



MERGANSER
CAPITAL MANAGEMENT

THE MERGANSER FLASH

FIXED INCOME INSIGHTS

AS OF OCTOBER 31, 2016

Market Commentary

THE ECONOMY

- Risk assets abroad recovered modestly while domestic assets were largely weaker as markets remain largely range bound in the face of increasing uncertainty. Inflation has begun to approach the levels telegraphed by the Fed as the prerequisite for a rate hike and employment remains firm. 3Q GDP was 2.9%, but after both 1Q and 2Q were below 1.5% it remains unlikely that full year GDP growth will be above 2%. While a pre-election hike in November remains a low probability, the likelihood of a rate hike in December continues to increase.

STRUCTURED MARKETS

- Notwithstanding a deluge of primary market activity in October (\$22B in new issue), ABS spreads held firm and in some cases tightened as investor appetite for high quality cash flows remains robust. Most benchmark deals from auto and credit card issuers have been upsized and priced at the tight-end of initial price talk, indicating demand is outstripping supply by a healthy margin.
- Looking ahead, the defensive nature of high quality ABS aligns well with investor concerns surrounding the pending election and a potential rate increase in December, which suggests we could continue to see outperformance due to the carry advantage and stable-to-tighter spreads.

CORPORATE CREDIT MARKET

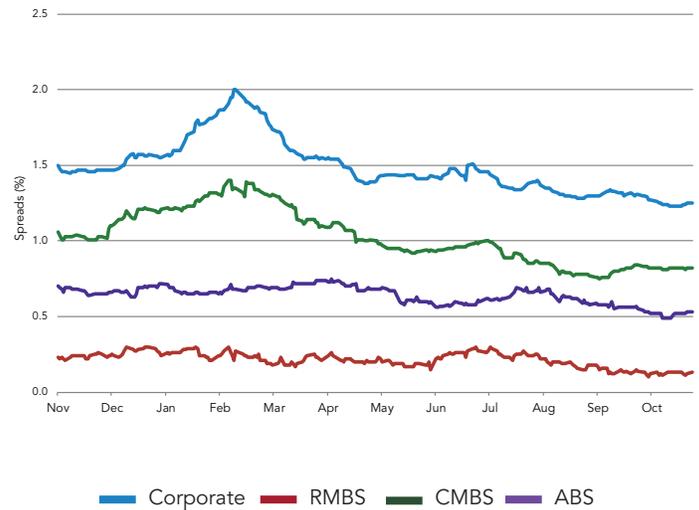
- The Barclays Corporate Index tightened 6 basis points (bps) in October, as spreads experienced a broad based recovery on better than expected 3Q earnings. The telecommunications sector was softer in the month due to a potential AT&T and Time Warner tie-up. This forced the market to evaluate a pending multi-tranche mega issuance and reassess the changing TMT landscape.
- MTD primary activity was roughly \$100B, but looking ahead, supply is expected to be robust given the spate of M&A related headlines.

GOVERNMENT MARKET

- Yields across the curve increased in October. The 2-yr, 5-yr, 10-yr and 30-yr have increased 8 bps, 16 bps, 24 bps and 28 bps respectively.

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SPREADS TO TREASURIES



BARCLAYS BENCHMARK DATA

	Total Return MTD
1-3 Gov/Credit	-0.04%
Int. Gov/Credit	-0.41%
Aggregate	-0.76%
1-3 Yr US Treasury	-0.07%
3-5 Yr US Treasury	-0.40%
5-10 Yr US Treasury	-1.11%
10-20 Yr US Treasury	-2.19%
20+ Yr US Treasury	-4.30%

SECTOR DATA FROM BARCLAYS AGGREGATE

	Total Return MTD	Excess Return* MTD	Current YTM
Corporates	-0.81%	0.57%	2.95%
Financials	-0.32%	0.64%	2.74%
Industrials	-1.01%	0.50%	3.04%
Utilities	-1.25%	0.74%	3.13%
RMBS	-0.26%	0.01%	2.27%
CMBS	-0.79%	0.05%	2.28%
ABS	-0.03%	0.10%	1.45%
Agencies	-0.47%	0.11%	1.73%

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