Invesco Fixed Income

Global Fixed Income Strategy

March 29, 2016

March takeaways

- Credit downgrades among several higher quality energy companies recently surprised markets. However, they may drive a positive shift in corporate behavior, largely to the benefit of creditors. (page 8)
- We believe certain European bank contingent convertibles (CoCos) still offer opportunities. Recent European Central Bank (ECB) actions may provide further support. (page 10)
- Recent central bank actions may also have helped alleviate concerns that tightening global financial conditions could stall economic recoveries and heighten market volatility.

Global macro strategy

Federal Reserve (Fed) coasts as ECB and China accelerate

Central banks around the world appear to have noticed the signs that financial conditions have tightened. Policy makers in the US, Europe and China seem to have set course accordingly to avoid risking a collision with markets or putting the brakes on fragile economic recoveries.

Financial conditions a rising source of concern

Last month we asked whether US financial conditions were too tight and if they posed a risk to our constructive US growth outlook. Declining equity prices, widening credit spreads and increased financial market volatility had indicated that financial conditions had tightened in the US. We have held that tightening financial conditions could derail positive US economic performance, especially via the consumption channel.

By examining three major sources of financing, capital markets debt, equity and bank loans, we determined that US financial conditions – while tighter in recent months – are generally healthy and do not pose a risk to US economic momentum. Last month we noted that, "As growth expectations stabilize, we believe Fed policy makers will modulate the expected path of interest rate hikes to provide stability to credit spreads and market volatility." We believe the Fed's March decision to keep policy rates on hold ratifies that expectation and suggests that recent tightening in financial conditions has been taken into account in the Fed's overall tightening cycle.

Fed reads the signs

The result of the March Federal Open Market Committee (FOMC) meeting indicates that the Fed is placing greater weight on financial conditions than it has in previous meetings. The FOMC's March statement was not downbeat on domestic growth and inflation but it did little to acknowledge recent data points that indicate moderate growth and firming inflation. In our view, this underscores that the committee continues to see risks coming from the global economy and volatile financial markets. The March statement suggests that the Fed is going to give the economy some additional time to generate growth and inflation before it begins to hike interest rates again.

Go to The Bottom Line

We speak with the Global Liquidity team about the possibility (low) of negative interest rate policy in the US.

Page 12

ECB accelerates efforts

The ECB has also been actively easing financial conditions in Europe. The central bank announced a range of new measures this month to help boost struggling eurozone growth and push inflation closer to its 2% target over the medium term (about a two-year timeframe). Markets were pleasantly surprised by the inclusion of corporate bonds in the bank's bond purchasing program (QE) and the forward guidance that its deposit rates will likely stay very low beyond the end of QE – and could go lower.

China aims to ease policy while keeping currency stable

In addition, the Chinese authorities have been easing financial conditions through multiple channels. The primary challenge for Chinese policy is how to manage its monetary, fiscal and currency policy in the face of slowing growth. Because China's currency is roughly pegged to the US dollar, its monetary policy is effectively tied to monetary policy in the US. By tightening capital controls, the Chinese have increased their ability to pursue an independent monetary policy. The Chinese authorities have, so far, been able to use this policy freedom to ease monetary and fiscal policy without causing significant depreciation in their currency.

Implications for bond investors

The combination of these three major central bank policy actions has helped reverse some of the tightening in global financial conditions. With easier financial conditions and the reduced risk of a depreciation-driven financial shock from China, we believe global financial markets may be able to stabilize and return to valuations more aligned with current economic and credit fundamentals.

With the Fed on hold and the ECB targeting easing measures more directed toward credit easing and less toward euro depreciation, we believe US dollar strength is likely to be muted going forward. A pause in the US dollar may help alleviate corporate earnings concerns for US-based companies, while also providing support to emerging market currencies. Overall, we believe this policy backdrop is positive for risky credit assets and a benign backdrop for developed market growth.

Robert Waldner, Chief Strategist, James Ong, Senior Macro Strategist

Interest rate outlook

US: The FOMC has shown increasing concern about global developments and tightening financial conditions against a backdrop of modest US growth and firming inflation. This has been positive for US interest rates across the yield curve. We expect US growth to continue at a moderate pace and inflation to remain firm. If the US economic situation evolves as we expect, the US yield curve may steepen as inflation risk rises. We believe this inflation dynamic is likely to benefit inflation-protected bonds (TIPS) relative to nominal US Treasury securities.

Europe: The ECB acted in March to combat tightening financial conditions by cutting deposit rates, increasing asset purchases and introducing new long-term financing programs (LTROs). ECB President Draghi hinted there would be no more deposit rate cuts - an important change in tack. This means banks are now being supported in their lending by the new LTROs rather than punished with even more negative deposit rates. The impact on growth is uncertain, however, as credit demand remains a big problem. Overall, we expect the impact of the ECB's actions to be limited given that overall risk sentiment (driven by developments in the US and China) is the key driver. We expect the 10-year bund yield to move higher from its current level of around 0.2%.[1]

China: China has further loosened its fiscal and monetary policies, as we anticipated. The government projects a higher 2016 budget deficit and has cut the required reserve ratio for commercial banks. There are budding signs of reflation in China as indicated by the robust housing market, and we expect producer price deflation to subside. We expect the Chinese government yield curve to steepen as reflationary policies intensify. On February 24, the Chinese authorities announced the opening of the onshore interbank renminbi bond market to medium and long-term investors without quotas. Once the details of the new policy are clarified, we expect more foreign capital to flow into this market.

