



Daily Market View

Wednesday, May 23, 2018

Portfolio Advisory Group – U.S. Fixed Income

Market Snapshot	7:30am CDT	Prior
30-year UST	3.16	3.21
10-year UST	3.01	3.06
5-year UST	2.85	2.90
2-year UST	2.55	2.57
6-Mo UST	2.13	2.13
3-Mo UST	1.93	1.93
10-year TIPS	0.87	0.90
10-year Corp	4.33	4.33
10-yr AAA Muni	2.54	2.54
3M LIBOR	2.33	2.33
Fed Funds	1.75	1.75
Prime Rate	4.75	4.75
CPI (YoY)	2.50	2.20
NASDAQ*	7,378	7,378
DJIA*	24,834	25,013
S&P 500*	2,724	2,733
Oil	\$71.74	\$72.13
Gold	\$1,294.10	\$1,292.00
Copper	\$305.25	\$311.90
Yen / US Dollar	¥109.87	¥110.90
Euro / \$US	€ 1.1709	€ 1.1779

Link: [Bloomberg Economic Calendar](#)

*Previous Day

Client Friendly Publications

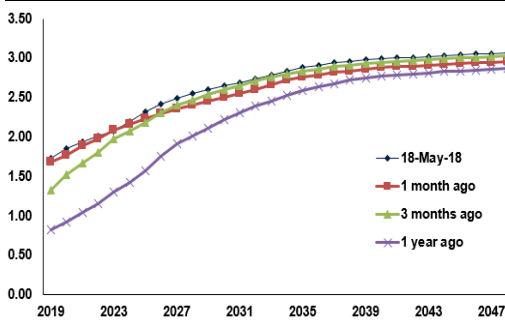
Municipal Market Insight [May 2018](#)

Credit Market Insight [April 2018](#)

Global Insight Weekly [May 17, 2018](#)

Global Insight Monthly [May 2018](#)

Municipal AAA GO Yield Curve



Source: RBC Wealth Management, MMD

Rates

Treasuries are having themselves a day this morning as risk-off trades spread over the market. The 10Y yield is down 6 bps to 3% for the first time since early last week, and the yield curve is flattening, with the 2s/10s down 4 bps to 44 bps.


Today at 2pm eastern time, the Fed is set to release the minutes from its meeting earlier this month. 3 weeks ago the Fed held rates unchanged between 1.50% and 1.75%, but struck a fairly dovish tone as it pertains to inflation. Officials reintroduced the word 'symmetric' when referring to its 2% inflation target, and even categorized market-based inflation expectations (which are at multi-year highs) as 'low.' Recent commentary from officials like Atlanta Fed President Raphael Bostic indicate that even if inflation does break past 2%, policymakers are unlikely to deviate from a gradual path, but today's minutes should provide us with more insight into the discussions behind the scenes.

For all of the concerns over the Fed's much anticipated balance sheet unwind, there has been very little news on that front in recent months. The Fed's balance sheet is already \$132B lighter than it was in October 2017 when the process began. For a quick refresher, the unwinding process is being implemented with a series of caps, or limits, to the amount of principal that is allowed to mature (or roll off) without reinvestment. The process started with caps of \$6B and \$4B for treasuries and mortgages, per month, respectively. These roll off caps are in place for 3 months, and then raised to the next threshold, and at this point the caps allow \$30B of securities to roll off per month (\$18B TSY, \$12B Mtg), more than halfway to the terminal pace of \$50B per month. Yet, the drop in total assets is an almost unidentifiable blip when compared to the massive \$4T total size. The pace of maturities rolling off without reinvestment is set to increase in the coming months, but its important to remember that the way in which the Fed has laid out the roll-off is one that is fairly small in scale compared to how quickly it built up the balance sheet, and we expect the unwind to continue at is has so far – in the background.

Munis

High grade municipal benchmark yields were unchanged on Tuesday as Treasuries also finished little changed. Municipal trading activity remained relatively light throughout the day, but the primary market was busy as roughly \$3.2B priced, which is a sizeable portion of this week's \$6.8B calendar.

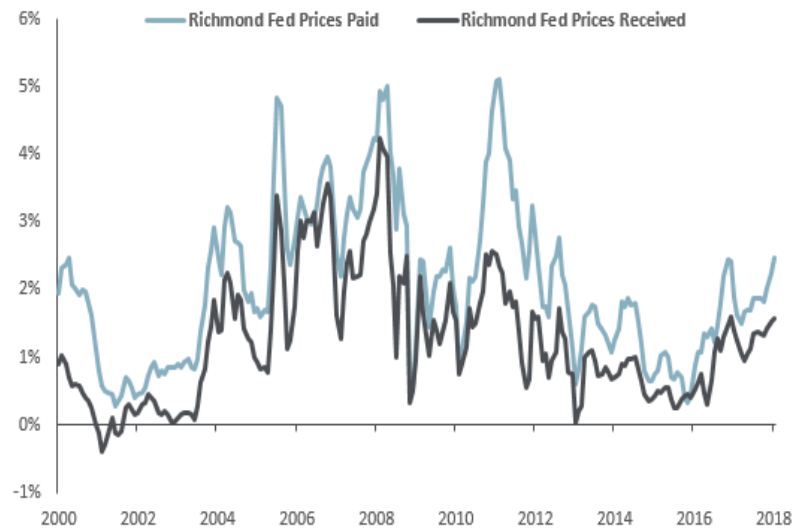
Fort Worth, Texas's finances should be in ship-shape since it is one of the fastest-growing cities in the U.S. and home to a booming economy. Instead, the city faces a \$3.1 billion pension liability that's caused credit-rating downgrades. S&P Global Ratings lowered the city one notch to AA from AA+ May 17. For years, Fort Worth contributed less in payments to the pension than what actuaries recommend and after the 2008 financial crisis the pension started to lower its exposure to risk assets.

