Bond Market Watch
June 30, 2016

The second quarter continued to see a tightening credit spread environment, which started in late February and has lasted into June. The securitized credit sector and commodity-related sectors including energy, basics, metals and mining posted the strongest performance after being the worst performers in the first month of the year. Financial credit has lagged alongside bank stocks and a flatter yield curve than many bank analysts had anticipated at the start of the year. Corporate credit has tightened through spread levels seen at the start of the year after widening in the first month and a half. The credit markets have largely shrugged off exogenous macroeconomic shocks such as the Brexit, record low global bond yields, and a tepid global growth forecast. West Texas Intermediate crude oil price had plunged all the way to $26.21 per barrel on February 11, 2016 and has recovered since then to trade at $48.33 as of end of June 2016. Copper, also recovered from its all-time low in January at $1.95 per pound and ended the Q2 2016 at $2.19/lb. Despite the volatility in the credit markets, year-to-date issuance in the investment-grade corporate debt market is reminiscent to what we saw in 2015 (2015 issuance of $1.28 trillion). 2016 YTD issuance was ~$712 billion. The yield on 30-year Treasury was 2.28% at the end of June as compared to the 2015-year end yield of 3.01%. The 10-year Treasury yielded 2.26% at the end of 2015 and decreased to 1.47% in June of 2016. As we write this, the yield on the 30-year Treasury is at 2.18% and the yield on the 10-year is 1.46% after posting intraday lows of 1.32% in early July. The Fed has largely remained dovish in the face of so much global macroeconomic uncertainty. Competing global bond yields such as German bunds and Japanese JGB's have kept a bid for the longer date US rate market.

Within high-grade fixed income, credit spreads in the Barclays Aggregate Index widened to 200 bps in February from 155 bps at the end of 2015. By the end of June, spreads tightened back to 147 bps retracing all of their widening. Spreads ended 2011 at 217 bps, 2012 at 131 bps, 2013 at 111bps, and widened to 125 bps at 2014 before widening further in 2015. The year-to-date excess return for the Barclays Credit Index was positive 119 bps along with longer duration credit outperforming duration neutral treasuries by 192 bps.

By the end of 2015, corporate spreads had widened to 165 bps from cyclical lows of 99 bps in June 2014 and tightened by 12 bps to 156 bps towards the end of June 2016. The Barclays Corporate IG Index produced a positive 357 bps return for the quarter and positive 120 bps excess return over duration neutral Treasuries year-to-date. At the sector level, spreads on Industrial credit tightened by 9 bps to 159 bps, from 168 bps off Treasuries at the Q1 2016. Year-to-date, the sector produced a positive 203 bps of excess return. Spreads on financial credit tightened by 3 bps to 152 bps from the previous quarter end, and the sector produced a negative 49 bps of excess return YTD. Utilities also saw spreads tighten by 9 bps to 142 bps from 151 bps in March and posted positive 128 bps of excess return YTD.

The agency MBS sector ended first quarter widened by 5bps at 29 bps from 24 bps at Q1 2016. Year-to-date the sector delivered a negative 39 bps of excess return. On the other hand, ABS spreads tightened by 13 bps from 74 bps in March to 61 bps, and the sector produced a positive 66 bps of excess return. CMBS spreads tightened from 121 bps in 2015 to 98 bps at quarter-end. The sector produced a positive 97 bps of excess return. CMBS AAA new issue spreads have rallied substantially. Although recent CMBS 2.0 subordinates have tightened as well lately, they have still lagged other investment grade sectors. The Barclays Aggregate Index posted a positive 2.21% total return for the Q2 2016.

