APPLETON PARTNERS, INC.

THIS WEEK IN THE BOND MARKET 5/9/2016

HEADLINE NEWS

Disappointing Employment Data Dampens Rate Hike Expectations

- Nonfarm payrolls were released at a disappointing 160k versus the expectation of 200k, with the unemployment rate ticking up to 5.0% from 4.9%. Also indicative of a challenged labor market, the Initial Jobless Claims were higher than expected at 274k (versus 260k expectation) for the second consecutive week. On a more positive note, Average Hourly Earnings YoY increased by 2.5%, more than the expected 2.4%.
- The Implied Probability of the next Fed Funds hike, which previously reached 50% in December 2016, has been pushed off further by the market and is under 50% for February 2017. Retail sales and PPI are expected on Friday.

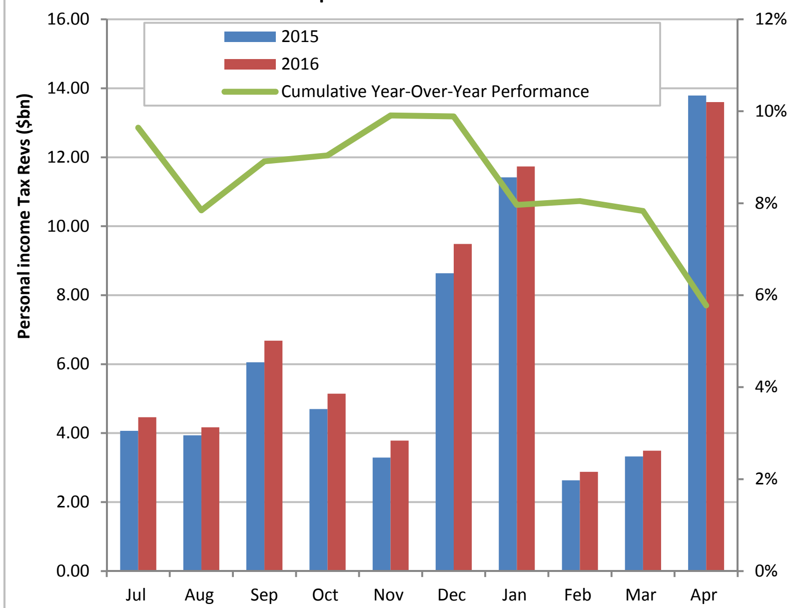
California Tax Revenues Hit a Bump in the Road

- Preliminary personal income tax revenues collected by the State of California for the key month of April *declined* by 2.8% year-over-year to $13.6 billion, compared to projections for a 4.6% *increase*. The underperformance likely points to lower capital gains experienced in 2015 due to weaker performance in financial markets and not necessarily a downturn in the state's economic activity.
- Despite the $1 billion "miss," personal income tax revenues, and California's tax revenues, in general, remain strong this year. Through the first 10 months of fiscal 2016, personal income taxes of $65.2 billion are still $3.4 billion, or 5.5%, above the prior year's collections. Through the end of March, total general fund revenues for the State are 7.1% above last year's performance and 3.0% above the governor's original budget.
- California's financial position is also stronger than it has been historically, particularly its higher reserve balances, allowing the state to better weather revenue volatility. Currently, California expects to finish fiscal 2016 with $8.7 billion in reserves or a healthy 7.5% of revenues.
- The Governor and the bipartisan Legislative Analyst's Office will release new budget projections later in May, which will provide better clarity on the State's fiscal trajectory.

FIXED INCOME INDEX RETURNS AS OF 5/6/2016	MTD	YTD
Barclays 3Yr	0.06	1.08
Barclays 5Yr	0.15	1.79
Barclays 7Yr	0.26	2.45
Barclays MM Short 1-5Yr	0.07	1.14
Barclays MM 1-10Yr	0.21	2.19
ML US Gov/Corp 1-10 Yr	0.18	2.60

Source: Interactive Data

Despite April Weakness California's Personal Income Tax Revenues Are Up 5.5% Over Fiscal 2015



Source: California Department of Finance, California State Controller's Office

MARKET UPDATE

Muni Market Overview

- The municipal curve inside of 10Yrs was stronger for the week with 7Yrs lower by 5bps as it followed the Treasury curve after the disappointing jobs report on Friday. Demand for Munis has continued as shown by $2.5 billion in fund flows for the week ending 5/4/16 to bring the year to date total to $22 billion. This week marks the largest weekly inflow since the 2nd week in February.
- Issuance is expected at about $8.3 billion this week and 30-day visible notched up slightly to $13.35 billion, above the average for the year of $10 billion. The largest deal this week is $662 million Alameda Corridor Transportation Authority (Baa2/BBB+/BBB+) in CA followed by $546 million City of Chicago Second Lien Water (Baa2/A/AA).

Corporate Market Overview

- Investment grade issuance began the week looking as if it was going to disappoint expectations of between $20 - $25 billion. However, Thursday's surge of $15.525 billion brought the week's total to $29.375 billion. The largest deal of the week was Shell International Finance's (RDSALN Aa2/A+/AA-) $7.25 billion across 4 maturities. The deal priced at +118 in ten years and was well received.
- IG credit spreads were slightly wider last week after several weeks of continued tightening. Treasury yields tracked lower all week and the 10Yr benchmark note ended the week 10 bps lower at 1.77.

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