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INCOME RESEARCH + MANAGEMENT

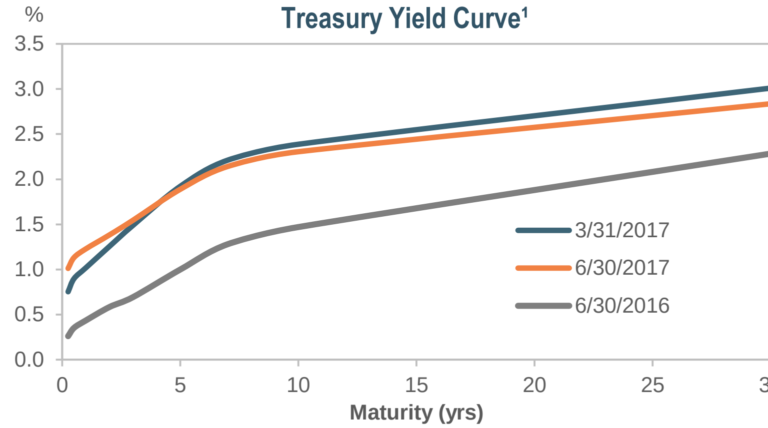
IR+M MARKET UPDATE
SECOND QUARTER REVIEW + OUTLOOK

July 17, 2017

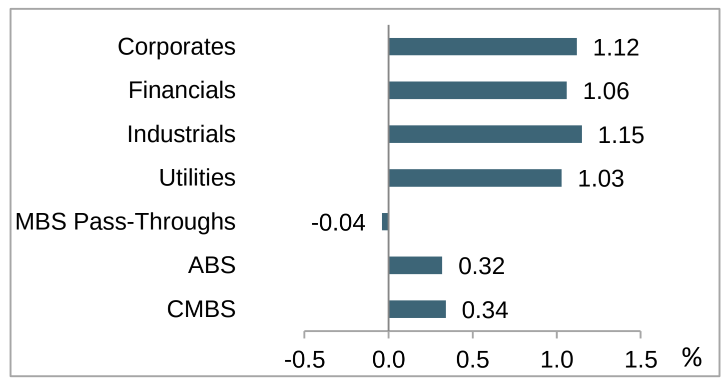
SECOND QUARTER RECAP

- The Federal Reserve (Fed) hiked rates in June, setting the federal funds rate target at 1.00-1.25%[1]
- The Treasury curve flattened over the quarter, as the short end reacted to monetary policy tightening, and the long end was affected by market unease and uninspiring economic data[1]
  - The spread between the 2-year and 30-year Treasury rates dropped 29bps to 146bps – the 5-year average is around 240bps
- Better than expected earnings helped performance in the corporate sector, as a majority of S&P 500 companies beat both top and bottom line estimates[1]
- Investment grade supply slowed while demand remained healthy, which supported spreads and drove a generally firm market tone [2]
- In the asset-backed securities (ABS) market, despite robust issuance, investors clamored for the high-quality spread product, driving up subscription levels and benefitting both primary and secondary spreads[1]
- Mortgage-backed securities (MBS) weakened modestly amid increased attention on the Fed's strategy for shrinking the balance sheet[1]

Treasury Yield Curve[1]



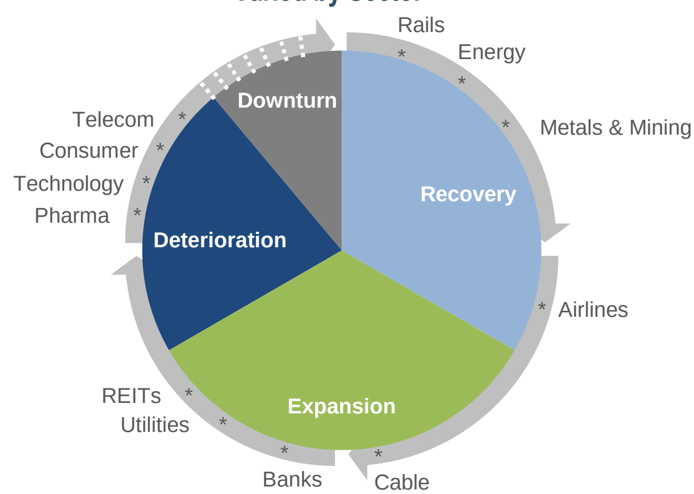
Second Quarter Excess Returns[3]



2017 GOING FORWARD

- The US economy has been improving, but at a slow pace, and many analysts anticipate that trend to continue[1]
- Corporate spreads have tightened and are trading at levels the market hasn't seen since 2014[1]
  - Technicals and overall liquidity remain healthy, while the fundamental picture is mixed
- Oil prices fell and are hovering around $45 per barrel – further weakness could introduce volatility[1]
- In the securitized market, the Fed outlined a plan to unwind its $4.5 trillion balance sheet later this year[1]
  - The plan calls for a gradual increase in the amount of securities maturing without reinvestment

Investment Grade Credit Market Conditions Varied by Sector[4]



Overall market volatility remains at historically low levels; however, geopolitical risks and elevated valuations across asset classes have introduced a sense of complacency among investors. At IR+M, we continued to trim risk, on the margin, through the first half of the year. Our recent bias for higher quality, more liquid securities has generated dry powder, which we're prepared to deploy should weakness materialize and offer attractive buying opportunities.

As of: 6/30/17. Sources: 1. Bloomberg 2. Citigroup 3. Bloomberg Barclays. 4. IR+M. Excess returns are the curve-adjusted excess return of a given index relative to a term structure-matched position in Treasuries. The views contained in this report are those of IR+M and are based on information obtained by IR+M from sources that are believed to be reliable. This report is for informational purposes only and is not intended to provide specific advice, recommendations for, or projected returns of any particular IR+M product.

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