Payden&Rygel
Investment Management

WEEKLY MARKET UPDATE

September 9, 2016

MARKET LEVELS

	Friday*	Last week	Dec. 31, 2015	One year ago
Dow Jones Industrial Avg	18,289	18,492	17,425	16,330
S&P 500	2,155	2,180	2,044	1,952
NASDAQ	5,202	5,250	5,007	4,796
Russell 2000	1,239	1,252	1,136	1,153
DJ STOXX Europe 600 (€)	345	350	366	359
Nikkei Index (¥)	16,966	16,926	19,034	18,300
MSCI EM Index	467	458	411	410
Fed Funds Target	0.25%-0.50%	0.25%-0.50%	0.25%-0.50%	0.00%-0.25%
2-Year Treasury Yield	0.79%	0.79%	1.05%	0.74%
10-Year Treasury Yield	1.67%	1.60%	2.27%	2.22%
U.S. $ / Euro	1.12	1.12	1.09	1.13
U.S. $ / British Pound	1.33	1.33	1.47	1.54
Yen / U.S. $	102.69	103.92	120.22	120.62
Gold ($/oz)	$1,333.59	$1,325.07	$1,061.42	$1,110.75
Oil	$46.79	$44.44	$37.04	$45.92

**Levels reported as of 7:55 a.m. PDT*

MARKET RETURNS

Year-to-date (12/31/15 – 09/09/16) *

Dow Jones Indus Avg.	7.05%
S&P 500	7.07%
NASDAQ	4.87%
Russell 2000	10.19%
MSCI World Index	4.91%
DJ STOXX Europe 600	-2.67%
MSCI EM Index	13.61%

Year-to-date (12/31/15 – 09/08/16)

90 Day T-Bill	0.22%
2-Year Treasury	1.12%
10-Year Treasury	6.95%
ML High Yield Index	14.87%
JPM EMBI Global Diversified	13.37%
JPM Global Hedged	6.61%

**Returns reported as of 7:55 a.m. PDT*

RECAP OF THE WEEK'S ECONOMIC RELEASES

Date	Report	Survey	Actual	Prior	Details
09/06	(US) ISM Non-Manf. Composite	54.9	51.4	55.5	US ISM Services index fell to its lowest level since February 2010.
09/07	(US) JOLTS Job Openings	5630	5871	5624	Job openings in the US surged to their highest level on record.

ECONOMIC OVERVIEW

Data released by the Bureau of Labor Statistics this week indicated that job openings in the United States reached all-time highs just shy of 6 million. The number of new hires rose, too, at a slightly slower pace. Combined with yet another week of exceptionally low initial claims for unemployment insurance (the lowest as a share of the labor force in history at 0.17%), the US labor market remains healthy. No surprise then to see the non-voting, Boston Federal Reserve Bank President Eric Rosengren advocating for continued slow increases in the federal funds rate. The only missing piece, wage growth, has begun to perk up.

US MARKETS:

TREASURIES

- Treasuries were at the mercy of other developed bond curves as the European Central Bank left rates and quantitative easing language unchanged which kept duration under pressure. The market’s interpretation of this as “no change at all” and “QE forever not happening” caused government bonds to bear steepen taking Treasuries out of their well-defined and painful trading ranges.

- Adding to the pressure was a glut of corporate bond supply and anticipation of 10 and 30-year Treasury supply setup early next week. The Fed only had tier 2 speakers this week and the implied probability of a Fed rate hike in September was unchanged. The move came in 30-year bonds which sold off 20 basis points from the low yields of the week.

LARGE-CAP EQUITIES

- The U.S. Equity Market fell for the third time in four weeks as fears of rising interest rates globally drove a risk-off tone across capital markets. Market volatility picked up as the week wore on as broad equities (S&P 500) slid lower by more than -1.6% on Friday, which was the biggest one-day loss since Brexit.

