nuveen
A TIAA Company

Weekly Fixed Income Commentary

9 September 2019

Positive investor sentiment buoys yields

U.S. Treasury yields rose last week as investor sentiment improved, led by longer maturities. After a soft start due to weak U.S. manufacturing data and geopolitical concerns, market sentiment was boosted by improved prospects for Brexit and a sense of easing tensions in Hong Kong and U.S./China trade talks. The market probability of the Federal Reserve (Fed) cutting rates at the September meeting stands at 100%.

HIGHLIGHTS

- **Emerging markets enjoyed the highest total return, followed by preferred securities. High yield and senior loans also delivered solid weekly returns.**
- **Municipal bond yields rose, but the market ended the week with a constructive tone.**
- **Investment grade corporates suffered the lowest total return, due to the sector's long duration.**

Bill Martin
Head of Global Fixed Income

John Miller
Head of Municipals

IMPROVED SENTIMENT LIFTS TREASURY YIELDS

U.S. Treasury yields rose last week as investor sentiment improved.[1] The move was led by longer maturities, with 10- and 30-year rates increasing a similar amount.[1] The week started on a soft note. Interest rates fell as weak U.S. manufacturing data added to concerns about trade and geopolitical risks. However, market sentiment turned more positive due to improved developments for Brexit, and a sense of easing tensions in Hong Kong and U.S./China trade talks. Treasury rates rose in response, with the largest move happening on Thursday when yields jumped 8 to 10 basis points (bps) led by 5-year maturities.[1]

The risk-on market tone buoyed non-Treasury sector performance.[1] All sectors outperformed similar-duration Treasuries, but several sectors endured negative total returns for the week due to rising yields.[1] Emerging markets enjoyed the highest total return, followed closely by preferred securities. High yield and senior loans also delivered solid returns. Mortgage-backed and asset-backed securities posted slightly positive returns.[1] Investment grade corporates suffered the lowest total return for the week, as the sector's long duration hurt returns.[1] Commercial mortgage-backed and government-related securities followed Treasuries with negative total returns.[1] The global aggregate sector matched U.S. market performance, as stronger returns in Europe were offset by a weaker Asian Pacific region.[1]

Current market-based probabilities show a 96% chance of the Fed cutting interest rates by 25 bps at the September meeting. Markets are also pricing in a 62% chance of an additional 25 bps cut at the next meeting on October 30.

The strong Treasury market means we view any selloffs in the municipal market as a buying opportunity.

MUNICIPALS OFFER OPPORTUNITY

Municipal bond and U.S. Treasury bond yields closed higher last week, but both markets ended with constructive tones.[1] Municipal new issuance totaled $8.3 billion and deals were well received.[2] Fund flows were positive for the 35th consecutive week at $820 million.[3] This week's new issue supply is expected to be robust once again at $9 billion.[2]

U.S. Treasuries sold off slightly last week, as investors grew more confident that the U.S. will not suffer negative yields like so much of the rest of the world. The U.S. economy appears strong enough to stave off recession, and the Fed stands ready to cut short-term rates in September to help maintain the economy. Supply has increased as issuers take advantage of low borrowing rates. Demand has eased due to a lower number of bond calls and, as expected, municipals are trading cheaper. However, we expect fixed income yields in general to be lower for longer. Thus, institutional investors appear to see the current municipal selloff as a buying opportunity.

The state of California issued a whopping $2.4 billion general obligation bonds.[4] Although in-state investors continue to generate strong demand, the deal was priced cheaply and was well received. Bonds were trading at premiums from where they were issued after the deal was free to trade.

High yield municipal bond credit spreads contracted last week.[1] Yields for U.S. Treasuries and AAA-rated municipal bonds increased by 6 bps, while high yield municipal bond yields increased just slightly.[1] High yield municipal fund flows slowed $184 million, with a new high yield municipal bond closed-end fund offering likely diverting flows from open-end funds.[3] Ten high yield municipal bond deals are expected this week, headlined by a $600 million deal for Marathon Oil.[4] Last week's $400 million Chicago Board of Education deal was heavily oversubscribed, another successful step in improving its fiscal health.[4]

EMERGING MARKETS LEAD THE WAY

Emerging markets (EM) debt led all taxable categories for the first time in nine weeks.[1] EM spreads tightened by 10 basis points as investors welcomed signs of progress in the U.S./China trade dispute, and Hong Kong's leader formally withdrew the bill that has sparked waves of anti-government protests. Local-currency markets outperformed their U.S. dollar-denominated counterparts as the dollar weakened.[1] Primary markets revived after a late-summer lull, with most of the activity coming from Asia.

