



# The Investment Conversation: Focusing on Fixed Income Markets in 2026



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*In this podcast, Lord Abbett Portfolio Managers Rob Lee and Steve Rocco explore the factors that could influence the performance of taxable fixed income investments in 2026.*

**ANDY D'SOUZA:** Welcome back to *The Investment Conversation*. I'm Andy D'Souza, partner and chief marketing officer here at Lord Abbett. As part of our 2026 investment outlook, we're going to talk with our investment leaders about key themes for the markets in the coming year across equities, municipal bonds, taxable fixed income, and private credit.

**D'SOUZA:** Today I'm here speaking with our co-heads of taxable fixed income, Steve Rocco, hey, Steve.

**STEVE ROCCO:** Thanks for having me. Excited to be here.

**D'SOUZA:** Glad to have you here, Steve. And Rob Lee.

**ROB LEE:** Hi, Andy and great to be with both of you again.

**D'SOUZA:** Again is right, Rob. Awesome. So, last time we were together in this room speaking on a podcast it was halfway through the year with our midyear outlook, and a lot of things were happening. We had just sort of come off of Liberation Day [the April 2 U.S. tariff announcement]. There's a lot of noise and a lot of news out there to digest. But just taking a step back, where we are today now as we enter the end of the calendar year 2025, what do you guys see as far as big picture in terms of just the economy in general? I'll throw it out there. So, Rob, do you want to start with the economy? What are your thoughts on the economy overall?

**LEE:** Sure. I think the single-best word to describe the U.S. economy (we'll talk about the U.S. first), is resilience. As far as I can tell we haven't had a recession and are not in recession right now. Growth has been positive, and that's despite some

pretty significant changes in trade policy and the tariffs that you alluded to.

Liberation Day was the height of the tariff fears and uncertainty but here we are towards the end of 2025, and we've seen positive real GDP [gross domestic product] growth in the U.S. Why is that the case? Well, I would point to a couple of things. The first is a number of different adjustments by the Trump administration on tariffs. There was a 90-day delay. There are exemptions for certain countries and certain goods. There have been trade deals. You could also just view it as prudent adjustments and negotiation. And that's one reason we didn't get the worst of the, you know, maximal tariffs. The second reason is corporate America and the corporate world, they're quite resilient and resourceful and creative.

They will and have found various ways to adjust to whatever the policy is. It helps when the policy is set and more stable, but it's, I think, pretty clear that we have more certainty around it more than seven months later after Liberation Day. So, decent growth in the U.S. It's not gangbusters. It's lower than it was in the second half of 2024. But we're sitting here towards the end of the year, and things look like we're in pretty good shape.

**D'SOUZA:** Steve, what do you think?

**ROCCO:** Sure, let me just add on here. So, I'd say, Q3 [third quarter U.S. gross domestic product growth] looks to be shaping up 3% to 4%. That's a pretty strong quarter, probably the strongest we'll have this year. You know, Rob is right to say



that it seems like the worst expectations for tariffs have not come to pass.

That being said, like in Q4 [fourth quarter of 2025], we've had a prolonged government shutdown which will, I think, lower growth in Q4. I think that's what the market's a little bit worried about. But I also at the same time have inflation coming down in Q4.

Now, the struggle is we haven't had a whole lot of data, but we can look at, like inflation swaps, which are now down to 2.5%. So, you have a Q4 setup of, you know, kind of slowing growth and possibly a little bit lower inflation, still above the Fed [U.S. Federal Reserve] target.

And I think, you know, for me the big thing is kind of this upcoming Fed meeting where, you know, expectation right now, it ebbs and flows, but it's about 50/50. And my view is they actually should cut here. And it looks like we have a very divided [Fed] committee. I think that's what the market is kind of struggling with at the moment. But that could be a very temporary thing because if we fast forward to Q1 [first quarter of 2026] you'll see more fiscal [stimulus] kind of play through. And also, you'll probably have a new, you know, in May you'll definitely have a new Fed chair. You'll have an announcement of who that is pretty soon actually, and I'm assuming that person will kind of drive an agenda that will mean lower rates. So, I think what we're experiencing right now, although very minor, could resolve itself to the positive as we head into Q1 next year.

**D'SOUZA:** What about the consumer? It's a large part of the economy obviously. Data's been a little bit, I don't know, hard to get these days perhaps you might say. What are your thoughts on those two things, the consumer overall and this whole idea of the data not being there, not being as clear or as current?

