APPLETON PARTNERS, INC.

This Week in the Bond Market 03/28/16

Headline News

April Rate Hike Still Unlikely

- During the market holiday on Friday, 4Q15 GDP final revision was released at 1.4%, which was higher than the expected 1.0%. Household purchases led the increase with the 2.4% annual pace better than the estimated 2% pace. On Friday, the jobs report will receive extra scrutiny, given the uncertainty in other macroeconomic data. The expectation is 210k new jobs for March, after an increase of 242k for February. While a rate hike in April is possible, it remains unlikely. In the meantime, Fed Chair Janet Yellen will speak at the Economic Club in NYC on Tuesday.

Pennsylvania Finally Approves a Budget

- Governor Tom Wolf, a Democrat, conceded to the Republican legislature and allowed the opposition's proposed budget to become law on Wednesday, March 23rd, ending a 266-day stand-off. Pennsylvania's current fiscal year began on July 1, 2015. Illinois is now the only state not to have a budget for the current fiscal year.
- The budget supplements a partial spending plan approved earlier this year and provides short-term relief to those entities that rely on state funding, such as school districts. However it fails to address a sizable budget gap and the need for tackling long-term liabilities associated with retiree benefits.
- Governor Wolf continues to press for tax increases, while Republicans are hesitant to increase levies and are focused on pension reform. Despite the budget approval removing an overhang for the State, the lack of real progress on fixing Pennsylvania's fiscal profile continues to be a concern.

Illinois Supreme Court Strikes Down Chicago Reforms

- In a ruling that was largely expected, the Illinois Supreme Court upheld a lower court decision that Chicago's pension reforms for the laborer's and municipal employees' funds were unconstitutional under state law.
- The ruling by the high court mirrors a similar outcome from May 2015, under which the State Supreme Court invalidated pension reforms enacted at the State level.
- Illinois' constitution includes a pension protection clause that is very direct in prohibiting the impairment of accrued and promised benefits. We note this level of constitutional "protection" is rare and not afforded in all states. The legal precedent set by these rulings is largely specific to Illinois.
- Chicago's already stressed financial position will now face additional pressure. The City was relying on the reforms and legislation, which has not been approved by the Governor, to help alleviate a spike in pension funding levels. Chicago earlier in the week tapped a line of credit to finance a $220 million contribution to the police and firefighters pension plans, reflecting a tight liquidity position.

Market Update

Muni Market Overview

- The municipal yield curve was essentially unchanged for the week. Supply, at $6.3 billion for this week, is dominated by a single deal: Trustees of California State University. (Aa2/Applied/NR) are bringing a $1.3 billion deal on Wednesday.
- Demand has remained strong with primary deals being oversubscribed and continued inflows into muni funds. For the week ending 3/23/16, inflows to muni bond funds were $902 million. For the year, the weekly inflows have averaged $1.1 billion.

FIXED INCOME INDEX RETURNS AS OF 3/24/2016

	MTD	YTD
Barclays 3Yr	-0.31	0.71
Barclays 5Yr	-0.59	0.93
Barclays 7Yr	-0.48	1.14
Barclays MM Short 1-5Yr	-0.42	0.68
Barclays MM 1-10Yr	-0.54	1.00
ML US Gov/Corp 1-10 Yr	-0.17	1.72

Source: Interactive Data

Corporate Market Overview

- All was relatively quiet in the Investment Grade Credit space last week. The abbreviated holiday week left issuers on the sidelines, as only $15 billion came to market. This was the second lowest week of issuance behind the week ending 02/12/16 in which only $1 billion was issued. One issue of note was the $2 billion deal brought by FedEx (FDX Baa2/BBB) which came at +135 in 10Yrs and +185 in 20Yrs. Spreads continue to tighten and demand for credit continues to be strong. Amidst a bit of rate volatility midweek, the 5Yr & 10Yr treasury benchmarks closed out the week relatively unchanged at 1.38% and 1.90% respectively.

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APPLETON PARTNERS, INC. ONE POST OFFICE SQ. BOSTON, MA 02109 TEL. 617.338.0700 WWW.APPLETONPARTNERS.COM