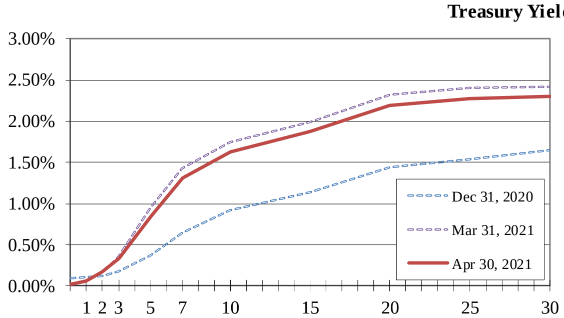
Baird Advisors
Fixed Income Market Commentary
April 2021

Rates Decline and Curve Flattens as Fed Maintains Extremely Accommodative Policies

The 10yr Treasury yield fell 11 bps in April to 1.63% and the yield curve flattened with the 2yr unchanged. Both these moves in the level and shape of the yield curve were countertrend and a partial reversal of the bear steepener we experienced in Q1. Employment grew at a faster-than-expected pace (March nonfarm payrolls +916k vs +660k market consensus), and Q1 GDP came in at +6.4%, though a strong number, was below expectations due to forced inventory drawdowns as supply chain shortages limited companies' ability to quickly ramp up production. Growth expectations for 2021 are in the +6-8% range last seen in 1984, propelled by large fiscal stimulus and a big bounce in consumer spending as pandemic-related restrictions ease. March personal income increased $4.2T annualized (+21.1% from prior month) and March consumer spending increased $616B annualized (+4.2% from prior month) on pandemic relief payments. President Biden outlined his agenda before a joint session of Congress, including the American Families Plan which would spend $1.8T on social programs and be partially paid for by higher personal tax rates and the American Jobs Plan which would spend $2.25T on broad infrastructure needs and be partially paid for by higher corporate tax rates. Strong growth expectations and supply chain bottlenecks in many industries are creating market concerns over inflation (March CPI 2.6% YoY; April expected 3.6% CPI YoY). However, Fed Chair Jay Powell believes the inflation will be transitory, and it's too soon to discuss tapering the Fed's extraordinary QE purchases of $120B/month. "We've had one great jobs report; it's not enough. We're going to act on actual data, not our forecast." said Powell.

Treasury Yields



Maturity	12/31/20	3/31/21	4/30/21	1Mo Chg	YTD Chg
3 Mo	0.09%	0.02%	0.02%	-0.01%	-0.08%
1	0.11%	0.06%	0.05%	-0.01%	-0.06%
2	0.12%	0.16%	0.16%	0.00%	0.04%
3	0.17%	0.35%	0.33%	-0.02%	0.16%
5	0.36%	0.94%	0.85%	-0.09%	0.49%
7	0.65%	1.42%	1.31%	-0.11%	0.66%
10	0.92%	1.74%	1.63%	-0.11%	0.71%
30	1.65%	2.42%	2.30%	-0.12%	0.65%

Spreads Tighter Across Most Market Segments in April

The Fed's very accommodative messaging contributed to spreads tightening across most market segments in April. Lower-quality segments tightened the most, with Emerging Market Debt tightening 27 bps and ending the month at 496 bps, while High Yield Corporates tightened 19 bps to end the month at 291 bps. In comparison, Investment Grade Corporates were a scant 3 bps tighter, ending at 88 bps. Agency Pass-throughs tightened 5 bps during the month (-32 bps YTD), ending the month near all-time tights at 7 bps, as the Fed continues its rapid pace of Quantitative Easing purchases.

Option-Adjusted Spreads (in bps)

	12/31/20	3/31/21	4/30/21	1Mo Chg	YTD Chg
U.S. Aggregate Index	42	31	29	-2	-13
U.S. Agency (non-mortgage)	10	4	4	0	-6
Mortgage and ABS Sectors					
U.S. Agency Pass-throughs	39	12	7	-5	-32
U.S. Agency CMBS	44	34	30	-4	-14
U.S. Non-Agency CMBS	109	99	93	-6	-16
Asset-Backed Securities	33	35	31	-4	-2
Corporate Sectors					
U.S. Investment Grade	96	91	88	-3	-8
Industrial	101	93	91	-2	-10
Utility	106	99	96	-3	-10
Financial Institutions	83	84	79	-5	-4
Other Govt. Related	66	58	58	0	-8
U.S. High Yield Corporates	360	310	291	-19	-69
Emerging Market Debt	503	523	496	-27	-7

Source: Bloomberg Barclays Indices

Sector Returns Positive for April; Mixed YTD

After a challenging Q1, all sectors posted positive returns in April, resulting in mixed YTD returns. Emerging Market Debt was the top performer for the month (+2.50%) driven by strong demand for yield. The Aggregate Index rebounded in April (+0.79%) after its worst quarterly return since 1981 (-3.37%), yet remains in negative territory for the year (-2.61%). TIPS (+1.40%) outperformed nominal Treasuries (+0.75%) again this month as inflation expectations inched higher. The 10-year TIPS inflation breakeven now implies 2.41% average inflation over the next decade, up from 2.37% at the start of the month. U.S. Investment Grade Corporates (+1.11%) and U.S. High Yield Corporates (+1.09%) also performed well in April, while ABS (+0.14%) delivered the smallest returns.

Total Returns of Selected Bloomberg Barclays Indices and Subsectors

	April	YTD	Effective Duration (years)
U.S. Aggregate Index	0.79%	-2.61%	6.39
U.S. Gov't/Credit Index	0.88%	-3.44%	7.42
U.S. Intermediate Gov't/Credit Index	0.50%	-1.37%	4.16
U.S. 1-3 Yr. Gov't/Credit Index	0.08%	0.03%	1.93
U.S. Treasury	0.75%	-3.53%	6.86
U.S. Agency (Non-Mortgage)	0.42%	-1.18%	3.83
U.S. Agency Pass-Throughs	0.55%	-0.55%	3.90
CMBS (Commercial Mortgage Backed Securities)	0.94%	-1.40%	5.21
ABS (Asset-Backed Securities)	0.14%	-0.02%	2.05
U.S. Corporate Investment Grade	1.11%	-3.59%	8.54
U.S. High Yield Corporates	1.09%	1.95%	3.85
Emerging Market Debt	2.50%	-0.64%	5.30
Municipal Bond Index	0.84%	0.48%	5.12
TIPS (Treasury Inflation Protected Securities)	1.40%	-0.09%	7.77

<u>Disclosures</u>

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.

JG2020-1203*

Robert W. Baird & Co. Incorporated