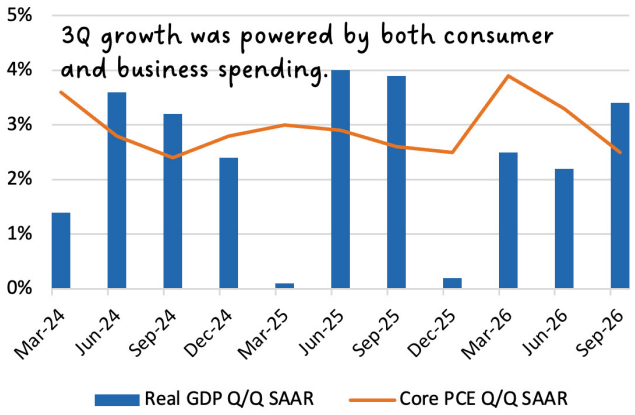
Touchstone Investments®
DISTINCTIVELY ACTIVE®

Fixed Income:
Economic Backdrop

Authors: Erik M. Aarts, CIMA / James Macey, CFA, CAIA / Tim Paulin, CFA / Crit Thomas, CFA, CAIA **November 3, 2026**

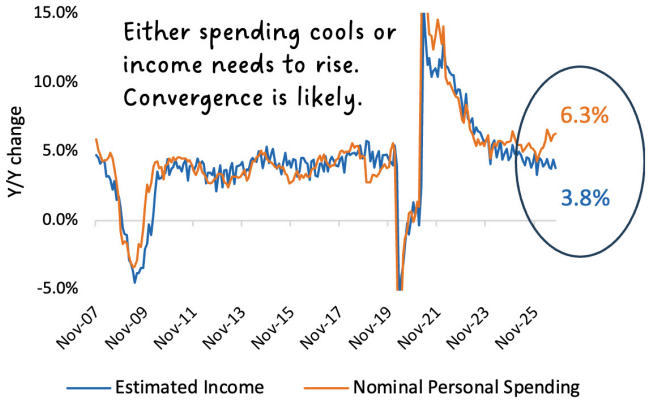
- **Growth Has an AI Assist:** The economy posted surprisingly strong growth in the third quarter, with real GDP rising 3.4% annualized, supported by consumer spending and stronger business investment, including information processing equipment. AI-related investment is playing an increasingly important role across data centers, semiconductors, power and related equipment. But growth remains uneven and some momentum faded late in the quarter. Data center construction continues to rise even as construction outside data centers has declined, while housing remains pressured by elevated financing costs.
- **Scrappy Consumer:** Consumers remained a powerful engine of third quarter growth, contributing roughly 2.5 percentage points to the economy's 3.4% expansion. Historically low initial unemployment claims remain an important support, but spending outpaced income during the quarter and households entered the fourth quarter with less momentum. Real spending was essentially flat in September, real disposable income declined, and the savings rate fell to 3.8%. Healthy employment should continue to support spending, but slower income growth and less savings cushion point toward moderation.
- **Inflation Remains Sticky:** Inflation has moderated, but progress toward the Fed's 2% target has stalled. Headline PCE inflation reached 3.6% in September, while core PCE remained elevated at 3.1%. Energy remains an important contributor, while goods inflation is firming amid strong demand for technology equipment and other inputs. With inflation still well above target and new price pressures emerging, the Fed has more work to do.
- **Fed Has Work to Do:** Strong economic growth and inflation well above target would ordinarily argue for additional monetary tightening. The Fed held rates in October after removing some accommodation in September, while higher market yields tightened financial conditions. Chair Warsh continues to avoid forward guidance, but other policymakers suggest the Committee remains biased toward another rate increase, potentially in December. Unless inflation expectations become unanchored, we expect a modest policy adjustment rather than a significant tightening cycle, particularly if financial conditions continue to do some of the Fed's work.
- **Measured Risk-Taking:** Growth and corporate earnings remain supportive of TAAC's moderate equity overweight, while sticky inflation, elevated financing costs and increasing dispersion argue against becoming more aggressive. Within fixed income, higher yields offer attractive income and improved prospective returns, while October provided encouraging evidence that high-quality bonds can diversify portfolios when risk assets weaken.

