



MERGANSER
CAPITAL MANAGEMENT

THE MERGANSER FLASH

FIXED INCOME INSIGHTS

AS OF AUGUST 31, 2015

Market Commentary

THE ECONOMY

- The US economic performance remains good, but not great, as retail sales improved after a weak July release, offset by concerns of inflation remaining too low. Employment data remains on the stronger side, although slow real wage growth persists. With second quarter GDP growth at 3.7%, the Fed's base case of a 2015 hike is still intact. However, questions remain about the effects of instability abroad and market participants have become less convinced that September will be liftoff. We remain cautious that the economic recovery lingers on unstable ground and is increasingly vulnerable to exogenous shocks.
- Markets shrugged off the signing of the 3rd Greek bailout in 5 years as all eyes remain myopic in their focus on the slowdown of China's economy. Commodity markets and global equity markets went into a tailspin as fewer market participants and lack of transparency from China exacerbated volatility. The official policy responses from China during the month include removing their exchange rate peg and lowering the reserve ratio for the 5th time this year, while unofficially the PBOC continues to oscillate in its level of direct intervention in stock markets.

STRUCTURED MARKETS

- CMBS spreads widened across the capital stack during August against a backdrop of a busy primary market, interest rate volatility and investor anticipation of the first Fed liftoff. Benchmark 10-yr new issue conduit AAA paper is now trading at swaps +119 basis points (bps), the widest levels seen in 2015.
- Although we feel spreads will compress in the 4th quarter, the near-term directionality is less certain, particularly given the upcoming Fed calendar and a heavy new issue pipeline, which is expected to exceed \$11 billion in September.

CORPORATE CREDIT MARKET

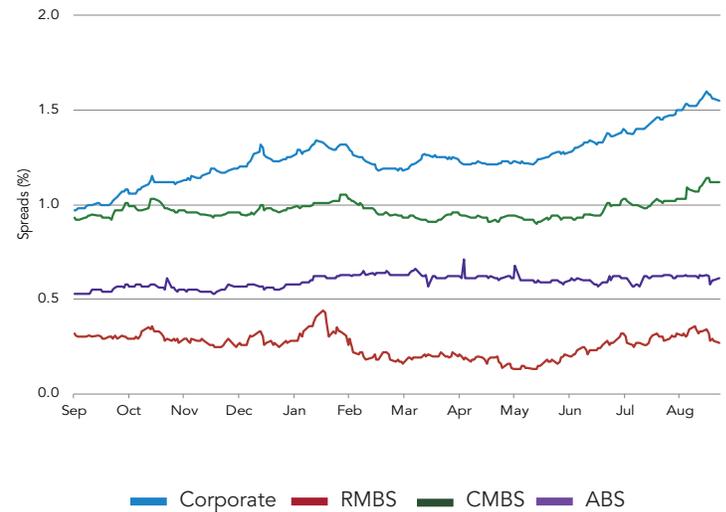
- The corporate index widened 9 bps in August, as China's slowdown and commodities weakness continued to weigh on performance. The devaluation of the Yuan and weaker than expected manufacturing data from China prompted global markets to reprice; pushing US stock indexes down more than 6% for the month (including the largest intra-day decrease of the Dow Jones Industrial Index on August 25th). Nevertheless, US fundamentals remained solid with over 74% of S&P 500 constituents beating earnings estimates for the quarter.
- Over \$54 billion in IG issues priced, a robust amount for a seasonally quiet month, bringing YTD supply to \$904 billion. September is expected to be another blockbuster month, reflected by consensus expectations for \$100 billion in supply, as issuers look to take advantage of low all-in financing costs.

GOVERNMENT MARKET

- Treasury rates were slightly higher for the period among all maturities. Yields on the 2-yr ended the month 8 bps higher, while the 30-yr rose 6 bps. The 10-yr and 5-yr were up 4 bps and 2 bps respectively.

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SPREADS TO TREASURIES



BARCLAYS BENCHMARK DATA

	Total Return MTD
1-3 Gov/Credit	-0.06%
Int. Gov/Credit	-0.08%
Aggregate	-0.14%
1-3 Yr US Treasury	-0.05%
3-5 Yr US Treasury	0.04%
5-10 Yr US Treasury	0.21%
10-20 Yr US Treasury	-0.25%
20+ Yr US Treasury	0.01%

SECTOR DATA FROM BARCLAYS AGGREGATE

	Total Return MTD	Excess Return* MTD	Current YTM
Corporates	-0.59%	-0.59%	3.48%
Financials	-0.16%	-0.17%	3.06%
Industrials	-0.82%	-0.81%	3.69%
Utilities	-0.63%	-0.62%	3.71%
RMBS	0.08%	0.08%	2.71%
CMBS	-0.32%	-0.35%	2.57%
ABS	0.10%	0.11%	1.49%
Agencies	-0.34%	-0.33%	1.95%

*Month-to-date performance of spread bearing bonds versus duration-matched Treasuries