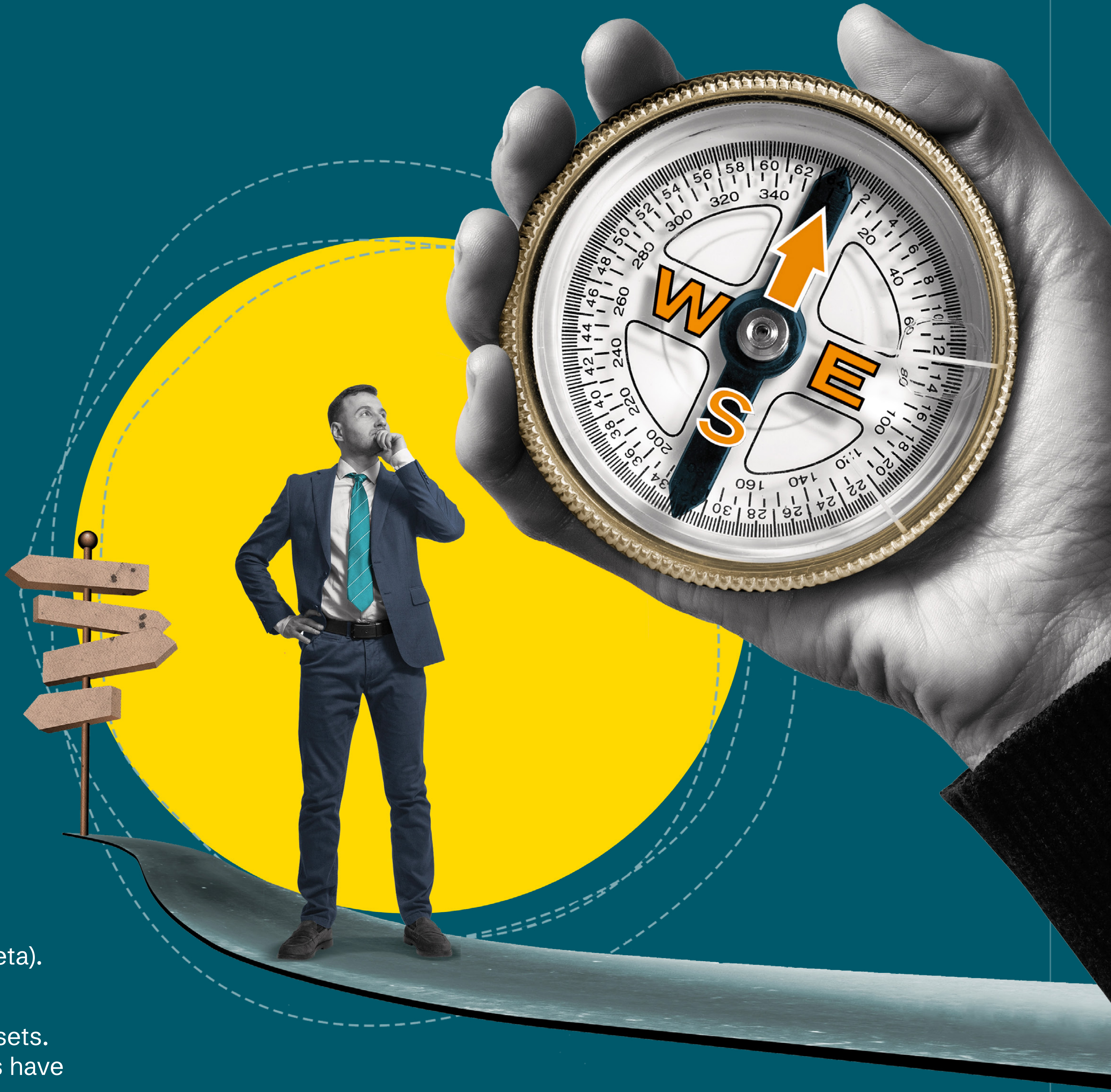
Compass

Each quarter, we plot a course through global fixed income markets by distilling top-down macro perspectives and bottom-up market intelligence into a cohesive outlook. Compass draws on the insights from our “Matrix Pods” - dynamic, cross-functional groups that unite subject matter experts including portfolio managers, strategists, economists and traders.

The latest Compass at a glance:

- **Volatility changes pace**
  Fixed income markets have moved from a phase of acute and indiscriminate disruption to a prolonged phase of re-adjustment.
- **Competing risks**
  Inflation and central bank tightening is the immediate risk, but risks to economic growth pose a longer-term challenge.
- **Carry is still core**
  Despite the turbulence, fundamentals so far remain intact and carry remains the driver of fixed income returns.
- **Protection and selection**
  Investors should focus on selection for credit quality and resilience rather than exposure to broader market moves (beta).
- **Emerging market opportunities**
  Within EM, the most compelling opportunities are in local assets. Large price adjustments and widespread position reductions have reset valuations, creating attractive opportunities.



