

# Fourth Quarter 2020 Bond Market Commentary

Bond market returns for 2020 were surprisingly strong. Unexpectedly, the 20+ year Treasury, A rated Credit and TIPS indices recorded double digit annual returns. According to Bloomberg, 10-year U.S. Treasuries traded in a range of 1.85% to 0.52% for the year, producing an annual return of 11.0%.

Supported by the Fed, short-term interest rates were pegged at a range of 0.00% to 0.25%. The Fed's aggressive monthly bond buying supported the credit and municipal markets, also limiting the impact of rising rates on the longer end of the yield curve.

With the election uncertainty behind us, focus has returned to 2021 economic growth, potential changes in political priorities and getting the public vaccinated. Uncertainty remains elevated, leading markets to remain highly vulnerable and volatile.

Since the beginning of the year, we have witnessed a significant increase in the slope of the yield curve. While short-term interest rates remain at historical lows, 10-year and longer rates have risen over 20 basis points. These short-term increases in interest rates led to negative year to date returns in all U.S. Treasuries from 3-year to 30-year maturities. Bloomberg calculated that 30-year U.S. Treasuries have produced a -5.2% year to date return through January 11, 2021.

We expect that the yield curve will continue to steepen as the economy recovers and the vaccine becomes more broadly disseminated. The amount of debt that the U.S. Treasury must issue to cover all the Covid-19 rescue packages is historic. This will crowd out other issuers and pressure interest rates higher, particularly in the long end of the yield curve.

We are often faced with the question, "why should we hold our bonds if we face the price declining as interest rates rise?" The simple answer is you will continue to receive the higher income stream you purchased at the start, the volatility will remain consistent with expectations and the asset will provide protection against a significant decline from riskier assets.

Rising interest rates will negatively affect the price of existing bonds in the short run. However, over time the reinvestment of the income and principal at higher interest rates provide increasing protection and ultimately, through the power of compounding, the returns rise to the yields that were originally expected.

Higher interest rates will lead directly to higher future expected returns. Just be patient and remain invested in a portfolio that is structured consistent with your investment objectives.

| Index Returns As of 12/31/20                | Performance Period |         |        |
|---|--------------------|---------|--------|
|   | 3 Month            | 6 Month | 1 Year |
| Bloomberg Barclays US Treasury Intermediate | -0.23              | -0.04   | 5.78   |
| Bloomberg Barclays Govt/Credit Intermediate | 0.48               | 1.10    | 6.43   |
| Bloomberg Barclays Intermediate Aggregate   | 0.42               | 0.90    | 5.60   |
| Bloomberg Barclays US Treasury              | -0.83              | -0.66   | 8.00   |
| Bloomberg Barclays Govt/Credit              | 0.82               | 1.60    | 8.92   |
| Bloomberg Barclays Aggregate                | 0.67               | 1.29    | 7.51   |
| Bloomberg Barclays US Treasury 20+ Year     | -3.02              | -2.89   | 18.10  |
| Bloomberg Barclays Corporate                | 3.05               | 4.63    | 9.89   |
| Bloomberg Barclays Corporate Intermediate   | 1.78               | 3.11    | 7.47   |
| Bloomberg Barclays Corporate High Yield     | 6.45               | 11.34   | 7.11   |
| Bloomberg Barclays Credit AAA               | 0.28               | 0.73    | 6.51   |
| Bloomberg Barclays Credit AA                | 1.46               | 2.33    | 9.10   |
| Bloomberg Barclays Credit A                 | 2.12               | 3.29    | 10.01  |
| Bloomberg Barclays Credit BAA               | 4.03               | 6.21    | 9.43   |
| Bloomberg Barclays MBS                      | 0.26               | 0.36    | 3.87   |
| Bloomberg Barclays TIPS                     | 1.62               | 4.70    | 10.99  |
| Bloomberg Barclays Inter-Short Muni         | 0.82               | 1.88    | 3.97   |

