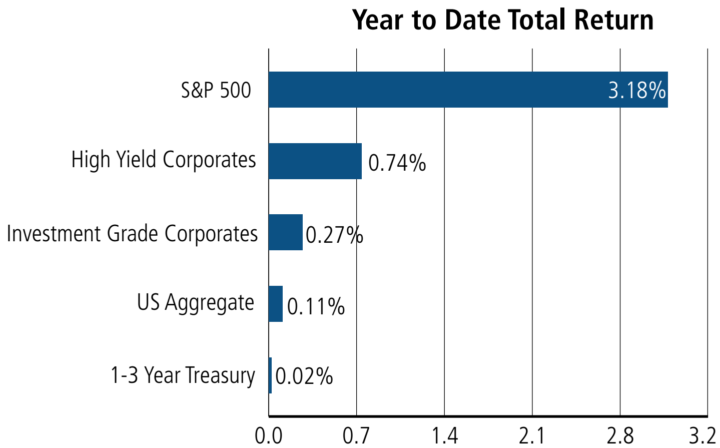
Week Ending **February 17, 2017**

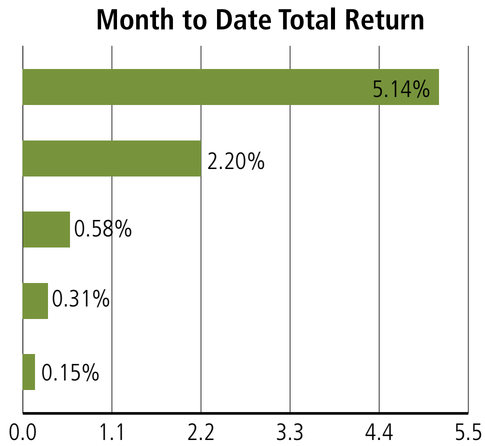
What A Difference A Year Makes!

Economic Overview:

What a difference a year makes! One year ago investors fretted over China's devaluation, global deflation and a U.S. recession. One Wall Street strategy team urged clients to "sell everything except high quality bonds. This is about return of capital, not return on capital." But, in fact, it was excellent return on capital that rewarded those able to see through the early 2016 fog. Oil prices are up nearly 40%, U.S. stocks soared nearly 30% and U.S. high yield corporate bonds have rallied more than 26% since the lows in February last year. This year, while many worry about European elections and elevated valuations, the economic fundamentals continue to impress. We don't think it is time to sell everything, yet.

Total Returns by Asset Class





Highlights of the Week:

- **Treasuries:** Treasuries absorbed stronger economic data and a more hawkish Yellen at the Humphrey-Hawkins testimony to finish the week 10-12 bps lower in yield. March rate hike probabilities popped from 35% Monday to 50% on Wednesday to end the week at 40%. A little over two hikes are priced in for 2017, and only two hikes are priced for 2018. European concerns and Trumponomics remain the focus with risk off the theme for the latter part of the week. Markets are still waiting with bated breath for Trump's "phenomenal" tax plan and whether or not it will include a border adjustment tax (BAT). Next week we have 2,5, and seven-year Treasury auctions with sizes unchanged.
- **Equities:** The U.S. Equity Market surged to new record highs this week on increased investor optimism surrounding the Trump administration's tax reform, improving economic data, and strong corporate earnings results. In M&A news, Kraft Heinz surprised market participants after it was reported that the food and beverage company offered to buy global giant Unilever in hopes to create one of the world's largest consumer-goods company. However, Unilever declined the offer on the premise that the proposed takeout price significantly undervalues the company.
- **Corporates:** The engine that is the primary corporate market continues to operate at full steam. The issuance was a mix of blue-chip industrials including Honda, Boeing, and Philip Morris, and in financials, we saw supply from Mitsubishi, JP Morgan, and Goldman Sachs. The market continues to await more news on the policy front from Washington eagerly, but in the interim sentiment remains positive. Highlighting this positive tone is the headline today that Kraft-Heinz is pursuing an acquisition of Unilever.
- **Securitized Products:** In the latest blow to marketplace lenders, Ellington Financial canceled a loan buying agreement with consumer finance company LoanDepot Inc. Also this week, On Deck Capital, arranger of small-business loans over the internet, tumbled after fourth-quarter losses widened and loss provisions rose more than anticipated. Not to be deterred, LendingClub said it plans to fund its loans via ABS. The Arcadia Receivables Credit Trust 2017-1 with LendingClub collateral is being marketed with Jefferies as the lead.
- **High Yield:** The maturity profile of the high yield debt market is a proxy for refinancing risk and represents an important measure of its underlying health. As companies have refinanced much of their debt over the past several years, only 14% of the market needs to be refinanced before 2020, so refinancing risk will remain low over the medium term.
- **Emerging Markets:** Ecuador is scheduled to hold presidential elections this weekend. The candidate from the incumbent's left-leaning Alianza Pais party, Lenin Moreno, retains a lead. However, with Moreno's momentum slowing, there are doubts about whether he will be able to win enough votes (40 percent of votes plus a 10 percentage point lead over his nearest competitor) to secure a first round victory.
- **Currencies:** The recently calm British pound declined by 0.5 per cent against the U.S. dollar after data released on Friday showed UK retail sales falling for the second consecutive month. Economists think that the plunge in the pound that followed the UK's decision to leave the EU has pushed up the cost of imports, lifting high street inflation and leaving shoppers balking at the higher prices. The unexpected slowdown in UK wage growth and the increasing likelihood of interest rate rises in the U.S. also weighed on the currency.
- **Municipals:** Municipals bonds are at the cheapest levels relative to taxable bonds since at least December, with ratios to taxable Treasury bonds making munis look more attractive. The 10-year and 30-year ratios are currently at 100% and 105%, respectively.