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Weekly Fixed Income Commentary

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Strong economic data boosts Treasury yields

U.S. Treasury yields resumed their increase last week, with the 10-year yield rising 5 basis points, after U.S. and global economic data were stronger than expected. Credit sectors performed well, with high yield in particular generating robust returns.

HIGHLIGHTS

- **Corporate credit, including high yield and investment grade, provided positive returns. Preferreds also outperformed, while structured products lagged.**
- **Municipal bond yields held steady. New issue supply was $5.4 billion, with flows of $161 million. This week's new issue supply is expected to be a robust $9 billion ($3.0 billion taxable).**
- **Emerging markets weakened as improving U.S. economic data boosted dollar strength.**

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Watchlist

- *Treasury yields rose after economic data surprised to the upside, signaling stronger U.S. and global growth*
- *Risk assets performed well, with high yield spreads tightening to their narrowest levels since 2007*
- *Municipal bonds are unlikely to remain so rich*
- *The dollar strengthened, pressuring emerging markets, but is more likely to depreciate moving forward*

INVESTMENT VIEWS

Unprecedented global fiscal stimulus will boost consumption and growth this year.

Zero/negative global interest rate policy remains a key market support, but investors are beginning to focus on the eventual normalization of policy.

Record supply of investment grade corporates has been followed by issuance from high yield, middle market loans, broadly syndicated loan market and certain COVID-exposed names/sectors. Taxable municipal supply continues to grow.

We favor a risk-on stance, focused on credits with durable free cash flow and solid balance sheets across a wide range of sectors. Mid-quality rating segments remain particularly attractive. Essential service municipal credits also look compelling.

KEY RISKS

- Further complications with the COVID-19 vaccine rollout.
- Geopolitical flare-ups: China, Russia, Turkey, Iran.
- Policymakers become cautious or run out of stimulus capacity.
- Inflation rises in a disorderly way, forcing premature policy tightening.

CORPORATE CREDIT LEADS THE WAY

U.S. Treasury yields increased last week. The 10-year yield rose 5 basis points (bps) after economic data beat expectations, signaling that the global economy is expanding at an even more robust pace than previously thought. The March jobs report showed that the U.S. added 916,000 net jobs last month, plus another 156,000 in revisions to the prior two months of data, beating expectations for 660,000. Separately, global manufacturing PMIs rose again in March, rising 1.1 points to 55.7, the highest level since before the pandemic. The U.S. ISM manufacturing survey rose 3.9 points to 64.7, its highest level since the 1980s.

Investment grade credit appreciated 0.52% last week, worth around 74 bps of excess returns versus similar-duration Treasuries. The asset class saw another week of positive inflows, with $1.69 billion entering investment grade funds. Structured products were somewhat weaker, with mortgage-backed securities giving -0.12% total returns but still-positive excess returns of 4 bps.

High yield credit outperformed strongly, with total returns of 0.45%. Spreads tightened -23 bps to 302 bps, the narrowest level since 2007, as the better economic data provided further evidence that defaults should remain low and earnings growth strong throughout this year. High yield saw inflows of $809 million, while senior loans had a twelfth consecutive weekly inflow of $562 million.

Emerging markets lagged the moves in U.S. credit, with total returns of -0.08%. The better U.S. economic data pushed the dollar to its strongest level in five months, which weighed on non-U.S. fixed income. Nevertheless, emerging markets spreads were mostly flat, and local yields fell -3 bps.

MUNIS HOLD STEADY AS INFLATION CONCERNS CONTINUE

Municipal bond yields held steady last week in a light, holiday-shortened week.

The U.S. economy continues to heat up, as evidenced by last week's jobs and manufacturing numbers. And the Biden administration proposed an additional $2 trillion infrastructure plan on top of the $2 trillion American Rescue Plan Act recently approved by Congress.

Investors continue to be wary that all this stimulus may overheat the economy and cause inflation. The 10-year Treasury bond yield reached 1.75% last week. Friday's muted trading due to an early close for Good Friday means we don't have a firm market reaction to Friday's employment number. Fed Chairman Powell continues to be the key person to watch for Washington's response to keeping inflation in check. Fed officials remain confident, but robust numbers like Friday's employment report mean officials will have to assert that they stand ready to fight inflation. Otherwise, investors may lose confidence.

The City of San Antonio issued $332 million electric and gas systems junior lien revenue bonds (rated Aa2/A+). The deal was priced to sell and well received. The 10-year bond was priced as a 5% coupon bond at a yield of 1.34%, versus the 10-year Treasury yield of 1.75%. Many maturities traded at a premium in the secondary market.

