MORNINGSTAR Indexes

Morningstar US Fixed-Income Monitor: April-June 2025

Risk takers rewarded as high yield bonds outperform.

Morningstar
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Contents

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Executive Summary

This is the latest installment of the Morningstar US Fixed-Income Monitor, which is designed to help investors stay on top of the latest trends in the fixed-income asset space as tracked through the lens of four Morningstar fixed-income indexes: Morningstar US 1-3 Month Treasury Bill Index, Morningstar US Treasury Bond Index, Morningstar US Corporate Bond Index, and Morningstar US High-Yield Bond Index.

Key Takeaways

- In the second quarter of 2025, the Federal Reserve maintained a cautious approach by keeping the target federal-fund rate unchanged.
- The US Personal Consumption Expenditures Price Index indicated inflation was still above the 2% target set by the Fed.
- The second quarter witnessed lower nonfarm payroll employment, and a stable unemployment rate.
- The longer-maturity Treasury rates saw an increase of 15-20 basis points while the lower maturity rates remained unchanged. The medium-term rates saw a decline of 15 basis points.
- The Morningstar US High Yield Bond Index provided the best risk/return characteristics over the second quarter of 2025. This was followed by the Morningstar US Corporate Bond Index. The Morningstar US Treasury Bond Index and the Morningstar US 1-3 Month Treasury Bill Index experienced muted returns over the second quarter of 2025.
- The option-adjusted spread for US corporate bonds witnessed a sharp increase in April 2025. The next two months saw the spreads drop to 80 basis points, highlighting investor preference towards riskier assets to capture higher yield.
- The investment-grade corporate bond space posted positive returns of 1.7%, with technology, healthcare and energy sectors contributing the most to the positive second-quarter returns.
- The high-yield corporate bond space posted stellar positive returns of 3.5%, with the healthcare and services sectors providing the highest contribution to the second quarter returns.
- BBB rated corporate bonds witnessed a positive return of 2%. Among high-yield corporate bonds, CCC rated bonds provided 4.75% returns over the second quarter while BB and B rated bonds posted returns to the tune of 3.5%.

Market Update

Federal Reserve Holds Rates Steady Amid Rising Uncertainty

The Fed maintained the target federal-funds rate at 4.25% to 4.50% in both the May and June 2025 Federal Open Market Committee meetings.

The first quarter of 2025 witnessed a 0.5% decline in real gross domestic product as compared with a 2.4% growth in the fourth quarter of 2024.[1] This marks the first decline in real GDP in three years. Projections for 2025, however, indicate heightened economic uncertainty due to the uncertainty surrounding tariffs and wars in the Middle East. The projections for annual real GDP growth in 2025 was downgraded to 1.4% from the earlier projection of 1.7%. Similarly, PCE inflation projections were raised by 30 basis points to 3.0%.[2]

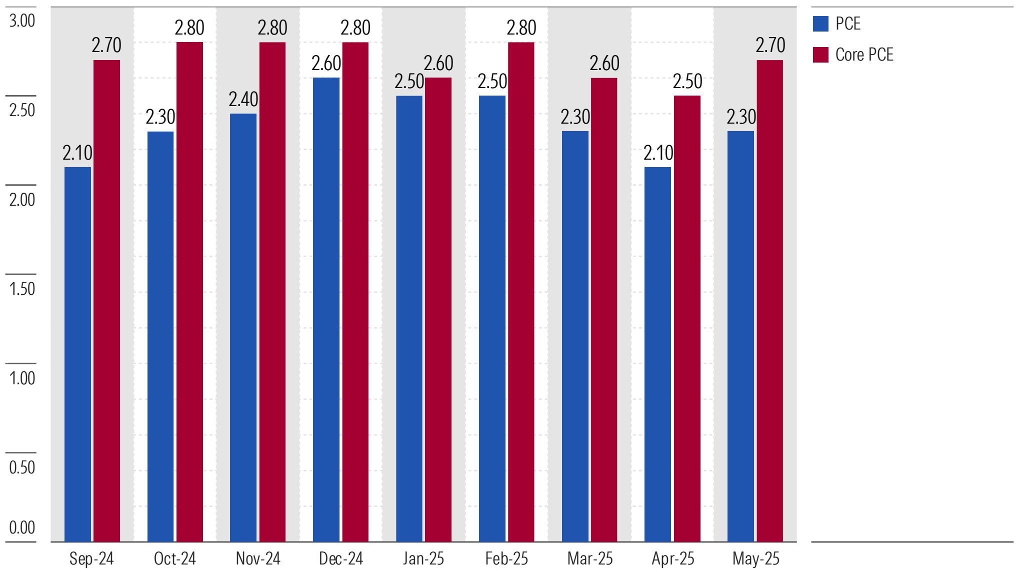
Tariff uncertainty, sticky inflation and a stable economic outlook facilitated the Fed's decision to maintain the status quo in interest rates. The wars and its impact on growth, however, do bring additional complexity to future decisions.

Persistent Inflation: Holding Firm Above the Target 2%

US PCE inflation continued to remain above the Fed's target of 2%. March and April 2025 witnessed a slight decline in both the PCE and Core PCE indexes, only to see it reversed in May 2025. With inflation remaining stubbornly persistent above the target of 2%, the Fed signaled its intention to remain cautious with further rate cuts, especially since the impact from the ongoing tariffs and wars were yet to materialize.

1 Data source for GDP growth rates: Bureau of Economic Analysis, US Department of Commerce, released on June 26, 2025.
2 Real GDP growth rates projections data source: FOMC Projection Material, Federal Reserve.