**ROCCO:** Yeah. So, we have other sources of data obviously. You also have data from, you know, large retailers. We had, you know, obviously Walmart report yesterday, which is actually pretty strong. But there is some effects, right? You're seeing a trade-down effect for sure. You're seeing pressure on the subprime consumer; actually more pressure on the near-prime consumer. So, I think those are the folks that may have got too extended, where the subprime consumer is kind of living in the world that they've been accustomed to which, you know, is dependent really on a lot of variability in oil price.

When oil prices are lower, that's to the benefit of the subprime consumer. I think it's where you've seen a little bit of aggression, it's been more in that near-prime and that's played out. But, in aggregate the consumer data has actually held up pretty well, pretty strong. And most of the spending, as we know, is the upper tier. So, that accounts for 80-plus-percent of consumer spending. So, while there's pockets of weakness, I'd say in aggregate it is still pretty strong, right? That's the Q3 [third quarter 2025] data we talk about. But there's no doubt there's been a little bit of a slowdown in Q4. And as I touched on, some of that's government shutdown, right?

But there has been a general slowing that we've seen in the data. We talk about restaurant spend, you know, food away from home, that's kind of one indicator I look at, and that's kind of slowed, not rapidly but it's moderated.

**LEE:** Yeah, if I had to add one thing there. Putting my take on it, another construct or framework you can use is what economists call the K-shaped economy. I'm sure many listeners will have heard that. The top part of the K, capital K I guess, is the high-income, higher-wealth cohorts. And the bottom part of the K is the lower-income, lower-wealth cohorts. What Steve's referring to is that the bottom part of the K has faced pretty great pressure. Some of it is because in recent years we've had pretty high inflation, so even though inflation rates have come down, the price level is pretty high. And that makes it more challenging for spending, for discretionary spending, and to meet your day-to-day everyday necessities. And you're seeing some signs of that in subprime auto delinquencies for example, and Steve alluded to that.

The upper part of the K is doing quite well because, until recently (but overall this year), stocks are up, cryptocurrencies are up, house prices are up. Wealth and household net worth is very, very high. It's near all-time highs. And the majority of spending is done by the wealthier, higher-income cohorts.

The real question that, and a real, I'd say, tension and key question for the coming year is, to use another letter. If you use capital E and you're talking about instead of high and low income and wealth you talk about high middle and medium, and low. How does that middle category do? And there are at least some concerns about some of the headwinds that the lower part of the E are facing might spill over into the middle.

**ROCCO:** And then, you know, frankly the labor market has kind of stalled here, right? Not a lot of hiring or firing, it slowed down. We got some data for September, and you saw the revisions to July and August, which were negative prints. We won't get payroll data for November, you know, it'll come after the Fed meeting in December at that point. But the labor market will be key here because if we start seeing, you know, layoffs and a weakening labor market, then that's going to affect a broader subset of consumers than what we're talking about here. And that'll play through the aggregate data.

And that's one of the reasons why I think the Fed should keep cutting because they are restrictive and the labor market's weakening. And so, I think it pays to get closer to what they believe their neutral rate is. And I actually believe they'll do that. But it's now an open debate here, but we have a couple weeks to find out.

**LEE:** Right, you can't talk about the consumer and the U.S. without talking about the job market. And Steve, I completely agree, is right. The way I'd characterize it is low hiring rates but also low firing or layoff rate. Another way to say it is kind of a low churn, low turnover. There's been a deceleration from, say, a year ago from 2024 in job creation and new jobs. Some of that is probably due to the changes in immigration policies and net immigration to this country. But there's no doubt there's been some deceleration.

This is why the Fed has started to resume its fed-cutting campaign. They cut 50 basis points in September and October of this year, just a couple months ago, after pausing. They cut about 100 basis points toward the end of 2024. They paused for nine months, and they've resumed that rate-cutting path. They see the softness or the deceleration of the labor market, and they are resuming their rate cut path to, I think, buy insurance. They call it risk



management cuts, to buy insurance, because for the labor market and the U.S. economy, because monetary policy, as we all know, works with a lag.

**D'SOUZA:** And last time we spoke, Steve, you had mentioned the idea that the subtle difference between the soft data and the hard data. Is anything here sort of diverging from that sense or doesn't make sense in the whole equation of what's going on?

**ROCCO:** Well, it's hard because we haven't had any data here for months. So, it's hard to see what divergences are. You know, generally speaking, the softer data has been a touch weaker. Some of the confidence data, some of the survey stuff have been weaker. I'm talking about Michigan Consumer Confidence. It's also been a split between Republican and Democrat, which you see often when it comes to this confidence data, depending on who's in office. So, there's that. That being said, we had a series of data releases here in the last week or two where you saw some of that soft data on the service side in Europe, service side in U.S. kind of holding in okay.

