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Treasury yields rise, and the Fed remains patient

U.S. Treasury yields increased amid positive U.S. economic data, progress on trade negotiations and hawkish commentary from the U.S. Federal Reserve. Markets are now pricing in just 2.7 Fed rate cuts for 2025.

HIGHLIGHTS

- **Treasuries, investment grade corporates, MBS and CMBS had negative total returns.**
- **High yield corporates, preferred securities, senior loans, emerging markets and CLOs all had positive total returns.**
- **Municipal bond yields ended the week mixed. New issue supply was \$13B, and fund inflows were \$1.1B. This week's new issuance is expected to be \$13.8B.**



Anders Persson
CIO of Global Fixed Income



Daniel Close
Head of Municipals

OPINION PIECE. PLEASE SEE IMPORTANT DISCLOSURES IN THE ENDNOTES.

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Watchlist

- *Treasury yields moved higher, and we continue to expect elevated volatility, a wider trading band and a modest rally from current levels.*
- *Spread sectors gained versus Treasuries amid better economic data.*
- *We expect the technical environment for municipal bonds to improve as the year progresses.*

INVESTMENT VIEWS

We believe fixed income **yields generally present one of the best entry points in a generation**, creating attractive income opportunities.

Downside risks are material, despite strong fundamentals, with tariffs likely to compress consumer spending and weigh on business fixed investment. A recession is not our base case.

Risk premiums may widen further, with entry points likely to become more attractive over the coming quarters. Duration is likely to reassume its role as a growth hedge.

KEY RISKS

- Tariffs further undermine consumer and business confidence, raising prices while weighing on sentiment and activity.
- Inflation fails to continue moderating as expected, weighing on asset prices.
- Geopolitical flare-ups intensify around the world.

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HIGH YIELD CORPORATE PERFORMANCE LED BY LOWER-RATED SEGMENTS

U.S. Treasury yields rose again last week, with the 10-year yield ending 7 basis points (bps) higher at 4.38%. 2-year yields rose by a similar magnitude. U.S. economic data was generally healthy, headlined by a surprising uptick in services sector business sentiment. Wednesday's Fed meeting resulted in no changes to policy, although Chair Powell suggested that the central bank will remain patient as it evaluates the impact of tariffs on its employment and inflation mandates. Markets have gone from pricing more than 4 rate cuts this year as of the end of April, to pricing just 2.7 cuts as of Friday's close. That movement reflects the better economic outlook, Powell's hawkish tone and signs of progress on tariffs. President Trump announced a trade deal with the UK and a temporary agreement with China.

Investment grade corporates retreated alongside Treasury yields, returning -0.10% for the week, but the asset class outperformed similar-duration Treasuries by 21 bps. Spreads tightened 3 bps to 99 bps, the tightest since 2 April and now just 6 bps away from their closing level before 2 April. Inflows accelerated substantially at \$3.2 billion, while supply was also larger than expected at \$43.2 billion. Despite that upside surprise, demand remained strong, and new issue concessions averaged 2.3 bps. This is still well below the prior year-to-date average.

High yield corporates advanced, returning 0.15% and beating similar-duration Treasuries by 26 bps. Most of that rally was driven by lower-rated segments, with CCC rated corporates returning 0.58% versus a 0.13% rally for BB rated corporates. That outperformance mostly closed the gap since 2 April. Lower-rated names led the selloff amid the tariff concerns and have led the subsequent rally, such that relative performance between segments is now close to neutral. Senior loans returned 0.38%. Both high yield and loans enjoyed inflows, of \$1.6 billion and \$59 million, respectively.

Emerging markets outperformed, returning 0.14% and outpacing similar-duration Treasuries by 41 bps. As in U.S. corporates, returns were driven by lower-rated segments, with high yield sovereign spreads tightening 33 bps versus only 9 bps for investment grade names. Emerging markets funds also enjoyed a large acceleration in inflows totaling \$481 million. New issuance was healthy, with \$6.7 billion pricing, averaging oversubscription rates of 3.5x.

