increased possibility of hikes with a decline in long-run inflation expectations. However, this move was quickly undone following Warsh's July press conference. Despite the brief, yet firm, language in the statement on maintaining price stability, many of Warsh's answers during the press conference left the impression that he is in no hurry to hike. What was expected to be a hawkish hold was a decidedly dovish hold. The market reaction was swift, with front-end yields declining and the 30-year yield rising by over 10 basis points. The market gave Warsh the benefit of the doubt following his first appearance but took it away after this showing. It is not a surprising reaction to the contradictory perception of the June and July press conferences that left the market wondering, "who is the real Warsh?" Warsh wanted the market to become an input into his process, but he may be getting more than he bargained for with the possibility that the market attempts to force his hand. This is also putting on display a potential side effect of more limited Fed communication: greater yield volatility. As we've mentioned in the past, great volatility (whether rate- or spread-driven) generally presents opportunity for active managers with deep research efforts.

U.S. Federal Reserve (the Fed)

The FOMC held rates steady, but three Fed presidents preferred to hike rates. While Warsh came across as dovish, the focus of the dissenters and most of the FOMC is on upside risks to inflation. The hurdle to hike rates remains low and every FOMC meeting is live.

Bank of Japan (BoJ)

Policy rate held at 1%. The BoJ is not pushing back against market expectations of two more rate hikes over the next year. Growth seems likely to strengthen, supported by government policy. Inflationary price pressures are evident and are further fueled by currency weakness.

European Central Bank (ECB)

In July, the ECB kept their policy rate unchanged at 2.25%. A hike in September to 2.5% is expected by consensus. Inflationary pressures from energy costs and government spending are likely to influence the ECB's rates decisions thereafter.

Bank of Canada (BoC)

The BoC is comfortably on hold at 2.25%. Inflation looks increasingly like an energy story, not a demand problem, while excess capacity and labour market slack keep underlying pressures contained. Growth is rebounding, but trade tensions remain the key risk. New U.S. tariffs could quickly tilt the outlook toward weaker growth.

Bank of Mexico

Banxico is firmly in pause mode at 6.50%. Inflation is cooling and Q2 growth surprised to the upside, but core inflation and expectations remain above target. With the easing cycle likely over, policymakers appear content to sit tight and let disinflation continue.

Central Bank of Brazil (BCB)

The BCB is still cutting, but carefully. Inflation has improved and activity is cooling, supporting another small cut in August. Still, elevated inflation expectations, rising FX volatility and a tight labour market argue for a gradual, meeting-by-meeting easing path.

People's Bank of China (PBoC)

The PBoC remains in fine-tuning mode. Growth is slowing but is still supported by exports and AI-related investment, while higher energy prices limit the case for aggressive easing. Expect targeted support, not broad stimulus.

Valuations

- **Leveraged loans:** We are modestly overweight. The floating rate nature of the loan market has protected the asset class from rising U.S. Treasury yields that have pushed prices of other fixed income sectors lower. Persistently wide spreads in the software sector have helped increase the overall income available in the asset class as long as defaults remain low. To the extent some of this credit risk is realized through losses, the opportunity for active management to generate alpha has become more significant.
- **High yield:** We are modestly overweight. High yield spreads are still in the bottom decile relative to history, reflecting strong balance sheets and low realized losses from defaults and restructurings. The increase in Treasury yields is putting downward pressure on prices, but not enough to offset a high level of income. "Breakeven" (yield per unit of duration) is an important metric used in simulating potential return outcomes for fixed income - high yield bond screen well. Dislocations at the industry- and issuer-level focus our attention on idiosyncratic opportunities as we patiently wait for signs that the credit cycle is turning. We are also watching supply and demand dynamics as data centre funding has ramped up significantly.
- **U.S. investment-grade corporates:** We are underweight. Earnings for large-cap companies are robust, balance sheets remain strong, and the longer-term appreciation in the equity market has increased the cushion beneath the debt in the capital structure, justifying current valuations. However, if fundamentals unexpectedly deteriorate, the sector may be vulnerable to significant underperformance with even a minor fundamental hiccup or technical imbalance (seeing signs of supply/demand mismatch in the AI ecosystem). As such, we are patiently waiting for better entry points.
- **International credit (hedged):** We are modestly overweight. The spread advantage relative to U.S. credit that we saw earlier in 2025 is mostly gone, though there is still a carry advantage after hedging currency risk. In addition, the shorter duration and higher quality of the European benchmarks could justify further spread tightening. We still value the diversification and security selection benefits of evaluating a larger pool of investment-grade issuers.
- **Emerging markets debt:** Emerging markets continue to be one of the best performing sectors, with riskier credits (below investment-grade) leading the way. We continue to own idiosyncratic risk through selective ownership of names in Brazil, Colombia and Mexico. More aggressive U.S. foreign policy decisions have not led to higher spread volatility thus far.
- **U.S. Treasuries:** The trend of higher yields on U.S. Treasury securities continues, increasing the attractiveness of an already appealing asset class. Treasury volatility has increased as market prices in the uncertainty of the new Fed Chair and the potential absence of forward guidance. We have added duration as nominal interest rates move up to or above the high end of the three-year range. Treasuries exposure remains close to the highest level in the history of the strategy. This position has been, and will be, the source of funding when the market gives us an opportunity to buy credit sectors.

