Taplin, Canida & Habacht

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Fixed income market update

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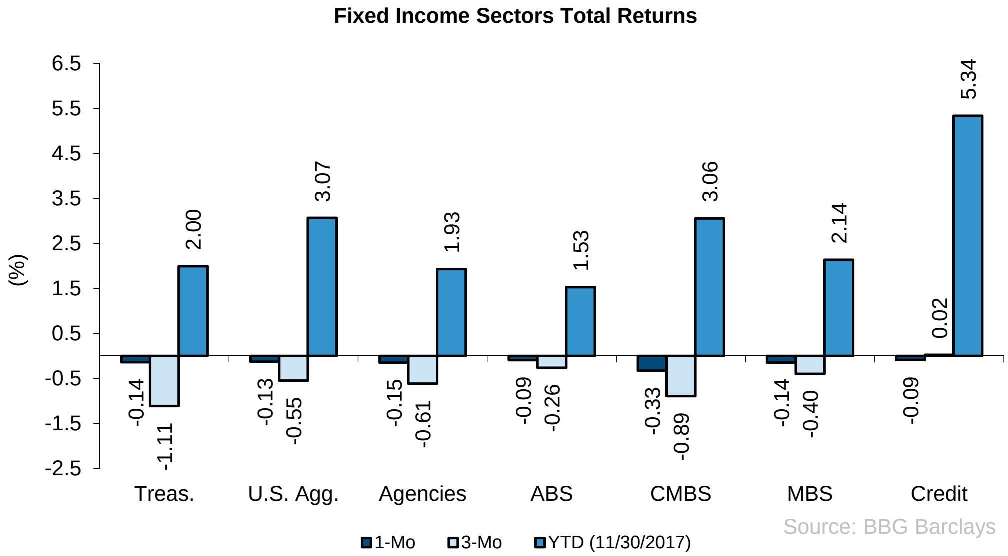
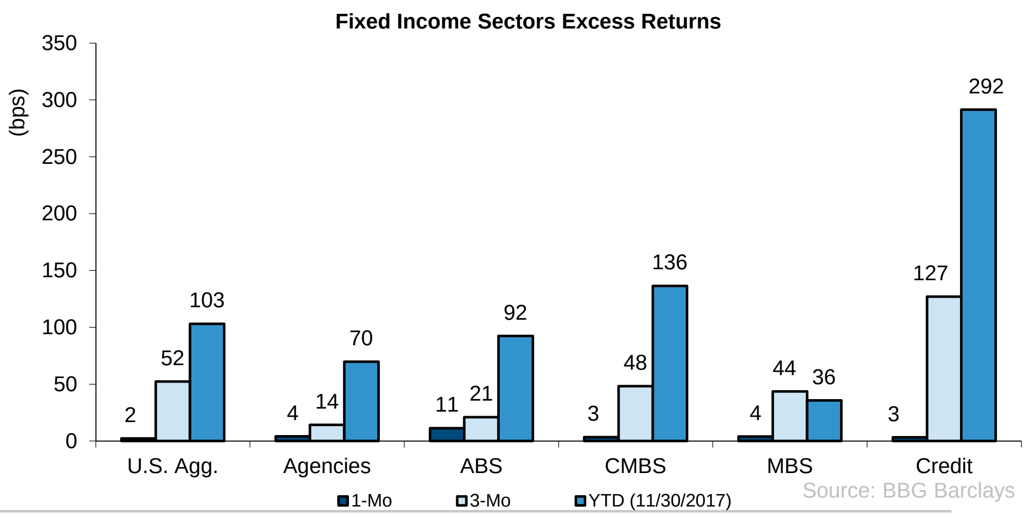
Fixed income market update

- For the month ended November 30, 2017, the Bloomberg Barclays U.S. Aggregate Bond Index returned -0.13%. Year to date, the index has returned 3.07%.
- U.S. Treasuries returned -0.14% during the month as the yield on the 10-year U.S. Treasury rose to 2.41% from 2.38% at the end of October. For the month, long Treasuries (+0.72%) outperformed intermediate Treasuries (-0.31%).
- Mortgage-backed securities (MBS) returned -0.14% during the month, outperforming duration-matched Treasuries by 4 basis points. The option adjusted spread (OAS) of the Bloomberg Barclays U.S. Mortgage Index widened 3 basis points to end the month at 24 basis points.