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Carry on and focus on fundamentals

This quarter's Compass is published at a time when geopolitics has reasserted itself as a defining feature of the investment landscape.

Fixed income markets were already in the late stage of the credit cycle, but the elevated conflict risk, energy price uncertainty and persistent inflation sensitivities have reinforced that dynamic across markets. In such an environment, the central question is not whether risks exist, but how markets will respond to them. Will they shift abruptly? Or will we see a more prolonged and uneven adjustment?

The view from our most recent round of Matrix Pods is that while downside risks remain firmly present, the balance of probabilities has shifted away from a single, sudden dislocation and towards a period of ongoing volatility and cross-currents.

During the early stage of the recent Middle East conflict, defensive positioning was both prudent and necessary, but as the crisis has continued, the emphasis has moved away from pure protection. This is not complacency, but a reassessment of the speed at which markets are moving. The consensus from our Matrix Pods was that over the weeks ahead there is a reduced likelihood of indiscriminate, rapid widening in spreads and instead a greater emphasis on path dependency, differentiation and income discipline.

In that setting, carry regains relevance, not as a reason to ignore risk, but as reminder that when fundamentals remain broadly intact and an adjustment is taking place over time, elevated all-in yields are still a powerful contributor to overall returns.

Pod discussions across credit, rates, liquidity and emerging markets (EM) have consistently reinforced the importance of selectivity, quality bias and resilience, rather than broad beta exposure (see the Matrix Pod summary table in Figure 1).

Crucially, these views have not been formed as part of a rigidly scheduled process. Several Pods have met ad hoc and out-of-cycle in recent weeks, reflecting the fluidity of events and demonstrating the agility of the Matrix framework: a globally connected group, able to convene quickly, share insight across asset classes and recalibrate assumptions in real time.

That collective advantage is reinforced through our Strategic Hedging, Integrated Exposure and Loss Defence model (SHIELD), which channels Pod insights into creative defensive strategies.

In volatile conditions, protection is not solely about dampening risk, but about maintaining agility — allowing portfolios to remain resilient while retaining the ability to benefit from dislocation whenever volatility becomes a potential source of return.

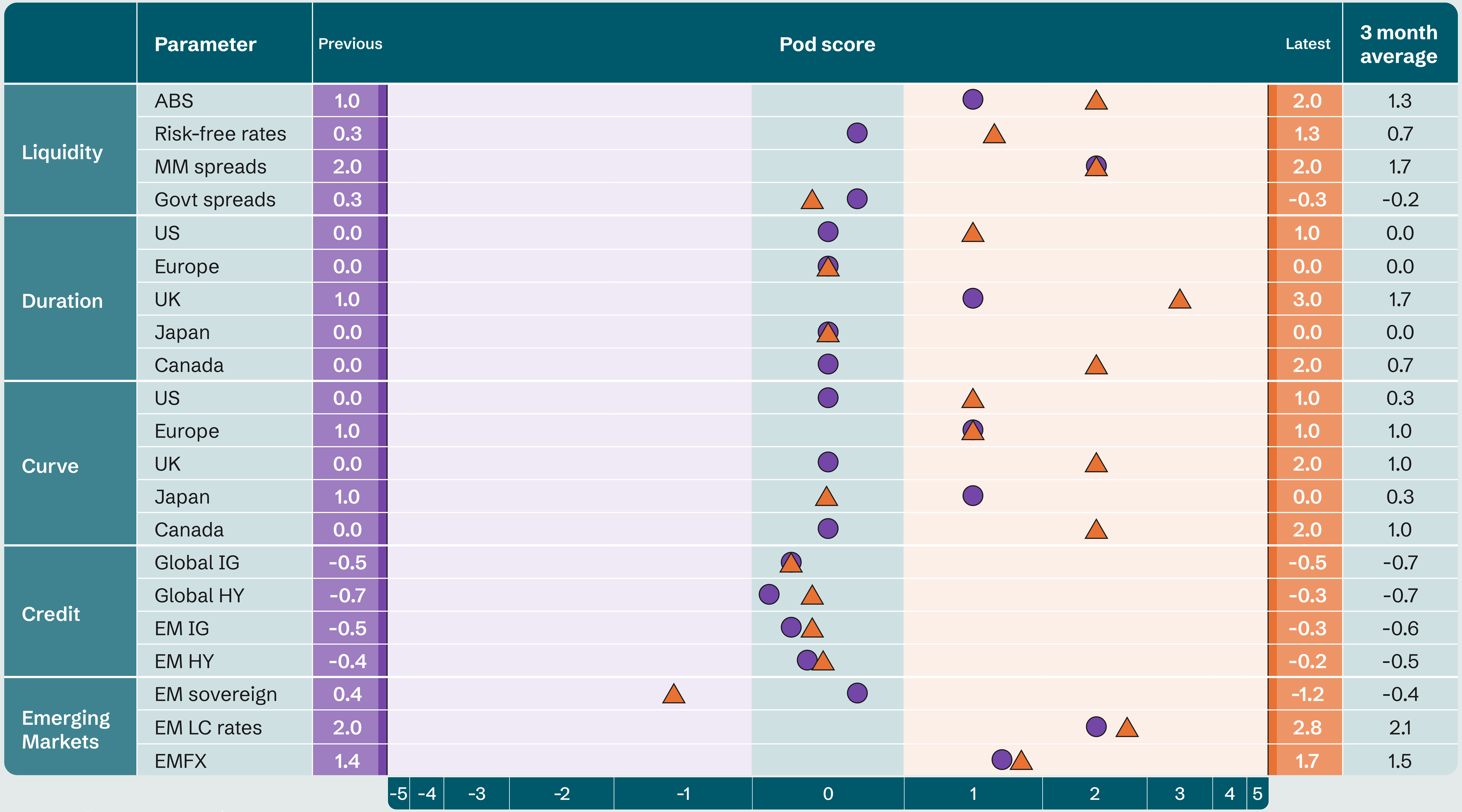
Rarely have flexibility, real-time analysis and insight been so important for fixed income investment.