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Yield and Total Returns									
Ryan Labs Indexes	**YTW**	**QTD**	**YTD**	**12M[1]**	**Ryan Labs Indexes**	**YTW**	**QTD**	**YTD**	**12M[1]**
RL 2 Year Indexes					RL 10 Year Indexes				
TIPS	-0.74	0.81	2.73	1.34	TIPS	0.13	1.86	7.37	4.91
Treasury *(OTR)*	0.59	0.51	1.33	0.99	Treasury *(OTR)*	1.49	2.97	7.97	8.93
Financials	1.73	1.13	2.45	2.98	Financials	3.43	3.64	7.17	9.86
Industrials	1.56	1.26	2.98	3.10	Industrials	3.24	5.06	11.10	11.97
Utilities	1.79	1.72	3.28	2.84	Utilities	3.33	5.00	11.13	10.32
AAA Corporate	0.91	0.62	2.09	2.40	AAA Corporate	2.45	3.35	8.27	11.22
AA Corporate	1.19	0.74	2.25	2.73	AA Corporate	2.63	3.19	8.25	11.23
A Corporate	1.46	1.06	2.60	2.98	A Corporate	2.85	4.27	10.07	12.70
BBB Corporate	2.09	1.76	3.31	2.83	BBB Corporate	3.90	5.21	10.06	9.27
RL 5 Year Indexes					RL 30 Year Indexes				
TIPS	-0.34	1.30	5.25	3.39	TIPS	0.73	4.10	14.10	9.88
Treasury *(OTR)*	1.01	1.35	4.35	4.26	Treasury *(OTR)*	2.31	7.25	16.93	19.63
Financials	2.42	2.04	4.93	6.42	Financials	4.25	5.27	9.92	14.15
Industrials	2.32	2.25	6.03	6.65	Industrials	4.18	6.84	15.36	15.84
Utilities	2.59	3.69	7.69	6.73	Utilities	3.99	7.29	15.27	15.73
AAA Corporate	1.46	1.48	4.52	5.29	AAA Corporate	3.36	6.30	13.80	19.11
AA Corporate	1.83	1.57	5.12	6.85	AA Corporate	3.61	5.55	13.54	17.90
A Corporate	2.10	1.89	5.48	6.74	A Corporate	3.90	6.24	13.60	16.30
BBB Corporate	2.90	3.03	6.43	5.60	BBB Corporate	4.78	8.21	15.97	12.44
Barclays Indexes					Barclays Indexes				
BC Aggregate	1.91	2.21	5.31	6.00	BC ABS	1.28	1.17	2.54	2.72
BC Credit Long	4.16	6.65	13.92	13.76	BC MBS	2.08	1.11	3.11	4.36
BC High Yield	7.27	5.52	9.06	1.62	BC CMBS	2.12	2.24	5.93	6.22

See disclosures on the next page.

Ryan Labs TIPS				
	Yield To Worst (%)	MDuration (Years)	Year To Date Returns (%)	Last 12 Month Returns (%)
2 Year TIPS	-0.74	2.23	2.73	1.34
5 Year TIPS	-0.34	5.07	5.25	3.39
10 Year TIPS	0.13	9.08	7.37	4.91
30 Year TIPS	0.73	22.69	14.10	9.88
RL TIPS Index	-0.09	8.52	6.47	4.26

Market Implied Breakeven Inflation Expectation				
	Yield To Worst (%)		Inflation (%)	
	Nominals [1]	TIPS	BEI [2]	Current [3]
CPI (1 Month Lag)				1.0
2 Year	0.59	-0.74	1.33	
5 Year	1.01	-0.34	1.35	
10 Year	1.49	0.13	1.36	
30 Year	2.31	0.73	1.59	
RL Index	1.35	-0.09	1.44	

1) Nominals represent conventional U.S. Treasury Bonds and Notes.

2) BEI = Breakeven Inflation Rate (Nominal yields minus TIPS yields). Widening BEI indicates that TIPS are outperforming nominal bonds. When realized inflation is greater than implied inflation, TIPS also outperform.

3) Current Inflation = Bureau of Labor Statistics, Year over Year Consumer Price Index (non-seasonally adjusted, all items, 1 month lag)

ABOUT RYAN LABS ASSET MANAGEMENT

Ryan Labs Asset Management is an institutional fixed income manager that provides custom and market index strategies tailored to the unique needs of institutional clients since 1988. Our diversified, disciplined, and structured investment process is employed versus popular market indexes as well as custom liability indexes.

Ryan Labs employs a disciplined investment process that seeks to add value through issue selection and sector rotation, not through interest rate anticipation. All of our strategies are actively managed in a total return framework.