Payden&Rygel Investment Management WEEKLY MARKET UPDATE

September 16, 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 7:46 a.m. PDT*

MARKET RETURNS

Year-to-date (12/31/15 – 09/16/16)*

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 – 09/15/16)

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 7:46 a.m. PDT*

RECAP OF THE WEEK'S ECONOMIC RELEASES

Date	Report	Survey	Actual	Prior	Details
09/14	(UK) ILO Unemployment Rate 3Mths	4.90%	4.90%	4.90%	UK unemployment remained at its lowest levels since October 2005.
09/16	(US) CPI Ex Food and Energy YoY	2.20%	2.30%	2.20%	US core inflation accelerated with large increases in medical-care and medical drugs categories.

ECONOMIC OVERVIEW

There is nothing we like better than new information disrupting stale economic narratives. Since the end of the recession, perhaps no narrative has dominated quite like the "stagnant income growth" story. When we mention that 14 million jobs have been added since 2009, or that the unemployment rate is now back below its long run average of 5%, or that layoffs are lower today than in any previous economic cycle in the post-war era, our critics reply, "Sure, but incomes have been stagnant!" Perhaps this is changing. Data released this week by the Census Bureau showed that real (inflation-adjusted) median household income in America surged 5.2% in 2015—the largest single-year increase on record dating back to 1968. The naysayers will still assert that the surge marks just one year of gains and that real household incomes are still below their 2007 levels—and this is all true. But, we're moving in the right direction.

US MARKETS:

TREASURIES

- This week in treasuries was defined by a massive curve steepening move due to the Bank of Japan's talk of possible reverse twist and the European Central Bank's lack of any policy or rate change. The Bank of England did nothing as well on Thursday, as was anticipated, which added to the steepener moves.

- The flattening trade that has been in place for the last 4 months or so was quickly and severely unwound with 5/30's moving from a low of 102 basis points to as wide as 130 basis points as of yesterday. There is a bit of a breather today with some of it coming off resting around the 125 level. Brainerd's speech on Monday was anticipated to be the nail in the coffer for the last hawkish Fed speak before the FOMC but she remained true to her colors. Her speech on Monday was dovish and reversed out 50% of what was priced in for a September rate hike, moving from 40% as of last Friday to now just a 20% chance. December has always been on the table and still hovers around the 50% chance. Next week we have 2 major focuses with the BOJ meeting and the FOMC including updated dots.

LARGE-CAP EQUITIES

- Equity markets recovered some of the losses seen the prior week despite the rise in market volatility as the S&P 500 produced three days of moves greater than 1% this week. Trading volumes were higher than usual due to quadruple witching this Friday, the quarterly expiration of both options and futures on stocks and stock indices.

- For the week, the S&P 500 index gained +0.4%, while the Dow Jones Industrial Average was up +0.2%. Small-cap stocks underperformed large-cap stocks with the Russell 2000 index only up +0.3%. In terms of style, large-cap growth stocks outperformed large-cap value stocks. The best performing sector was information technology, which was up +2.9%, while the worst performing sector was energy, which was down -2.8% for the week. On the market close this Friday, the S&P 500 will implement its quarterly rebalancing, which will separate real estate investment trusts into its own sector for the first time in history. In M&A news, Bayer AG agreed to acquire Monsanto Co. for $66 billion to create the world's largest maker of seeds and pesticides for the agricultural industry.

CORPORATE BONDS

- September's issuance took a brief hiatus on Monday as the market swayed and issuers awaited a stronger tone. Tuesday was deemed worthy of issuance, with roughly $30 billion in just two days and nearly $35 billion for the week. This was in line with expectations of $30-$40 billion during the week. One notable deal was issued by Cisco on Tuesday, a five-tranche deal totaling $6.25 billion. The deal managed to price 15 basis points inside of initial price talk on just 2.3 times demand; bonds were unchanged on the break and currently 3-5 basis points tighter.

- In corporate news, multiple chemical companies have agreed to join forces in the past week—namely, Bayer is buying Monsanto and Agrium and Potash are merging. Given the influx of new issue, there was a lull in secondary trading which averaged less than in the summer months. Corporate Index Option-Adjusted Spread (OAS) finished the week at +140, three wider on the week. Overall metals/mining were five wider and energy was one wider. Senior and subordinated financials were each six wider. Industrials were three wider and utilities were wider by one.

