



MERGANSER
CAPITAL MANAGEMENT

THE MERGANSER FLASH

FIXED INCOME INSIGHTS

AS OF DECEMBER 31, 2016

Market Commentary

THE ECONOMY

- The Fed raised rates for the first (and only) time in 2016 by a unanimous decision while also increasing its projected number of rate increases next year from two to three. 3Q GDP was revised up to 3.5%, putting 2% growth for the full year in play, which combined with a continued rise in inflation expectations has maintained the risk asset rally. OPEC's production cut continued to boost oil prices as the market prices improved quota compliance. As we enter 2017, we expect market focus to shift from predicting potential policy to evaluating enacted policy and the international economic impacts.

STRUCTURED MARKETS

- As is typical for this time of the year, activity in the ABS market has ground to a halt with just \$6.5B of new deals pricing this month and low secondary trading volumes. YTD supply now stands at \$198B versus \$193B for the full year 2015, with the increase driven primarily by an uptick in the credit card segment.
- During the month, spreads have been stable and the ABS market responded favorably to the Fed rate hike and expectations of stronger growth stemming from a Trump presidency.

CORPORATE CREDIT MARKET

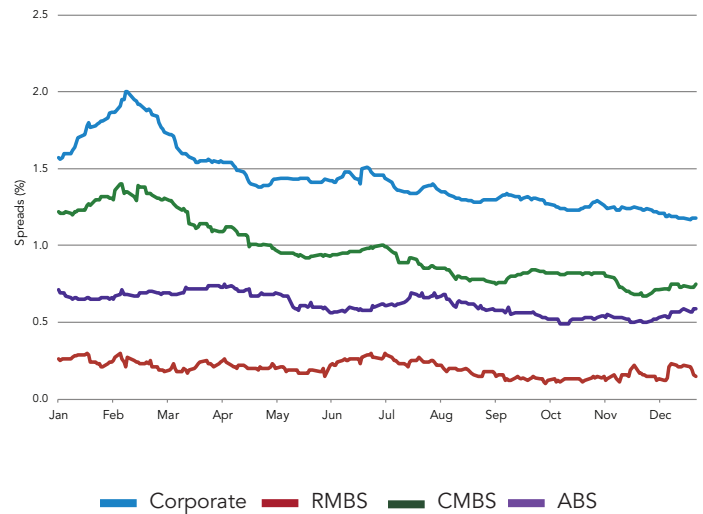
- The IG Corporate Index tightened 6 basis points (bps) in December as the Trump rally, slowdown in primary issuance and light dealer inventories provided yet another month of favorable technicals for corporate spreads. In addition, we are seeing heightened demand for floating rate notes as investors embrace future inflation expectations given the president-elect's untested growth policies.
- The primary market capped off a banner year in issuance (~\$1.3T or +2% YoY) with 2017 volume expected to decline on higher funding costs, slowdown in M&A activity and potential corporate tax reforms.

GOVERNMENT MARKET

- 2-yr and 5-yr yields increased by 4 bps and 3 bps respectively. On the longer end of the curve 10-yr yields stayed flat while 30-yr yields decreased by about 4 bps.

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SPREADS TO TREASURIES



BARCLAYS BENCHMARK DATA

	Total Return MTD
1-3 Gov/Credit	0.06%
Int. Gov/Credit	0.07%
Aggregate	0.14%
1-3 Yr US Treasury	0.03%
3-5 Yr US Treasury	-0.01%
5-10 Yr US Treasury	-0.12%
10-20 Yr US Treasury	-0.32%
20+ Yr US Treasury	-0.56%

SECTOR DATA FROM BARCLAYS AGGREGATE

	Total Return MTD	Excess Return* MTD	Current YTM
Corporates	0.67%	0.83%	3.35%
Financials	0.40%	0.50%	3.14%
Industrials	0.81%	1.00%	3.44%
Utilities	0.65%	0.90%	3.55%
RMBS	0.00%	0.07%	2.85%
CMBS	-0.41%	-0.32%	2.77%
ABS	-0.15%	-0.17%	1.85%
Agencies	0.23%	0.29%	2.15%

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