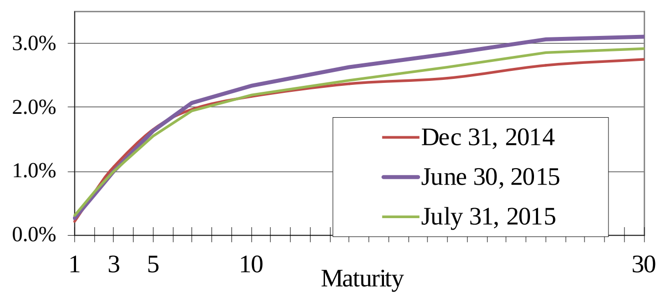
Baird Advisors
Fixed Income Market Comments
July 2015

Curve Flattens, Intermediate and Long Yields Decline

The yield curve flattened in July as tepid wage inflation (Q2 Employment Cost Index +0.2%, the smallest quarterly rise since 1996) and weaker U.S. growth (2Q GDP +2.3%, 1Q GDP revised from -0.2% to +0.6%) contributed to an 18 bp decline in the 30yr Treasury yield to 2.93%. Additional factors included a continued decline in Chinese stocks and lower commodity prices (WTI Crude oil fell 21%), implying lower expectations for global growth. However, short term U.S. yields inched higher (see table below right) as Fed Chairwoman Yellen continued to signal in her report to Congress that "liftoff", the first Fed Funds rate increase, could commence before year end if the U.S. economy makes further progress.

Treasury Yields

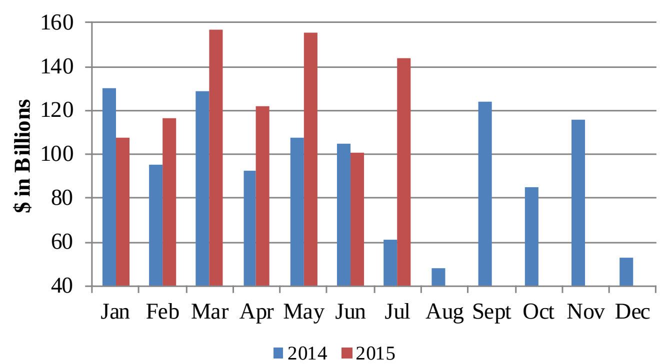


Maturity	Dec 31, 2014	Jun 30, 2015	Jul 31, 2015	1Mo Change	YTD Change
1	0.21%	0.26%	0.31%	0.05%	0.10%
2	0.66%	0.63%	0.67%	0.04%	0.01%
3	1.07%	0.99%	0.99%	0.00%	-0.08%
5	1.65%	1.63%	1.55%	-0.08%	-0.10%
7	1.97%	2.06%	1.94%	-0.12%	-0.03%
10	2.17%	2.33%	2.20%	-0.13%	0.03%
30	2.75%	3.11%	2.93%	-0.18%	0.18%

Record-Setting Corporate Issuance

Investment Grade Corporate issuance of $144B set a record for the most new supply in the month of July, putting YTD supply 25% ahead of last year's pace. As such, 2015 could be on pace to top the 2014 record for most issuance in a year. Summer months are typically a slower time for corporate issuance, but this year July issuance rose markedly (see chart at right) as industrial companies funded acquisitions and banks issued more debt to increase regulatory-driven liquidity metrics. Although credit fundamentals generally remain solid, market volatility and the additional supply widened Investment Grade Corporate spreads 9 bps to 154 bps. Heightened macro volatility and falling commodity prices put additional pressure on highly-levered energy and commodity companies as spreads on High Yield Corporates widened 37 bps to 513 bps.

Corporate Gross Issuance



Returns Rebound in July, Except for High Yield

Treasuries delivered the strongest returns in July (+0.83%) as yields fell on intermediate and long maturities. Investment Grade spread sectors (e.g. IG Corporates +0.67%) lagged Treasuries but still delivered solid nominal returns. The curve flattening detracted from returns of shorter maturities, as yields rose on the short end, but short duration spread sectors such as ABS (+0.19%) had positive returns. Corporate High Yield (-0.58%) was the only sector to post negative returns in July, but still leads the pack for the year (+1.93%). After a solid month, most sectors are back into positive territory for the year with the exception of IG Corporates (-0.25% YTD).

Total Returns of Selected Barclays Indices and Subsectors

Barclays Index/Sector	July	YTD
U.S. Aggregate Index	0.70%	0.59%
U.S. Gov't/Credit Index	0.73%	0.43%
U.S. Intermediate Gov't/Credit Index	0.36%	1.18%
U.S. 1-3 Yr. Gov't/Credit Index	0.06%	0.78%
U.S. Treasury	0.83%	0.87%
U.S. Agency	0.44%	1.04%
MBS (Mortgage-Backed Securities)	0.63%	0.94%
CMBS (Commercial Mortgage-Backed Securities)	0.65%	1.34%
ABS (Asset-Backed Securities)	0.19%	1.27%
U.S. Corporate - Investment Grade	0.67%	-0.25%
Corporate High Yield	-0.58%	1.93%
Municipal Bond Index	0.72%	0.84%
TIPS (Treasury Inflation Protected Securities)	0.21%	0.55%

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.