Market Review and Outlook
March 31, 2019

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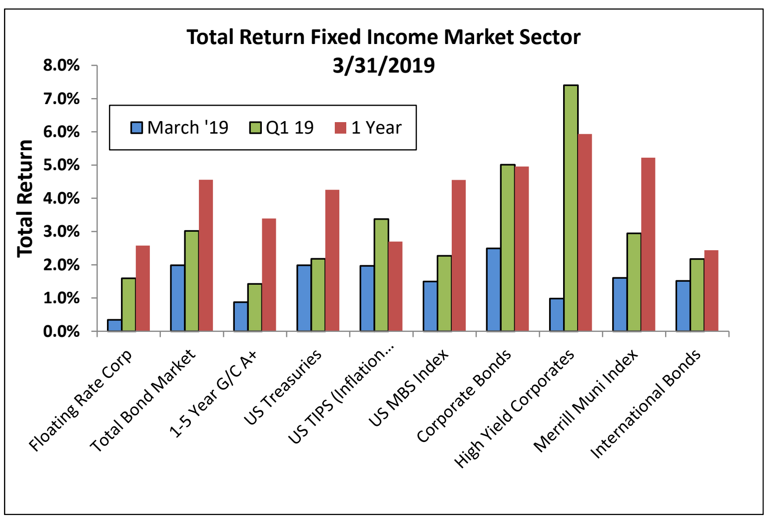
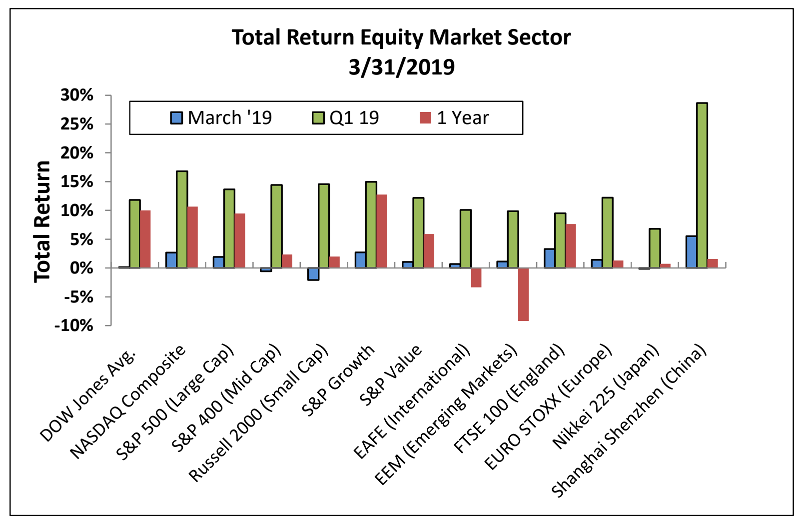
Market Summary

March 2019

- After an aggressive reversal of monetary policy by the Fed in Q1 from tightening to "flexible" in order to reverse the adverse impact of the December rate hike, the fourth of 2018, investor sentiment shifted and equity markets recovered from their correction of Q4 2018.
- The shift in Fed policy also included an end to winding down Quantitative Easing, which combined with a neutral rate stance helped drive down interest rates and generated significant gains in the bond market.
- All assets rose as the Fed brought the punchbowl back out. Equities returned toward their highs with growth stocks resuming their leadership, and other risk assets such as High Yield and deeper credit bonds recovering.
- The US economy has continued to perform well; however, the market is preoccupied by the risk of the global economy pushing the US into a recession and has pushed interest rates down, providing economic stimulus and supporting equities.