Real GDP and Inflation



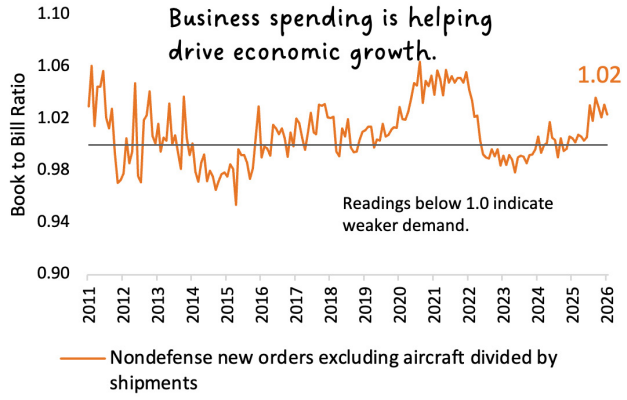
Source: Bloomberg. 3 years of quarterly data through Sep 2026. SAAR = Seasonally Adjusted Annual Rate.

Income and Spending



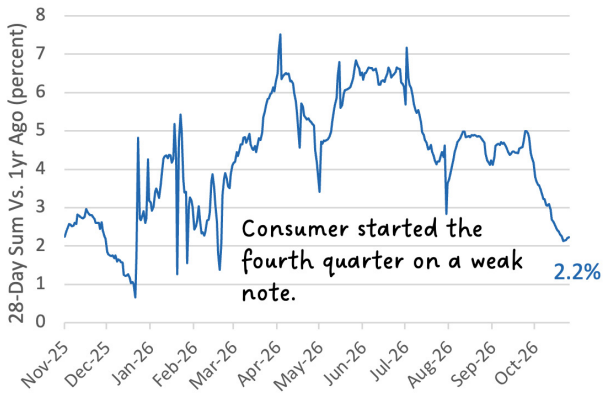
Source: Bloomberg. 20 years of monthly data through Sep 2026; Estimated Income is the product of number of employe, hours worked, and hourly wage.

Capital Goods Book to Bill Ratio



Source: Bloomberg. 15 years of monthly data through Sep 2026.

Credit and Debit Card Transactions



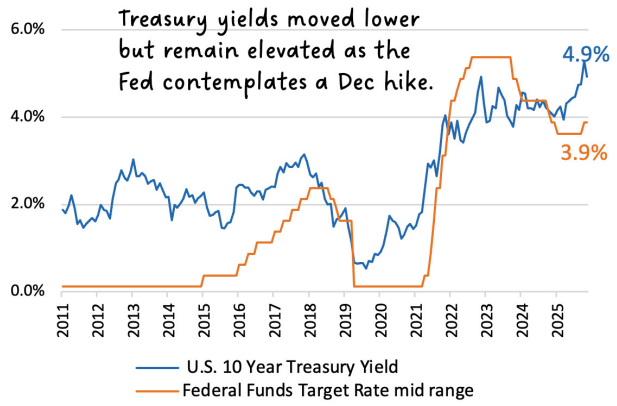
Source: Bloomberg. 1 year of daily data through Oct 26 2026.

Fixed Income:
Interest Rate Risk

Authors: Erik M. Aarts, CIMA / James Macey, CFA, CAIA / Tim Paulin, CFA / Crit Thomas, CFA, CAIA **November 3, 2026**