MORTGAGE-BACKED SECURITIES

- Despite equity market volatility, Agency mortgages held steady versus US Treasuries. Economic reports were weak enough to provide support to the Fed relent camp. The increased chance of no rate hike at the next meeting helped rates and mortgage spreads stabilize after last week's volatility.

- Heavy mortgage originations were partially offset by the Fed reinvestment program and domestic bank buying. Money managers were also short covering recent mortgage basis short positions post the September prepayment report. Prepayments are expected to slow over the coming months as primary mortgage rates drift higher and seasonals turn favorable. Looking into the asset class, Ginnie Mae underperformed as Asian activity was muted. 15-year MBS bested 30-year with the recent yield curve steepening. In mortgage credit, credit risk transfer mortgage bonds richened from a favorable technical landscape. Not so for commercial mortgage bonds, as the supply spigot turned on after a three week hiatus. There has been a slew of non-agency and agency CMBS deals pressuring spreads a smidge wider (two-to-four basis points). As an example, the latest Wells Fargo 10-year AAA-rated class offering priced at swaps plus 108 basis points versus the 10-year.

- For the week, the 30-year current coupon versus the ten-year US Treasury narrowed by two basis points to 76 basis points. According to Freddie Mac, the 30-year mortgage rate rose to 3.50%.

ASSET-BACKED SECURITIES

- By the end of the day, this week's deal total will reach 20, the most since October 2014 when 15 ABS deals were completed according to data compiled by Bloomberg. With the ABS East conference looming next week, issuers collectively decided this is the time to hit the market. The strategy worked as deals cleared the marketplace in an orderly fashion. Post conference, we expect a steady stream of supply until the holiday season approaches.

- CLOs are the definition of grinding tighter. While overall spreads may seem tight, they are still lagging other sectors like SFR and CRT. Part of the reason may be attributable to premium prices and the option to call the deal by the equity holder. Like the underlying loans that have trouble trading much higher than $102 due to refinance risk, premium CLO classes are facing similar struggles.

MUNICIPAL BONDS

- The municipal issuance calendar was extremely heavy this week with close to $14 billion coming off of a light holiday shortened week last week. Heavy supply helped municipal rates keep pace with Treasuries and sent rates higher early in the week.

- This move proved timely as many investors used it as an opportunity to buy the dip at higher rates. Investor demand and cash levels proved to be exceptionally strong once again as most deals were heavily oversubscribed, despite the heavy total issuance. The calendar was headlined by a $1 billion deal from the New York Metropolitan Transportation Authority which issued its first bonds backed by real estate. The bonds are backed by revenues the agency receives by leasing land in the Hudson Yards area in Manhattan. Demand for the deal was heavy and the bonds repriced 7.5 basis points lower.

HIGH-YIELD BONDS

- The BofA Merrill Lynch BB/B cash pay constrained index was down -0.51% this week as spreads widened by 16 basis points for an option-adjusted-spread of +416 basis points. The BofA Merrill Lynch BB/B index that excludes utilities and energy was down -0.49% for an OAS of +399 as the spread of that index also widened by 16 basis points. The BofA Merrill Lynch Euro BB/B constrained index was down -0.73% as the spread of that index widened by 27 basis points for an OAS of +370.

- High-yield moved lower this week along with other risk markets and continued the selloff that began last Friday, with some relief seen on Monday and Thursday as stocks rallied. Concerns over rising rates and the future direction of stimulus by central banks along with softer oil prices caused investors to shed risk and position their portfolios more defensively.

- Fund flow activity confirmed this cautious bias as daily outflows have been reported since Thursday of last week. A total outflow of $2.45 billion left high-yield funds for the week with $2.1 billion of the outflows coming from high-yield ETF's while actively-managed funds had a milder outflow of $357 million. Last week saw an inflow of $610 million and year-to-date flows into high-yield now stand at $7.9 billion versus an outflow of $6.7 billion year-to-date for 2015.

- New issue was busy again this week after last week saw almost $11 billion across fifteen tranches priced. New issue volume this week was $9.15 billion across a dozen tranches. The majority of the new issues priced so far this month are still trading above new issue pricing despite the softer market conditions.

