Monthly Market Review

November 2016

Economic Highlights

- Donald Trump's presidential victory scrambled financial markets and pushed economic news to the back burner. The unforeseen election outcome sent equity prices and bond yields plummeting. However, both recovered quickly on the expectation that the Trump-led government would cut taxes and boost infrastructure spending, thereby stoking government borrowing and inflation.
- In a revised estimate of third-quarter growth, the U.S. economy expanded at an even faster pace (3.2%) than the first estimate (2.9%) — an increase driven by personal consumption. Business investment and government consumption saw their pace of growth revised downward from the first estimate, demonstrating that the economy remains dependent upon consumers.
- November was the 74th consecutive month of job growth, with the U.S. labor market adding 178,000 jobs, in line with estimates. The unemployment rate fell to 4.6% — a new post-recession low. In another positive sign, job openings remained near record highs, while initial unemployment claims stayed near record lows.
- With economic data indicating a stronger pace of expansion, and inflation approaching the coveted 2% level, the Federal Reserve (Fed) is expected to raise short-term rates on December 14.

Bond Markets

- Global bond yields skyrocketed as the president-elect's proposed policies on taxes and spending fueled inflation expectations and the Fed prepared to raise rates for the first time in a year.
- Treasury yields rose across all maturities, with longer maturities leading the charge and the yield curve steepening significantly. The two-year Treasury yield rose 27 basis points (bps) to 1.11% while the 10-year yield rose 56 bps to 2.38%. Yields finished November at their highest levels of the year.
- The surge in Treasury yields resulted in uniformly negative returns across all bond market indexes. 1-3 year bond indexes lost -0.42%, but their year-to-date (YTD) return remained positive at 1.22%. 1-10 year indexes lost -1.70%, but their return for the year was 1.94%.
- Rising rates, coupled with a lack of supply, kept Federal Agency spreads suppressed, causing the sector to outperform Treasuries for the month.
- Investment-grade corporate yield spreads ended the month near their lowest levels of the year. Corporate bonds modestly outperformed comparable-maturity Treasuries, adding to the sector's excess returns this year.
- Asset-backed securities (ABS) and mortgage-backed securities (MBS) underperformed comparable-maturity Treasuries amid the rise in rates and increased volatility.
- Yields on money market securities (those with maturities of less than one year) remained elevated due to expectations for a December rate hike.

Equity Markets

- Broad domestic equity indexes posted their largest monthly gains since July as investors digested the implications of Trump's victory. The S&P 500 Index had a total return of 3.7%, while the industrial, blue-chip Dow Jones returned 5.8%.
- Performance varied across sectors. Financial, industrial, and energy sectors led gains while utilities, consumer staples, and real estate investment trusts (REITs) fell.
- While most developed market equities rose when measured in their local currencies, a sharp rise in the value of the U.S. dollar (USD) meant that in USD terms, these equities registered declines. In Europe, equity declines were segmented as peripheral Europe saw multi-percent declines while the United Kingdom ended the month unchanged. In Asia, indexes were much the same as in Europe, as Japan fell more than -3% while China rose 2.9% in USD terms.

PFMAM Outlook

- What moved the markets in November was not the economy, which was steady, nor central banks, whose policies remained unchanged, but rather political events. It is Washington, not Wall Street, that will be the focus for investors as potential changes in taxes, regulatory policy, trade and government spending have the potential to move markets before they affect the economy.
- Financial markets expect a 0.25% increase in the federal funds rate at the Fed's December meeting, and the possibility exists for an additional step-up in the first half of 2017. However, global central banks outside the U.S. remain accommodative for now.
- With the sharp rise in rates, the yield curve has steepened. Portfolios whose durations approximate those of benchmarks will have the potential to benefit from the added income that longer-maturity securities offer, and benefit from a yield curve roll-down.
- As investment-grade corporate yield spreads remain narrow, incremental return potential in the corporate bond sector now requires careful relative value analysis. Because liquidity is limited, new issues are usually offered at more attractive yields than secondary market securities.
- MBS that have stable cash flows may offer some benefits when compared with direct agency securities. But holding MBS will increase the sensitivity of portfolio market values and returns to interest rate changes.
- In the money market realm, short-term credit instruments such as commercial paper and certificates of deposit continue to offer exceptional value.

