Payden&Rygel Investment Management WEEKLY MARKET UPDATE

July 29, 2016

MARKET LEVELS

	Friday*	Last week	Dec. 31, 2015	One year ago
Dow Jones Industrial Avg	18,384	18,571	17,425	17,746
S&P 500	2,165	2,175	2,044	2,109
NASDAQ	5,150	5,100	5,007	5,129
Russell 2000	1,213	1,213	1,136	1,232
DJ STOXX Europe 600 (€)	340	340	366	396
Nikkei Index (¥)	16,569	16,627	19,034	20,523
MSCI EM Index	446	443	411	437
Fed Funds Target	0.25%-0.50%	0.25%-0.50%	0.25%-0.50%	0.00%-0.25%
2-Year Treasury Yield	0.68%	0.70%	1.05%	0.73%
10-Year Treasury Yield	1.48%	1.57%	2.27%	2.26%
U.S. $ / Euro	1.12	1.10	1.09	1.09
U.S. $ / British Pound	1.32	1.31	1.47	1.56
Yen / U.S. $	102.57	106.13	120.22	124.14
Gold ($/oz)	$1,346.67	$1,322.45	$1,061.42	$1,088.57
Oil	$41.03	$43.49	$37.04	$48.52

**Levels reported as of 7:33 a.m. PDT*

MARKET RETURNS

Year-to-date (12/31/15 – 07/29/16)*

Dow Jones Indus Avg.	7.10%
S&P 500	7.26%
NASDAQ	3.63%
Russell 2000	7.66%
MSCI World Index	2.69%
DJ STOXX Europe 600	-4.44%
MSCI EM Index	8.58%

Year-to-date (12/31/15 – 07/28/16)

90 Day T-Bill	0.18%
2-Year Treasury	1.15%
10-Year Treasury	7.91%
ML High Yield Index	12.05%
JPM EMBI Global Diversified	12.19%
JPM Global Hedged	7.18%

**Returns reported as of 7:33 a.m. PDT*

RECAP OF THE WEEK'S ECONOMIC RELEASES

Date	Report	Survey	Actual	Prior	Details
07/27	(UK) GDP YoY	2.10%	2.20%	2.00%	UK GDP came out stronger than expected in the quarter before the Brexit vote. Consensus is for a slowdown in the coming quarters.
07/29	(US) GDP Annualized QoQ	2.50%	1.20%	1.10%	US GDP came in weaker than expected but consumer spending made its largest contribution since Q4 2014.

ECONOMIC OVERVIEW

Gross domestic product (GDP) is a measure of output. Statisticians measure GDP indirectly as the sum of all the "spending" in the economy. But spending is not the same as output. Sometimes more is spent than produced, or vice versa. Statisticians adjust for this by measuring the change in inventories each quarter. Put simply, if a hat retailer sells hats off the shelves during the quarter, statisticians subtract the change in hat stockpiles from overall hat sales to get actual output. In Q2 2016, the change in inventories sliced 1.2 percentage points from growth. Further, inventories have detracted from US GDP for 5 consecutive quarters—the longest such streak in more than 20 years! As forecasters, how does the above picture change our outlook? We think the inventory drag will eventually fade and consumer spending, led by strong employment and rising wage growth, will endure, leading to better GDP growth figures ahead. We still expect 2% growth in the US this year.

US MARKETS:

TREASURIES

- Treasuries have traded in a tight, nine basis point range for the past two weeks on below average volumes and uninspiring flows. That was until the July FOMC on Wednesday where the Fed tried its best to keep the market's hopes for a rate hike this year alive. However, despite the positive outlook on the labor market, Treasuries rallied and the curve flattened.

- One hike for the remainder of the year is less likely than a coin flip as implied by the futures markets as traders wait for the July payrolls number next week and Chair Yellen's statements at the Jackson Hole conference at the end of August. The Bank of Japan underwhelmed the markets by leaving rates unchanged and not adding to their monetary base which left Treasuries under pressure moving in line with JGBs and the strength in Yen. This move proved short lived though as Q2 GDP surprised to the downside and month end extension trades dominated the market to end the finish the week. Crude oil also finished at the lowest levels in 5 months adding to the bid in nominal yields.