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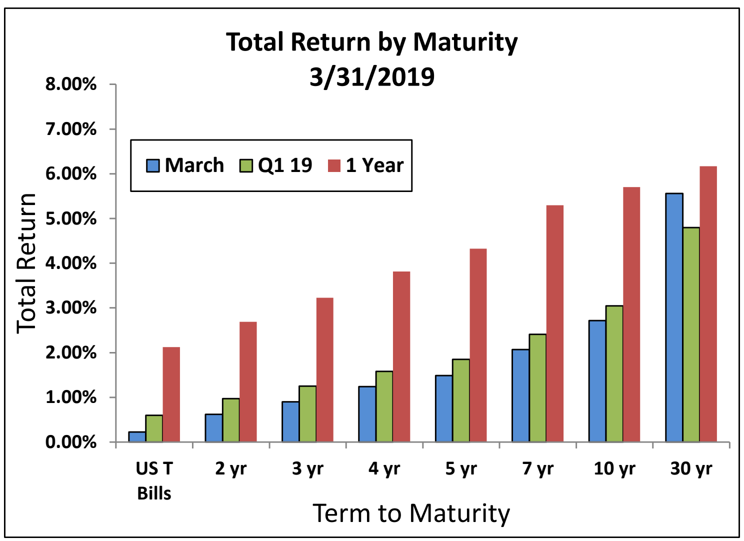
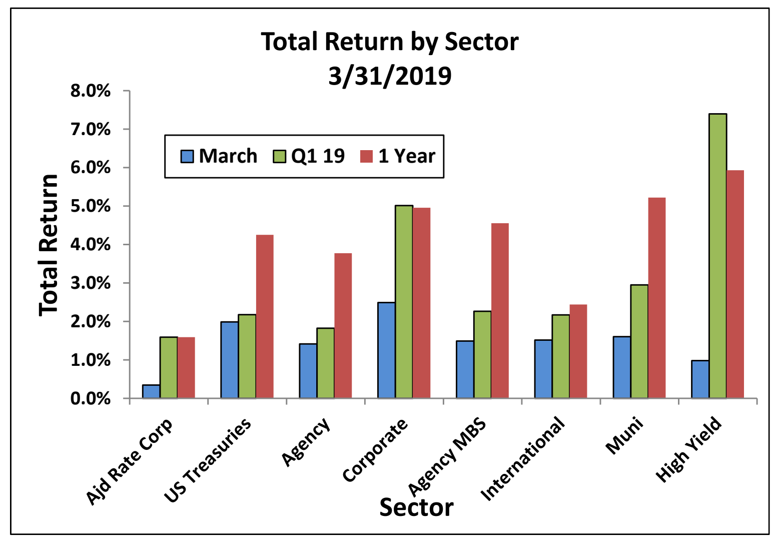
Market Review

Yield Curve and Sector Returns – March 2019

- Total returns in Treasuries were significantly positive in Q1 as the Fed shifted policy and fears of economic slowdown grew. March was a significant move that dominated the quarter.
- Putting the past two quarters together has generated significant positive returns for bonds, particularly longer maturities, and has offset the impact of the rise in rates for much of 2018.
- Credit spreads reversed course and tightened across the credit spectrum, generating strong returns particularly in the deeper credit and the high yield sector.
- Mortgage backed securities performed well in lower coupons, but higher coupons widened out due to increased prepayment risk and have again become relatively attractive looking forward.





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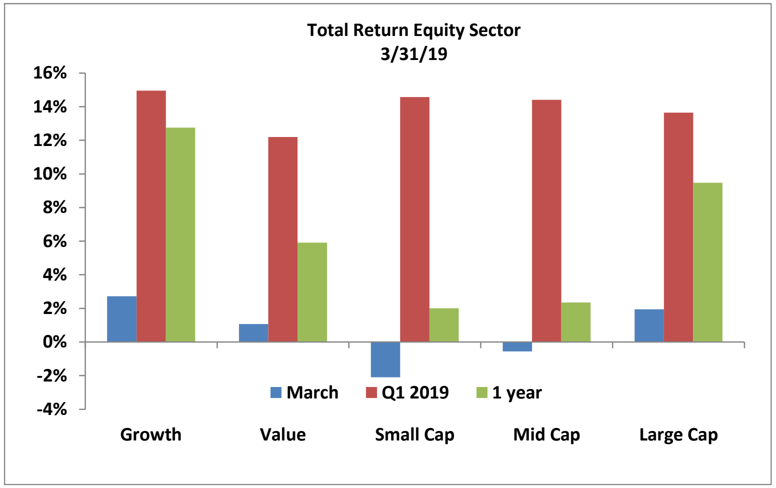
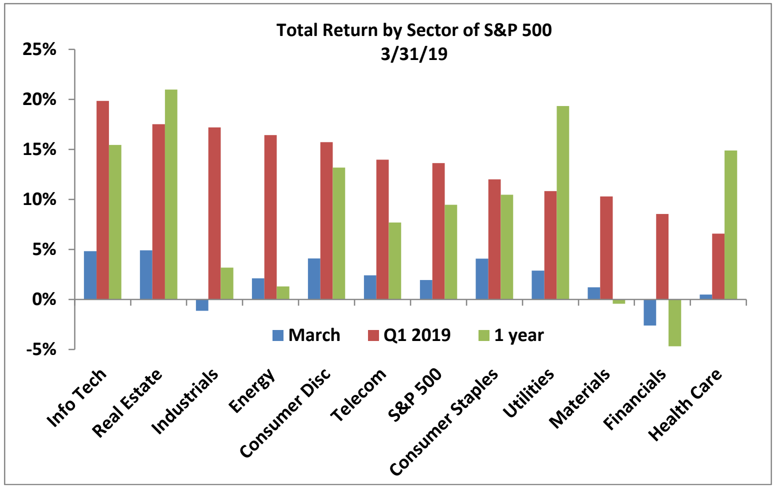
Market Review

