Payden&Rygel
Investment Management

WEEKLY MARKET UPDATE

July 8, 2016

MARKET LEVELS

	Friday*	Last week	Dec. 31, 2015	One year ago
Dow Jones Industrial Avg	18,077	17,949	17,425	17,549
S&P 500	2,121	2,103	2,044	2,051
NASDAQ	4,941	4,863	5,007	4,922
Russell 2000	1,171	1,157	1,136	1,234
DJ STOXX Europe 600 (€)	327	332	366	381
Nikkei Index (¥)	15,107	15,682	19,034	19,856
MSCI EM Index	424	427	411	441
Fed Funds Target	0.25%-0.50%	0.25%-0.50%	0.25%-0.50%	0.00%-0.25%
2-Year Treasury Yield	0.63%	0.59%	1.05%	0.59%
10-Year Treasury Yield	1.39%	1.45%	2.27%	2.32%
U.S. $ / Euro	1.10	1.11	1.09	1.10
U.S. $ / British Pound	1.30	1.33	1.47	1.54
Yen / U.S. $	100.56	102.52	120.22	121.34
Gold ($/oz)	$1,355.29	$1,341.85	$1,061.42	$1,159.43
Oil	$45.52	$48.99	$37.04	$52.78

**Levels reported as of 8:06 a.m. PDT*

MARKET RETURNS

Year-to-date (12/31/15 – 07/08/16)*

Dow Jones Indus Avg.	5.25%
S&P 500	4.98%
NASDAQ	-0.59%
Russell 2000	3.97%
MSCI World Index	-1.13%
DJ STOXX Europe 600	-8.13%
MSCI EM Index	3.17%

**Returns reported as of 8:06 a.m. PDT*

Year-to-date (12/31/15 – 07/07/16)

90 Day T-Bill	0.17%
2-Year Treasury	1.34%
10-Year Treasury	9.04%
ML High Yield Index	10.21%
JPM EMBI Global Diversified	11.52%
JPM Global Hedged	7.56%

RECAP OF THE WEEK'S ECONOMIC RELEASES

Date	Report	Survey	Actual	Prior	Details
07/06	(US) ISM Non-Manf. Composite	53.3	56.5	52.9	After falling to its lowest level since February 2014 last month, ISM Services bounced back this month.
07/08	(CA) Unemployment Rate	7.00%	6.80%	6.90%	Canadian unemployment rate fell to levels last seen in July 2015.
	(US) Change in Nonfarm Payrolls	180k	287k	38k	Job growth in the US bounced back, further providing evidence that last month's low number was an aberration.

ECONOMIC OVERVIEW

Last month the key macro question was whether or not the +38k nonfarm payroll employment number for May signaled a more significant slowdown in the economy. At the time, our bias was skepticism toward the May jobs data, combined with a healthy recognition that the labor market is now tighter than at any time in the last decade.

Today's report (+287k for June, way above expectations) suggests the +38k (revised to +11k) told us little about the underlying economic trend. The economy is not adding jobs at a +287k monthly clip nor is it struggling along at +11k. The truth probably lies somewhere in between. The topic is an important one because it occupied the minds of policymakers at the June FOMC meeting. With Brexit lurking, the slump in payrolls perplexed policymakers. Minutes from the June meeting released this week showed that some policymakers "noted that the lower rate of payroll gains could instead be indicative of a broader slowdown in growth of economic activity". With the benefit of hindsight these fears may have been overdone. How much sway did such fears hold over the Committee? It's difficult to say. Based on the economic data, our bias is to keep at least 1 rate hike in our outlook for 2016. Maybe the FOMC finds a reason to delay until after the election, but how much longer can they drag this out if the data hold up?

US MARKETS:

TREASURIES

- The Treasury market tried its hardest to selloff to end the week after investment grade bond issuance and better than expected economic data pressured yields. However, the selloff was short lived. The global reach for yield was the theme this week as 20-year Japanese government bonds reached negative levels for the first time and the relentless bid for German bunds continued.

