

29 April 2019

Treasury yields decline on global growth concerns

U.S. Treasury yields declined across all maturities last week, led by the short end of the yield curve. Weak economic data in Europe triggered the mid-week decrease, although Treasury yields declined less than European yields. The decline continued Friday with U.S. GDP data showing underlying weakness. The Federal Reserve (Fed) meets this week, but we don't expect any significant news.

HIGHLIGHTS

- **All U.S. sectors except the preferred, corporate high yield and mortgage-backed security sectors outperformed similar-duration Treasuries.**
- **Municipal bonds closed stronger by the end of the week, with the market remaining solid.**
- **Investment grade corporate bonds outperformed their high yield counterparts.**

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TREASURY RATES DECLINE WITH GLOBAL BOND YIELDS

U.S. Treasury yields declined across all maturities last week, led by the shorter end of the yield curve.¹ The decline was sparked mid-week by weak economic data in Europe. Treasury rates continued to decline on Friday after the release of first quarter gross domestic product (GDP). GDP growth exceeded estimates, but the underlying data showed tepid consumer spending and business investment. Much of the growth was driven by trade, which is likely related to stockpiling ahead of trade negotiations.

Declining yields resulted in positive total returns for all U.S. sectors.¹ All sectors except the preferred, high yield and mortgage-backed security sectors outperformed similar-duration Treasuries.¹ The preferred sector posted the weakest total and relative returns, followed by the high yield sector as spreads widened.¹ High yield underperformance was broad based, but led by the growth-sensitive capital goods sector. In non-U.S. markets, the global aggregate and emerging markets sectors posted positive total returns.¹ However, emerging markets underperformed, posting the weakest relative performance of all fixed income sectors.¹ The emerging markets underperformance was driven by the Latin American region.¹

The weakness in the underlying GDP data added fuel to the market's belief that the Fed will cut rates before the end of the year. The Fed will meet later this week, but we don't expect policy rate changes. The Fed has emphasized its willingness to be patient and responsive to incoming data. The post-meeting statement and press conference will likely stress the Fed's patient posture.

Fair value for tax-exempt income may need to be reassessed due to tax reform.

MUNICIPAL SUPPLY IS NOT MEETING DEMAND

Municipal bonds closed stronger by the end of the week, with long municipals outperforming Treasuries and the shorter municipals lagging.¹ New issue supply of \$5.8 billion was readily absorbed.² Most deals were priced higher in the secondary market. Fund flows were positive for the 16th consecutive week at \$1.6 billion.³ New issue supply this week is expected to be only \$5 billion, likely not enough to meet demand.²

The municipal market remains solid, as does the general fixed income market.

Economic growth remains moderate in the U.S. and other parts of the world, which bodes well for fixed income. Some experts suggest that municipal bond yields are too expensive versus Treasuries, but the fact remains: Municipal supply is not meeting heightened demand. Fair value for tax-exempt income may need to be reassessed due to tax reform. Since the new tax laws allow for a low deduction of state and local taxes (SALT), municipals remain one of the only ways left to reduce taxes.

Los Angeles Department of Power and Water (DEWAP) issued \$313 million revenue bonds (rated AA).⁴ The deal was well received, and the issuer lowered yields upon final pricing. California reflects the need for tax-exempt income under the new reduced SALT deductions.

High yield municipal bonds offer attractive yields compared to high grades.¹

High yield failed to keep up with a decline in 30-year AAA municipal yields last week, causing credit spreads to retrace higher.¹ Municipal-to-Treasury ratios are collapsing across the yield curve, with the 30-year ratio less than 90% for the first time in many years.¹ High yield municipal market technical strength continues, as fund flows totaled \$297 million last week.³

The tobacco sector is exhibiting early signs of deteriorating fundamentals, with tobacco consumption decreasing. However, the municipal market has not yet priced in these risks, and several buyers are still active in the market.

MARKET TECHNICALS BOOST INVESTMENT GRADE CREDIT

Investment grade corporate bonds outperformed their high yield counterparts.¹ Dealer inventories remained light, and less than \$6 billion in new issuance was brought to market, versus expectations of \$15 to \$20 billion.² While supply was scant, demand was robust, with inflows of \$5.9 billion—the second-largest weekly amount on record.³ Spreads were flat overall amid lower U.S. Treasury yields and idiosyncratic weakness in revenues and earnings.¹

High yield corporate spreads widened for the second week in a row.¹ The asset class produced modest results against a mixed backdrop of rising oil prices, lower Treasury yields and fund outflows. High yield sector performance was led by the food and beverage, transportation (ex-air) and publishing sectors. Aerospace, telecom and restaurants lagged the most. In terms of quality, lower-rated (CCC) bonds posted the highest returns, and Bs outperformed BBs.¹ New issuance consisted of seven deals totaling \$2.8 billion.²

CCC bonds posted the highest returns, and Bs outperformed BBs.

