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Weekly Fixed Income Commentary

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Treasury yields rise despite shifting risk sentiment

U.S Treasury yields rose last week, led by longer maturities. Investors remain focused on uncertain prospects for additional fiscal stimulus, and a tumultuous presidential debate provided little clarity. The shift in yields was slight across the board, with the news that President Trump had contracted COVID-19 only slightly souring investor sentiment.

HIGHLIGHTS

- **High yield corporates delivered the best returns, followed by preferred securities.**
- **Municipal bond yields moved for the first time in 21 days.**
- **Emerging markets debt rose slightly for the week, as spreads tightened modestly.**

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TREASURY YIELDS RISE DESPITE POLITICAL TURMOIL

U.S. Treasury yields rose last week, led by longer maturities, despite shifting risk sentiment. Investors remain focused on wavering prospects for additional fiscal stimulus, and a rancorous presidential debate did little to improve clarity. After the debate, interest rates moved higher in what turned out to be the most significant change of the week. However, movements in Treasury yields were relatively muted for the month, with all maturities finishing September within 2 basis points (bps) of where they began. An announcement on Friday that President Trump had contracted COVID-19 slightly damaged investor confidence, but saw Treasury yields drift higher.

A positive risk sentiment tightened spreads for non-Treasury sectors, more than offsetting the increase in base yields. All sectors outperformed Treasuries as a result, and most posted positive weekly total returns. High yield corporates delivered the best returns, followed by preferred securities. Taxable municipals were hurt by their relatively long duration, suffering the worst performance for the week as the only area of the market to underperform Treasuries. Government-related and commercial mortgage-backed securities (CMBS) joined taxable municipals with negative weekly returns. The global aggregate index outperformed last week, with returns boosted by the European region.

September proved challenging for most sectors, as only senior loans, CMBS and ABS posted positive total returns. However, the third quarter was strong overall, with every sector delivering solidly positive total returns and outdistancing Treasuries.

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MUNICIPAL YIELDS RISE SLIGHTLY

Municipal bond yields increased slightly last week, following Treasury yields. Weekly new issue supply of $9.6 billion was priced to sell and well received. Weekly fund flows turned negative for the first time in 20 weeks at -$775 million. This week's new issue supply is expected to be $17.7 billion ($5.9 billion taxable).

Municipal yields moved from unchanged for the first time in 21 consecutive days, the longest stretch in 40 years. The municipal market still has a strong tone, despite negative weekly fund flows and an outsized new issue calendar this week. Institutional investors hold a tremendous amount of short-duration bonds earning close to zero. And the steep yield curve means these investors may look for an opportunity to move out longer on the curve. We remain convinced that rates will be lower for longer. Thus we would view a short-term selloff as a potential buying opportunity.

The city of Philadelphia issued $385 million airport revenue bonds (rated A2). A non-AMT 30-year bond was priced with a 3% coupon at a yield of 3.15%. These bonds traded in the secondary market at 3.10 %, even though Treasuries were trading cheaper. Investors believe that once the coronavirus pandemic is under control, airports in major markets like Philadelphia will resume as an essential service.

High yield municipals yields have increased, credit spreads widened and flows flipped modestly net negative. The supercharged political environment will likely present longer-term implications for state and local aid and individual income tax rates, and the market is absorbing a surge in new issuance as many deals are being pulled forward ahead of the election. High yield municipal fund flows totaled -$56 million last week. The new issue calendar is headlined by a $700 million refunding deal for Michigan Tobacco, a massive $377 deal for a National Senior Living obligated group and a $800 million offering for Brightline West.

HIGH YIELD CORPORATES LEAD ALL SECTORS, BOUNCING BACK INTO POSITIVE TERRITORY

High yield corporate bonds reversed the previous week's loss, reclaiming a positive return for the year. Spreads tightened by 27 basis points (bps) despite equity market volatility around uncertain economic growth, stalled stimulus and the dramatic news that President Trump and the first lady had contracted COVID-19. New high yield issuance slowed to $5.6 billion. Fund flows were negative (-$3.6 billion) for the second week in a row. From a quality standpoint, lower-rated CCC bonds outperformed their B and BB counterparts.

Investment grade corporate bonds eked out a gain, improving over the prior week's negative return but lagging their high yield counterparts. Spreads narrowed by 6 bps, and fund flows stayed positive, albeit at a slower pace of just $2 billion. The primary market was also quieter, with $13.5 billion in new issuance. Among investment grade sectors, aerospace/defense and technology were leaders, while energy was hamstrung by another weekly drop (-8%) in oil prices.