High yield municipal fund flows were nearly identical to last week at $250 million. The limited new issue deals were heavily oversubscribed, even an extremely speculative deal for CONSOL Energy, and Buckeye Tobacco coupons bonds traded as tight as 3.35%.

High yield corporate spreads tightened to 302 bps, the narrowest level since 2007.

In focus

A tough quarter for fixed income

Fixed income returns were broadly negative in the first quarter. The culprits: rising long-term interest rates and fears of higher inflation, driven by accelerating COVID-19 vaccinations, robust economic growth, new fiscal stimulus and a Federal Reserve firmly committed to maintaining easy monetary policy.

The bellwether 10-year U.S. Treasury yield jumped 81 bps during the period, from 0.93% to 1.74%. With the Fed anchoring short-term rates, the yield curve steepened significantly. Against this backdrop, the Bloomberg Barclays U.S. Aggregate Bond Index returned -3.37% — its worst quarterly result on record. Non-U.S. markets, represented by the global aggregate (-4.46%) and global emerging market (-3.48%) indexes, also fared poorly.

All U.S. aggregate sectors recorded losses, ranging from -4.65% for investment grade corporate bonds to a high of -0.16% for asset-backed securities. Meanwhile, senior loans (+2.01%) and high yield corporates (+0.86%) were the only U.S. taxable categories to post gains, boosted by demand for higher-yielding risk assets, and in the case of variable-rate senior loans, protection against interest rate risk.

The first quarter's bond market selloff reflected stronger global growth, upward pressure on yields and prospects for hotter inflation. Looking ahead, we think these themes will persist, and we continue to prefer high yield, senior loans and preferred securities over longer-duration and higher-quality segments.

U.S. Treasury market

		Change (%)		
Maturity	Yield	Week	March 2021	Year-to-date
2-year	0.19	0.05	0.03	0.07
5-year	0.98	0.11	0.21	0.62
10-year	1.72	0.05	0.34	0.81
30-year	2.36	-0.02	0.26	0.71

Source: Bloomberg L.P. As of 02 Apr 2021. **Past performance is no guarantee of future results.**

Municipal market

		Change (%)		
Maturity	Yield to Worst	Week	March 2021	Year-to-date
2-year	0.15	0.01	-0.05	0.01
5-year	0.52	0.02	-0.05	0.30
10-year	1.11	0.00	-0.02	0.40
30-year	1.73	-0.01	-0.05	0.34

Source: Bloomberg L.P. As of 02 Apr 2021. **Past performance is no guarantee of future results.**

Yield ratios

	Ratio (%)
10-year AAA Municipal vs Treasury	66
30-year AAA Municipal vs Treasury	74
High Yield Municipal vs High Yield Corporate	87

Source: Bloomberg L.P., Thompson Reuters. As of 02 Apr 2021. 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	March 2021	Year-to-date
Municipal	1.16	–	5.26	0.09	0.62	-0.27
High Yield Municipal	3.62	209[1]	7.31	0.26	1.08	2.25
Short Duration High Yield Municipal[2]	3.01	223	3.72	0.14	0.57	1.96
Taxable Municipal	2.49	79[3]	9.83	-0.14	-1.54	-3.29
U.S. Aggregate Bond	1.63	32[3]	6.50	0.00	-1.25	-3.28
U.S. Treasury	1.03	–	6.88	-0.25	-1.54	-4.20
U.S. Government Related	1.48	43[3]	6.09	-0.12	-0.83	-2.79
U.S. Corporate Investment Grade	2.27	89[3]	8.55	0.52	-1.72	-4.32
U.S. Mortgage-Backed Securities	1.85	14[3]	4.25	-0.12	-0.51	-1.17
U.S. Commercial Mortgage-Backed Securities	1.73	70[3]	5.21	-0.43	-1.12	-2.40
U.S. Asset-Backed Securities	0.58	34[3]	2.07	-0.10	-0.16	-0.20
Preferred Securities	2.78	160[3]	4.79	0.35	1.19	-0.12
High Yield 2% Issuer Capped	4.17	302[3]	3.85	0.45	0.16	1.04
Senior Loans[4]	4.90	453	0.25	0.06	0.06	2.04
Global Emerging Markets	4.01	276[3]	6.78	-0.08	-1.25	-3.33
Global Aggregate (unhedged)	1.16	33[3]	7.48	-0.35	-1.92	-4.37

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 02 Apr 2021. **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, 02 Apr 2021. **Fund flows:** Lipper. **New deals:** Market Insight, MMA Research, 31 Mar 2021.

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.

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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 professional 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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