

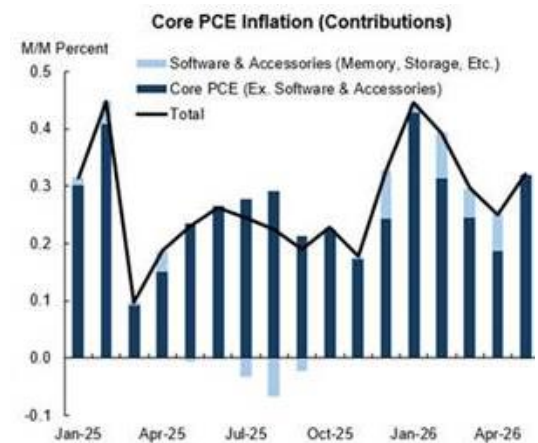
The Underappreciated AI Risk

WEEKLY VIEW FROM THE DESK | June 29, 2026

[LINK TO WEEKLY RETURNS TABLE](#)

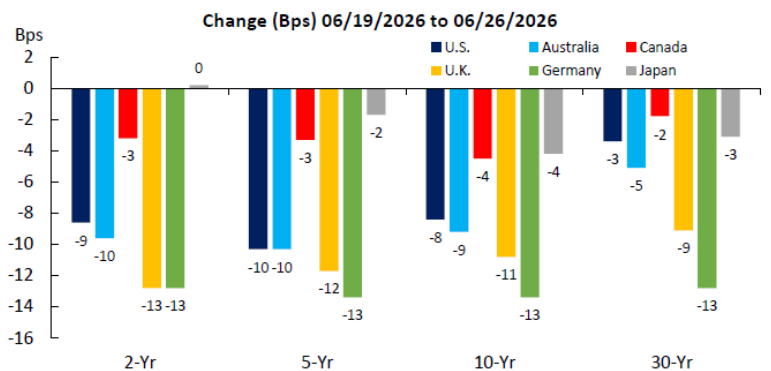
MACRO

- The market performance over the first half of 2026 reiterates the macro tailwinds that we referenced in our [Mid-Year Outlook](#) and that the right tail of the probability distribution—primarily driven by the AI-investment boom—remains in charge. However, the tailwinds are also subject to risks, with two of the more prominent being concentration and backlash risks. For example, AI-related investments account for anywhere between 50-75% of the U.S. GDP growth impulse through capex and the downstream effects on consumption.
- AI-driven inflation effects are another channel to watch. The software and accessories component of the PCE inflation report, while small, has increased significantly in price and is making a material contribution to core PCE inflation (see accompanying chart).
- Yet, we see the backlash against AI as perhaps the more underappreciated risk. Indeed, more than 70% of Americans surveyed in a recent Gallup poll oppose building a datacenter in their community, and \$130B in datacenter projects were reportedly blocked or stalled in Q1 2026 alone.
- AI will be a prominent issue in the upcoming midterm elections as 40 out of 69 competitive House districts have data centers planned or under construction. Another critical decision looms in New York with legislation that could impose a one-year moratorium on data center construction—the first of its kind in the country—and Governor Hochul is expected to make a decision by December 31, 2026.
- In addition to possible developments around the midterms and in New York, there is also the potential for antitrust or regulatory action towards large AI-related firms. We will also be monitoring for potential capex discipline from the hyperscalers in their Q3 reports.
- Shifting to broad positioning comments, directional rate views in both DMs and EMs remain challenged by the cross-currents of lower oil prices and a hawkish Fed. We continue to favor carry and selective opportunities in credit, flatter U.S. yield curves, paying U.S. rates versus Europe, and USD appreciation against major currencies.



DEVELOPED MARKET RATES

- Following a string of strong U.S. data reports and Kevin Warsh's first meeting as Fed chair, the markets appear braced for a modest rate hiking cycle. The upside risk in rates is if payroll growth continues and/or strengthens from here, and that risk would likely be concentrated at the front of the yield curve. After all, the market appears confident in the Fed's long-term inflation control, which could keep long rates stable to lower, supporting a flatter yield curve dynamic.
- Agency MBS spreads tightened modestly last week, benefiting from stable/range-bound Treasury yields, lower rate volatility, and limited new-issue supply. Furthermore, the 10-year Treasury yield moving below roughly 4.40% is supportive as it reduces convexity-related selling pressure.



