



INTERMEDIATE MATURITY MUNI



COMMENTARY – THIRD QUARTER 2018

MACRO OVERVIEW

US Treasury yields marched steadily higher over the quarter led by the front-end of the curve as the Federal Reserve implemented its third interest rate hike this year in September. The yield curve continued to bear flatten as short-term rates (1YR) were higher by 36 basis points while the long-end of the curve (30YR) was higher by 22 basis points. Risk assets performed well especially in the U.S. as both the S&P and DJIA were up approximately 7% for the period. A steady supply of strong economic releases (Q2 GDP, NFP, and wage growth) helped fuel the rally in equities, while a continued lack of long-term global inflation expectations prevented intermediate and longer-term interest rates from moving meaningfully higher. Looking ahead, we continue to see the likelihood of gradual and deliberate rate normalization as recent FOMC statements have upgraded the committee’s assessment of US growth to “strong”.

- Final Q2 GDP came in at 4.2%, the first time it has bested 4% since 2014. Q3 GDP expectations appear stout with Atlanta Fed GDP Now forecasting 4.1%.
- Job growth has been strong year-to-date and the third quarter was no exception with Nonfarm Payrolls averaging 190k during the quarter.
- The Fed is on track to raise rates for the 4th time this year in December (currently ~75% probability) while the most recent Fed Dot Plots suggest an additional 3 hikes in 2019.
- Markets have largely ignored the potential impacts of ongoing trade disputes which could curb growth both abroad and here in the US.

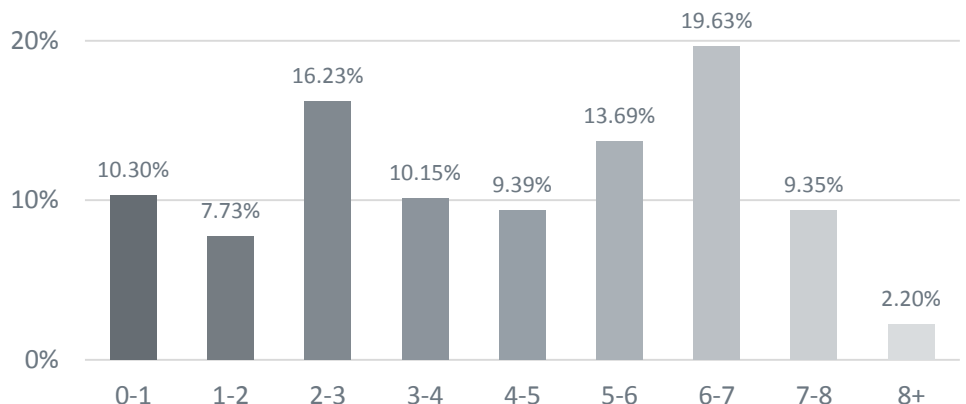
MARKET DYNAMICS

The lack of supply which plagued the muni market during the first half of the year continued, albeit to a lesser degree. Looking at quarter-over-quarter issuance, Q3 supply was down approximately 10% while year-to-date supply is now down approximately 13%. Total issuance has been dominated by new money (83%) as borrowers have begun to cautiously take on new infrastructure projects. Muni yields generally followed UST yields higher during the quarter with the 10YR portion of the curve performing best. For the period, the 2YR AAA muni benchmark was higher by 33bps, the 5YR higher by 21bps while the 10YR was higher by only 12bps. Over the near-term, munis should take their cues from the UST market which is expected to drift moderately higher. We continue to believe this presents a compelling entry point for tax aware investors wishing to reallocate or de-risk investment strategies.

DURATION PROFILE

COMPOSITE CHARACTERISTICS

Duration: 4.29 yrs
 Yield-to-Worst: 2.51 %
 Yield-to-Maturity: 2.69 %
 Maturity: 6.19 yrs



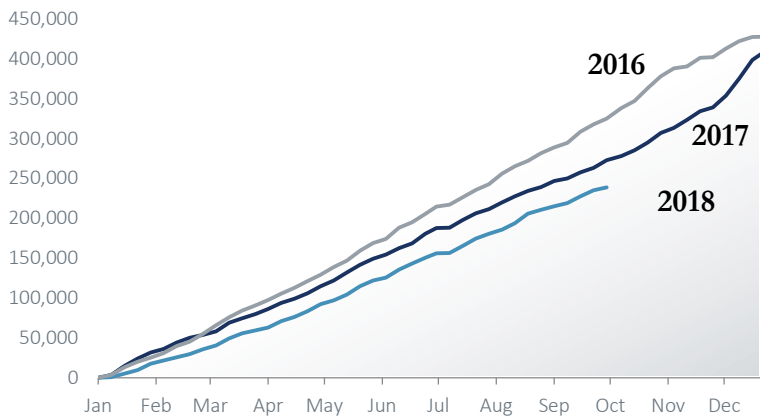


PERFORMANCE NOTES

Strategy performance was in-line to slightly below benchmarks for the quarter. Mild underperformance was mainly attributed to the rally in August where the longer duration benchmarks benefitted. However, our short of benchmark duration proved additive in September as munis were weaker during the month. YTD returns are now modestly negative, after withstanding a meaningful selloff in both January and February and again in September. Shorter maturity positions were the worst performers over the quarter due to a drift higher in yields prior to the September Fed hike and a general correction in this part of the curve from being over-bought earlier in the year.

TOTAL MUNICIPAL ISSUANCE YOY (\$BLN)

SOURCE: BLOOMBERG



“Demand remained steady throughout the quarter, especially from the retail sector and the muted supply proved constructive from a technical standpoint. The recent moderate move to...

**higher absolute yields
provides an attractive entry
point into munis**

... and a good place to realize superior diversification benefits.”

10 YR MMD

SOURCE: BLOOMBERG



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