Exhibit 1 US PCE and Core PCE Inflation Data Year Over Year



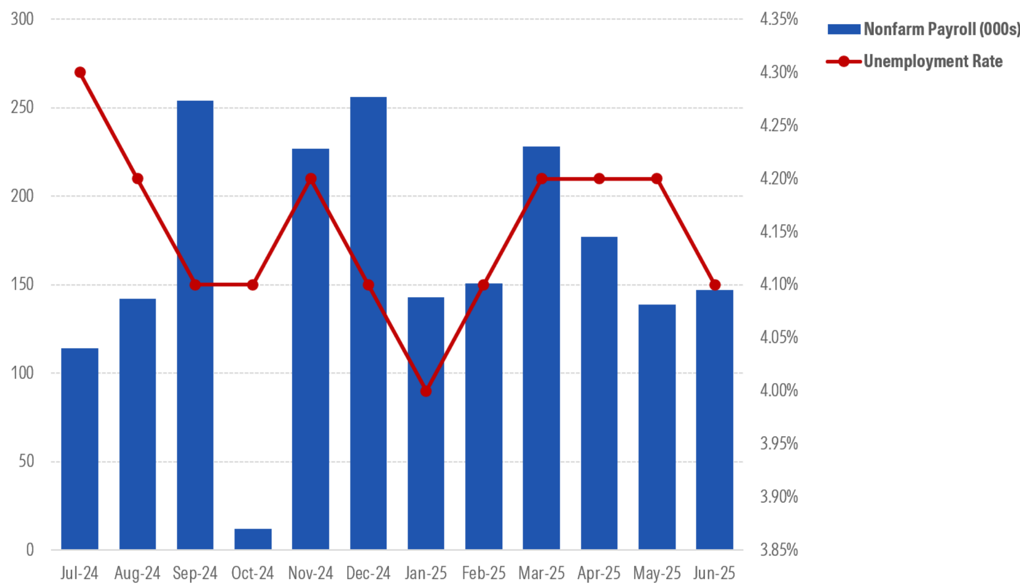
Source: Bureau of Economic Analysis. Data as of June 30, 2025.

Jobs Data Update

US nonfarm payroll employment saw an increase of around 177,000, 139,000 and 147,000 jobs in April, May and June respectively. The second quarter added an average of 154,000 new jobs compared with 174,000 in the first quarter of 2025.

US unemployment remained stable at 4.2% in April and May, with a marginal decline to 4.1% in June 2025. Despite witnessing a decline in growth and jobs, the Fed continued to hold rates steady amid growing concerns of the impact of tariffs and wars on inflation.

Exhibit 2 US Jobs Data

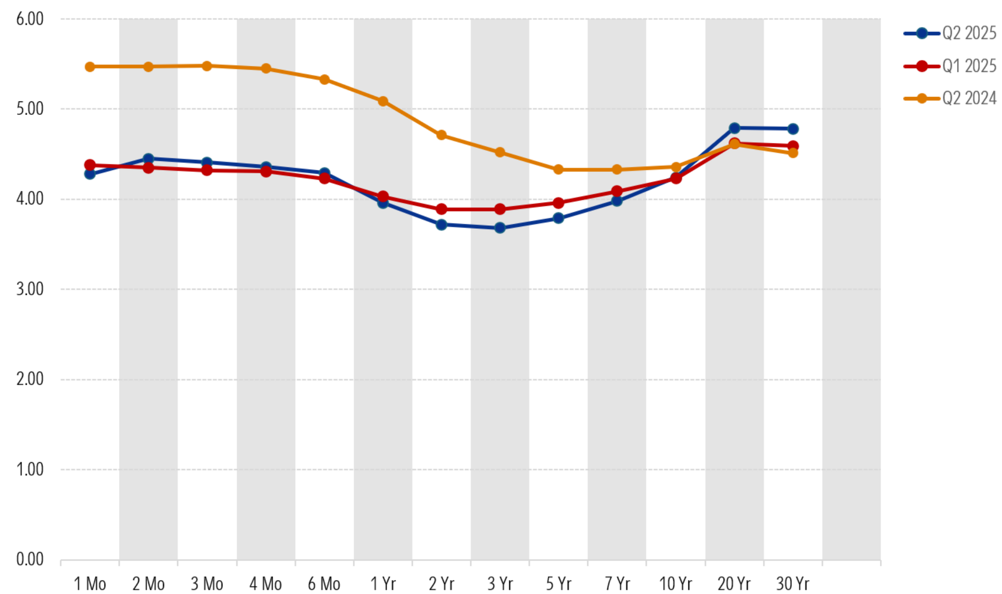


Source: Bureau of Labor Statistics. Data as of July 3, 2025.

US Yield Curve and Interest-Rate Movement Summary

The second quarter of 2025 saw no significant movement in short-term rates. Treasury rates up to one year rose 5 basis points on average. Longer maturity term rates beyond 10 years saw an increase of 15-20 basis points. The medium tenure term rates between two to seven years saw a decline of 15 basis points on average. The term structure has witnessed marginal steepening in the latter part of the curve over the second quarter. However, the term structure has steepened significantly over the last 12 months.