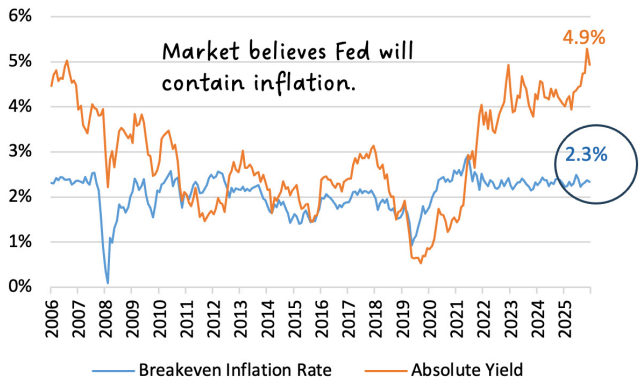
- **AI Cuts Both Ways:** AI has become an important influence on rates as enormous investment needs compete with government borrowing for capital. Continued investment can support growth and higher real yields but also raises questions about whether that investment will generate adequate returns. As markets increasingly scrutinize the economics of the AI buildout, disappointment could tighten financial conditions, slow investment and increase demand for high quality bonds. The new equilibrium for rates may be higher, but it is not necessarily one-directional.
- **Bonds Rediscover Their Balance:** Falling Treasury yields drove a sharp rebound across fixed income in October, with the Bloomberg Long Term Treasury Index gaining 5.2% and the Bloomberg U.S. Aggregate returning 2.4%, reversing much of September's selloff. Returns generally increased with maturity, demonstrating the diversification benefit duration can provide when yields fall. One month does not establish a new correlation regime, but October provided encouraging evidence that higher starting yields have restored some of fixed income's traditional shock-absorber role.
- **Flatter Curve Message:** The Treasury curve has flattened meaningfully since February. With inflation still sticky and the Fed retaining a tightening bias, front-end yields remain anchored by policy expectations while longer yields increasingly reflect the possibility that restrictive conditions will moderate growth and contain inflation. A more hawkish Fed does not necessarily mean higher long-term yields if investors believe tighter policy will ultimately work. Heavy Treasury supply and elevated term premiums remain important risks at the long end.
- **Not All Duration Is Created Equal:** Where investors source duration may matter as much as how much they own. Treasuries offer protection against economic weakness but remain exposed to term-premium risk. Investment-grade corporates generally provide additional duration and income, but with relatively tight spreads. Mortgage-backed and other securitized assets provide income while amortization, repayments and prepayments return capital for reinvestment. Active managers can combine these exposures to balance income, duration, spread risk and cash flow characteristics.
- **Income, Diversification and Optionality:** The case for fixed income has strengthened. Real yields remain elevated, starting income is attractive, and October demonstrated that bonds may provide meaningful diversification when market risks shift. We remain neutral on duration, favoring intermediate maturities that offer attractive carry while limiting exposure to long-end fiscal and term-premium risk. Bonds no longer need falling rates to work, but October showed how much they can benefit when rates do fall.

Interest Rates



Source: Bloomberg. 15 years of monthly data through Oct 2026.

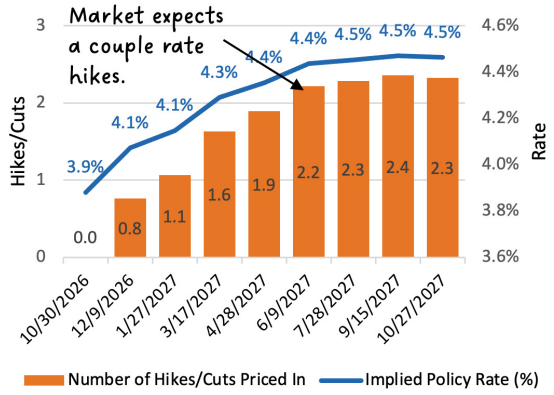
U.S. 10-year Treasury Bond



Source: Bloomberg. 20 years of monthly data through Oct 2026. Breakeven inflation rate is a measure of expected inflation derived from the difference between the 10-year Treasury yield and the 10-year TIPS yield.

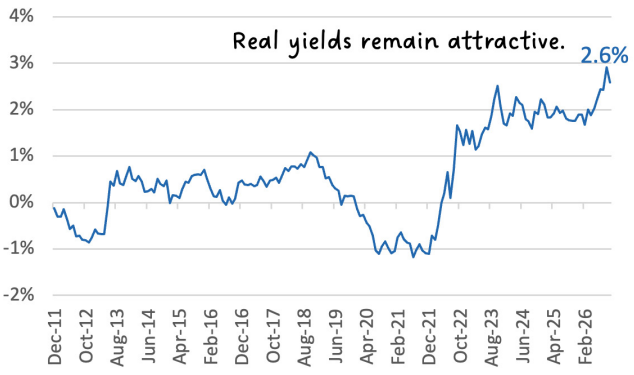
Federal Funds Rate

Implied Overnight Rate & Number of 25bp Hikes/Cuts



Source: Bloomberg. Data as of Oct 30 2026.

