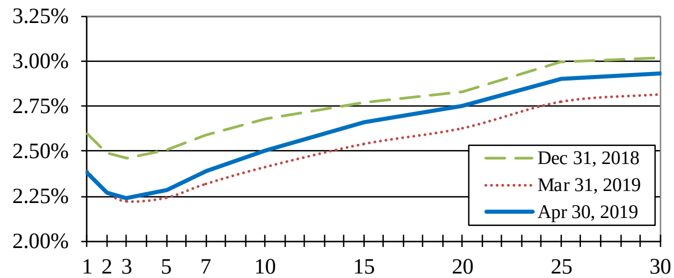
Baird Advisors
Fixed Income Market Commentary
April 2019

Modestly Higher Rates on Global Stabilization

Rates moved slightly higher last month with long rates rising more than short, modestly steepening the curve. The benchmark 10yr Treasury yield rose 10 bps to end at 2.51%, which is still 17bps lower YTD. Upward pressure on rates was driven by clear signs of stabilization in the global economy led by China, and continued improvement in risk assets. In the U.S., economic data also stabilized as the economy added 196K jobs in March, returning to trend after a weaker February report. The unemployment rate held steady at 3.8%, retail sales rebounded and consumer confidence remained high. Despite stronger signs of growth and a powerful 40% rise in oil prices since year end as Iranian oil waivers are set to expire, core inflation data has slowed. The Core Personal Consumption Expenditure (PCE) Index slipped to 1.6% YoY, down from 2.0% at year-end. While the Fed continues to view inflation below its 2.0% target rate as transitory, the market isn't convinced and was pricing in a 67% probability of a Fed rate cut before year end. Outside the U.S., China has decided to forego further stimulus efforts while awaiting additional economic data and much anticipated confirmation of a trade deal with the U.S. In the U.K., leaders were unable to reach a Brexit deal by the April 12th deadline and delayed the date for departure from the European Union to October 31st.



Treasury Yields

Maturity	12/31/17	12/31/18	3/31/19	4/30/19	1Mo Chg	YTD	Q2 Chg
1	1.73%	2.60%	2.39%	2.38%	-0.01%	-0.22%	-0.01%
2	1.88%	2.49%	2.27%	2.27%	0.00%	-0.22%	0.00%
3	1.97%	2.46%	2.22%	2.24%	0.02%	-0.22%	0.02%
5	2.21%	2.51%	2.24%	2.28%	0.04%	-0.23%	0.04%
7	2.33%	2.59%	2.32%	2.39%	0.07%	-0.20%	0.07%
10	2.41%	2.68%	2.41%	2.51%	0.10%	-0.17%	0.09%
30	2.74%	3.02%	2.82%	2.94%	0.12%	-0.08%	0.12%

Corporates Tighten, Mortgage Pass-throughs Widen in April

Solid economic data helped corporate spreads move 8 bps tighter in April to 111 bps (42 bps tighter YTD), while fixed income mutual fund and ETF inflows continued at the strong pace seen in the first quarter. The favorable economic backdrop also helped U.S. High Yield move 33 bps tighter in the month as U.S. equities returned to all-time highs. U.S. Non-Agency CMBS followed the move in credit, 6 bps tighter on the month, aided in part by limited supply in the sector. However, Agency Pass-throughs widened as more price-sensitive investors continue to replace the Fed's ownership. The Fed still owns about one quarter of the bonds in the MBS index, down from one third at this time in 2016. As a reminder – that's projected to go to zero as the Fed intends to return the composition of its securities portfolio to 100% Treasuries over time.

Option-Adjusted Spreads (in bps)

	12/31/18	3/31/19	4/30/19	1Mo Chg	YTD Chg
U.S. Aggregate Index	54	44	44	0	-10
U.S. Agency (non-mortgage)	16	13	13	0	-3
Mortgage and ABS Sectors					
U.S. Agency Pass-throughs	35	35	41	6	6
U.S. Agency CMBS	55	45	44	-1	-11
U.S. Non-Agency CMBS	107	85	79	-6	-28
Asset-Backed Securities	53	39	38	-1	-15
Corporate Sectors					
U.S. Investment Grade	153	119	111	-8	-42
Industrial	157	125	116	-9	-41
Utility	144	116	108	-8	-36
Financial Institutions	147	109	101	-8	-46
Other Govt. Related	90	76	72	-4	-18
U.S. High Yield Corporates	526	391	358	-33	-168
Emerging Market Debt	560	493	509	16	-51

Source: Bloomberg Barclays Indices

Corporates Outperform; Mixed Monthly Returns, Positive YTD

Overall returns were mixed this month – Investment Grade Corporates (+0.54%) rose, while Treasuries (-0.28%) posted negative returns as spread sectors outperformed. High Yield Corporates moved in step with equity markets, posting the highest overall returns both for the month and year to date (+1.42% April, +8.78% YTD). Returns for all sectors remain in positive territory YTD.

Total Returns of Selected Bloomberg Barclays Indices and Subsectors

	April	YTD 2019	Effective Duration
U.S. Aggregate Index	0.03%	2.97%	5.89
U.S. Gov't/Credit Index	0.05%	3.31%	6.54
U.S. Intermediate Gov't/Credit Index	0.19%	2.52%	3.89
U.S. 1-3 Yr. Gov't/Credit Index	0.23%	1.44%	1.90
U.S. Treasury	-0.28%	1.83%	6.15
U.S. Agency (Non-Mortgage)	0.05%	1.87%	4.08
U.S. Agency Pass-Throughs	-0.06%	2.11%	4.36
CMBS (Commercial Mortgage Backed Securities)	0.21%	3.46%	5.27
ABS (Asset-Backed Securities)	0.26%	1.75%	2.19
U.S. Corporate Investment Grade	0.54%	5.71%	7.41
U.S. High Yield Corporates	1.42%	8.78%	3.38
Emerging Market Debt	-0.07%	5.81%	4.62
Municipal Bond Index	0.38%	3.28%	5.61
TIPS (Treasury Inflation Protected Securities)	0.33%	3.54%	1.15

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 Bloomberg 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 Bloomberg 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 Bloomberg 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 Bloomberg 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 Bloomberg 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 Bloomberg Barclays CMBS ERISA-Eligible Index is the ERISA-eligible component of the Bloomberg 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 Bloomberg 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.

Emerging Market: Bloomberg uses a fixed list of countries defined as emerging markets countries for index inclusion purposes that is based on World Bank Income group definitions (Low/Middle), IMF country classifications (Non-Advanced Economies), and other advanced economies that may be less accessible or investable for global debt investors.

The Bloomberg 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 Bloomberg 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.

Ratings are measured on a scale that ranges from AAA or Aaa (highest) to D or C (lowest). Investment grade investments are those rated from highest down to BBB- or Baa3.

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