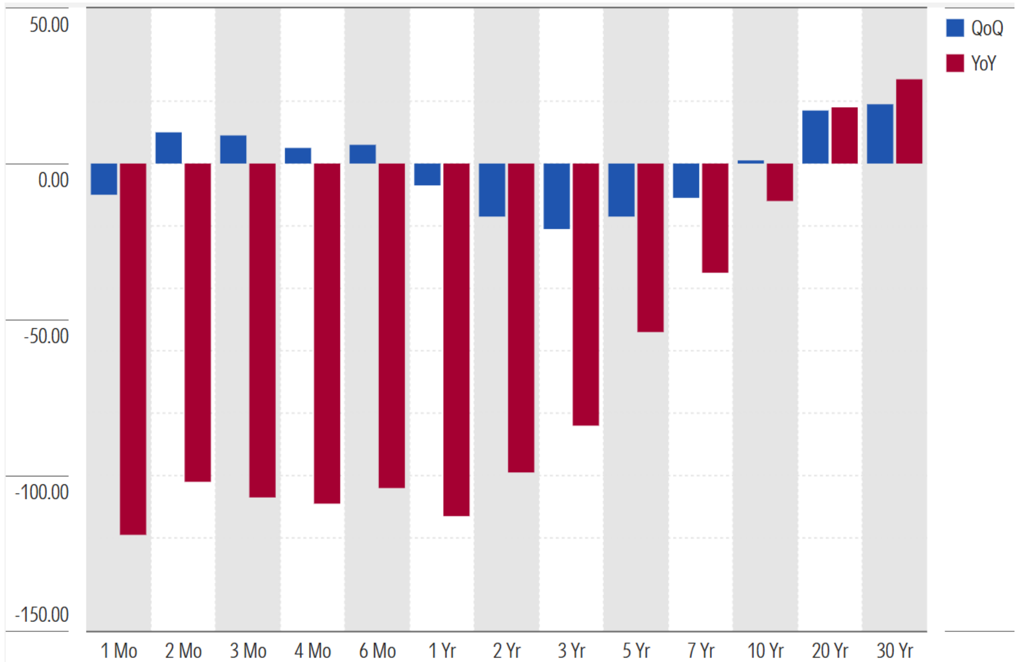
Exhibit 3 Yield Curve



Source: US Department of Treasury. Data as of June 30, 2025.

As can be seen from Exhibit 4, the second quarter witnessed a marginal steepening of the curve. While the lower-maturity Treasury rates remained unchanged, the longer-maturity rates saw an increase of 15-20 basis points.

Exhibit 4 Change in US Term Rates (Basis Points)

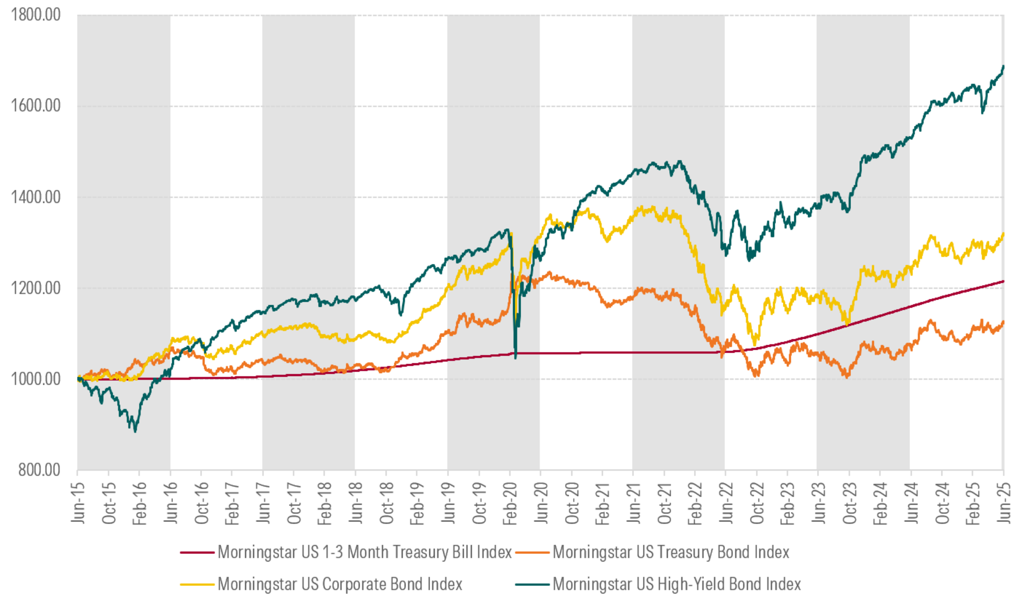


Source: US Department of Treasury. Data as of June 30, 2025.

Morningstar Fixed-Income Indexes Performance Summary

Exhibit 5 highlights the performance of Morningstar US Fixed-Income Indexes. As expected, over the last 10 years, the Morningstar US High-Yield Bond Index has provided the best overall returns, albeit at a higher risk, as can be seen in Exhibit 6.

Exhibit 5 Performance Chart of Morningstar US Fixed-Income Indexes



Source: Morningstar. Data as of June 30, 2025.

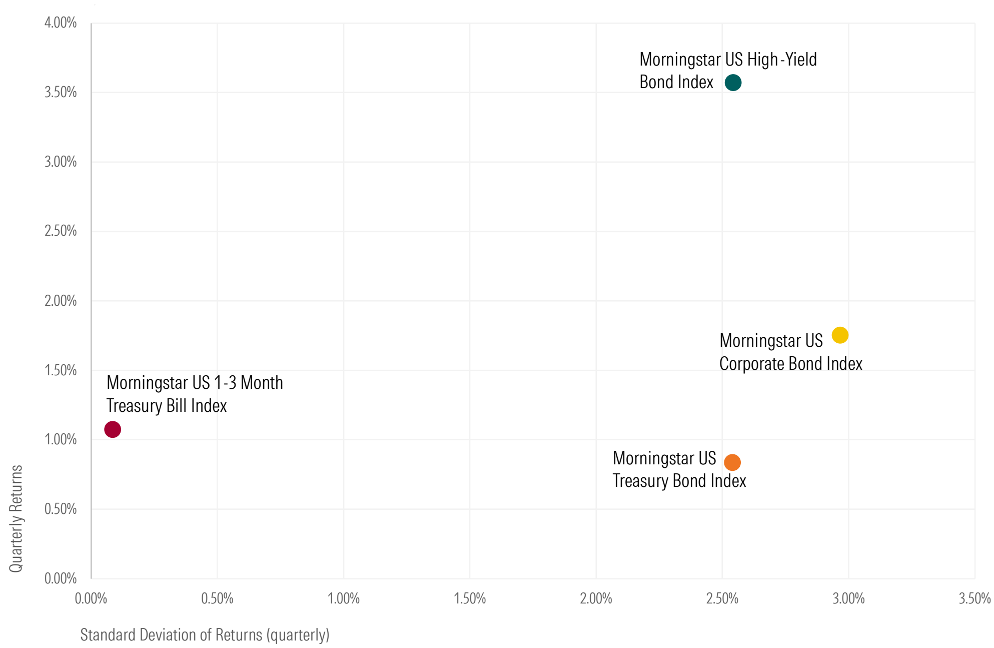
Exhibit 6 Risk/Return Characteristics

Parameters	Morningstar US 1-3 Month Treasury Bill Index	Morningstar US Treasury Bond Index	Morningstar US Corporate Bond Index	Morningstar US High-Yield Bond Index
Start Date	2015-06-30	2015-06-30	2015-06-30	2015-06-30
End Date	2025-06-30	2025-06-30	2025-06-30	2025-06-30
Return (%)	1.97	1.20	2.83	5.38
Risk (%)	0.56	4.87	6.89	7.61