- **U.S. Treasury Inflation-Protected Securities (TIPS):** We have a zero weighting in TIPS. Longer-term inflation break-evens have been 2.2% to 2.4% for the better part of three years. On an absolute basis, real rates have risen to the highest level in nearly two decades. The Iran conflict has pushed oil prices higher, leading to an increase in inflation expectations in the very short end of the yield curve (e.g. less than two years). We prefer the liquidity of nominal U.S. Treasuries, with volume 10-20 times greater than TIPS.
- **Mortgage-backed securities (MBS):** We have a zero weighting in MBS. Spreads against U.S. Treasuries around 30 basis points are not compelling for this strategy, and we prefer the liquidity and stability of U.S. Treasuries.
- **Structured product:** We are selectively overweight, specifically in franchise bonds and airplane financing. We have a very small allocation to commercial mortgage-backed securities due to valuations. We continue to look for well-structured, idiosyncratic exposure, using our research edge.
- **Local currency debt:** We only own idiosyncratic exposure, with the total size of the allocation near 1%. Currency volatility is significantly higher than rate volatility – approximately three times higher. We own exposure in Brazil, with Brazilian local currency bonds currently yielding over 14%.

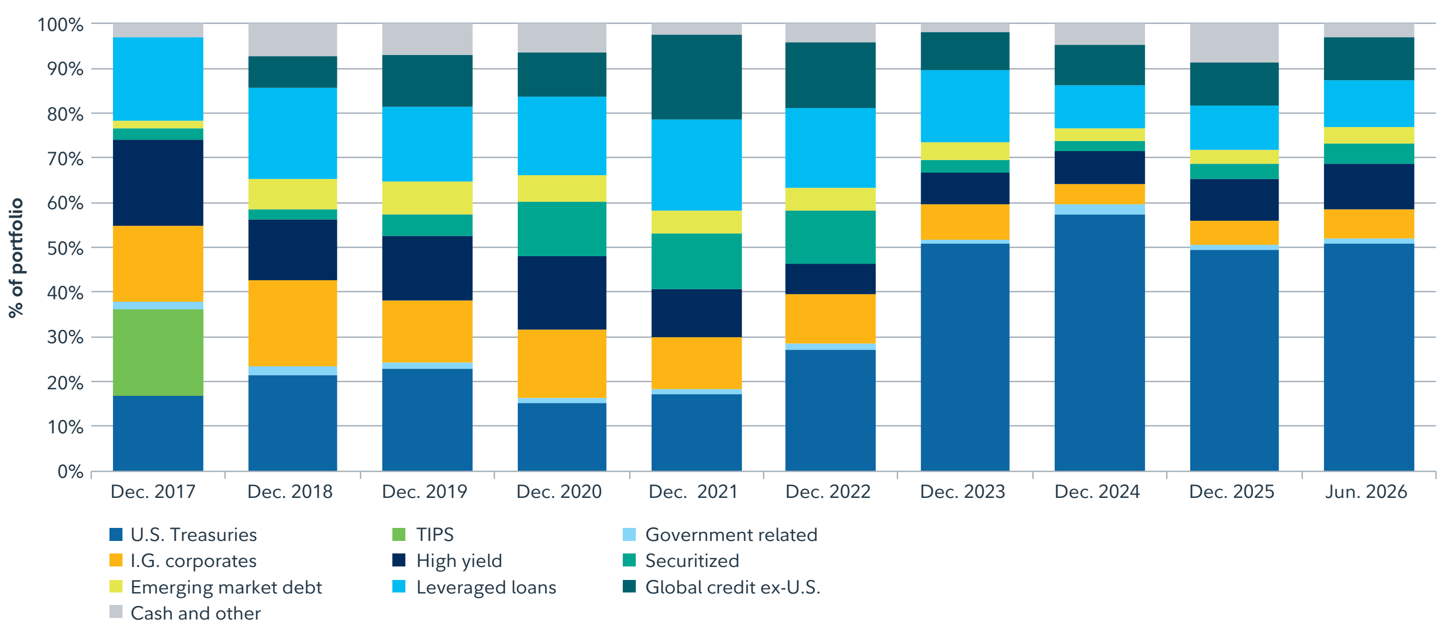
Performance (%)

As at July 31, 2026	3-month	YTD	1-year	2-year	3-year	5-year	Since inception*
Fidelity Multi-Sector Bond CN Fund – Sr. F	-1.0	-1.2	1.0	1.5	2.6	-0.3	1.8
Fidelity Investment Grade Total Bond CN Fund – Sr. F	-1.0	-1.1	1.0	1.6	2.7	-0.7	1.3
Fidelity Global Core Plus Bond ETF	-1.0	-1.0	1.0	1.7	2.9	0.0	1.0
Fidelity Global Investment Grade Bond ETF	-0.9	-0.9	1.1	1.6	2.6	-0.8	0.1
Fidelity Tactical Credit Fund – Sr. F	-0.1	0.5	2.6	3.4	4.6	-	2.9

Source: Fidelity Investments Canada ULC. Performance shows annual compounded returns as at July 31, 2026, net of fees, in Canadian dollars.

* Since-inception date for Fidelity Multi-Sector Bond Currency Neutral Fund is May 10, 2017. Since-inception date for Fidelity Investment Grade Total Bond Currency Neutral Fund is January 24, 2018. Since-inception date for Fidelity Global Core Plus Bond ETF is September 20, 2019. Since-inception date for Fidelity Global Investment Grade Bond ETF is June 5, 2020. Since-inception date for Fidelity Tactical Credit Fund is January 25, 2022.

A flexible approach to fixed income: Fidelity Multi-Sector Bond Fund historical exposure



Source: Fidelity Investments Canada ULC. As at June 30, 2026. Benchmark: Bloomberg U.S. Aggregate Bond Index.

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