Bond Market Review

January 13, 2025

Summary

- Economic resilience remains a primary theme to start 2025 as a strong December jobs report pushed the 10-year Treasury yield to its highest level since late 2023. Since the Fed cut interest rates in mid-September, the 10-year yield is over 100 bps higher on economic strength, the fiscal outlook, and worries of higher inflation. In fact, the University of Michigan 1-year Inflation Expectations report showed consumers now expect inflation to rise by 3.3% over the next 12-months compared to estimates of 2.8%. After the sharp rise in rates and inflation expectations, Fed funds futures now predict only one rate cut all year which is down from six expected cuts in early 2024.

Treasury Yields			
Term	Treasury Yield	∆ MTD	∆ YTD
3 Month	4.32	0.00	0.00
6 Month	4.29	0.02	0.02
1 Year	4.21	0.07	0.07
2 Year	4.38	0.14	0.14
5 Year	4.57	0.19	0.19
10 Year	4.76	0.19	0.19
30 Year	4.95	0.17	0.17

Taxable

Heavy New Issuance to Start Year

- We expect the investment grade corporate primary market stole most of the attention as $66 billion in new issuance hit the street. The market was well set up for this in our view, with negative dealer inventories providing plenty of support for what turned out to be a modest amount of secondary market selling. Rising interest rates due to strong economic data put pressure on equities but investment grade spreads were largely steady all week. Publicly traded utilities in California came under pressure as wildfires broke out across Los Angeles, although the cause of the fires is still under investigation.

High Yield Posts Modest Gains

- The high yield corporate market posted modest gains in the first full week of the year with spreads 6 bps tighter, driving excess returns of 0.27%. So far this month the ICE BofA High Yield Master II Index option-adjusted spread is 10 bps tighter, unwinding a little more than half of the widening we saw in December. Higher rates drove the conversation last week with the 5-year Treasury yield increasing by 9 bps, causing the market to hit some resistance. However, with yields above 7.4%, buyers appear to be stepping in on weakness.

Municipal Yields								
Term	Municipal Yield	∆ MTD	∆ YTD	Tax-Equivalent Yield	Tax-Equivalent Spread (bps)	Muni/Treasury Ratio (%)	∆ MTD	∆ YTD
1 Year	2.80	-0.17	-0.17	4.31	10.32	66.59	-5.05	-5.05
2 Year	2.85	0.02	0.02	4.38	-0.23	64.97	-1.52	-1.52
5 Year	2.98	0.08	0.08	4.59	1.40	65.20	-1.03	-1.03
10 Year	3.24	0.11	0.11	4.98	21.93	67.99	-0.47	-0.47
30 Year	4.10	0.22	0.22	6.30	135.31	82.78	1.75	1.75

Tax-Free

Muni Yields Follow Treasuries Higher

- It was a challenging week for the bond market, including munis as interest rates rose across the curve in a bear steepening fashion. The 1-10 year AAA-rated tax-exempt curve was 8-17 bps higher and is now upward sloping across every maturity tenor. Although the current 39 bps of slope in the curve is wider than the 3 month average, it remains well below the 120 bps experienced in June of 2022.

Nine States Lower Income Taxes

- Nine states lowered income tax rates which took effect on January 1. Two of these states, Iowa and Louisiana, moved to a flat income tax structure at 3.8% and 3.0% respectively reflecting a notable 1.9% and 1.25% decline in just one year's time. The remaining seven are taking a more gradual approach and include Indiana, Mississippi, Missouri, Nebraska, New Mexico, North Carolina, and West Virginia.

Fed = Federal Reserve. bps = basis points. Data is as of 01.10.2025. Sources: Bloomberg L.P.; ICE BofA. Please refer to page 3 for important definitions and disclosures.

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International Yields

	Germany	Japan	U.K.	France	Italy	Spain	Greece
2 Year	3.07	2.28	0.65	4.54	2.48	2.6	2.43
5 Year	3.17	2.38	0.83	4.55	2.99	3.1	2.82
10 Year	3.44	2.60	1.20	4.84	3.43	3.77	3.27
30 Year	3.54	2.79	2.31	5.41	3.94	4.4	3.90

Sectors[1]

	Duration	Spread	∆ MTD	∆ YTD	52- Week High	52-Week Low
Investment Grade Corporate	7	80	0	0	111	74
▪ Financial	5	83	1	1	115	74
▪ Industrial	7	78	0	0	107	73
▪ Utility	8	84	2	2	116	78
High Yield	3	274	-13	-13	381	253
Securitized	6	48	3	3	58	41
▪ Commercial Mortgage-Backed Securities	4	78	-2	-2	122	78
▪ Asset-Backed Securities	3	43	-1	-1	66	43
▪ Mortgage-Backed Securities	6	46	3	3	56	37

Equity

	Current	∆ MTD	∆ YTD
Dow Jones	41,938.45	-605.77	-605.77
S&P 500	5,827.04	-54.59	-54.59
Nasdaq	19,161.63	-149.16	-149.16

Volatility

	Current	∆ MTD	∆ YTD
VIX	19.54	2.19	2.19
MOVE	96.57	-2.23	-2.23

Commodities

	Current	∆ MTD	∆ YTD
CRB	305.97	9.25	9.25
Gold	2715.00	74.00	74.00
Oil	76.57	4.85	4.85
Gas	207.49	6.57	6.57

Currency

	Current	∆ MTD	∆ YTD
U.S. Dollar	109.65	1.16	1.16
Euro	1.02	-0.01	-0.01
Pound	1.22	-0.03	-0.03
Yen	157.73	0.49	0.49
Canadian Dollar	1.44	0.00	0.00
Franc	0.92	0.01	0.01

