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Weekly Fixed Income Commentary

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Positive risk sentiment buoys Treasury yields

Long U.S. Treasury yields ended modestly higher, while shorter maturity yields were nearly unchanged to slightly lower. Investors were optimistic about continued progress toward a coronavirus vaccine and an orderly transfer of U.S. political power. In reference to its asset-purchase programs, the Federal Reserve (Fed) acknowledged, "...circumstances could shift to warrant such adjustments."

HIGHLIGHTS

- **High yield corporates posted the best return, followed by preferred securities and senior loans.**
- **The municipal market continued to grind higher.**
- **The global aggregate index performance was boosted by strong returns in Europe.**

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POSITIVE MARKET TONE LIFTS LONG TREASURY RATES

Longer-maturity U.S. Treasury yields closed modestly higher last week, while shorter maturity yields were nearly unchanged to slightly lower. A positive market risk sentiment buoyed rates early in the week and was supported by record Treasury issuance. Investors were optimistic about continued progress toward a coronavirus vaccine and an orderly transfer of U.S. political power. In the first two days of the holiday-shortened week, the fixed income markets digested $193 billion in Treasury supply that included a record-sized $56 billion 7-year note auction. By Wednesday, the 30-year Treasury yield was more than 10 basis points (bps) higher. A portion of the increase was offset on Friday, as market sentiment cooled and yields dropped in what turned out to be the largest move of the week.

Fed meeting minutes were heavily scrutinized for clues about possible future increases to asset-purchase programs. Without giving specifics, the Fed acknowledged, "… that circumstances could shift to warrant such adjustments."

Most fixed income sectors enjoyed positive total returns, outpacing the lagging Treasury market. High yield corporates posted the best return, followed by preferred securities and senior loans. High yield corporates joined asset-backed securities as the only U.S. sectors outperforming similar-duration Treasuries for the year. The highest quality sectors were not as well supported last week and government-related securities, mortgage-backed securities and taxable municipals endured negative weekly total returns. The non-U.S. markets experienced solidly positive weekly returns, with global aggregate index performance boosted by strong returns in Europe.

The municipal bond new issue calendar returns in earnest this week.

A LARGE MUNICIPAL BOND COUPON REINVESTMENT IS DUE

The municipal market continued to grind higher last week, closing Friday with a solid tone. The new issue calendar was small at $1.5 billion due to the Thanksgiving holiday, but deals were well received. Fund flows were positive at $832 million. The new issue calendar returns in earnest this week, with $8.7 billion in new issues expected.

The municipal market remains well bid, and this trend should continue. A large December 1 coupon reinvestment is due this week and another on January 1. The new issue calendar should be robust for the next few weeks and be well received. We continue to believe that interest rates will remain lower for longer, which should bode well for municipal bonds. We would consider any dips in bond prices as a potential buying opportunity.

The New York Transportation Development Corporation issued $331 million bonds for the Terminal 4 JFK International Airport Project (rated Baa1). On new issue, 4% bonds due in 2040 priced at a yield of 2.68%. These bonds traded up 7 bps (lower in yield) in the secondary market. The fact that an airport bond had ready access to the debt market shows that investors believe that people will return to air travel in earnest at some point.

High yield municipal credit spreads have contracted at an accelerated pace over the last two weeks. Spreads have narrowed by 3 bps for all of high yield and 11 bps for short duration high yield, even with AAA-rated municipal bond yields decreasing by 7 to 13 bps. High yield municipal fund flows have totaled $57 million in the last two weeks, with consecutive flows of $369 million and -$312 million. Last week's outflows appear concentrated, rather than systemic. The broader industrial development sector, which is more economically sensitive, has lead performance in November, with tobacco, higher education and hospitals also outperforming. This week's new issue calendar should be modestly higher and will likely be aggressively consumed.

HIGH YIELD CORPORATES CLAIM MARKET LEADERSHIP FOR THE WEEK, MONTH AND QUARTER

High yield corporate bonds were the top performer last week. Overall spreads narrowed by 11 bps, to 412 bps — their lowest level to end a week since February and more than 115 bps tighter than their long-term average. High yield fund flows were positive at approximately $1 billion heading into the Thanksgiving holiday. Having recorded positive returns for four weeks in a row and eight of the last nine, the asset class is the leading fixed income sector for both November and the fourth quarter.

Investment grade corporates realized a slight gain, but lost some of their luster from the previous week when they outperformed all other fixed income categories. Spreads tightened by 4 bps, to 106 bps — their narrowest level in nine months. The average investment grade yield dipped to 1.82%, matching its all-time low.

