

Macro Uncertainty's Economic Effects

WEEKLY VIEW FROM THE DESK | May 11, 2026

[LINK TO WEEKLY RETURNS TABLE](#)

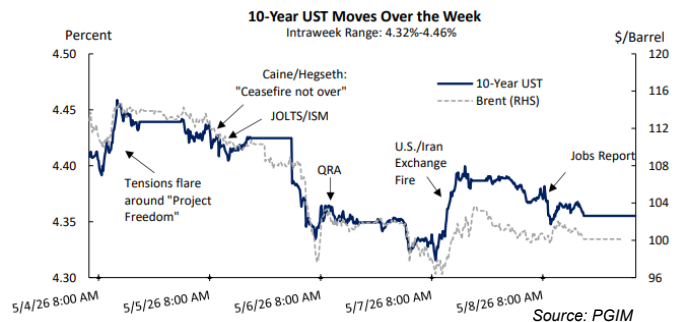
MACRO

- As we consider the broad macro uncertainty stemming from the Middle East and the rapid evolution of artificial intelligence, we see three factors—fiscal support, investments in the AI buildout, and continued strength amongst upper-income households—supporting U.S. growth. Over the next 12 months, we see U.S. growth coming in above trend at 2.5%+ along with sticky inflation (see more below). In the event that the inflation trajectory turns lower, potential monetary policy easing through Q1 could support our “overheating” base case (40% probability). The tails risks around the base case remain thick, and—given the shifting narratives that could indicate a prolonged conflict—we shifted 5 percentage points (pp) from our Muddle Through scenario (now 15%) to our Mild Stagflation scenario (15%).
- The April CPI report showed another high print for headline inflation, which increased +0.64% m/m. Energy-related inflation rose 3.8%, which was high but also down notably from the 10.9% expansion in March. On a y/y basis, headline CPI inflation expanded 3.8%—the fastest pace since mid-2023. Core CPI came in at +0.38% m/m—above the recent run rate of around 0.25% per month—and 2.8% y/y. While the headline figures were a tad firmer than expected, on net this was largely positive news for core inflation: oil pass-through looks limited and tariff pressures are mostly complete. However, the persistent strength in non-shelter services inflation continues to be a concern, and the longer the oil shock continues, the higher the risk that energy pressures can spill into non-energy prices. All told, we remain cautious and still see risks as tilted to the upside.
- Europe is in a relatively more vulnerable position, hence, the energy shock may translate into weaker activity, which explains the 5 pp shift from our Overheating scenario (now 15%) to Mild Stagflation (20%). Our Euro Area base case remains a Muddle Through (40%) scenario as fiscal support is expected to maintain a floor under growth, especially in Germany where government spending is expected to account for most of the growth. However, regulatory and planning bottlenecks are restraining the fiscal multipliers.
- Elsewhere, we expect China to meet its growth target, although possibly toward the lower end of its range, which is reflected in the 5 pp probability reduction in our Soft Landing base case (now 55%). We expect infrastructure upgrades, AI-related capex, and continued strength in advanced manufacturing and emerging sectors to support growth. We shifted the 5 pp to our Mild Stagflation scenario, reflecting sensitivity to the oil price shock. We believe China can manage oil prices of less than \$100/barrel using policy tools, but the risk of demand destruction rises meaningfully if oil prices are sustained around \$130-\$140/barrel.
- Our market-related base case assumes a gradual reopening of the Strait of Hormuz where Brent prices remain in a \$80-\$100/barrel range. As such, risk assets are pricing in strong growth while trading lightly on the inflation front. Indeed, the accompanying chart indicates that short-term inflation readings have surged, while 5-year, 5-year forwards remain relatively flat.



DEVELOPED MARKET RATES

- At this point, the rates markets appear to be more sensitive to movements in oil prices as they continue to generally move in tandem (see accompanying chart). However, the marginal retracement in oil prices failed to keep pace with the rally in risk assets, indicating that the inflation risk may be underappreciated.
- At this point, markets are pricing in the prospect of only limited rate cuts through year end. In addition to the April CPI report, the inflation uncertainty is also reflected in the internal divisions at the Fed as reflected by handful of dissents at the prior FOMC meeting.
- In MBS, mortgages fully reversed the post February cheapening, led by higher coupons, with OAS back to levels last seen in 2022. Current valuations reflect optimism around Iran de escalation, muted origination, slower prepayments, and yield-driven demand. At this point, we recommend trimming MBS exposure at the sector level, particularly in production and premium coupons (5s and higher), and we prefer waiting for a better entry point later.



