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Weekly Fixed Income Commentary

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Treasury yields rise as the risk-on trade continues

U.S. Treasury yields increased last week, led by the 5-year and closely followed by 30-year maturities. Investors continued to focus on global issues, as U.S. economic data was light throughout the week. Federal Reserve (Fed) meeting minutes reinforced a patient policy approach and benign outlook for inflation.

HIGHLIGHTS

- **High yield corporates posted the best returns, followed by senior loans and investment grade corporates.**
- **Municipal bonds remained steady, outperforming the slight selloff in Treasury bonds.**
- **The non-U.S. developed regions outperformed emerging markets, boosted by the European region.**

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RISK-ON CONTINUES, DRIVING RATES HIGHER

U.S. Treasury yields increased last week for all maturities, led by the 5-year and closely followed by the 30-year.[1] Treasury supply in the form of 3-, 10-, and 30-year auctions had little effect on rates.[1] Through Thursday's close, most Treasury yields were virtually unchanged.[1] Investors continued to focus on global trends during a relatively light week for economic data. Consequently, overnight trading sessions were quiet until stronger Chinese economic data pushed yields higher on Friday. This largest move of the week resulted in the majority of the week's increase.[1]

Continued positive risk sentiment helped all sectors outperform the lagging Treasury market.[1] However, rising yields dragged down total returns, and the higher quality sectors posted negative total returns for the week.[1] Within the taxable fixed income market, the credit sectors showed the strongest returns.[1] The best return was delivered by high yield, followed by senior loans and investment grade corporates. The global aggregate sector and preferred securities also posted positive returns. The non-U.S. developed regions outperformed emerging markets, boosted by the European region.

Last week's Fed meeting minutes held no surprises and largely reinforced a patient approach to monetary policy. The minutes did contain a significant discussion about persistently soft inflation and inflation expectations. This issue remains critical, as market outlooks are widely predicated on a benign outlook for inflation. However, the Fed's five-year forward breakeven inflation rate has risen steadily this year since bottoming on 3 January.

Positive risk sentiment helped all fixed income sectors outperform the lagging Treasury market.

MUNICIPAL MARKET TECHNICALS REMAIN SUPPORTIVE

Municipal bonds remained steady last week, outperforming the slight selloff in Treasury bonds.[1] Both markets ended the week with a constructive tone. New issue municipal supply was $7.3 billion and was well received.[2] Demand remained strong, with weekly mutual fund flows of $956 million.[3] This week's new issue supply is expected to be just $3.3 billion due to the holiday-shortened week.[2] As a result, we expect municipal bonds to perform well this week as institutional investors are forced to access the secondary market to invest their continued positive flows.

Fixed income in general has a good tone. The Fed recently indicated that rates should remain unchanged as long as inflation pressures remain low. Municipal supply remains muted. For April, Citigroup projects $31 billion in new issuance and $36 billion available from bond calls and coupon payments. Thus, by the end of April the market will have less supply outstanding than when the month started. Demand remains robust, with 14 consecutive weeks of positive flows.[3]

State of California issued a whopping $2 billion of general obligation bonds (rated AA3/AA-).[4] Strong demand allowed the underwriter to lower yields from where the deal was originally priced. Low "SALT" was the major factor. The 2018 tax reform bill reduced state and local tax (SALT) deductions from federal income taxes to $10,000. Investors have been flocking to municipal bonds as a means to reduce taxes.

High yield municipal bond fund flows continued at historically strong levels last week, adding $367 million.[3] New issue supply is expected to be minimal this week, outside a $600 million non-rated industrial bond deal for Hunt Refining in Alabama.[4] Puerto Rico Electric Power Authority (PREPA) is moving closer to a restructuring deal with creditors, and a bill that would provide pricing support to First Energy and other providers of clean energy has been introduced in the Ohio state legislature.[4]