MUNI BONDS ARE CHEAP ENOUGH TO ATTRACT CROSSOVER BUYERS

Municipal bond yields ended last week mixed, with the short-term yields declining by 3 bps and long-term yields increasing by 2 bps. The new issue calendar was priced to sell and deals were well received. Fund flows were positive for the second consecutive week, including exchange-traded inflows of \$387 million. This week's new issue calendar is expected to be priced to sell, and deals should clear the market.

The municipal market currently represents fair value, even though new issue supply has been relentless and is expected to continue. However, approximately \$120 billion of reinvestment money should come due through the summer, improving supply/ demand equilibrium. We would view any selloff due to outsized supply as a potential buying opportunity. Munis are cheap enough now to attract crossover buyers who offer access to a large pool of cash.

State of Connecticut Health and Educational Facilities Authority for Yale University issued \$500 million revenue bonds (rated Aaa/AAA). The deal comprised three separate put bonds, which were all well received. Each traded in the secondary market at a premium to where they were originally issued.

The high yield municipal market has been stabilizing recently with accelerating fund inflows. The new issue calendar was heavy last week, and Nuveen tracked 19 deals. Deals were consistently oversubscribed, even deals Nuveen chose to pass on for credit reasons. We are identifying many secondary opportunities where yields have not recovered from the dislocations caused by April's explosion of volatility. But we expect yields and credit spreads to compress over the coming weeks now that demand has improved.

Investment grade corporate spreads tightened to 99 bps, the tightest since 2 April.

In focus

Fed emphasizes patience over preemption

Citing continued uncertainty over the magnitude and persistence of tariffs, last week the Federal Reserve held its target fed funds rate range at 4.25%-4.50%. However, the central bank signaled that its next move is likely to be a rate cut later this year.

The Fed, in its policy statement, stated that “uncertainty about the economic outlook has increased further” and that “the risks of higher unemployment and higher inflation have risen.”

In his press conference, Chair Jay Powell emphasized that, given the high level of uncertainty and positive economic fundamentals, there is no urgency to cut rates in the near-term. He said, “the right thing to do is await further clarity” and “we can be patient,” especially because it remains to be seen exactly how the “scale, scope, timing, and persistence of the tariffs” will evolve. Powell explicitly stated that this is “not a situation where we can be preemptive,” suggesting that the Fed will wait to see actual deterioration in the labor market data before feeling compelled to lower rates.

We anticipate two 25 basis point rate cuts this year, followed by three cuts in 2026. These forecasts are based on our macroeconomic outlook and a probability-weighted view on the outlook for tariffs. But if tariffs end up higher than our models suggest, the Fed could loosen policy more aggressively (and vice versa).

U.S. Treasury market

Maturity	Change (%)			
	Yield	Week	Month-to-date	Year-to-date
2-year	3.89	0.07	0.29	-0.35
5-year	4.00	0.08	0.28	-0.38
10-year	4.38	0.07	0.22	-0.19
30-year	4.84	0.04	0.16	0.05

Source: Bloomberg L.P., 09 May 2025. Performance data shown represents past performance and does not predict or guarantee future results.

Municipal market

Maturity	Change (%)			
	Yield to worst	Week	Month-to-date	Year-to-date
2-year	2.86	-0.03	-0.06	0.04
5-year	2.94	-0.03	-0.08	0.07
10-year	3.29	0.00	-0.05	0.23
30-year	4.38	0.02	0.00	0.48

Source: Bloomberg L.P., 09 May 2025. Performance data shown represents past performance and does not predict or guarantee future results.

Yield ratios

	Ratio (%)
10-year AAA Municipal vs Treasury	75
30-year AAA Municipal vs Treasury	91
High Yield Municipal vs High Yield Corporate	75

Source: Bloomberg L.P., Thompson Reuters, 09 May 2025. AAA municipals represented by the MMD scale. The high yield ratio equals the yield-to-worst for the Bloomberg High Yield Municipal Index divided by the yield-to-worst for the Bloomberg High Yield Corporate Index. Performance data shown represents past performance and does not predict or guarantee future results.

For more information, please visit nuveen.com.