- Supply this week came in the form of new 2-year, 5-year and 7-year notes and the first two proved difficult given the proximity to the Fed statement. Both 2s and 5s came with sizable tails and poor demand statistics leaving dealers with having to sell post auction.

LARGE-CAP EQUITIES

- The U.S. Equity Market ended the week little changed as strong corporate earnings and mixed economic indicators weighed on market sentiment. Broad equities (S&P 500) fluctuated in a narrow price range for the second straight week amid low conviction and light seasonal trading volumes.

- The S&P 500 index was unchanged for the week, while the Dow Jones Industrial Average fell -0.7%. Helped by strong corporate earnings, the tech-focused NASDAQ Composite jumped +1.3% for the week. The higher beta small-cap stocks outperformed large-cap stocks. In terms of style, large-cap growth stocks outperformed large-cap value stocks. The best performing sectors were tech and health care, while the worst performing sectors were energy and consumer staples.

- Friday capped a busy week of earnings with nearly 40% of the S&P 500 companies reporting quarterly results in the past five trading sessions. 2nd quarter earnings continue to be better than expected with 8 out of every 10 companies beating consensus estimates. This week was headlined by bellwether tech firms such as Apple, Facebook, Alphabet and Amazon, which all posted strong quarterly results.

CORPORATE BONDS

- The last week of July was steady in the corporate market, with spreads changing little during the week. Primary issuance beat expectations with $24.5 billion new bonds versus $15-$20 billion. One of the biggest deals of the week was $6 billion issued by Verizon, spanning the maturity spectrum but concentrated on the intermediate and long end. Verizon is known for the largest issuance in investment grade corporate history, a $49 billion deal issued in 2013. All tranches priced 20-25 basis points inside of initial price talk, and were flat to slightly better on the break.

- In corporate news, the planned acquisition of SABMiller by AB InBev was altered since the British Pound tumbled after the vote in the UK. AB InBev increased the share price from £44 to £45, and is still working to reach an agreement. Earnings season continues to move forward with nearly half of companies in the S&P reporting as of Wednesday. Most companies reported better results than expected, but earnings expectations were cut back during the quarter. The Corporate Index Option-Adjusted Spread (OAS) finished the week at +144, one wider on the week. Overall metals/mining were three tighter and energy was eight wider. Senior were four tighter and subordinated financials were seven tighter. Industrials were one wider and utilities were one tighter.

MORTGAGE-BACKED SECURITIES

- The Agency mortgage market started the week a bit sluggish as originator mortgage supply depressed prices. Over the last portion of the week supply decreased and steady demand from overseas investors as well as domestic banks led to increased performance for Agency mortgages relative to Treasuries.

- Lower coupon mortgages, primarily FN/FH/GNMA 3.0's, led the way as higher coupon mortgages lagged. The GNMA market slightly outperformed, led again by the 3.0% coupon. Foreign demand for U.S mortgages continues, particularly from Japan, as they kick off the first month of their new year. Prepayment speeds come out next week with increased speeds expected due to the drop in mortgage rates and seasonal activity.

ASSET-BACKED SECURITIES

- It feels like Groundhog week. New issues are pre-marketed and the books are fully subscribed with barely enough time to do the due diligence credit research. Deals are officially announced with tighter price talk and taken subject soon after. Allocations are poor and prices are higher on the break. Repeat. This grab for yield is getting silly, but in a world of negative rates, we guess it all makes sense.

- We met with Fitch this week and fortunately or unfortunately there were few surprises consistent with the groundhog theme. Even the most uneventful meetings can unveil a few nuggets of insight that make them worthwhile. This time it was the Verizon deal. The Verizon presale report was the most downloaded report in history, by far. There were 12 countries represented. While there are no imminent deals, the conversations are beginning with the rating agencies, and we should expect the rest of the smartphone service providers to tap the ABS market in 2017.

