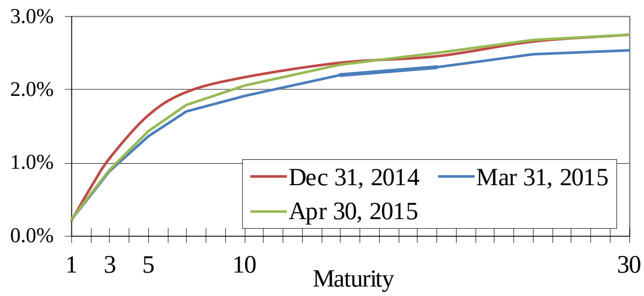
Baird Advisors
Fixed Income Market Comments
April 2015

Yields Rise and Curve Steepens in April

U.S. yields rose and the curve steepened in April despite weaker U.S. economic data as global bond yields rose in reaction to an easing of deflationary concerns. The 21 bps rise in the 30yr Treasury bond to 2.75% occurred even as March nonfarm payrolls (+126K vs 245K market expectation) and 1Q GDP (+0.2% vs 1.0% consensus expectation) came in weaker than expected as transitory headwinds (west coast port strikes/closures and inclement weather) slowed growth. The statement from the Fed's April 29th meeting was not surprising but was worded to remove all date references and allow the Fed to be truly data dependent in its determination of when to raise the Fed Funds rate. The market continues to anticipate a Fed funds rate increase in the second half of this year – with September likely to be the earliest FOMC meeting for "liftoff" given the weak first quarter.

Treasury Yields

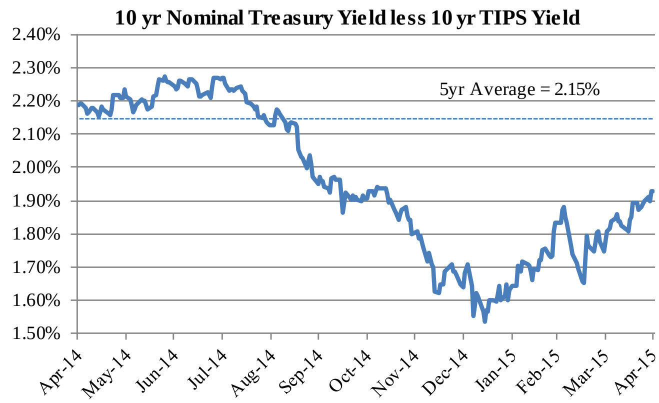


Maturity	Dec 31, 2014	Mar 31, 2015	Apr 30, 2015	1Mo Change	YTD Change
1	0.21%	0.23%	0.23%	0.00%	0.02%
2	0.66%	0.56%	0.58%	0.02%	-0.08%
3	1.07%	0.88%	0.91%	0.03%	-0.16%
5	1.65%	1.37%	1.44%	0.07%	-0.21%
7	1.97%	1.71%	1.80%	0.09%	-0.17%
10	2.17%	1.92%	2.05%	0.13%	-0.12%
30	2.75%	2.54%	2.75%	0.21%	0.00%

Inflation Expectations Rebound

U.S. inflation expectations continued to rebound this month after a steady decline last year. The graph at right shows the expected level of inflation implied by the TIPS market. The 10 year inflation protected Treasury went from pricing in less than 1.6% average annual inflation at year end to over 1.9% currently (although inflation expectations still remain below the 5yr average). Anecdotally, some investors who previously worried that the Fed would be too hawkish - raising rates too early and suffocating an economic recovery- have instead grown concerned that the Fed will be too dovish and leave extremely accommodative policy in place long enough to spur inflation.

TIPS Breakeven Inflation



High Yield, TIPS Outperform as Most Sectors Decline

Rising yields led to negative returns in many bond sectors this month with the exception of TIPS (+0.74%) as prices rose to reflect higher inflation expectations and Corporate High Yield (+1.21%) where this sector followed equity prices higher. Mortgage-Backed Securities (+0.04%) managed to deliver flat returns as higher interest rates alleviated some of the immediate prepayment risks on premium-priced MBS securities and Asset-Backed Securities (ABS +0.08%) weathered rising yields due to the relatively short duration of the sector. The Investment Grade Corporate sector (-0.70%) had some of the weakest total returns as Long Corporates fell over 2% due to rising yields.

Total Returns of Selected Barclays Indices and Subsectors

Barclays Index/Sector	April	YTD
U.S. Aggregate Index	-0.36%	1.24%
U.S. Gov't/Credit Index	-0.53%	1.30%
U.S. Intermediate Gov't/Credit Index	-0.04%	1.41%
U.S. 1-3 Yr. Gov't/Credit Index	0.08%	0.67%
U.S. Treasury	-0.53%	1.10%
U.S. Agency	-0.16%	1.01%
MBS (Mortgage-Backed Securities)	0.04%	1.10%
CMBS (Commercial Mortgage-Backed Securities)	-0.08%	1.69%
ABS (Asset-Backed Securities)	0.08%	0.98%
U.S. Corporate - Investment Grade	-0.70%	1.60%
Corporate High Yield	1.21%	3.76%
Municipal Bond Index	-0.52%	0.48%
TIPS (Treasury Inflation Protected Securities)	0.74%	2.17%

Disclosures

This is not a complete analysis of every material fact regarding any company, industry or security. The information has been obtained from sources we consider to be reliable, but we cannot guarantee the accuracy.

