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Investment Perspectives

Why Investment Grade Floating Rate Makes Sense in Today's Market

In addition to higher yields, investment-grade, floating-rate securities offer the potential for effective diversification with less duration risk than their fixed-rate counterparts.

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After an extended period of low interest rates, fixed-income yields remain historically attractive and offer investors an opportunity to reassess their portfolio allocations. We believe the opportunity for the asset class, as a significant part of long-term asset allocations, is compelling. What might be the best way to balance those fixed-income allocations in today's volatile and uncertain rate environment? Here, we will focus on a particularly attractive opportunity in investment-grade, floating-rate strategies.

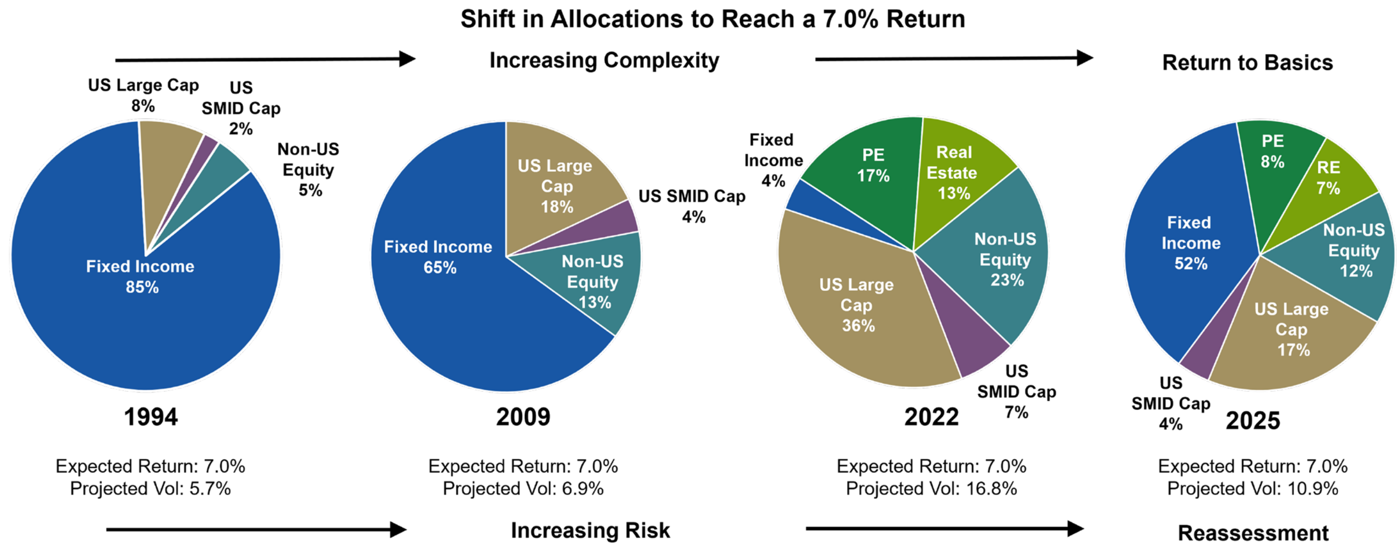
The Rate Environment Has Changed

There was a tactical rush to bonds in late 2023, as markets responded to falling inflation readings and dovish commentary from U.S. Federal Reserve (Fed) officials by quickly pricing in over six 25-basis-point rate cuts before the end of 2024.

As 2025 progresses, inflation has continued to moderate and economic data has remained resilient. Signs of softening employment figures have prompted the Fed to begin easing, with market expectations for two more 25-basis-point rate cuts by year-end, reflecting investors' reassessment of the Fed's balancing act between supporting the labor market and managing inflationary pressures.

While uncertainty persists, the current environment of elevated yields remains supportive of higher bond allocations. Take a look at Figure 1, based on data from institutional consultant Callan. Investors with fixed return targets were forced out of low-yielding fixed income over the last 15 years, opting instead for higher-risk options in public and private equity and real estate. With today's attractive yields, investors can potentially hit return targets with much less volatility by incorporating a higher proportion of fixed income.

Figure 1. Fixed Income's Renewed Role in Asset Allocations



Source: Callan Capital Market Assumptions (CMA). Data as of December 31, 2024. CMAs are developed by institutional investment consultants and represent long-term, return expectations across asset classes. A complete, long-term CMA may also include expected volatility, or standard deviation of returns, as well as the expected return correlation and other projections. PE=private equity. RE=real estate. Cap=capitalization. Vol=volatility. Treasuries are risk-free debt securities issued by the U.S. government and secured by its full faith and credit. Income from Treasury securities is exempt from state and local taxes. **Past performance is not a reliable indicator or guarantee of future results.** The historical data shown in the chart above are for illustrative purposes only and do not represent any specific portfolio managed by Lord Abbett.