High yield corporate bonds recorded a third consecutive week of positive returns.[1] The asset class got off to a rocky start, but the tone improved later in the week, supported by an upbeat equity market. New high yield issuance of $3.8 billion was far below expectations.[2] This limited supply was met with strong demand, bolstering prices. Investors again showed a bias for higher-quality paper in both the primary and secondary markets, as bonds rated BB and B outperformed lower-rated (CCC) credits.[1]

Unusually heavy supply may have affected investment grade corporate performance.

Investment grade corporates posted a loss and finished behind all other fixed income sectors, a rare occurrence this quarter.[1] Unusually heavy supply may have been a factor: Last week marked a record high in terms of new investment grade issuance ($70+ billion across 50 deals).[2] The previous record, set in 2013, was $66+ billion and 20 deals.[2]

In focus

Reducing risk with ESG fixed income

Demand for fixed income strategies incorporating environmental, social and governance (ESG) factors continues to grow. Investors increasingly recognize the potential of these strategies to deliver both compelling returns and positive ESG outcomes. Importantly, these bonds may also help manage risk.

How might such strategies contribute to risk management? One way is by investing in ESG leaders—issuers that have historically scored better than their peers based on industry- or sector-specific ESG criteria.

In our experience, ESG leaders have tended to demonstrate superior operational and management qualities. This makes them less likely to experience acute financial distress, and thus less likely to detract from portfolio performance.

Independent research[5] has likewise found ESG leaders to be historically less susceptible to environmental liabilities, product safety/recall concerns and poor governance—all of which can negatively affect cash flows and credit ratings.

A focus on ESG leadership can be implemented in a variety of ways, depending on the asset manager, type of investment vehicle and other factors. We believe active management with a high degree of analytical rigor is the most effective approach to identifying relative value and managing risk—two crucial objectives in this late-cycle environment.

U.S. Treasury market

		Change (%)		
Maturity	Yield	Week	Month-to-date	Year-to-date
2-year	1.54	0.04	0.04	-0.95
5-year	1.43	0.05	0.05	-1.08
10-year	1.56	0.06	0.06	-1.12
30-year	2.03	0.06	0.06	-0.99

Source: Bloomberg L.P. As of 6 Sep 2019. **Past performance is no guarantee of future results.**

Municipal market

		Change (%)		
Maturity	Yield to Worst	Week	Month-to-date	Year-to-date
2-year	1.05	0.04	0.04	-0.73
5-year	1.07	0.04	0.04	-0.87
10-year	1.28	0.06	0.06	-1.00
30-year	1.90	0.06	0.06	-1.12

Source: Bloomberg L.P. As of 6 Sep 2019. **Past performance is no guarantee of future results.**

Yield ratios

	Ratio (%)
10-year AAA Municipal vs Treasury	83
30-year AAA Municipal vs Treasury	94
High Yield Municipal vs High Yield Corporate	70

Source: Bloomberg L.P., Thompson Reuters. As of 6 Sep 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

				Returns (%)		
Index	Yield to Worst (%)	Spread (bps)	Effective Duration (years)	Week	Month-to-date	Year-to-date
Municipal	1.69	–	5.22	-0.16	-0.16	7.44
High Yield Municipal	3.99	228[6]	6.90	-0.14	-0.14	9.77
Short Duration High Yield Municipal[7]	3.46	234	3.56	-0.01	-0.01	6.25
U.S. Aggregate Bond	2.15	47[8]	5.77	-0.15	-0.15	8.93
U.S. Treasury	1.60	–	6.71	-0.21	-0.21	8.40
U.S. Government Related	2.24	62[8]	5.83	-0.12	-0.12	9.31
U.S. Corporate Investment Grade	2.84	119[8]	7.90	-0.24	-0.24	13.66
U.S. Mortgage-Backed Securities	2.29	45[8]	2.45	0.01	0.01	5.54
U.S. Commercial Mortgage-Backed Securities	2.20	69[8]	5.31	-0.16	-0.16	9.21
U.S. Asset-Backed Securities	1.91	33[8]	2.12	0.01	0.01	4.29
Preferred Securities	2.98	109[8]	4.34	0.45	0.45	15.54
High Yield 2% Issuer Capped	5.66	385[8]	3.05	0.27	0.27	11.30
Senior Loans[9]	6.19	479	0.25	0.08	0.08	6.03
Global Emerging Markets	4.86	325[8]	6.17	0.49	0.49	11.30
Global Aggregate (unhedged)	1.23	45[8]	7.23	-0.15	-0.15	7.26

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 6 Sep 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, 6 Sep 2019. **3** Lipper Fund Flows. **4** Market Insight, MMA Research, 4 Sep 2019. **5** *Incorporating Environmental, Social and Governance (ESG) Factors into Fixed Income Investment,* Inderst, G. and Stewart, F., World Bank Group publication, April 2018.

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%.

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.

GCM-946771PR-W0919P GPE-FIWCOM2-0919P