 Key U.S. Economic Data Releases

Event	Period	Survey	Actual	Prior	Our Thoughts
MBA Mortgage Applications	May 18	-	-2.6%	-2.7%	New home sales are expected to have cooled a bit in April after a fairly strong start to the year. Higher mortgage rates have yet to take a material bite out of sales, with elevated home prices acting as the biggest headwind, though economists expect another positive contribution to GDP in Q2
New Home Sales m/m	Apr	-2.1%	-	4.0%	

Prior Session Highlights & Analysis

Event	Period	Survey	Actual	Prior	Our Thoughts
Richmond Fed Manufacturing Index	May	10	16	-3	Companies slow to pass on higher costs to customers



Source: RBC Wealth Management, Bloomberg, Richmond Federal Reserve

In the only economic data release of the day, the Richmond Fed bounced back for the month of May to a level of 16 after a dismal April fell to -3 – the lowest level since 2016. Regional manufacturing readings rarely garner any attention outside of economists, but there are always little kernels of information that investors may find noteworthy. For example, the Richmond Fed publishes its sub-indices that comprise the headline reading, including how prices are trending. Today’s print indicated that managers are reporting increases in both prices paid *and* prices received, rising 2.63% and 1.75%, respectively. Both of which are near the highest levels of the last 5 years, yet the important kernel here is that prices paid are accelerating much faster, which highlights the stickiness of company pricing to consumers. This region is essentially reporting that despite strong levels of demand in the form of new orders and shipments, input prices are rising 0.88% faster than end-prices are being raised. The chart shows that inflation peaks for consumers are often lower than for input prices, and given the level of competition in the current marketplace, companies are likely to absorb much of the impact from higher costs, keeping inflation tame relative to past cycles.

RBC Capital Markets – Daily Deck

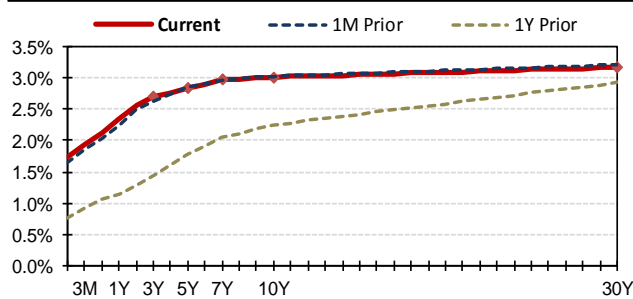
The upcoming FOMC Minutes for the May meeting are the highlight in a relatively light week for economic events. Look for the inflation discussion, the debate about neutral rates, and a nascent talk about balance sheet/policy frameworks to define this round of minutes. On inflation, recall that the committee was much gentler with their tweaks than they could have been in the May statement. Still, the mark-to-market on inflation outlooks continues to trend up. So look for the minutes to reflect a relatively hawkish slant on this front nonetheless. The debate about the neutral rate should also continue to ramp up. Even the majority of members that have pushed back against the idea of a rising neutral rate (namely, Williams) acknowledge that the committee will probably need to overshoot neutral at some point (as is typical of tightening cycles). The market currently has the Fed stopping near the lower end of neutral estimates (which is about 2.5% on Fed Funds). We think a re-pricing to a steeper tightening path will continue to play out in the months ahead... Finally, while unlikely to have been a big topic of discussion at the May confab, the Fed’s monetary policy framework is poised for some significant debate. As our Interest Rate Strategy team discussed last week given the risk of reserve stress at the end of this year, the Fed will need to begin communicating its plans for the monetary policy framework (specifically as to how it impacts balance sheet management) in the coming months.



