MERGANSER
CAPITAL MANAGEMENT

THE MERGANSER FLASH

FIXED INCOME INSIGHTS

AS OF MARCH 31, 2017

Market Commentary

THE ECONOMY

- The Fed increased the policy rate in March as economic data continues to support a gradual tightening of monetary policy. While retail sales data softened, inflation and employment remain at levels that satisfy the Fed. Current market expectations suggest the next rate hike will occur during the summer. Energy commodities have increased in volatility as the resurgence of non-OPEC supply has market participants questioning the resolve of OPEC members. After the pulled vote on AHCA, the market has begun to question the probability of significant changes coming from Washington, resulting in heightened market concern.

STRUCTURED MARKETS

- CMBS and structured products in general took the Fed rate hike in stride. Higher rates are a vote of confidence in continued job growth and economic expansion, which should benefit all sectors. CMBS demand remains strong, with improved credit quality from risk retention and a significant negative net supply technical still in place. Private label CMBS new issuance is down 22% versus last year.
- Negative headlines around big box retailers have accelerated, pressuring specific tranches of CMBX, but have not spilled over into cash bonds. News of a major retailer's 138 store closures was notable for its modest impact on CMBS, with only 11 CMBS assets immediately affected. We expect closings will continue over the coming years and CMBS will feel both direct and indirect impact over time.

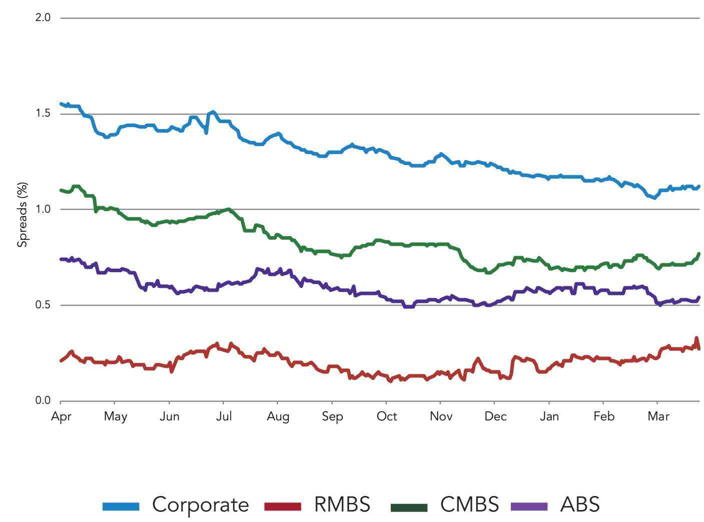
CORPORATE CREDIT MARKET

- The US Corporate Index widened 5 basis points (bps) in March to end at 118 bps. Despite a mid-month slowdown from winter storm Stella, a confluence of factors including the Fed rate hike, Brexit, lower oil prices and the administration's inability to push through the AHCA vote forced spreads to widen at the end of March.
- Primary market finished the month at $128B and capped off Q1 at an all-time high of $391B. Looking ahead, issuers' capacity to bring new deals may be dampened by the overall softer market tone.

GOVERNMENT MARKET

- The 2-yr, 5-yr and 10-yr yields each decreased about 1 bp for the month, while the yield on the 30-yr increased about 1 bp.

SPREADS TO TREASURIES



BARCLAYS BENCHMARK DATA

	Total Return MTD
1-3 Gov/Credit	0.05%
Int. Gov/Credit	0.05%
Aggregate	-0.05%
1-3 Yr US Treasury	0.04%
3-5 Yr US Treasury	0.07%
5-10 Yr US Treasury	0.03%
10-20 Yr US Treasury	-0.15%
20+ Yr US Treasury	-0.59%

SECTOR DATA FROM BARCLAYS AGGREGATE

	Total Return MTD	Excess Return* MTD	Current YTM
Corporates	-0.23%	-0.15%	3.33%
Financials	-0.08%	-0.05%	3.11%
Industrials	-0.27%	-0.17%	3.42%
Utilities	-0.58%	-0.40%	3.53%
RMBS	0.03%	0.04%	2.90%
CMBS	0.03%	-0.01%	2.79%
ABS	0.18%	0.17%	1.88%
Agencies	0.22%	0.22%	2.15%

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