Daily Market View

Friday, May 17, 2019

Portfolio Advisory Group – U.S. Fixed Income

Market Snapshot	7:30am CDT	1-week Prior
Federal Reserve		
Fed Funds	2.50	2.50
Inflation (1-month prior)	1.55	1.80
3m Libor	2.53	2.53
Treasuries		
3-Month	2.33	2.42
2-year	2.17	2.27
5-year	2.14	2.26
10-year	2.37	2.47
30-year	2.81	2.89
Corporates		
Investment Grade		
IG Index	**3.58**	**3.62**
AAA	3.21	3.24
AA	3.01	3.05
A	3.31	3.35
BBB	3.89	3.93
Speculative Grade		
HY Index	**6.37**	**6.33**
BB	4.94	4.93
B	6.43	6.37
Preferreds		
Hybrids	5.70	5.72
Fixed-rate	5.88	5.91
Municipals		
3-year	1.65	1.70
10-year	1.96	2.01
15-year	2.29	2.34
Long	2.75	2.80
Equities		
S&P 500	2,876	2,881
Dow Jones	25,863	25,942
NASDAQ	7,898	7,917
Commodities		
Oil	$63.29	$61.66
Gold	$1,285	$1,286

Link: Bloomberg Economic Calendar

Credit

As U.S. and China continued to clash over trade, souring sentiment across markets, high-yield corporate bond funds saw the pace of outflows accelerate. Investors yanked $2.57 billion from retail funds in the weekly reporting period ended May 15, according to data from Lipper. The outflow is the biggest cash withdrawal for corporate high yield since December and a sharp rise from the $212 million pulled last week.

Weekly Junk Bond Outflows Reach Highest Rate since December

Chart Source: Lipper, Bloomberg

Regardless of the fund outflows, other measures of the junk bond market remain quite healthy. Year-to-date net inflows stand at about $14 billion as of May 13, a stark reversal from outflows of about $19.6 billion a year ago. And although U.S. junk bond returns for the year dipped below 8% for the first time in five weeks on Wednesday, high yield remains one of the top performers in fixed income, behind only preferreds.

Junk bond issuers have also continued to access the primary market through macro volatility. Six new deals worth $5 billion are marketing this week, with about $4 billion scheduled to price. Last week Washington-Beijing trade tension dominated the headlines, but high-yield supply totaled $12 billion, making it the busiest week in nearly 20 months.

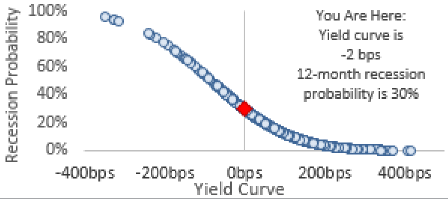
It's a similar story for new deal flow in the U.S. investment-grade bond market. The tariff tit-for-tat dampened issuance conditions and kept borrowers sidelined on Monday, but 18 companies have since come forward to raise almost $30 billion of new bonds.

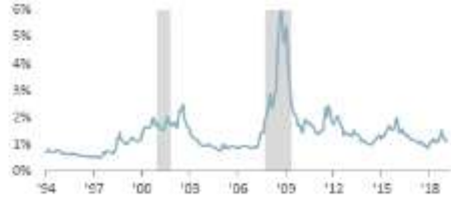
High-grade corporate bond funds also remain on a tear. Inflows of $2.17 billion for the period ended May 15 mark the 16th consecutive week cash has poured in. Investors added $3.3 billion last week. The total influx now stands at $44 billion since the streak began in January.

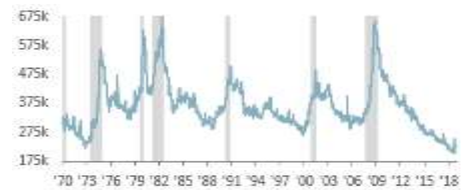
Other positive measures for investment-grade include return levels and cash spreads, which have managed to stay flat to marginally tighter this week. High grade, like high yield, is among the best performing fixed-income asset classes, currently returning 6.1% to investors, up from 5.67% last week.

Recession Watch Dashboard – Yield curve flashing yellow, but credit spreads & the labor market look solid

Yield Curve (10Y – 3m)			IG Corporate Credit Spreads			Weekly Jobless Claims		
Current	1w Change	Recession	Current	YTD Change	Recession	May 4	52w High	Recession
-2 bps	-7 bps	**30%**	1.17%	**-0.36%**		228k	**253k**	







Our Thoughts: The **yield curve** is on the verge of inverting again for the first time since March. **Investment grade credit spreads** have tightened from the January high of 157bps along with the equity market rally, a sign that credit markets are pricing reduced recession risk; **jobless claims** have jumped back to ~230k after record lows in recent weeks.