Japan: The Bank of Japan (BoJ) hopes its recently implemented negative interest rate policy will stimulate expansion in capital spending and housing investment, but the impact is uncertain. Inflation continues to come in below expectations and, with inflation expectations declining, the BoJ is likely to ease further to minimize the chances of the deflationary mindset setting back in. The April or July meetings are the most likely timing for such easing, given that these meetings coincide with updates to both growth and inflation forecasts. Longer maturity Japanese government bonds are likely to be the biggest beneficiary, given that they are the only part of the curve offering positive yields.

UK: Expectations of Bank of England interest rate hikes have been pushed out meaningfully since the start of the year. We are unlikely to see significant change in these expectations until after the European Union (EU) referendum has been held (June 23). Gilts could come under pressure (foreign selling) in the run-up to the event, but we would expect any sell-off to be limited, given that domestic equity holders are likely to switch asset classes (into gilts) on the back of heightened uncertainty. The UK economy continues to experience relatively strong, albeit unspectacular, levels of growth and we would expect that to continue over the coming quarters, providing the country opts to stay within the EU.

Canada: Higher commodity prices will likely help stabilize Canada's structurally weak economy. Unfortunately, higher commodity prices have been accompanied by appreciation of the Canadian dollar from its January lows. Without a weaker currency, net trade will likely fail to contribute positively and the consumer will remain limited due to high debt burdens. Weak domestic demand and a resurgence in the Canadian dollar will likely cap core inflation, providing support for the longer end of the government yield curve. We expect 10-year Canadian government bond yields to trade in a range of 1-1.8% in 2016.

Australia: Expectations of Australian central bank (RBA) easing declined significantly after a jump in iron ore prices and a strong 2015 GDP report. This interest rate re-pricing put Australian bonds under pressure. However we believe the outlook for Australian bonds going forward is much brighter as the recent strength in the Australian dollar and surprisingly dovish March FOMC meeting will likely put pressure on the RBA to ease and guide policy expectations lower, thus supporting Australian bonds.

Rob Waldner, Chief Strategist, James Ong, Senior Macro Strategist, Nick Wall, Portfolio Manager, Sean Connery, Portfolio Manager, Avi Hooper, Senior Portfolio Manager, Josef Portelli, Portfolio Manager,
Ken Hu, CIO Asia Pacific

1 Source: Bloomberg L.P., as of March 18, 2016.

Currency outlook

USD: Monetary policy divergence has paused, as the Fed relents on its tightening bias and global central banks target easing measures other than those aimed at currency weakness. Although we continue to expect the US to fundamentally diverge from the rest of the world, US dollar strength will likely continue to be challenged until strength in economic data forces the market to price in further interest rate hikes.

EUR: We remain on the sidelines regarding the euro, but acknowledge the near-term risk for upside pressure in the aftermath of a less currency-focused ECB and optimally controlled Fed (approach to monetary policy that involves choosing the interest rate path that generates the best outcome for inflation and unemployment). The macro risk environment remains challenging, as structural economic headwinds battle cyclical policy tailwinds. There are easier currency trades to implement, in our view, than the euro following the ECB credit easing announcement and March Fed decision to stay on hold, and that is where we are focusing our risk budget.

JPY: The Japanese yen has appreciated since the start of the year, despite the introduction of negative interest rate policy by the BoJ at its January meeting. This, along with disappointing spring wage negotiations and a less hawkish Fed, are likely to lead to additional easing by the BoJ, sooner rather than later, as it continues its efforts to get inflation back on target. We would expect the yen to trade in a 110-115 range versus the US dollar over the shorter term, as increased expectations for further easing are offset by a decline in global risk sentiment.

GBP: We have recently moved overweight sterling, on the basis that short positioning appears to be nearing record highs, we expect the UK referendum to result in a "remain" outcome, and UK interest rate hike expectations have been pushed out very far (although prone to a correction, especially if the UK votes to remain in the EU). The primary risk to the trade is an increased appetite for the UK to leave the EU, while a general decrease in global risk sentiment would also likely create headwinds.

CAD: The Canadian dollar has benefited heavily from higher oil prices and a stall in the Fed's hiking cycle. However, the Bank of Canada may opt to cut interest rates to help stem currency strength. The balance of payments remains vulnerable as domestic capital searches for higher investment returns in global markets. We have limited currency risk in our domestic strategies, but continue to position for Canadian dollar underperformance against the more competitively priced Mexican peso.

