CAPRIN

knowledge preserves wealth

Q1 2016 Short Maturity Muni and Low Duration Taxable Quarterly Commentary

MACRO

At the end of 2015 we concluded our macro overview by saying "we wonder if the 'gradual' estimates will be difficult to achieve while domestic and global headwinds abound." Our reflections were directed at the then just-released projection of a 1.4% year-end 2016 Fed Funds Rate driven by estimates of approximately four, 25 basis point (.25%) rate hikes. This view of an overly optimistic central bank was certainly not unique, but what caught many off-guard was the significant volatility and weaker tone that washed over markets to begin the New Year. Equity and other risk assets were quickly plagued by renewed concerns over "true" Chinese growth prospects and that government's ability to continue its deliberate support of an already over-leveraged and inflated system. The rout, already well established, in commodities made new bottoms with crude oil prices declining nearly 30% by late January, and touching a 12 year low of approximately $26 per barrel. Yields on the 10-yr US Treasury, in concert with the aggressive risk-off move, declined nearly 60 bps from its 2015 close, to a level (1.65%) not seen since the same time a year prior, and credit spreads generically moved to their widest level in four years. As the quarter drew on though, markets did eventually find footing with the slowing of negative headlines from Asia and crude oil prices that stabilized on rumors of OPEC production cuts. Federal Reserve members unsurprisingly erred on the side of caution when they met in March, choosing not to pursue a rate increase while also making significant downward revisions to their short and intermediate-term rate outlooks. Now just two, 25 basis point (.25%) hikes are implied for 2016. We certainly see this as a more realistic expectation given the uninspired growth prospects both domestically and abroad but continue to question if even this may be hard to achieve.

MARKET DYNAMICS

The return of volatility was a persistent theme throughout financial markets over the quarter, and front-end rates were certainly not overlooked. Short dated treasury and money market yields have been whipped around by expectations of FOMC action over the last six months anticlimactically, to be left almost unchanged heading into the second quarter of 2016. The broader yield curve has continued to flatten mildly, led by the short end, as longer maturities have stayed anchored on subdued growth and inflation expectations. The spread between US Treasury 2-yr and 10-yr notes has been on the decline since June 2015 and decreased another 18 bps in the first quarter. We expect front-end flow and yields to remain hinged on Federal Reserve rhetoric and trader's interpretation of economic data both foreign and domestic.

PERFORMANCE NOTES

Deliberate name selection in the Low Duration Taxable strategy was additive to return characteristics and helped reduce performance deviations while significant credit spread volatility gripped the asset class over much of the quarter. Duration targeting was conservative coming out of 2015 and adjustments are underway to reflect reduced front end rate pressures for 2016. We continue an overweight in the Short Municipal strategy to more robust yield sectors such as hospitals, housing, and other direct revenue stream issuers that we believe provide sound credit metrics and incremental income in this still challenging yield environment.

1802 Bayberry Court, Suite 202
Richmond, Virginia 23226
804] 648-3333
CAPRINBONDS.COM
Media Contact:
aplotkin@caprinbonds.com

SHORT MATURITY MUNI COMPOSITE CHARACTERISTICS

AS OF: 3/31/2016

Duration: 1.38 yrs

Yield-to-Worst: 0.84%

Yield-to-Maturity: 0.86%

Maturity: 1.44 yrs

LOW DURATION TAXABLE COMPOSITE CHARACTERISTICS

AS OF: 3/31/2016

Duration: 1.41 yrs

Yield-to-Worst: 0.96%

Yield-to-Maturity: 0.96%

Maturity: 1.44 yrs

FIGURE 1: SPREAD BETWEEN 2-YR AND 30-YR US TREASURY YIELDS
Source: Bloomberg

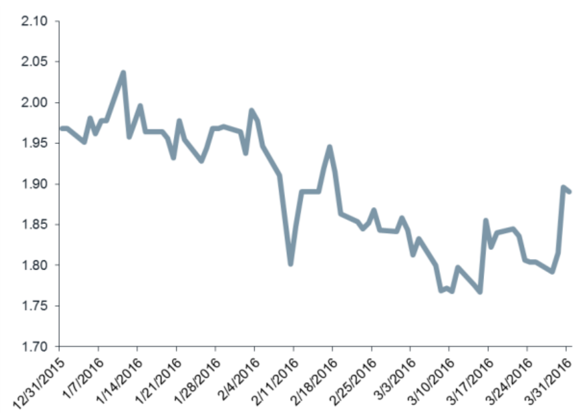

FIGURE 2: 2-YR US TREASURY YIELDS VS. 2-YR MUNI YIELDS
Source: Bloomberg; MMD