- The S&P 500 ended the week down approximately -1.7%, also the worst week since late June. The Dow Jones Industrial Average declined -1.6% for the week, while the tech-focus NASDAQ Composite fell -1.8%. Large-cap stocks performed in with small-cap stocks. In terms of style, large-cap value stocks outperformed large-cap growth stocks. The best performing sectors were energy and utilities, while the worst performing sectors were materials and consumer staples.

CORPORATE BONDS

- September opened with a rush of issuance, posting $38 billion in just two days after the holiday weekend and $46 billion for the week. This was largely anticipated with the market expecting $35-$40 billion for the week, which is necessary given that September issuance will likely total $120-$130 billion. One noteworthy piece on Tuesday and Wednesday was that the issuance was not from any especially large deals, but from a wide range of issuers coming to the market simultaneously, 12 deals each day. Furthermore, there was an outsized amount of front end paper, and most all of it was rated single-A or better.

- Corporate news opened the week with some merger and acquisition activity, as Enbridge Inc. purchased Spectra Energy in a $28 billion transaction. The Corporate Index Option-Adjusted Spread (OAS) finished the week at +138, three wider on the week. Overall metals/mining were flat and energy was two wider. Senior financials were three wider and subordinated financials were four wider. Industrials were two wider and utilities were wider by two.

MORTGAGE-BACKED SECURITIES

- The summer doldrums are over. Agency mortgages outperformed US Treasuries as hawkish Fed speak lifted yields above the recent trading range. The move higher yield was welcomed by mortgage investors concerned about refinance risk. Pass-through spreads were modestly tighter by two-to-four basis points on the production coupons.

- Speaking of refinance risk, the release of the September prepayment report, representing the peak speeds for the cycle, came in faster-than-expected. Overall prepayment experiences were 30+% higher than the previous period but selected coupon and vintages were 50%+ faster. Adjustable rate mortgage speeds were also aggressive but not to the degree of fixed rate mortgages. Ginnie Mae mortgage refinance activity also posted elevated results due to robust Federal Housing and Veteran's administration loan application volume in May and June. As for performance, higher coupons bested lower coupons and conventionals outperformed Ginnie Mae mortgages. In commercial MBS, the new issue calendar picked up steam after a three-week hiatus. There are two conduit and two single borrower commercial MBS transactions in the marketing phase. Price talk is a tad wider than secondary pricing levels. As an example, the latest Wells Fargo 10-year AAA-rated class offering is talked at swaps plus 106 basis points versus the 10-year. Secondary bonds are trading two-to-four basis points inside of that.

- For the week, the 30-year current coupon versus the 10-year US Treasury narrowed by four basis points to 74 basis points. According to Freddie Mac, the 30-year mortgage rate held steady at 3.44%.

ASSET-BACKED SECURITIES

- Herd mentality. That describes the 17 ABS issuers that are going to hit the market next week, the week before the ABS East conference in Miami. Speaking of Miami, the Zika virus is exerting its influence as there are cancellations left and right. Post conference, expect ABS issuance to remain heavy until the holiday season is upon us. CLO issuance remains robust with a number of deals in the pipelines.

- The gravity defying Manheim Used Vehicle Index actually dipped a tenth this month to 126.9. Other than last month, there are only two data points in 2011 that registered higher. With the record numbers of off-lease vehicles hitting the used car market, one could logically conclude that used car prices should fall, but that logic has been flawed for a number of years now.

MUNICIPAL BONDS

- Municipal issuance was below trend again this week at just $5.3 billion as participants returned from Labor Day weekend. Fittingly, market activity has been driven by a disappointing nonfarm payrolls employment release on Friday. Coming off this backdrop, secondary trading in the municipal market has been relatively muted.

- After Treasury rates had slowly drifted higher over the past two weeks, as Fed speakers jawboned the increasing merit of another rate hike, the lackluster NFP print cooled expectations of a hike and Treasury yields across the curve sit near 2-week lows. Accordingly, while muni performance hasn't been robust, as ratios to Treasuries are towards the low end of the recent range, the market has remained firm. We expect the market's resilience could be tested next week, as the calendar for new supply has been steadily building and is now slated for as much as $14 billion, well above the $7.6 billion YTD weekly average.