Central Bank Rates

	Current	∆ MTD	∆ YTD
United States	4.50	0.00	0.00
Europe	3.15	0.00	0.00
United Kingdom	4.75	0.00	0.00
Japan	0.25	0.00	0.00
Canada	3.25	0.00	0.00

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[1]Sectors are represented by the following indices: Investment Grade Corporate = Bloomberg U.S. Corporate Bond; Financial = Bloomberg U.S. Aggregate Investment Grade Finance; Industrial = Bloomberg U.S. Aggregate Investment Grade Industrial; Utility = Bloomberg U.S. Investment Grade Utility; High Yield = Bloomberg U.S. Corporate High Yield; Securitized = Bloomberg U.S. Securitized; Commercial Mortgage-Backed Securities = Bloomberg U.S. Aggregate CMBS; Asset-Backed Securities = Bloomberg U.S. Aggregate ABS; Mortgage-Backed Securities = Bloomberg U.S. Aggregate MBS.

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Technical Terms: Duration: a tool used in assessing the price volatility of a fixed-income security. **Gross Domestic Product (GDP)** A comprehensive measure of U.S. economic activity. GDP measures the value of the final goods and services produced in the United States (without double counting the intermediate goods and services used up to produce them). The **federal funds rate** is the interest rate at which depository institutions (mainly banks) lend reserve balances to other depository institutions overnight on an uncollateralized basis. In simpler terms, it's the rate banks charge each other for short-term loans to meet their reserve requirements. **Municipal/Treasury Ratio**: a comparison of the current yield of municipal bonds to U.S. Treasuries. **Non-farm payroll** refers to the number of jobs in the private sector and government agencies. It excludes farm workers, private household employees, proprietors, non-profit employees, and actively serving military. **Option-Adjusted Spread (OAS)** is the measurement of the spread of a fixed-income security rate and the risk-free rate of return, which is then adjusted to take into account an embedded option. Typically, an analyst uses Treasury yields for the risk-free rate. The spread is added to the fixed-income security price to make the risk-free bond price the same as the bond. **Personal consumption expenditures (PCE)** is the primary measure of consumer spending on goods and services in the U.S. economy. **Tax-Equivalent Spread** is the spread needed on a taxable bond to produce the same yield as a municipal bond. **Tax-Equivalent Yield**: the return that is required on a taxable investment to make it equal to the return on a tax-exempt investment. **Yield Spread**: the difference between the quoted rates of return between two different investment vehicles; also called the credit spread. **Yield-To-Worst:** Is a measure of the lowest possible yield that can be received on a bond that fully operates within the terms of its contract without defaulting. It is a type of yield that is referenced when a bond has provisions that would allow the issuer to close it out before it matures.

The volatility of an index varies greatly. All indices are unmanaged, and investments cannot be made directly in an index.

The **Commodity Research Bureau Index** (CRB) comprises a basket of 19 commodities, with 39% allocated to energy contracts, 41% to agriculture, 7% to precious metals, and 13% to industrial metals. The CRB is designed to isolate and reveal the directional movement of prices in overall commodity trades. The **Consumer Price Index (CPI)** is a measure of the average change overtime in the prices paid by urban consumers for a market basket of consumer goods and services. **Dow Jones Industrial Average (DJIA)** an index that tracks 30 large, publicly-owned blue-chip companies trading on the New York Stock Exchange (NYSE) and the NASDAQ. **The ICE BofA High Yield Master II Index** is an unmanaged index comprised of over 1,200 high yield bonds representative of high yield bond markets as a whole. It includes zero-coupon bonds and payment-in-kind (PIK) bonds. **The ICE BofA MOVE Index** is a well-recognized measure of U.S. interest rate volatility that tracks the movement in U.S. Treasury yield volatility implied by current prices of one-month over-the-counter options on 2-year, 5-year, 10-year and 30-year Treasuries. **The Nasdaq Composite Index** the market capitalization-weighted index of over 2,500 common equities listed on the NASDAQ stock exchange. The types of securities in the index include American depositary receipts, common stocks, real estate investment trusts (REITs) and tracking stocks, as well as limited partnership interests. The index includes all Nasdaq-listed stocks that are not derivatives, preferred shares, funds, exchange-traded funds (ETFs) or debenture securities. **The ICE BofA 1-10Y Municipal Securities Index** is a subset of the ICE BofA U.S. Municipal Securities Index including all securities with a remaining term to final maturity less than 10 years. **The S&P 500® Index** is a readily available, carefully constructed, market-value-weighted benchmark of common stock performance. Currently, the S&P 500 Composite includes 500 of the largest stocks (in terms of stock market value) in the United States and covers approximately 80% of available market capitalization. **The CBOE Volatility Index**, or VIX, is a real-time market index representing the market's expectations for volatility over the coming 30 days. **The Bloomberg U.S. Corporate Index** covers performance for United States corporate bonds. This index serves as an important benchmark for portfolios that include exposure to investment grade corporate bonds. **The Bloomberg 1-3 Year U.S. Aggregate Bond Index** is the 1-3 year component of the U.S. Aggregate Index. The Bloomberg U.S. Aggregate Bond Index represents securities that are SEC-registered, taxable and dollar denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass through securities, and asset-backed securities. **Bloomberg L.P. Information:** "Bloomberg®" and the Bloomberg indices are service marks of Bloomberg Finance L.P. and its affiliates, including Bloomberg Index Services Limited ("BISL"), the administrator of the index (collectively, "Bloomberg") and have been licensed for use for certain purposes by Sterling Capital Management LLC and its affiliates. Bloomberg is not affiliated with Sterling Capital Management LLC or its affiliates, and Bloomberg does not approve, endorse, review, or recommend the product(s) presented herein.
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