U.S. 10-year Treasury Inflation-Protected (TIPS) Yield

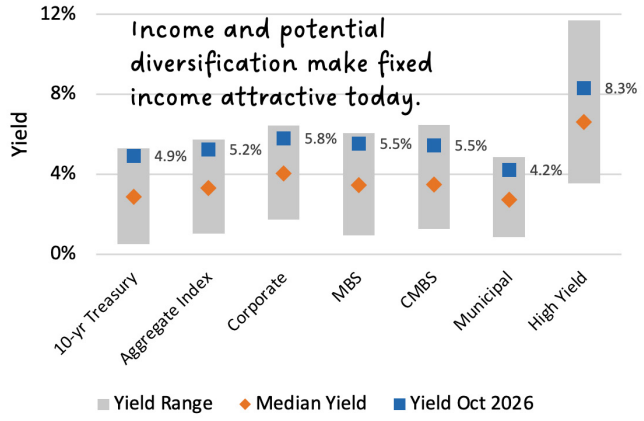


Source: Bloomberg. 15 years of monthly data through Oct 2026.

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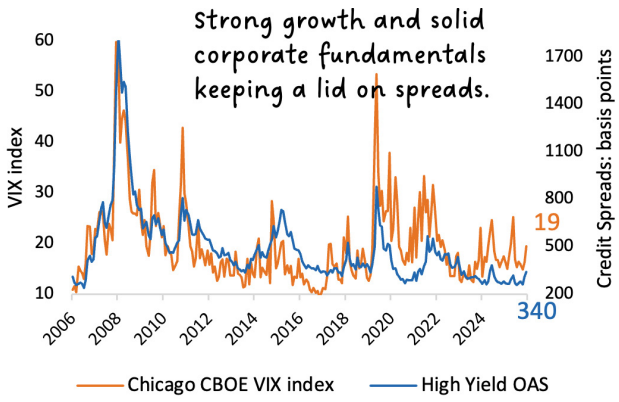
- **AI Gets More Complicated:** AI-related financing tests the market's capacity and willingness to fund the buildout. Demand for computing remains strong, but investors are becoming more selective as issuance grows and questions increase around leverage, free cash flow and whether investments can earn their cost of capital. Financing structures are also becoming more complex. Beyond senior unsecured debt backed by strong balance sheets, investors increasingly need to understand collateral, guarantees, counterparties and contractual relationships. In the AI debt universe, understanding the structure may be just as important as understanding the issuer.
- **Stress Remains Concentrated:** Credit markets have become more cautious, but the repricing remains concentrated among weaker borrowers. Over the past year, CCC bond spreads have widened more than 500 basis points and yields have climbed to 15.8%, while BB and single-B spreads have only moved modestly higher. Leveraged loans have broadly remained resilient, although distress is increasing among weaker borrowers as refinancing costs rise. We have yet to see fundamental deterioration across higher-quality credit, reinforcing our preference for quality while leaving room for active opportunities within high yield and loans.
- **Yield, Not Spread, Is Doing the Work:** September's selloff and October's rally were primarily driven by Treasury rates rather than major changes in credit spreads. Spreads widened in October, particularly in high yield, leveraged loans and emerging-market debt, but remain below their 10-year medians across most major sectors. Investment-grade widening has been modest, supported by healthy economic growth and corporate fundamentals. Meanwhile, all-in yields remain near the upper end of their historical ranges.
- **Structure Matters:** With spreads providing limited compensation for mistakes, how investors lend matters as much as who they lend to. We increasingly see credits with seniority, strong covenants, quality collateral and structural protections as key to improving outcomes. That discipline applies across corporate credit, loans, securitized assets and increasingly complex AI financings. Higher financing costs are also improving lender terms in selected transactions, creating opportunities for active managers able to distinguish between attractive complexity and uncompensated risk.
- **Be Selective, Not Defensive:** Healthy growth and corporate earnings continue to support credit, but tight spreads, refinancing costs and extreme dispersion at the lower end argue against indiscriminate risk-taking. TAAC remains neutral on investment grade and underweight high yield, reflecting a preference for quality rather than an absence of opportunity. Attractive starting yields allow investors to emphasize stronger credits across both investment-grade and below-investment-grade markets, while active management can selectively pursue opportunities where pricing, structure and downside protection justify the risk.