MUNICIPAL BONDS

- The relatively lighter calendar was well received this week with most attention paid to a few larger deals that included $600 million from the Michigan Finance Authority on behalf of the city of Detroit. Municipal rates generally followed as Treasuries rallied on the week with the front end seeing the best performance. Municipal demand continued this week for its 43rd consecutive week of positive fund flows. We continue to see most demand focused in high yield and long-term funds and continued weakness in money market funds as we approach the reform deadline.

- The expected new issue calendar for next week is unseasonably heavy at $12.5 billion as we typically experience light issuance in the late summer months. The Bond Buyer 30 Day Visible Supply has also seen a sharp increase and is currently 51% above the YTD average. Heavier issuance will be welcomed by the market as we anticipate demand to remain healthy and could, at the very least, provide resistance to lower municipal rates.

HIGH-YIELD BONDS

- The BofA Merrill Lynch BB/B cash pay constrained index was down -0.32% this week as spreads widened by 14 basis points to an option-adjusted-spread of +437 basis points. The BofA Merrill Lynch BB/B index that excludes utilities and energy was down -0.14% for an OAS of +415 as the spread of that index widened by 10 basis points. The BofA Merrill Lynch Euro BB/B constrained index was up +0.12% as the spread of that index ticked wider by one basis point for an OAS of +380.

- High-yield was softer this week as the pace of inflows slowed and then turned negative as the market absorbed an active new issue calendar that was busy throughout the first part of the week. Energy credits underperformed as the price of oil traded down to levels not seen since early April. Metals and mining credits outperformed as earnings in some of the sector came in better than expectations. Bonds of high-yield hospital and health care facility operators traded lower as disappointing earnings from some of the issuers dragged the sector lower. One of the better performing credits of the week was the debt of Sprint Corp. as the company reported improved subscriber trends and bonds were higher by as much as four points early on the week, but faded from those highs later in the week as profit takers emerged.

- Net outflows for the week were $175 million as ETF's had an outflow of $512 million versus an inflow of $336 million for actively-managed mutual funds. This was the first negative flow in three weeks as a $332 million inflow was reported last week and a whopping $6.15 billion of inflows in the prior two week period. Secondary volumes were busier than normal as $14.2 billion traded on Tuesday versus a year-to-date average of $12.8 billion. The increase in secondary activity can in part be attributed to the increase in new issue activity this week.

- $6.05 billion across ten tranches priced this week. Some of the new issues struggled to move higher when freed to trade as aggressive pricing and upsizing weighed on performance in the secondary. One of the best performing new issue was a $750 million five-year senior unsecured note brought by Navient Corp. The student loan provider and servicer priced the Ba3/BB- rated notes at a spread of 549 basis points over treasuries to yield 6.625%. Order books for the new notes were multiple-times oversubscribed and allocations were severe. The new notes traded up two points when freed to trade and tightened by 47 basis points for a yield of 6.15%.

INTERNATIONAL MARKETS:

GLOBAL BONDS AND CURRENCIES

- Global markets started the week on a cautious note as investors anticipated the outcome of several important policy meetings. On Wednesday, the Federal Reserve released a statement outlining the "diminishing risks" to the US economy, opening the door for a potential rate hike before the end of the year.

- However, the lower than expected Q2 GDP growth data released on Friday largely offset the effect of the relatively hawkish message and boosted the demand for safe-haven assets. On Friday, the Bank of Japan underwhelmed the markets by modestly expanding its monetary stimulus program and electing to keep interest rates unchanged. The move weighed on risk appetite as many had expected more aggressive easing measures from the central bank.

- In Europe, global government bond markets moved largely in line with their US counterparts and benefitted from the risk-off tone that dominated this week. The yield on the 10-year German Bund dropped 8 basis points lower, while UK Gilts outperformed, with the yield on the 10-year Gilt falling by 12 basis points on the week. UK Gilts were supported by Monetary Policy Committee member Weale's comments suggesting an increased likelihood of an interest rate cut at Bank of England's policy meeting next week.

