

20 July 2020

# Treasury yields hold steady as U.S. virus cases rise further

*U.S. Treasury yields traded in a tight range and ended the week slightly lower.<sup>1</sup> Investors weighed concerns about the rising number of U.S. coronavirus cases versus optimism over a potential vaccine. The European Central Bank indicated it plans to purchase the full value of its pandemic emergency purchase program. Markets await further word from the U.S. Federal Reserve (Fed) when it meets next week.*

## HIGHLIGHTS

- **Credit sectors delivered the strongest performance, led by high yield.**
- **The municipal market continued to grind richer.**
- **The global aggregate sector delivered positive total and relative returns, led by the U.S. and Pan-European region.**



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## TREASURY YIELDS TREAD WATER

**Treasury yields traded in a fairly tight range last week**, with yields across maturities declining by 2 basis points (bps) or less.<sup>1</sup> The market continues to balance concerns over rising U.S. coronavirus cases with optimism over a vaccine.<sup>1</sup>

**The European Central Bank (ECB) kept rates unchanged** at its meeting on Wednesday. During the post-meeting press conference, ECB President Christine Lagarde asserted that, barring a significant upside surprise, the ECB plans to use the full €1.35 trillion pandemic emergency purchase program. The ECB has purchased €360 billion through the end of June. But similar to the U.S. asset purchase programs, its pace has slowed due to financial market stabilization.

**All U.S. taxable sectors, except mortgage-backed securities, posted positive total returns last week.**<sup>1</sup> Credit sectors delivered the strongest performance, led by high yield corporates, as spreads declined.<sup>1</sup> The high yield and investment grade credit sectors have returned more than 2% so far in July.<sup>1</sup> All sectors except mortgage-backed securities also outperformed similar-duration Treasuries.<sup>1</sup> The outperformance of the high yield sector was broad-based, with all sub-sectors except restaurants outperforming.<sup>1</sup> Emerging markets debt also posted positive total returns and outperformed similar-duration Treasuries.<sup>1</sup> The global aggregate sector delivered positive total and relative returns, led by the U.S. and the Pan-European region.<sup>1</sup>

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## MUNICIPAL MARKET CONTINUES TO SEE POSITIVE FLOWS

**The municipal market continued to grind richer last week**, while U.S. Treasuries remained range bound.<sup>1</sup> Robust municipal new issue supply was priced to sell and well received.<sup>2</sup> Fund flows were positive for the ninth consecutive week at \$857 million.<sup>3</sup> This week's new issue supply is expected to be \$7.7 billion (\$3.2 billion taxable).<sup>2</sup>

**Fixed income in general has a very good tone.** The Fed signaled it will keep rates low throughout 2020, and nothing on the inflation front suggests that rates should rise. Municipal demand continues to outstrip the new issue supply expected throughout the summer. Thus, we expect rates in general – and municipals in particular – to remain lower for longer.

**The Cities of Dallas and Fort Worth** issued \$395 million in revenue bonds for Dallas Fort Worth International Airport (rated A1/A).<sup>4</sup> The deal was well received and traded at a slight premium in the secondary market. It reflects how investors are requiring more yield to compensate for the possible risks due to coronavirus. For example, the 10-year bonds were priced at a yield of 1.44%, which is substantially greater than risk-free rate of 10-year U.S. Treasury (0.6%) and AAA MMD bonds (0.8%).<sup>1</sup>

**High yield municipal yields decreased by 12 bps on average last week**, with the average credit spread standing at nearly 340 bps.<sup>1</sup> High yield municipal fund flows accelerated for the tenth consecutive week of inflows.<sup>3</sup> This week's expected new issuance remains sparse, as economic uncertainty is impacting project financing in general.<sup>2</sup> However, this week's calendar is due to be headlined by a large \$225 million refunding deal for Navistar and a \$68 million deal for Renaissance Charter Schools in Florida, one of the country's largest charter school networks.<sup>4</sup>

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## HIGH YIELD CORPORATES ARE THE WEEK'S TOP PERFORMER, FURTHER TRIMMING YEAR-TO-DATE LOSSES

**High yield corporate bonds led all fixed income sectors last week**, turning in their best weekly performance since early June.<sup>1</sup> Spreads tightened by 41 bps and fund inflows continued.<sup>1</sup> Trading volumes were light given the summer calendar. After last week's gains, the loss for the overall asset class now stands at just -1.70% this year – a remarkable recovery from late March, when high yield corporates were down nearly -20%.<sup>1</sup> Within high yield, BB rated securities beat lower-quality (B and CCC) credits for the week and have turned positive for the year.<sup>1</sup>

**Investment grade corporates delivered solid results for the third consecutive week.**<sup>1</sup> Their returns have been remarkably consistent during this stretch, rising approximately 0.70% each week.<sup>1</sup> Corporate spreads narrowed by 7 bps last week, and yields fell to a record-low 1.98%.<sup>1</sup> Market technicals were strong amid more Fed buying (\$780 million), further inflows (+\$4.5 billion) and muted new issuance (+\$9.5 billion).<sup>2,3</sup>

## *Corporate spreads narrowed by 7 bps, and yields fell to a record-low 1.98%.*

**Emerging markets (EM) debt extended its winning streak to 12 weeks and 13 of the last 15.**<sup>1</sup> Sovereign bonds outperformed corporate and local-currency issues. Favorable fund flows (+\$1.6 billion), tighter spreads (-7 bps) and optimistic headlines on a potential coronavirus vaccine helped mitigate risk-off sentiment driven by resurgent coronavirus cases.<sup>1,2</sup> Late-week profit-taking tempered gains.