Where those fixed-income allocations belong should be a primary consideration. Traditionally, investors have opted for the relative safety of high-quality investments for fixed-income allocations, choosing something similar to the Bloomberg US Aggregate Bond Index, popularly known as the "Agg." The Agg is comprised of nearly all fixed-rate instruments, largely U.S. Treasuries and agency mortgages, maturing over a range of dates but with average lives around five-to-seven years.

What this means is that most of the risk in traditional fixed-income portfolios is interest-rate risk. A standard risk model shown in Figure 2 highlights that movements in the yield curve contribute nearly all the volatility to the Agg.

Why does that matter? Over the last 40 years, having nearly all your fixed-income risk coming from interest-rate risk has been a positive. Rates have been in secular decline, providing a tailwind to returns, and rates-based fixed income has moved in the opposite direction of equities, providing valuable portfolio diversification. In an uncertain environment, however, those tailwinds are not likely to continue.

Investment Grade Floating Rate as a Complement to Agg Exposure

We strongly advocate for diversifying fixed-income exposure to balance risk and earn the higher yields available in corporate bonds and securitized products. Floating-rate exposures are a particularly effective way to bring balance to a portfolio that relies too much on rates. These instruments limit interest-rate risk by adjusting coupons to the prevailing rate environment. The result of this, from a risk allocation perspective, is dramatic. In Figure 3, we see that a floating-rate note index has completely different drivers of volatility than the Agg.

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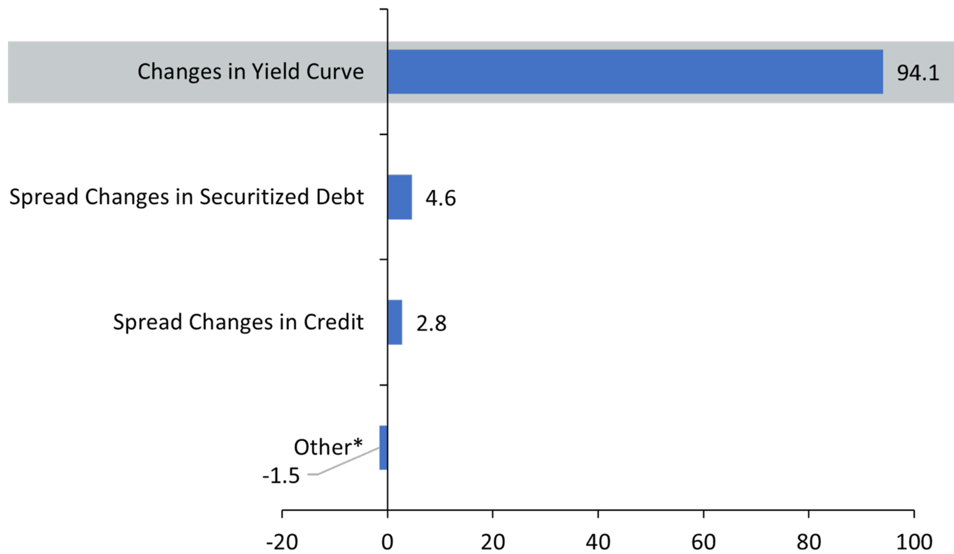
Figure 2. Interest-Rate Shifts Have Been the Primary Contributor to Volatility in the "Agg"

Contributing factors (in percent) to expected tracking error volatility for the Bloomberg US Aggregate Bond Index, as of September 30, 2025