Performance: Bloomberg, L.P. Issuance: The Bond Buyer, 09 May 2025. Fund flows: Lipper. New deals: Market Insight, MMA Research, 07 May 2025.

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.

Representative indexes: municipal: Bloomberg Municipal Index; high yield municipal: Bloomberg High Yield Municipal Index; short duration high yield municipal: S&P Short Duration Municipal Yield Index; taxable municipal: Bloomberg Taxable Municipal Bond Index; U.S. aggregate bond: Bloomberg U.S. Aggregate Bond Index; U.S. Treasury: Bloomberg U.S. Treasury Index; U.S. government related: Bloomberg U.S. Government-Related Index; U.S. corporate investment grade: Bloomberg U.S. Corporate Index; U.S. mortgage-backed securities: Bloomberg U.S. Mortgage-Backed Securities Index; U.S. commercial mortgage-backed securities: Bloomberg CMBS ERIISA-Eligible Index; U.S. asset-backed securities: Bloomberg Asset-Backed Securities Index; preferred securities: ICE BofA U.S. All Capital Securities Index; high yield 2% issuer capped: Bloomberg High Yield 2% Issuer Capped Index; senior loans: S&P UBS Leveraged Loan Index; CLO AA: J.P. Morgan Collateralized Loan Obligation AA Index; CLO BB: J.P. Morgan Collateralized Loan Obligation BB Index; global emerging markets: Bloomberg Emerging Market USD Aggregate Index; global aggregate: Bloomberg Global Aggregate Unhedged Index.

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Characteristics and returns

Index	Yield to worst (%)	Spread (bps)	Effective duration (years)	Returns (%)		
				Week	Month-to-date	Year-to-date
Municipal	4.03	—	6.55	0.11	0.26	-0.77
High yield municipal	5.81	166 ¹	7.29	0.05	0.23	-0.75
Short duration high yield municipal ²	5.64	259	4.02	0.13	0.16	0.47
Taxable municipal	5.18	73 ³	7.60	-0.16	-1.22	1.65
U.S. aggregate bond	4.71	37 ³	6.10	-0.17	-0.95	2.20
U.S. Treasury	4.18	—	5.89	-0.28	-1.12	2.42
U.S. government related	4.70	49 ³	5.35	-0.14	-0.82	2.49
U.S. corporate investment grade	5.30	99 ³	6.77	-0.10	-0.78	1.47
U.S. mortgage-backed securities	5.09	38 ³	6.16	-0.04	-0.85	2.47
U.S. commercial mortgage-backed securities	4.97	92 ³	4.01	-0.05	-0.78	2.69
U.S. asset-backed securities	4.70	69 ³	2.60	0.01	-0.39	1.62
Preferred securities	6.63	200 ³	5.32	0.35	0.50	0.08
High yield 2% issuer capped	7.74	343 ³	3.01	0.15	0.54	1.53
Senior loans ⁴	8.48	491	0.25	0.38	0.61	1.16
Collateralized loan obligations, AA	5.67	175 ³	0.25	0.16	0.32	1.67
Collateralized loan obligations, BB	11.52	763 ³	0.25	0.48	0.59	1.01
Global emerging markets	6.64	237 ³	5.93	0.14	-0.18	2.10
Global aggregate (unhedged)	3.57	36 ³	6.56	-0.46	-0.94	4.66

1 Yield difference between the Bloomberg 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 Standard & Poor's, 09 May 2025. Performance data shown represents past performance and does not predict or guarantee future results. Unless otherwise noted, the index is Bloomberg. 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 information has been obtained from sources believed to be reliable, but its accuracy is not guaranteed. There is no representation or warranty as to the current accuracy, reliability or completeness of, nor liability for, decisions based on such information and it should not be relied on as such. For term definitions and index descriptions, please access the glossary on nuveen.com. Please note, it is not possible to invest directly in an index.

Important information 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. These risks may be magnified in emerging markets. 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. Any investment in collateralized loan obligations or other structured vehicles involves significant risks not associated with more conventional investment alternatives.

Investors should contact a tax professional 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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