Week Ending **March 17, 2017**

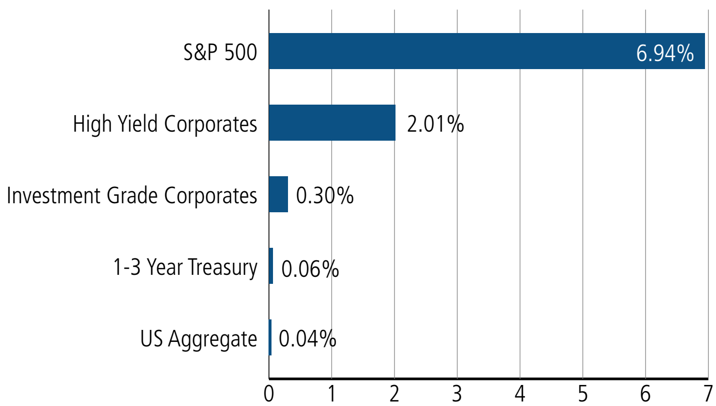
The Week of the Dovish Fed Hike

Economic Overview:

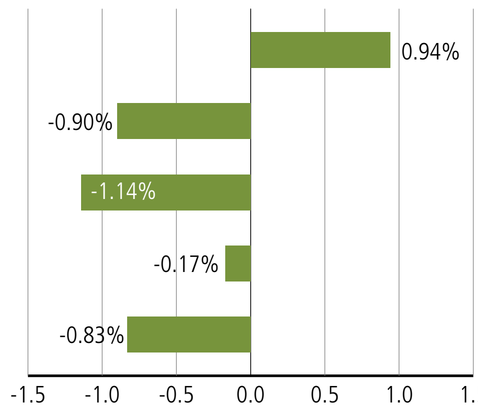
Data released this week from the U.S. Census Bureau showed construction of new single family homes proceeding at a pace not seen since 2007. No surprise then that home builders are reporting sentiment levels on par with 2005 (no, Donald Trump alone is not the reason for optimism). The remarkable endurance and health of the U.S. labor market, combined with the remarkable lack of single family home building in the past 10 years has pushed house prices back towards their pre-crisis peaks. Will higher mortgage rates crimp all the home buying activity? We doubt it. While Janet Yellen and the Washington Gang's rate hiking might slow refinancing activity, we think that U.S. households are in good enough financial shape to see through higher rates to the promised land of homeownership.

Total Returns by Asset Class

Year to Date Total Return



Month to Date Total Return



Highlights of the Week:

- **Treasuries:** The Fed delivered a "less hawkish" dot plot and economic projections, leaving traders with short belly and curve-flattener trades running for the hills to cover. The Fed's expected 2017 and 2018 rate hikes were left at 3 each with median rate projections unchanged and the terminal rate remaining at 3%. Five-year and 10-year yields fell by 10 bps each, steepening out the 5/30's curve.

- **Equities:** The world's largest chip company Intel Corp just got bigger as the company has agreed to acquire Mobileye, a global leader in autonomous car technology, for $15.3 billion in an all-cash offer. Intel is paying a 34% premium from Mobileye's prior day's closing price, which may be a reflection of the current bullish market sentiment. The U.S. broad equity market ended the week higher for the seventh time in the last eight weeks.

- **Corporates:** Oil has fallen 10% this month, so no one should be surprised that bonds in the energy sector have underperformed their peers. Energy bonds have moved nine basis points wider versus an average of two wider on the overall corporate index. That said, the sector outperformed strongly during 2016, especially given the broad assumption and hope that oil would stay above $50.

- **Securitized Products:** After a quiet start to the year, the commercial mortgage-backed securities market (CMBS) market revved up with over $5 billion in non-agency and agency deals in the marketing phase. Demand has been insatiable for top-tier assets in commercial real estate. This was confirmed by the strong demand for bonds on a $1 Billion trophy property in downtown Chicago, the Willis (Sears) Tower. The property, owned by Blackstone, commanded the tightest spreads for a single commercial mortgage-backed deal since 2013.

- **Emerging Markets:** Moody's changed Brazil's Ba2 sovereign outlook to 'stable' from 'negative.' In its statement, Moody's noted that the downside risks reflected in the 'negative' outlook had abated on signs of an economic recovery and better policy implementation.

- **Currencies:** The euro had another volatile session this week on the back of political developments in Europe. The worse than expected performance of the Eurosceptic VVD party in the Dutch elections made investors question the strength of populist movements in Europe and the euro rebounded. Yet, the "relief rally" quickly ran out of steam on Friday after the latest opinion polls in France indicated growing support for anti-EU presidential candidate Le Pen.

- **Municipals:** The municipal yield curve is near its steepest levels of the past year, characterized by a 215 basis point differential between 2-year and 30-year debt. Ratios to Treasuries are also near year-to-date highs, making municipals more attractive versus its taxable counterparts.