Source: BBG Barclays



Source: BBG Barclays

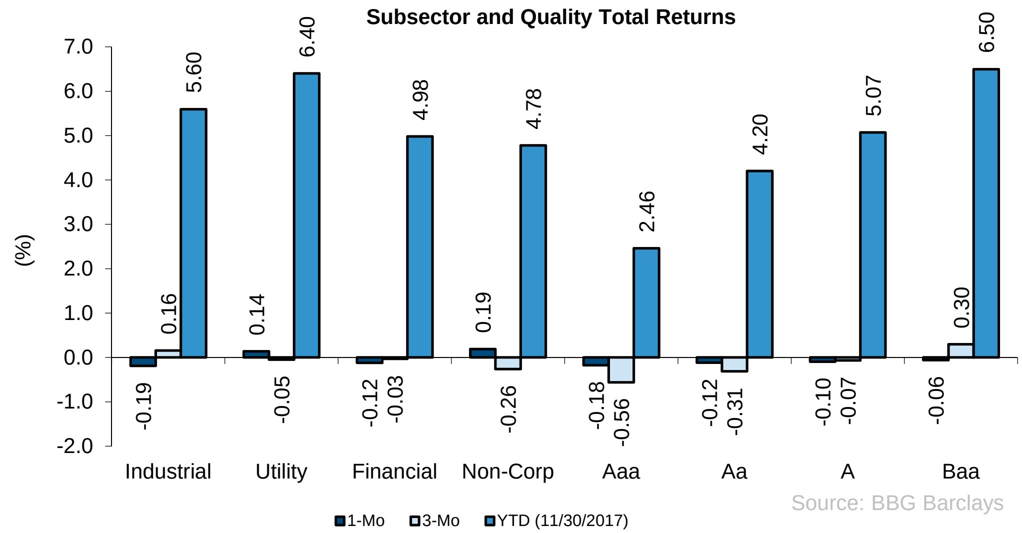
Investment cannot be made in an index. **Past performance is not necessarily a guide to future performance.**

Fixed income market update (continued)

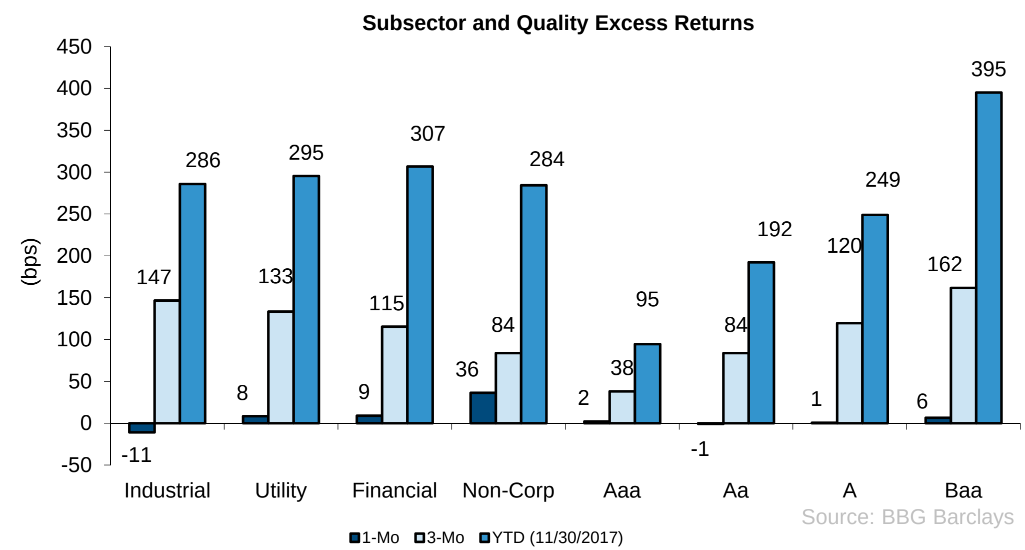
- Credit securities returned -0.09% for the month, outperforming Treasuries by 3 basis points on a duration-adjusted basis. The OAS of the Bloomberg Barclays U.S. Credit Index ended the period at 92 bps, 1 basis points wider than at the end of October. For the month, long credit (+0.41%) outperformed intermediate credit (-0.31%) by 8 basis points on a duration-adjusted basis.