IG CORPORATES

- Year-to-date issuance from the hyperscalers has already exceeded last year's full year total, with additional supply coming from data center issuers. The issuance includes a disproportionate share of long-duration issuance, heavily influencing index duration, and the heavy supply has prompted underperformance of hyperscaler bonds versus other high-quality industrials. These large issuers now represent meaningful index weights.
- The first quarter saw the largest amount of global M&A on record, with M&A new issue supply +50% YoY to \$105B in the quarter. Likewise, the first quarter brought a new record in share buybacks, with the market on track for \$1T in buybacks this year.

- In Europe, positives are limited, but the economy has held up so far, corporate fundamentals are solid, and corporate earnings remain strong, enabling yield buyers to support the asset class.

LEVERAGED FINANCE

- Despite a seemingly-endless flood of geopolitical headlines, spreads are approximately 65 bps tighter since March 30th and are now only 20 bps off the tight post-GFC—the technical strength of the market and underlying solid credit fundamentals have managed to offset an uncertain macro outlook that is further clouded by U.S.-Iran hostilities and elevated oil prices.
- Capital markets are functioning well, with QTD U.S. HY gross issuance of \$56B and many order books still oversubscribed by ~3-5x. Cash remains available on the sidelines capable of buying dips, although it is worth noting that the QTD supply surplus of \$33B is the first notable inflection in this technical since 2020, led by both AI-driven HY issuance and IG fallen angels.
- From a total return perspective, all credit tiers are positive so far in Q2: BBs have returned +1.68%, Bs have returned +2.08%, and CCCs have returned +2.58%. Total sector returns are mixed thus far in Q2. The top sectors are auto (+2.88%), super retail (+2.69%), and media (+2.53%). The weakest sectors are paper (-3.35%), cable (-0.81%), and food & drug retail (+0.60%).
- U.S. bank loans saw another positive week, with spreads tightening to a 2.5-month low and the percent of loans bid above par increasing to nearly 50% of the index amid solid earnings and inflows. In terms of issuance, \$23B of loans priced last week. Meanwhile loan funds reported inflows of \$844M, the largest weekly inflow in 16 weeks.
- European high yield bond spreads have continued to tighten, leaving them only modestly wider for the year. Issuance of €19.6B thus far in Q2 is 10% higher than the same period last year and heavily weighted to refinancing activity. Loan spreads have tightened thus far in Q2, with higher quality remaining well bid while distressed issuers continue to lag. Loan issuance of €4.9B thus far in Q2 is down 65% YoY and down 48% YTD.

EMERGING MARKETS

- As we move closer to mid-year, EM hard currency sovereign spreads are at YTD and post-GFC tightness. We note that tight spreads do not mean rich spreads. Tight spreads combined with unresolved risks call for deliberate positioning and a thorough examination of both the current backdrop as well as anticipating the downstream impacts from what is now an 11-week war and counting. Country dynamics, less so market beta, will likely be the main driver of performance for the rest of the year.
- Similarly, the EMFX short-term outlook depends on the evolution of U.S.-Iran and Strait of Hormuz dynamics. Performance across currencies has been driven by the price of oil and, by and large, oil exporters have outperformed. However, despite oil being \$30 higher since the conflict, even some oil importer currencies have nearly recovered their conflict losses (CEE3, EUR). Observing this, we conclude that USD is trading rather poorly since it is an energy exporter and the growth impact is less than many other parts of the world. One factor that we are watching closely is the nascent recovery in the U.S. labor market that can potentially prompt the Fed to shift from a neutral to hawkish bias, which could have implications for USD.
- The correlation of EM rates to crude prices remains very high, and pricing of monetary tightening in the future continues to swing big as headlines surface. Liquidity in rate markets remains very poor with wide bid and offer. EM central banks' policy response function depends on the second-order effects on inflation from supply-chain disruption caused by the war. So far, only the Philippines Central Bank has raised rates, and two central banks (Brazil and Mexico) have cut rates, although with a caution. Our base case is we have seen the worst of this crisis (a peak in oil prices). However, EM curves are still pricing aggressive tightening.
- With spreads at post-GFC tightness of 220 bps but yields still a reasonable 6% for an average IG-rated asset class, technicals in EM corporates are supportive and books have been building up strongly for new issues, including crossover demand given the yield pickup to developed markets. We are in the thick of earnings season, and industries like oil & gas, commodities, and chemicals are doing well. Some issuers in consumer, pulp & paper, manufacturing, and retail etc. have been negatively impacted by higher input costs and logistical challenges, but it has been manageable from a credit perspective given the strong starting point of fundamentals.