- We teamed up with the corporate bond group on an interesting taxable muni issue this week (issued with a corporate cusip) – Morgan Stanley priced a 100-year California Institute of Technology (Caltech) deal at +205 to OLB. When the coupon was locked, final pricing metrics were 4.283's of 09/01/2116 at $100. The deal was very well received, with issue size of $150 million being three times oversubscribed.

- The selloff in the short end of the curve finally took pause, with MMD 3 years and in flat on the week. The weekly SIFMA floating index was adjusted higher again, but only by 1 basis point this week after two successive 7 basis point jumps the previous two weeks - the rate now stands at 0.64. However, the anomaly of tax-exempt short-term rates exceeding taxable counterparts persists - SIFMA now exceeds 1 week LIBOR by 20 basis points. The front end of the MMD municipal yield curve finally saw a meaningful revision last week, moving fixed rates in the 3 year range closer in line with SIFMA.

HIGH-YIELD BONDS

- The BofA Merrill Lynch BB/B cash pay constrained index was up +0.29% this week and spreads as spreads tightened by eight basis points for an option-adjusted-spread of +390 basis points. The BofA Merrill Lynch BB/B index that excludes utilities and energy was up +0.23% for an OAS of +373 as the spread of that index tightened by six basis points. The BofA Merrill Lynch Euro BB/B constrained index was up +0.28% as the spread of that index tightened by three basis points for an OAS of +337.

- The focus in the high-yield sector was new issue as almost $11 billion across fifteen tranches during the holiday shortened week. This follows zero issuance in high-yield since August 18th and the resultant pent up demand for new paper by investors allowed issuers to easily place the new debt.
- Order books were massively oversubscribed and allocations were severe as demand outpaced supply. The final pricing of the majority of the deals did not move that dramatically from initial price talk and allowed for strong price appreciation when the deals were freed to trade on Wednesday and Thursday.

- On Friday high-yield was softer as rates rose and spreads widened with most of the new issuance giving back some of the earlier gains as concerns that central banks may be turning more hawkish.

- Fund flows were positive for the week as an inflow of $610 million was reported for the weekly period that ended Wednesday. Flows appeared to turn negative on Friday however, as multiple bid-wanted-in-competition lists were sent out by high-yield ETF's which normally signals money leaving the asset class. Year-to-date flows into high-yield now stand at $10.2 billion versus an outflow of $7.1 billion year-to-date for 2015.

INTERNATIONAL MARKETS:

GLOBAL BONDS AND CURRENCIES

- The non-US government bond markets sold off this week as the European Central Bank (ECB) kept policy on hold at its early September meeting. There had been some expectation of a possible further reduction in European interest rates or an expansion of the ECB's quantitative easing program. The ECB's inaction encouraged the sense that we could be approaching an end to the trend of ever-lower official interest rates, given the increasing debate over their effectiveness.

- The UK Gilt market underperformed, as 10-year yields ended the week 13 basis points higher at 0.86%. A series of stronger than expected economic data recently has reflected a sharp recovery in consumer and business confidence following the steep decline in the immediate aftermath of the Brexit vote; this has called into question the view that the UK economy is likely to move into recession. European bond yields were also higher on the week; 10-year German government bond yields rose by 4 basis points, ending the week at zero, having been negative for some time. Italian and Spanish 10-year yields were up by 7 and 5 basis points respectively, thereby underperforming the German market by a small margin. Japanese bond yields have also been on a rising trend recently; they ended the week modestly higher although, in contrast to Germany, yields remained slightly negative. The rise in bond yields led to a sell-off in stock markets late in the week, while credit spreads also came under some pressure in light of the change in interest rate expectations.