- For the month, on a duration-adjusted basis, non-corporates delivered 36 basis points of excess returns, outperforming financials, utilizes and industrials by 27, 28 and 47 basis points, respectively.

- BBB rated securities delivered 6 basis points of excess return for the month, outperforming AAA, AA and A rated securities by 4, 7 and 5 basis points of excess return, respectively. High yield delivered -2 basis points of excess return for the month.



Source: BBG Barclays



Source: BBG Barclays

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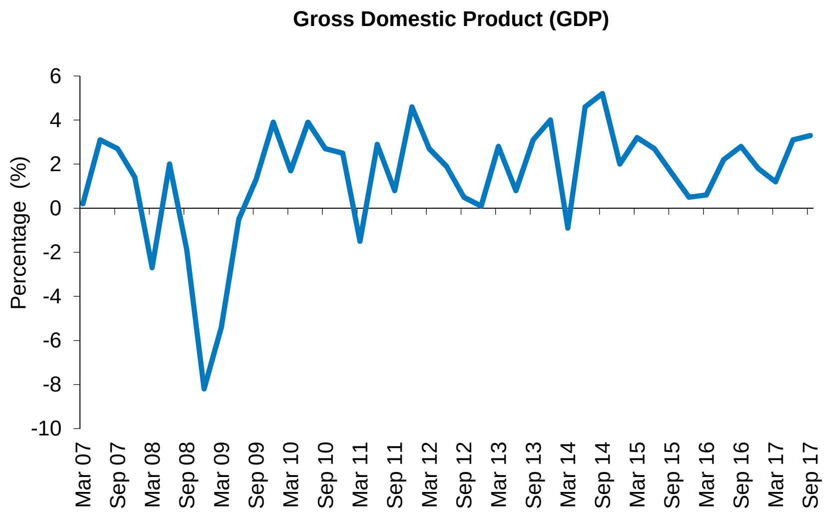
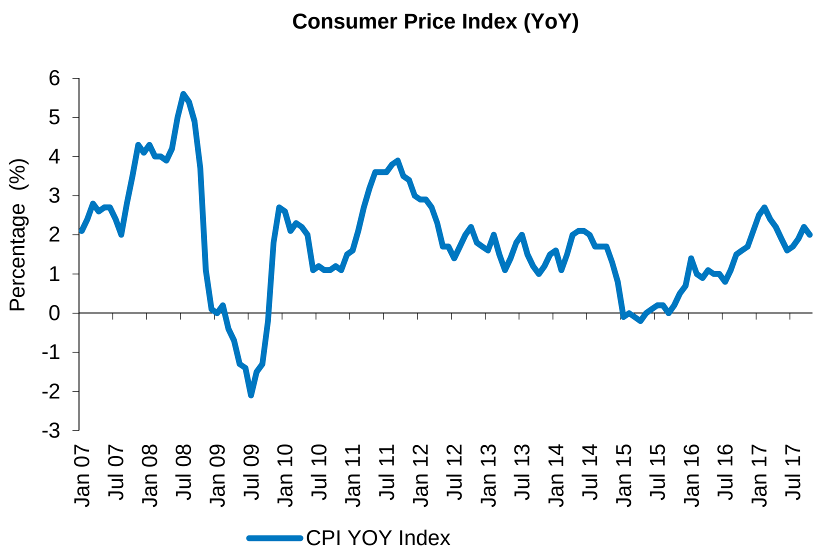
Economic update

Third quarter U.S. gross domestic product (GDP) was revised higher to a 3.3% annualized rate from 3.0%, exceeding expectations. The 3.3% growth rate is the highest of any quarter in three years. Consumer spending (+2.3%) moderated from the prior reading, but business investment (+10.4%) rose at the fastest rate in thee years. The Atlanta Fed's GDPNow estimates 2.7% growth for the fourth quarter (as of November 30), a 0.2% decrease from the projection at the end of October.