So, nothing super, super troubling. But we'll get more data again as the months pass. We're not really going to know, is my point, until probably January, February next year when everything plays through and we get all data catch-up. And I think that's contributing some of the uncertainty that we're talking about here because the market's been flying blind and so is the Fed at this point. But from what we can tell, I think the economy has slowed a little bit. Whether it's soft or hard data, but it's slowed a little bit.

**D'SOUZA:** Gotcha. We talked about monetary policy a bit. On the fiscal side of the house, for fiscal policy, what are your thoughts there, Rob?

**LEE:** I would call fiscal policy neutral to positive. So, the big picture is the One Big Beautiful Bill Act [2025 U.S. budget legislation] got passed earlier this year, and it was net stimulative. It wasn't hugely net stimulative. It doesn't increase the federal deficit by huge amounts but still net federal government spending. And that will boost the economy, all else being equal. How that gets distributed is an interesting and relevant question, and I would say (broadly speaking for corporate America and parts of the consumer balance sheet and consumers), generally positive.

So, I think you should expect net stimulus from a fiscal perspective. There is a timing issue there too because it doesn't always—over a one or five or a ten-year window—it is not always exactly smooth or even or level. And I would say in the first half of next year you should probably expect some net boost. That's the way the provisions were set up.

**ROCCO:** That's right.

**D'SOUZA:** Got it. And you mentioned the first half of next year and looking out so that the bond market is supposed to be looking into the future and tell us what it sees. So, with that backdrop in terms of the economy and fiscal and monetary policies, what's the bond market telling you guys right now?

**LEE:** Sure. Let me start with credit spreads and then we can talk rates, we can talk about shape of the curve. It's hard to deny that

credit spreads are tight. When you look at historical measures we could talk about investment-grade corporate bonds, we could talk about high-yield corporate bonds, we could talk about commercial mortgage-backed securities.

As a general statement, credit spreads are pretty tight. They are not at the year-to-date tight. They've given some of that back and widened a bit from the tight—five or six weeks ago. But when you look back at five, ten, twenty-year averages, we're pretty tight. I would argue though that generally speaking those tight spreads are reflecting pretty good fundamentals. Let me explain giving a couple of examples. We're almost all the way through third quarter earnings for larger companies.

And this is true for both second quarter and third quarter, pretty solid. That's true at the top line, the revenue line. It's true at the bottom line, the income/net income line. It's true for corporate margins. It's not universally true for every company or every industry or sector. But broadly speaking, we're talking about a mid-to-high single digit increase in revenue. Use S&P 500®, which is not the perfect proxy for bond sectors. And low to mid-double-digit net income growth. And this is at a time when there probably were some headwinds, right, from uncertainty around tariffs and things like that.

You might've seen it more in the second quarter earnings than the third. But broadly speaking, corporate America is doing pretty well. We have already talked about the consumer. Consumer balance sheets, with some differences by income cohort and wealth cohort, are in pretty solid shape. When people have jobs, the unemployment rate, the last we've seen, is 4.3%. It's off the lows but it's pretty low, historically speaking. So, I'd argue, from a corporate America point of view, pretty healthy fundamentals. From a household point of view, broadly speaking with some differences.

I'll use one other example. Let's talk about commercial and residential real estate. In pretty decent shape. We had 525 basis points of rate hikes back in 2022 and 2023. That made housing affordability challenging, it spiked mortgage rates, both on the consumer and the residential side. That was pain. We're a couple of years past that and yields, Treasury yields and mortgage rates, both commercial and residential, are definitely off the highs. That should be a boost and make affordability better for home buyers, some refinancing and some monthly savings on your monthly payment. And on the commercial side, lower cap rates, which should be good for a heavily financed sector. So, I won't say it's universally good, but I'd say the credit spreads are reflecting good fundamentals as a general statement.

**D'SOUZA:** Steve, the picture you painted there, Rob, as well, it seems pretty benign, seems okay. Things seem okay. But there are some headlines creeping in now about some certain episodes or instances in the market. Let's call it the cockroach comment, right? There was a couple things that hit the news recently. Do you see these as sort of idiosyncratic flareups or something people want to see? It feels almost like a canary in the coal mine. They want to see something and read into this a little bit more. What's your take on some of the problems people are having now?

**ROCCO:** So, I'd say we've talked about this in the past with the



rise of private credit, right, and also the changes in the broadly syndicated loan market. And I'll touch on some of those questions that you asked here in a minute. But the reason why the high yield market trades as high as it does in investment-grade is because a lot of - I'm not going to say bad lending but the more levered lending went to these markets, right, which leaves the high-yield market relatively cleaner.

