THE MERGANSER FLASH

FIXED INCOME INSIGHTS

AS OF FEBRUARY 29, 2016

MERGANSER CAPITAL MANAGEMENT

Market Commentary

THE ECONOMY

- Fears of further weakening in much of the global macro picture remain. China continued to ease monetary policy through its fifth cut to the required reserve ratio. Commodity markets remain quite volatile, heightening concerns about shrinking balance sheets of net commodity exporting economies. While spending on increased production of commodities has slowed, the supply response is unlikely to be swift enough to result in a V shaped recovery.
- Domestically, the economic picture remains solid but muted. While manufacturing continues to exhibit weakness, retail sales and inflation both ticked up on the month, reducing the likelihood of calls of a Fed "policy mistake." We remain cautious of spill-over effects from abroad but the pockets of strength in the US continue to carry the US economy outside of recessionary levels as evidenced by 4Q GDP of 1.0%.

STRUCTURED MARKETS

- After selling-off sharply towards the beginning of the month, CMBS spreads have stabilized along with other risk assets. Ongoing macro volatility and risk aversion continue to weigh on credit oriented sectors, which have become increasingly correlated during the first few weeks of 2016. Importantly, the bulk of the widening has been felt further down in the capital structure, with front pay bonds and short legacy credits holding up relatively well.
- Similar to other structured sectors, private label conduit issuance has been lackluster with only $10.7B pricing year-to-date, a 34% reduction from the same period last year. Although the forward calendar points to increased deal flow, ongoing volatility and regulatory uncertainty surrounding risk retention rules complicate the picture for the second part of the year, suggesting total issuance may come in well below street estimates.

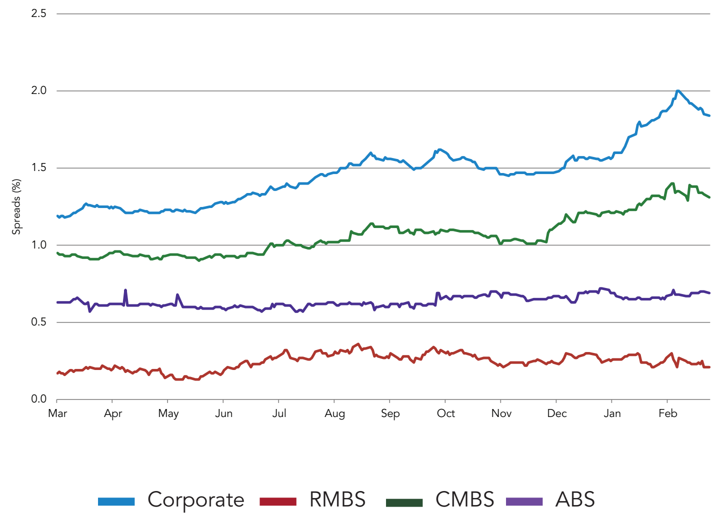
CORPORATE CREDIT MARKET

- Corporate spreads widened 1 basis point (bp) through February 29th due to volatility within financials (+19 bps). Concerns over Deutsche Bank's ability to pay coupons on its subordinated capital notes spilled over into several European banks due to ongoing concerns over profitability and restructuring risks. Spreads in the sector have retraced some of the widening mid-month given Deutsche's tender offer on some of its existing Euro and USD-denominated senior unsecured debt.
- Issuance volume picked up in the back end of the month with $105B in supply versus an initial forecast of $100B+. Barring further volatility, we expect another strong month in March.

GOVERNMENT MARKET

- The 2-yr yield ended the month flat while the 10-yr yield decreased 19 bps. The 5-yr and 30-yr yields decreased 12 bps and 13 bps respectively.

SPREADS TO TREASURIES



BARCLAYS BENCHMARK DATA

	Total Return MTD
1-3 Gov/Credit	0.09%
Int. Gov/Credit	0.49%
Aggregate	0.71%
1-3 Yr US Treasury	0.11%
3-5 Yr US Treasury	0.43%
5-10 Yr US Treasury	1.10%
10-20 Yr US Treasury	1.84%
20+ Yr US Treasury	3.13%

SECTOR DATA FROM BARCLAYS AGGREGATE

	Total Return MTD	Excess Return* MTD	Current YTM
Corporates	0.81%	-0.24%	3.61%
Financials	-0.16%	-1.01%	3.19%
Industrials	1.22%	0.14%	3.82%
Utilities	1.41%	-0.15%	3.54%
RMBS	0.37%	-0.14%	2.35%
CMBS	0.81%	0.05%	2.65%
ABS	0.21%	0.00%	1.54%
Agencies	0.59%	0.05%	1.78%

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