Source: RBC WM, Bloomberg; Recession probability based on NY Fed Yield Curve Model

Key U.S. Economic Data Releases

Event	Period	Survey	Actual	Prior
Leading Index	Apr	+0.2%	-	+0.4%
U of Michigan Consumer Sentiment	May P	97.2	-	97.2

Chart: Leading Economic Indicators Nearing Negative Territory

Source: RBC Wealth Management, Bloomberg

Our Thoughts

- **Leading Economic Indicators.** On a monthly basis, the index is expected to be up +0.2% largely fueled by the recovery in stock markets, but on a 6-month annualized basis—which is what the chart to the left shows—the index is nearing negative territory.
- But as the chart also shows, 0% on the index isn't unprecedented as we've already reached that level 3 times this cycle, it's not until level reach -5% that recession risks start to rise materially.

Prior Session Highlights & Analysis

Event	Period	Survey	Actual	Prior
Housing Starts	Apr	1,209k	**1,235k**	1,139k
Philly Fed Business Outlook	May	9.0	**16.6**	8.5
Jobless Claims	May 11	220k	**212k**	228k

Chart: Low mortgage rates boosting housing activity

Source: RBC Wealth Management, Bloomberg

Our Thoughts

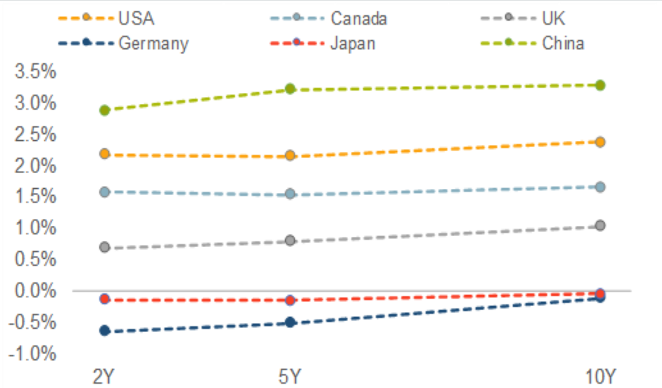
Market volatility a boon for housing

- **Housing.** Bloomberg: A stronger-than-expected increase in housing starts at the beginning of the second quarter bodes well for residential investment to make a contribution to GDP growth after five quarters of declines. Housing is one of the few sectors benefiting from current market jitters and flight to quality in bonds as lower interest rates improve affordability.
- A broad-based increase in housing starts supports our expectations for a modest 2% rise in residential investment in the second quarter.
- An 80-basis point decline in mortgage rates since November is fueling demand for housing. The shrinking gap between new and existing home prices makes newly built housing more attractive.

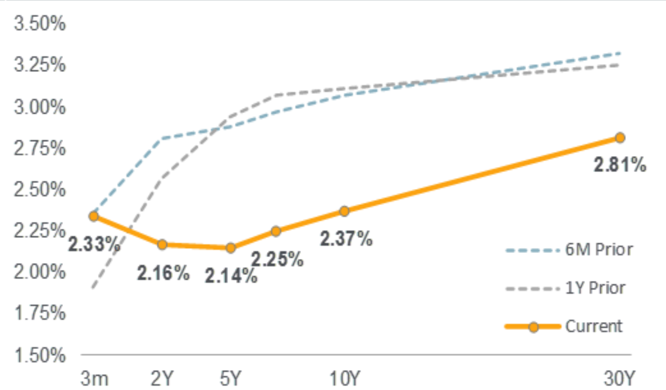
Federal Reserve & Sovereign Yields

		3M	1Y	2Y	5Y	7Y	10Y	15Y	20Y	25Y	30Y
Gov't	Treasuries	2.30	2.25	2.16	2.14	2.25	2.37	-	-	-	2.81
	Agencies	2.45	2.36	2.24	2.26	2.42	2.62	2.84	3.05	3.12	3.13
	AAA Munis	1.45	1.49	1.50	1.54	1.59	1.73	2.08	2.25	2.40	2.46
IG Corp	AA	2.50	2.52	2.50	2.68	2.89	3.15	3.51	3.76	3.83	3.84
	A	2.62	2.63	2.64	2.83	3.06	3.35	3.78	4.03	4.01	3.99
	BBB	2.84	2.88	2.95	3.26	3.57	3.93	4.42	4.71	4.66	4.58
HY Corp	BB	3.34	3.66	4.09	4.85	5.32	5.76	6.24	6.58	6.62	6.64
	B	3.80	4.17	4.69	5.65	6.20	6.65	7.17	7.63	7.60	7.60

Global Sovereign Yields



U.S. Treasury Yield Curve



Rate Forecasts	Current	2019	2020	2021
Fed's 'Dot Plot'	2.50%	2.50%	2.75%	2.75%
Market Pricing	2.50%	2.25%	2.00%	2.00%
Our View	2.50%	2.50%	2.50%	2.50%