- The curve in the US moved 10 basis points flatter as the front-end simply runs out of room to move lower. Friday's payroll number beat estimates by over 100,000 and dealers did see two-way trading but the tug-o-war seemed to be won out by the buyers as most believe one payroll print doesn't negate Brexit, Italian banks, etc. That is what we heard from the June FOMC minutes out this week mentioning "uncertainty" 32 times and this was before the UK vote. Further demand for duration was seen in the June stripping data where outstanding STRIPS hit the highest level in 17-years. Long dated STRIPS have returned roughly 29% in 2016 compared to the broad Treasury index which is up only 6.5%. With defined benefit pension ratios falling back to all-time lows, one could expect this bid to continue.

LARGE-CAP EQUITIES

- The U.S. Equity Market rallied for the second consecutive week as a string of strong economic data releases boosted stock prices globally. The big bounce back in the U.S. jobs report and increased M&A activity were the main drivers of performance this week as broad equities (S&P 500) closed just shy of record highs.

- The S&P 500 and Dow Jones Industrial Average indices both ended the week up approximately 0.8%, while the tech-focused NASDAQ Composite jumped 1.5%. 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 consumer discretionary and health care, while the worst performing sectors were energy and utilities.

- In fund flow news, Lipper reported domestic equity mutual funds saw investors redeemed $4.4 billion for the week, which has been the trend since the start of the year. Domestic equity mutual fund managers have only seen one weekly inflow in the last six months. International equity mutual funds also saw redemptions with investors redeeming $1.6 billion for the week.

CORPORATE BONDS

- The first week of July was very quiet after the holiday, with few deals coming to market. Thursday was the exception as we saw nine issuers tap the market. For the week, there was $18 billion in new issue versus $15-$20 billion expected. National Australia Bank was the only issuer on Tuesday. The deal's four tranches totaled $4 billion and each priced about 15 basis points inside of initial price talk, with just 2.5x demand. All tightened slightly on the break.

- In corporate news, Brexit continues to impact markets with worries swirling around global growth. Credit spreads moved very little, so as rates plunged, so did corporate yields. The Italian banking system is now facing problems with non-performing loans, especially impacting Banca Monte dei Paschi di Siena, the third largest bank in the country. There is concern that there could be contagion to other European banks. The Corporate Index Option-Adjusted Spread (OAS) finished the week at +153, six tighter on the week. Overall metals/mining were twelve tighter; energy was nine tighter. Senior financials were six tighter and subordinated financials were seven tighter. Industrials were four tighter and utilities were flat.

MORTGAGE-BACKED SECURITIES

- Agency mortgages lagged US Treasuries as long-term rates drifted lower into unchartered territory. The fallout from Brexit has been a downgrade of global growth forecasts and dovish tendencies by central banks. Lower interest rates from this point is bad for the mortgage market as refinancing risk leads to price compression for the outstanding mortgage universe. Prepayment speeds were expected to be faster but now the concern is a major a refinance tsunami is on the horizon. Despite the sound of alarm bells, mortgage investors did enjoy higher prices as consolation. Within the market, conventionals trumped Ginnie Mae MBS. 15-year MBS put on a good performance versus 30-years on a hedged adjusted basis. Mortgage originations remain tame as borrowers focus on the July 4th holiday versus interest cost savings. That may change next week if the trend continues.

- For the week, the 30-year current coupon versus the 10-year US Treasury widened by four basis points to 88 basis points. According to Freddie Mac, the 30-year mortgage rate edged lower to 3.48%.

ASSET-BACKED SECURITIES

- The largest new issuance ABS week in 2016 was the week of February 22nd when 12 deals priced for $6.7 billion according to Bloomberg data. Next week is going to surpass it. There are currently 12 visible deals in their premarketing phase with another 6 deals that have filed 15Gs. With 15Gs filed, issuers have the option to bring deals if they choose to do so. With the exception of dealer floorplans, Nissan (already

premarketing) and Ally (15G filed), there is no collateral segment overlap, so the issuance could grow even more.