Source: Morningstar. Data as of June 30, 2025.

The comparative risk/return performance of the Morningstar indexes over the last quarter is shown in Exhibit 7. The second quarter of 2025 has seen riskier assets outperform. The Morningstar US High Yield Bond Index led performance in the second quarter of 2025 with a stellar 3.5% returns, followed by the Morningstar US Corporate Bond Index that grew by 1.7%. Gains were primarily driven by the medium-duration profiles of both indexes, which benefited from a decline in medium-term Treasury yields during the quarter. The Morningstar US Treasury Bond Index posted subdued returns in the second quarter of 2025, reflecting investor willingness to gravitate towards riskier assets in search of higher yields. Meanwhile, the Morningstar US 1-3 Month Treasury Bill Index remained flat, as short-term interest rates held steady throughout the quarter.

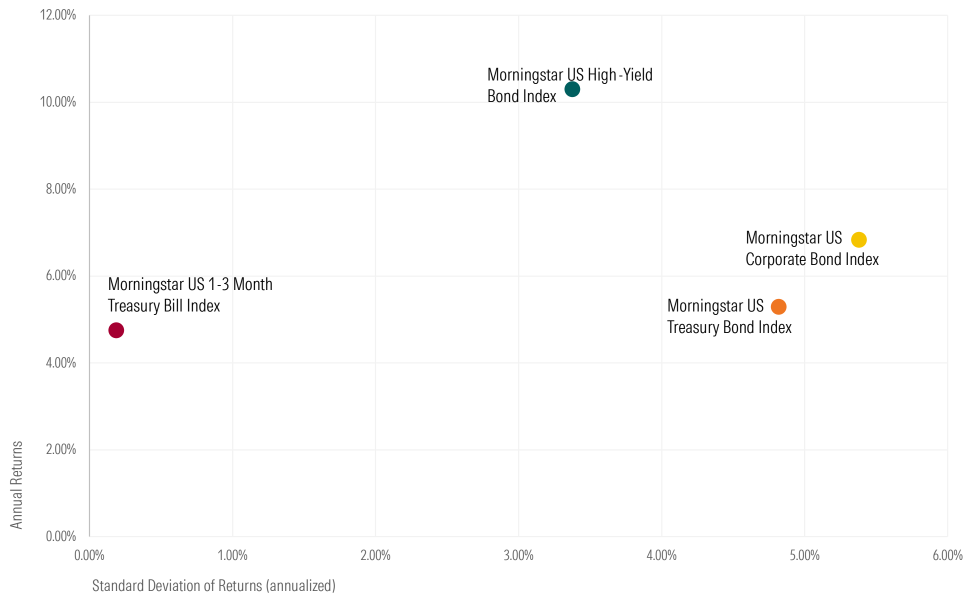
Exhibit 7 Second Quarter 2025 Performance



Source: Morningstar. Data as of June 30, 2025.

Exhibit 8 highlights the comparative performance over the previous 12 months. The Morningstar US High-Yield Bond Index provided the best risk/return characteristics. The previous 12 months have, however, proved to be quite volatile for US Treasury bonds, as showcased by the higher risk and lower returns of the Morningstar US Treasury Bond Index. The Morningstar US Corporate Bond Index has outperformed the US Treasury Bond Index while exhibiting marginally higher volatilities.

Exhibit 8 12-Month Performance Ending June 30, 2025

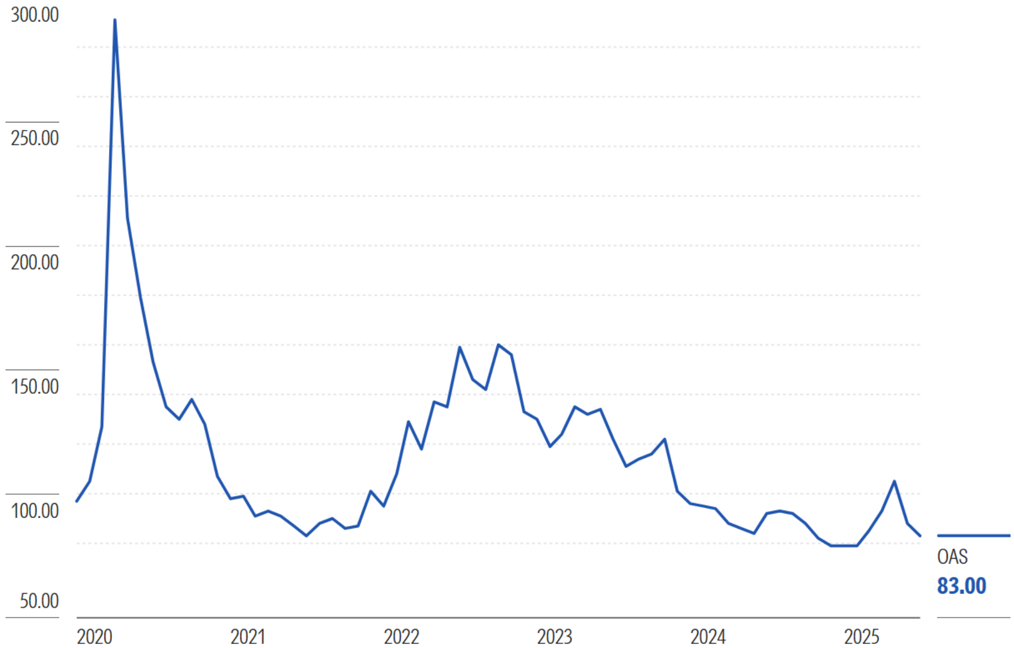


Source: Morningstar. Data as of June 30, 2025.