## *In focus*

# *Tax filing extension affects the muni market*

*To relieve taxpayers impacted by business shutdowns in light of the coronavirus pandemic, the U.S. Treasury Department and IRS extended the deadline for filing federal income taxes from April 15 to July 15. Additionally, many states followed suit and extended their deadlines.*

This three-month extension affected usual seasonal dynamics of the municipal bond market. The annual softness typically experienced in tax season is now behind us, and the market appears technically strong.

Municipal-to-Treasury ratios remain elevated above historical averages, drawing interest from crossover buyers. But as demand is increasing, supply is shrinking in light of bond redemptions. Historically, we see substantial bond redemptions from June through August, as heavy bond maturities and calls remove supply from the municipal bond market. Additionally, the amount of tax-exempt paper overall is decreasing. New issue supply is increasingly taxable, with taxable municipal issuance up 271% year over year.<sup>2</sup>

SIFMA, the most common measure of short-term tax-exempt rates, rose by 10 bps (to 21 bps) in response to increased demand for liquidity to make tax payments.<sup>1</sup> However, we expect this rate to drop again. Inflows will likely continue, given the market's recent strong performance and spread tightening.

## U.S. Treasury market

Maturity	Change (%)			
	Yield	Week	Month-to-date	Year-to-date
2-year	0.15	-0.01	0.00	-1.43
5-year	0.28	-0.02	-0.01	-1.41
10-year	0.63	-0.02	-0.03	-1.29
30-year	1.33	-0.01	-0.08	-1.06

Source: Bloomberg L.P. As of 17 Jul 2020. **Past performance is no guarantee of future results.**

## Municipal market

Maturity	Change (%)			
	Yield to Worst	Week	Month-to-date	Year-to-date
2-year	0.17	-0.07	-0.10	-0.87
5-year	0.31	-0.07	-0.10	-0.78
10-year	0.75	-0.06	-0.15	-0.69
30-year	1.47	-0.06	-0.16	-0.62

Source: Bloomberg L.P. As of 17 Jul 2020. **Past performance is no guarantee of future results.**

## Yield ratios

	Ratio (%)
10-year AAA Municipal vs Treasury	117
30-year AAA Municipal vs Treasury	111
High Yield Municipal vs High Yield Corporate	75

Source: Bloomberg L.P., Thompson Reuters. As of 17 Jul 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

Index	Yield to Worst (%)	Spread (bps)	Effective Duration (years)	Returns (%)		
				Week	Month-to-date	Year-to-date
Municipal	1.34	-	5.26	0.44	0.94	3.04
High Yield Municipal	4.64	337 <sup>5</sup>	8.92	0.84	1.69	-1.00
Short Duration High Yield Municipal <sup>6</sup>	4.25	371	4.03	0.34	0.56	-0.71
Taxable Municipal	2.30	153 <sup>7</sup>	10.08	0.25	1.08	8.30
U.S. Aggregate Bond	1.18	63	6.11	0.23	0.78	6.96
U.S. Treasury	0.48	-	7.26	0.05	0.38	9.13
U.S. Government Related	1.20	75 <sup>7</sup>	6.06	0.31	0.70	4.58
U.S. Corporate Investment Grade	1.98	136 <sup>7</sup>	8.72	0.73	2.06	7.18
U.S. Mortgage-Backed Securities	1.28	67 <sup>7</sup>	1.95	-0.03	0.06	3.56
U.S. Commercial Mortgage-Backed Securities	1.63	125 <sup>7</sup>	5.32	0.15	0.56	5.77
U.S. Asset-Backed Securities	0.83	67 <sup>7</sup>	2.15	0.07	0.15	3.47
Preferred Securities	3.68	266 <sup>7</sup>	4.39	0.61	1.64	-1.06
High Yield 2% Issuer Capped	6.16	557 <sup>7</sup>	3.71	1.13	2.21	-1.70
Senior Loans <sup>8</sup>	6.72	647	0.25	0.64	1.19	-3.63
Global Emerging Markets	4.48	393 <sup>7</sup>	6.62	0.58	1.37	0.94
Global Aggregate (unhedged)	0.91	55 <sup>7</sup>	7.35	0.25	1.09	4.11

<sup>5</sup> Yield difference between the Bloomberg Barclays High Yield Municipal Index and the 20-year AAA MMD scale. <sup>6</sup> 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. <sup>7</sup> Option-adjusted spread to Treasuries. <sup>8</sup> 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 17 Jul 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. All indexes are unmanaged and unavailable for direct investment.

## For more information, please visit nuveen.com.

<sup>1</sup> Bloomberg L.P. <sup>2</sup> The Bond Buyer, 17 Jul 2020. <sup>3</sup> Lipper Fund Flows. <sup>4</sup> Market Insight, MMA Research, 15 Jul 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.

**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 Taxable Municipal Bond Index** is a rules-based, market-value-weighted index engineered for the long-term taxable bond market. **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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