- There was little movement in the currency markets, although the ECB's decision to keep rates on hold did help to support a small (0.5%) rally in the Euro versus the US dollar. Sterling slipped by 0.2% versus the dollar, while the yen recovered slightly following its recent weakness, ending the week 1.1% stronger versus the greenback. The Australian and Canadian dollars ended 0.2% and 0.4% weaker versus the US dollar respectively.

EMERGING-MARKET BONDS

- Emerging market (EM) dollar-pay spreads tightened 17 basis points (bps) to 325 bps over US Treasuries, while local debt yields fell by 14 bps to 6.14%. EM currencies were stronger against the US dollar, led by the Colombian peso (+4.6%), South African rand (+3.3%) and Russian ruble (+3.0%).

- The Mexican government announced that Secretary of Finance Luis Videgaray would be replaced by José Antonio Meade. The cabinet reshuffle came amid reports that Videgaray was responsible for encouraging President Peña Nieto's recent meeting with US presidential nominee Donald Trump, which was viewed unfavorably by Mexican citizens. Late in the week, Meade, a former finance secretary and respected technocrat, presided over Mexico's 2017 budget reading, which seeks to tighten the budget and deliver a primary surplus of 0.4% of GDP.

- Turkey's second quarter GDP growth figure came below consensus at 3.1% year-over-year (y/y). On a sequential basis, the softer print was due to weakness in private consumption, private investment and negative net exports. Second quarter growth in South Africa came at 3.3% on a seasonally adjusted annualized basis, moving up year-over-year growth to a still-weak 0.6%. The better than expected figure was driven by improvement in the mining and manufacturing sectors.

- China released data showing better trade figures and slower inflation in August. Exports registered a decline of 2.8% y/y, while imports increased by 1.5% y/y; both results were ahead of expectations. Consumer price inflation eased to 1.3% y/y from 1.8% y/y the prior month, driven by a softening in the food component; core inflation declined to 1.6% y/y, from 1.8% y/y.

- Central banks in Poland, Malaysia and Peru held rates steady at 1.5%, 3.0% and 4.25%, respectively. Polish officials stated that rate hikes were not anticipated until late 2017, as prices gradually move away from deflation back towards the 2.5% inflation target. Malaysian policymakers see contained price pressures and solid domestic demand, but maintained their concerns about global growth. In Peru, inflation expectations for 2016 recently fell back under the top end of the central bank's 1-3% inflation target band.

HIGHLIGHTS OF NEXT WEEK'S ECONOMIC RELEASES

Date	Report	Consensus	Last
09/13	(UK) CPI MoM	0.40%	-0.10%
	(UK) CPI YoY	0.70%	0.60%
	(UK) CPI Core YoY	1.40%	1.30%
	(UK) House Price Index YoY	--	8.70%
	(EC) Employment YoY	--	1.40%
	(GE) ZEW Survey Current Situation	56	57.6
	(US) NFIB Small Business Optimism	94.8	94.6
09/14	(JN) Industrial Production YoY	--	-3.80%
	(UK) ILO Unemployment Rate 3Mths	4.90%	4.90%
	(EC) Industrial Production WDA YoY	-0.80%	0.40%
09/15	(UK) Retail Sales Ex Auto Fuel MoM	-0.70%	1.50%

	(EC) CPI YoY	0.20%	--
	(UK) Bank of England Bank Rate	0.25%	0.25%
	(UK) BOE Asset Purchase Target	435b	435b
	(US) Retail Sales Advance MoM	-0.10%	0.00%
	(US) Initial Jobless Claims	265k	259k
	(US) Philadelphia Fed Business Outlook	1.3	2
	(US) PPI Final Demand MoM	0.10%	-0.40%
	(US) Industrial Production MoM	-0.20%	0.70%
	(RU) Industrial Production YoY	0.60%	-0.30%
09/16	(US) CPI YoY	1.00%	0.80%
	(US) CPI Ex Food and Energy YoY	2.20%	2.20%
	(US) Real Avg Weekly Earnings YoY	--	1.40%
	(US) U. of Mich. Sentiment	91	89.8