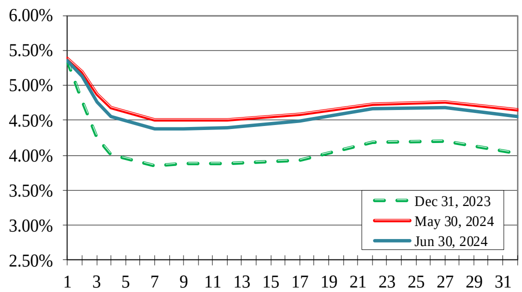
Baird Advisors
Fixed Income Market Commentary
June 2024

Treasury Yields Fall in June but End Higher for Q2, Resilient Economy Likely Delays Fed Rate Cuts

The 10yr Treasury yield covered a 50-bps trough-to-peak range (4.20% – 4.70%) in Q2 before settling at 4.40% at the end of June, up 20 bps for the quarter. The 2s10s Treasury curve inversion continued throughout but narrowed slightly to -36 bps from -42 bps at the start of the quarter. Yields rose early in the quarter on robust job creation and sticky inflation data. The Fed's preferred inflation measure, Core PCE, had held steady at a 2.8% annual rate for three consecutive months before easing in the May reading to 2.6%, helping to allay market concerns of a potential reacceleration in inflation. Yet, the Fed acknowledged in its June Summary of Economic Projections (SEP) a slightly higher for longer inflation outlook. The central tendency for Core PCE rose to 2.35% in 2025 from 2.20% in the March SEP outlook, while still expecting to achieve their 2.0% target rate in 2026. Market expectations for cuts this year fell to just over one (44 bps) from more than two (67 bps) in March (and six to start the year). Also, noteworthy this quarter was the updated Federal deficit forecast from the CBO for FY2024 which rose to $1.9T from $1.5T. The cumulative deficit over the next ten years also rose to $22.1T from $20T, and by 2034 they expect the federal debt held by the public to rise from $28.2T currently (99% of GDP) to $50.7T (122% of GDP).

Treasury Yields



Maturity	12/31/23	3/31/24	5/31/24	6/30/24	1 Mo Chg	Q2 Chg	YTD Chg
3 Mo	5.36%	5.38%	5.41%	5.36%	-0.05%	-0.02%	0.00%
1	4.78%	5.04%	5.19%	5.13%	-0.06%	0.09%	0.35%
2	4.25%	4.62%	4.88%	4.76%	-0.12%	0.14%	0.51%
3	4.01%	4.41%	4.68%	4.55%	-0.13%	0.14%	0.54%
5	3.85%	4.21%	4.51%	4.38%	-0.13%	0.17%	0.53%
7	3.88%	4.21%	4.51%	4.38%	-0.13%	0.17%	0.50%
10	3.88%	4.20%	4.50%	4.40%	-0.10%	0.20%	0.52%
20	4.20%	4.45%	4.73%	4.66%	-0.07%	0.21%	0.46%
30	4.03%	4.35%	4.65%	4.56%	-0.09%	0.21%	0.53%

IG Corporate Spreads Wider in June and Q2

IG Corporate spreads widened for June (+9 bps) and Q2 (+4 bps). Non-Agency CMBS also widened modestly for both the month (+6 bps) and quarter (+2 bps). Agency RMBS spreads ended the month at 48 bps, nearly unchanged for the quarter, but higher spread volatility continued in the sector (14bps OAS range in Q2).

Strong Agg Returns in June Turn Q2 Positive

The Agg Index return of +0.95% placed Q2 results back in positive territory (+0.07%). Excess returns for CMBS led investment grade sectors in Q2 (+0.24%). IG Corporate excess returns in June of -0.56% resulted in Q2 excess returns finishing modestly negative (-0.04%). High Yield was the outlier, achieving positive excess returns in June (+0.13%) and Q2 (+0.36%) despite modestly wider spreads.

Option-Adjusted Spreads (in bps)

	12/31/23	3/31/24	5/31/24	6/30/24	1 Mo Chg	Q2 Chg	YTD Chg
U.S. Aggregate Index	42	39	37	39	2	0	-3
U.S. Agency (non-mortgage)	17	15	13	13	0	-2	-4
Mortgage and ABS Sectors							
U.S. Agency RMBS (Pass-throughs)	47	49	50	48	-2	-1	1
U.S. Agency CMBS	48	41	39	40	1	-1	-8
U.S. Non-Agency CMBS	203	152	148	154	6	2	-49
Asset-Backed Securities	68	55	54	57	3	2	-11
Corporate Sectors							
U.S. Investment Grade	99	90	85	94	9	4	-5
Industrial	90	85	81	90	9	5	0
Utility	105	97	93	104	11	7	-1
Financial Institutions	112	96	88	97	9	1	-15
Non-Corporate Credit	55	53	50	53	3	0	-2
U.S. High Yield Corporates	323	299	308	309	1	10	-14
Emerging Market Debt	598	527	502	513	11	-14	-85

Source: Bloomberg Indices

Total Returns of Selected Bloomberg Indices and Subsectors

	MTD Total Return	MTD Excess Return	Q2 Total Return	Q2 Excess Return	YTD Total Return	YTD Excess Return	Effective Duration (years)
U.S. Aggregate Index	0.95%	-0.13%	0.07%	-0.03%	-0.71%	0.20%	6.13
U.S. Gov't/Credit Index	0.87%	-0.20%	0.05%	-0.01%	-0.68%	0.33%	6.22
U.S. Intermediate Gov't/Credit Index	0.80%	-0.08%	0.64%	0.08%	0.49%	0.30%	3.76
U.S. 1-3 Yr. Gov't/Credit Index	0.56%	-0.03%	0.95%	0.02%	1.38%	0.11%	1.85
U.S. Treasury	1.01%	0.00%	0.10%	0.00%	-0.86%	0.00%	5.93
U.S. Agency (Non-Mortgage)	0.77%	0.01%	0.76%	0.09%	0.83%	0.23%	3.05
U.S. Agency RMBS (Pass-Throughs)	1.17%	0.06%	0.07%	-0.09%	-0.98%	-0.23%	6.08
CMBS (Commercial Mortgage Backed Securities)	0.94%	-0.03%	0.68%	0.24%	1.53%	1.71%	4.23
ABS (Asset-Backed Securities)	0.67%	-0.02%	0.98%	0.17%	1.66%	0.71%	2.64
U.S. Corporate Investment Grade	0.64%	-0.56%	-0.09%	-0.04%	-0.49%	0.85%	6.92
U.S. High Yield Corporates	0.94%	0.13%	1.09%	0.36%	2.58%	1.96%	3.14
Emerging Market Debt	0.25%	-0.73%	1.17%	0.84%	5.93%	6.23%	4.82
Municipal Bond Index	1.53%	N/A	-0.02%	N/A	-0.40%	N/A	6.02
Taxable Municipal Bond: Agg Eligible	0.94%	-0.49%	-0.77%	-0.23%	-1.21%	1.30%	9.27
TIPS (Treasury Inflation Protected Securities)	0.78%	0.00%	0.79%	0.00%	0.70%	0.00%	6.53

*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.

RB2021-0805

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