

Bond Market Review

September 27, 2021

Summary

- The Treasury yield curve steepened last week following the FOMC (Federal Open Market Committee) meeting with ten-years rising eight basis points (bps) to 1.45% and 30-years rising nine bps to 1.99%. Fed Chair Powell emphasized a positive outlook for the economy and signaled the taper announcement at the November FOMC meeting, unless there is a delay in the recovery in the jobs market.
- The municipal market sold off in sympathy with Treasuries last week but outperformed government bonds, especially in the five-year part of the curve. This leaves short-term muni-to-Treasury ratios at untenable levels with the three-year at 37% and five-year at 46%, compared to 12-month averages of 67% and 57%, respectively.
- The corporate bond market proved its resilience last week as it ran the gauntlet of Evergrande default risk in China, a slightly hawkish Fed announcement and a sharp move higher in rates. The market sold off on Monday with equities down sharply, with investment grade and high yield widening two bps and 16 bps, respectively, as fears of an Evergrande default came to the fore. By the end of the week, however, fears of systemic risk abated and spreads were back to two bps and tighter for investment grade and three bps wider for high yield.

Treasury Yields

Term	Treasury Yield	Δ MTD	Δ YTD
1 Year	0.07	0.01	-0.03
2 Year	0.27	0.06	0.15
5 Year	0.95	0.17	0.59
10 Year	1.45	0.14	0.54
30 Year	1.98	0.05	0.34

Tax-Free

Infrastructure Bill During Labor Shortage

- The National League of Cities (NLC) released a report highlighting the problem with labor supply, should the \$550 billion infrastructure bill get passed. According to the report, an infrastructure plan of this magnitude would create 15 million jobs over the next decade. A nationwide labor shortage, particularly in specialized areas related to infrastructure, will create a major obstacle to achieving the administration's goals, which could lead to wage inflation or funds sitting un-deployed in municipal coffers after infrastructure-related appropriations have been made.

Diverging Views on Potential Program Similar to Build America Bonds (BABs)

- Analysts' views on the prospective taxable municipal bond program in the House Reconciliation Bill vary widely. On the one hand, Bank of America analysts claim a program similar to BABs will unleash trillions of dollars of state and local government bond sales into the market. On the other hand, JPMorgan analysts claim that such a program would do relatively little to spur additional borrowing since rates are already at historical lows.

Municipal Yields

Term	Municipal Yield	Δ MTD	Δ YTD	Tax-Equivalent Yield	Municipal/Treasury Ratio (%)	Δ MTD	Δ YTD
1 Year	0.11	0.03	-0.02	0.17	154.93	28.75	29.93
2 Year	0.14	0.03	0.00	0.22	51.95	-0.61	-63.66
5 Year	0.44	0.04	0.22	0.68	46.47	-5.01	-14.51
10 Year	1.00	0.08	0.29	1.54	68.92	-1.37	-8.83
30 Year	1.59	0.07	0.20	2.45	80.17	1.51	-4.33

Taxable

Investment Grade Dealer Inventories Heavily Lifted Following Surge in Yields

- Cash bonds caught a major bid on Thursday as the bond market's delayed reaction to the Fed meeting took hold and rates surged higher. Dealers were net lifted on about \$2 billion on the week, with \$1.6 billion of that figure coming over the last two sessions as investors lifted bonds up and down the curve at higher yields than we've seen in a few months. Foreign buying of the long end was fairly heavy while TRACE (Trade Reporting and Compliance Engine) shows that domestic investors were more focused on the belly.

Corporate Supply Surprised to the Downside

- Supply surprised to the downside last week as all issuers stood down on Monday in light of the Evergrande-induced volatility, and the market was essentially closed Wednesday for the FOMC meeting. For the week, supply totaled \$15.3 billion from 17 deals, bringing month-to-date supply to \$133 billion. Estimates for this week's supply is \$19 billion.