Spreads Remain Compressed, as Investors Look Towards Higher Yields

As seen in Exhibit 9, the spread between US corporate bonds and US Treasuries has been narrowing over the year. However, April 2025 saw a rapid increase in option-adjusted spread on account of the tariff uncertainties. The spread has increased to 105 basis points in April 2025 from 93 basis points the previous month. However, the spreads quickly subsided over the next couple of months, with June recording an 83 basis point spread.

Exhibit 9 Option-Adjusted Spread of Morningstar US Corporate Bond Index



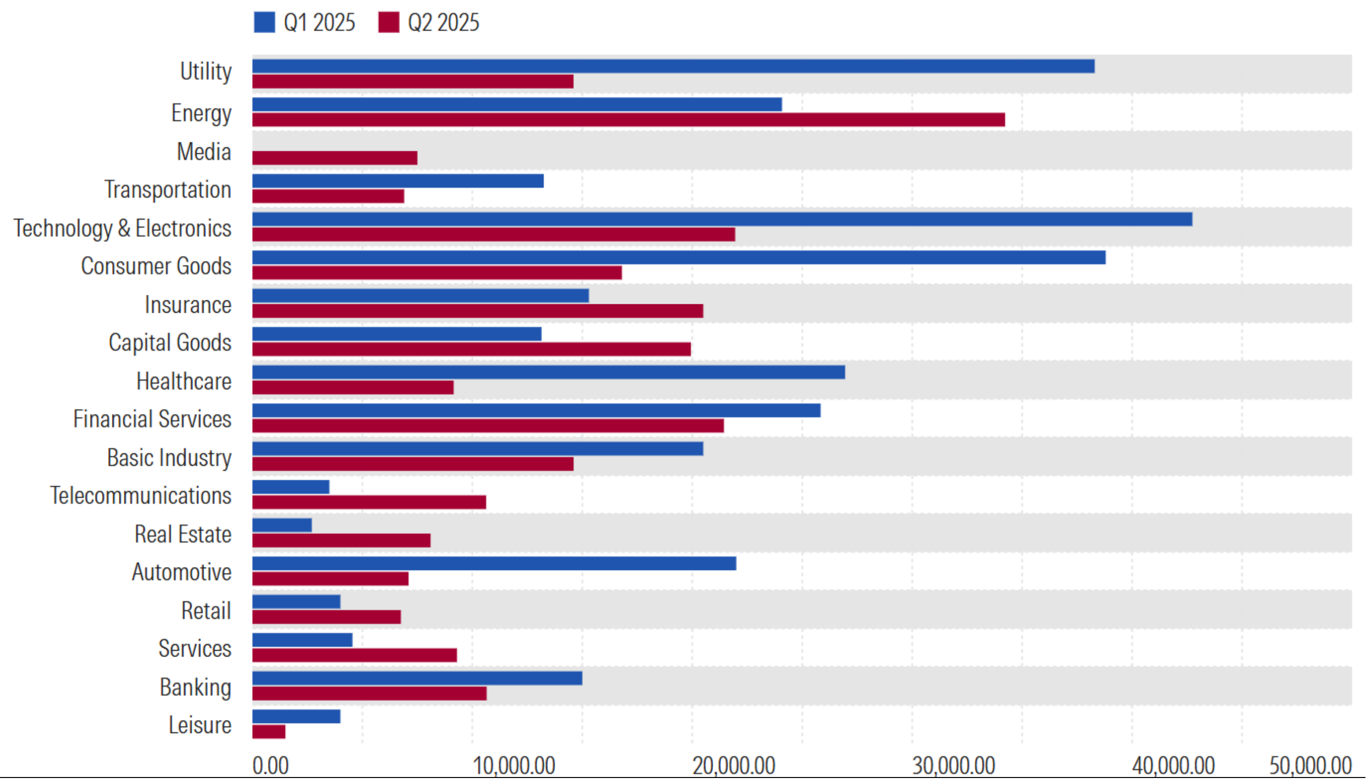
Source: Morningstar. Data as of June 30, 2025.

Sector Spotlight

Technology & Electronics Leads New Investment-Grade Issuances in First Quarter

According to Morningstar US Corporate Bond Index, the second quarter of 2025 witnessed new corporate issuances to the tune of USD 241 billion being added to the index as opposed to USD 314 billion in the first quarter of 2025. The highest issuances were in the technology & electronics, utility and consumer goods sectors as seen in Exhibit 10. Verizon Communications and Siemens Funding, emerged as the leading corporate debt issuers during the period, raising USD 6.6 billion and USD 6.5 billion respectively. Saudi Arabian Oil Company, Petronas Capital, Alphabet each issued USD 5 billion in the second quarter of 2025.

