PGIM FIXED INCOME

Q3 2025 Agency MBS Outlook

Transcript

[Music]

Andrew Harnischfeger, CFA, Portfolio Manager, Agency MBS: Mortgages ended the turbulent second quarter modestly positive in excess return terms, but lagged the timing and magnitude of the post-tariff announcement recovery in other risk product. We enter the second half of the year positive on mortgages with a collective fundamental, technical, and relative value lens. Mortgage spreads remain within a few basis points of three-year historical averages on our models, while other spread products are near multi-year tights. Additionally, interest rate volatility has fallen and remains somewhat contained versus recent history in the largely rangebound environment. The technical landscape has been particularly challenging for mortgages, but there are signs headwinds could soften. Origination has been light and should continue to decline with seasonals. Domestic banks have a clearer path to add from a regulatory perspective. Fixed income inflows can improve given the contained interest rate backdrop. Finally, growing odds of a clearer, easier Fed policy path could provide further impetus for the broad investor base to embrace fixed income. In examining the range of outcomes, mortgages have at least the possibility of further spread compassion, particularly versus other spread sectors, and limited relative downside into an unforeseen, broader risk-off event given their defensive makeup. We increased our exposure to mortgages in the second quarter widening across our account base with a preference for 30-year coupons at or just below production. We have tactically traded 30-year higher coupons given the rangebound rate environment, but hold a core underweight at the top of the stack on long-term concerns of the potential refinance response into modestly lower mortgage rates.

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Source(s) of data (unless otherwise noted): PGIM Fixed Income, as **July 2025**.

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