A.H. Williams

Spinnaker Report

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AHW &Co Quarterly Commentary
April 2015

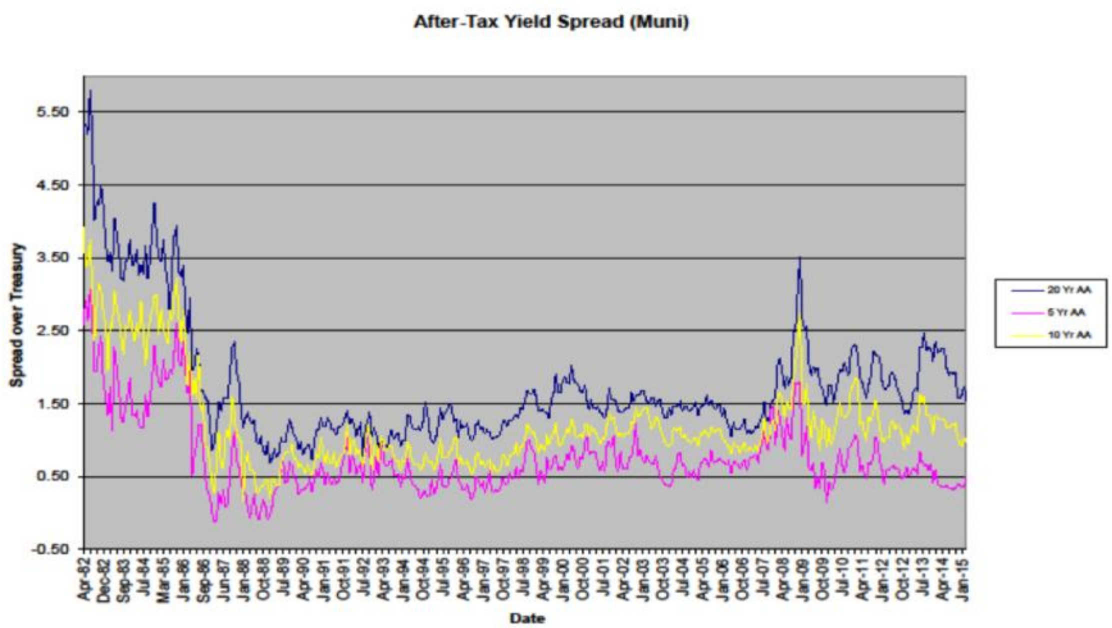
V is back. Not the sci-fi television series, but Valuation, Volatility, and Volume. The supply of new issues has driven returns in the first quarter of 2015. In January, the dearth of new bonds combined with cash from maturities and coupon payments gave us a big rally in munis. Treasury yields gave an extra boost as the 10 yr. fell from 2.17% to 1.68%. Both trends reversed in February as Treasury yields climbed back to 2%, and muni new issue volume surpassed most Februarys of the last six or seven years. March came in like a sad lion and went out like a happy one, ending at similar levels to its start. See this chart for a comparison of the bond volatility and that of stocks, as bond volatility went up and stock volatility went down:

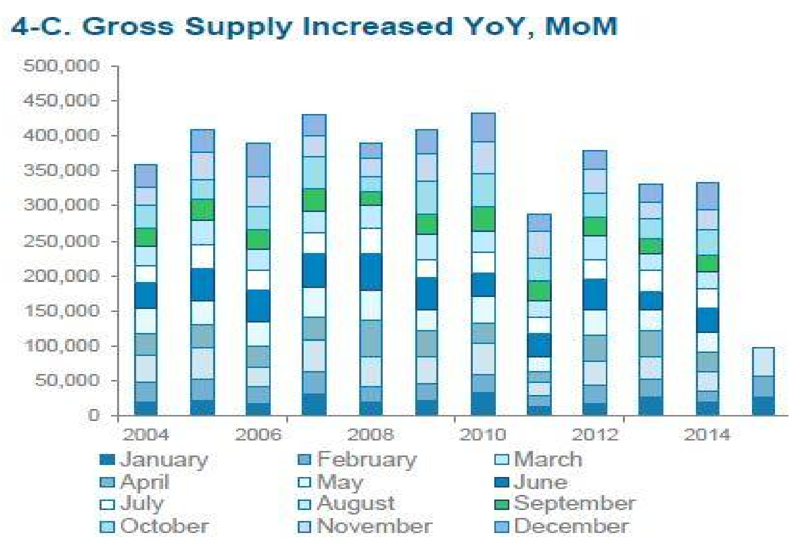
Here is the 10 year Treasury yield for the quarter:

Here is a valuation measure over the long term. Higher values indicate times when munis are cheap to Treasurys. It shows munis more attractive than some previous years, but not as attractive as this time last year. <u>As a result, we have lowered our leverage, and are emphasizing short-term trading to take advantage of the new issue calendar.</u>

The lower chart shows muni new issue volume by month over the last several years. 2015 has started with a bang.