INTERNATIONAL MARKETS:

GLOBAL BONDS AND CURRENCIES

- Global bond markets had a relatively volatile week as investors continued to focus on the timing of the next US interest rate hike. Conflicting comments from various Federal Reserve officials pushed market sentiment in opposite directions during the week. By the end of the week, lower than expected retail and industrial numbers from the US, sliding oil prices and rumors of a potential interest rate cut in Japan all weighed on market sentiment and supported government bonds across the board.

- In Europe, the 10-year German bund yield finished the week 3 basis points lower after the European Central Bank made no changes to its monetary policy at their latest meeting. The Bank of England also left rates unchanged and, in the absence of any major economic reports this week, Gilts finished the week flat. Peripheral European bond yield spreads to German bunds on the other hand widened significantly, led by Portugal. Portuguese bonds sold off this week as market participants tried to predict the outcome of a ratings meeting on Friday.

- In the currency markets, after a volatile week, the US dollar finished on a stronger note against the euro and sterling. The Japanese yen rose against the US dollar, despite rumors that the Bank of Japan may cut interest rates at its next meeting. Sterling sold off against most major currencies as the Bank of England hinted at the possibility of another interest rate cut before the end of the year.

EMERGING-MARKET BONDS

- Emerging market (EM) dollar-pay spreads widened by 20 basis points (bps) to 344 bps over US Treasuries, while local debt yields increased by twelve bps to 6.26%. EM currencies were largely weaker against the dollar, with the Mexican peso declining 3.3% and the South Korean won down by 1.7%. The South African ran (+1.4%) and the Peruvian sol (+0.4%) outperformed on the week.

- In China, high frequency data in August were solid, with industrial production (+6.3% y/y), retail sales (+10.6% y/y), fixed investment (+5.7% y/y), and, most importantly, aggregate credit growth coming in stronger than expected. In Paraguay, economic activity accelerated in the second quarter. Real GDP increased by 6.2% y/y, with electricity and manufacturing being the largest contributors to the outturn. This marked an uptick from the 1.5% y/y expansion registered last quarter. In Panama, Q2-16 growth increased 5.2% y/y, an acceleration versus the 4.6% expansion in Q1-16. Drivers of growth included financial intermediation, construction, and mining activity.

- Turning to monetary policy, the central bank of Thailand left its policy rate unchanged at 1.5%, citing a gradual recovery in growth. The decision was largely expected, with the Bank of Thailand remaining on hold for the last eleven months. In Chile, the central bank also stood pat, leaving the policy rate at 3.5%, in line with expectations. In its statement, the board's tone was broadly neutral. The Russian central bank lowered its policy rate by 50 bps, to 10%, marking the monetary authority's second rate cut this year. In its statement, the board indicated that it was unlikely that there would be further easing in the remainder of the year. Last, in Ukraine, the central bank cut its policy rate by 50 bps to 15%.

- In ratings news, S&P downgraded Rwanda's credit rating from 'B+' to 'B', highlighting the sovereign's growing external vulnerabilities. S&P expects the Rwandan current account deficit to register 16% of GDP this year and the external debt burden to increase. Separately, the International Monetary Fund (IMF) approved a $1 billion disbursement for Ukraine under the country's $17.5 billion Extended Fund Facility (EFF) arrangement. The distribution comes after a one-year delay in IMF fund disbursements due to the country's challenging political backdrop.

HIGHLIGHTS OF NEXT WEEK'S ECONOMIC RELEASES

Date	Report	Consensus	Last
09/19	(US) NAHB Housing Market Index	60	60
09/20	(US) Housing Starts	1190k	1211k
	(US) Housing Starts MoM	-1.70%	2.10%
	(US) Building Permits	1162k	1152k
	(US) Building Permits MoM	1.60%	-0.10%
09/21	(US) FOMC Rate Decision (Upper Bound)	0.50%	0.50%
	(US) FOMC Rate Decision (Lower Bound)	0.25%	0.25%
09/22	(US) Initial Jobless Claims	260k	260k
	(EC) Consumer Confidence	-8.2	-8.5
	(US) Existing Home Sales	5.45m	5.39m
	(US) Existing Home Sales MoM	1.10%	-3.20%
	(US) Leading Index	0.00%	0.40%
09/23	(CA) Retail Sales MoM	0.20%	-0.10%
	(CA) Retail Sales Ex Auto MoM	0.50%	-0.80%
	(CA) CPI YoY	1.40%	1.30%

	(CA) CPI Core YoY	2.10%	2.10%
	(US) Markit US Manufacturing PMI	52	52