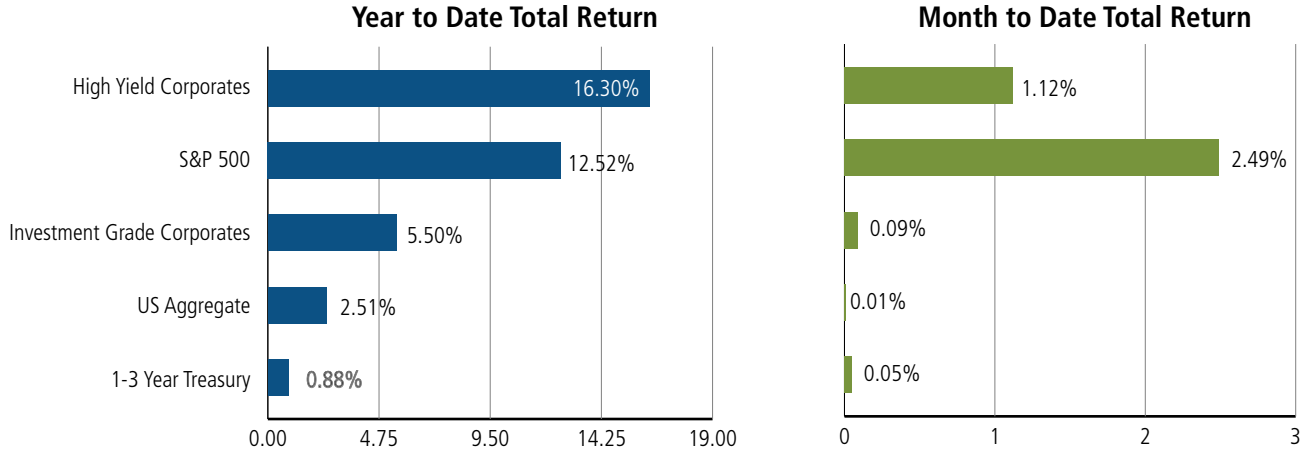
Week Ending **December 9, 2016**

America Is Open for Business

Economic Overview:

Global investors, dodging the slings and arrows of central bank policies (negative rates and QE), have increasingly turned to America's corporate bond market for liquidity and yield. Data released this week showed the "rest of the world's" holdings of corporate bonds soared to over 3.5 trillion in the third quarter of 2016. With the rest of the world also joining Payden in our optimism for US economic growth and the European Central Bank set to hoard euro area bonds for another year at least, the US corporate bond market should remain an attractive home for investors around the world.

Total Returns by Asset Class



Highlights of the Week:

- **Treasuries:** The ECB surprised markets with a "NO TAPER" reverse operation twist (aka BOJ curve control- like) with tapering long end purchases from €80bln to €60bln and lowering low duration purchase limits from 2 yrs to 1yr. The German 5/30's yield curve steepened 20 bps from 135 to 155 bps while the US 5/30's curve steepened 6 bps to 129bps. Next week we have the December FOMC on Wednesday with almost 100% priced in for a 25 bps rate hike.
- **Equities:** After six consecutive days of market gains and three record closes, the US equity market has continued to surge higher post-election. During that stretch, the financial sector has seen some of the biggest gains. Financials, the S&P 500's second largest sector, has rallied over 17%.
- **Corporates:** The banking sector has been fraught with worry this year, and none more than in Italy, which carries nearly €450 million in estimated bad loans. Now Monte dei Paschi di Siena, the world's oldest bank, is facing trouble after the European Central Bank refused to give them more time to seek out private funding. They are hoping the Italian government will step in as a last resort.
- **Securitized Product:** A few hundred people gathered at an annual CLO conference this week and $80 billion in CLOs (Collateralized Loan Obligations) have been issued year-to-date. Sentiment at the conference was that the credit cycle is in its later innings, although the senior CLO class still offers good relative value. Supply/demand dynamics strongly support US CLOs, but one drawback may be the strengthening USD. The first annual Marketplace Lending Conference, a high growth sector, was running concurrently. SoFi, a larger marketplace lender, announced their first Prime Jumbo RMBS deal this week.
- **High Yield:** This past week's inflow into floating-rate loan funds was the fourth largest ever as rising rates and risk-on sentiment drove demand for the asset class. However, despite these recent inflows, AUM for floating rate loan funds remains 26% below its 2013 peak, which suggests that demand for loans could continue to increase.
- **Emerging Markets:** Against expectations of a 25 bps cut, the Reserve Bank of India (RBI) chose to hold the benchmark reverse repo rate steady at 5.75%. Lower inflation and the hit to economic activity from the government's currency swapping exercise had prompted analysts to call for a continuation of the easing cycle. However, the RBI chose to take a more cautious approach, and it views any near-term economic slowdown as temporary.
- **Currencies:** The euro hit the headlines this week. First, there was the Italian referendum "no" vote, which led to some short-term volatility, followed by the victory of the center-left candidate in the Austrian presidential election. The latter boosted positive sentiment and helped the euro recoup the previous losses. However, euro strength proved short-lived as the markets chose to focus on the ECB's decision on Thursday to scale back the asset purchasing program next year. As a result, the euro was the worst performing major currency this week.
- **Municipals:** Municipals reversed course this week outperforming Treasuries as yields fell and Municipal/Treasury ratios declined; a possible reason being that Vice-President-elect Pence indicated during the week that tax reform might be delayed beyond the Administration's first 100 days in office.