Source: PGIM

IG CORPORATES

- Last week saw \$50B in new issuance, in line with expectations, with deals 3.2X oversubscribed. June will see more than \$200B in new issuance, a record for the month and well above estimates of about \$130B-\$150B. July estimates call for new issuance of about \$150B, also well above the average of \$110B.
- A tech-led selloff weighed on IG, with the Nasdaq Composite off 4% for the week. The SpaceX \$25B new deal has been an underperformer, something to watch as the company is likely to be back in the market frequently to support its ambitious growth goals.
- In Europe, continued lower oil prices have provided a reprieve for European rates, with 10-year bunds falling below 2.9% for the first time since early March. Despite the positive sentiment, continued supply and already tight spreads saw EUR IG spreads 2bps wider.

LEVERAGED FINANCE

- U.S. high yield spreads widened and yields increased last week, with lower quality, higher-beta names underperforming. Despite the volatility, capital markets remained active and are driving trading activity. Buyers continue to step in on weakness to buy higher-quality names, demonstrating that the technical is still healthy and investors have cash to put to work.

- Total returns were mixed across high yield sectors, with paper (0.49%), air transportation (0.46%), and consumer products (0.32%) performing the best. The three worst performing sectors were technology (-0.61%), telecom (-0.46%), and chemicals (-0.31%). High yield bond funds reported inflows totaling +\$287M, the tenth inflow in twelve weeks. Fourteen high yield bond deals priced for \$7.7B, with notable deals from Core & Main (\$750M 6% '34s), Starwood (\$500M 5.875% '29s), Amex GBT (\$1B 7.625% '33s), Oceaneering (\$500M 6.875% '34s), Yondr (\$715M 6.875% '31s) and GFL Environmental (\$750M 5.625% '31s). Year to date, HY volume totals \$186.0B, or \$81.5 ex-refi.
- U.S. bank loans posted negative returns last week amid heavy new issuance and some sector concerns. We finished the week with the lowest percentage of loans bid above par in two months at about 20% of the market. The financials and software sectors were both weaker, down 1-2 points generally. This week has seen slower new issuance thus far which, along with some paydowns, should help technicals.
- European high yield bond spreads were slightly wider last week. About €5.4B in issuance priced. However, just €1.4B of that was new money, which was easily absorbed by the market. In loans, 14 deals priced for about €15B, but just approximately €2B of that was new money.

EMERGING MARKETS

- EM sovereign spreads were wider last week on Treasury moves, oil prices, and moderation on the larger macro sentiment. Spreads widened across all rating categories, but there was clear credit decompression, particularly in single-B, CCC, and defaulted names. This is partly a function of oil price “leverage” for lower-rated EM sovereigns, but also due to country-specific factors. There was generous supply last week across sovereigns and corporates. Spreads are tight, and investors respect how well EM spreads have held up. It is still unclear what the next 60 days will look like and where oil prices will settle. Unless global conditions tighten considerably, or there is a dramatic move in oil prices, EM spread assets should broadly remain range bound.
- EM corporate spreads widened last week as some high-cost oil producers like Tullow and Kos were under pressure. Orbia bonds rallied after the company told investors that they will raise \$1B through asset sales and reduce debt. New World bonds also rallied on reports the company is considering a rights issue. Vedanta priced a \$1.75B three-tranche deal, which traded down 1 point on the break but saw some buying on Friday. Braskem entered mediation proceedings in Brazil and filed Chapter 15 in the U.S., which was not a total surprise but bonds initially corrected and then recovered.
- In EM rates, Brazil, Turkey, Poland, and Hungary were the biggest outperformers last week. In the swap space, 5-years outperformed the curve in most countries. We made changes to the portfolio by cutting our underweight in Thailand and Poland; adding to our overweight in Hungary, Colombia and Mexico; and increasing our underweight in the front end of South Africa. We also added to steepeners in Brazil. Our top-down view is that a tug-of-war between oil and U.S. rates is likely to remain the main driver for EMFX and rates. With oil prices back to February levels, we expect EM rates to trade better in the coming weeks. Risks to this constructive outlook could come from two sources: if the U.S.-Iran talks fall apart or if a further surge in U.S. inflation leads the Fed to hike earlier than market expectations.
- The EMFX index fell with performance broadly similar across regions. Signs of a more hawkish Fed have supported the broad dollar, and the currency is reacting more to the tightening spurred by the increase of real yields. With that said, domestic developments continue to be a driving force behind differentiation within regions. For instance, CE3 currencies largely followed the decline in EUR but with a slightly higher beta. We continue to employ relative value of long high yielder versus short low yielder as the largest thematic position, which continues to fare well as long as financial conditions remain loose and growth remains robust. We are becoming more attuned to USD strength on the back of U.S. data resilience and have continued to slowly increase our overall long USD bias against lower-yielding currencies in Europe and Asia.