Equity Market Returns - March 2019

- In the equity markets during the quarter, virtually all sectors rose in unison due to broad based reversal of market sentiment, although larger cap and growth oriented equities rose a bit more.
- Over the past year, and into March growth stocks and large cap maintained momentum as smaller caps gave back some gains recently.
- Economically sensitive sectors such as technology, industrials and consumer discretionary led gains for the quarter.
- The shift in monetary policy and lower rates has boosted the real estate market while also hurting the financial sector, and the rise in oil propelled energy.





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Market Environment Summary

March 2019

- The Federal Reserve dramatically shifted their policy stance and effectively eased in Q1 by halting the unwinding of Quantitative Easing and communicating they are likely done tightening for the year.
- The Fed communicated that despite the solid US economic conditions, their fear is that slower growth overseas would spread to the US. This fear dominated their emphasis.
- The return of the punch bowl to the market provided fuel for a full recovery in the equity market, led by growth stocks and other risk assets such as High Yield and deeper credit corporate bonds.
- Interest rates fell significantly, let by intermediate rates, which fell below the current Fed Funds rate and pricing in a cut in rates by the Fed in 2019. Rates should normalize at higher rates moving forward.
- Underlying US fundamentals remain quite strong, however economic statistics early in the quarter that were delayed, sporadic, and incomplete due to government shutdown influenced markets that took any sign of moderation and extrapolated it into assuming a recession was around the corner.
- Timely economic data have resumed, showing continued strong employment, wage growth, consumption, and a strengthening housing market. International data has stabilized.
- Equity markets recovered given stable economic fundamentals and, significantly, a return to accommodative Fed policy. Interest rates however remain artificially low due to Fed QE, and expectations of at least one Fed easing in 2019 – Unrealistic given the true fundamentals.
- The inverted front end of the yield curve does not imply a recession.