> "Fixed income markets are undergoing a protracted adjustment to the changed global economic environment. Risks cannot be ignored, but fundamentals are intact. In such an environment, carry will continue to be the workhorse of fixed income investment."

Fraser Lundie Global Head of Fixed Income

Figure 1. **Matrix Pod summary – fixed income allocation overview**

Key: ● Previous ▲ Latest



	Parameter	Previous	Latest	3 month average
Liquidity	ABS	1.0	2.0	1.3
	Risk-free rates	0.3	1.3	0.7
	MM spreads	2.0	2.0	1.7
	Govt spreads	0.3	-0.3	-0.2
Duration	US	0.0	1.0	0.0
	Europe	0.0	0.0	0.0
	UK	1.0	3.0	1.7
	Japan	0.0	0.0	0.0
	Canada	0.0	2.0	0.7
Curve	US	0.0	1.0	0.3
	Europe	1.0	1.0	1.0
	UK	0.0	2.0	1.0
	Japan	1.0	0.0	0.3
	Canada	0.0	2.0	1.0
Credit	Global IG	-0.5	-0.5	-0.7
	Global HY	-0.7	-0.3	-0.7
	EM IG	-0.5	-0.3	-0.6
	EM HY	-0.4	-0.2	-0.5
Emerging Markets	EM sovereign	0.4	-1.2	-0.4
	EM LC rates	2.0	2.8	2.1
	EMFX	1.4	1.7	1.5