IN CORPORATE CREDIT MARKETS, HIGH YIELD RUN CONTINUES

High yield corporate bonds led all fixed income categories last week, extending their April winning streak.[1] Strength in the high yield market was supported by dovish Fed meeting minutes, positive fund flows and light new issuance (four deals totaling less than $4 billion).[2] For the second week in a row, high yield spreads tightened by about 20 basis points.[1] All but one high yield sector (steel) had positive total returns, with autos, cable and retail posting the largest gains.[1] Reflecting last week's risk-on tone, CCC rated bonds outperformed higher-quality B and BB issues.[1]

Investment grade corporates had a banner week of fund flows, at a record $8.7 billion.[3] Spreads tightened 6 bps on the week and are more than 40 bps narrower year to date.[1] Prevailing bullish sentiment for U.S. corporate credit, driven by sound macro and company fundamentals, continued last week amid solid bank earnings and encouraging Chinese economic data. Steady buying from Asia, particularly in 10- and 30-year maturities, remained an important component of demand.

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New supply was the theme for emerging markets (EM) debt. Issuers and investment banks pushed to capitalize on the recent risk rally with more than $37 billion in EM primary issuance worldwide.[2] Overall, EM spreads barely budged on the week, and returns were mixed to slightly negative.[1]

In focus

Freedom from the federal tax man this week

As tax day draws nearer, taxpayers are realizing the effects of the Tax Cuts and Jobs Act of 2017. Some taxpayers who took numerous deductions in the past may find that they are subject to a higher overall tax bill for 2018, particularly due to the $10,000 state and local tax (SALT) deduction cap.

Tax Freedom Day is the day when the nation as a whole has earned enough money to pay its total tax bill for the year. In 2019, that day falls on 16 April, three days earlier than in 2018.[5] When looking at states individually, New York has the latest Tax Freedom Day (3 May), while Alaska has the earliest (25 March).

Americans are expected to pay nearly $5.2 trillion in federal, state and local taxes for 2019, or 29% of the nation's income.[5] This amount is higher than what Americans pay for housing, clothing and food combined.

Record flows into municipal mutual funds suggest that demand may be driven by some of the changes in tax law.

Tax-exempt investing continues to be an important part of a long-term wealth creation strategy for many investors. The interest earned on municipal bonds is exempt from regular federal taxation. Additionally, bonds issued from entities within a certain state are often exempt from taxation in that state. This tax treatment, combined with attractive fundamentals, should provide ongoing support for the municipal market.

U.S. Treasury market

Maturity	Yield	Change (%) Week	Month-to-date	Year-to-date
2-year	2.39	0.05	0.13	-0.10
5-year	2.38	0.08	0.15	-0.13
10-year	2.57	0.07	0.16	-0.12
30-year	2.98	0.07	0.16	-0.04

Source: Bloomberg L.P. As of 12 Apr 2019. **Past performance is no guarantee of future results.**

Municipal market

Maturity	Yield to Worst	Change (%) Week	Month-to-date	Year-to-date
2-year	1.55	0.02	0.06	-0.23
5-year	1.67	0.03	0.10	-0.27
10-year	1.93	0.00	0.07	-0.35
30-year	2.68	-0.02	0.08	-0.34

Source: Bloomberg L.P. As of 12 Apr 2019. **Past performance is no guarantee of future results.**

Yield ratios

	Ratio (%)
10-year AAA Municipal vs Treasury	75
30-year AAA Municipal vs Treasury	90
High Yield Municipal vs High Yield Corporate	78

Source: Bloomberg L.P., Thompson Reuters. As of 12 Apr 2019. 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