Source: Bureau of Economic Analysis

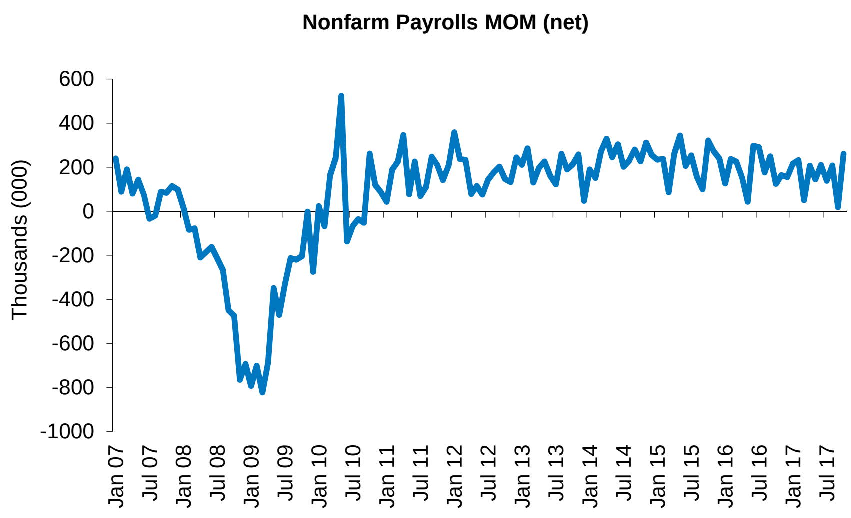


Source: Bureau of Labor Statistics

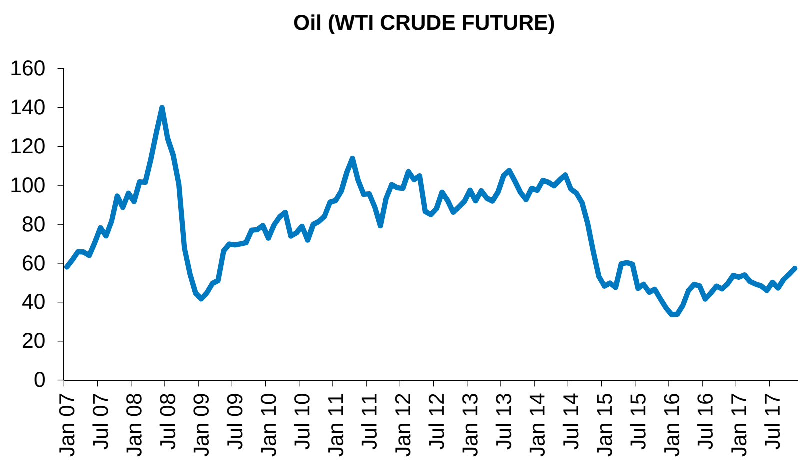
The Consumer Price Index (CPI) rose 0.1% in October and 2.0% for the past year, a decline of 0.2% from the September report. Core CPI, which excludes the impact of energy and food, rose by 0.1% for the month and 1.8% for the trailing year, a modest increase from the 1.7% increase in September, representing the first increase in core CPI since January. Core personal consumption expenditures (PCE), the Fed's preferred inflation gauge, rose 0.2% in October and 1.4% for the trailing year.

Economic update (continued)

Non-farm payroll data for October showed a gain of 261,000 jobs in the month, below expectations, but still the largest gain since the middle of 2016. The September jobs report, which had showed the first decline in jobs in seven years, was revised to show a gain of 18,000 jobs. These updates increased job gains by 90,000 the past two months and lengthened the streak of months with positive job gains to 85. The unemployment rate declined to 4.1%, the lowest level since 2000 as labor force participation dropped 0.4% to 62.7%. Underemployment rate dropped from 8.3% to 7.9%, the lowest level since 2006.



Source: Bureau of Labor Statistics



Source: Bloomberg

Oil closed the month at $57 a barrel, the highest level since mid-2015. Oil prices rose during the month with growing tensions between Saudi Arabia and Iran as well as markets anticipating the OPEC (Organization of the Petroleum Exporting Countries) meeting on November 30th in Vienna. A deal was announced that extended production cuts previously agreed to between OPEC and non-OPEC nations, particularly Russia, to the end of 2018. The list of participating nations expanded to include Nigeria and Libya.

