nuveen
A TIAA Company

Weekly Fixed Income Commentary

2 March 2020

Treasury yields plunge as coronavirus fears intensify

U.S. Treasury yields fell to record lows last week, led by shorter maturities. The yield curve steepened as a result. Plummeting yields supported positive total returns for all but the highest risk sectors. Markets now expect the Federal Reserve (Fed) to cut rates at its March 18 meeting.

HIGHLIGHTS

- **All sectors underperformed Treasuries, although total returns were mixed.**
- **The municipal bond market continued its rally, posting all-time low yields.**
- **Emerging markets debt posted a loss for the first time in 13 weeks.**

Bill Martin
Head of Global Fixed Income

John Miller
Head of Municipals

CORONAVIRUS FEARS PUSH RATES TO RECORD LOWS

Fear regarding the coronavirus spreading within and across countries caused U.S. Treasury yields to plunge last week, led by 2- to 5-year maturities.[1] Longer Treasury yields fell by less, but the 10-year hit a record low on Tuesday, as did the 30-year, which had already reached record territory.[1] The pace of declines then accelerated, with the largest drop of the week occurring Friday.[1] The yield curve steepened as a result, in this case reflecting higher probabilities of Fed rate cuts rather than expectations for better future economic growth and inflation. Treasury issuance of $113 billion throughout the week had little effect on market rates.[1]

The pervasive risk-off tone caused all sectors to underperform Treasuries, although total returns were mixed.[1] Plummeting yields supported positive total returns for all but the highest risk sectors.[1] Preferreds and high yield corporates suffered the worst performance, with weekly total returns lower than -2%, while the Treasury sector was up more than +2%.[1] Senior loans and emerging markets suffered negative total returns below -1%.[1] The taxable municipal sector return was once again boosted by its relatively longer duration and stood as the only sector with a higher weekly total return than Treasuries.[1] On a relative performance basis, commercial mortgage-backed and asset backed securities are the only sectors outpacing similar-duration Treasuries in 2020.[1]

Markets expect the Fed will cut rates at its March 18 meeting. Market-based probabilities for rate cuts in March increased from 0.2 cuts early in the week to more than 1.5 cuts, or roughly 38 basis points (bps) of easing at the next meeting.

Only commercial mortgage-backed and asset backed securities are outpacing similar-duration Treasuries in 2020.

THE MUNICIPAL MARKET RALLY CONTINUES

The municipal bond market continued its rally last week, following U.S. Treasuries, with both markets posting all-time low yields.[1] The new issue calendar was $13.3 and was well received.[2] Fund flows were positive at $2.3 billion, marking the 60th consecutive positive week.[3] This week's new issue supply is expected to be $8.9 billion ($2 billion taxable).[2]

The market reflects a dire assessment of how low rates can go if the coronavirus throws the global economy into recession. Potential quarantines may include closing schools and businesses, as well as employees working remotely. With this thought process, it is not difficult to see why bond rates are so low. Governments across the globe must show they are able to contain the virus. Fed Chairman Powell announced that the Fed is ready to lower rates if the virus continues to dampen the U.S. economy.

Buckeye Tobacco Settlement Financing Authority (Ohio) issued $4.9 billion of bonds secured by payments from major tobacco companies (rated A-, junior lien bonds rated BBB+).[4] The deal was very well received, and underwriters lowered the yield by 25 bps upon final pricing. The bonds traded in the secondary market 45 bps richer than where the deal was sold.

The high yield municipal market is participating in the flight to quality, adding to the already heavily entrenched rally. Investor flows remained historically strong last week, and the Buckeye Tobacco deal revealed the extent of unmet demand.

HIGH YIELD SPREADS WIDEN DRAMATICALLY AS RISK-OFF SENTIMENT SWEEPS MARKETS

High yield corporate returns turned negative for the year amid the largest weekly spread widening (+156 bps) of the credit cycle.[1] High yield, which had posted gains in the previous three weeks, lost more than 2.5% last week and now lags all other fixed income sectors in 2020.[1] Reflecting the market's strong risk-off tone, lower-quality (CCC) credits underperformed B and BB issues.[1] Outflows from high yield bond funds totaled $4.2 billion last week, the largest since October 2018.[3] The new-issue market was completely quiet.[2]

Investment grade corporate bonds again proved resilient in the face of coronavirus-driven volatility, delivering positive results for the seventh week in a row.[1] Despite spread widening, the relatively longer duration of the asset class bolstered total returns as long-term interest rates fell sharply. Real estate investment trusts (REITs), retail and utilities were among the week's best-performing sectors, while energy, autos, and travel and leisure struggled.[1] Inflows of $4.5 billion reflected still-healthy demand for investment grade credit.[3]

Inflows of $4.5 billion reflected still-healthy demand for investment grade credit.

Emerging markets (EM) debt posted a loss for the first time in 13 weeks.[1] Spreads widened by 56 bps as coronavirus fears intensified.[1] In sovereign markets, higher-yielding issuers that rely on oil and other commodities fared the worst.[1] Among EM currencies, the Russian ruble was the notable underperformer as oil prices tumbled.

