knowledge preserves wealth

CAPRIN

@Caprin_Asset

Q3 2015 SHORT MATURITY QUARTERLY COMMENTARY

SHORT MATURITY MUNI COMPOSITE CHARACTERISTICS

AS OF: 9/30/2015

Duration: 1.54 yrs
Yield-to-Worst: 0.85%
Yield-to-Maturity: 0.88%
Maturity: 1.64 yrs

LOW DURATION TAXABLE COMPOSITE CHARACTERISTICS

AS OF: 9/30/2015

Duration: 1.81 yrs
Yield-to-Worst: 1.22%
Yield-to-Maturity: 1.22%
Maturity: 1.90 yrs

Strategic Overview

Macro: Volatility reigned again in the third quarter of 2015. Greece finally submitted to creditor demands and reached a deal to remain in the Eurozone, calming months of anxiety over the fallout from a "Grexit". However, global growth concerns triggered a flight to quality into U.S. Treasuries. Yields on the benchmark 5-yr, 10-yr and 30-yr Treasury fell 34bps, 38bps, and 35bps, respectively during the quarter. Signs of economic slowdown in China (the world's second largest economy) coupled with sporadic intervention by the Chinese government to stabilize equity markets forced U.S. equities lower. The Dow Jones Industrial Average fell 7.58% during the quarter, headlined by an approximate 1,900 point decline over six days in late August. Emerging markets continued to be plagued by falling commodity prices, a stronger dollar, and the potential for higher U.S. interest rates. Domestically, the U.S. economy continued to progress, although at a sluggish rate. Second quarter GDP ended with a final revision up to 3.9%, after an insignificant 0.6% pace during Q1. Growth was driven largely by personal consumption, business fixed investment and government spending, but not without the caveat of meaningfully higher inventories. On the jobs front a strong positive trend stalled abruptly as the September Nonfarm payroll print came in at 142k, 60k less than estimated, with significant downward revisions to prior months. Commodity softness continued with the price of crude falling 24% during Q3 to trade around $45 barrel, and core PCE (the FOMC's favorite measure of inflation) remained stubbornly below their 2% target. All of this together was enough for the FOMC to delay hiking interest rates during a highly-anticipated September meeting. Although an October hike has been all but taken off the table, we expect heightened volatility during the latter part of Q4 as the FOMC remains vocal about its desire to raise rates by year end.

Market Dynamics: In a tumultuous quarter for money market and front-end yields, we continued to face persistent low rates and strained supply. As forecasted, speculation was rampant amid the heightened volatility surrounding what was ultimately an uneventful September FOMC meeting. Front-end treasury and swap yields plunged post announcement, and the subsequent rally continued into the end of the third quarter. Similar to Q2, trading ranges for short dated notes were wide, but decreases of 1bp and 10bps for 2Y and 3Y notes respectively between quarter ends was less dramatic. Contrary to the more hawkish Fed governor rhetoric following the FOMC statement, derivative markets pushed out their pricing of 'liftoff' into the early months of 2016. This fact, together with recent softer U.S. economic data prints, will likely keep short rates depressed until the FOMC can more clearly communicate its plans to normalize policy. Looking ahead, volatility will likely remain elevated, particularly around the October and December FOMC meetings. And although the global growth picture is bleak, we still do not rule out an eventual curve flattening led by higher front-end rates.

Caprin Performance Notes: Factoring in the late quarter rally following the FOMC announcement, short maturity strategies posted respectable gains. Although the back half of the quarter's performance was mostly Fed-driven, our overweight to spread sectors continued to aid total return by producing higher income levels, and the short dated corporates were far less susceptible to the spread widening seen further out the curve. We continue to fine tune the duration and maturity structures of portfolios seeking a balance of income and preparation for potential FOMC action. Our taxable muni holdings added incremental value as this sector was one of the better performers over the quarter, though the availability of purchase opportunities was limited.

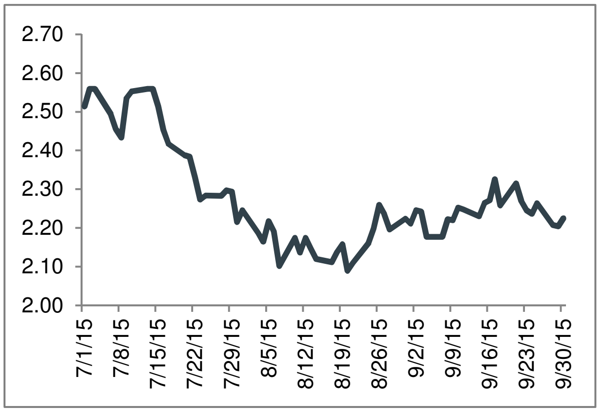

Figure 1: Spread between 2-Yr and 30-Yr US Treasury Yields
Source: Bloomberg

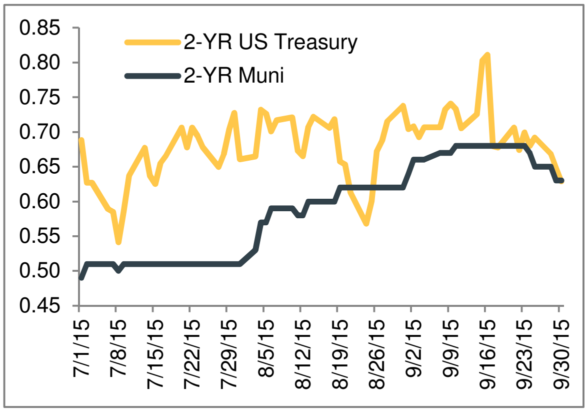

Figure 2: 2-Yr US Treasury Yields vs. 2-Yr Muni Yields
Source: Bloomberg; MMD

1802 Bayberry Court, Suite 202
Richmond, Virginia 23226
804] 648-3333
CAPRINBONDS.COM

Media Contact:
aplotkin@caprinbonds.com