10-year Yield Range for Fixed Income Sectors



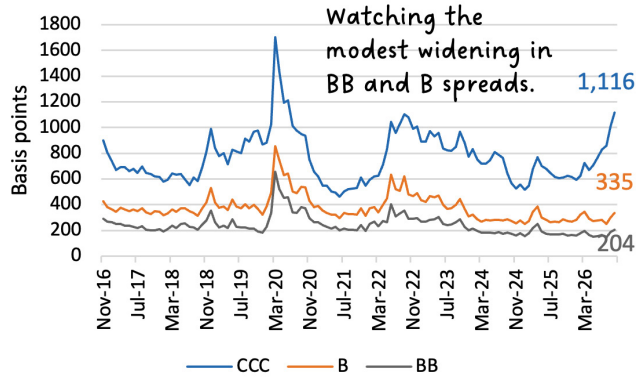
Source: Bloomberg. 10 years of monthly data through Oct 2026.

Credit Spread versus Implied Stock Volatility



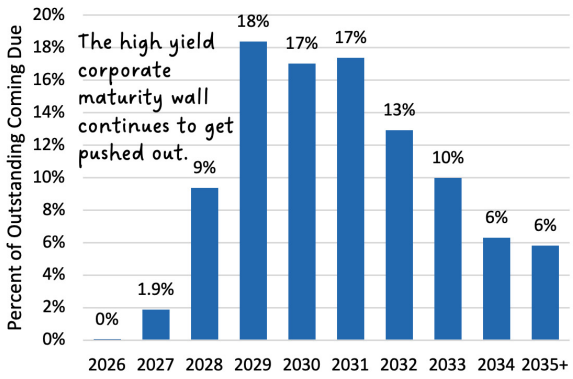
Source: Bloomberg. 20 years of monthly data through Oct 2026.

Bloomberg U.S. HY Option Adjusted Spreads



Source: Bloomberg. 10 years of monthly data through Oct 30 2026.

Bloomberg High Yield Maturity Schedule



Source: Bloomberg. Data as of Sep 2026.

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The Indexes mentioned are unmanaged statistical composites of stock market or bond market performance. Investing in an index is not possible.

Total Returns

	Oct 2026	YTD	2025	2024	2023	Duration years
Bloomberg Long Term Treasury	5.2%	-2.9%	5.6%	-6.4%	3.1%	13.7
Bloomberg U.S. TIPS	2.6%	0.4%	7.0%	1.8%	3.9%	5.6
Bloomberg U.S. Aggregate	2.4%	-0.5%	7.3%	1.3%	5.5%	5.8
Bloomberg U.S. Agg Corporates	2.2%	-1.0%	7.8%	2.1%	8.5%	6.4
Bloomberg U.S. Agg ABS	1.1%	1.4%	5.9%	5.0%	5.5%	2.9
Bloomberg U.S. Agg MBS	3.1%	-0.3%	8.6%	1.2%	5.0%	5.7
Bloomberg U.S. Agg CMBS	1.5%	0.4%	7.7%	4.7%	5.4%	3.6
Bloomberg Municipal Bond	3.9%	-0.5%	4.2%	1.1%	6.4%	6.9
Bloomberg 1-3 year Corporate	0.9%	1.9%	5.9%	5.3%	5.5%	1.8
S&P Preferred Stock	-4.2%	-3.9%	5.0%	9.2%	12.0%	NA
Bloomberg High Yield	0.3%	0.4%	8.6%	8.2%	13.4%	3.1
S&P UBS Leveraged Loan	-0.2%	3.2%	5.9%	9.1%	13.0%	NA
Bloomberg Global Agg	1.4%	-1.3%	8.2%	-1.7%	5.7%	6.1
Bloomberg Emerging Markets USD	1.3%	-0.3%	11.1%	6.6%	9.1%	5.7