AUD: Expectations of RBA easing were toned down significantly after a jump in iron ore prices and strong 2015 growth data. These developments, plus a positive risk backdrop, have helped the Australian dollar. However, we believe the outlook for the Australian dollar is limited since the recent strength in the AUD/USD exchange rate and surprisingly dovish March FOMC will likely put pressure on the RBA to ease and drive policy expectations lower. This will likely cause the currency to decline, but would be good for the economy since a weak Australian dollar is one of the key factors needed to help rebalance the domestic economy.

Ray Uy, Head of Macro Research and Global Multi-Sector Portfolio Management, James Ong, Senior Macro Strategist, Avi Hooper, Senior Portfolio Manager, Sean Connery, Portfolio Manager, Josef Portelli, Portfolio Manager

Global investment themes

This section highlights the key themes driving Invesco Fixed Income's global macro and credit research process and views. Themes are updated based on evolving trends and expectations.

Global macro themes

Global convergence: Market risks decreasing

Rationale

A dovish Fed, no more rate cuts from the ECB and China easing combined with capital controls should help support USD stability.

IFI strategy

We favor playing the current risk-on rally tactically as concerns remain over China and EM growth dynamics. We believe reducing credit risk into the rally is appropriate.

Asian deflation

Rationale

Slowing growth in China continues to put pressure on Asian economies. We expect growing inflation and policy differentials to put pressure on Asian currencies.

IFI strategy

Allocations to currency and interest rate risk remain at the low end of the range. Seek to add JPY exposure on weakness as a strategy hedge.

Global credit themes

Geographical themes

Investment grade (IG): Global energy and metals rebound, cycle differences remain

Rationale: Europe at earlier stage of credit cycle. ECB QE provides tailwind, supporting valuations. Asia benefits from lower supply expectations. US valuations may offer more yield, but reflect rising fundamental and supply pressure.

IFI strategy: Favor gaining exposure to select higher quality issuers in energy and metals sectors where shorter-term maturities are well covered by liquid assets.

Emerging markets (EM): Stabilization in commodities

Rationale: Still in EM bear market, in our view, however seeing stabilization in commodity markets- USD30 oil is key level to hold. Global deflationary pressures to persist with weaker EM growth impulses going forward. Idiosyncratic risks remain high. Earnings rebound continually delayed.

IFI strategy: Prefer to add risk through high conviction views, not high-beta exposure. Keeping China beta low.

US commercial mortgage backed securities (US CMBS): Macroeconomic volatility headwind

Rationale: Despite positive fundamentals, expect heightened near-term macroeconomic volatility to limit the potential for credit spread tightening. Cautious on exposures in energy sensitive regions. Dwindling supply creating good technicals.

IFI strategy: Remain negative on recent vintage subordinate tranches. Prefer seasoned US CMBS as cycle progresses. Credit differentiation is accelerating, placing premium on selection.

US residential mortgage backed securities (US RMBS): Valuations stretched, liquidity inconsistent, favorable fundamentals

Rationale: Legacy non-agency RMBS may underperform other credit markets as investors see better relative value in sectors that have experienced more widening. Liquidity remains inconsistent. Market remains sensitive to supply.

IFI strategy: Prefer higher quality legacy prime, alt-A, seasoned credit risk transfer, 2014-early 2015 vintages. Favor avoiding sub-prime, option adjustable rate mortgages.

Global investment themes continued

US asset backed securities (US ABS): Value in subordination

Rationale: US ABS has been less volatile versus US IG. Fundamentals are strong but modestly weaker as collateral performance has moved off of historical low delinquency and loss levels. Technicals benign.

IFI strategy: Prefer adding exposure to subordinate tranches where collateral performance remains stable. Lower volatility AAA attractive, in our view. Believe senior auto ABS and esoteric issuers can provide opportunities. Favor avoiding deep subprime auto ABS.

Sector themes

Commodities: Global rebound in energy, metals

Rationale: Expect slightly better risk premiums in global IG credit in next quarter as market digests transition of energy and metals credits to high yield. Expect elevated issuance to pressure valuations while fundamental credit quality concerns remain due to modest economic growth.

IFI strategy: Favor gaining exposure to select higher quality issuers in energy and metals sectors where shorter-term maturities are well covered by liquid assets.

Consumer story more nuanced globally

Rationale: Solid US labor market and low gas prices are supportive, but consumers more value-conscious and international retail demand deteriorating, due partly to strong US dollar.

IFI strategy: Favor select US consumer sectors including autos, restaurants, leisure and housing-related sectors. Negative on "big box" retailers that lack differentiated products.

Post-merger and acquisitions (M&A) deleveraging plays

Rationale: M&A activity at post-recession high, driven by large cash balances, low all-in financing cost, lack of organic growth, and need to reposition business portfolios.

IFI strategy: Preference to play post-transaction bond issuance, typically characterized by size, liquidity, concessions and plans to deleverage. Due to rise in M&A related issuance, believe more discriminating approach to this strategy now warranted.