And that's one of the reasons, among many, high yield markets also shortened, that spreads are what they are and may be kind of justified. Now, there is a vintage problem in private credit. I don't think it's shocking to say, I've been saying it for years, now it's coming through, right?

And that's that 2021, maybe 2022 vintage. And if you remember what was going on in 2021, you had zero base rates and it was a little bit of euphoria, and there's certainly a lot of capital there that needed to be deployed and naturally you see a loosening. And I think that is what you're seeing with some of these. And by the way, not all of it's private credit, right? You know, First Brands [auto parts supplier that defaulted in September 2025] was a broadly syndicated loan. Let's make that clear, right? Private credit folks owned it, but it was a broadly syndicated loan.

But I'm expecting you'll see more, right? But I don't think it's a systemic risk because by definition, it is private credit. It is not like the financial crisis when everything was on a bank balance sheet. This is off a bank balance sheet and it's in private hands.

But I do think you'll see more of that play through. Now, for it to get worse from here I think you would need to see the economy get a whole lot worse from here. But there's still this pressure, right, because base rates are still relatively elevated and there was lending that probably should not have gotten done. And so, I'm not surprised to see it. Now, the media's all over it. And they're going to report on every single default. But this gets into another thing. There's a lot of dispersion among BDCs [business development companies], right? There's a lot of the larger BDCs, if you look at the non-accruals, you know, there's not many. And you look at some of them, there's some problems, right? And the same is true in credit markets. There's a lot more dispersion now than there was, let's say, when we were doing this podcast six, seven months ago.

And I expect that'll continue, and that hopefully plays to the benefit of an active manager, where you can pick and choose where you want to be. But I think it's more of a systematic thing than systemic when it comes to this, where you may see more and more and more.

But at the same time, if I look at credit markets in aggregate, and I touched on the private non-accrual, but if you look at, the high yield default rate with distressed exchange its about 1.5%. Without it's about 0.5%. Maybe elevate it a little bit next year, but if we have the outlook right, I don't think you elevate all that much. You may not even elevate at all. And so that's why I think it's much more of a resilient asset class.

So, you know, we'll see what happens here. But I think there'll be more and I think the media, as always, will be focused on it and

they are. But you've got to take a step back and not paint everything with a broad brush. But no doubt for 2021 vintage I'd have some worry.

**D'SOUZA:** So, maybe a vintage isolation in some sense issue. So, maybe more cockroaches [i.e., negative credit events] but not an infestation may be a way to put it?

**ROCCO:** That's probably right.

**D'SOUZA:** That's what I think about it.

**LEE:** You know, let me add a comment or two here. So, Steve and I broadly agree here. So, Jamie Dimon, if I can use that name, so he talked about there's never just one cockroach. You should expect more. I generally agree with that as a blanket statement. When it's a bull market, when the economy is strong, when the credit markets are open and liquid and issuance is getting done, throughout various cycles lenders sometimes get lax. I'm not saying we don't do very detailed and rigorous work.

But the system as a whole, it naturally happens. It's just the nature of cycles. So, do I expect more? Yes. And we've seen a few more. That's the first statement I would make. Is the media hypersensitive and reports on every single one of those? With thousands and thousands and tens of thousands of loans and companies, of course there's going to be a dispersion. Of course there's going to be some. So, there'll probably be more. I think it makes sense. But the second question is, "How many and is it systemic?" I'll make a general statement. I don't think it's systemic. I agree with Steve. If you're talking about private credit, I would argue it's in very strong hands. People who are investing in private credit, as a general statement, know the liquidity of what they're investing in. They know the risk. You don't get high yields and wide spreads for nothing. It's pretty locked up, stable capital, as a general statement.

We don't know (and most people don't know, including the end investor, doesn't know), exactly what's in those portfolios. And the opacity, the lack of transparency there, means nobody knows for sure. The very last thing I'd say is in private credit the large majority of it is floating rate.

The Fed has cut 150 basis points in the last year and change. That, all else being equal, eases the debt service burden for all those issuers. If they need to do more, they will do more. We'll see what happens in December. But don't forget the big picture. And the big picture is the Fed's cutting. That's going to make servicing debt easier. It won't save over-levered capital structures. So, I think there's room for caution. We'll probably see more. I don't think it's systemic.

**ROCCO:** You know, the other thing I'd say, just to touch on what Rob was saying, the bigger headwind for public versus private may just be more the rate story, where, yes, it helps from a company perspective, when your interest expense moves lower and the economy holds. But also, we're dealing with floating-rate interest rates. And if the Fed keeps cutting rates, your yields are coming down.