Market Environment Summary

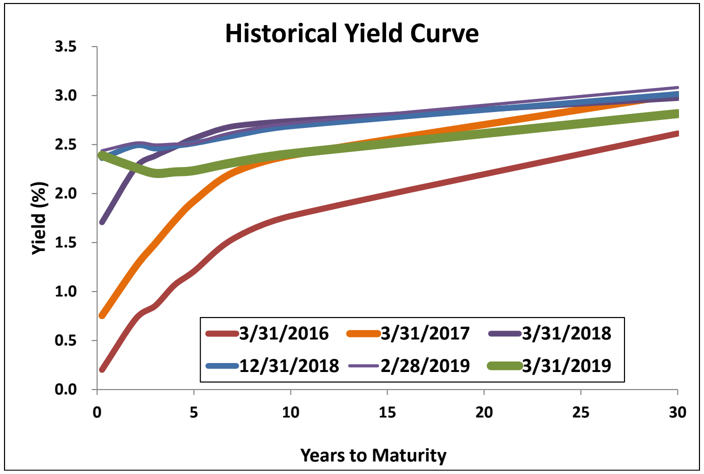
March 2019

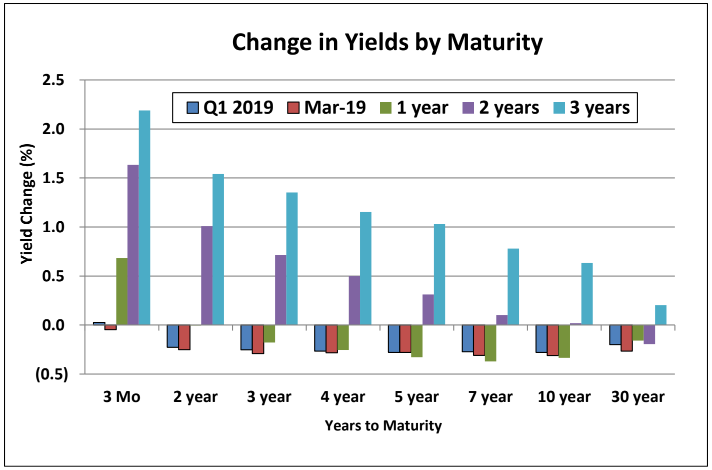
- Stocks rebounded from their "correction" lows on the back of the Fed adjusting their policy and strong economic fundamentals, including a robust employment report and positive trade talks. Stocks continued to march higher throughout the quarter toward previous highs.
- Interest rates remained low, with intermediate rates lower than the Fed Funds rate, explicitly pricing in at least one Fed easing this year and next. None of the Fed Governors have indicated a plan to ease, and 6 governors continue to see some probability of tightening later this year. We do not see an ease in 2019.
- Our expectations are for rates to reestablish their higher levels in the range established last year and hold there for some time. Income should dominate total return as the year progresses and volatility recedes.
- The equity market will be driven by earnings growth in the coming quarter with year over year comparisons low given the significant post tax cut boost to earnings last year. Markets expect a decline in earnings in the quarter, so upside surprises will drive markets higher.
- Despite the implications of the push lower in rates, corporate spreads, particularly deeper credit have tightened considerably reflecting solid corporate conditions.
- Higher input costs from labor may impact corporate earnings, and oil prices have risen significantly.
- While market behavior has clearly influenced Fed policy, inflation continues to drive the discussion of where policy is heading, and Fed policy is significantly impacting market activity, supporting equities.
- Current inflation has risen and established a range at the Fed targets. Wages continue to rise as employment continues to grow with adds to payrolls, increased labor force participation, and few layoffs.

Market Review

Yield Curve – March 2019

- Interest rates continued to fall from their multi year highs established in Q4 as the Fed dramatically reversed course and effectively eased monetary policy in Q1.
- Despite the strong US economy and equities nearing old highs, markets continue to be preoccupied by fears of a global slowdown pushing the US into a recession, and have pushed intermediate rates down below the current Fed funds rate, implying an easing by the Fed this year.
- Despite recovery in risk assets, the flight to quality and Fed policy have pushed rates excessively low, which the Federal Open Mouth Committee continues to promote through discussions of low inflation and global economic risk.
- Low rates will stimulate already solid economic activity which will ultimately push rates higher as expectations of an ease are unwound.

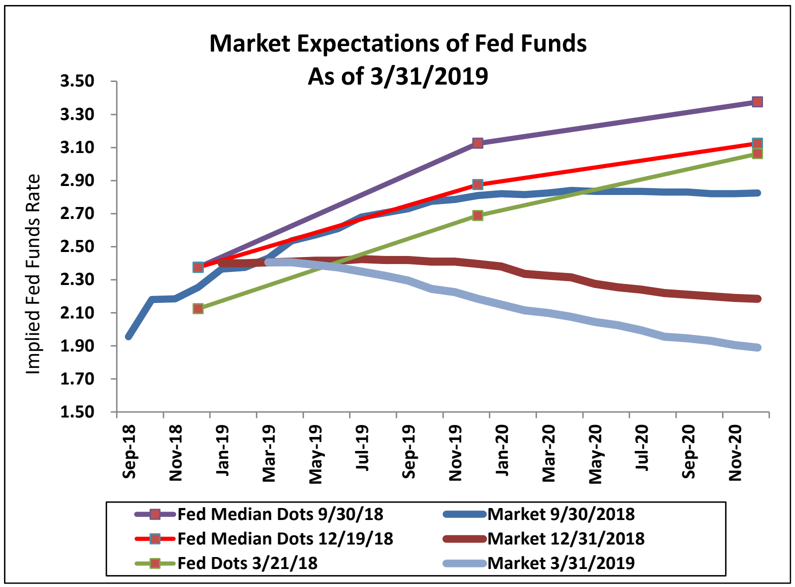




Market Review

Monetary Policy – March 2019

- The Fed dramatically reversed course and effectively eased policy by stating they may not move at all in 2019, while also halting the unwinding of the balance sheet built up by QE.
- The market is pricing in at least one ease for 2019 and 2020. The Fed "dot plot" shows the Fed lowered expectations, but still expecting to hike rates as their next move, with no Fed governors expecting a drop in policy and 6 still expecting a tightening this year.
- The Fed also reduced their estimate of GDP and inflation for the year given the moderation in global growth, uncertain trade environment, and market conditions.