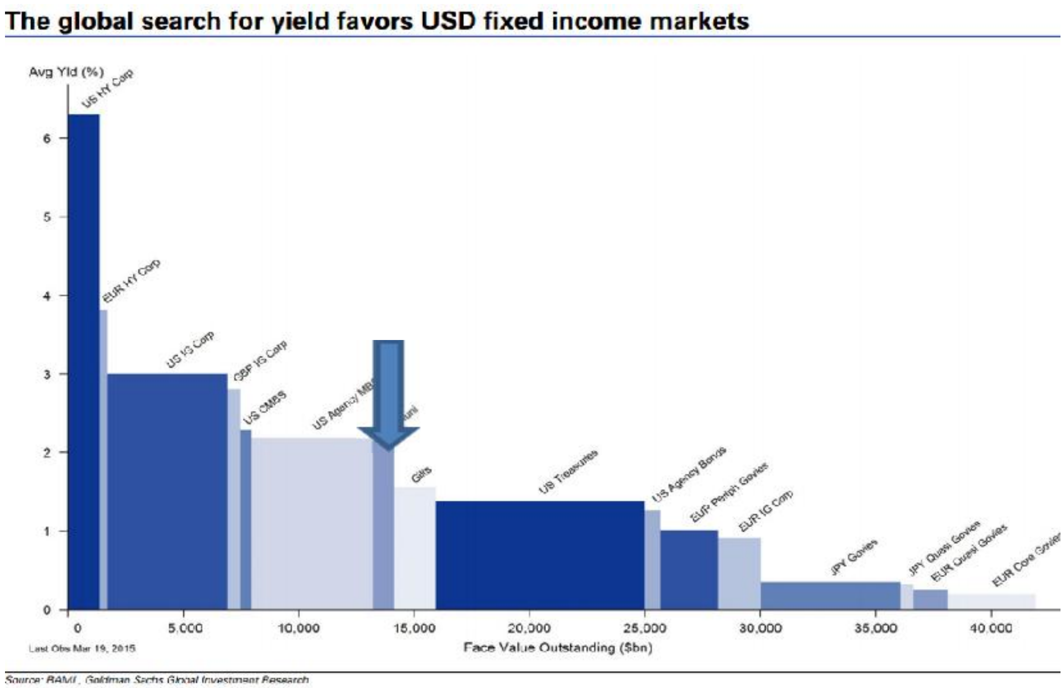
Chart2

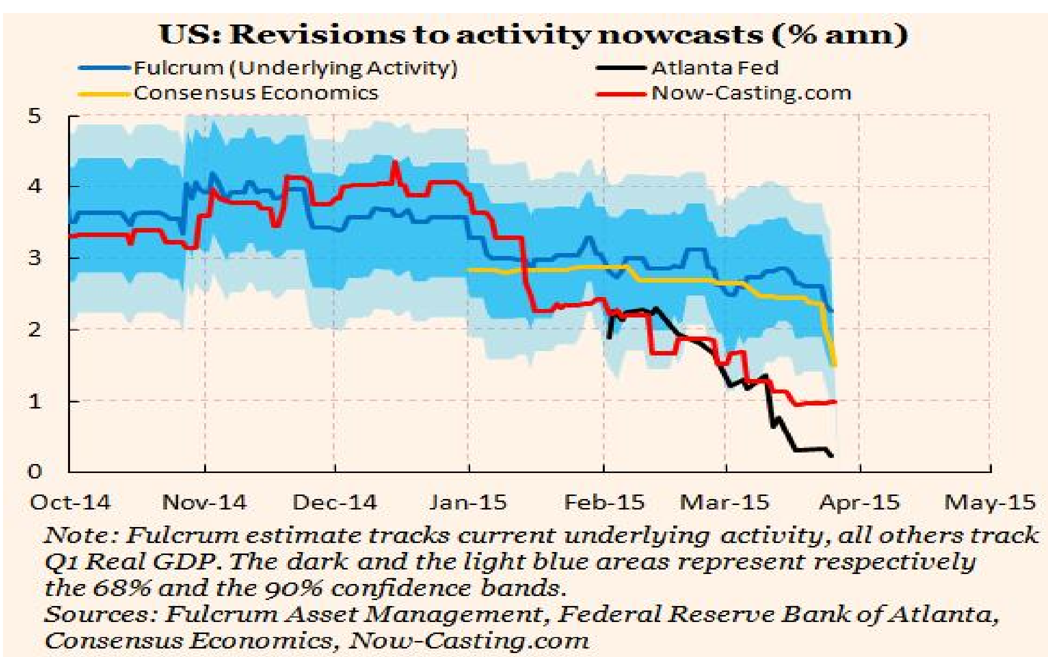




Source: Morgan Stanley Research, Bond Buyer

Look at how U.S. bond markets compare in size to those of Europe and Japan. Notice how small the muni market is compared to the rest of the developed bond markets! But its yield is very competitive. And the economic forecasts keep getting weaker, which would bring yields down even more.





Next, look at how negative yields are spreading around the world. Who would have thought…

The Race to Negative Yields: Global 10-Year Yields (%)				
Country (highlight = all-time low today)	10-year Yield (Jan 1 2014)	10-year Yield (Today)	Difference	All-Time Low in 2015?
SWITZERLAND	1.07	-0.08	-1.15	Yes
GERMANY	1.93	0.21	-1.72	Yes
FINLAND	2.13	0.22	-1.91	Yes
NETHERLANDS	2.23	0.26	-1.98	Yes
AUSTRIA	2.27	0.28	-1.99	Yes
DENMARK	1.98	0.29	-1.69	Yes
JAPAN	0.74	0.42	-0.32	Yes
BELGIUM	2.56	0.43	-2.12	Yes
FRANCE	2.56	0.48	-2.08	Yes
IRELAND	3.51	0.72	-2.79	Yes
SWEDEN	2.50	0.75	-1.76	Yes
ITALY	4.13	1.15	-2.97	Yes
SPAIN	4.15	1.18	-2.97	Yes
HONG KONG	2.31	1.42	-0.89	No
NORWAY	3.00	1.48	-1.53	Yes
CANADA	2.76	1.53	-1.23	Yes
PORTUGAL	6.13	1.66	-4.47	Yes
UNITED KINGDOM	3.02	1.81	-1.21	Yes
UNITED STATES	3.03	2.14	-0.89	No
SOUTH KOREA	3.59	2.32	-1.27	Yes
SINGAPORE	2.56	2.45	-0.11	No
POLAND	4.35	2.46	-1.89	Yes
AUSTRALIA	4.24	2.59	-1.65	Yes
NEW ZEALAND	4.72	3.38	-1.34	Yes
CHINA	4.78	3.53	-1.25	No
PHILLIPPINES	4.12	4.06	-0.06	No
MEXICO	6.45	6.04	-0.40	No
INDIA	8.83	7.76	-1.06	No
INDONESIA	8.45	7.85	-0.61	No
SOUTH AFRICA	7.91	7.90	-0.01	No
GREECE	8.42	10.78	2.36	No
RUSSIA	7.88	12.71	4.82	No