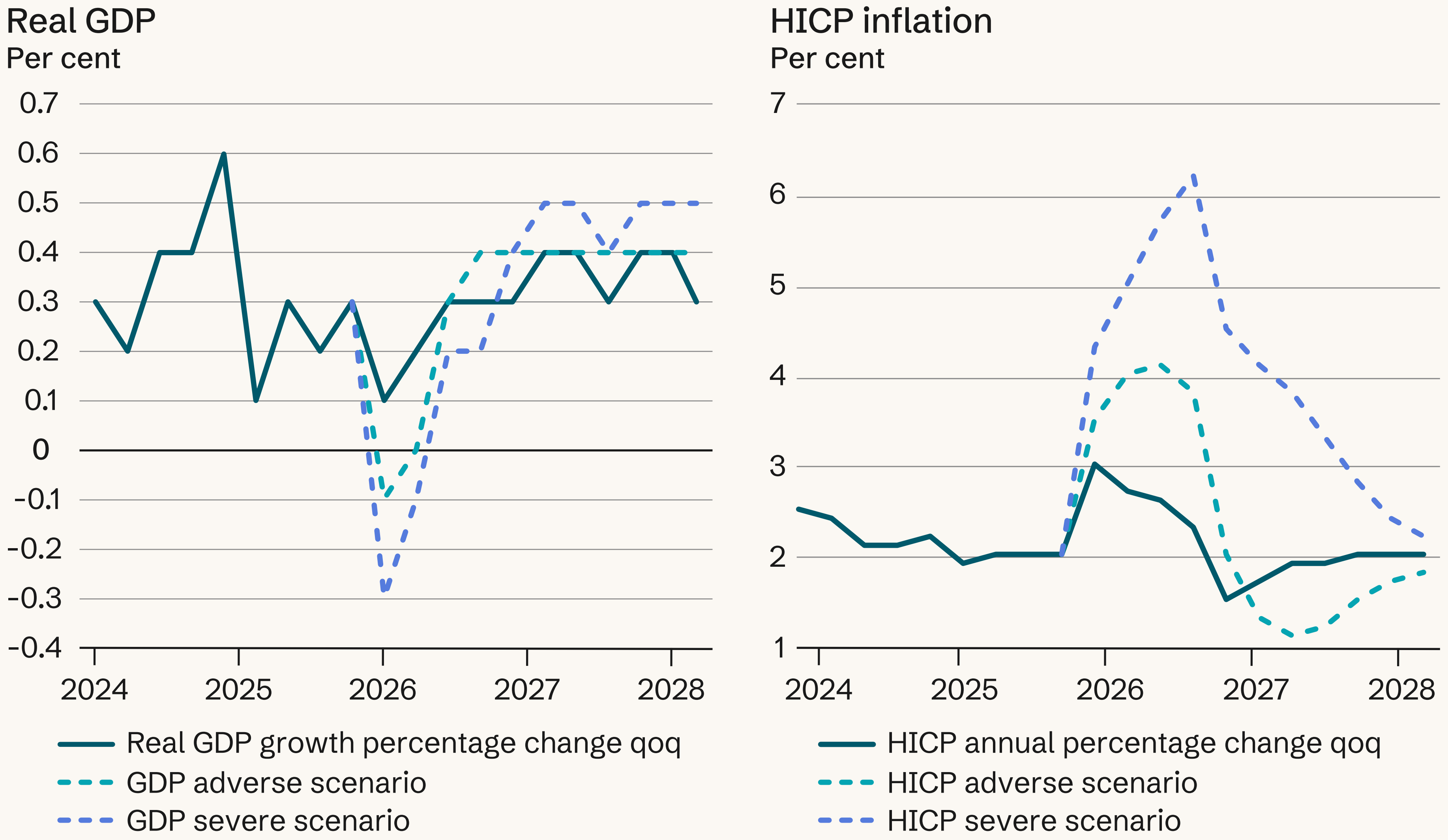
Key: ● Previous ▲ Latest

Note: Duration = A positive score indicates bond yields expected to fall, negative to rise. Curve = A positive score indicates a steeper yield curve expected, negative a flatter curve. The score-band widths proportionally weighted provide a conceptual guide to expected conviction dispersion, not a statistical model. Source: Aviva Investors. Data as of April 2026.

Liquidity Pod:
Selectively bullish

The pod remains selectively bullish, with its strongest conviction in front-end UK rates. Conviction has increased on asset-backed securities (ABS) and money markets but remains mostly neutral on government bonds, apart from a slight bearish stance in the UK. Conviction is low on investment grade (IG) credit and the view on covered bonds continues to be neutral.

Figure 2. **The impact of ECB's alternative scenarios**


Real GDP
Per cent

HICP inflation
Per cent

Past performance is not a reliable indicator of future returns.

Note: GDP data is unadjusted for seasonality. Source: Aviva Investors, ECB staff macroeconomic projections for the euro area, March 2026, as at April 2026.

Macro and rates

We remain bullish on front-end rates in the UK as the state of the economy will likely constrain the number of rate hikes from the Bank of England. In Europe, the ECB's firm inflation mandate supports a neutral to modestly bullish stance. However, under the ECB's "severe" scenario (see Figure 2), downside risks to growth would likely limit meaningful monetary tightening. The Fed's balanced communication and adherence to its dual mandate support the current market pricing that indicates no near-term hikes or cuts in the US (neutral stance).

Money markets

Conviction in money markets is higher, though we remain mindful of the potential for further widening of spreads, as well as some technical factors including reduced excess liquidity and increased participation in ECB open market operations.

Government bonds

Slightly bearish on UK government bond swap spreads, reflecting political uncertainty and upcoming local elections. The view on US Treasuries and bunds remains neutral.

Our slight positive bias in other sovereign, supranational and agency bonds (SSAs) is unchanged from the first quarter, with the view on periphery eurozone government bond spreads becoming less bearish following recent weakness.[1]

Credit and ABS

We have increased conviction on ABS. Prime residential mortgage-backed securities (RMBS) are particularly attractive following spread widening, with stable credit fundamentals, especially in AAA tranches. Our view on IG credit is now slightly bearish as valuations remain tight and structural risks persist, including inflation, private credit growth, and AI-related disruption. We hold a neutral stance on covered bonds – which we see as overvalued relative to other bank capital instruments and ABS.

What this means for positioning and implementation

Amid the recent geopolitical volatility, positioning remains focused on liquidity, using high quality ABS markets and favouring credits with stable fundamentals.

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[1] SSAs: Sub-sovereign, Supranational, and Agency bonds are high-quality, government-related debt securities issued by institutions like the World Bank, European Investment Bank, or government agencies to fund public projects.

Duration and Curve Pod:

Increasing duration

Higher inflation expectations following the energy supply shock from the Gulf conflict have driven markets to reprice policy rates higher. While this response is understandable given elevated uncertainty, we believe current pricing reflects a more severe conflict outcome and underestimates the potential drag on growth from a prolonged disruption. Against this backdrop, we see value in the front end of developed bond markets.

Regional views

US

US moves have been far more contained than other markets. We believe the next rate move is still likely to be a cut and have a bullish view on front-end rates with a steepening bias, but also recognise the potential for fiscal risk premia to be priced back into the curve.