Emerging markets (EM) debt endured a volatile week to post a slight gain.¹ This relative underperformance resulted from a combination of factors, including the Easter bombings in Sri Lanka, political uncertainty in Ukraine following the presidential election and a stronger U.S. dollar that hurt local EM currencies, especially the Argentine peso. Emerging markets spreads widened on the week for the first time since the end of March, and inflows into EM bond funds were at their lowest level of the year.^{1,3}

In focus

Emerging markets debt offers value and yield

Many macro headwinds facing emerging markets debt (EMD) last year have diminished: U.S./China trade tensions have eased, the Fed and other central banks have adopted far more dovish policy stances and global risk assets have recovered from the fourth quarter selloff. Meanwhile, inflation remains tame in most EM countries and elsewhere around the world.

Against this backdrop, EMD has rallied in 2019. Spreads on the Bloomberg Barclays Emerging Markets USD Aggregate Index have narrowed by 52 basis points year to date, with total returns exceeding 5.6%.¹ Returns have also been positive for EM corporate (+6.1%) and local-currency (+3.0%) indexes.^{1,5}

EMD valuations remain relatively attractive, even after this strong performance. But the degree of spread tightening that has already occurred in 2019 means greater selectivity will be needed to uncover further opportunities for yield compression among EM sovereign and corporate bonds. Yield income, however, continues to be an attractive component of return across the EMD landscape.

EMD yields still compare favorably to alternatives such as U.S. investment grade and high yield corporate bonds. We are cautiously optimistic regarding the value of EM currencies, which have been generally flat versus the U.S. dollar in 2019, reflecting a degree of stability after declines in 2018.

U.S. Treasury market

Maturity	Change (%)			
	Yield	Week	Month-to-date	Year-to-date
2-year	2.28	-0.10	0.02	-0.21
5-year	2.29	-0.08	0.06	-0.22
10-year	2.50	-0.06	0.09	-0.19
30-year	2.92	-0.04	0.11	-0.09

Source: Bloomberg L.P. As of 26 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	1.57	0.01	0.08	-0.21
5-year	1.64	-0.03	0.07	-0.30
10-year	1.87	-0.08	0.01	-0.41
30-year	2.55	-0.15	-0.05	-0.47

Source: Bloomberg L.P. As of 26 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	87
High Yield Municipal vs High Yield Corporate	76

Source: Bloomberg L.P., Thompson Reuters. As of 26 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	2.31	–	5.62	0.49	0.30	3.20
High Yield Municipal	4.66	227 ⁶	8.48	0.73	0.53	4.38
High Yield Municipal, ex Puerto Rico	4.53	214 ⁶	7.74	0.62	0.52	4.02
Short Duration High Yield Municipal ⁷	3.82	212	3.80	0.19	0.29	2.92
Short Duration High Yield Municipal, ex Puerto Rico ⁷	3.75	205	3.68	0.18	0.27	2.69
U.S. Aggregate Bond	2.97	43 ⁸	5.88	0.38	0.02	2.97
U.S. Treasury	2.42	–	6.16	0.38	-0.30	1.80
U.S. Government Related	3.01	59 ⁸	5.47	0.45	0.14	3.25
U.S. Corporate Investment Grade	3.60	110 ⁸	7.42	0.45	0.54	5.71
U.S. Mortgage-Backed Securities	3.17	38 ⁸	4.29	0.29	-0.01	2.15
U.S. Commercial Mortgage-Backed Securities	3.03	65 ⁸	5.26	0.44	0.13	3.37
U.S. Asset-Backed Securities	2.69	38 ⁸	2.20	0.23	0.20	1.69
Preferred Securities	4.20	153 ⁸	4.65	0.11	1.15	9.57
High Yield 2% Issuer Capped Senior Loans ⁹	6.15	359 ⁸	3.37	0.20	1.30	8.66
Senior Loans ⁹	6.63	431	0.25	0.26	1.47	5.31
Global Emerging Markets	5.36	291 ⁸	5.86	0.07	0.21	5.65
Global Aggregate (unhedged)	1.81	45 ⁸	7.04	0.05	-0.44	1.75

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 26 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, 26 Apr 2019. **3** Lipper Fund Flows. **4** Market Insight, MMA Research, 24 Apr 2019. **5** Based on the JPMorgan Corporate Emerging Markets Bond Index Diversified and JPMorgan Emerging Markets Bond Index Global Diversified in U.S. dollar terms

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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