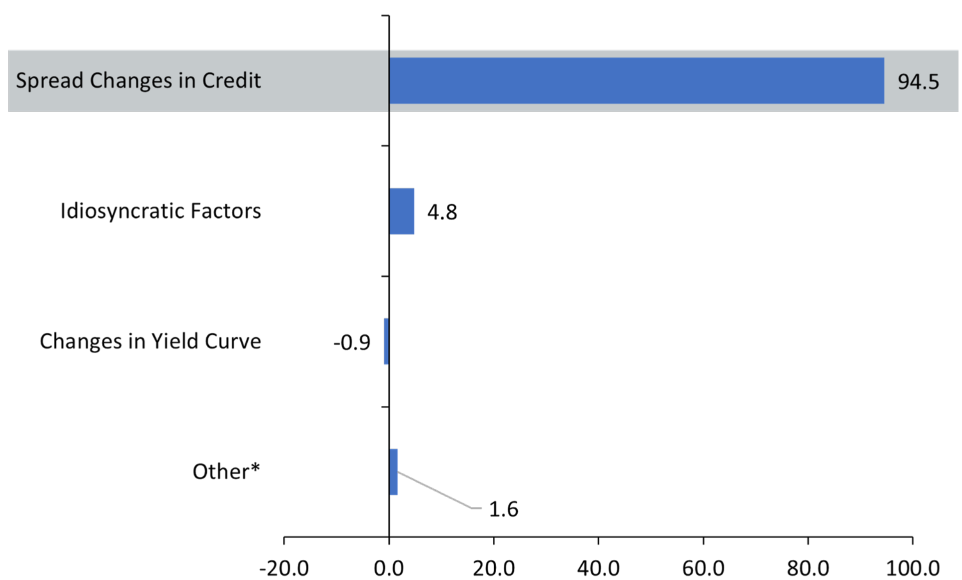


*Includes impact of spreads on government-related debt, rate volatility, credit defaults, and idiosyncratic risk factors.

Source: Bloomberg. Data as September 30, 2025.. The chart shows the degree to which each listed factor contributes to overall volatility displayed by the Bloomberg US Aggregate Bond Index ("Agg"), based on an ex-ante (derived from estimates) risk model from Bloomberg. Tracking error is the standard deviation of returns relative to a portfolio or benchmark. For illustrative purposes only and does not represent any specific portfolio managed by Lord Abbett or any particular investment. **Past performance is not a reliable indicator or guarantee of future results.**

Figure 3. Factors Driving Volatility in Investment Grade Floating Rate Differ Greatly from the "Agg"

Contributing factors (in percent) to expected tracking error volatility for the Bloomberg U.S. Floating Rate Note Index, as of September 30, 2025

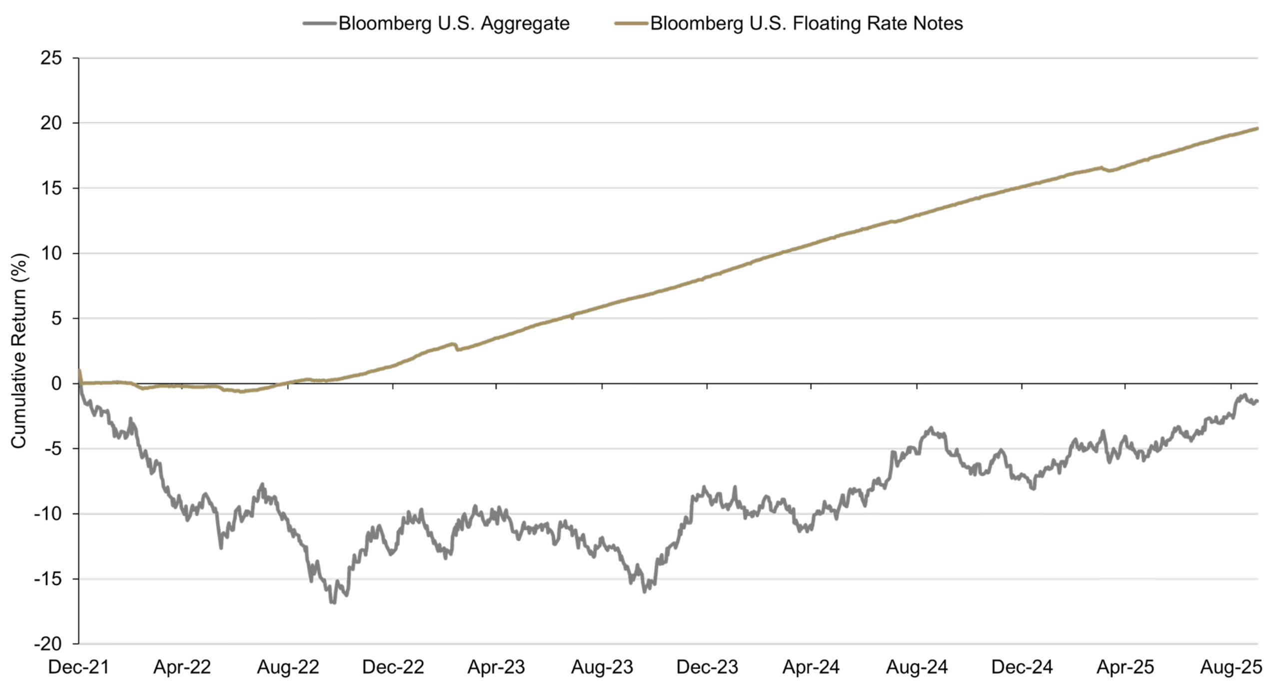


*Includes impact of spreads on government-related debt, swap spreads, rate volatility, foreign-exchange effects, and credit defaults.