SECURITIZED PRODUCTS

- In CMBS, valuations for most property types have stabilized and we expect 2026 price appreciation to be marginally positive across property types. Near-term rent growth should improve as new supply pressures abate in property sectors such as multifamily and industrial. We continue to find value in high-quality SASB deals with significant structural protection from moderating real estate fundamentals. Conduit AAA spreads screen as fair to corporate bonds.
- In RMBS, relatively tight inventories and strong demographics have supported housing values despite historically high mortgage rates. Recent supply uptick and regional softness in sunbelt and western MSAs show growing regional divergence. We expect +1% HPA for FY 2026. Non-QM is currently the most scalable opportunity to gain exposure to mortgage credit where we are focused on high-credit mortgages across favored doc types, with investor loans featuring embedded prepay penalty protections among the most attractive.
- CLO tranches continue to offer attractive value versus other fixed income assets. Given current market valuations, we find the most value in senior tranches, with selective opportunities in higher-quality mezzanine tranches. Spreads remain inside long-term averages but marginally wide of YTD tightness. Although pockets of demand have developed, we do not expect spreads to move uniformly tighter and see potential for broader widening, resulting in mixed near-term valuations and selective entry points.
- Global ABS valuations appear full relative to other securitized products sectors. We remain positioned towards top-tier originators and thematically favor commercial obligor exposures for diversification, bank originated collateral, defined versus general corporate purpose consumer loans, and short-dated maturity consumer loans.

MUNICIPALS

- Muni performance remains strong YTD, with the sector largely outperforming other fixed income asset classes (mostly recapturing underperformance from last year). Supply continues to run 5-10% above record 2025 levels, though net supply of ~\$31B has been entirely offset by inflows of \$33B YTD.
- Above trend U.S. economic growth, as well as strong capital markets, should continue to support tax collections, benefiting state and local governments. We expect volatility to remain elevated with a new Fed regime, geopolitical risks, and midterms.

THE RETURNS TABLE AS OF MAY 8, 2026

	Duration	YTM	OAS	WTD	Yield / OAS change (bps)				WTD	MTD	Total return (%)		
					MTD	QTD	YTD	Prior year			QTD	YTD	Prior year
Sovereign rates													
U.S. 2-Year	1.88	3.89	---	1	1	9	41	1	0.07	0.07	0.20	0.43	3.36
U.S. 5-Year	4.47	4.00	---	-1	0	6	28	2	0.13	0.12	0.09	0.08	3.74
U.S. 10-Year	7.86	4.36	---	-2	-2	4	19	-2	0.22	0.30	0.09	-0.02	4.56
U.S. 10-Year Breakeven	--	2.46	---	-4	-3	15	21	15	---	---	---	---	---
U.S. 10-Year TIPS	4.37	1.89	---	2	1	-12	-1	-17	0.08	0.43	1.95	1.88	6.95
U.S. 20-Year	12.55	4.92	---	-4	-4	1	13	5	0.48	0.74	0.19	-0.08	3.54
U.S. 30-Year	15.43	4.94	---	-3	-3	2	9	9	0.46	0.78	-0.10	0.20	2.93
U.S. SOFR	---	---	---	-4	-6	-8	-27	-69	0.07	0.08	0.39	1.31	4.14
UK 10-Year	7.49	4.91	---	-5	-10	0	44	37	0.41	0.77	0.54	-0.96	2.40
Germany 10-Year	8.30	3.00	---	-3	-3	0	15	47	0.32	0.33	0.37	0.04	-0.51
Switzerland 10-Year	8.87	0.36	---	-2	-2	2	8	11	0.16	0.16	-0.16	-0.35	-0.53
Japan 10-Year	7.87	2.47	---	-3	-4	13	41	115	0.29	0.37	-0.57	-1.96	-6.34
Australia 10-Year	7.85	4.99	---	-3	-8	1	25	75	0.33	0.65	0.46	-0.16	-0.90
Canada 10-Year	8.01	3.47	---	-5	-7	0	4	27	0.48	0.60	0.35	0.86	1.80
Major fixed income multi-sector indices YTW													
Global Aggregate Unhedged	6.33	3.76	27	-1	-1	-5	-1	-10	0.36	0.56	1.81	0.72	4.02
Global Aggregate Hedged	6.33	3.76	27	-1	-1	-5	-1	-10	0.30	0.39	0.69	0.53	3.73
U.S. Aggregate	6.00	4.59	26	0	0	-5	-1	-12	0.26	0.37	0.49	0.44	5.53
Euro-Aggregate (Unhedged)	6.31	3.24	43	-3	-2	-8	0	-16	0.41	0.41	0.87	0.22	0.91
Japanese Aggregate	8.02	2.22	0	0	0	0	0	0	0.14	0.29	-0.37	-1.96	-5.83
Major fixed income credit indices YTW													
Mortgage-Backed (Agency)	5.45	4.82	19	0	-1	-5	-3	-21	0.30	0.45	0.52	0.92	7.09
Global IG Corporate Bonds	6.01	4.66	81	-1	-1	-12	1	-24	0.34	0.55	1.83	0.54	6.67
U.S. IG Corporate Bonds	6.96	5.10	77	-2	-1	-11	0	-22	0.38	0.52	0.98	0.44	6.74
European IG Corporate	4.62	3.53	81	-1	-1	-16	3	-27	0.30	0.30	1.24	0.24	2.27
U.S. High Yield Bonds	3.21	6.94	266	2	-2	-51	0	-76	0.05	0.18	1.88	1.37	8.48
European High Yield Bonds	3.15	5.81	290	-8	-7	-57	9	-74	0.49	0.49	2.42	0.88	4.65
U.S. Leveraged Loans	0.3	8.72	480	-6	-8	-34	25	-12	0.25	0.27	1.50	1.02	5.86
European Leveraged Loans	0.3	7.78	476	-4	-9	-61	2	-11	0.23	0.24	1.96	1.13	4.16
EM Hard Currency Sovereigns	6.39	6.86	238	-6	-10	-51	-16	-107	0.53	0.83	3.71	2.39	14.56
EM Corporates	4.42	6.44	221	-1	-2	-27	-16	-58	0.25	0.31	1.93	1.72	8.62
EM Currencies	---	5.84	---	-1	-1	-2	0	0	1.06	1.07	3.49	2.72	8.59
EM Local Rates	5.27	6.19	6	0	0	0	0	0	0.40	0.40	1.44	0.30	5.48
CMBS	3.75	4.68	66	-1	-1	-5	-9	-27	0.18	0.24	0.41	0.73	5.75
ABS	2.82	4.44	48	-1	-1	-4	-4	-21	0.14	0.18	0.47	0.79	5.09
CLOs	4.01	5.00	128	-1	-1	-6	-3	-16	0.13	0.15	0.69	1.72	5.55
Municipal Bonds	6.17	3.66	---	-2	-2	-11	7	-37	0.20	0.21	1.36	1.18	6.34