Europe

We have been structurally bearish on Europe given expectations of stronger growth and increased supply. That said, the repricing of rate expectations since the start of the Middle East conflict, appears excessive, and we have moved to a neutral/long view in the front end. We continue to see the curve steepening, driven by both the front end and ongoing higher term premia.

UK

The positive long-duration view we expressed in Q1 has been challenged by the Iran conflict. However, current market pricing of two rate hikes is excessive given the weak state of the economy and the expected growth hit from a prolonged conflict. We maintain a high-conviction, bullish stance.

Japan

We retain our neutral duration and curve view heading into Q2 as the domestic picture is broadly unchanged. With focus firmly on the Middle East conflict, the Bank of Japan (BOJ) is likely to be cautious in the short term given the risks to growth.

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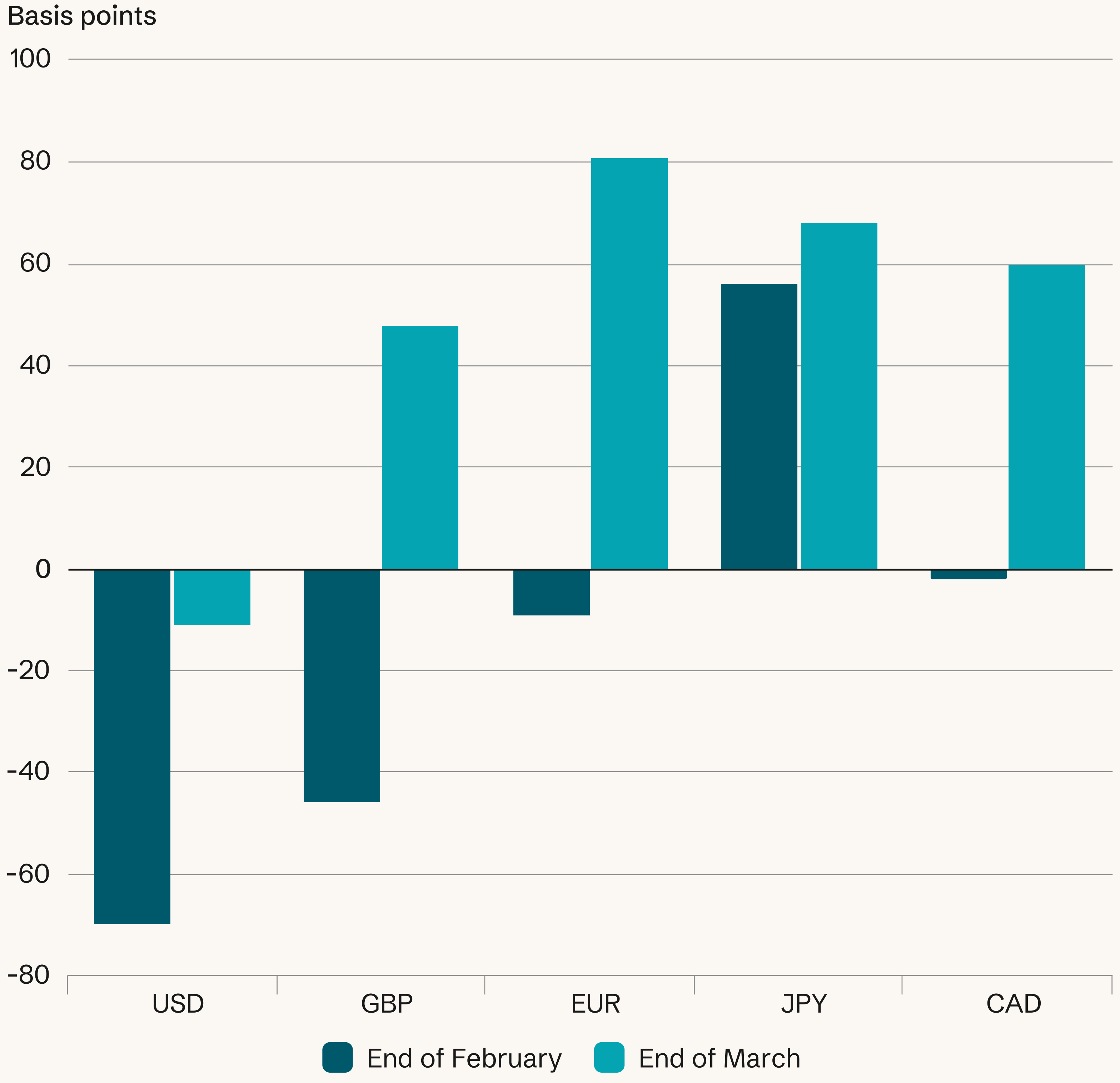
Regional views

Figure 3. **1yr ahead rate expectations since the start of the conflict**



Past performance is not a reliable indicator of future returns.

Source: Aviva Investors, Bloomberg, as at April 14, 2026.