Oil and Natural Gas Prices Continued to Rise

- Oil and natural gas prices moved up more last week with Brent nearing \$80/barrel, a three-year high, and NYMEX (New York Mercantile Exchange) gas up more than 100% year-to-date. Europe is facing a potential energy crisis over the winter as Russia limits natural gas supplies to the continent, pushing prices higher as power and chemicals producers with feedstock flexibility switch from natural gas to oil/naphtha. Despite the Chinese selling from their strategic reserve, demand is set to exceed supply over the next three to six months.

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Sectors ¹						
	Duration	Spread	Δ MTD	Δ YTD	52- Week High	52-Week Low
Investment Grade Corporate	8.79	82	-5	-14	138	80
- Financial	6.61	73	-3	-10	129	71
- Industrial	9.61	85	-5	-16	142	83
- Utility	10.58	95	-5	-11	142	93
High Yield	3.90	277	-11	-83	528	262
Securitized	4.56	32	-3	-10	67	11
- Commercial Mortgage-Backed Securities	5.12	60	-1	-21	108	54
- Asset-Backed Securities	2.26	29	2	-4	42	22
- Mortgage-Backed Securities	4.54	30	-3	-9	64	7

International Yields							
	Germany	Japan	U.K.	France	Italy	Spain	Greece
2 Year	-0.69	-0.11	0.38	-0.69	-0.48	-0.59	--
5 Year	-0.57	-0.08	0.59	-0.36	0.02	-0.32	0.10
10 Year	-0.23	0.06	0.93	0.11	0.78	0.41	0.84
30 Year	0.26	0.69	1.23	0.90	1.74	1.30	--

Equity			
	Current	Δ MTD	Δ YTD
Dow Jones	34,798.00	-562.73	4191.52
S&P 500	4,455.48	-67.20	699.41
Nasdaq	15,047.70	-211.54	2159.42

Volatility			
	Current	Δ MTD	Δ YTD
VIX	17.75	1.27	-5.00
MOVE	58.46	-1.08	9.48

Commodities			
	Current	Δ MTD	Δ YTD
CRB	225.31	7.15	57.51
Gold	1,751.70	-66.40	-143.40
Oil	73.98	5.48	25.46
Gas	218.75	4.56	77.74

Currency			
	Current	Δ MTD	Δ YTD
U.S. Dollar	93.327	0.701	3.390
Euro	1.172	-0.009	-0.050
Pound	1.368	-0.008	0.001
Yen	110.730	0.710	7.530
Canadian Dollar	1.265	0.004	-0.008
Franc	0.925	0.010	0.039

Central Bank Rates			
	Current	Δ MTD	Δ YTD
United States	0.25	0.00	0.00
Europe	0.00	0.00	0.00
United Kingdom	0.10	0.00	0.00
Japan	0.10	0.00	0.00
Canada	0.25	0.00	0.00
TED Spread	10.7	2.26	-7.31

As of 09.24.2021. Source: Bloomberg. Please see page 3 for important disclosures and definitions.

¹Sectors are represented by the following indices: Investment Grade Corporate – Bloomberg U.S. Corporate Bond; Financial – Bloomberg U.S. Aggregate Investment Grade Finance; Industrial – Bloomberg U.S. Aggregate Investment Grade Industrial; Utility – Bloomberg U.S. Investment Grade Utility; High Yield – Bloomberg U.S. Corporate High Yield; Securitized – Bloomberg U.S. Securitized; Commercial Mortgage-Backed Securities – Bloomberg U.S. Aggregate CMBS; Asset-Backed Securities – Bloomberg U.S. Aggregate ABS; Mortgage-Backed Securities – Bloomberg U.S. Aggregate MBS.



Important Information

Technical Terms

Duration: a tool used in assessing the price volatility of a fixed-income security

Municipal/Treasury Ratio: a comparison of the current yield of municipal bonds to U.S. Treasuries

Tax-Equivalent Yield: the return that is required on a taxable investment to make it equal to the return on a tax-exempt investment

TED Spread: the difference between the three-month Treasury bill and the three-month LIBOR based in U.S. dollars

Yield: income-only return on investment expressed as an annual percentage

Yield Spread: the difference between the quoted rates of return between two different investment vehicles; also called the credit spread

Index Definitions

The volatility of an index varies greatly; all indices are unmanaged and investments cannot be made directly in an index.