SECURITIZED PRODUCTS

- CMBS conduit AAA spreads were wider in the primary market last week, with top-tier names pricing at +80. Subordinate tranches were framed 5 bps wider, in the +190 context and BBB-s in the mid to high +400s. SASB spreads tightened on the back of strong new issue demand. Top-tier AAA floaters are clearing in the +130 area. Fixed-rate seniors are trading in the +80s amid increased dispersion by property type and sponsor. CRE CLO spreads were unchanged, with AAA new issue in the +135-140 area, while tier-two issuers were 5-25 bps wider. Five deals priced-two SASB, one conduit, one CRE CLO, and one agency.
- In RMBS, Non-QM AAAs saw a sharp move wider, with first-tier OBX pricing at T+130-about 15 bps wider than last week despite a largely stable broader market. The widening was driven by heavy supply, with seven deals pricing last week and five still in the market. First-tier AAAs are pricing near T+130. Second-lien CES AAAs widened to T+125, roughly 10 bps softer following the Non-QM move. CRT spreads were largely flat last week amid lighter trading volume and no new issuance, holding near the tightness on strong technicals.
- U.S. CLO spreads were generally unchanged despite strong new issuance. The term curve remains flat as investors balance seasoned pools with shorter spread duration. Dispersion in lower mezzanine tranches is growing, driven by differences in portfolio quality and tail-risk exposure. U.S. issuance was \$11.3B across 25 deals and European issuance was €4.8B across 12 deals.
- ABS spreads were flat to tighter on the week. Capital stack compression materialized as below IG bonds outperformed. U.S. and European sectors are at or near YTD tightness. Australia remains an exception at 10-20 bps off the tightness depending on issuer, point in capital stack. Broker dealers remain net sellers, taking advantage of strong demand by end accounts. Balance sheets remain well positioned to provide liquidity in case of any market back-ups.

MUNICIPALS

- Munis underperformed Treasuries on a yield ratio basis on the front end, while outperforming Treasuries on the long end. Munis continue to post strong returns relative to other fixed-income asset classes.
- Positive flows continue with more than \$633M last week and \$45B YTD, the second-highest on record (trailing only 2021). Supply is manageable at ~\$5B for this holiday-shortened week.
- May median state tax collections grew 1.9% year-over-year, led by strong sales tax collections. Separately, Moody's has warned that the data center surge presents risk for states and muni finances, with some states pausing tax credits to reassess the situation.