- In the currency markets, the US dollar lost some ground on the back of the lower than expected GDP growth numbers for Q2. The Japanese yen rose against most major currencies after the Bank of Japan's latest monetary policy move fell short of market expectations. The euro and sterling benefitted from the recent US dollar weakness and rose against the greenback.

EMERGING-MARKET BONDS

- Emerging market (EM) dollar-pay spreads widened by 10 basis points (bps) to 365 bps over US Treasuries, while local debt yields declined by 3 bps to 6.29%. EM currencies were mixed against the dollar with the South African rand (2.9%) and the Turkish lira (2.5%) exhibiting the strongest performance. The Colombian peso (-4.8%) and Russian ruble (-2.8%) underperformed.

- In monetary policy news, the Central Bank of Israel (BOI) maintained its reference rate at 0.1%, in line with expectations. The BOI has been on hold since February 2015. Similarly, the Hungarian central bank left its policy rate unchanged at 0.9%, marking its third month on hold. In its statement, it noted that while the activity was picking up, there was still slack in the economy and inflation was contained. The Russian central bank also left its reference rate steady as 10.5% following 50 bps of easing last month. In Sri Lanka, the central bank, under its new governor Indrajit Coomaraswamy, hiked rates by 50 bps. Its communiqué cited inflation concerns linked to supply side effects (weak monsoon and tax revisions) as well as aggregate demand pressures.

- In Saudi Arabia, Q1-16 growth printed an expansion of 1.5% y/y, with a pullback in government services weighing on activity. In Mexico, the preliminary estimate for second quarter GDP pointed to a deceleration in activity. While the economy expand by 2.4% y/y, it contracted on a sequential basis (quarter-on-quarter, seasonally adjusted) by 0.3%.

- In Indonesia, President Joko Widodo replaced his Finance Minister in the context of a cabinet reshuffle. Widodo tapped Sri Mulyani Indrawati as his new Finance Minister; she is a well-respected World Bank Managing Director who has served as Finance Minister previously. Separately, Egyptian authorities confirmed that the country is negotiating a $12 billion, three year loan with the IMF. The Egyptian government is reportedly looking to secure additional funding from other international organizations such as the World Bank and African Development Bank.

- Turning to ratings, Fitch put Colombia's 'BBB' sovereign rating on 'negative' outlook, citing a deterioration in the country's fiscal trajectory as well as an increase in the current account deficit. Fitch is the second rating agency, after S&P, to put Colombia's credit rating on 'negative' outlook.

HIGHLIGHTS OF NEXT WEEK'S ECONOMIC RELEASES

Date	Report	Consensus	Last
08/01	(US) Markit US Manufacturing PMI	52.9	52.9

	(US) ISM Manufacturing	53	53.2
	(US) ISM New Orders	--	57
08/02	(JN) Consumer Confidence Index	42	41.8
	(EC) PPI YoY	-3.40%	-3.90%
	(US) PCE Core YoY	1.60%	1.60%
	(CA) RBC Canadian Manufacturing PMI	--	51.8
	(US) Wards Total Vehicle Sales	17.05m	16.61m
08/03	(EC) Retail Sales YoY	1.80%	1.60%
	(US) ADP Employment Change	170k	172k
	(US) Markit US Composite PMI	--	51.5
	(US) ISM Non-Manf. Composite	56	56.5
08/04	(UK) Bank of England Bank Rate	0.25%	0.50%
	(US) Factory Orders Ex Trans	--	0.10%
	(US) Durable Goods Orders	-4.00%	-4.00%
	(JN) Real Cash Earnings YoY	--	0.20%
	(RU) CPI YoY	7.40%	7.50%
08/05	(CA) Unemployment Rate	6.90%	6.80%
	(US) Change in Nonfarm Payrolls	180k	287k
	(US) Unemployment Rate	4.80%	4.90%
	(US) Average Hourly Earnings YoY	2.60%	2.60%