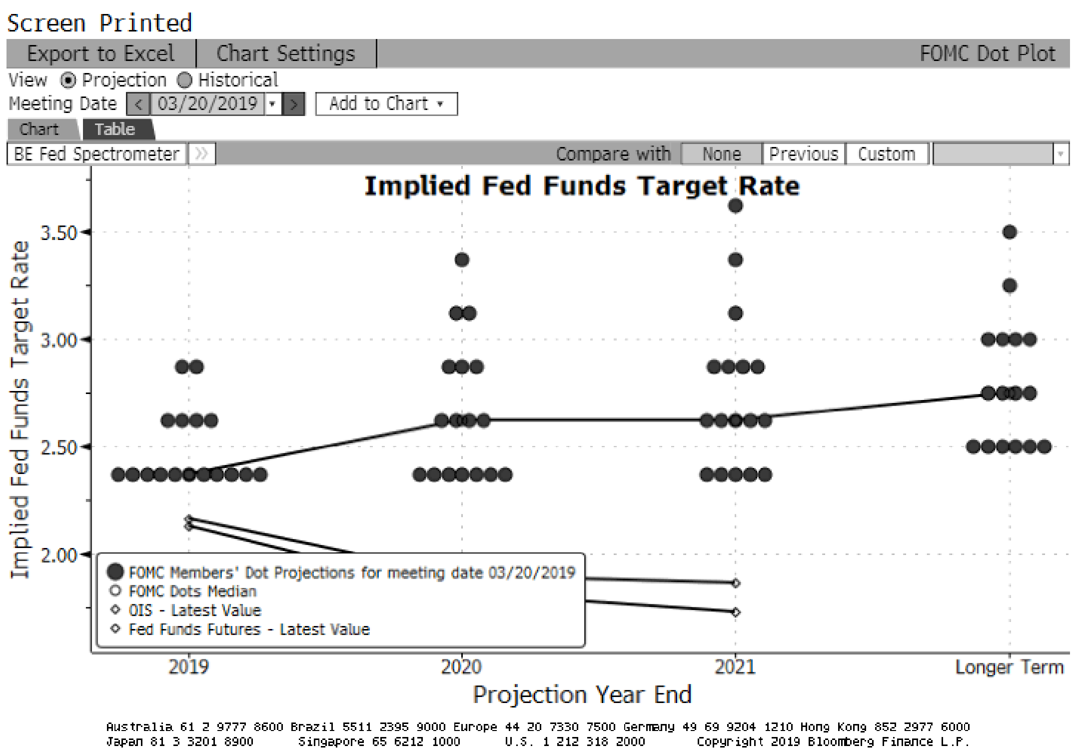


Federal Reserve Median Economic Projections As of 3/20/2019					
Change in GDP	**Actual**	**2019**	**2020**	**2021**	**Longer Run**
March 2019 Projection		2.1	1.9	1.8	1.9
Dec 2018 Projection		2.3	2.0	1.8	1.9
Actual Q4 2018 yoy/qoq	**3/3.4%**				
Unemployment Rate					
March 2019 Projection		3.7	3.8	3.9	4.3
Dec 2018 Projection		3.5	3.6	3.8	4.4
Actual Q4 2018	**3.9%**				
PCE Inflation					
March 2019 Projection		1.8	2.0	2.0	2.0
Dec 2018 Projection		1.9	2.1	2.1	2.0
Actual Sept 2018	**1.8%**				
Core PCE Inflation					
March 2019 Projection		2.0	2.0	2.0	
Dec 2018 Projection		2.0	2.0	2.0	
Actual August 2018	**1.9%**				
Projected Policy Path- Fed Funds					
March 2019 Projection	2.375	2.4	2.6	2.6	2.8
Dec 2018 Projection	2.375	2.9	3.1	3.1	2.8

Market Review

Monetary Policy – March 2019

- The Fed messaging has been for no rate hikes in 2019, which is where the median dots (individual Fed Governors outlooks) implied. No Governors expect an ease, 6 still expect a hike this year, and most expect one next year..
- The market is pricing in an ease this year and next. The current Fed Funds target is a range between 2.25% - 2.5%.