That could be the bigger story than the actual credit cycle turning. And that may favor more of a fixed-rate exposure. In fact, that's





what I believe. And so that may favor an asset class like IG [investment grade bonds] or high yield relative to private credit. We can move away from the hysteria or the default cycles. That may be the bigger driver. And, you know, private credit spreads, generally what you see when the front end [of the yield curve] comes down is you see those spreads come up. So, they'll kind of offset.

And all that being said, the time to do the deal, we talk about the 2021 vintage. I think the 2024 and 2025 vintage are great for that reason, because it's kind of eyes wide open on base rate. You're getting wider spreads. You can forecast out what you think the base rate's going to be. You're in a much more, I think, reasonable environment than in 2021. So, that goes back to pick your manager wisely, right? And I'm excited that we launched our efforts in 2024, and I think it was very well timed. So, to me that's a huge opportunity and that actually excites me. But there's no doubt going to be more to play out here as we walk through it.

**D'SOUZA:** And what about technicals in the market as far as supply and demand and whether it's high-quality sectors or leveraged credit sectors. What have you guys seen sort of in supply and demand?

**ROCCO:** So, generally speaking, let's touch on different markets. High yield issuance is up. Net issuance is up a little bit. Projecting up, a good year for high yield, about \$300 billion to \$350 billion gross issuance [high yield bond]. Project that for next year, if you want to take the over, it would be in a more robust M&A [mergers and acquisitions] environment.

The market has shrunk, right? We talked about the move to BSL [broadly syndicated loan] in private credit. And maybe some of that comes back into the high yield market. But overall, I'd say relatively tame from the supply side. Still a lot of refi [refinancing] and still a lot of demand for yields. Now, IG [investment grade], you've seen increasing supply in IG. Rob knows better than I do, but I think maybe the projection next year is about \$1.7 trillion or \$1.8 trillion.

**LEE:** Depends on who you ask but a little higher.

Rocco: Who you ask but what's happened recently there. It could go higher. And I always take the over on IG supply. There, it could be M&A. But what's happening in IG is really, we haven't touched on AI [artificial intelligence] yet, right? It's the hyperscaler spend, right? And so, to the extent you believe that, and I think it's very believable, and some of this will be on balance sheet, some will be off-balance sheet. We can get into that if we want.

Some of this will be JV [joint venture], some of it will be on balance sheet. But if you believe the spend [on AI infrastructure], which, by the way, everyone underestimates every year, if [Lord Abbett Director of Equities] Matt DeCicco was here he would tell you that, and it's true, then you'll probably see more IG issuance.

You may even see more high-yield issuance, right, because we now have about 100 basis points into the index [ICE BofA U.S. High Yield Index] of what I call AI supply. And so you'll probably see more of that because there's definitely a big capital need. You'll probably see more of that in private credit too. It's kind of all hands

on deck. So, on supply overall I would, sitting here right now, given my outlook I always like to fall on Say's Law, you know, supply creates its own demand.

**LEE:** Here's the only thing I'd add, and maybe I'm just saying it a different way than Steve said it. I'd say when I look at supply and demand in fixed income markets, I'll talk about high-quality fixed income, balanced. So, supply, as Steve said, is high. That's true for gross supply. It's true for net supply. I wouldn't say it's extraordinarily high normalized for the size of the economy, the growth in U.S. and global population, you know, past years. It's not off the charts by any stretch of the imagination.

But the federal government runs \$1.5 trillion or \$2 trillion deficits in recent years. They have to finance that somehow. So, the net supply of Treasuries is roughly what that number is. So, you're talking about almost \$2 trillion a year.

Investment-grade corporates, Steve gave you the numbers, you're talking about in gross supply, I'll use a point estimate, the year's not over, \$1.8 trillion this year. Roughly a third of that's net supply, so call it \$600 billion. So, there's growth there.

It's true in agency mortgage-backed securities. It's true in some of the smaller sectors too. So, you have a healthy supply. Steve said it. Demand's pretty healthy. That's true on the retail, mutual fund, and other vehicles side. It's true for a lot of other institutional investors, think banks, insurance companies, foreign buyers in general.

**ROCCO:** Yeah. I think generally if the market's good, the market's accepting of the supply. I mean, there are periods where you see, like, maybe a chalking in that indigestion, you know, period. What we saw in IG in the last month or two where I think, some of this was done off balance sheet and some of it came on balance sheet and the CapEx (capital expenditure) numbers were ratcheted up. The market had to adjust to that, then it did adjust to that.

**LEE:** You touched on this, Andy, and you alluded to this, and so did Steve. The very large, I call it massive, projected build-out of AI, gen (generative) AI, data centers, the power generation needs to power all that is a big deal and one needs to think about it and it will affect supply.

