IR+M INCOME RESEARCH + MANAGEMENT

IR+M CLIENT UPDATE
March 2015

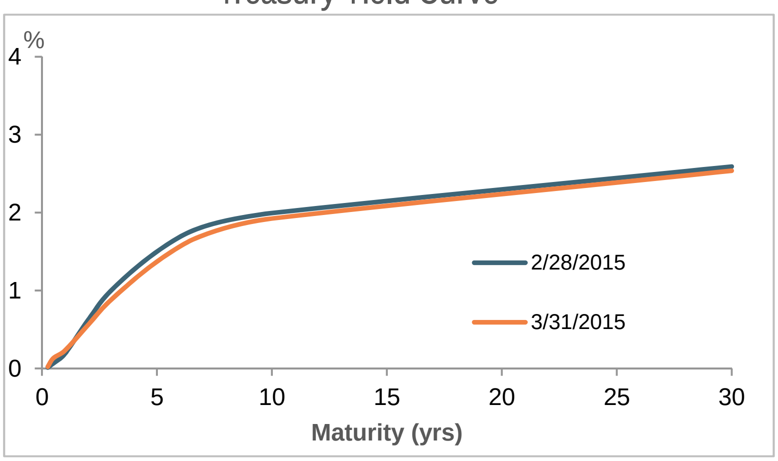
April 1, 2015

MARKET NEWS

- Intermediate Treasury yields staged a modest rally in March after the market pushed out expectations regarding when the Federal Reserve (Fed) will start raising benchmark interest rates
  - The 5-year Treasury rate, most sensitive to changes in monetary policy, fell 13bps to 1.37%[1]
- March's Federal Open Market Committee (FOMC) meeting was largely supportive of the bond market, despite dropping accommodative interest rate guidance from the statement
  - The FOMC reassured the market that future rate hikes will be gradual as the economy continues to heal
- February's employment report suggested that economic conditions have improved in the first quarter, surprising investors who anticipated growth to be mitigated by harsh winter weather
  - The economy added a better-than-anticipated 295,000 jobs as unemployment fell 0.2% to 5.5%[1]
- The continued recovery in the labor market drove improved consumer sentiment, as the US consumer confidence index climbed more-than-anticipated to 101.3 in March[1]
- An increase in merger and acquisition (M&A) activity drove robust corporate bond issuance in March – sales of investment-grade corporate bonds totaled over $134 billion during the month[2]
  - First quarter issuance reached over $320 billion, which is a 17% increase over last year's first quarter supply and the heaviest quarterly total in history
- Corporate bonds underperformed Treasuries amid the onslaught of supply and weakness in the equity markets, but wrapped up the quarter with solid absolute gains
  - Corporate bonds generated a first quarter total return of 2.32%, but trailed duration-matched Treasuries by 0.43% on the month[3]
- Agency MBS underperformed Treasuries modestly as low mortgage rates kept fears of increased prepayments alive
- Commercial mortgage-backed securities (CMBS) and asset-backed securities (ABS) outperformed Treasuries on account of low correlation to macro headwinds, favorable technicals, and improving fundamentals
- Increased refinancing activity drove heavy municipal issuance in the first quarter, as issuers took advantage of low interest rates to refund obligations – first quarter issuance totaled nearly $101 billion, a 59% increase over 2014[1]
  - Demand for tax-exempt debt remained strong – municipal bonds outpaced Treasuries during the month, as the 10-year municipal relative value ratio fell 3% to 103%

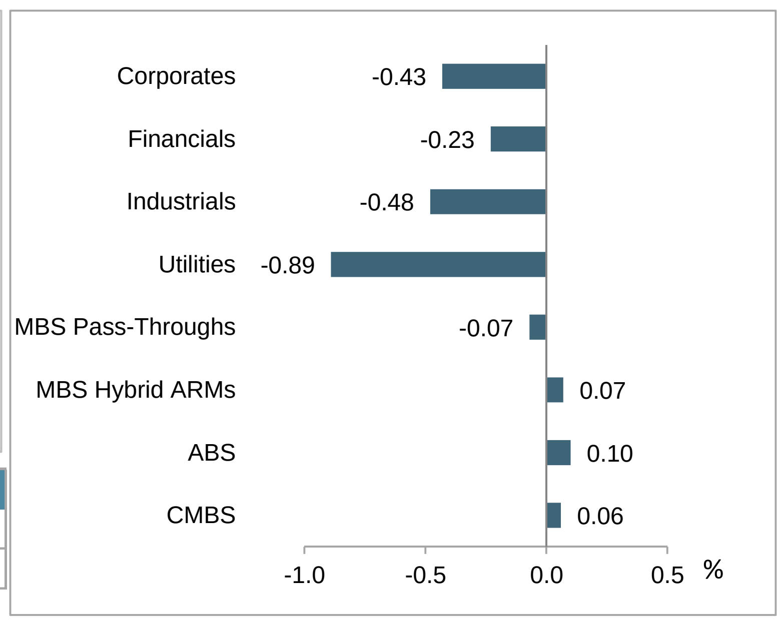
MARKET STATISTICS

Treasury Yield Curve[1]



Maturity	2-year	5-year	10-year	30-year
3/31/2015	0.56	1.37	1.92	2.54
MTD Change	-0.06	-0.13	-0.07	-0.05

March Excess Returns[2*]



As Of: 3/31/15. Sources: 1. Bloomberg 2. Citi 3. Barclays

*Excess returns are the curve-adjusted excess return of a given index relative to a term structure-matched position in Treasuries.