



MERGANSER
CAPITAL MANAGEMENT

THE MERGANSER FLASH

FIXED INCOME INSIGHTS

AS OF MARCH 31, 2016

Market Commentary

THE ECONOMY

- Further stimulus from the ECB (including a willingness to buy European corporate bonds) highlighted a strong month for international markets as central bank accommodations far outweighed underlying fundamental weaknesses. Commodity markets remain quite volatile, but with an upward bias for the month.
- In the US, manufacturing continues to exhibit weakness and retail sales stalled, but the continued strength of the labor market and nascent signs of inflation have solidified the efficacy of the first rate hike. With the Fed revising its forward guidance for interest rate increases down by 2 hikes for 2016, monetary policy should likely remain more accommodative than initially anticipated through 2016. 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 1.4%.

STRUCTURED MARKETS

- The tone in CMBS improved during the month of March along with other credit oriented sectors, particularly following the FOMC meeting on March 16th which was viewed as dovish and supportive of risk assets.
- New issue activity remains tepid with only two non-agency conduit deals pricing during the month. In fact, year-to-date supply is down approximately 40% versus the same period last year. The absence of new deals in the market coupled with reduced dealer inventories has created a positive technical environment for CMBS, which should keep spreads well bid.

CORPORATE CREDIT MARKET

- The Barclays US Corporate Index tightened 30 basis points (bps) through March, with higher beta sectors leading the charge (e.g. Energy and Communications at 99 bps and 38 bps respectively). The movement in spreads was largely driven by the European Central Bank's decision to buy certain investment grade corporate bonds in an effort to reduce borrowing costs within the region.
- Issuance picked up in March, with MTD volume at \$111B and YTD total of up to \$364B. In the near term, we expect issuance trends to continue given a mix of refinancing and M&A transactions (e.g. Sherwin-Williams/Valspar, Walgreens/Rite Aid, Pfizer/Allergan).

GOVERNMENT MARKET

- 2-yr yields decreased 5 bps while the 5-yr and 30-yr yields decreased about 1 bp each. 10-yr yields increased about 3 bps in March.

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SPREADS TO TREASURIES



BARCLAYS BENCHMARK DATA

	Total Return MTD
1-3 Gov/Credit	0.36%
Int. Gov/Credit	0.72%
Aggregate	0.92%
1-3 Yr US Treasury	0.17%
3-5 Yr US Treasury	0.30%
5-10 Yr US Treasury	0.09%
10-20 Yr US Treasury	0.18%
20+ Yr US Treasury	-0.02%

SECTOR DATA FROM BARCLAYS AGGREGATE

	Total Return MTD	Excess Return* MTD	Current YTM
Corporates	2.77%	2.71%	3.22%
Financials	1.72%	1.57%	2.94%
Industrials	3.49%	3.47%	3.34%
Utilities	1.26%	1.16%	3.43%
RMBS	0.30%	0.15%	2.35%
CMBS	1.25%	1.07%	2.44%
ABS	0.12%	-0.06%	1.55%
Agencies	0.67%	0.49%	1.66%

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