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@Caprin_Asset

INTERMEDIATE TAXABLE COMPOSITE CHARACTERISTICS

AS OF: 12/31/2014

Duration: 4.09yrs
Yield-to-Worst: 2.01%
Yield-to-Maturity: 2.01%
Maturity: 4.64yrs

Strategic Overview

Macro: The most highly anticipated event of 2014 – the end of Fed tapering – happened in October, ending an era of unprecedented economic stimulus. Fed officials long telegraphed the end of the asset purchasing program, allowing US yields to absorb the news easily. After tapering ended, focus shifted seamlessly to Fed statements and press conferences as traders tried to determine the Fed hike timeline. Volatility ensued as Fed officials used statements deemed overly hawkish or dovish relative to market expectations. Traders became highly conscious of the phrase 'considerable time,' verbiage the Fed left unchanged in Q4. This quelled much of the fear and reassured markets that the hike was still off in the distance. Economic struggles in Europe and Asia and their impact on US markets moved to the fore for the remainder of 2014. While the US recovery gained modest momentum, European and Asian countries considered expanded QE to help avoid recession. This global slowdown sent G-7 bond yields plummeting and re-ignited a powerful rally in US fixed income. Foreign investors flooded into the haven of US Treasuries and, capturing significant relative value, drove yields to 18-month lows in mid-December. Inflationary pressures vanished, encouraging particularly strong performance in longer maturities. Against almost everyone's forecasts, intermediate and long bond prices finished 2014 far higher than where they started.

Sector Notes: Investment grade and High Yield Corporate spreads widened in the quarter: HYG (the iShares iBoxx $ High Yield Corporate Bond ETF) fell to its lowest price since June of 2012, while the Markit CDX Investment Grade Corporate Index, a popular index to measure risk spreads, softened modestly. Weakness in Corporates was attributable mostly to the spillover from global challenges and the sharp drop in oil prices. Not all corporate sectors struggled, though; utilities were strong and benefitted from the oil rout.

Caprin Performance Notes: A higher quality bias and yield curve positioning contributed to favorable performance in the quarter. The quality bias helped protect portfolios from the worst of the spread widening, and emphasizing 5 – 10 year maturities helped position portfolios longer than the benchmark. This maturity structure also helped capture some of the positive effects from the recent curve flattening. Exposure to the utility sector boosted performance, and the sector remains a go-to to improve income and to help insulate against cyclical shocks.

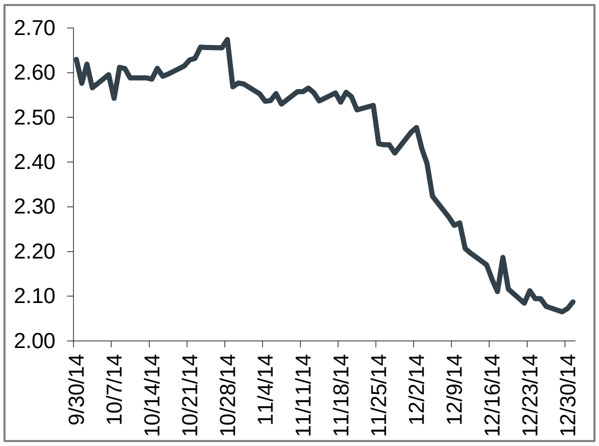

Figure 1: Spread Between 2-Yr and 30-Yr US Treasury Yields
Source: Bloomberg

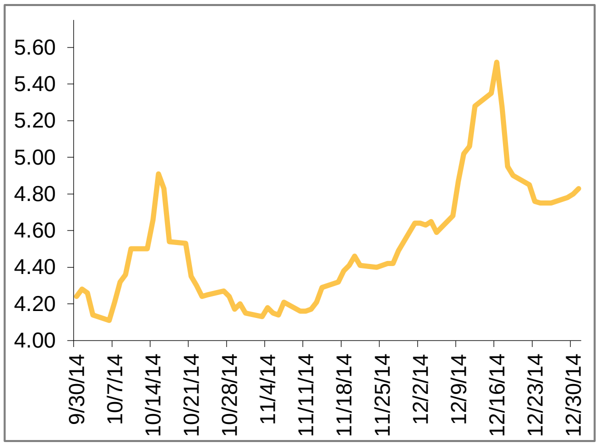

Figure 2: Barclays US Corporate High Yield OAS
Source: Bloomberg

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