IR+M MARKET UPDATE
THIRD QUARTER REVIEW + OUTLOOK

October 14, 2016

INCOME RESEARCH + MANAGEMENT

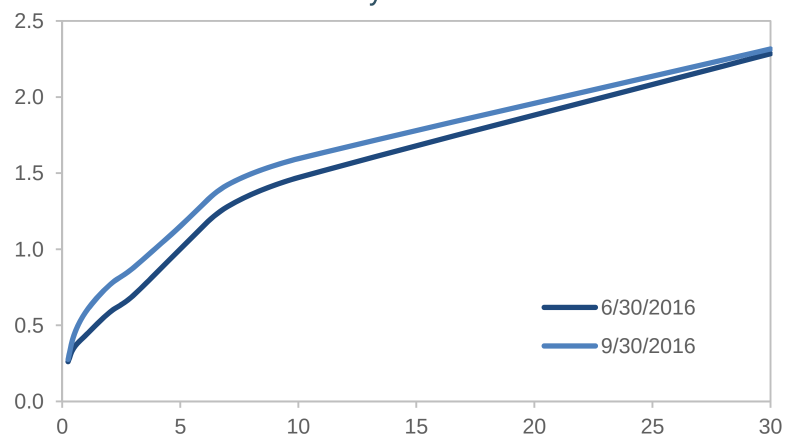
THIRD QUARTER RECAP

- Treasury rates rose across the curve during the quarter, particularly in short and intermediate maturities, as strong US data reignited expectations of a potential rate hike from the Federal Reserve (Fed)
    - The 5-year Treasury rate rose 15bps to 1.15%, while the 30-year rate increased just 3bps to 2.31%[1]
- US economic data displayed improving trends, with unemployment holding steady at 4.9%, while wages and inflation ticked up[1]
- In the corporate sector, investment-grade issuers priced over $320 billion in debt as companies attempted to fuel expansion through shareholder-friendly activity and M&A[1]
    - Strong demand for yield supported valuations, with corporate spreads tightening 18bps to 138bps
- The mortgage market benefited from a strong technical environment, as the Fed signaled that it would continue to reinvest paydowns from its mortgage portfolio
- Commercial mortgage- and asset-backed sectors outperformed Treasuries, as improvement in the housing and consumer markets attracted buyers seeking assets supported by high-quality collateral

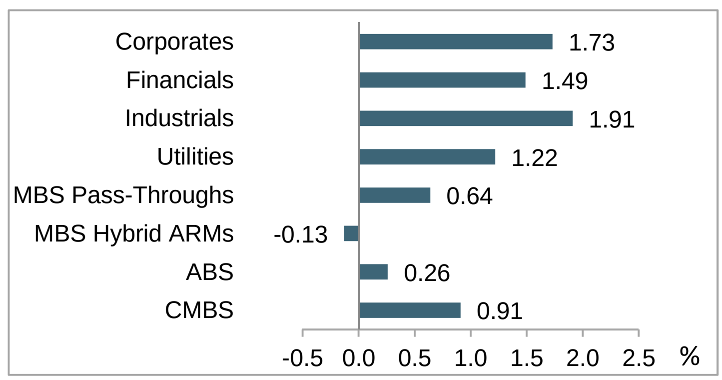
2016 GOING FORWARD

- As we enter the fourth quarter, improving economic data and more hawkish Fed messaging support the case for a rate hike before year-end
- Foreign monetary policy decisions may also be at the forefront, as global economic conditions and overseas demand continue to influence the US fixed income market
- In the corporate market, 2016 is set to be a record-breaking year for primary activity, with year-to-date supply quickly approaching the $1 trillion mark in October[1]
- As illustrated on the right, many corporate sectors are beginning to show late-cycle fundamental trends, which may negatively impact the market
- Securitized bonds will likely benefit from the strong housing market and a low correlation to corporates

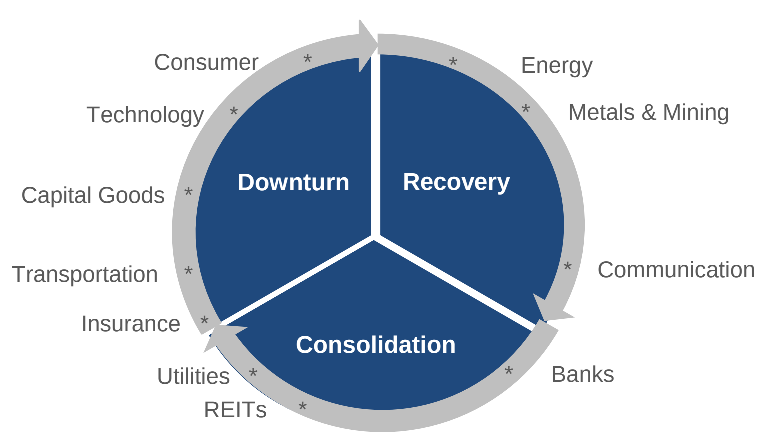
Treasury Yield Curve[1]



Third Quarter Excess Returns[1, 2]



Credit Market Conditions Varied by Sector[1]



Entering the fourth quarter, the upcoming elections coupled with hawkish Fed messaging may drive increased volatility in the US fixed income market. At IR+M, we believe bottom-up fundamental analysis and security selection can provide superior results during periods of uncertainty. We maintain a pragmatic overweight to spread product and believe high-quality income is important in the current low-rate environment.

As of: 9/30/16. Sources: 1. Bloomberg Barclays 2. Excess returns are the curve-adjusted excess return of a given index relative to a term structure-matched position in Treasuries.