BRAZIL	13.26	13.13	-0.12	No

Pension Partners
THE ATAC ROTATION MANAGER

The other part of valuation is trade execution, where we excel. Here is what Nuveen had to say:

TWEET OF THE DAY BY KATE SMITH

Pricing Inefficiency Leaves Mom and Pop in the Dust

Nuv Nuveen Investments @NuveenInv

.@NuveenAssetMgmt: In a low yield environment, pricing matters when it comes to trading muni bonds. #muniland ow.ly/JPBhe
Details

A lack of a central marketplace for municipal trading can leave retail investors at a disadvantage compared to their institutional counterparts, tweeted Nuveen Investments quoting a report from its Asset Management arm.

Note that A.H. Williams & Co. <u>is</u> a fiduciary.

Monday Money Tip: Beware financial advisers who are not fiduciaries

Erin E. Arvedlund, *Inquirer Staff Writer*

Posted: Monday, March 30, 2015, 1:08 AM

The Inquirer

Your stockbroker is not a "fiduciary." What exactly does that mean? Stockbrokers don't always have your best financial interest at heart.

Don't get me wrong: I have friends (and family) who work on Wall Street. And many brokers do right by their clients, i.e. not pushing their firms' own fee-larded products on their investors. They are good people, but they are not fiduciaries. Before you sign on with a money manager, ask: Are you a fiduciary? If yes, great. If not, go in with your eyes open.

Fiduciaries, by law, have to do the right thing by their clients. No one on Wall Street wants, by law, to have to do the right thing. Some street professionals are fiduciaries; registered investment advisers generally are, brokers are not.