In focus

U.S. corporate credit is resilient amid market selloff

Investors who own credit-sensitive corporate debt, such as senior loans and high yield bonds, take risks similar to equity investors. These investors are, in effect, anticipating strong corporate earnings, a healthy consumer and stable or improving economic conditions.

The S&P 500 Index fell nearly 13% in just over a week, despite strong fundamentals, as investors are clearly concerned about the further spread of the coronavirus.[1]

Senior loans and high yield corporate bonds, however, again proved to be more defensive. Loans have declined roughly 1.5% since the selloff began on February 20.[5] High yield is down just over 3%, being more subordinate in the capital structure relative to senior loans.[5] This result shouldn't be surprising, as corporate credit has historically outperformed equities during market volatility.[1]

While technically part of the fixed income market, both senior loans and high yield bonds can be considered defensive equity exposure, since they correlate more closely with stocks than traditional bonds (which were mostly higher last week amid lower interest rates).[1] In that sense, loans and high yield may be an overlooked asset class for equity investors seeking to maintain exposure to a growing economy, but in a more defensive way.

U.S. Treasury market

		Change (%)		
Maturity	Yield	Week	February 2020	Year-to-date
2-year	0.92	-0.44	-0.40	-0.66
5-year	0.94	-0.39	-0.38	-0.76
10-year	1.15	-0.32	-0.36	-0.77
30-year	1.68	-0.24	-0.32	-0.71

Source: Bloomberg L.P. As of 28 Feb 2020. **Past performance is no guarantee of future results.**

Municipal market

		Change (%)		
Maturity	Yield to Worst	Week	February 2020	Year-to-date
2-year	0.73	-0.11	-0.10	-0.31
5-year	0.73	-0.12	-0.11	-0.36
10-year	0.93	-0.21	-0.22	-0.51
30-year	1.52	-0.30	-0.28	-0.57

Source: Bloomberg L.P. As of 28 Feb 2020. **Past performance is no guarantee of future results.**

Yield ratios

	Ratio (%)
10-year AAA Municipal vs Treasury	72
30-year AAA Municipal vs Treasury	85
High Yield Municipal vs High Yield Corporate	53

Source: Bloomberg L.P., Thompson Reuters. As of 28 Feb 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	February 2020	Year-to-date
Municipal	1.27	–	5.03	0.74	1.29	3.11
High Yield Municipal	3.29	196[6]	5.60	1.06	2.11	4.62
Short Duration High Yield Municipal[7]	2.66	187	3.33	0.52	1.22	2.76
Taxable Municipal	2.29	107[8]	9.66	2.46	3.54	7.88
U.S. Aggregate Bond	1.68	50[8]	5.88	1.26	1.80	3.76
U.S. Treasury	1.09	–	6.92	2.16	2.65	5.16
U.S. Government Related	1.82	71[8]	6.06	0.80	1.50	3.68
U.S. Corporate Investment Grade	2.40	122[8]	8.15	0.54	1.34	3.71
U.S. Mortgage-Backed Securities	1.88	54[8]	2.17	0.69	1.04	1.74
U.S. Commercial Mortgage-Backed Securities	1.74	73[8]	5.34	1.47	1.91	4.45
U.S. Asset-Backed Securities	1.31	37[8]	2.17	0.72	0.89	1.90
Preferred Securities	4.14	229[8]	5.10	-2.97	-2.16	-0.98
High Yield 2% Issuer Capped	6.23	500[8]	3.48	-2.56	-1.41	-1.38
Senior Loans[9]	6.03	510	0.25	-1.52	-1.35	-0.83
Global Emerging Markets	4.78	365[8]	6.30	-1.35	-0.20	1.34
Global Aggregate (unhedged)	1.07	47[8]	7.23	1.38	0.67	1.96

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 28 Feb 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 indices are unmanaged and unavailable for direct investment.

For more information, please visit nuveen.com.

1 Bloomberg L.P. **2** The Bond Buyer, 28 Feb 2020. **3** Lipper Fund Flows. **4** Market Insight, MMA Research, 26 Feb 2020. **5** Credit Suisse.

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%.

This material is not intended to be a recommendation or investment advice, does not constitute a solicitation buy, sell or hold a security or an investment strategy, and is not provided in a fiduciary capacity. The information provided does not take into account the specific objectives or circumstances of any particular investor, or suggest any specific course of action. Investment decisions should be made based on an investor's objectives and circumstances and in consultation with his or her advisors.

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.

This information represents the opinion of Nuveen, LLC and its affiliates and is not intended to be a forecast of future events and or guarantee of any future result. Information was obtained from third party sources which we believe to be reliable but are not guaranteed as to their accuracy or completeness. There is no assurance that an investment will provide positive performance over any period of time.

The investment advisory services, strategies and expertise of TIAA Investments, a division of Nuveen, are provided by Teachers Advisors, LLC and TIAA-CREF Investment Management, LLC. Nuveen Asset Management, LLC, Symphony Asset Management LLC and NWQ Investment Management Company LLC are registered investment advisers and affiliates of Nuveen, LLC.