Global technology – big data

Rationale: Global use of data expected to further expand and transition to cloud-based platforms.

IFI strategy: Prefer to gain exposure to software and services, cell towers and select wireless issuers. Avoiding hardware original equipment manufacturer issuers.

Yield curve themes

Credit curve positioning, expecting flattener

Rationale: Zero interest rate policy globally has forced cash investors and sovereign wealth funds into 3-5 year part of the credit yield curve, creating steep 5-7 year part of the curve. As Fed normalizes policy and money market rates become more attractive, expect some outflows from 1-3 year part of the curve into money market funds, but expect demand for 5-year paper to be resilient.

IFI strategy: Prefer 7-10 and select 30-year points on US IG credit yield curve. New issuance at longer maturities comes at healthy concessions.

Rob Waldner, Chief Strategist, Ray Uy, Head of Macro Research and Global Multi-Sector Portfolio Management, Tony Wong, Head of Global Research, Joe Portera, Head of Global High Income, Michael Hyman, Head of Investment Grade

Global sector strategy

US investment grade

Cautious on energy credit as commodity price volatility persists

Rating downgrades punish energy sector

Several highly punitive credit downgrades of higher quality energy companies surprised the investment grade bond market recently, with some downgrades representing cuts of four-to-five notches. We believe there may be a silver lining to these downgrades, however. Together with low commodity prices, these moves may be driving a positive shift toward more prudent corporate balance sheet management, largely in favor of creditors. While commodity price volatility, challenged oil market fundamentals (supply in excess of demand) and broader macroeconomic uncertainty cause us to be very cautious about investing in energy-related credit, we believe such volatility and change in corporate behavior may create unique opportunities for active investment managers.

Fundamental crude outlook downgraded, but companies have responded positively

Forward commodity price assumptions are key inputs in the credit rating process of many energy-related companies. Following OPEC's decision to leave currently elevated production levels in place at its December meeting (rather than agreeing to any form of production freeze or reduction), crude prices have remained volatile in 2016. Rating agencies have accordingly lowered their forward commodity price assumptions under the view that oil price weakness could persist for an extended period of time. These price assumption revisions have resulted in meaningful credit rating downgrades.

We believe that certain rating agencies have taken the view that depressed commodity prices may have severely compromised the energy industry's cash flow generative capacity. Historically, many energy companies have relied on access to public debt and equity markets to help fund growth and operations. If a company anticipated generating negative cash flow given large capital expenditure requirements, it could typically fully or partially offset this with public debt or equity issuance. However, with capital markets remaining highly volatile during recent months, many energy companies have generated negative cash flow in the absence of full debt and equity market access.

While this funding gap has proven highly negative from a ratings standpoint, the silver lining is that it has forced reductions in both operating and capital spending to better align operating cash flow with capital expenditures throughout the industry. When combined with rating agency downgrade risk, the result is an ongoing shift in industry-wide balance sheet and cash flow management, largely to the ultimate benefit of bondholders, in our view.

Commodity weakness and ratings downgrades spur renewed balance sheet focus

As industry-wide cost structure rationalization continues, we expect companies to remain keenly focused on (i) targeting breakeven cash flow at depressed commodity prices (exclusive of capital market access), and (ii) reducing balance sheet and cash flow risk via dividend reductions, asset sales, equity offerings, etc. We have recently seen a number of companies execute on various balance sheet-oriented corporate actions, including equity offerings, asset monetizations, reductions in capital spending programs, tender offers and dividend reductions or eliminations and we expect this behavior to continue.

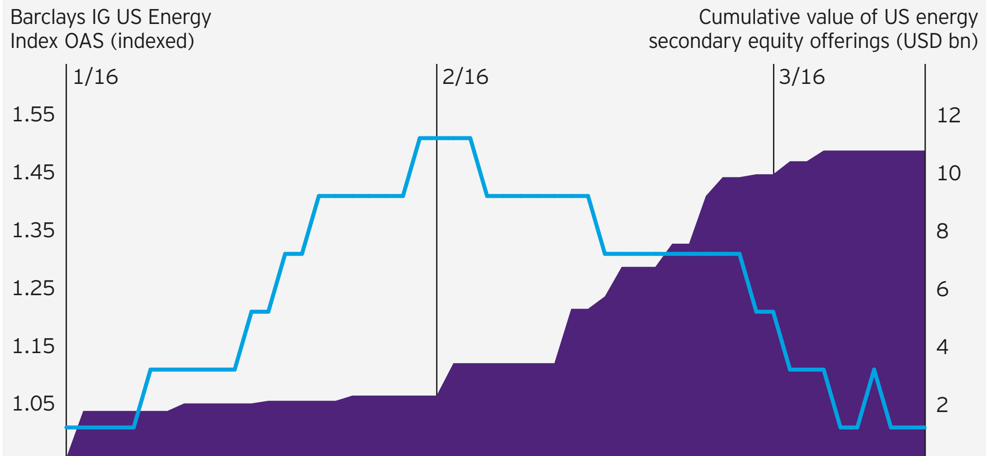
Remaining nimble, disciplined and opportunistic while cautiously awaiting industry recovery

Given a renewed focus by management teams on maintaining healthy balance sheets, we anticipate further creditor-friendly corporate activity. As energy balance sheets continue through the de-risking process, downside creditor protection should be further enhanced, in our view – a key requirement of our highly selective investment process. While we remain highly cautious and selective in the near term, it is encouraging to see a focus on balance sheet strengthening from management teams across the industry. We continue awaiting further improvement in crude market fundamentals, but we believe the ongoing balance sheet preservation trend will potentially provide unique investment opportunities for selective and risk-averse, value-oriented credit investors in the volatile commodity price environment.

