Principal Fixed Income

Principal Asset Management℠

MULTI-SECTOR

Monthly commentary

31 JANUARY 2026

OVERVIEW

Most major fixed income sectors posted positive results in January. High yield, municipals and emerging market debt led total returns, while bank loans and U.S. Treasurys were the laggards. Geopolitical headlines drove volatility during the month, but performance was broadly supported by resilient economic data and investors' persistent appetite for risk.

RATES

The U.S. yield curve shifted slightly higher with the 2-year up 5 bps, the 10-year up 7 bps, and the 30-year up 3bps. Globally, yields generally moved higher, most notably in Japan, following the new prime minister's call for a snap election in February and a pledge to cut taxes and pursue additional expansionary fiscal policies. These announcements spurred investor concern about Japan's debt burden and led to a meaningful selloff across the curve with Japanese government bond yields jumping 15-30bps higher over a matter of a few days.

SPREADS

Credit spreads tightened with U.S. and global investment grade closing the month 5 bps tighter and high yield 1 bp tighter, reaching levels last seen in the 1990s. The tightening was driven by a strong start to Q4 earnings season and a seemingly insatiable amount of demand for credit risk. Despite heavy supply in January, it was easily absorbed by the market, and solid technicals remain a key tailwind for credit markets.

ECONOMY

December U.S. economic data was largely in-line with expectations and supportive of further rate cuts later this year. The labor market continued to soften, with only 50k jobs added in December and the unemployment rate remaining elevated at 4.4%. Headline CPI came in at 2.7% year-over-year, with core CPI slightly lower at 2.6%. Inflation remains above the Fed's 2% target, but services inflation, which accounts for ~60% of total inflation, remains on a downward trajectory.

POLICY

We expect monetary policy to diverge globally, with the U.S. Federal Reserve likely to cut rates, Europe remaining on pause, and Japan moving toward further rate hikes. As expected, the Federal Reserve (Fed) left the policy rate unchanged at 3.50–3.75% at its January meeting, citing solid economic growth, a stable labor market, and somewhat elevated inflation. The committee signaled a more constructive tone on the economy but reiterated its continued focus on incoming data, which will inform decisions at future meetings. Outside the U.S., the Bank of Japan (BOJ) also had its first meeting of the year in January and left rates unchanged at 0.75%. Despite the pause, markets are anticipating multiple hikes from the BOJ later this year given expectations of stronger growth and higher inflation.

OUTLOOK

Looking ahead, we remain constructive on fixed income markets as we expect more growth-friendly policies like deregulation and tax cuts to gain traction, providing a solid backdrop for credit. We're also starting to see signs of productivity growth, which we're watching closely. Productivity gains could give the Fed more leeway to cut rates and continue supporting modest economic growth without stoking inflation. Our Macro Risk Outlook (MRO) score remains "Risk-On," and we are relatively neutral duration versus benchmarks with a steepening bias, favoring the short-to-intermediate part of the curve. Despite spreads being tight across most credit sectors, we remain selectively constructive on risk and favor sectors with strong fundamentals and supportive technicals.

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Representative Multi-Sector Portfolio	Month-end Positioning | Last 12 Months												Bloomberg U.S. Aggregate Index
	Feb-25	Mar-25	Apr-25	May-25	Jun-25	July-25	Aug-25	Sep-25	Oct-25	Nov-25	Dec-25	Jan-26	Jan-26
Active Market Value (%)*													***Market Value (%)***
Treasurys	-37	-36	-35	-36	-36	-38	-39	-35	-35	-35	-37	**-39**	46
Gov't Related	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	-3	**-3**	3
Agency MBS	4	4	4	5	4	4	4	8	8	8	8	**2**	24
IG Credit	9	10	11	13	14	14	13	5	6	5	6	**8**	24
High Yield	13	11	9	10	11	11	11	12	12	13	13	**16**	–
Bank Loans	5	5	5	3	3	3	3	3	3	2	2	**2**	–
Emerging Market	1	1	1	1	1	1	1	1	1	1	1	**1**	1
Securitized Debt	12	13	12	14	13	12	12	12	11	11	12	**14**	2
ABS	9	10	9	10	9	8	8	8	8	8	8	**10**	0
CMBS	3	3	3	4	4	4	4	4	3	3	4	**4**	1
Cash/Other	-4	-5	-4	-7	-7	-4	-2	-3	-3	-2	-2	**0**	–
***Active Duration** (years)**													***Duration** (years)*
Portfolio	**0.24**	**0.26**	**0.27**	**0.35**	**0.20**	**0.34**	**0.10**	**0.05**	**0.14**	**0.34**	**0.36**	**0.00**	**5.76**

*Active positions are relative to the Bloomberg U.S. Aggregate Index. Positive (+) number = overweight or out-of-benchmark exposure; Negative (-) number = underweight. Market value weight of Bloomberg U.S. Aggregate Index may not total 100% due to rounding.

As of 31 January 2026. Source: Principal Global Investors. *Active positions are relative to the Bloomberg U.S. Aggregate Index, which 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. These major sectors are subdivided into more specific indices that are calculated and reported on a regular basis. Indices are unmanaged and do not take into account fees, expenses, and transaction costs, and it is not possible to invest in an index. Past performance is no guarantee of future results and should not be relied upon to make investment decisions. Portfolio positioning provided is from the representative portfolio of the Multi-Sector strategy. Each portfolio included in the strategy is managed according to unique investment restrictions & limitations and, as a result, their characteristics may vary from those of the representative portfolio presented.

Risk considerations

Investing involves risk, including possible loss of principal. Past performance is no guarantee of future results. Fixed income investments are subject to interest rate risk; as interest rates rise, their value will decline. Lower-rated securities are subject to additional credit and default risks. Potential investors should be aware that Investment grade corporate bonds carry credit risks, default risk, liquidity risks, currency risks, operational risks, legal risks, counterparty risk and valuation risks. Fixed income and asset allocation investment options that invest in mortgage securities are subject to increased risk due to real estate exposure. Emerging market debt may be subject to heightened default and liquidity risk. Securitized debt presents investors with several risks, including credit, interest rate, prepayment, and liquidity risks. Its reliance on the performance of underlying assets, such as mortgages and auto loans, makes it vulnerable to market volatility and economic downturn.

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