Canada

The pod switched from a neutral to a long duration view in March. Growth weakness heading into the Iran conflict, and the uncertain outlook, is likely to make Bank of Canada cautious in reacting to higher inflation. This backdrop supports our ongoing steepening view and increases our conviction.

What this means for positioning and implementation

We have added to long UK and Canada positions and increased exposure to EU steepening strategies. We have also used the sell-off to close our short US exposure and move to a neutral/long position.

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Credit Pod:

Light beta given downside risks

Our view on credit is broadly one of caution, given that the macro backdrop remains negative and could feed through into fundamentals, and we have a stronger preference for IG versus high yield (HY). Meanwhile, emerging market credit deserves more focus given the secular fundamental improvements in the region.

Macro and fundamentals

Macro developments are a negative factor across the board because of the elevated geopolitical tensions, energy prices, potential second-order inflationary effects and risks to growth. While credit fundamentals remain solid at present, there is a growing expectation that conditions are likely to deteriorate. The timing and pace of any weakening are difficult to predict, so vigilance will be critical.

Valuation and technicals

Credit spreads have recently tightened at a rate that exceeds what underlying fundamentals would justify, amplifying the potential for downside risk. If economic malaise results in a sharp contraction in government bond yields, it may produce a knee-jerk bearish response in credit spreads. Technicals remain positive for IG, however, reflecting a healthy support from buyers for primary issuance thanks to the relatively high all-in yield levels.

Private debt: Evolving risk-adjusted return dynamics

Private debt continues to offer attractive relative value, supported by a higher-for-longer rates environment and elevated illiquidity premia. Across investment grade assets, the illiquidity premia of around 100 basis points (bps) based on our proprietary dataset remains above long-term averages, with spreads tightening less aggressively than in public credit.

In sub-IG grade assets, our proprietary dataset highlights the average illiquidity premia is closer to 300bps, but with more variation across private debt sectors, reflecting both elevated compensation for risk and structurally lower competition from banks and insurers.[2]

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[2] “House View Q2 2026, Market Outlook”, Aviva Investors, April 2026.

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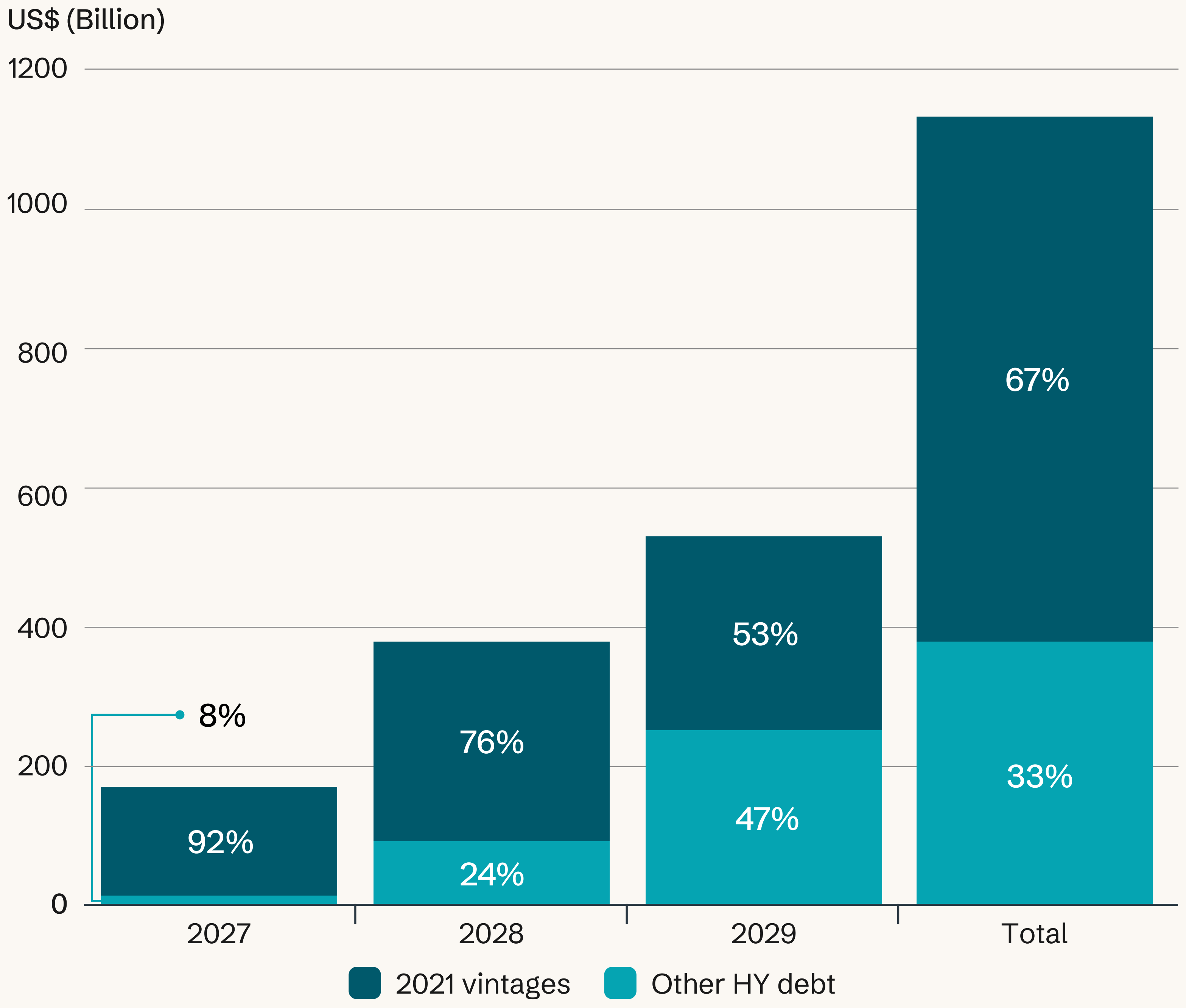
Figure 4. **US high yield - maturity wall for the 2021 vintage**