Economic and market perspective

- On November 16th, the U.S. House of Representatives passed tax reform long anticipated by the market. On November 28th, the Senate Budget Committee approved bringing the bill to the broader Senate. Various tweaks to the bill have been debated among Senate Republicans as the bill has been expected to only garner Republican support. The bill appeared to be losing momentum, but is now expected to come to vote on December 1. The House and Senate versions of the bill include differences that will have to be addressed in the reconciliation process. Among the expected differences, the Senate version includes the repeal of the individual mandate within ObamaCare.

- North Korea launched another missile test during November, saying that the Hwasong-15 missile could be armed with a "super-large heavy nuclear warhead." In this test, the intercontinental ballistic missile rose to the highest altitudes yet seen from North Korean missile tests before landing in Japan's exclusive economic zone. It is believed that if fired on a more standard trajectory this missile would have enough range to threaten any part of the United States. The move is seen as the latest provocation from the rogue nation to regional and global stability. After speaking with Chinese President Xi Jinping, President Trump called for "additional major sanctions" on North Korea.

- On November 2, President Trump announced his nominee for the next Chair of the Federal Reserve to be Jerome Powell, a Fed Governor since 2012. On the Dovish/Hawkish scale, the presumptive Chair is viewed as having a generally similar dovish outlook to Chair Yellen. Mr. Powell's confirmation hearing before the Senate Banking Committee began on November 28th, he is expected to be confirmed. Chair Yellen announced that she would resign her Fed Governorship after her successor takes office. During November, President Trump nominated Marvin Goodfriend, an academic with Fed experience, for one of the open governorships. Assuming he is confirmed, two additional seats remain vacant with another opening with resignation of Yellen in February.

Outlook and conclusions

- As expected, the Federal Open Market Committee did not raise the Fed Funds rate when it met on October 31-November 1. The minutes from that meeting, released on November 22, reflect a generally positive economic outlook from the Fed, though noting that core inflation continues “to surprise on the downside.” The minutes indicate that the Fed expects to raise the Fed Funds rate in the “near term”, which the market has interpreted as the December 12-13 meeting. As of the end of November, markets are pricing in a near certainty of a hike at the final meeting of the year. Fed projections call for three additional rate hikes in 2018.

- In her final appearance before the Joint Economic Committee of Congress, Chair Yellen emphasized the need to continue raising the Fed Funds Rate gradually to avoid causing “a boom-bust condition in the economy.” Her comments were interpreted as further supporting a December rate hike. She also observed that while asset valuations were “high by historical standards, overall vulnerabilities in the financial sector appear moderate” and that she was “very worried about the sustainability of the U.S. debt trajectory.”

- In our view, the Fed has adequately signaled their intention to raise the Fed Funds rate in December such that the market will be comfortable when it is formally announced. Continued strengthening of the growth and employment data support such a move, while the calls for gradualism given the persistently below target inflation are also appropriate. With rates and spreads having moved little in the past month, but economic data continuing to improve on the margin and fiscal policy appearing more likely to support future growth, our outlook remains positive for fixed income overall with a focus on uncovering idiosyncratic security selection opportunities.

Fixed income returns as of November 30, 2017

Index Returns as of November 30, 2017				
	Total Return (%)		Excess Return (%)	
	Month-to-Date	Year-to- Date	Month-to-Date	Year-to- Date
U.S. Aggregate	-0.13	3.07	0.02	1.03
U.S. Treasury	-0.14	2.00	-	-
Intermediate	-0.31	1.11	-	-
Long	0.72	6.70	-	-
TIPS	0.13	2.07	-	-
Agencies	-0.15	1.93	0.04	0.70
U.S. MBS	-0.14	2.14	0.04	0.36
U.S. Credit	-0.09	5.34	0.03	2.92
Intermediate	-0.31	3.41	0.01	2.15
Long	0.41	9.98	0.09	4.78
Industrial	-0.19	5.60	-0.11	2.86
Utility	0.14	6.40	0.08	2.95
Financial	-0.12	4.98	0.09	3.07
Non-Corporate	0.19	4.78	0.36	2.84
Aaa	-0.18	2.46	0.02	0.95
Aa	-0.12	4.20	-0.01	1.92
A	-0.10	5.07	0.01	2.49
Baa	-0.06	6.50	0.06	3.95
High Yield	-0.26	7.18	-0.02	5.85
Floating Rate Notes	0.14	2.16	0.06	1.43

Source: Bloomberg Barclays

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Disclosures

All investments involve risk, including the possible loss of principal.

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