And the distinction grows every day. Anyone whose job is to raise sales cannot meet the fiduciary standard, notes Knut Rostad, president of the Institute for the Fiduciary Standard.

"Brokers may provide useful product recommendations, but they cannot meet the fiduciary standard," Rostad says.

"They can no more provide objective advice about investments than can the Ford car salesman objectively advise on cars. They may be terrific people but, by virtue of what they do, they will most assuredly provide terrible advice."

The issue is confusing, and Wall Street wants to keep it that way.

Plaintiffs' lawyers last week noted that nine U.S. brokerage firms - Merrill Lynch, Fidelity Investments, Ameriprise Financial, Wells Fargo, Morgan Stanley, Allstate Financial, UBS, Berthel Fisher, and Charles Schwab - "advertise in public as though they are trusted fiduciaries acting in the best interest of investors and then deny in nonpublic arbitration cases that they have any such duty to avoid conflicted advice."

The Public Investors Arbitration Bar Association report is available online at www.piaba.org.

"Investors believe they are doing business with individuals they can trust . . .. Yet when that trust is breached, these same firms disclaim liability when held to account in arbitration, and rely on case law to say no such duty exists," wrote co-author Christine Lazaro, director of the Securities Arbitration Clinic at St. John's University School of Law.

One example the report cited is Ameriprise Financial.

This firm advertised: "*Once you've identified your dreams and goals, and you and the advisor have decided to work together, you can count on sound recommendations that address your goals. Our advisors are ethically obligated to act with your best interests at heart.*"

However, in a recent arbitration proceeding with a real investor, the firm stated: "Respondent owed no fiduciary duties to claimants and, even if it did, no such duties were breached.

Finally, we love to see contrasts between states, and this is good for a laugh. It shows highest frequency of Google searches by state for "What does ____ cost?" Not a good sign for New Jersey…

Commentary from independent sources follows. Thank you for your business!