So, Steve talked about some of the big hyperscalers who are the largest companies from a market cap [capitalization] perspective who are investing hundreds of billions of dollars a year in this built-out for lots of reasons that we can talk about, will slowly and are already starting to affect supply (nets and gross supply), in fixed income markets and the composition of it in terms of sector and issuer.

It's important to have a game plan and to be thoughtful around that. There's a lot to be discussed on this topic, but I can assure you that we've been thinking through it and studying it very closely. And I would say here we believe that it is still pretty early in the build-out.

We're still building the infrastructure, if you will. Think of GPUs [graphic processing unit] from NVIDIA and other semiconductor makers. Think of the build-out of data centers to power the training



of AI and training and inference, and the power in the grid to provide what's needed, the massive power needs for that. So, I'd say we are thinking about it and there are both opportunities and risks here. I can expand if you want.

**ROCCO:** Generally speaking, right, just to touch on a few things there to follow up on what Rob's saying, with these big infrastructure builds. You can go back to telecom [the telecommunications sector] in the 1990s, I even put in energy shale revolution, which high yield financed, right, and now AI, they usually end in bust, right? But there's usually a benefit and the benefit goes to the user and the consumer. We're all better off for having all that fiber deployed in the '90s. We're all better off for the shale revolution because we have lower oil prices. And I think we're much better off with AI.

So, you have to be careful because I'm willing to finance a data center build, right, I'm willing to finance certain things. But the history of these things you see a lot of issuance in one sector, your antenna should be up. And you want to be very thoughtful from the top down. That's why we're encouraging the teams because you can get very marginal very quickly, right, in terms of how things are done and get very loose very quickly. And you saw that with high yield and U.S. shale, where it started with the best and it got to the worst and it was a completely over-supply situation, and that could happen here.

**LEE:** Let me give you one other example. I agree it's early but we have to be very vigilant. So, if the big hyperscalers, these tech behemoths, need to issue \$20 billion or \$25 billion or \$30 billion of debt multi-tranche at a time more than once a year they usually have to come at a price-spread yield concession.

They have to make it attractive to place all that paper. These are massive cash flow and despite all the CapEx [capital expenditures] and investments, most of them are still free-cash flow positive. These are double-A and triple-A rated companies. And if you come at a nice concession with very credit-worthy household names with moats and real giant businesses, it's attractive.

How long you want to stay around, how you monetize or take profits or not, is key to active management and something that, you know, is what we do every single day. That's the opportunity side of it. It's true on the high yield side and the leverage loan side and the private credit side and securitization side.

There's ABS (asset-backed securities) and CMBS (commercial mortgage-backed securities) data center securitizations, and they're not all created equal. And sometimes they come at very attractive levels. You just have to make sure you understand where this is going and study it very closely, be very selective, choose the best assets, benefit from this build-out and the high issuance needs. We went from primarily cash flow finance for this giant AI build-out and data center build-out and now it is increasingly moving to debt finance and that's our world.

**D'SOUZA:** So, we've gone through a lot of the ideas in terms of what are the challenges and opportunities ahead of us here. You can give me a challenge or an opportunity I think, but maybe one that we haven't talked about yet.

**LEE:** Okay, I'll start. And first, let me cover high level. The key debates question that we need to answer are the things that we're really focused on. We touch on it, but it helps, and I think it helps to take a step back. One is this whole AI, technology, hyperscaler, data center, power build-out, very important. Not a prediction, (but if it's a bubble and it crashes at some point (I'm not saying it's a bubble, by the way), that will have ramifications across all capital markets in the U.S. economy. So, that's a key debate question that needs to be studied. I don't think it's a bubble yet. I think there's some frothy signs, but I don't think it's a bubble yet. That's just my view. I can elaborate. That's number one.

Number two is what I would call, and we talked about the economy. So, this is pretty healthy GDP data but a softer labor market. Is that a wedge or discrepancy or tension? There's an argument to be made that it is. You usually don't have both of those happening simultaneously. And if one resolves in the direction of the other, meaning GDP starts to weaken a lot in a sustained way and we go into recession to match, a softer but not falling-off-a-cliff labor market is key. Or does the labor market start to rebound and stabilize? That's a key number two. That's kind of the number two key question to me.

Third is cockroaches credit cracks. Is it systemic? How many more are we going to see? How bad is it? This is true for private credit and payment in kind. This is true for lots of credit markets.

The fourth is the consumer. We talked about K-shaped and E-shaped and, you know, low income and high income. All key debates. It's also probably my top four right now. I'll give you one or two more that (and this is really the gist of your question that), I'm thinking about.

