

Preferred Securities Market Insight | August 2025

Investor Appetite Buoy Preferreds Amid Macro and Fiscal Shifts

Key takeaways

- » The ICE BofA Fixed Rate Preferred Index returned 1.45% in July, bringing YTD gains to 2.47%. The \$25 par ICE BofA Core Plus Fixed Rate Preferred Securities Index rebounded with a 2.77% return, while ETF inflows exceeded \$150 million.
- » Q2 bank results showed stable net interest income (NII), modest loan growth and healthy credit quality. Several banks raised full-year NII guidance, and capital positions remain robust.
- » July payrolls rose by just 73,000, with large downward revisions to prior months. The unemployment rate ticked up to 4.2%, and market pricing now reflects a likely rate cut at the September 17 FOMC meeting.
- » The Fed is fast-tracking Basel Endgame and SLR reforms, supporting capital flexibility and M&A. The One Big Beautiful Bill Act (OBBBA) codifies student loan reforms, but tariff income may offset much of the fiscal impulse from the \$3.4 trillion bill.

Recap

Preferred securities continued to deliver solid performance in July, with the ICE BofA Fixed Rate Preferred Index up 1.45% for the month and 2.47% year-to-date. The \$25 par ICE BofA Core Plus Fixed Rate Preferred Securities Index reversed months of underperformance, gaining 2.77%, while the \$1,000 par ICE BofA US Investment Grade Institutional Capital Securities Index returned 0.42%. Investor demand remains robust, as evidenced by over \$150 million in ETF inflows for July—including a \$100 million rebound in the final week.

On the supply side, technicals remain favorable. Year-to-date bank preferred issuance has reached \$27.5 billion, a 27% increase over the same period last year. Redemptions and calls totaled \$18.7 billion, resulting in positive net issuance of \$8.8 billion. July's new issue calendar was active:

- One money-center bank priced \$2.7 billion of Ba1/BBB- \$1,000 par perpetual non-call 5 preferreds at 6.875% (reset CMT5 +2.89%).
- A second money-center bank issued \$2.5 billion of Baa2/BBB- \$1,000 par perpetual non-call 5 preferreds at 6.25% (reset CMT5 +2.351%).
- A regional bank brought \$400 million of Baa3/BBB+ \$25 par perpetual non-call 5 preferreds at 6.50% (reset CMT5 +2.629%).

These deals were well absorbed by the market, reflecting both the diversity of issuers and the ongoing appetite for yield and income.

Second-quarter earnings confirmed the resilience of the US banking sector. Net interest income (NII) generally trended upward, with several banks raising full-year NII guidance. Margin expansion was supported by fixed-asset repricing, modest loan growth and easing deposit cost pressure. Regional banks reported average loan growth of about 1% quarter over quarter, with commercial and industrial portfolios leading the way. Some banks saw sequential loan growth of 2% or more, partly driven by businesses accelerating inventory builds in anticipation of tariffs.

Credit quality remained stable or improved, with net charge-offs and nonperforming asset ratios generally flat or declining. Allowance levels were largely unchanged or slightly reduced, and banks continued to proactively manage riskier segments, especially office commercial real estate, with no signs of systemic deterioration. Capital positions remain robust, with most banks operating well above regulatory minimums and several announcing or executing share repurchases. Management teams remain optimistic for the second half of 2025, expecting continued NII growth, stable credit and capital flexibility to support higher payouts and selective loan growth.

The macro backdrop softened notably in July. Payrolls rose just 73,000 with large downward revisions to May and June. The unemployment rate ticked up to 4.2%, and labor force participation fell to 62.2%, with immigration restrictions likely contributing to the decline. While the rise in unemployment remains within the past year's range, the slower pace of job creation keeps downside risks elevated. Federal Reserve chair Jerome Powell has emphasized the unemployment rate as a key metric. Another employment report is due before the September 17 FOMC meeting, where markets are now pricing in a rate cut.

The fiscal backdrop is also shifting. The One Big Beautiful Bill Act (OBBBA), signed into law on July 4, introduces \$3.4 trillion in tax cuts and spending over ten years, with an additional \$700 billion in interest costs. Despite its size, the bill hasn't triggered a meaningful reaction in the Treasury market. The muted response reflects several factors: Much of the bill extends existing provisions, and new tariff revenues (estimated at \$2.8 trillion over 10 years) are projected to help offset the fiscal impulse. The Fed has maintained a restrictive posture and an easing bias, with Powell stating that the bill is "not particularly stimulative" at the July FOMC meeting. However, long-term risks remain. Debt-to-GDP ratios are projected to exceed 120% by 2035, and term premium models suggest a potential 70 to 80 basis point upward drift in long-term yields. The risk of a "Liz Truss moment"—a sudden market repricing due to fiscal complacency—can't be ignored.

Looking ahead

As we enter the final stretch of summer, preferreds are navigating a more complex macro and regulatory landscape. Disinflation trends have stalled with tariff uncertainty. Labor market softness and fiscal uncertainty are shifting the policy outlook. The Fed's easing bias is now paired with market expectations for a September rate cut, while the OBBBA's muted fiscal impulse and rising tariff revenues are helping contain long-end yields for now.

Bank fundamentals remain strong, and capital distributions are likely to increase in Q3 and Q4. We wouldn't be surprised to see more calls and refinancing from the 2020 vintage of preferred issuance. Political risks, including rhetoric on Fed independence, fiscal spending and tariff-led inflation, may lift term premia and support demand for income-generating hybrids. We continue to favor callable fixed-to-floating structures with qualified dividend income treatment for taxable investors, particularly in the bank and utility sectors. High yields, stable credit and supportive technicals should continue to attract investor demand, positioning preferreds for continued strength in the months ahead.

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