	Total return (%)						Change (%)						
	Level	WTD	MTD	QTD	YTD	Prior year	Spot	WTD	MTD	QTD	YTD	Prior year	
Equity / volatility indices													
S&P 500 Index	7,399	2.4	2.7	13.4	8.5	32.3	FX / commodities						
DAX	24,339	0.2	0.2	7.3	-0.6	4.2	EUR / USD	1.2	0.6	0.5	2.0	0.3	5.0
Stoxx 600	612	0.3	0.4	6.0	5.1	18.1	USD / JPY	156.7	-0.2	0.1	-1.3	0.0	7.4
Nikkei 225	62,714	5.4	5.8	22.8	25.5	72.8	GBP / USD	1.4	0.4	0.2	3.1	1.2	2.9
Shanghai Composite	4,180	1.7	1.7	7.4	5.5	27.9	EUR / CHF	0.9	0.0	-0.2	-1.0	-1.7	-2.1
MSCI ACWI Index	1,106	2.4	2.7	13.2	9.7	33.1	USD / CHF	0.8	-0.7	-0.6	-2.9	-2.0	-6.6
FTSE 100	10,233	-1.2	-1.4	0.9	4.4	23.8	USD (DXY)	97.9	-0.3	-0.2	-2.1	-0.4	-2.7
MOVE Index	67	-4.5	-6.7	-30.0	5.1	-31.8	Oil	95.4	-6.4	-9.2	-5.9	66.2	59.3
VIX Index	17	1.2	1.8	-31.9	15.0	-23.5	Gold	4715.3	2.2	2.1	1.0	9.2	42.6

Past performance is not a guarantee or a reliable indicator of future results. Sources: Bloomberg except EMD (J.P. Morgan), HY (ICE BofAML), Bank Loans (S&P), and CLOs (Palmer Square). European returns are unhedged in euros unless otherwise indicated. An investment cannot be made directly in an index.

NOTICE: IMPORTANT INFORMATION

Source(s) of data (unless otherwise noted): PGIM as of May 11, 2026.

For Professional or Institutional Investors only. All investments involve risk, including the possible loss of capital.

PGIM is the principal asset management business of Prudential Financial, Inc. (PFI), and a trading name of PGIM, Inc. and its global subsidiaries and affiliates. PGIM, Inc. is an investment adviser registered with the U.S. Securities and Exchange Commission (SEC). Registration with the SEC does not imply a certain level of skill or training.

This material is provided for informational purposes only and is not intended as investment advice or a recommendation, nor is it a solicitation. Views and opinions expressed may not reflect PGIM's and are subject to change.

Any forecasts or forward-looking statements are subject to uncertainty and are not guarantees of future results. Past performance is not a reliable indicator of future results. An investment cannot be made directly in an index. References to specific trades or positions reflect PGIM's portfolio management activity and are not recommendations for individual investors.

Please refer to the Terms and Conditions on www.pgim.com for important information.

PFI is not affiliated in any manner with Prudential plc, incorporated in the United Kingdom, or with Prudential Assurance Company, a subsidiary of M&G plc, incorporated in the United Kingdom.

© 2026 PFI and its related entities.

5481445