We remain highly focused on selectively evaluating the volatile energy landscape in search of investment opportunities that exhibit a few key investment attributes; (i) attractive downside protection afforded through favorable competitive and/or operating characteristics, (ii) strong near-term liquidity, (iii) identifiable positive catalysts and (iv) attractive risk-adjusted return potential.

Increasing US energy equity issuance coincides with credit spread volatility and elevated credit stress

- Cumulative secondary US energy equity offerings
- Barclays IG US Energy Index OAS (Dec. 31, 2015 =1)



Source: Barclays, Bloomberg L.P., data from Dec. 31, 2014 to March 17, 2016. OAS is option adjusted spread.

Bixby Stewart, Analyst

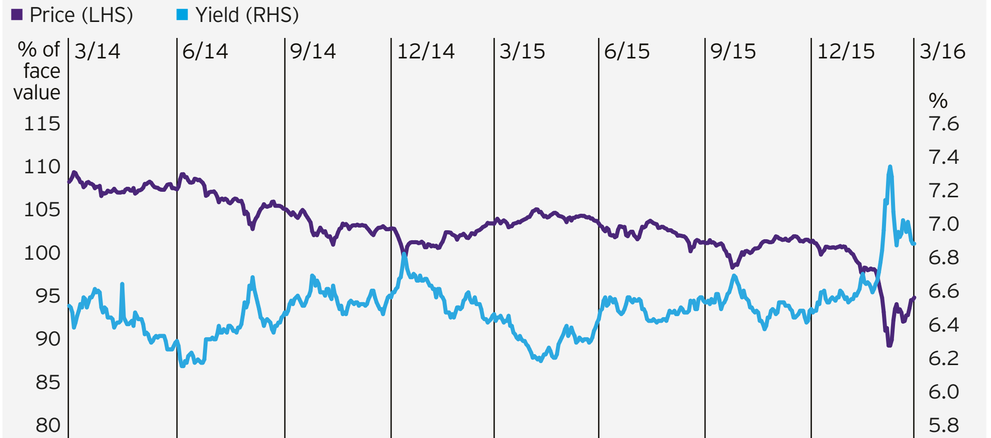
European investment grade

Certain European Bank CoCos Still Offer Opportunities

Recent ECB actions provide further support for AT1 securities

European banks' contingent convertible (CoCo) junior subordinated Additional Tier 1 (AT1) securities – the junior subordinated subset of the CoCo family – suffered a significant sell-off in January and February from which they have only partly recovered. However, Invesco Fixed Income believes the investment thesis for this asset class remains intact, especially following the European Central Bank's (ECB) constructive actions announced on March 10.

CoCos are up but still some way from their highs



Source: Bloomberg L.P., Bank of America Merrill Lynch Contingent Capital Index, data from March 3, 2014 to March 9, 2016.

Possible causes of the recent weakness in European bank assets include the restructuring of four small second and third tier Italian banks last year, the weak macro backdrop around the world (which led to fears of further declines in interest rates to negative territory), and the worry that the UK could vote to leave the EU in a referendum.

However, we believe the fundamental balance sheet strength of European banks is at a multi-year high – with solid capitalization, liquidity and asset quality – with only some specific exceptions. While profitability has remained under pressure as a result of weak economic activity, most banks do remain profitable. Moreover, the equity market's very positive reaction to the ECB's March 10 announcement, which instituted new cheap financing lines for banks, suggests negative rate concerns have diminished. At the same time, banks can do more to reduce costs and provisions.

Global sector strategy continued

European banks' junior subordinated AT1 securities have a number of equity-like features that increase their riskiness. However, most, if not all, remain likely to be called at their call date — if not for economic reasons then to maintain the issuing bank's reputation with fixed income investors whose support will continue to be required for future funding needs. Write-downs or conversion to equity is a vanishingly remote possibility, in our view, due to the very high buffers to the relevant capitalization triggers. In most cases, issuers also boast reasonably high buffers above the coupon suspension triggers, and in any case regulators are thinking of allowing coupon payments to have priority over the usually much larger dividend payments, further supporting valuations.