If inflation picks back up, stays stubbornly high, most inflation measures (there are dozens of them), around 3%. That's above the Fed's target of 2%. I think it's likely, my base case and I think Steve agrees, likely to keep coming down for various reasons. But if we're wrong, and through various factors we get a surprise and stays here and/or goes higher, it's going to make the Fed's job harder in terms of its cutting campaign. So, an unexpected and/or sustained increase in inflation would be bad for risk assets in general. That's one.

Somewhat related, and then I'll stop with two, is I think even though copious amounts of work and research and articles have been spilled on this topic I still think it may be under-appreciated, it actually ties into all the things we've been talking about so far, is the immigration trends, the effect on certain industries, the effect on wages.

It has an impact on labor supply, on wages, and on potential GDP growth. So, how that all plays out I think it is still perhaps an under-appreciated impact on various parts of the economy.

**D'SOUZA:** Got it. Steve?

**ROCCO:** I'll give you one.

**D'SOUZA:** Give me one.

**ROCCO:** But it's broad. Something on my mind—we've touched on what's worked in the market. There's been earnings power, and



that's generally coming from large-cap tech companies. Not all of it, but most of it—the free cash flow generators.

Maybe that free cash flow isn't what it was in the past because, as we just discussed, they're spending more. So they lose some of that free cash flow yield edge. And then we're talking about this idea that as we roll into Q1 next year, there's also a midterm next year, which is important.

We might be in a bit of a lull now, but if we're right, Q1 picks up. The market's priced in a lot of cuts—which may or may not happen. And we're going to have a new Fed chair.

I'm assuming that new Fed chair is someone who's going to cut. That's my assumption, right or wrong. Maybe there's more debate and discussion, but probably someone who's going to cut in the face of inflation that's not at target, in what could be a cyclical acceleration. Does that unleash a little bit of animal spirit—some of that higher nominal [economic growth rate] environment? From the standpoint of what's worked in the market, it's been tech and AI.

But maybe you get a little more cyclical, which hasn't worked in the market. Part of that is driven by the economy accelerating and the housing market unlocking, which, frankly, has stalled with higher rates. I think the administration is very focused on housing. Once that chain gets working, you unleash cyclical and earnings power. Maybe next year is better for cyclicals versus tech, which is not how people are positioned, I'd say.

Those are things on my mind. I think they're plausible. Or it could just be more of the same where the winners keep winning and large caps keep winning, but maybe not. I think that'll [potentially] play well toward a down-in-quality type of exposure. Generally speaking, that's what happens in a higher nominal environment.

**D'SOUZA:** So, a lot on your minds, a lot of opportunities but a lot of things to be concerned about in a healthy way as well. Guys, thank you for the time today.

**ROCCO:** Thank you.

**D'SOUZA:** Really appreciate it. And-- happy New Year pretty soon.

**LEE:** Yeah, great to be here.

**D'SOUZA:** Thanks, Rob.

**ROCCO:** Thank you, Andy.

**D'SOUZA:** Thanks, Steve.

**D'SOUZA:** This has been *The Investment Conversation* podcast. Be sure to visit [lordabbett.com](http://lordabbett.com) to find our complete 2026 Investment Outlook, along with other market and economic insights. Thank you all for listening.



## GLOSSARY OF TERMS USED IN THIS BROADCAST

**Base rate** is the minimum interest rate set by a country's central bank or regulatory authority. Variable interest rates fluctuate in line with a base rate which, typically, shifts in reaction to market factors.

A **basis point** is one one-hundredth of a percentage point.

**Broadly syndicated loans (BSL)** are floating-rate loans made to corporate borrowers with generally greater than \$50 million in EBITDA and in most cases, at least \$100 million. They are senior in the capital structure and have a first claim on the assets of the borrower.

**Business Development Company (BDC)**, is a regulated investment vehicle created under the Investment Company Act of 1940 and introduced by Congress in 1980. Its primary purpose is to provide financing to small and mid-sized U.S. businesses, often those that cannot easily access traditional bank loans or public capital markets.

**Capital Expenditures (CapEx)** refers to the funds that a company uses to acquire, upgrade, and maintain physical assets such as property, plants, buildings, technology, or equipment. These expenditures are considered investments in the company's future operations and growth.

**Carry** is the difference between the yield on a longer-maturity bond and the cost of borrowing.

**Commercial mortgage-back security (CMBS)** is a type of mortgage-backed security backed by commercial and multifamily mortgages or mortgages on commercial property.

**Corporate margins** refer to the percentage of revenue that a company retains as profit after accounting for costs and expenses.