- The inaugural Verizon smartphone deal is now live. It will be a $1+ billion 144a private placement deal rated AAA by S&P and Fitch at the senior level. There will be two additional subordinate classes rated AA and A respectively. It will begin with a 2-year principal revolving period followed by a principal amortization period resulting in a 2.52 year, 3.22 and 3.25 year weighted average life. Initial price talk is Swaps +75/85 for the AAAs, and +15 basis points back for the AAs, and another +15 basis points back for the As.

MUNICIPAL BONDS

- Agency mortgages held in reasonably well despite record lows in intermediate and long-term US Treasuries. Pass-through spreads only widened modestly by one-to-three basis points for the production coupons. The lending community has not increased capacity to lower the primary rate to generate a refinance tsunami. They are focusing on margin over volume. At current rates, 80 percent of the mortgage market has an incentive to refinance but the benefit is less dramatic than previous refinance cycles. The June prepayment report was released today showing a modest pickup in prepayment experiences. Peak prepayment levels are not expected until the September report accounting for uptick in refinance volumes. Intra-market, Ginnie Maes lagged conventionals in the bond market rally and lower coupons outperformed higher coupons. Not a surprise.

- For the week, the 30-year current coupon versus the 10-year US Treasury held steady at 88 basis points. According to Freddie Mac, the 30-year mortgage rate edged lower to 3.41%.

HIGH-YIELD BONDS

- The BofA Merrill Lynch BB/B cash pay constrained index was up +0.55% this week as spreads tightened by nine basis points to an option-adjusted-spread of +481 basis points. The BofA Merrill Lynch BB/B index that excludes utilities and energy was up +0.51% for an OAS of +464 as the spread of that index tightened by 10 basis points. The BofA Merrill Lynch Euro BB/B constrained index was up +0.08% as the spread of that index ticked wider by two basis points for an OAS of +428.

- High-yield opened softer this week in a relatively quiet session on Tuesday as just $8.2 billion traded versus a year-to-date daily average of $12.8 billion. Wednesday's session started the day with a heavy tone as Brexit concerns continued and European stocks traded lower. This led to a weak opening for US stocks and other risk markets, but away from Yankee bonds with European exposure, US high-yield did not see much selling and quickly moved back to unchanged and then rallied higher along with equities. Levels for high-yield credits continued to move higher on Thursday, and Friday's stronger than expected nonfarm payrolls report boosted the market even further as investors struggled to find offerings on high-yield bonds as risk markets rallied strongly.

- Technical factors are still supportive for high yield as Thursday saw the first new issuance since June 20th and dealer inventories remain relatively low. Accounts are reported to have adequate cash to invest and are looking to add to desired credits on any weakness.

- Fund flows for high-yield mutual funds for the reporting week were a positive $1.8 billion with high-yield ETF's accounting for $1.6 billion of the total inflow. This breaks the streak of three consecutive weeks of outflows which totaled $4.2 billion Year-to-date fund flows total a positive $5.4 billion as compared a total inflow of $247 million at this time in 2015.

- The lone new issue this week and the first for July was a $1.25 billion senior unsecured note from Transocean Inc. with proceeds earmarked to redeem outstanding debt. The offshore drilling contractor reduced the size of the offering from the originally planned $1.5 billion issue size and widened final pricing to a 9% coupon with an original issue discount of 97.50 to yield 9.499%.The downsize and widening was

due to tepid demand for the fallen angel driller, and the new bonds were unchanged in the secondary market when freed to trade.

INTERNATIONAL MARKETS:

GLOBAL BONDS AND CURRENCIES

- The markets started the week on a cautions note as concerns about political instability in the UK, combined with lower liquidity due to the Independence Day holiday in the US, weighed on market sentiment. Core global government bond yields reached new lows, including the benchmark 10-year note in the US, which touched 1.357% for the first time. However, strong economic data from the US helped sentiment improve somewhat by the end of the week after a better than expected US jobs report on Friday eased some of the recent concerns about the health of the global economy.