The ECB's announcement on March 10, which included a deposit rate cut but also measures to offer banks cheap ECB funding, caused equities and AT1 bonds to rally, the latter by about 2 points [1] in price across the board. However, with the most solid Swedish, Swiss and Dutch names still yielding in the 6% to 7% range[1], we believe there are still attractive investment opportunities.

Ian Centis, Senior Analyst

1 Source: Bloomberg L.P., as of March 10, 2016

Laurie Brignac,
Head of Global Liquidity Portfolio Management

Laurie is responsible for providing senior management oversight of liquidity products in the US, EMEA and Asia Pacific Regions. Ms. Brignac has served as a member of the Tri-Party Repo Infrastructure Reform Task Force and participates in various industry committees in the US and globally.

Marques Mercier,
Head of Government Global Liquidity

Marques is responsible for the management of all cash management products, including institutional, retail and offshore money market funds, as well as private accounts.

The Bottom Line

We speak with Laurie Brignac, Head of Global Liquidity Portfolio Management and Marques Mercier, Head of Government Global Liquidity, about why a robust Fed toolbox and uncertain consequences make negative US interest rates unlikely.

Q: What is negative interest rate policy, or "NIRP"?

Laurie: NIRP is an unconventional monetary policy tool that central banks use to discourage banks from holding cash by charging them a negative interest rate on excess reserves, thereby encouraging them to lend money instead. This should lead to increased lending, promoting further spending by businesses and consumers, and lead to economic recovery. Denmark was the first to institute NIRP in July 2012, followed by the ECB, Sweden and Switzerland. The latest central bank to join the fray was Japan at the end of January.

Q: Why has there been speculation that the Fed might implement NIRP in its quest to boost the economy?

Marques: The BoJ's implementation of NIRP certainly put the subject back in the news. At the same time, disappointing US macroeconomic data earlier this year coupled with financial market volatility raised the question of whether the Fed might consider NIRP as a potential monetary policy tool.

Laurie: In fact, the Fed highlighted the concept of negative interest rates in two important policy communications in January: its announcement of scenarios for its 2016 bank stress tests, the Comprehensive Capital Analysis and Review (CCAR), and Fed Chair Yellen's semi-annual testimony to Congress, the Humphrey-Hawkins testimony.

Q: How was the Fed thinking about negative interest rates?

Marques: One of the new scenarios within the CCAR's "severe adverse market shocks" that could negatively impact banks included negative Treasury bill rates (along with other shocks such as an unemployment rate of 10%, heightened corporate financial stress and other dire scenarios). The inclusion of negative Treasury bill rates in the CCAR led to speculation that the Fed might follow the lead of Europe and Japan and implement NIRP in the US. As a result, Fed Chair Janet Yellen was asked about NIRP at her semi-annual testimony to Congress, where she said the Fed does not intend to implement or see the need for NIRP at this time but would not take negative rates off the table as a potential policy option. She further emphasized that negative interest rates are not a preferred tool for stimulating the economy and that "...we have work to do to judge whether they would be workable here," she said.

Q: How likely do you believe NIRP is in the US?

Marques: We believe US economic fundamentals do not justify such a dramatic move. Invesco Fixed Income is calling for US GDP growth of 2.4% in 2016 and year-over-year core inflation (which the Fed watches) of around 2% - nowhere near the conditions necessary to justify NIRP, in our view.

Laurie: Additionally, the Fed has many other tools it can deploy before reverting to such a dramatic interest rate policy, i.e. cut the federal funds rate back to 0%-0.25%, increase QE purchases, redeploy a maturity extension program such as 'Operation Twist', and, of course, they can always use forward guidance to influence interest rates.

Marques: It is also unclear whether US law, specifically the Federal Reserve Act that governs the Fed, permits negative interest rates. The Act gives the Federal Reserve Board a lot of leeway: "The Board is authorized ... to determine what shall be deemed a payment of interest," but we believe Congress and the public may strongly question the official use of negative interest policy.

Q: Assuming that legal hurdles were overcome, what would be the impact of negative interest rates on the US money market?

Laurie: The outcome is uncertain. Many question whether negative interest rates would have their intended effect in the US. With a large and vibrant money market fund industry, the structure of the US money markets is vastly different from those in Europe and Japan. Negative policy rates in the US could be disruptive to the US money markets, potentially creating an arbitrage between retail bank deposits and retail money market funds. This could lead to large asset flows, pushing cash back into the banking system and disrupting the money markets in general, which, in our view, would not be supportive of economic growth as intended.

