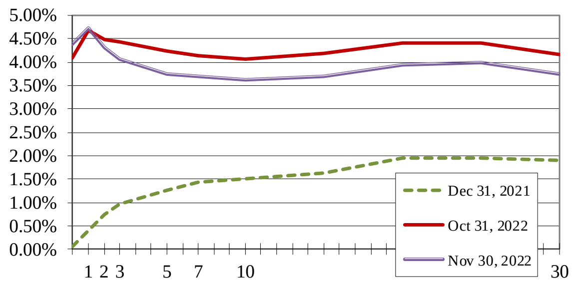
Baird Advisors
Fixed Income Market Commentary
November 2022

Bond Market Rallies Sharply on Additional Signs of Cooling Inflation

Treasury yields declined across the curve except for the 1yr maturity. The 10yr yield ended November at 3.61%, 44 bps lower for the month, a sharp reversal from the recent 3-month stretch of rising yields. Although yields in both maturities fell, the 2s10s curve segment ended November at -70 bps, only slightly less inverted than the cycle low of -78 bps achieved intra-month. November started with a soft market tone as the Fed hiked its policy rate by the expected 75 bps, the 4th consecutive move of this size, and the labor market remained resilient with an above consensus +261k increase in non-farm payrolls. Market tone improved significantly on November 10th when the CPI rose a less than expected 7.7% YoY and continued its downward trend from June's 9.1% YoY peak. Bond yields declined and credit spreads narrowed on news of cooling inflation. Fed Chair Powell spoke at a Brookings Institution event at month end and confirmed that moderating the pace of 75 bps rate hikes "may come as soon as the December meeting" but emphasized "we have a long way to go in restoring price stability." That view underscores the need to allow "some time" for the 3.75% of cumulative hikes since March to work through the economy, principally labor and housing. Midterm elections results split party control in Congress. The near-term possibility of additional spending in the lame duck session exists but may be followed by a more challenging environment for major new legislation in Washington.

Treasury Yields



Maturity	12/31/21	10/31/22	11/30/22	1Mo Chg	YTD Chg
3 Mo	0.06%	4.09%	4.38%	0.29%	4.32%
1	0.39%	4.67%	4.74%	0.07%	4.35%
2	0.74%	4.49%	4.31%	-0.18%	3.57%
3	0.96%	4.44%	4.05%	-0.39%	3.09%
5	1.27%	4.23%	3.74%	-0.49%	2.47%
7	1.44%	4.15%	3.68%	-0.47%	2.24%
10	1.51%	4.05%	3.61%	-0.44%	2.10%
20	1.94%	4.41%	3.93%	-0.48%	1.99%
30	1.91%	4.17%	3.74%	-0.43%	1.83%

IG Corporate Spreads Tighten Further in November

IG Corporate spreads remained on a tightening trend, moving -25 bps for the month to +133, below the October peak (+165), despite issuance exceeding expectations. Financials, the IG Corporate subsector that had widened most in 2022 through October, tightened most (-32). Agency RMBS spreads fell 21 bps and like corporates ended over 30 bps tighter than the 2022 wides (+87). ABS spreads were the only sector to move wider (+8) and now stand +50 bps wider during the past two months. US High Yield (-16) lagged the tightening in IG. Emerging Markets tightened a dramatic -95 bps but remain +138 wider for the year.

Monthly US Agg Returns Highest Since December 2008

US Aggregate return of 3.68% showcased broad strength and erased a portion of the YTD declines (-12.62%). IG Corporate debt performed well, producing +2.11% of excess returns. Agency RMBS also posted strong excess return (+1.35%) after three prior months of negative excess returns. ABS was the only major sector with negative excess returns (-0.08%). Emerging Markets provided the highest nominal (+8.22%) and excess returns in November (+5.90%). Municipal returns were tops domestically at +4.68%, particularly when adjusted for their tax advantage. TIPs, despite a higher duration, returned only 1.83%.

Option-Adjusted Spreads (in bps)

	12/31/21	10/31/22	11/30/22	1Mo Chg	YTD Chg
U.S. Aggregate Index	36	65	53	-12	17
U.S. Agency (non-mortgage)	8	26	25	-1	17
Mortgage and ABS Sectors					
U.S. Agency RMBS (Pass-throughs)	31	73	52	-21	21
U.S. Agency CMBS	34	66	59	-7	25
U.S. Non-Agency CMBS	95	190	188	-2	93
Asset-Backed Securities	38	95	103	8	65
Corporate Sectors					
U.S. Investment Grade	92	158	133	-25	41
Industrial	95	148	125	-23	30
Utility	107	155	136	-19	29
Financial Institutions	83	177	145	-32	62
Non-Corporate Credit	55	76	67	-9	12
U.S. High Yield Corporates	283	464	448	-16	165
Emerging Market Debt	581	814	719	-95	138

Source: Bloomberg Indices

Total Returns of Selected Bloomberg Indices and Subsectors

	MTD Total Return	MTD Excess Return	QTD Total Return	QTD Excess Return	YTD Total Return	YTD Excess Return	Effective Duration (years)
U.S. Aggregate Index	3.68%	0.94%	-2.09%	0.00%	-12.62%	-1.06%	6.22
U.S. Gov't/Credit Index	3.57%	0.79%	-1.89%	0.40%	-13.16%	-0.58%	6.47
U.S. Intermediate Gov't/Credit Index	2.17%	0.43%	-1.00%	0.16%	-8.07%	-0.34%	3.86
U.S. 1-3 Yr. Gov't/Credit Index	0.82%	0.17%	-0.53%	0.05%	-3.87%	-0.05%	1.88
U.S. Treasury	2.68%	0.00%	-2.25%	0.00%	-12.01%	0.00%	6.16
U.S. Agency (Non-Mortgage)	1.52%	0.12%	-1.37%	-0.34%	-7.83%	-0.93%	3.37
U.S. Agency RMBS (Pass-Throughs)	4.08%	1.35%	-2.59%	-0.95%	-11.42%	-2.26%	5.75
CMBS (Commercial Mortgage-Backed Sec.)	2.63%	0.52%	-2.16%	-0.75%	-10.95%	-1.57%	4.66
ABS (Asset-Backed Securities)	0.99%	-0.08%	-1.02%	-0.67%	-4.92%	-0.89%	2.89
U.S. Corporate Investment Grade	5.18%	2.11%	-1.38%	1.12%	-15.39%	-1.42%	7.22
U.S. High Yield Corporates	2.17%	0.37%	0.66%	1.81%	-10.63%	-3.34%	3.90
Emerging Market Debt	8.22%	5.90%	2.61%	4.22%	-13.32%	-3.56%	5.04
Municipal Bond Index	4.68%	N/A	-0.18%	N/A	-8.79%	N/A	6.17
TIPS (Treasury Inflation Protected Sec.)	1.83%	0.00%	-3.73%	0.00%	-10.94%	0.00%	6.80

*Excess return represents the return of a spread sector versus a like-duration U.S. Treasury.

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 U.S. 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 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 Intermediate U.S. Government/Credit Bond 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 1-3 Year U.S. Government/Credit Bond 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 zero and three years.

The Bloomberg 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 CMBS ERISA-Eligible Index is the ERISA-eligible component of the Bloomberg 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 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 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 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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