Note: US corporate high yield debt issued in 2021. Percentages represent the per cent of total in each of the two categories.
Source: Aviva Investors, Bloomberg, as at April 18, 2026.

Asset class views

Global IG

We believe IG remains structurally supported, with limited fundamental downside expected in the near term. The technicals backdrop remains buoyant because of persistent robust demand and attractive yield levels. Even if rates decline, they are unlikely to fall far enough to undermine the technical strength. IG corporates are generally well-hedged against immediate energy cost shocks, while financials, a significant portion of IG indices, are not considered to be at the centre of current turbulence.
In EM, we believe there is too much pessimism around underlying fundamentals, particularly when we compare EM IG with DM IG.

Global HY

HY faces greater vulnerability and potential dispersion in spreads. Uncertainty and heightened sensitivity to macro and growth risks could impact issuers disproportionately and we are likely to see a deterioration in fundamentals for some issuers or at sector level. Technicals remain weak, partly due to a large volume of poorly underwritten debt coming to maturity in a market where investors are becoming more selective (see Figure 4).

What this means for positioning and implementation

The pod will maintain core exposure across portfolios in IG, being more comfortable in carrying beta than in other segments. Given our expectation for modest spread widening, the focus will be on quality, defensiveness, and sectors with strong technicals. Similarly, HY positioning will focus on higher quality, avoid exposure to the credit cycle and look for idiosyncratic opportunities.

Emerging Markets Pod:

Local in focus

We remain constructive on EM local currency debt relative to hard currency credit. Following significant price adjustments, valuations look compelling and provide a cushion against further inflation pressures, leaving a high hurdle for yields to rise meaningfully without renewed FX or credit stress.

Macro and fundamentals

Higher real rates, stronger public finances and balance of payment positions, combined with nimble policy reactions by their central banks have improved the resilience of many EMs. If the Middle East conflict is prolonged, our base case is for greater EM dispersion rather than synchronised stress, with EM countries with strong external balances and policy credibility being better placed.

Valuation and technicals

Real yields in EM local debt sit at the upper end of their historical ranges, providing highly attractive risk premia. This level of compensation materially raises the bar for further upside in yields. Technicals are not providing any strong signals and our view is neutral.

