



NUVEEN ASSET MANAGEMENT

Treasury Yield Curve Steepens Amid Risk Friendly Sentiment

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Treasury yield curve steepens amid risk-friendly sentiment

10- and 30-year Treasury yields rose last week while shorter maturity rates fell, steepening the Treasury yield curve.¹ These moves were likely driven by heavy corporate bond issuance and shifting estimates of future purchases of Treasuries. The Federal Reserve (Fed) offered no surprises at its April meeting, but recommitted to supporting smooth market functioning.

HIGHLIGHTS

- **Emerging markets enjoyed the strongest weekly returns, followed by preferred securities and high yield corporates.**
- **Municipal yields declined on the long end of the curve, with a strong rally on Friday.**
- **Investment grade corporates posted their first loss after five consecutive weekly gains.**



Bill Martin

Head of Global Fixed Income



John Miller

Head of Municipals

TREASURY YIELD CURVE REVERSES RECENT FLATTENING

10- and 30-year U.S. Treasury yields rose and shorter maturity rates fell last week, steepening the yield curve.¹ A steeper curve with higher long rates typically reflects greater confidence toward future growth and inflation. However, amid astoundingly weak economic data, this steepening was likely driven by heavy corporate bond issuance and shifting estimates of future Treasury purchases by the Fed. The week ended on a soft note when aggressive trade rhetoric from the Trump administration fueled a risk-off market tone, but overall market movements reflected risk-friendly sentiment.

April's recovery in risk assets culminated with positive returns for the month.¹

All sectors outperformed similar-duration Treasuries last week, and only investment grade corporates endured a negative total return.¹ Although investment grade corporate spreads tightened, the sector's long duration dragged total returns into negative territory.¹ Emerging markets enjoyed the strongest weekly returns, followed by preferred securities and high yield corporates.¹ April was a positive month for risk assets, with all sectors producing higher total returns than Treasuries and outpacing similar-duration Treasuries.¹ Despite a strong month, all sectors still lag Treasury returns for the year.¹

The Fed's meeting produced no surprises, but noted the considerable risks for the U.S. economy over the medium term. It reinforced its commitment to support smooth market functioning through liquidity enhancing facilities, and differentiated these programs from true monetary policy accommodation.

April was a strong month for risk assets, with all sectors outpacing similar-duration Treasuries.

MUNICIPAL MARKET RECEIVES FUNDAMENTAL SUPPORT

Municipal yields ended the week lower on the long end of the curve, with a strong rally on Friday.¹ New issuance was \$8.9 billion and fund flows were negative at -\$1.3 billion.^{2,3} This week's new issue supply is expected to be \$5.8 billion (\$1.9 billion taxable).²

The municipal market is recovering

after Senate Majority Leader Mitch McConnell recently commented that some municipalities should consider bankruptcy. Counter arguments highlighted the support for municipalities during this crisis, including House Speaker Nancy Pelosi's hopes that Congress would appropriate \$500 billion to aid the states. Additionally, investors were cheered by prospects that the federal government will buy almost all municipal credits through its Municipal Liquidity Facilities program, initially funded at \$500 billion. Finally, Fed Chairman Powell pledged that the Fed will keep interest rates low until the U.S. economy "is solidly on the road to recovery."

Power Authority of New York issued \$1.1 billion tax-exempt bonds (rated Aa1/AA).⁴ The deal came midweek, amid high uncertainty in the municipal market. However, by week's end the 4% maturity due in 2055 (which came at a yield of 3.22%) traded in the secondary market at 2.92%.

The high yield municipal market is much more stable than it was in March, but headline risk and general uncertainty continues to put pressure on fund flows and market performance. The market has experienced a steady weakening of performance after the mini recovery rally in the first week of April, responding to expectations of Fed intervention in the municipal market, which has yet to materialize. Fund flows totaled -\$790 million last week, as negative macro level headlines stirred fears in an environment already uncertain over the revenue impacts of the coronavirus shutdown on issuers.³ However, market pricing is not recognizing the security features in place, and comprehensive credit analysis considered more than just revenue impacts.

HIGH YIELD CORPORATES AND EM DEBT REBOUND

Emerging markets (EM) debt was the week's top performer.¹ A rebound in oil prices, coupled with month-end positioning, helped the asset class end April on an upbeat note. Both sovereign and corporate EM segments benefited from narrowing spreads, although EM bond fund flows (-\$1.46 billion) were negative for the second straight week.³ Some aggressive measures by EM central banks drove yield-curve flattening in select markets, notably Hungary and Mexico.

High yield corporate bonds swung into positive territory after the previous week's decline.¹ The week's main theme was month-end positioning, as high yield indexes finished recalibrating to accommodate the recent influx of fallen angels. Spreads tightened by 31 bps, led by areas that had widened the most in March, such as energy and gaming/leisure.¹ Fund flows were positive at \$743 million, extending a five-week stretch that totaled \$19.6 billion – recouping the \$19.2 billion of outflows from the prior five weeks.³

High yield corporate fund flows were positive at \$743 million, extending a five-week stretch.