- Traders Seeing Treasury Yields Too Low Belied by Surprise Index
- 2015-02-19 12:58:55.578 GMT
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- By Wes Goodman and Lucy Meakin
- (Bloomberg) -- Investors who say yields are too low, given what's happening in the U.S. economy, should look at the Citi Economic Surprise Index.
- It shows U.S. economic data are failing to meet expectations by the most in 2 1/2 years. The figure gels with a Federal Reserve statement Wednesday signaling policy makers'
- willingness to keep interest rates low for longer, given risks to the economy ranging from a stronger dollar to wages and housing.
- "Data undershooting people's expectations can help keep a lid on yields," said Peter Jolly, the Sydney-based head of market research at National Australia Bank Ltd., the nation's largest lender by assets. "Though it's surprising to the downside, it's not like it's collapsing."
- The U.S. 10-year yield was little changed at 2.08 percent as of 7:55 a.m. New York time, according to Bloomberg Bond Trader data. The price of the 2 percent note due in February
- 2025 was 99 9/32.
- Treasuries were also supported as oil fell for a second day in the U.S. The price of West Texas Intermediate crude for March delivery dropped as much as 4.6 percent to $49.73 a barrel in electronic trading on the New York Mercantile Exchange. It recovered to $50.07, down 4 percent.
- Bond bears who predict a pickup in U.S. growth have pushed yields up from January's low of 1.64 percent.
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- Fed Minutes
-
- U.S. government debt has plunged 2.1 percent in February, headed for its worst month in five years, Bank of America Merrill Lynch indexes show.
- Ten-year yields are still less than the average of 3.28 percent for the past decade. They may rise to 2.5 percent by Dec. 31, National Australia's Jolly said.
- Many Fed officials "indicated that their assessment of the balance of risks associated with the timing of the beginning of policy normalization had inclined them toward" keeping rates near zero "for a longer time," according to minutes of the Jan. 27-28 policy meeting.
- Investors are looking to congressional testimony next week by Fed Chair Janet Yellen for signs as to the timing of a rate increase.
- Policy makers will raise borrowing costs in about 6 1/2 months, a Morgan Stanley index shows.
- The Fed may not wait that long, said Tony Crescenzi, a market strategist at Pacific Investment Management Co. based in Newport Beach, California.
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- Rate Expectations
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- U.S. economic growth will be in the high 2 percent area, which will help reduce unemployment, he said Wednesday on Bloomberg Television.
- "June is still live as a date for the Fed to move,"
- Crescenzi said. "The job story has been good. That's the precondition for a hike."
- Reports over the past month on durable goods orders, gross domestic product, factory orders and retail sales all failed to meet economists' expectations.
- The minutes highlighted concern that inflation remains too low. A gauge of expectations for inflation starting five years from now, based on Treasury securities, dropped to as low as
- 1.75 percent last month, data compiled by the Fed show.
- The U.S. Treasury will auction $9 billion of 30-year inflation linked securities later Thursday. A sale of the bonds on Oct. 23 received the highest demand on record from a group of investors that includes foreign central banks. The TIPS yielded
- 0.985 percent.
-
- Jobs Data
-
- The outlier in last month's data was the monthly employment data that showed payrolls rose more than forecast in January, capping the strongest three months of jobs growth in 17 years.
- The report was on Feb. 6, after the Fed's January policy meeting.
- "The Fed, as eager as they are to raise interest rates, are highly suspect at doing so prematurely," said Mark Luschini, the president of Janney Capital Management, which is based in Pittsburgh. "There is a majority of members who host a fear that doing so prematurely may either choke off the recovery they've worked so hard to sustain, or secondly, that they might have to turn around and cut," he said Wednesday on Bloomberg Television.
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- Record ETF Flows Persist Amid Warning ’15 Will Hurt: Muni Credit
- 2015-03-05 15:23:08.158 GMT
-
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- (For more credit-market news, click on TOP CM. For Municipal Credit Markets column alerts, see SALT MUNCREDIT.)
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- By Michelle Kaske
- (Bloomberg) -- Investors are pouring a record amount of money into exchange-traded funds that focus on municipal debt even as the consensus on Wall Street calls for higher interest rates in coming months.
- Individuals this year have added about $1 billion to ETFs that purchase state and local bonds, the fastest annual start since the funds started in 2007, according to data compiled by Bloomberg. The investment tools, which typically track indexes and can be bought and sold during the trading day, have taken on a growing role for muni investors, almost doubling in assets since 2010.
- With local-government finances improving five years after the recession and the top federal income-tax rates the highest since 2000, investors are increasingly turning to ETFs as a way into the tax-exempt market. The 2015 inflow underscores that investors aren’t shying away from munis in the face of projections that the Federal Reserve will lift its benchmark interest rate from near zero, where it’s been since 2008.
- They “have heard this cry-wolf call for so long,” said Vikram Rai, a municipal analyst at Citigroup Inc. in New York.
- “They’ve become a little jaded towards it.”
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- 2014 Lure
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- The $3.5 trillion municipal market is coming off its strongest year since 2011, after posting a 9.8 percent return in 2014, according to Bank of America Merrill Lynch data. That performance may be luring investors, said Tom Doe, president of Concord, Massachusetts-based Municipal Market Analytics.
- “Individual investors who predominately use the ETFs through their registered investment advisers are chasing last year’s phenomenal returns,” Doe said.
- Munis may not repeat their 2014 earnings as states and localities increase borrowings with interest rates close to 50- year lows, Doe said. Municipal securities have gained about 0.5 percent in 2015, the worst start to a year since 2011, according to Bank of America data.
- About a third of the added cash has flowed into the largest muni ETF, the $4.5 billion iShares National AMT-Free Muni Bond ETF, known as MUB. The ETF traded Thursday at about $109.90 per share, close to the lowest since December.
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- Issuance Swing
-
- Issuers from Washington to New York sold $62 billion of fixed-rate, long-term debt in the first two months of the year, almost double the $32.1 billion tally for the same period in 2014.
- Bond investors face another headwind as a growing economy spurs bets that the Fed will increase its target rate as soon as July, according to the median forecast of 39 analysts surveyed by Bloomberg.
- Treasury yields may head higher too. Interest rates on 30- year federal debt will probably reach 3.38 percent in the first quarter of 2016, from about 2.7 percent now, a separate poll shows.
- That shift in yields may reverse ETF inflows, said Bart Mosley, co-president of Trident Municipal Research in New York.
- Investors may pull money from muni ETFs depending on how high interest rates rise, he said.
- “As soon as they start to see last year’s gains get challenged, people will become a lot more cautious on bonds fairly quickly,” Mosley said.
- A reversal may not diminish the role of ETFs in the tax- exempt market.
- Investors held $13.4 billion in muni ETFs as of Sept. 30, up from $7.6 billion at the end of 2010, according to Fed data.
- In comparison, muni mutual fund assets climbed about 23 percent in that period, to $645 billion.
- “It’s hard to source bonds,” Citigroup’s Rai said. “So this is a quick way of investing your money into munis.”
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A.H. Williams

1650 Market Street
53rd Floor
Philadelphia, Pa 19103
215-569-9800
www.ahwilliamsco.com

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