10-Year Treasury Yield Forecasts	Q219	Q319	Q419	Q120
Consensus	2.62%	2.69%	2.75%	2.78%
RBC Capital Markets	2.55%	2.65%	2.75%	2.90%

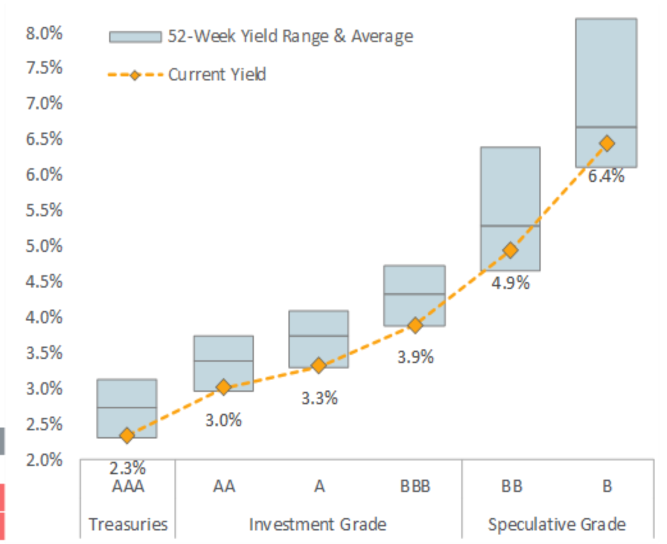
Corporates

Sector	1w Chng	Year-to-Date Performance
Treasuries	0.30%	2.5
Investment Grade		
Index	0.31%	6.0
AA	0.26%	4.0
A	0.32%	5.3
BBB	0.31%	6.9
Speculative Grade		
Index	-0.07%	8.2
BB	0.02%	8.0
B	-0.11%	8.2
Preferred Shares		
Fixed-Rate	0.53%	9.9
Hybrids	0.53%	9.8
Equities		
S&P 500	-0.10%	15.7

Credit Spreads over Treasuries (bps)

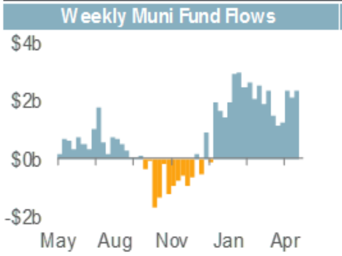
	Current	5Y Low	5Y Avg	5Y High
Investment Grade	117	85	127	215
Speculative Grade	392	303	440	839

Corporate Bond Yields by Credit Quality

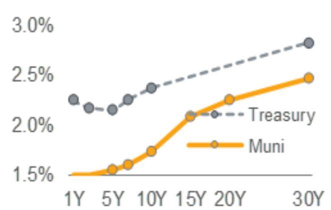


Municipals

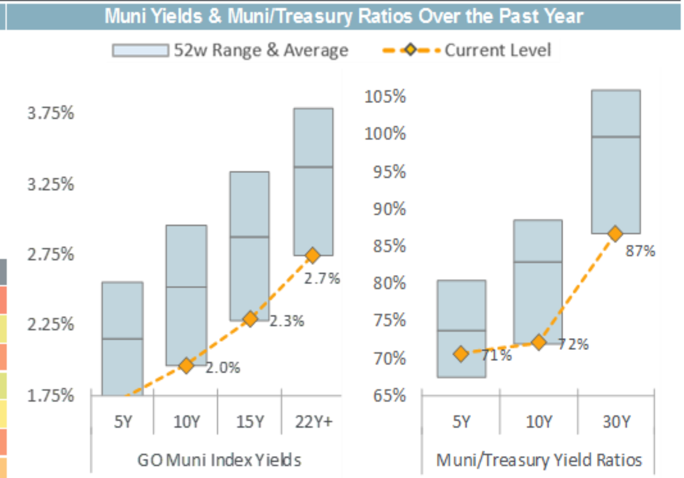
Weekly Muni Fund Flows



AAA Munis vs. Treasuries



Muni Yields & Muni/Treasury Ratios Over the Past Year



Select State Benchmark Yields

CA	1.99%	PA	2.33%	AZ	2.01%
NY	2.05%	OH	2.14%	CT	2.16%
TX	2.14%	VA	2.04%	NC	2.03%
FL	2.19%	MD	1.98%	MI	2.23%
WA	2.01%	NJ	2.56%	WI	2.11%
IL	2.70%	CO	2.30%	OR	2.02%
MA	2.05%	GA	2.10%	MN	2.07%

Source: RBC Wealth Management, Bloomberg Barclays Indexes, Federal Reserve

Portfolio Advisory Group – U.S. Fixed Income Strategies