Investment grade corporates posted their first loss after five consecutive weekly gains.¹ Spreads tightened overall, led by big moves in the energy sector, while pharmaceuticals, retailers and real estate investment trust (REIT) spreads were unchanged to a few basis points wider.¹ Inflows continued for the third week in a row, coming in at \$2.25 billion.³ New supply remained steady, with \$80 billion brought to market by 33 issuers, skewed heavily toward non-financial sectors.²

In focus

The Fed recaps its massive monetary stimulus

Since early March, the Fed has cut interest rates to zero, relaunched virtually all of its emergency stimulus programs from the financial crisis and implemented several new ones. At its April meeting, the Fed provided an update on these efforts to keep the U.S. financial system and economy afloat amid the coronavirus pandemic.

In addition to maintaining its fed funds policy range at 0% to 0.25%, the Fed reinforced plans to continue its bazooka of large-scale asset-purchase programs and lending facilities.

The Fed added a new sentence to its policy statement, describing the public health crisis as posing risks to the economic outlook over the “medium term” – likely one to two years. This outlook hints strongly that the Fed believes it will still need to guide the economy when the country reopens, presumably over the next few months.

In his post-meeting press conference, Chair Jerome Powell indicated that interest rates would remain at or near zero “for a good while.” He also continued to emphasize that the Fed’s current role is to help keep financial markets functioning and minimize the economic damage. Powell also made clear that he believes expansive fiscal stimulus – not monetary policy – is the most effective way to fill the economic hole. And that hole is big: U.S. GDP contracted at a -4.8% annualized rate in the first quarter.

U.S. Treasury market

Maturity	Change (%)			
	Yield	Week	April 2020	Year-to-date
2-year	0.19	-0.04	-0.05	-1.38
5-year	0.35	-0.02	-0.02	-1.34
10-year	0.61	0.01	-0.03	-1.31
30-year	1.25	0.08	-0.04	-1.14

Source: Bloomberg L.P. As of 1 May 2020. Past performance is no guarantee of future results.

Municipal market

Maturity	Change (%)			
	Yield to Worst	Week	April 2020	Year-to-date
2-year	0.87	-0.03	-0.15	-0.17
5-year	1.04	0.03	0.00	-0.05
10-year	1.35	0.07	0.13	-0.09
30-year	2.16	0.03	0.29	0.07

Source: Bloomberg L.P. As of 1 May 2020. Past performance is no guarantee of future results.

Yield ratios

	Ratio (%)
10-year AAA Municipal vs Treasury	211
30-year AAA Municipal vs Treasury	170
High Yield Municipal vs High Yield Corporate	70

Source: Bloomberg L.P., Thompson Reuters. As of 1 May 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	April 2020	Year-to-date
Municipal	2.19	–	6.03	-0.42	-1.26	-1.55
High Yield Municipal	5.62	367 ⁵	10.78	-0.38	-3.37	-9.52
Short Duration High Yield Municipal ⁶	4.97	382	4.32	-0.05	-0.98	-4.66
Taxable Municipal	2.81	231 ⁷	9.85	-0.39	1.62	2.86
U.S. Aggregate Bond	1.34	76 ⁷	5.76	-0.12	1.78	4.86
U.S. Treasury	0.54	–	7.23	-0.37	0.64	8.81
U.S. Government Related	1.53	105 ⁷	5.83	0.56	0.93	1.38
U.S. Corporate Investment Grade	2.72	206 ⁷	8.37	-0.36	5.24	1.08
U.S. Mortgage-Backed Securities	1.03	41 ⁷	1.34	0.32	0.63	3.47
U.S. Commercial Mortgage-Backed Securities	2.17	171 ⁷	5.33	0.10	1.23	2.42
U.S. Asset-Backed Securities	1.80	156 ⁷	2.11	0.30	1.34	1.18
Preferred Securities	4.55	330 ⁷	4.67	0.99	7.72	-4.93
High Yield 2% Issuer Capped	8.05	744 ⁷	3.93	0.68	4.53	-8.89
Senior Loans ⁸	8.94	854	0.25	0.01	4.29	-9.58
Global Emerging Markets	6.82	623 ⁷	6.25	1.15	2.60	-7.10
Global Aggregate (unhedged)	1.02	70 ⁷	7.22	0.89	1.96	1.58

⁵ Yield difference between the Bloomberg Barclays High Yield Municipal Index and the 20-year AAA MMD scale. ⁶ 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. ⁷ Option-adjusted spread to Treasuries. ⁸ 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 1 May 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, 1 May 2020. **3** Lipper Fund Flows. **4** Market Insight, MMA Research, 29 Apr 2020.

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