Intermediate Maturity Taxable

Commentary – Fourth Quarter 2019

Macro Overview

2019 wrapped up with renewed optimism for a possible phase one trade deal between China and the United States. This, in part, helped U.S. equities stage an impressive Q4 rally, bringing returns for the full year above 30% (S&P 500). The Federal Reserve continued easing during the quarter, cutting overnight interest rates an additional 25bps at their October meeting. In total, the Fed cut rates 3 times (75bps cumulative) during the year, a stark reversal from their policy stance heading into 2019. Bond yields ended Q4 marginally higher; however, for the calendar year rates were lower by approximately 90bps on the front-end of the curve and nearly 80bps out 10 years. Looking ahead, the Fed appears to be on hold while the U.S. economy remains on stable footing, but global economic weakness persists.

- Recent geopolitical risks in the Middle East and any renewed political posturing ahead of signing a trade deal are the most likely catalysts for market volatility heading into Q1 '20.
- Markets have largely dismissed the House's decision to impeach the President, labeling it political gamesmanship. Popular narrative suggests there are not enough votes in the Senate to convict President Trump.
- The Fed remains constructive on U.S. job market and overall growth; their most recent forecast sees GDP up 2% in '20. Fed Funds forecasts suggest the Fed will be on hold in '20 with a single hike taking place in '21.

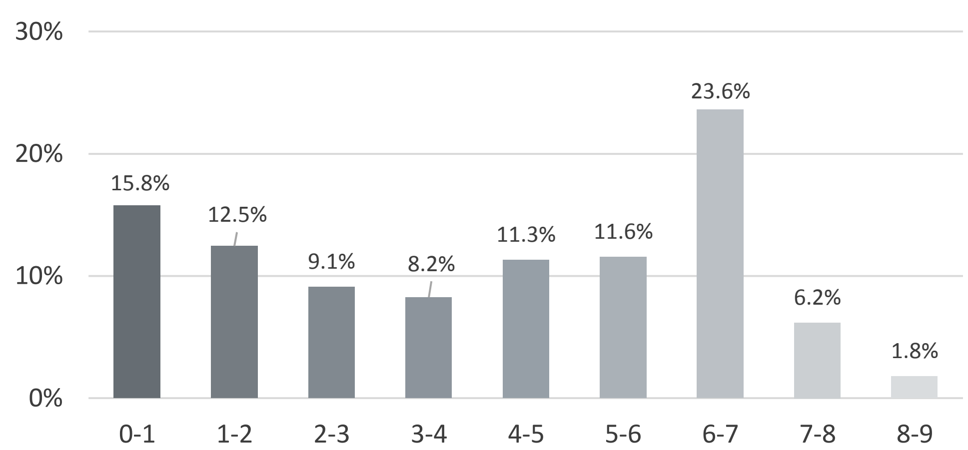
Market Dynamics

Over the quarter, corporate credit spreads tightened to levels not seen since February 2018. Fueling the steady decline in high grade bond spreads was a late year rally in risk assets as trade tensions deescalated and economic readings that began to show some resilience. For the full year, spreads contracted by nearly 60bps as domestic equities reached all-time highs. While current levels do not appear as attractive as they did to begin 2019, we see several reasons that 2020 should continue to see support for high grade debt. Lower net supply, still positive US growth, and an accommodative Federal Reserve for the foreseeable future should all continue to draw yield starved investors into U.S. corporate bonds. Bouts of volatility are certainly a possibility though, with rising Middle East tensions and the upcoming election as the primary catalysts.

Composite Characteristics

Duration: 3.97 yrs
Yield-to-Worst: 2.13 %
Yield-to-Maturity: 2.15 %
Maturity: 5.65 yrs

Duration Profile

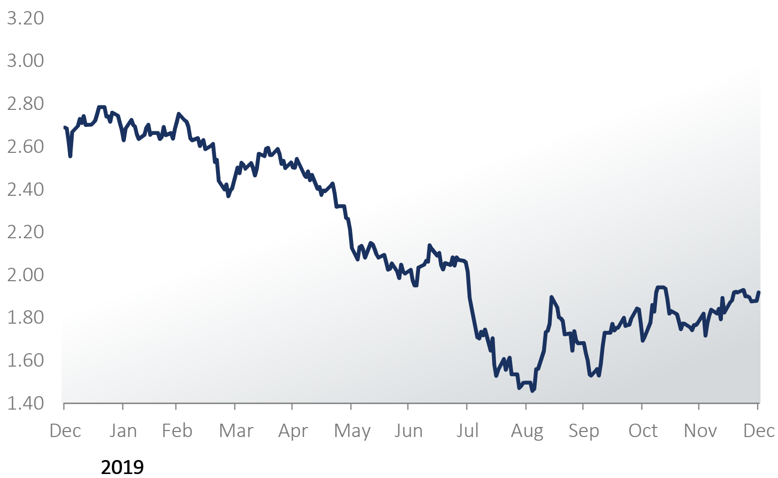


Performance Notes

Although US Treasury yields rose moderately over the quarter, the intermediate taxable strategy was well positioned to benefit from the aforementioned corporate credit spread tightening. Overall performance during the period was modestly ahead of benchmark with neutral-to-slightly longer duration and maturity positioning. The strategy's overweight to investment grade corporate debt has been notably additive to total return over the course of the year as demand for positively yielding US debt has been exceptionally strong. Although cautious of potential spread widening catalysts mentioned above, our outlook does not see a significant deterioration in corporate credit health in the near-term. We continue to view our ability to select large, higher quality corporate issuers with sound balance sheets as a way to buffer potential volatility.

10-YR US Treasury Yield (%)

Source: Bloomberg



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US Credit Index – Spread (%)

Source: Bloomberg

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