**Cryptocurrency** is a form of digital or virtual currency that uses cryptography, a form of encryption, for security and operates on decentralized networks, typically powered by blockchain technology.

**Duration** is a measure of the sensitivity of the price (the value of principal) of a fixed income investment to a change in interest rates.

The **Federal Reserve (Fed)** is the central bank of the United States. The federal funds (fed funds) rate is the target interest rate set by the Fed at which commercial banks borrow and lend their excess reserves to each other overnight.

The **federal funds rate** is the interest rate at which depository institutions lend reserve balances to other depository institutions overnight on an uncollateralized basis.

**Free cash flow (FCF)** is the amount of cash a company generates after covering operating expenses and capital expenditures (CapEx) needed to maintain or expand its asset base. It represents the cash available for discretionary uses.

**Gross Domestic Product (GDP)** is the total monetary value of all final goods and services produced within a country's borders during a specific period, usually a quarter or a year.

**Hyperscalers** are large technology companies that operate massive, globally distributed data centers designed to deliver cloud computing, storage, and networking services at extreme scale.

**Idiosyncratic risk—also called specific risk** or unsystematic risk—is the risk that is unique to a particular asset, company, or sector, rather than the entire market.

**Issuance** refers to the process by which an entity—such as the U.S. government, a municipality, or a corporation—raises capital by selling debt securities (bonds) to investors. When investors buy these bonds, they are effectively lending money to the issuer in exchange for periodic interest payments (coupon payments) and repayment of principal at maturity.

**Joint venture (JV)** is a business arrangement where two or more parties agree to pool resources—such as capital, expertise, or technology—to accomplish a specific goal or project, while sharing profits, losses, and responsibilities.

A **K-shaped economy** refers to when the path of different parts of the economy, when charted together, may diverge, resembling the two arms of the letter "K."

**Levered lending** refers to the practice of providing loans to borrowers—typically businesses—that already have high levels of debt or lower credit ratings, making them riskier than traditional borrowers. Because of this elevated risk, these loans generally carry higher interest rates and often include stricter terms or covenants.

**Mortgage-Backed Security (MBS)** are debt obligations that represent claims to the cash flows from pools of mortgage loans, most commonly on residential property.

**Multi-tranche debt** refers to a financing structure where a single debt issuance or loan facility is divided into multiple tranches (segments), each with distinct characteristics, such as risk level, interest rate, maturity, or repayment priority.

**Near prime** refers to a segment of borrowers whose credit profiles fall between prime and subprime categories.

**Net income—also called net profit or net earnings**—is the amount of money a company retains after subtracting all expenses from total revenue.

**Private credit** refers to loans and debt financing provided by non-bank lenders to businesses, typically outside of public markets.

**Securitized products** broadly refer to pools of financial assets that are brought together to create a new security, which is then divided and sold to investors. The value and cash flows of the new asset are based on its underlying securities.

**Shale revolution** refers to the period in the energy industry beginning in the early 2000s that was marked by the widespread adoption of hydraulic fracturing (fracking) and horizontal drilling technologies to extract oil and natural gas from shale formations.

**Spread** is the percentage difference in current yields of various classes of fixed-income securities versus Treasury bonds or another benchmark bond measure. A bond spread is often expressed as a difference in percentage points or basis points (which equal one-one hundredth of a percentage point). The option-adjusted spread (OAS) is the measurement of the spread of a fixed-income security rate and the risk-free rate of return, which is adjusted to take into account an embedded option. Typically, an analyst uses the Treasury securities yield for the risk-free rate.

**Spread products** are any bonds that are not a government bond.

**Spread yield** concession refers to the additional yield spread offered on a bond (versus a benchmark) to make it attractive to investors, combined with the selling concession paid to underwriters or brokers.

**Subprime lending** refers to the practice of extending credit to borrowers who have weakened or lower credit profiles and are considered higher risk than prime borrowers.

**Vintage** refers to the year in which a loan or investment is originated.

**Yield** is the income returned on an investment, such as the interest received from holding a security. The yield is usually expressed as an annual percentage rate based on the investment's cost, current market value, or face value.

**Yield curve** is a line that plots the interest rates, at a set point in time, of bonds having equal credit quality, but differing maturity dates. One such





comparison involves the two-year and 10-year U.S. Treasury debt. This yield curve is used as a benchmark for other debt in the market, such as mortgage rates or bank lending rates. The curve is also used to predict changes in economic output and growth.

**Yield curve** steepeners are trading strategies that seek to gain from a greater spread between short- and long-term yields-to-maturity by combining a “long” short-dated bond position with a “short” long-dated bond position. A yield curve flattener involves the sale of short-term bonds and purchase of long-term bonds.

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