Investment grade corporate spreads are their narrowest in nine months.

Emerging markets (EM) debt posted a mildly positive return amid modest spread tightening (-4 bps) and an eighth consecutive week of inflows into EM bond funds. Within EM, local-currency debt again bested U.S. dollar-denominated issues, but by a smaller margin than in the prior week. Demand for EM assets continued to be supported by vaccine optimism, with more promising trial results announced early last week.

In focus

Advance refunding drives growth in taxable municipal issuance

Taxable municipal bonds are growing as a meaningful source of supply as the continued low-rate environment fuels advanced refunding in the taxable market. New taxable municipal issuance for 2020 is expected to reach a record-breaking $180 billion. Early projections for 2021 taxable municipal supply are again expected to break records, possibly reaching $200 billion.

The growth in taxable municipal issuance has been met with strong demand from both foreign and domestic investors. Investors are attracted to their diversification benefits, historically low default rates, essential-service nature and attractive valuations relative to other high-quality fixed income.

Foreign demand is further buoyed by low hedging costs, making taxable municipals attractive relative to negative rates foreign government bonds. As the market continues to grow, we expect demand sources will also continue to grow as more traditional fixed income buyers become familiar with the once-overlooked asset class.

This growth in investor appetite should support the long-term viability of the taxable municipal market as issuers enjoy the benefits of a more diversified buyer base.

U.S. Treasury market

		Change (%)		
Maturity	Yield	Week	Month-to-date	Year-to-date
2-year	0.15	-0.01	0.00	-1.42
5-year	0.37	-0.01	-0.02	-1.33
10-year	0.84	0.01	-0.04	-1.08
30-year	1.57	0.05	-0.09	-0.82

Source: Bloomberg L.P. As of 27 Nov 2020. **Past performance is no guarantee of future results.**

Municipal market

		Change (%)		
Maturity	Yield to Worst	Week	Month-to-date	Year-to-date
2-year	0.15	0.00	-0.06	-0.89
5-year	0.23	0.01	-0.07	-0.86
10-year	0.73	0.00	-0.20	-0.71
30-year	1.42	0.00	-0.29	-0.67

Source: Bloomberg L.P. As of 27 Nov 2020. **Past performance is no guarantee of future results.**

Yield ratios

	Ratio (%)
10-year AAA Municipal vs Treasury	87
30-year AAA Municipal vs Treasury	90
High Yield Municipal vs High Yield Corporate	90

Source: Bloomberg L.P., Thompson Reuters. As of 27 Nov 2020. AAA municipals represented by the MMD scale. The high yield ratio equals the yield-to-worst for the Bloomberg Barclays High Yield Municipal Index divided by the yield-to-worst for the Bloomberg Barclays High Yield Corporate Index. **Past performance is no guarantee of future results.**

Characteristics and returns

				Returns (%)		
Index	Yield to Worst (%)	Spread (bps)	Effective Duration (years)	Week	Month-to-date	Year-to-date
Municipal	1.18	–	5.24	0.08	1.43	4.50
High Yield Municipal	4.23	303[1]	7.98	0.24	2.32	2.87
Short Duration High Yield Municipal[2]	3.92	350	3.81	0.23	1.40	2.20
Taxable Municipal	2.21	128[3]	10.03	-0.03	1.88	9.30
U.S. Aggregate Bond	1.16	48[3]	6.24	-0.03	0.91	7.28
U.S. Treasury	0.57	–	7.27	-0.13	0.31	8.21
U.S. Government Related	1.11	57[3]	6.01	-0.09	0.89	5.44
U.S. Corporate Investment Grade	1.82	106[3]	8.84	0.13	2.57	9.18
U.S. Mortgage-Backed Securities	1.29	50[3]	2.31	-0.05	0.08	3.66
U.S. Commercial Mortgage-Backed Securities	1.42	95[3]	5.29	0.07	0.70	7.23
U.S. Asset-Backed Securities	0.52	37[3]	2.10	0.01	0.11	4.27
Preferred Securities	2.60	182[3]	4.25	0.43	3.05	6.07
High Yield 2% Issuer Capped	4.72	412[3]	3.62	0.63	3.88	4.99
Senior Loans[4]	5.50	524	0.25	0.36	2.07	1.40
Global Emerging Markets	3.70	302[3]	6.87	0.21	3.08	4.94
Global Aggregate (unhedged)	0.86	40[3]	7.43	0.27	1.81	7.74

1 Yield difference between the Bloomberg Barclays High Yield Municipal Index and the 20-year AAA MMD scale. **2** Data is a subset of the S&P Short Duration Municipal Yield Index that is below investment grade/nonrated. Spread is the yield difference between this subset and the subset rated AAA. **3** Option-adjusted spread to Treasuries. **4** Spread refers to the 3-year discount margin. Duration is estimated based on the frequency of the reset date.

