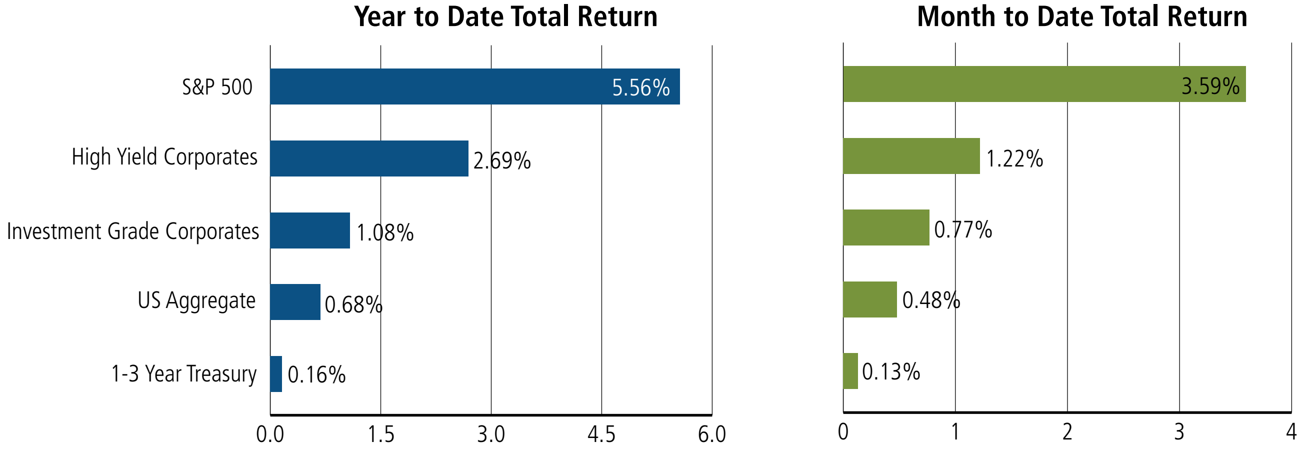
Week Ending **February 24, 2017**

Spread the Love for High Yield

Economic Overview:

After last week's chart showing the performance of different asset classes over the last year, some people wondered, are high yield spreads abnormally low? Well, it depends on how you define normal. We looked at 20 years of data on the high yield corporate bond market and here's what we found. Most often, spreads are between 400 and 500 basis points, and the events people worry most about (e.g. spreads at +800 basis points) are exceedingly rare. In fact, since 1997, high yield spreads have been above 800 basis points only 7% of all days.

Total Returns by Asset Class



Highlights of the Week:

- **Treasuries:** U.S. Treasury rates moved down 5-8 basis points across the curve as yields have again reached the lows for 2017. Markets were hopeful of a bit more direction from the Federal Reserve but received a bland directive of "many officials saw a chance of hike fairly soon if the economy remained on track" in the January FOMC meeting minutes released this week.
- **Equities:** The U.S. equity market climbed modestly higher in a holiday-shortened week. With the fourth quarter earnings season now behind us and a relatively light week of corporate headlines, investors' were squarely focused on the new Administration's corporate tax reform. Despite the lack of market catalysts, the Dow Jones Industrial Average index still managed to post new records highs. In fact, the world's oldest stock index posted ten consecutive record closes before snapping its streak on Friday.
- **Corporates:** The Royal Bank of Scotland was hit this week for the ninth year in a row with an annual loss totaling £7 billion. The losses were due to misconduct and restructuring charges. Still, the bank has a positive outlook for 2018 and is targeting a profit for the first time in a decade.
- **Securitized Products:** The annual Structured Finance Industry Group (SFIG) Vegas conference is set to kick off this Sunday at the Aria hotel with 7,000 registered attendees. The 4-day event brings together all parties involved in the securitization process including issuers, investors, rating agencies, lawyers, regulators, and more. Hot topics are anticipated to be marketplace lending, solar and of course, the new Administration and how it will affect the markets and regulations.
- **High Yield:** With over two-thirds of the loan index trading above par, issuers are taking advantage of strong demand for higher yielding paper by refinancing their bank debt. Although discount margins have declined as a result of the refinancing, leveraged loans continue to offer attractive yields given LIBOR rates that continue to climb above 100 basis points.
- **Emerging Markets:** The IMF announced a staff level agreement with Mongolia for a $440 million three-year Extended Fund Facility. The program is accompanied by an additional $5 billion in bilateral financing from China, Japan, and South Korea. The program mitigates concerns about upcoming bond maturities and Mongolia's low foreign exchange reserve levels.
- **Currencies:** The recent weakness of the U.S. dollar supported emerging market currencies across the board this week. One of the currencies that rose the most against the greenback was the South African rand. The currency reached an 18-month high against the U.S. dollar in response to Finance Minister Gordhan's latest budget speech. However, the rally proved to be short-lived and the rand dropped sharply on Friday after president Zuma said the government will allow the expropriation of land without compensation.
- **Municipals:** On the holiday-shortened week, new issue supply was very subdued, with around $4 billion of issuance. 30-day visible supply fell to $8 billion—the lowest level this year. This supply deficit should continue to provide support for the municipal market.