Bloomberg U.S. Aggregate ABS Index: A component of the Bloomberg U.S. Aggregate Index, the Bloomberg U.S. Aggregate ABS Index includes pass-through, bullet and controlled amortization structures. The Index includes only the senior class of each ABS issue and the ERISA-eligible B and C tranche.

Bloomberg U.S. Aggregate CMBS Index: A component of the Bloomberg U.S. Aggregate Index, the Bloomberg U.S. Aggregate CMBS Index includes investment grade securities that are ERISA-eligible under the underwriter's exemption.

Bloomberg U.S. Aggregate MBS Index: A component of the Bloomberg U.S. Aggregate Index, the Bloomberg U.S. Aggregate MBS Index covers the mortgage-backed pass-through securities of Ginnie Mae (GNMA), Fannie Mae (FNMA) and Freddie Mac (FHLMC). The Index is formed by grouping the universe of over 600,000 individual fixed rate MBS pools into approximately 3,500 generic aggregates.

Bloomberg U.S. Aggregate Investment Grade Finance Index: A component of the Bloomberg U.S. Corporate Bond Index, the Bloomberg U.S. Aggregate Investment Grade Finance Index measures publicly issued investment grade U.S. corporate bonds in the Finance sector.

Bloomberg U.S. Aggregate Investment Grade Industrial Index: A component of the Bloomberg U.S. Corporate Bond Index, the Bloomberg U.S. Aggregate Investment Grade Finance Index measures publicly issued investment grade U.S. corporate bonds in the Industrial sector.

Bloomberg U.S. Aggregate Investment Grade Utility Index: A component of the Bloomberg U.S. Corporate Bond Index, the Bloomberg U.S. Aggregate Investment Grade Finance Index measures publicly issued investment grade U.S. corporate bonds in the Utility sector.

Bloomberg U.S. Corporate Bond Index: The Bloomberg U.S. Corporate Bond Index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD-denominated securities publicly issued by U.S. and non-U.S. industrial, utility and financial issuers.

Bloomberg U.S. Corporate High Yield Bond Index: The Bloomberg U.S. Corporate High Yield Bond Index measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below.

Bloomberg U.S. Securitized Index: Bloomberg U.S. Securitized Index is comprised of predominantly MBS Agency securities, but also includes ABS, CMBS and covered securities. Bloomberg U.S. Treasury Strips 20+ Year Index tracks the performance of zero coupon U.S. Treasuries with a duration of 20 years or more.

CRB: The Commodity Research Bureau (CRB) Index acts as a representative indicator of today's global commodity markets. It measures the aggregated price direction of various commodity sectors.

Dow Jones: The Dow Jones Industrial Average (DJIA) is an index that tracks 30 large, publicly-owned blue chip companies trading on the New York Stock Exchange (NYSE) and the NASDAQ.

ICE BofAML 1-10 Year Municipal Securities Index: The ICE BofAML 1-10 Year Municipal Securities Index is a subset of the ICE BofAML U.S. Municipal Securities Index including all securities with a remaining term to final maturity less than 10 years.

MOVE: The MOVE Index is a well-recognized measure of U.S. interest rate volatility that tracks the movement in U.S. Treasury yield volatility implied by current prices of one-month over-the-counter options on 2-year, 5-year, 10-year and 30-year Treasuries.

Nasdaq: The Nasdaq Composite Index is the market capitalization-weighted index of over 2,500 common equities listed on the Nasdaq stock exchange. The types of securities in the index include American depositary receipts, common stocks, real estate investment trusts (REITs) and tracking stocks, as well as limited partnership interests. The index includes all Nasdaq-listed stocks that are not derivatives, preferred shares, funds, exchange-traded funds (ETFs) or debenture securities.

S&P 500: The S&P 500 Index is widely regarded as the best single gauge of the U.S. equities market. The index includes a representative sample of 500 leading companies in leading industries of the U.S. economy. The S&P 500 Index focuses on the large-cap segment of the market; however, since it includes a significant portion of the total value of the market, it also represents the market.

VIX: The CBOE Volatility Index, or VIX, is a real-time market index representing the market's expectations for volatility over the coming 30 days.

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