MANAGER COMMENTARY

FIXED INCOME

GREAT LAKES ADVISORS

A WINTRUST WEALTH MANAGEMENT COMPANY

MANAGER COMMENTARY

Third Quarter 2020

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MARKET REVIEW

Despite equity market gyrations over the period, the bond markets stayed relatively steady throughout the quarter. The treasury market barely reacted to news regarding economic stimulus and potential cures for COVID-19 as the short end of the curve remained anchored to historic low yields. The Fed said they intend to let inflation run hot until they believe the economy is reviving. That may take some time. The usual drama before an election is upon us, and will likely be the driver of short-term volatility, as will the rush to find a vaccine.

INDEX RETURNS FOR THE PERIOD ENDING SEPTEMBER 30, 2020

	Q3 2020	YTD
BB Aggregate	0.62%	6.79%
Corporate	1.54%	6.64%
Treasuries	0.17%	8.90%
ABS	0.80%	4.14%
Mortgages	0.11%	3.62%
High Yield	4.60%	0.62%
Municipal	1.23%	3.33%
2-year Treasury	0.07%	3.03%
10-year Treasury	0.06%	12.77%
30-year Treasury	-0.80%	23.91%

Source: Bloomberg

SECTOR HIGHLIGHTS

Credit

- Corporate Spreads were tighter by 14 basis points in the third quarter.
- Longer dated securities outperformed shorter dated securities and BBB rated securities outperformed A rated securities.

Mortgage-Backed Securities

- Agency MBS barely outperformed their treasury hedges for Q3. Mortgages posted 11 basis points of total return.
- In Q3, production coupons outperformed the broader mortgage market, which is not surprising as the Fed continues to support the current coupon.
- The FHFA, along with FNMA and FHLMC, announced new buyout protocols. The previous standard of 4 months of delinquencies was replaced with a 24 month standard.

Asset-Backed Securities

- ABS posted a strong quarter of returns with 80 bps of total return.
- ABS origination was robust in September with the heaviest supply of the year. However, on a year-over-year basis new issue volumes are down 17%.
- Within the sectors, credit cards have outperformed autos.

Commercial Mortgage-Backed Securities

- CMBS returned 132 basis points of total return for the quarter.
- CMBS delinquencies continue to improve, but will likely take 2-3 years to recover to pre-COVID performance – especially in the hotel and retail sectors.
- There was strong money manager demand for both conduit AAA and BBB paper over the third quarter.

Treasuries

- Treasuries had a rather benign third quarter, returning only about 17 basis points. The 10-year treasury yield started the quarter at 0.676% and ended at 0.684%, essentially no change.
- The 10-year rate did drop to a low of 50 basis points in early August, but climbed back from that low. In addition, the entire curve basically did not shift in Q3, looking at the beginning and the end. The 2yr/10yr part of the curve did flatten a touch during July dropping just below 40 basis points in early August, but steepened since then ending the quarter at 55 basis points compared to 50 basis points at the beginning.
- The largest move for yields in the quarter across the entire curve happened in the 6 month tenor where rates dropped just 5 basis points.

Municipals

- Munis benefitted from lower rates and increased demand in the quarter.
- Returns for the quarter were positive in all Muni composites.
- We expect the usual rush to market before elections for new issuance this month.

GLA FIXED INCOME PRELIMINARY RETURNS[1]

	Q3	YTD
Core	1.08%	8.02%
BB Agg	0.62%	6.79%
Intermediate G/C	0.64%	6.16%
BB Int G/C	0.61%	5.92%
Short Term	0.80%	3.58%
BB Gov/Credit 1-3	0.23%	3.12%
Municipal	1.36%	3.24%
BB Muni 1-10	1.07%	3.21%

Core Fixed

- We outperformed by 46 basis points versus the index for the quarter.
- Our overweight to Corporates added about 32 basis points, however our selection detracted 6 basis points, specifically within Consumer Cyclicals.
- Our underweight to Mortgages added 7 basis points, and our selection added 5 basis points.
- Treasuries added 13 basis points, but our ABS were not significant contributors or detractors.

Intermediate Fixed

- Intermediate portfolios outperformed by a handful of basis points for the third quarter of 2020.
- Portfolio allocation led performance by contributing 10 basis points overall, while selection detracted by 7 basis points.
- Our overweight to the corporate sector performed well with the intermediate (5-7yr) part of the curve outperforming the wings. Also, our overweight to the financial sector led corporate performance. Our out of index allocation to mortgages and agency CMBS also provided positive performance.

Short-Term Fixed

- We outperformed the index by 57 basis points.
- ABS added 5 basis points, and MBS added 1 basis point.
- Our overweight to Corporates added 14 basis points, and our underweight to Treasuries added 6 basis points.
- Our selection within Corporates added 35 basis points, with Financials adding the most alpha.

MARKET OUTLOOK

Going forward, we continue to view treasuries as range bound. Virus outbreaks during the cold months and the high probability of presidential election turmoil will keep rates from increasing, while the potential for positive vaccine news and an expected Biden/democratic senate victory could mean a strong stimulus package, which would keep rates from dropping significantly.

1. Returns are preliminary and from a representative account.

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