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U.S. Treasury Yields

Maturity	Nov 30, 2015	Oct 31, 2016	Nov 30, 2016	Monthly Change
3 Month	0.17%	0.30%	0.48%	0.18%
6 Month	0.39%	0.50%	0.61%	0.11%
2 Year	0.93%	0.84%	1.12%	0.28%
5 Year	1.65%	1.31%	1.84%	0.53%
10 Year	2.21%	1.83%	2.38%	0.55%
30 Year	2.97%	2.58%	3.04%	0.46%

Yields by Sector and Maturity as of November 30, 2016

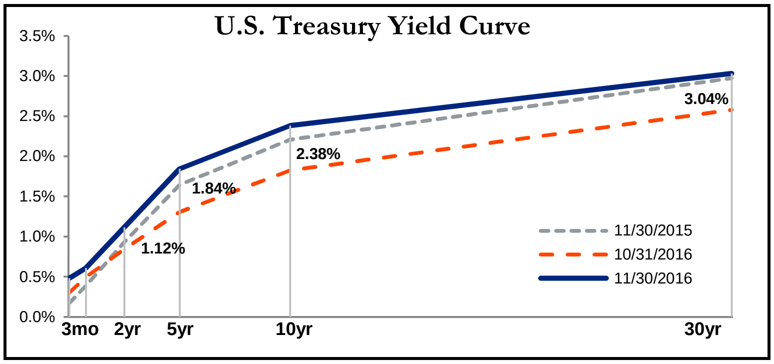
Maturity	U.S. Treasury	Federal Agency	Corporates-A Industrials	Municipals
3 Month	0.48%	0.46%	1.09%	-
6 Month	0.61%	0.55%	1.16%	-
2 Year	1.12%	1.20%	1.65%	1.24%
5 Year	1.84%	1.93%	2.48%	1.87%
10 Year	2.38%	2.74%	3.31%	2.64%
30 Year	3.04%	3.30%	4.24%	4.72%

Spot Prices and Benchmark Rates

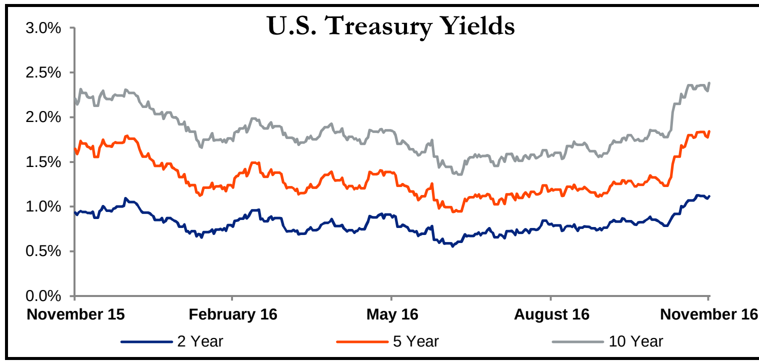
Maturity	Nov 30, 2015	Oct 31, 2016	Nov 30, 2016	Monthly Change
1 Month LIBOR	0.24%	0.53%	0.62%	0.09%
3 Month LIBOR	0.42%	0.88%	0.93%	0.05%
Effective Fed Funds Rate	0.08%	0.31%	0.31%	0.00%
Fed Funds Target Rate	0.25%	0.50%	0.50%	0.00%
Gold ($/oz)	$1,066	$1,273	$1,171	-$102
Crude Oil $/Barrel	$41.65	$46.86	$49.44	$2.58
U.S. Dollars per euro	$1.06	$1.10	$1.06	-$0.04

November's Economic Indicators

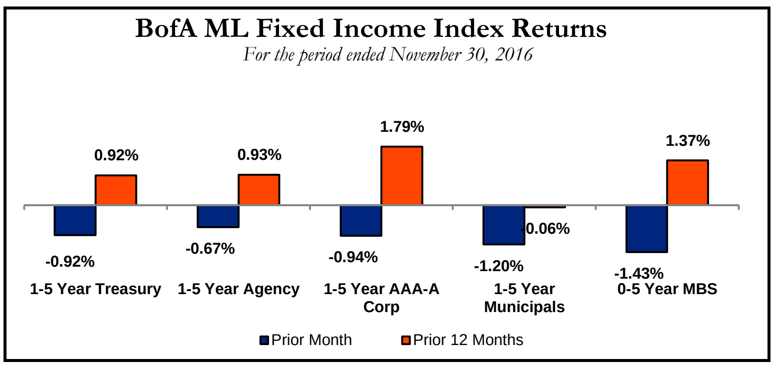
Indicator Name	Release Date	Period	Actual	Survey (Median)
Change in Nonfarm Payrolls	Nov 04	Oct	161k	173k
Retail Sales MoM	Nov 15	Oct	0.80%	0.60%
CPI Ex Food & Energy YoY	Nov 17	Oct	2.10%	2.20%
Existing Home Sales	Nov 22	Oct	5.60m	5.44m
New Home Sales	Nov 23	Oct	563k	590k
Consumer Confidence	Nov 29	Nov	107.1	101.5
GDP Annualized QoQ	Nov 29	3Q (2nd)	3.20%	3.00%