Yields

			Last 10 years			
	Oct 2026	YTD Change bps	Current Percentile	Median	Min	Max
10 year Treasury	4.9%	76	99	2.9%	0.5%	5.3%
2 year Treasury	4.6%	111	90	2.6%	0.1%	5.2%
10 year TIPS	2.6%	69	99	0.8%	-1.2%	2.9%
Bloomberg U.S. Aggregate	5.2%	92	97	3.3%	1.0%	5.7%
Bloomberg U.S. Agg Corporate	5.8%	98	96	4.0%	1.7%	6.4%
Bloomberg U.S. Agg ABS	5.2%	107	88	3.1%	0.4%	6.0%
Bloomberg U.S. Agg MBS	5.5%	89	98	3.5%	0.9%	6.1%
Bloomberg U.S. Agg CMBS	5.5%	102	89	3.6%	1.4%	6.6%
Bloomberg Municipal Bond	4.2%	62	97	2.7%	0.9%	4.9%
Bloomberg 1-3 year Corporate	5.2%	117	85	3.2%	0.5%	6.2%
Bloomberg High Yield	8.3%	178	86	6.6%	3.5%	11.7%
S&P UBS Leveraged Loan	9.9%	184	79	6.2%	3.6%	13.1%
Bloomberg Global Agg	4.3%	73	98	2.0%	0.8%	4.5%
Bloomberg Emerging Markets USD	6.8%	111	77	5.8%	3.5%	8.7%

Option Adjusted Spreads (bps)

			Last 10 years			
	Oct 2026	YTD Change	Current Percentile	Median	Min	Max
Bloomberg U.S. Corporate Agg	90	12	29	106	71	373
Bloomberg 1-3 year Corporate	59	8	57	56	31	390
Bloomberg U.S. Agg ABS	51	-1	56	48	22	325
Bloomberg U.S. Agg MBS	34	12	43	36	7	132
Bloomberg U.S. Agg CMBS	75	0	48	84	62	275
Bloomberg High Yield	340	74	44	351	250	1100
S&P UBS Leveraged Loan (discount margin)	510	55	71	473	379	1275
Bloomberg Emerging Markets USD	197	19	11	285	152	720

For Index Definitions see: TouchstoneInvestments.com/insights/investment-terms-and-index-definitions

2024 – Economic growth continued unabated, driven by consumer spending. Inflation moderated further. The Federal Reserve pause continued until September, after which it cut interest rates three times by a total of 1 percentage point. Bond yields rose in response, resulting in only modest gains for high quality fixed income but better returns for riskier areas of fixed income.

2025 – The economy remained resilient, and inflation stayed sticky, keeping yields elevated but allowing high-quality intermediate maturity bonds to generate solid returns as the Fed cut rates late in the year. Steady growth and improving liquidity supported tighter spreads, driving performance in credit-sensitive areas of the fixed income market.

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The Touchstone Asset Allocation Committee (TAAC) consisting of Erik M. Aarts, CIMA – Vice President and Senior Fixed Income Strategist, James Macey, CFA, CAIA – Assistant Vice President, Global Market Strategist, Tim Paulin, CFA – Senior Vice President, Investments and Practice Consulting, and Crit Thomas, CFA, CAIA – Global Market Strategist, develops in-depth asset allocation guidance using established and evolving methodologies, inputs and analysis and communicates its methods, findings and guidance to stakeholders. TAAC uses different approaches in its development of Strategic Allocation and Tactical Allocation that are designed to add value for financial professionals and their clients. TAAC meets regularly to assess market conditions and conducts deep dive analyses on specific asset classes which are delivered via the Asset Allocation Summary document. Please contact your Touchstone representative or call 800.638.8194 for more information.

A Word About Risk

Investing in fixed-income securities which can experience reduced liquidity during certain market events, lose their value as interest rates rise and are subject to credit risk which is the risk of deterioration in the financial condition of an issuer and/or general economic conditions that can cause the issuer to not make timely payments of principal and interest also causing the securities to decline in value and an investor can lose principal. When interest rates rise, the price of debt securities generally falls. Longer term securities are generally more volatile. Investment grade debt securities which may be downgraded by a Nationally Recognized Statistical Rating Organization (NRSRO) to below investment grade status. U.S. government agency securities which are neither issued nor guaranteed by the U.S. Treasury and are not guaranteed against price movements due to changing interest rates. Mortgage-backed securities and asset-backed securities are subject to the risks of prepayment, defaults, changing interest rates and at times, the financial condition of the issuer. Foreign securities carry the associated risks of economic and political instability, market liquidity, currency volatility and accounting standards that differ from those of U.S. markets and may offer less protection to investors. Emerging markets securities which are more likely to experience turmoil or rapid changes in market or economic conditions than developed countries.

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