Lower-rated CCC bonds outperformed their B and BB counterparts.

Emerging markets (EM) debt rose slightly for the week, as spreads tightened modestly. Within EM, local-currency issues outperformed both sovereign and corporate bonds. In the corporate EM space, higher-quality, shorter-duration and more liquid securities outperformed. Investor appetite for the overall asset class remained intact but diminished, based on subdued inflows in recent weeks.

In focus

Muni issuers get ahead of the election

Municipal issuance in October has been historically strong. The trend continues in 2020, as municipal new issue supply builds due to yields near record lows and potential risks associated with the U.S. presidential election.

Prior to the last presidential election in October 2016, new issuance soared to a then-record $52.5 billion. This year, some new issue deals planned for November and December have already been pulled forward into October. We expect more will be announced in the coming weeks. This would add to an already attractive rate environment for borrowers that could test record monthly issuance levels. However, consistent with year-to-date issuance, much of this municipal supply will likely be taxable.

Yields are expected to remain lower for longer, due to mixed economic data and the a Federal Reserve committed to maintaining extraordinarily accommodative monetary policy. Thus, any increase in yields due to a material increase in supply or volatility surrounding the election could be potential a buying opportunity.

We expect demand for municipal bonds to remain strong over the long-term, and the deluge of municipal market supply in October could offer the long-term municipal bond investor an opportunity to purchase credit quality at attractive yields.

U.S. Treasury market

Maturity	Yield	Change (%) Week	September 2020	Year-to-date
2-year	0.13	0.00	0.00	-1.44
5-year	0.29	0.02	0.01	-1.41
10-year	0.70	0.05	-0.02	-1.22
30-year	1.49	0.09	-0.02	-0.90

Source: Bloomberg L.P. As of 02 Oct 2020. **Past performance is no guarantee of future results.**

Municipal market

Maturity	Yield to Worst	Change (%) Week	September 2020	Year-to-date
2-year	0.13	0.00	0.03	-0.91
5-year	0.26	0.02	0.00	-0.83
10-year	0.88	0.05	-0.06	-0.56
30-year	1.63	0.05	-0.06	-0.46

Source: Bloomberg L.P. As of 02 Oct 2020. **Past performance is no guarantee of future results.**

Yield ratios

	Ratio (%)
10-year AAA Municipal vs Treasury	126
30-year AAA Municipal vs Treasury	110
High Yield Municipal vs High Yield Corporate	80

Source: Bloomberg L.P., Thompson Reuters. As of 02 Oct 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	September 2020	Year-to-date
Municipal	1.34	–	5.49	-0.14	0.02	3.24
High Yield Municipal	4.57	315[1]	9.13	-0.21	0.10	0.26
Short Duration High Yield Municipal[2]	4.22	371	4.18	0.05	0.22	0.63
Taxable Municipal	2.24	139[3]	10.09	-0.47	0.39	8.88
U.S. Aggregate Bond	1.18	59[3]	6.15	-0.09	-0.05	6.74
U.S. Treasury	0.50	–	7.28	-0.32	0.14	8.75
U.S. Government Related	1.14	68[3]	6.01	-0.07	-0.10	4.91
U.S. Corporate Investment Grade	2.01	134[3]	8.71	0.06	-0.29	6.66
U.S. Mortgage-Backed Securities	1.27	59[3]	2.15	0.07	-0.11	3.63
U.S. Commercial Mortgage-Backed Securities	1.44	105[3]	5.29	-0.03	0.34	6.99
U.S. Asset-Backed Securities	0.54	41[3]	2.11	0.02	0.13	4.14
Preferred Securities	3.01	225[3]	4.24	0.71	-0.80	2.86
High Yield 2% Issuer Capped	5.71	511[3]	3.73	0.88	-1.03	0.73
Senior Loans[4]	6.02	578	0.25	0.08	0.69	-0.83
Global Emerging Markets	4.08	348[3]	6.76	0.04	-1.26	1.92
Global Aggregate (unhedged)	0.91	49[3]	7.40	0.37	-0.36	5.74

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 Oct 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.

Performance: Bloomberg L.P. **Issuance:** The Bond Buyer, 02 Oct 2020. **Fund flows:** Lipper Fund Flows. **New deals:** Market Insight, MMA Research, 30 Sep 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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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 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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