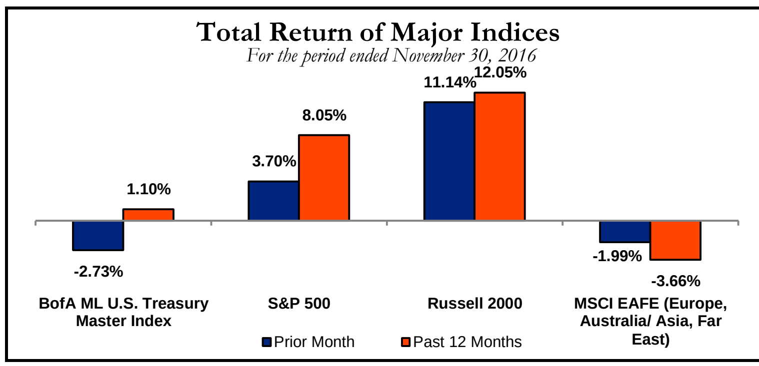
Treasury yields rose sharply in November, led by longer-term maturities, as Donald Trump's presidential victory fueled expectations for inflationary policies.



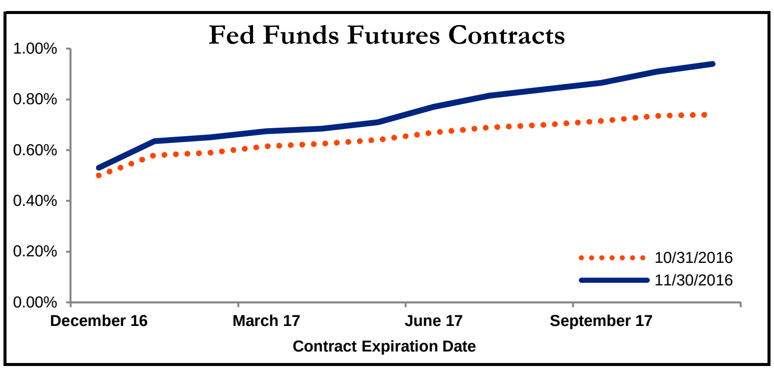
Treasury yields rose in November to their highest levels of the year, more than erasing all declines for the year.



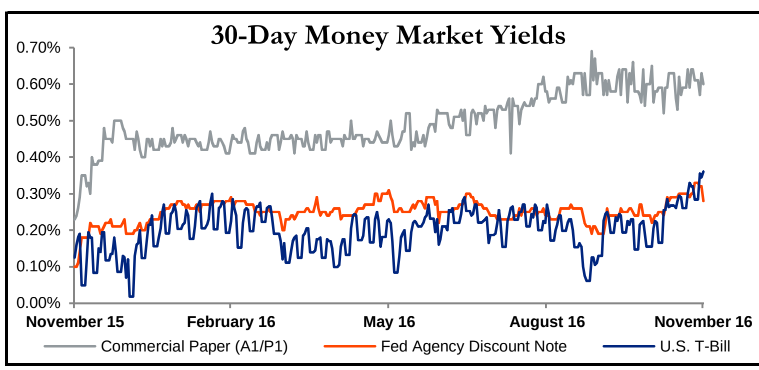
Most fixed income indexes posted a second consecutive month of declines, led by longer-term indexes, as yields rose and the yield curve steepened.



Domestic equity indexes posted their strongest monthly returns since July, while international indexes suffered losses as the dollar strengthened.



Rate hike expectations increased further in November as the probability of a hike at the Fed's December meeting rose to 100%.



Wide spreads persisted between commercial paper and government securities, although they tightened as the market further priced in a Fed rate hike in December.

Source: Bloomberg. Data as of November 30, 2016 unless otherwise noted.