Source: Bloomberg L.P. and Credit Suisse. As of 27 Nov 2020. **Past performance is no guarantee of future results.** Unless otherwise noted, the index is Bloomberg Barclays. All index returns are shown in U.S. dollars. **Yield to worst** is the lowest potential yield that can be received on a bond without the issuer actually defaulting. **Effective duration** (expressed in years) measures the price sensitivity of a fixed-income investment to a change in interest rates, considering that expected cash flows will fluctuate as interest rates change. Index performance is shown for illustrative purposes only. Index returns include reinvestment of income and do not reflect investment advisory and other fees that would reduce performance in an actual client account.

For more information, please visit nuveen.com.

Performance: Bloomberg, L.P. **Issuance:** The Bond Buyer, 27 Nov 2020. **Fund flows:** Lipper. **New deals:** Market Insight, MMA Research, 25 Nov 2020.

Any reference to credit ratings refers to the highest rating given by one of the following national rating agencies: S&P, Moody's or Fitch. Credit ratings are subject to change. AAA, AA, A and BBB are investment grade ratings; BB, B, CCC, CC, C and D are below-investment grade ratings.

Representative indexes: municipal: Bloomberg Barclays Municipal Index; **high yield municipal:** Bloomberg Barclays High Yield Municipal Index; **short duration high yield municipal:** S&P Short Duration Municipal Yield Index; **taxable municipal:** Bloomberg Barclays Taxable Municipal Bond Index; **U.S. aggregate bond:** Bloomberg Barclays U.S. Aggregate Bond Index; **U.S. Treasury:** Bloomberg Barclays U.S. Treasury Index; **U.S. government related:** Bloomberg Barclays U.S. Government-Related Index; **U.S. corporate investment grade:** Bloomberg Barclays U.S. Corporate Index; **U.S. mortgage-backed securities;** Bloomberg Barclays U.S. Mortgage-Backed Securities Index; **U.S. commercial mortgage-backed securities:** Bloomberg Barclays CMBS ERISA-Eligible Index; **U.S. asset-backed securities:** Bloomberg Barclays Asset-Backed Securities Index; **preferred securities:** ICE BofA U.S. All Capital Securities Index; **high yield 2% issuer capped:** Bloomberg Barclays High Yield 2% Issuer Capped Index; **senior loans:** Credit Suisse Leveraged Loan Index; **global emerging markets:** Bloomberg Barclays Emerging Market USD Aggregate Index; **global aggregate:** Bloomberg Barclays Global Aggregate Unhedged Index.

A word on risk

Investing involves risk; principal loss is possible. Debt or fixed income securities are subject to market risk, credit risk, interest rate risk, call risk, derivatives risk, dollar roll transaction risk and income risk. As interest rates rise, bond prices fall. Below investment grade or high yield debt securities are subject to liquidity risk and heightened credit risk. Preferred securities are subordinated to bonds and other debt instruments in a company's capital structure and therefore are subject to greater credit risk. Foreign investments involve additional risks, including currency fluctuation, political and economic instability, lack of liquidity and differing legal and accounting standards. Asset-backed and mortgage-backed securities are subject to additional risks such as prepayment risk, liquidity risk, default risk and adverse economic developments. The value of convertible securities may decline in response to such factors as rising interest rates and fluctuations in the market price of the underlying securities. Senior loans are subject to loan settlement risk due to the lack of established settlement standards or remedies for failure to settle. These investments are subject to credit risk and potentially limited liquidity, as well as interest rate risk, currency risk, prepayment and extension risk, and inflation risk

Investors should contact a tax advisor regarding the appropriateness of tax-exempt investments in their portfolio. If sold prior to maturity, municipal securities are subject to gain/losses based on the level of interest rates, market conditions and the credit quality of the issuer. Income may be subject to the alternative minimum tax (AMT) and/or state and local taxes, based on the state of residence. Income from municipal bonds held by a portfolio could be declared taxable because of unfavorable changes in tax laws, adverse interpretations by the Internal Revenue Service or state tax authorities, or noncompliant conduct of a bond issuer. It is important to review your investment objectives, risk tolerance and liquidity needs before choosing an investment style or manager.

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