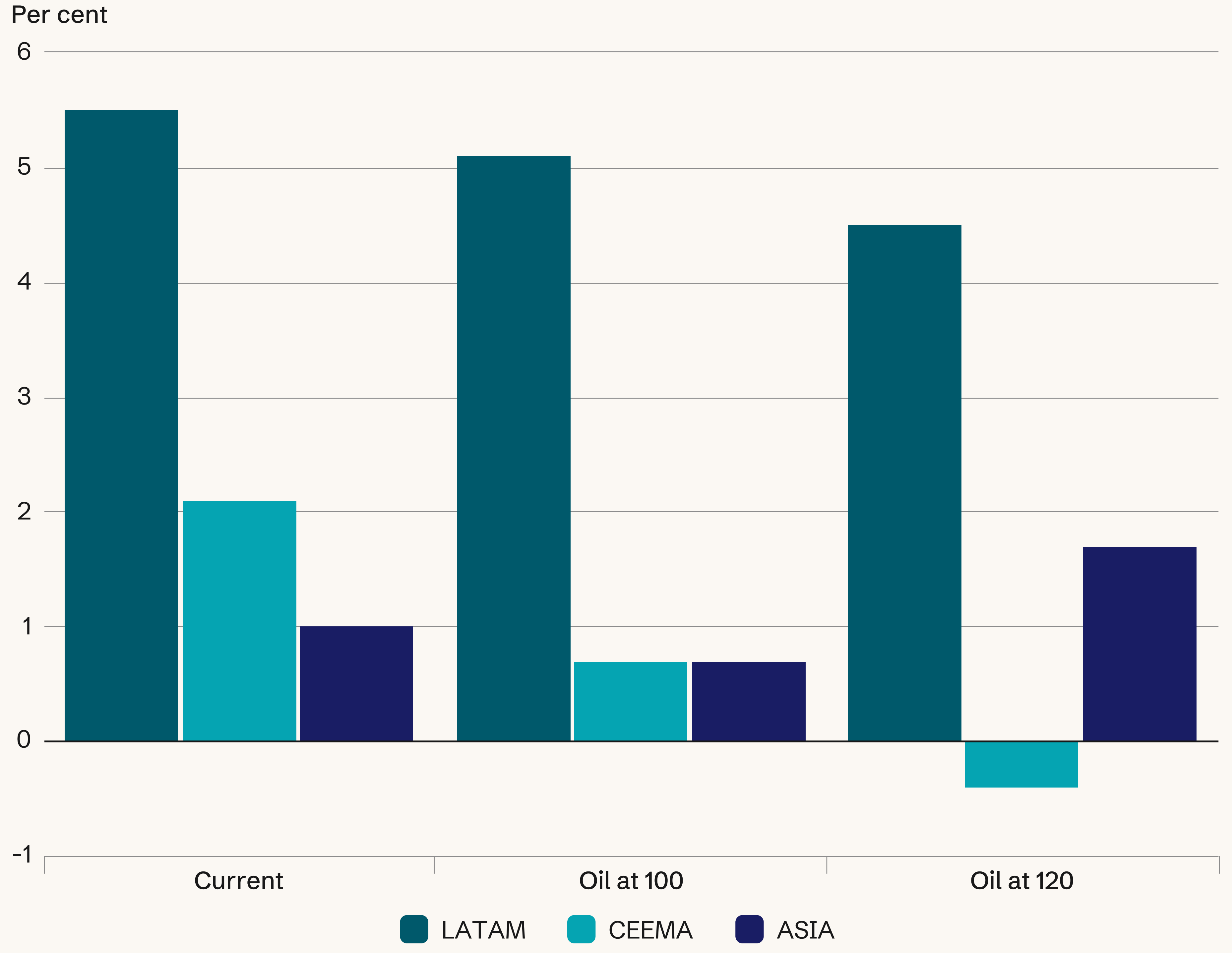


Figure 5. Real policy premiums by region under oil shock scenarios

Past performance is not a reliable indicator of future returns.

Source: Aviva Investors, Bloomberg, as at April 7, 2026.

Asset class views

EM local currency debt

EM local currency markets are supported by attractive real yields and more contained inflation than in past cycles, giving policymakers greater scope for patience even in the face of higher energy prices. With valuations reset after recent volatility and FX increasingly a source of return rather than risk, local markets offer a compelling risk-reward.

EM FX

EM currencies are benefiting from more contained inflation, resilient external balances and high real interest rate buffers, which help absorb near-term energy-driven shocks. With the US dollar losing momentum and valuations more attractive after recent volatility, EMFX offers selective upside as a source of diversification and return.

EM sovereign credit

We remain cautious on EM sovereign credit as rising macro and geopolitical uncertainty increases spread risk. The recent spread widening looks like early-shock repricing, reflecting uncertainty rather than a deterioration in underlying fundamentals or default dynamics. Current EM spread levels, while off their tights, remain well below historical stress peaks, reinforcing this interpretation.

What this means for positioning and implementation

We remain invested in core long positions across EM local markets, where strong fundamentals, supportive macro dynamics and attractive valuations continue to align.
In credit, a more meaningful widening in spreads could create selective opportunities. Until then the opportunity for broad-based dip-buying remains limited, with our focus firmly on identifying idiosyncratic, flow-driven dislocations where technical factors may present compelling entry points.

The main risks to watch and how we're hedging them

The main risks in rates may come through a surge in volatility in front-end rates in the UK and Europe, as well as tail risks rising in the US. Our preference is to fade the front-end moves by using long positions via options rather than cash. To hedge against large, volatile shifts in interest rates, we favour strategies involving option structures that benefit as interest rates fall.

We are cautious on credit, keeping beta light, and are mindful of risks such as a spike in volatility, inverted term structures and significant widening of credit spreads. Hedging strategies will include positions to benefit from wider spreads in financials.

The key risk for emerging markets remains the potential for further escalation in the Iran conflict and uncertainty over how long it will continue. To manage this risk, we continue to take a targeted and disciplined approach to portfolio protection. This includes selective credit default swap (CDS) positions to help mitigate downside in higher yielding and frontier exposures, alongside option strategies that allow us to express a more constructive view on EMFX.

Key risks

Investment risk and currency risk

The value of an investment and any income from it can go down as well as up and can fluctuate in response to changes in currency and exchange rates. Investors may not get back the original amount invested.

Credit risk

Bond values are affected by changes in interest rates and the bond issuer's creditworthiness. Bonds that offer the potential for a higher income typically have a greater risk of default.

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