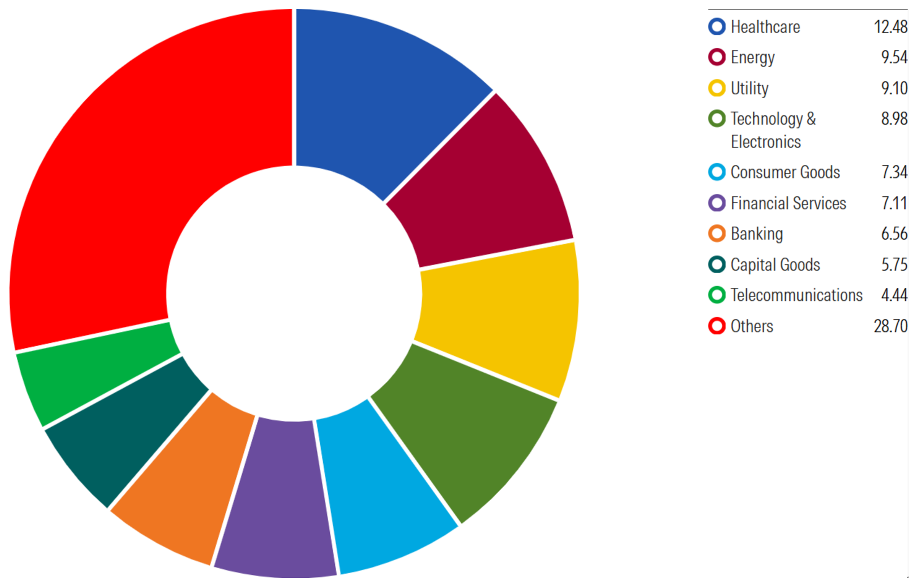
Exhibit 10 New Issuances (USD million)



Source: Morningstar. Data as of June 30, 2025.

As shown in Exhibit 11, the healthcare, energy, utility and technology sectors represent the largest exposures within the Morningstar US Corporate Bond Index, collectively accounting for approximately 40% of the index's total market value.

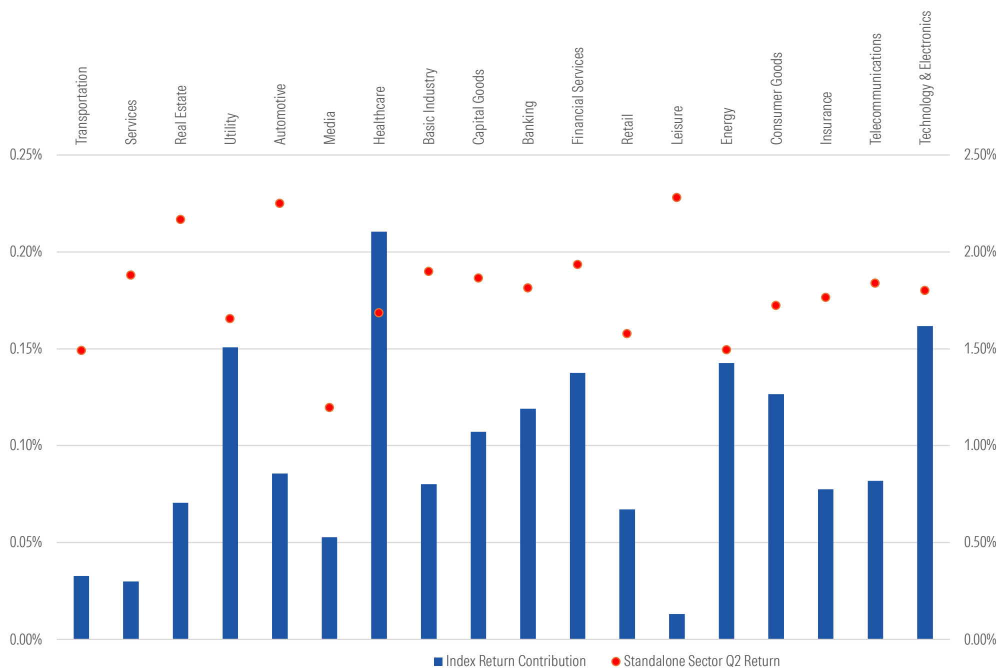
Exhibit 11 Morningstar US Corporate Bond Index Sector Distribution



Source: Morningstar. Data as of June 30, 2025.

The investment-grade corporate bonds represented by the Morningstar US Corporate Bond Index provided positive returns in the second quarter to the tune of 1.7%, driven primarily by overperformance in the healthcare, technology and utility sectors as illustrated in Exhibit 12. On a stand-alone basis, automotive, leisure and real estate registered the highest returns.

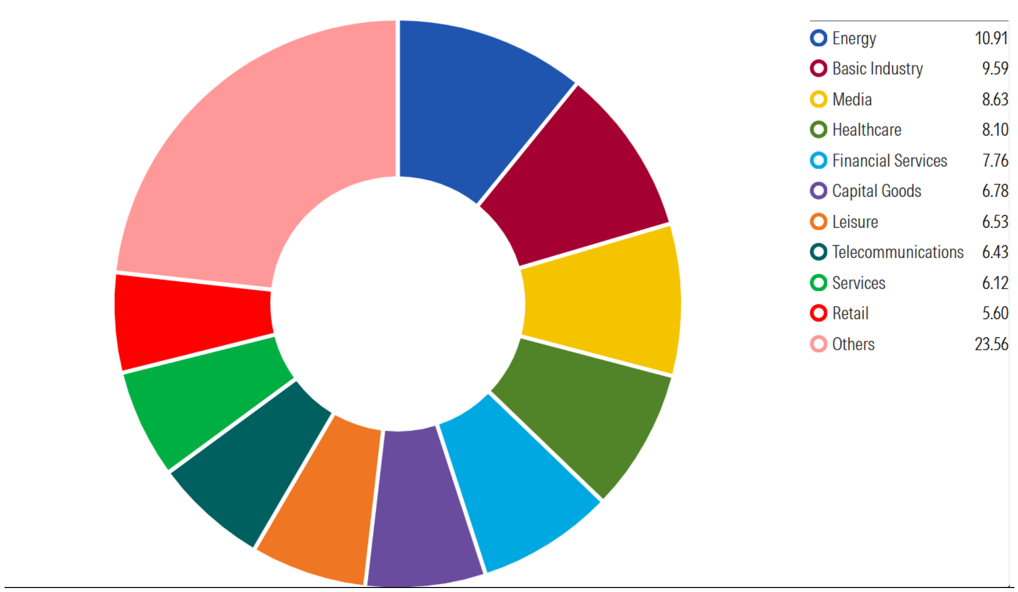
Exhibit 12 Morningstar US Corporate Bond Index Sector Return Contribution



Source: Morningstar. Data as of June 30, 2025.