Index	Yield to Worst (%)	Spread (bps)	Effective Duration (years)	Returns (%) Week	Month-to-date	Year-to-date
Municipal	2.38	–	5.85	0.08	-0.22	2.67
High Yield Municipal	4.74	224[6]	8.83	0.11	-0.24	3.58
High Yield Municipal, ex Puerto Rico	4.62	212[6]	7.74	0.15	-0.14	3.34
Short Duration High Yield Municipal[7]	3.87	213	3.80	0.07	0.01	2.64
Short Duration High Yield Municipal, ex Puerto Rico[7]	3.79	205	3.68	0.07	0.02	2.44
U.S. Aggregate Bond	3.03	42[8]	5.91	-0.12	-0.41	2.52
U.S. Treasury	2.50	–	6.20	-0.32	-0.77	1.32
U.S. Government Related	3.10	60[8]	5.49	-0.15	-0.42	2.68
U.S. Corporate Investment Grade	3.67	110[8]	7.41	0.20	-0.01	5.13
U.S. Mortgage-Backed Securities	3.19	35[8]	4.37	-0.12	-0.27	1.89
U.S. Commercial Mortgage-Backed Securities	3.11	65[8]	5.25	-0.15	-0.42	2.80
U.S. Asset-Backed Securities	2.79	37[8]	2.15	-0.04	-0.10	1.38
Preferred Securities	4.08	135[8]	4.65	0.11	0.78	9.17
High Yield 2% Issuer Capped	6.11	349[8]	3.37	0.57	1.07	8.40
Senior Loans[9]	6.82	440	0.25	0.35	0.99	4.80
Global Emerging Markets	5.35	283[8]	5.86	-0.20	-0.02	5.41
Global Aggregate (unhedged)	1.85	45[8]	7.07	0.16	-0.32	1.88

6 Yield difference between the Bloomberg Barclays High Yield Municipal Index and the 20-year AAA MMD scale. **7** 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. **8** Option-adjusted spread to Treasuries. **9** 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 12 Apr 2019. **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. All indices are unmanaged and unavailable for direct investment.

For more information, please visit nuveen.com.

1 Bloomberg L.P. **2** The Bond Buyer, 12 Apr 2019. **3** Lipper Fund Flows. **4** Market Insight, MMA Research, 10 Apr 2019. **5** Tax Foundation.

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.

Bloomberg Barclays Municipal Index covers the USD-denominated tax-exempt bond market. **Bloomberg Barclays High Yield Municipal Index** covers the USD-denominated, below investment grade tax-exempt bond market. **S&P Short Duration Municipal Yield Index** tracks the municipal bond market with maturities from 1 to 12 years. **Bloomberg Barclays U.S. Aggregate Bond Index** covers the U.S. investment grade fixed rate bond market. **Bloomberg Barclays U.S. Treasury Index** includes public obligations of the U.S. Treasury. **Bloomberg Barclays U.S. Government-Related Index** includes debt guaranteed, owned and sponsored by the U.S. government; it does not include debt directly issued by the U.S. government. **Bloomberg Barclays U.S. Corporate Index** is a broad-based benchmark that measures the investment grade, fixed-rate, taxable corporate bond market. **Bloomberg Barclays U.S. Mortgage-Backed Securities Index** is the MBS component of the U.S. Aggregate index and includes the mortgage-backed pass-through securities of Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC). **Bloomberg Barclays CMBS ERISA-Eligible Index** is the CMBS component of the U.S. Aggregate index and includes CMBS investment grade securities that are ERISA eligible under the underwriter's exemption. **Bloomberg Barclays Asset-Backed Securities Index** is the ABS component of the U.S. Aggregate index and includes credit and charge cards, autos and utilities. **ICE BofA Merrill Lynch U.S. All Capital Securities Index** is a subset of the BofA Merrill Lynch U.S. Corporate Index including all fixed-to-floating rate, perpetual callable and capital securities. **Bloomberg Barclays High Yield 2% Issuer Capped Index** measures the market of USD-denominated, non-investment grade bonds and limits each issue to 2% of the index. The **Credit Suisse Leveraged Loan Index** is designed to mirror the investable universe of the U.S. dollar-denominated leveraged loan market. Loans are added to the index if they qualify according to the following criteria: The highest Moody's/S&P ratings are Ba1/BBB+, only funded term loans are included, and the tenor must be at least one year. **Bloomberg Barclays Emerging Market USD Aggregate Index** is a flagship hard currency Emerging Markets debt benchmark that includes USD denominated debt from sovereign, quasi-sovereign, and corporate EM issuers. **Bloomberg Barclays Global Aggregate Unhedged Index** measures the performance of global bonds. It includes government, securitized and corporate sectors and does not hedge currency. One **basis point** equals .01%, or 100 basis points equal 1%.

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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 suitability 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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