Recent IFI publications

1. **The UK reconsiders its membership in the European Union,** February 2016, Sean Connery, Portfolio Manager
2. **Investor double-take: US Agency MBS,** December 2015, Rich King, Head of Structured Investments
3. **Invesco Fixed Income: Investor's Summit Outlook November 2015,** December 2015, CEO Greg McGreevey and Chief Strategist Rob Waldner
4. **Understanding the emerging markets credit cycle, Part 1,** December 2015, Rashique Rahman, Head of Emerging Markets, Jay Raol, Analyst
5. **IMF and World Bank annual meetings recap,** October 2015, by Arnab Das, Head of EM Macro, Sean Newman, Senior Portfolio Manager
6. **What are US Commercial Mortgage-Backed Securities (US CMBS)?,** October 2015, by Kevin Collins, Head of CMBS Credit and Daniel Saylor, Senior Analyst
7. **What are GSE Credit Risk Transfer securities?,** October 2015, by David Lyle, Head of RMBS Credit
8. **Structured Convertibles: A Custom Portfolio Solution,** September 2015, by Robert Young, Senior Portfolio Manager

Market monitors

Fixed income market monitor

	Coupon (%)	Yield to worst (%)	1 month change in YTW	Option-adjusted spread current	Option-adjusted spread 1 month change in spread	Option-adjusted spread 10 year range min	Option-adjusted spread 10 year range max	Returns 1 mth (%)	Returns 3 mth (%)	Returns YTD (%)	Returns 12 mth (%)
Global Aggregate (USD hedged)	2.90	1.45	-0.12	57	2	23	156	0.96	2.16	2.44	2.19
U.S. Aggregate	3.17	2.26	-0.08	64	1	32	258	0.71	1.77	2.10	1.50
U.S. Mortgage-backed	3.68	2.35	-0.12	21	-1	-16	181	0.37	1.64	1.68	2.51
Global Inv Grade Corporate (USD hedged)	3.91	2.97	-0.05	188	6	55	515	0.56	0.32	1.02	-1.00
U.S. Investment Grade Corporate	4.23	3.55	-0.07	197	3	76	618	0.81	0.38	1.17	-1.49
Emerging Market USD Sovereign	n/a	6.27	-0.23	454	-9	157	906	1.91	0.30	1.72	1.11
Emerging Market Corporate	n/a	6.16	-0.30	467	-18	120	1,032	1.03	-0.57	0.67	0.13
Global High Yield Corporate (USD hedged)	6.44	8.42	0.00	702	5	231	1,845	0.29	-3.48	-1.09	-6.67
U.S. High Yield Corporate	6.62	9.02	-0.15	726	-7	233	1,971	0.57	-3.54	-1.04	-8.30
Bank Loans	4.80	5.34	0.07	n/a	n/a	n/a	n/a	-0.56	-2.22	-1.28	-3.27
Municipal Bond	4.80	1.90	-0.01	n/a	n/a	n/a	n/a	0.16	2.06	1.35	3.95
High Yield Municipal Bond	5.41	6.64	-0.01	n/a	n/a	n/a	n/a	1.10	1.83	1.67	2.11

Treasury market monitor

	Coupon (%)	Yield to worst (%)	1 month change in YTW	Returns in local currency 1 mth (%)	Returns in local currency 3 mth (%)	Returns in local currency YTD (%)	Returns in local currency 12 mth (%)
United States	2.07	1.33	-0.07	0.89	2.87	3.04	2.88
Canada	2.58	1.01	0.02	0.32	2.50	1.32	1.15
United Kingdom	3.78	1.38	-0.16	1.50	4.19	5.38	5.68
Germany	2.30	-0.12	-0.15	1.55	3.03	4.10	2.32
Italy	3.88	0.95	0.02	0.28	0.69	1.43	1.72
Japan	1.17	0.03	-0.18	1.85	3.94	3.25	5.06
China	3.66	2.84	-0.06	0.60	2.52	0.86	6.64
EM Local Currency Governments	n/a	n/a	n/a	0.65	1.68	2.05	3.55

FX market monitor[1]

	Current	10 year range min	10 year range max	Returns 1 mth (%)	Returns 3 mth (%)	Returns YTD (%)	Returns 12 mth (%)
EURUSD	1.09	1.06	1.60	-0.14%	2.92%	0.10%	-2.88%
USDJPY	112.69	75.82	124.77	7.37%	9.25%	6.71%	6.15%
GBPUSD	1.39	1.38	2.11	-3.58%	-7.57%	-5.56%	-9.85%
USDCNY	6.55	6.04	8.28	0.37%	-2.39%	-0.92%	-4.39%
USDCHF	1.00	0.75	1.39	2.13%	3.05%	0.38%	-4.47%
AUDUSD	0.71	0.60	1.10	0.38%	-1.19%	-1.99%	-8.54%
CADUSD	0.74	0.72	1.09	2.98%	-1.34%	2.17%	-7.65%
EURJPY[2]	122.53	94.31	169.49	7.52%	6.14%	6.62%	9.31%
EURGBP[2]	0.78	0.70	0.84	-3.44%	-10.18%	-5.67%	-7.16%