As shown in Exhibit 13, the energy, basic industry, media and healthcare sectors remain key components of the Morningstar US High-Yield Bond Index, together accounting for approximately 37% of the index's total market value.

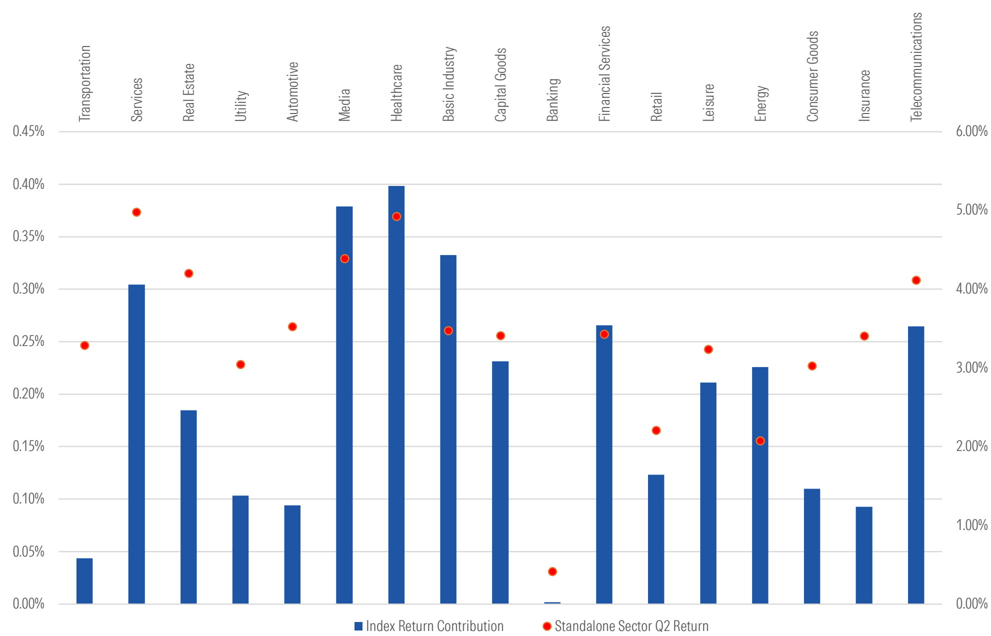
Exhibit 13 Morningstar US High-Yield Bond Index Sector Distribution



Source: Morningstar. Data as of June 30, 2025.

Healthcare and media sectors were the major contributors to the Morningstar US High-Yield Bond Index returns in the second quarter of 2025 as seen in Exhibit 14. Healthcare and services outperformed on a stand-alone basis, while banking underperformed.

Exhibit 14 Morningstar US High-Yield Bond Index Sector Return Distribution

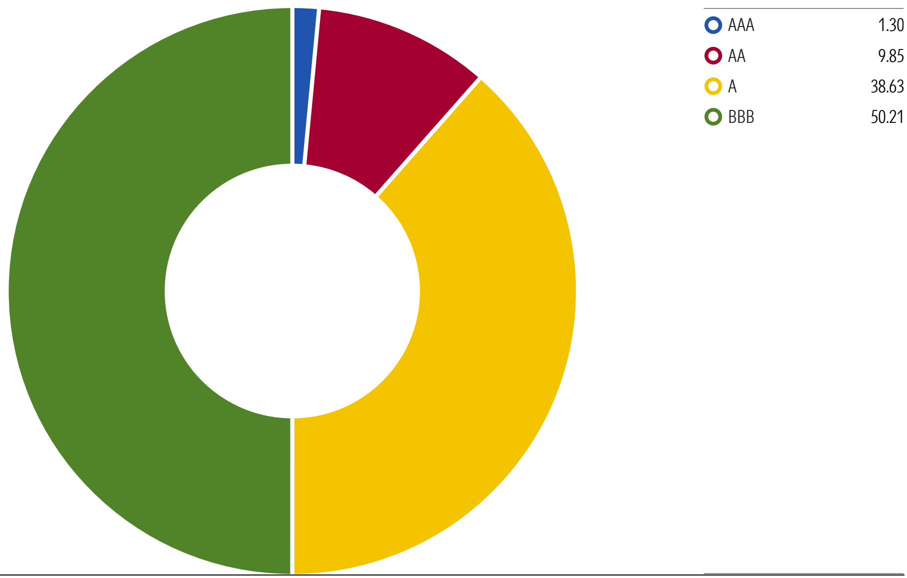


Source: Morningstar. Data as of June 30, 2025.

Credit Ratings Radar

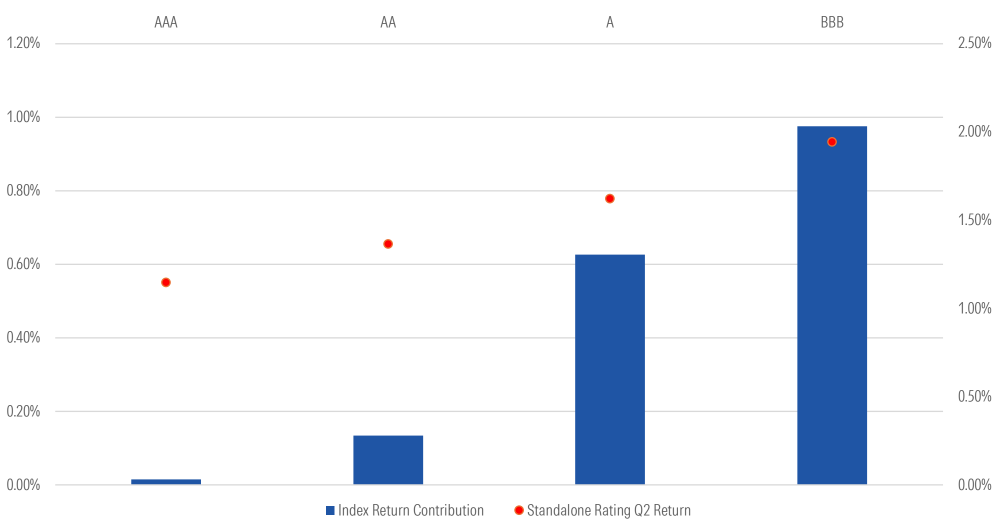
Per Exhibit 15, the Morningstar US Corporate Bond Index is primarily constituted of BBB and A rated corporate bonds, and hence, these two rating cohorts have the highest contribution to the index returns. As can be seen from Exhibit 16, on a stand-alone basis, BBB and A rated corporate bonds witnessed the highest returns.