- UK gilts outperformed their European and US counterparts, gaining support from the on-going post-"Brexit" uncertainty. Dovish comments by Bank of England's Governor Carney, a sharp decline in consumer sentiment and uncertainty about who the new leader of the ruling Conservative party will be, all boosted the demand for safe-haven assets. Risk appetite was additionally hurt by woes in the UK commercial real estate sector, which led to a number of large open-ended property funds halting redemptions. As a result, the yield on the 10-year UK Gilt dropped by 7 basis points by Friday. In Europe, concerns about the Italian banking sector supported German Bunds and the 10-year German bund yield finished the week 4 basis points lower.

- In the currency markets, the sterling continued to sell off, this time on the back of the UK commercial property sector volatility, in addition to the continuing "Brexit" turmoil. The US dollar rose against the euro, supported by strong US jobs numbers on Friday. However, the greenback weakened against the yen, which rose due to safe-haven buying throughout the week.

EMERGING-MARKET BONDS

- Emerging market (EM) dollar-pay spreads narrowed 7 basis points (bps) to 381 bps over US Treasuries, while local debt yields fell 3 bps to 6.3%. EM currencies were generally weaker against the US dollar, with the Brazilian real (-2.0%) and Mexican peso (-1.6%) registering the largest declines. The Argentine peso (+2.8%) and Peruvian sol (0.4%) were the strongest performers versus the dollar.

- June manufacturing PMI data were largely unchanged in Emerging Markets versus May, with the aggregate EM PMI at 49.3. Notably, PMI data in Brazil and Russia, which are in the midst of recession, registered healthy improvements. Brazilian and Russian manufacturing PMIs printed 43.2 (+1.6 pts m/m) and to 51.5 (1.9 pts m/m), respectively. In contrast, Turkey and Mexico were notable underperformers, falling to 47.4 (-2pts m/m) and 47.5 (-4.4 pts m/m), respectively.

- Costa Rican GDP picked up in Q1-16, printing a 4.8% y/y expansion; the manufacturing sector demonstrated solid momentum (+5.1% y/y) following a weak 2015. In the Dominican Republic, the economy grew by 6.1% y/y in the first quarter, a modest deceleration from the 7% y/y growth registered in Q4-15. In Senegal, GDP increased by 6.4%, with the tertiary sector (services) growing 7.8% y/y.

- Turning to monetary policy, the Polish central bank left its benchmark rate unchanged at 1.5%. The decision was in line with market expectations, with the new central bank governor, Adam Glapinski, highlighting authorities' focus on financial stability following the UK's EU referendum. In China, June reserves increased by a higher-than-expected $13.5 billion; FX reserves registered $3.2 trillion.

- In other news, the Sri Lankan Central Bank appointed a new Governor, Dr. Indrajit Coomaraswamy. The announcement was positive, with Dr. Coomaraswamy expected to exercise more independence than the former central bank governor. Brazil's economic team announced its fiscal target for 2017, an event that garnered interest in the context of the new administration's promised fiscal adjustment. Next year's primary

deficit is expected to register 2.1% of GDP a modest improvement from the 2.6% of GDP deficit expected in 2016.

HIGHLIGHTS OF NEXT WEEK'S ECONOMIC RELEASES

Date	Report	Consensus	Last
07/10	(JN) Money Stock M3 YoY	2.80%	2.80%
07/11	(CA) Housing Starts	189.0k	188.6k
07/12	(US) JOLTS Job Openings	--	5788
07/13	(JN) Industrial Production YoY	--	-0.10%
	(EC) Industrial Production WDA YoY	1.30%	2.00%
	(CA) Bank of Canada Rate Decision	0.50%	0.50%
07/14	(UK) Bank of England Bank Rate	0.25%	0.50%
	(CA) New Housing Price Index YoY	--	2.10%
	(US) PPI Final Demand MoM	0.30%	0.40%
07/15	(EC) CPI YoY	0.10%	0.10%
	(US) Retail Sales Advance MoM	0.10%	0.50%
	(US) CPI YoY	1.10%	1.00%
	(US) CPI Ex Food and Energy YoY	2.20%	2.20%
	(US) Real Avg Weekly Earnings YoY	--	1.10%
	(US) Industrial Production MoM	0.20%	-0.40%
	(US) U. of Mich. Sentiment	93.5	93.5
	(RU) Industrial Production YoY	0.80%	0.70%