MERGANSER
CAPITAL MANAGEMENT

THE MERGANSER FLASH

FIXED INCOME INSIGHTS

AS OF JANUARY 31, 2017

Market Commentary

THE ECONOMY

- Economic news was relatively quiet to start the year as markets waited for the incoming administration to take control. Full year GDP growth for 2016 was 1.9% and inflation remains within striking distance of the Fed's targets, adding to the upward pressure on ultrashort interest rates. Market expectations are for the first rate hike in 2017 to occur at the June meeting. While energy prices remained largely range bound (outside of seasonal volatility in natural gas), both metals and agricultural commodities increased dramatically during the month due to stimulus from China and dollar weakness. We expect bouts of volatility as the new administration begins enacting policy changes.

STRUCTURED MARKETS

- While the private-label CMBS market has yet to find its footing, the Agency CMBS market is off to a strong start with Freddie Mac and Fannie Mae printing in excess of $4B YTD across six separate transactions.
- Given the supply imbalance and the narrowing of private-label spreads, longer duration Agency CMBS looks increasingly compelling.

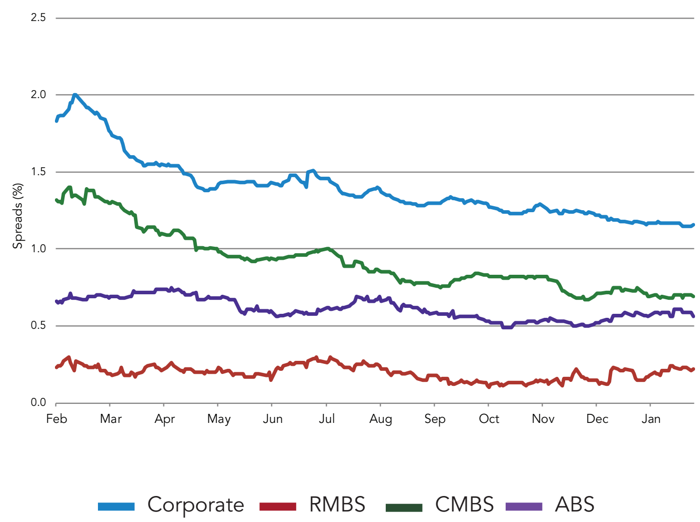
CORPORATE CREDIT MARKET

- The IG Corporate Index tightened 1 basis point (bp) to end at 121 bps in January as the Trump rally lost steam in the month. The market's ambivalence about the incoming administration caused spreads for Industrials, Financials and Utilities all to end roughly +/- 2 bps. Primary market was heavy at approximately $176B versus an initial street estimate of $110B. Financials accounted for a large portion of overall issuance as they exited the fourth quarter earnings blackout. Street expects another robust month for February ($100-110B) with M&A being the wild card.

GOVERNMENT MARKET

- Yields in January ended up relatively close to where they started at the beginning of the month. The 2-yr and 10-yr increased by about 2 bps and 1 bp respectively, while the 5-yr and 30-yr both decreased by about 1 bp.

SPREADS TO TREASURIES



BARCLAYS BENCHMARK DATA

	Total Return MTD
1-3 Gov/Credit	0.19%
Int. Gov/Credit	0.27%
Aggregate	0.20%
1-3 Yr US Treasury	0.13%
3-5 Yr US Treasury	0.25%
5-10 Yr US Treasury	0.22%
10-20 Yr US Treasury	0.29%
20+ Yr US Treasury	0.40%

SECTOR DATA FROM BARCLAYS AGGREGATE

	Total Return MTD	Excess Return* MTD	Current YTM
Corporates	0.31%	0.06%	3.34%
Financials	0.33%	0.11%	3.12%
Industrials	0.28%	0.03%	3.43%
Utilities	0.46%	0.18%	3.53%
RMBS	-0.03%	-0.24%	2.90%
CMBS	0.61%	0.37%	2.72%
ABS	0.22%	0.06%	1.83%
Agencies	0.31%	0.11%	2.16%

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