Exhibit 15 Morningstar US Corporate Bond Index Rating Distribution



Source: Morningstar. Data as of June 30, 2025.

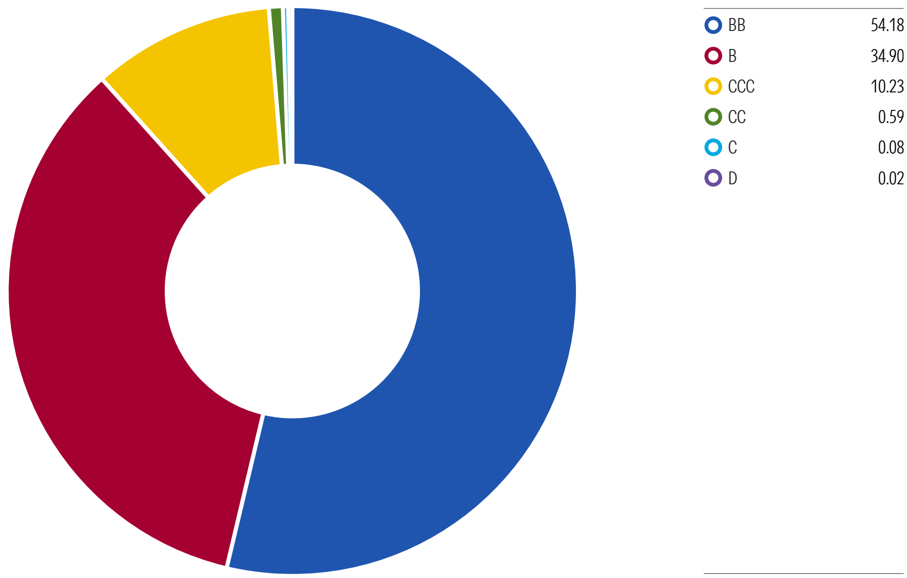
Exhibit 16 Morningstar US Corporate Bond Index Rating Return Contribution



Source: Morningstar. Data as of June 30, 2025.

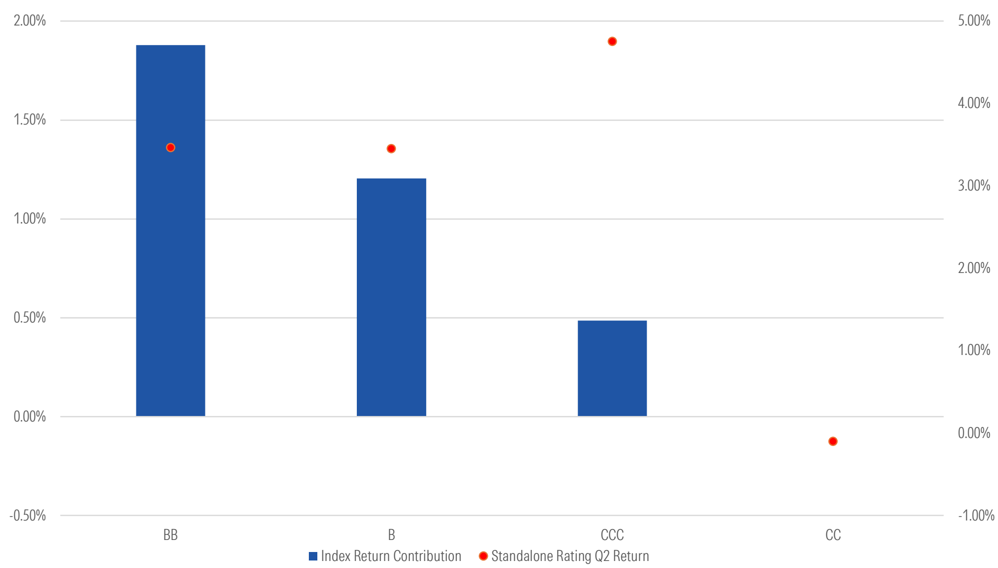
The Morningstar US High-Yield Bond Index is primarily constituted of BB and B rated corporate bonds and therefore these rating cohorts contribute the most to the index returns. As can be seen from Exhibit 18, the lower-rated CCC bonds provided the highest returns on a stand-alone basis.

Exhibit 17 Morningstar US High-Yield Bond Index Rating Distribution



Source: Morningstar. Data as of June 30, 2025.

Exhibit 18 Morningstar US High-Yield Bond Index Rating Return Contribution



Source: Morningstar. Data as of June 30, 2025.

About Morningstar Indexes
Morningstar Indexes was built to keep up with the evolving needs of investors—and to be a leading-edge advocate for them. Our rich heritage as a transparent, investor-focused leader in data and research uniquely equips us to support individuals, institutions, wealth managers and advisors in navigating investment opportunities across major asset classes, styles and strategies. From traditional benchmarks and unique IP-driven indexes, to index design, calculation and distribution services, our solutions span an investment landscape as diverse as investors themselves.

Please visit indexes.morningstar.com for more information.

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