THE MERGANSER FLASH

FIXED INCOME INSIGHTS

As of December 31, 2021

MARKET COMMENTARY

Fixed Income Market Summary

Risk assets outperformed in the final month of 2021, but investment grade fixed income total returns were negative, with the Bloomberg Aggregate Index returning -0.26%. Treasury yields rose across maturities, in part pricing in future rate hikes, which are expected to occur in the new year following an accelerated taper. The curve has been flattening lately, settling in at a level that is close to the ten-year average (2s10s), but still well above the averages seen during periods of Fed tightening. Although new variants of COVID-19 threaten economic growth prospects, inflation remains a topic of concern and impetus for investors to seek higher yielding income opportunities. Overall, seasonal outflows from investment grade funds continued in December but reversed in the final week of the year.

Structured

Structured products generally benefitted from spread tightening and outperformed like-duration Treasuries in December. Mortgages were the top performing subsector, generating 21 bps of excess returns. The asset backed sector continues to perform well from a collateral standpoint and anticipated increased supply should be easily digested by strong investor demand. Spreads of traditional ABS sectors were flat to a few bps tighter. Within the benchmark, CMBS spreads tightened and outperformed (both agency and non-agency). Outside the benchmark, SASB spreads widened amidst record pace issuance, most severely impacting lower quality tranches. YTD, total non-Agency CMBS issuance totaled $155.6 bn and Agency CMBS totaled $199.8 bn. Non-agency new supply more than doubled the pace of 2020 ($63.9 bn) led by SASB deals which totaled $76.7 bn, up from $24.3 bn a year prior.

Corporate Credit

Investment grade corporate bonds outperformed like-duration Treasuries in the final month of 2021 with spreads tightening 7 bps on the whole. The corporate portion of the Bloomberg Aggregate Index was up by 60 bps. Industrials generated the strongest excess returns followed by financials and utilities. As expected, new issue activity experienced its seasonal swoon, but remained elevated versus a typical December ($60 bn). IG supply for the year was $1.475 trillion, ending 18% below 2020's record pace but up nearly a third from 2019 and marking the second largest annual volume ever.

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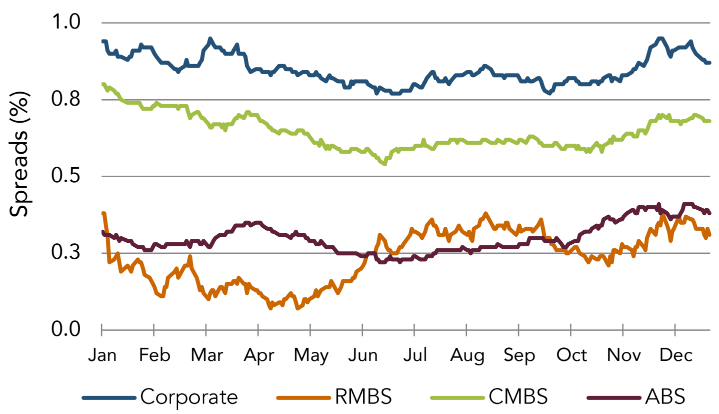
SPREADS TO TREASURIES



TREASURY YIELD CURVE CHANGES

	Current YTM	Change From Previous Month
3 Month	0.03%	-0.02%
1 Year	0.38%	+0.16%
2 Year	0.73%	+0.17%
3 Year	0.96%	+0.12%
5 Year	1.26%	+0.10%
10 Year	1.51%	+0.07%
30 Year	1.90%	+0.11%

BLOOMBERG AGGREGATE SECTOR DATA

	Total Return MTD	Excess Return* MTD	Current YTM
Corporates	-0.08%	0.60%	2.36%
Financials	0.00%	0.47%	2.10%
Industrials	-0.04%	0.72%	2.45%
Utilities	-0.70%	0.16%	2.65%
RMBS	-0.09%	0.21%	1.98%
CMBS	-0.16%	0.18%	1.88%
ABS	-0.16%	0.05%	1.10%
Agencies	-0.29%	0.02%	1.18%

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