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Corporate Bond Market Insight | December 2025

How are Government Shifts, Fed Divisions and AI Ambitions Shaping 2026?

Key takeaways

» Fourth-quarter GDP is estimated to reduce between 1.0% to 2.0% because of the record-breaking government shutdown. However, the Atlanta Federal Reserve GDPNow is still projecting nearly 4% Q4 growth.

» There seems to be growing division among the Federal Open Market Committee (FOMC) committee members. With several committee members supporting more cuts, the odds of a December cut rose to nearly 80%.

» Issuance expectations for next year are increasing. Mergers, acquisition financing and the needs of the artificial intelligence hyperscalers suggest that 2026 could set a record.

» Consumer sentiment has declined, but American consumers are generally still in solid shape with declining but still high employment numbers and steadily rising wages.

Recap

November marked the end of the longest government shutdown in US history, a one-year trade truce with China, evidence of a deepening split in the Federal Open Market Committee (FOMC) and strong corporate earnings growth. Large capitalization equity indexes ended the month near all-time highs, interest rates fell and credit spreads widened.

The 43-day government shutdown is estimated to have reduced fourth-quarter GDP by between 1.0% to 2.0%. Despite this reduction, it's likely that growth will still be between 1.5% and 2.0%, consistent with growth in recent quarters and with the unofficial sources we monitor. While the lack of official economic data makes tracking less dependable, the Atlanta Federal Reserve GDPNow is currently projecting nearly 4% Q4 growth.

The Fed didn't meet in November, but the minutes of the October meeting highlight the growing division among the FOMC committee members. At the press conference following the October meeting Fed chair Jerome Powell clearly stated that a rate cut at the December meeting wasn't "a foregone conclusion, far from it." The October meeting minutes were also hawkish. After their release, rate cut odds for December collapsed to only 33%. Later in the month, the odds of a December rate cut rose nearly 80% after speeches from several committee members supported more cuts and a particularly dovish speech by vice chair John Williams.

Credit spreads have widened somewhat from recent record lows, but investment-grade (IG) corporate fundamentals are solid. Quarterly S&P® earnings growth of more than 10% supports balance sheets, and new rules around depreciation are producing estimates of 17% earnings growth for 2026. Rating changes show upgrades exceeded downgrades by roughly two to one.

On a less promising note, issuance expectations for next year are increasing. Mergers and acquisition financing and the needs of the artificial intelligence hyperscalers suggest that 2026 could set a new record. Issuers like Meta, Google, Amazon and Oracle have recently issued more than $100 billion. Estimates suggest that they will need another $3 trillion in cash for 2026. Half the need will be taken from free cash flow, but the other half will come from debt issuance. Record supply may cause spreads to widen modestly, but so far the market response has been reasonable and demand has remained robust.

Against this backdrop, the 10-year Treasury yield fell six basis points (bps) while credit spreads widened two bps on the month. The ICE BofA/Merrill Lynch 1–10 Year US Corporate Index returned 0.68% for the month, and 7.28% for the trailing one year. Sector level spreads were uniformly wider with media and technology, two sectors with large issuance, widening the most. Some finance companies, particularly those that provide funding to small, medium sized and financially distressed companies, such as business development companies, also underperformed. Best performing sectors include transport, telecommunications, energy and banking. Quality factors were mixed, but in general, lower quality outperformed higher quality.

Due to the government shutdown, most economic reports have been delayed and, in some cases, cancelled. But private sources like Advanced Data Processing (ADP) and the Institute of Supply Management, combined with the limited releases that the government provided, offer enough data to draw at least preliminary conclusions. For instance, the Institute of Supply Management Manufacturing Purchasing Managers' Survey weakened slightly. This is the eighth consecutive month below 50, the level that delineates expansion from contraction. The forward-looking new orders segment rose modestly, as did the employment survey. The services survey at 52 and new orders at 56 are consistent with expansion. On a more negative note, manufacturing and service surveys both continue to reflect significant pricing pressures.

After reporting negative job growth in August and September, ADP suggested that 42,000 jobs were added in October. This was significantly more than expected. Private employers added jobs for the first time since July. The September jobs report, released in late November, was also much stronger than expected. The 119,000 new non-farm jobs added were much stronger than consensus expectations. The unemployment rate rose from 4.3% to 4.4%. While the rise in the rate was unwelcome, it was mostly due to people entering the labor force.

While consumer sentiment has declined, American consumers are in solid shape, in aggregate. Employment is high, wages have steadily risen, savings are high with more than $8 trillion allocated between money market and certificates of deposit. Of these consumers, 60% have exposure to the equity markets and 65% own their homes outright. While lower economic cohorts are struggling, betting against American consumers is still a poor wager.

Looking forward

2026 will be a midterm election year. The sitting President's party generally loses Congressional seats in midterms so, policies aimed at maintaining control of the house are likely to become the top priority. There could be temptation to push the Fed to run easy monetary policy given the President will have the opportunity to appoint a more compliant chair once Fed chair Powell's term ends in May. In addition, the Treasury could run stimulative fiscal policy. Treasury secretary Scott Bessent has the power to guide Treasury issuance and buyback programs to influence the Treasury yield curve and market interest rates. Economic strength in 2026 may well surprise on the upside with the combination of stimulus from the budget reconciliation bill, new corporate depreciation rules and the continued build out of artificial intelligence infrastructure.

While not as uncertain as when entering 2025, next year will still hold plenty of questions. What will be the impact of the administration's efforts to influence the midterm elections? Who will be the new chair of the Federal Reserve, and what will be the bias of monetary policy? Will the stimulus from artificial intelligence spending be enough to continue driving the economy forward? Will the weakness at the bottom of the consumer economy spread? Will the courts nullify the International Emergency Economic Powers Act tariffs? If so, what will they be replaced with? Fortunately, we believe the structure of the corporate ladders should continue to provide a solid hedge against the uncertainty.

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Parametric is headquartered at 800 Fifth Avenue, Suite 2800, Seattle, WA 98104. For more information regarding Parametric and its investment strategies, or to request a copy of Parametric's Form ADV or a list of composites, contact us at 206 694 5500 or visit www.parametricportfolio.com.

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