Source: Bloomberg Barclays

## Daily Generic Municipal Bond Yields as of 12/31/20

| Term   | Maturity | AAA  | AA   | A    | BAA  |
|--------|----------|------|------|------|------|
| 1 Yr.  | 2022     | 0.11 | 0.24 | 0.47 | 1.04 |
| 2 Yr.  | 2023     | 0.12 | 0.25 | 0.49 | 1.05 |
| 3 Yr.  | 2024     | 0.13 | 0.26 | 0.50 | 1.05 |
| 4 Yr.  | 2025     | 0.16 | 0.31 | 0.54 | 1.10 |
| 5 Yr.  | 2026     | 0.19 | 0.35 | 0.58 | 1.14 |
| 7 Yr.  | 2028     | 0.36 | 0.51 | 0.74 | 1.31 |
| 9 Yr.  | 2030     | 0.59 | 0.74 | 0.97 | 1.57 |
| 10 Yr. | 2031     | 0.67 | 0.82 | 1.05 | 1.66 |
| 12 Yr. | 2033     | 0.82 | 0.96 | 1.19 | 1.82 |
| 14 Yr. | 2035     | 0.92 | 1.08 | 1.32 | 1.96 |
| 15 Yr. | 2036     | 0.97 | 1.14 | 1.38 | 2.04 |
| 17 Yr. | 2038     | 1.07 | 1.22 | 1.47 | 2.13 |
| 19 Yr. | 2040     | 1.15 | 1.30 | 1.54 | 2.21 |
| 20 Yr. | 2041     | 1.18 | 1.33 | 1.58 | 2.25 |
| 25 Yr. | 2046     | 1.35 | 1.50 | 1.74 | 2.44 |
| 30 Yr. | 2051     | 1.41 | 1.58 | 1.81 | 2.50 |

Source: Bloomberg



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### Index Descriptions:

**Bloomberg Barclays US Intermediate Treasury Index** Unmanaged index includes all publicly issued, US Treasury securities that have a remaining maturity of greater than or equal to 1 year and less than 10 years, are rated investment grade, and have \$250 million or more of outstanding face value.

**Bloomberg Barclays Intermediate Government/Credit Index:** Is an unmanaged index based on all publicly issued intermediate government and corporate debt securities with maturities of 1-10 years. This index represents asset types which are subject to risk, including loss of principal.

**Bloomberg Barclays U.S. Treasury Bond Index:** Is part of Bloomberg Barclays global family of government bonds indices. The index measures the performance of the U.S. Treasury bond market, using market capitalization weighting and a standard rule based inclusion methodology.

**Bloomberg Barclays Government/Credit Bond Index** Unmanaged index that tracks the performance of US Government and corporate bonds rated investment grade or better, with maturities of at least one year.

**Bloomberg Barclays Intermediate Aggregate Index:** Is an unmanaged index that consists of 1-10 year Governments, 1-10 year Corporates, all Mortgages, and all Asset-Backed securities within the Aggregate Index (i.e. the Aggregate Index less the Long Government/Corporate Index).

**Bloomberg Barclays U.S. Aggregate Bond Index:** Is an unmanaged index composed of securities from the Bloomberg Barclays Government/Corporate Bond Index, Mortgage-Backed Securities Index and the Asset-Backed Securities Index. Total return comprises price appreciation/depreciation and income as a percentage of the original investment. Indices are rebalanced monthly by market capitalization.

**Bloomberg Barclays U.S. Credit Index:** Is composed of all publicly issued, fixed-rate, nonconvertible, investment-grade corporate debt. Issues are rated at least Baa by Moody's Investors Service or BBB by Standard & Poor's, if unrated by Moody's. Collateralized Mortgage Obligations (CMOs) are not included. Total return comprises price appreciation/depreciation and income as a percentage of the original investment.

**Bloomberg Barclays U.S. Intermediate Credit Index:** Measures the investment-grade, U.S. dollar-denominated, fixed-rate, taxable corporate and government-related bond markets. The index only includes securities with maturity between one and ten years. It is composed of the Bloomberg Barclays U.S. Corporate Index and a non-corporate component that includes foreign agencies, sovereigns, supranationals and local authorities.

**Bloomberg Barclays U.S. Corporate High Yield Index:** Is an unmanaged index that is comprised of issues that meet the following criteria: at least \$150 million par value outstanding, maximum credit rating of Ba1 (including defaulted issues) and at least one year to maturity.

**Bloomberg Barclays U.S. Mortgage-Backed Securities Index:** Is an unmanaged index that tracks agency mortgage backed pass-through securities (both fixed-rate and hybrid ARM) guaranteed by GNMA, FNMA, and FHLM.

**Bloomberg Barclays U.S. Treasury Inflation-Protected Securities (TIPS) Index:** Represents securities that protect against adverse inflation and provide a minimum level of real return. To be included in this index, bonds must have cash flows linked to an inflation index, be sovereign issues denominated in U.S. currency, and have more than one year to maturity, and, as a portion of the index, total a minimum amount outstanding of 100 million U.S. dollars. An individual cannot invest directly in an index.

**Bloomberg Barclays Municipal Bond Inter-Short 1-10 Year Index:** Is an unmanaged index of municipal bonds traded in the U.S. with maturities ranging from 1-10 years.

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