THE RETURNS TABLE AS OF JUNE 26, 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	1.90	4.09	---	-9	9	30	62	37	0.24	0.13	0.35	0.58	2.75
U.S. 5-Year	4.48	4.13	---	-10	-1	19	40	33	0.52	0.34	0.11	0.11	2.28
U.S. 10-Year	7.91	4.37	---	-8	-7	5	20	13	0.76	0.87	0.64	0.54	3.37
U.S. 10-Year Breakeven	--	2.20	---	-6	-20	-10	-4	-8	---	---	---	---	---
U.S. 10-Year TIPS	4.30	2.16	---	-2	13	15	26	22	0.46	-0.15	1.49	1.42	4.58
U.S. 20-Year	12.50	4.87	---	-5	-10	-5	7	6	0.71	1.78	1.62	1.34	3.69
U.S. 30-Year	15.49	4.87	---	-3	-11	-5	2	6	0.66	2.18	1.78	2.09	3.54
U.S. SOFR	---	---	---	0	-1	-6	-25	-78	0.07	0.28	0.88	1.81	4.05
UK 10-Year	7.39	4.73	---	-11	-8	-18	26	26	0.86	0.91	2.44	0.89	3.09
Germany 10-Year	8.20	2.85	---	-13	-9	-15	0	28	1.01	0.78	1.81	1.47	0.85
Switzerland 10-Year	8.75	0.24	---	-9	-14	-9	-3	-13	0.79	1.05	1.09	0.89	1.63
Japan 10-Year	7.69	2.61	---	-4	-5	26	55	119	0.32	0.46	-0.97	-2.35	-6.20
Australia 10-Year	7.75	4.72	---	-9	-11	-26	-2	61	0.73	1.14	3.09	2.45	0.00
Canada 10-Year	8.39	3.39	---	-1	-3	-9	-5	5	0.37	0.71	1.64	2.16	3.47
Major fixed income multi-sector indices YTW													
Global Aggregate Unhedged	6.31	3.76	27	1	1	-5	0	-5	0.17	-0.59	0.98	-0.10	0.84
Global Aggregate Hedged	6.31	3.76	27	1	1	-5	0	-5	0.50	0.57	1.50	1.34	3.43
U.S. Aggregate	5.98	4.66	26	0	1	-4	-1	-6	0.49	0.60	1.03	0.98	4.31
Euro-Aggregate (Unhedged)	6.29	3.14	44	1	1	-7	1	-9	0.75	0.48	2.01	1.36	1.70
Japanese Aggregate	8.02	2.30	0	0	0	0	0	0	0.34	0.58	-0.67	-2.25	-5.88
Major fixed income credit indices YTW													
Mortgage-Backed (Agency)	5.44	4.89	22	-1	0	-2	0	-12	0.58	0.64	1.01	1.41	5.64
Global IG Corporate Bonds	6.01	4.66	79	2	3	-14	-1	-12	0.25	-0.33	1.57	0.28	3.25
U.S. IG Corporate Bonds	6.94	5.14	75	2	4	-13	-2	-11	0.41	0.51	1.73	1.19	5.00
European IG Corporate	4.60	3.41	80	2	0	-18	1	-15	0.59	0.48	2.39	1.37	2.59
U.S. High Yield Bonds	3.27	7.21	282	16	24	-35	15	-11	-0.06	0.06	2.26	1.75	6.03
European High Yield Bonds	3.05	5.68	289	11	7	-58	8	-43	0.20	0.43	3.31	1.76	4.30
U.S. Leveraged Loans	0.3	9.03	500	11	13	-14	45	37	-0.15	0.05	1.76	1.27	4.40
European Leveraged Loans	0.3	7.78	478	3	3	-59	4	16	0.04	0.30	2.61	1.77	3.43
EM Hard Currency Sovereigns	6.31	6.90	241	12	4	-48	-12	-83	0.08	0.62	4.53	3.31	12.07
EM Corporates	4.35	6.48	221	8	3	-27	-16	-51	0.17	0.47	2.48	2.27	7.04
EM Currencies	---	6.18	---	0	0	-1	0	1	-0.52	-0.98	1.93	1.17	3.77
EM Local Rates	5.26	6.05	6	0	0	0	0	0	0.48	1.15	2.86	1.71	5.69
CMBS	3.71	4.81	65	0	0	-6	-10	-20	0.46	0.37	0.66	0.98	4.22
ABS	2.87	4.59	45	0	-2	-8	-7	-12	0.31	0.33	0.87	1.18	4.18
CLOs	3.92	5.10	128	0	0	-6	-4	-10	0.05	0.33	1.32	2.34	5.19
Municipal Bonds	6.03	3.60	---	-1	-8	-18	0	-38	0.15	0.80	2.33	2.15	6.99

	Total return (%)						Change (%)						
	Level	WTD	MTD	QTD	YTD	Prior year	Spot	WTD	MTD	QTD	YTD	Prior year	
Equity / volatility indices													
S&P 500 Index	7,354	-1.9	-2.9	13.0	8.1	21.2	FX / commodities						
DAX	24,671	-1.3	-1.7	8.8	0.7	4.3	EUR / USD	1.1	-0.8	-2.4	-1.5	-3.1	-2.7
Stoxx 600	636	0.1	1.7	10.8	9.9	22.1	USD / JPY	161.7	0.3	1.6	1.9	3.2	12.0
Nikkei 225	69,361	-2.7	4.6	35.8	38.9	78.4	GBP / USD	1.3	-0.2	-1.9	-0.2	-2.0	-3.8
Shanghai Composite	4,027	-1.3	-0.5	4.3	2.4	19.7	EUR / CHF	0.9	-0.4	1.2	-0.2	-1.0	-1.6
MSCI ACWI Index	1,103	-2.1	-2.4	13.2	9.7	23.3	USD / CHF	0.8	0.3	3.7	1.3	2.2	1.2
FTSE 100	10,508	1.4	1.1	4.1	7.7	24.1	USD (DXY)	101.4	0.5	2.4	1.4	3.1	4.3
MOVE Index	67	2.1	-4.9	-30.5	4.4	-25.3	Oil	69.2	-9.6	-20.8	-31.7	20.6	6.1
VIX Index	18	9.7	20.2	-27.1	23.1	11.0	Gold	4088.7	-1.6	-9.9	-12.4	-5.3	22.9

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.

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Source(s) of data (unless otherwise noted): PGIM as of June 26 2026.

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