Sources: Barclays, JPMorgan, Bloomberg L.P., as of Feb. 29, 2016. Credit Suisse Leveraged Loan data as of Feb. 29, 2016.
Within the Treasury monitor, United States is represented by Barclays US Treasury Index; Canada is represented by Barclays Global Treasury Canada Index; United Kingdom is represented by Barclays Sterling Gilts Index; Germany is represented by Barclays Global Treasury Germany Index; Italy is represented by Barclays Global Treasury Italy Index; Japan is represented by Barclays Global Treasury Japan Index; China is represented by Barclays China Aggregate Treasuries Index; EM Local Currency Governments is represented by J.P. Morgan GBI_EM Broad Diversified Index. In the Fixed Income Monitor, Global Aggregate is represented by Barclays Global Aggregate (US$ Hedged) Index; US Aggregate is represented by Barclays US Aggregate Index; US Mortgage-backed is represented by Barclays US Mortgaged-backed Index; Global Investment Grade Corporate is represented by Barclays Global Aggregate Corporate (US$ hedged) Index; U.S. Investment Grade Corporate is represented by Barclays Aggregate Corporate Index; Emerging Market USD Sovereign is represented by the J.P. Morgan EMBI Global Diversified Index; Emerging Market Corporate is represented by J.P. Morgan CEMBI Broad Diversified Index; Global High Yield Corporate is represented by the Barclays Global High Yield Corporate (US$ hedged) Index; U.S. High yield Corporate is represented by Barclays U.S. Corporate High Yield Index; Bank Loans is represented by the Credit Suisse Leveraged Loan Index; Municipal Bond is represented by Barclays Municipal Bond Index; High Yield Municipal Bond is represented by Barclays Municipal Bond High Yield Index.
Yield to Worst (YTW) is the lowest expected yield calculation given maturity and call features. Option Adjusted Spread (OAS) is the yield difference relative to similar maturity Treasuries that incorporates call, put, sinking fund or paydown features of a bond. Past performance cannot guarantee future results. An investment cannot be made directly in an index. Returns less than one year are cumulative.

1 Positive number represents the currency appreciated against USD, negative number represents currency depreciated against USD.
2 Positive number represents the currency appreciated against EUR, negative number represents currency depreciated against EUR.

Invesco's fixed income team contributors

Atlanta

Rob Waldner
Invesco Fixed Income Chief Strategist
+1 404 439 4844
robert.waldner@invesco.com

Ray Uy
Head of Macro Research
+1 404 439 4822
raymund.uy@invesco.com

James Ong
Senior Macro Strategist
+1 404 439 4762
james.ong@invesco.com

Avi Hooper
Senior Portfolio Manager
+1 404 439 4877
avi.hooper@invesco.com

Tony Wong
Head of Global Research
+1 404 439 4825
tony.wong@invesco.com

Joseph Portera
Head of Global High Income
+1 404 439 4814
joseph.portera@invesco.com

Michael Hyman
Head of Investment Grade
+1 404 439 4827
michael.hyman@invesco.com

Laurie Brignac
Head of Global Liquidity Portfolio Management
+1 404 439 4799
Laurie.brignac@invesco.com

Marques Mercier
Head of Government Global Liquidity
+1 404 439 4786
Marques.mercier@invesco.com

Bixby Stewart
Analyst
+1 404 439 4827
Bixby.stewart@invesco.com

Ann Ginsburg
Senior Market Analyst
+1 404 439 4860
ann.ginsburg@invesco.com

Carolyn Gibbs
Senior Strategist
+1 404 439 4848
carolyn.gibbs@invesco.com

London

Sean Connery
Portfolio Manager
+44 20 3219 2714
sean.connery@invesco.com

Nick Wall
Portfolio Manager
+44 20 3219 2724
nicholas.wall@invesco.com

Josef Portelli
Portfolio Manager
+44 20 3219 2709
josef.portelli@invesco.com

Ian Centis
Senior Analyst
+44 20 3219 2730
ian.centis@invesco.com

Hong Kong

Ken Hu
CIO Asia Pacific
+852 3128 6886
ken.hu@invesco.com

Important information

This document is not an offering and is not intended for and should not be distributed to, or relied upon, by members of the public. Circulation, disclosure, or dissemination of all or any part of this document to any unauthorized person is prohibited.

This document may contain statements that are not purely historical in nature but are "forward-looking statements," which are based on certain assumptions of future events. Forward-looking statements are based on information available on the date hereof, and Invesco does not assume any duty to update any forward-looking statement. Actual events may differ from those assumed. There can be no assurance that forward-looking statements, including any projected returns, will materialize or that actual market conditions and/or performance results will not be materially different or worse than those presented.

All material presented is compiled from sources believed to be reliable and current, but accuracy cannot be guaranteed. Investment involves risk. Please review all financial material carefully before investing. The opinions expressed are based on current market conditions and are subject to change without notice. These opinions may differ from those of other Invesco investment professionals.

The distribution and offering of this document in certain jurisdictions may be restricted by law. Persons into whose possession this marketing material may come are required to inform themselves about and to comply with any relevant restrictions. This does not constitute an offer or solicitation by anyone in any jurisdiction in which such an offer is not authorised or to any person to whom it is unlawful to make such an offer or solicitation.

All information is sourced from Invesco, unless otherwise stated. All data as of Feb. 29, 2016, unless otherwise stated. All data is USD, unless otherwise stated.