Source: Bloomberg. Data as September 30, 2025. The chart shows the degree to which each listed factor contributes to overall volatility displayed by the Bloomberg US Floating Rate Note Index, based on an ex-ante (derived from estimates) risk model from Bloomberg. Idiosyncratic risks are rooted in individual companies (or individual investments) as opposed to systemic risks, which emerge from macroeconomic developments. For illustrative purposes only and does not represent any specific portfolio managed by Lord Abbett or any particular investment. **Past performance is not a reliable indicator or guarantee of future results.**

Figure 4. Investment Grade Floating Rate Outperformed the "Agg" in a Period of Greater Interest-Rate Volatility

Total return for indicated indexes, December 31, 2021–September 30, 2025



Source: Bloomberg. Data as of September 30, 2025. Total return indexed to one at December 31, 2021. Bloomberg US Aggregate = Bloomberg US Aggregate Bond Index ("Agg"). Bloomberg US Floating Rate Notes = Bloomberg US Floating Rate Note Index. For illustrative purposes only and does not represent any specific portfolio managed by Lord Abbett or any particular investment. **Past performance is not a reliable indicator or guarantee of future results.**

Probably more interesting is the result on returns and experienced volatility. Figure 4 shows that during a period of significant interest-rate volatility, returns on the Agg predictably suffered—notably at the same time equities were doing poorly as pricing adjusted to the new rate environment—while the floating-rate index performed extremely well with limited volatility

Conclusion

The last few years have seen the creation of several investment products focused on investment-grade, floating-rate assets. We favor an active, flexible approach to the space that can adjust to various market environments by rotating among corporate bonds and securitized sectors, as well as adjusting industry and quality exposures. At Lord Abbett, we have a deep and experienced team of investment professionals who have been investing in floating-rate corporates, collateralized loan obligations, asset-backed securities, commercial mortgage-backed securities, and other floating-rate asset classes for decades.

The case for fixed income as a core component of long-term asset allocation remains strong. Attractive yields offer an opportunity to potentially achieve return targets with less volatility. Yet, how those allocations are constructed matters. In today's volatile and uncertain rate environment, investment-grade, floating-rate strategies may offer an opportunity to complement Agg exposure through lower interest-rate risk, while also tapping into the attractive yields and differentiated risk drivers of corporate and securitized credit.

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Glossary & Index Definitions

A **basis point (bp)** is equal to one one-hundredth of a percentage point.

Collateral Loan Obligation (CLO) is a special purpose vehicle (SPV) with securitization payments in the form of different tranches. Financial institutions back this security with receivables from loans. Collateralized loan obligations are the same as collateralized mortgage obligations (CMOs) except for the assets securing the obligation. CLOs allow banks to reduce regulatory capital requirements by selling large portions of their commercial loan portfolios to international markets, reducing the risks associated with lending.

Asset-Backed Security (ABS) is a financial security backed by a loan, lease or receivables against assets other than real estate and mortgage-backed securities. For investors, asset-backed securities are an alternative to investing in corporate debt.

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

Commercial mortgage-backed securities (CMBS) are a type of fixed-income investment product that is backed by mortgages on commercial properties rather than residential real estate.

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.

Floating Rate Notes (FRNs) are fixed income securities that pay a coupon determined by a reference rate which resets periodically. As the reference rate resets, the payment received is not fixed and fluctuates over time.

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-to-maturity (YTM) represents the expected return (expressed as an annualized rate) from the bond's future cash flows, including coupon payments over the life of the bond and the bond's principal value received at maturity. Yield-to-worst refers to the lesser of a bond's (a) yield-to-maturity or (b) the lowest yield-to-call calculated on each scheduled call date.

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.

Tactical asset allocation is a short to medium-term investment approach that adjusts the asset mix based on market conditions, economic forecasts, or perceived opportunities. Strategic asset allocation is a long-term investment approach that establishes a target mix of asset classes based on an investor's goals, risk tolerances, and time horizon.

Tracking error volatility is a statistical measure of how closely an investment portfolio follows, or tracks, its benchmark index. It is the standard deviation of the difference between the portfolio's returns and the benchmark's returns over a given period.

Index Information:

The **Bloomberg U.S. Aggregate Bond Index** represents securities that are SEC-registered, taxable, and dollar denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities.

The **Bloomberg U.S. Floating-Rate Note Index** measures the performance of USD-denominated, investment-grade, floating-rate notes across corporate and government-related sectors. This index is not part of the U.S. Aggregate Index, which is a fixed coupon index.

Bloomberg Index Information