	High Yield Corp		Investment Grade Corp			Government Related			% of Curve Captured
	B	BB	BBB	A	AA	AAA Munis	Agencies	Treasury	
3M	3.75%	3.59%	2.60%	2.40%	2.30%	-	1.93%	1.93%	60.8%
6M	3.90	3.71	2.72	2.50	2.38	-	1.97	2.12	67.1%
1Y	4.18	3.95	2.94	2.68	2.53	1.76%	2.14	2.32	73.4%
2Y	4.74	4.42	3.30	3.01	2.84	1.86	2.57	2.55	80.6%
3Y	5.19	4.80	3.56	3.24	3.04	1.96	2.72	2.69	84.8%
4Y	5.55	5.09	3.75	3.39	3.19	2.05	2.88	2.77	87.3%
5Y	5.87	5.36	3.93	3.53	3.34	2.13	3.03	2.85	89.9%
7Y	6.42	5.84	4.25	3.77	3.47	2.32	3.31	2.89	91.2%
8Y	6.63	6.01	4.37	3.86	3.58	2.40	-	2.93	92.5%
9Y	6.81	6.16	4.47	3.94	3.68	2.48	-	2.97	93.8%
10Y	6.99	6.31	4.56	4.02	3.76	2.54	3.36	3.01	95.1%
15Y	7.83	6.87	4.85	4.31	3.83	2.84	-	3.05	96.3%
20Y	8.18	7.02	4.93	4.38	4.03	2.99	3.33	3.09	97.5%
25Y	8.36	6.79	4.91	4.37	4.12	3.07	3.52	3.13	98.8%
30Y	8.27	6.78	4.90	4.36	4.17	3.13	-	3.17	100.0%

Global Sovereign 10Y Yields				Credit Spreads (5-Years; Average: Orange line)			
	Current	-1m	-6m	Investment Grade			
USA	3.01	2.98	2.32				
Canada	2.44	2.35	1.89				
Brazil	5.43	5.03	4.60				
Mexico	4.59	4.40	3.51				
UK	1.45	1.54	1.25				
France	0.80	0.84	0.68				
Germany	0.50	0.63	0.35				
Italy	2.44	1.79	1.77				
Spain	1.46	1.31	1.46				
Portugal	1.97	1.68	1.91				
Greece	4.34	4.01	5.30				
Japan	0.03	0.06	0.02				
Australia	2.84	2.87	2.51				
Hong Kong	2.22	2.13	1.74				
China	3.64	3.59	4.00				

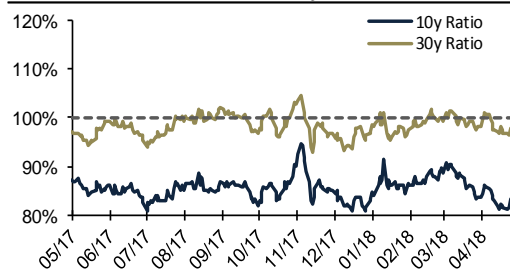
Treasury Yield Curve



3-Month UST Curve Spread Trends		
2s - 5s	Now 36	
	Avg 34	
2s - 10s	Now 51	
	Avg 53	
5s - 30s	Now 27	
	Avg 41	
7s - 10s	Now 4	
	Avg 6	
10s - 30s	Now 12	
	Avg 22	

Corporate Bonds	Spread Performance			
	OAS	1w % Δ	1m % Δ	1y % Δ
Treasury Index	-	-	-	-
Investment Grade	101	0.8	2.3	-12.24
AA	60	0.0	-1.6	-13.04
A	89	1.1	0.0	-2.20
BBB	136	0.0	0.7	-3.55
Barclays US HY Index	336	1.5	0.9	-6.67
S&P Pref. Stock Index	-	-	-	-
Bank Loans (BKLN)	-	-	-	-

10-Year & 30-Year Muni/Treasury Yield Ratios



	GO Municipal Benchmark 10y Yields (%)		
	Current	-1M	-6M
Composite	2.54	2.47	2.09
California	2.62	2.58	2.23
New York	2.53	2.51	2.06
Texas	2.73	2.62	2.21
Florida	2.67	2.57	2.25
Pennsylvania	3.16	3.05	2.61
Minnesota	2.74	2.55	2.16
Puerto Rico	13.86	11.77	11.53

Sector Performance	Spread Performance			
	OAS	1w % Δ	1m % Δ	1y % Δ
Basic Materials	127	1.3	4.0	-13.74
Communications	144	1.8	6.7	-8.33
Cons. Discretionary	97	-0.1	0.7	-15.42
Cons. Staples	97	1.6	3.4	-7.97
Energy	123	-0.5	0.3	-13.07
Financials	85	0.5	2.8	-0.08
Health Care	97	0.9	1.6	-10.24
Industrials	87	0.3	2.2	-10.47
Technology	78	0.3	-0.1	-20.28
Utilities	100	0.9	2.6	-18.94

UNITED STATES	10-Year Yield Forecasts (%)					
	2Q2018	3Q2018	4Q18	1Q19	2Q19	3Q19
Survey Month: <i>May</i>						
RBC Capital Markets	3.00	3.15	3.30	3.45	3.60	3.70
Bloomberg Median	3.00	3.10	3.19	3.25	3.30	3.42
<i>Bloomberg 1-Month Prior</i>	2.92	3.02	3.15	3.25	3.30	3.43

	Pre-Crisis Low	CDS Price & Spread Levels			
		Current	-1M	-3M	-1Y
CDX Investment Grade	30bps	62.6	61.8	55.3	61.9
CDX High Yield	191bps	340.6	346.2	331.0	327.1

Portfolio Advisory Group – U.S. Fixed Income Strategies

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