Fixed income is generally considered to be a more conservative investment than stocks, but bonds and other fixed income investments still carry a variety of risks such as interest rate risk, credit risk, inflation risk, and liquidity risk. In a rising interest rate environment, the value of fixed-income securities generally decline and conversely, in a falling interest rate environment, the value of fixed-income securities generally increase. High yield securities may be subject to heightened market, interest rate or credit risk and should not be purchased solely because of the stated yield.

Indices are unmanaged, and are not available for direct investment. *Past performance is not a guarantee of future results.*

The Barclays Aggregate Bond Index is an index comprised of approximately 6000 publicly traded bonds including U.S. Government, mortgage-backed, corporate, and Yankee bonds with an average maturity of approximately 10 years.

The Barclays Government/Credit Index is a combination of the Government Index which measures government-bond general and Treasury funds, and the Credit Bond Index, which is a market value-weighted index which tracks the returns of all publicly issued, fixed-rate, nonconvertible, dollar-denominated, SEC registered, investment grade Corporate Debt.

The Barclays Intermediate Government/Credit Index is a combination of the Government Index which measures government-bond general and Treasury funds, and the Credit Bond Index, which is a market value-weighted index which tracks the returns of all publicly issued, fixed-rate, nonconvertible, dollar-denominated, SEC registered, investment grade Corporate Debt with maturities between one and ten years.

The Barclays Government/Credit Intermediate Index (1 – 3 yr.) is a combination of the Government Index which measures government-bond general and Treasury funds, and the Credit Bond Index, which is a market value-weighted index which tracks the returns of all publicly issued, fixed-rate, nonconvertible, dollar-denominated, SEC registered, investment grade Corporate Debt with maturities between zero and three years.

The Barclays U.S. Treasury Index includes public obligations of the U.S. Treasury. Treasury bills are excluded by the maturity constraint of at least one year but are part of a separate Short Treasury Index. In addition, certain special issues, such as state and local government series bonds (SLGs), as well as U.S. Treasury TIPS, are excluded. STRIPS are excluded from the index because their inclusion would result in double-counting. Securities in the Index roll up to the U.S. Aggregate, U.S. Universal, and Global Aggregate Indices. The U.S. Treasury Index was launched on January 1, 1973.

U.S. Agency: This index is the U.S. Agency component of the U.S. Government/Credit index. Publicly issued debt of U.S. Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the U.S. Government (such as USAID securities). The largest issues are Fannie Mae, Freddie Mac, and the Federal Home Loan Bank System (FHLB). The index includes both callable and non-callable agency securities.

U.S Corporate – Investment Grade: This index is the Corporate component of the U.S. Credit index. It includes publicly issued U.S. corporate and specified foreign debentures and secured notes that meet the specified maturity, liquidity, and quality requirements. To qualify, bonds must be SEC-registered.

CMBS (Commercial Mortgage-Backed Securities): This index is the CMBS component of the U.S. Aggregate index. The Barclays CMBS ERISA-Eligible Index is the ERISA-eligible component of the Barclays CMBS Index. This index, which includes investment grade securities that are ERISA eligible under the underwriter’s exemption, is the only CMBS sector that is included in the U.S. Aggregate Index.

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

ABS (Asset-Backed Securities): This index is the ABS component of the U.S. Aggregate index. The ABS index has three subsectors: credit and charge cards, autos, and utility. The index includes pass-through, bullet, and controlled amortization structures. The ABS Index includes only the senior class of each ABS issue and the ERISA-eligible B and C tranche. The Manufactured Housing sector was removed as of January 1, 2008, and the Home Equity Loan sector was removed as of October 1, 2009.

Corporate High Yield: The Barclays U.S. High Yield Index covers the universe of fixed rate, non-investment grade debt. Eurobonds and debt issues from countries designated as emerging markets (sovereign rating of Baa1/BBB+/BBB+ and below using the middle of Moody’s, S&P, and Fitch) are excluded, but Canadian and global bonds (SEC registered) of issuers in non-EMG countries are included. Original issue zeroes, step-up coupon structures, 144-As and pay-in-kind bonds (PIKs, as of October 1, 2009) are also included.

The Barclays Municipal Bond Index is a broad-based, total-return index. The bonds are all investment-grade, tax-exempt, and fixed-rate securities with long-term maturities (greater than 2 years). They are selected from issues larger than $50 million.

The Barclays TIPS Index consists of Treasury Inflation Protected Securities (TIPS). TIPS are securities whose principal is tied to the Consumer Price Index. TIPS pay interest semi-annually, based on the fixed rate applied to the adjusted principal.