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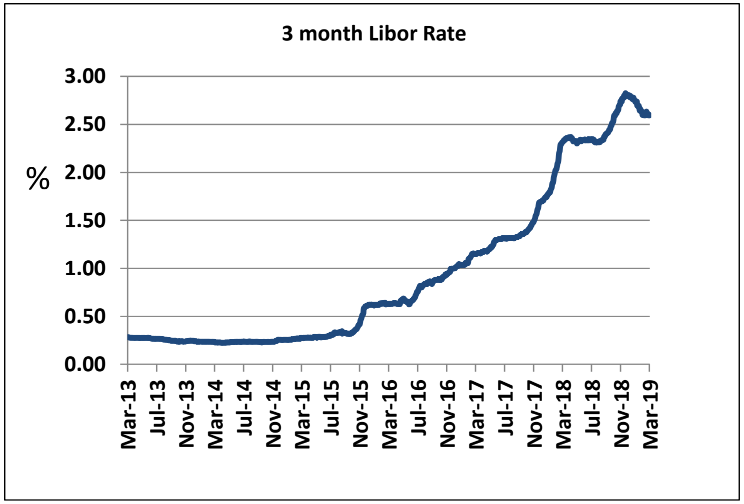
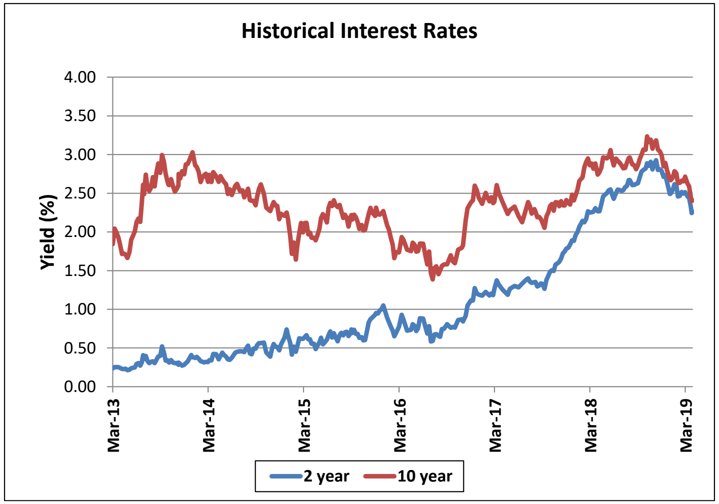
Market Review

Yield Curve – March December 2019

- Reflecting the move in Fed activity, 3 month libor has risen significantly, and has leveled off as the Fed reversed course. Most floating rate notes are benchmarked off of libor, providing increasing coupons with stable prices.
- Short rates fell somewhat but intermediate and longer term rates fell significantly at first due to fears of global slowdown. As rates pushed lower market technicals took over as some investors such as hedge funds and mortgage investors were forced to buy duration, further pushing rates artificially low.
- Despite the turn in market expectations to a dramatically slowing economy, the return of equities to their highs, continued economic growth, rising inflation, and increased net issuance will likely cause longer rates to return to previous levels..





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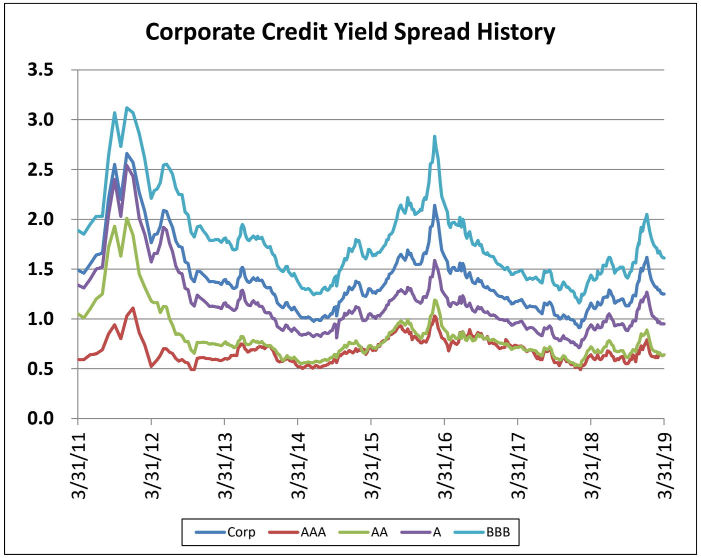
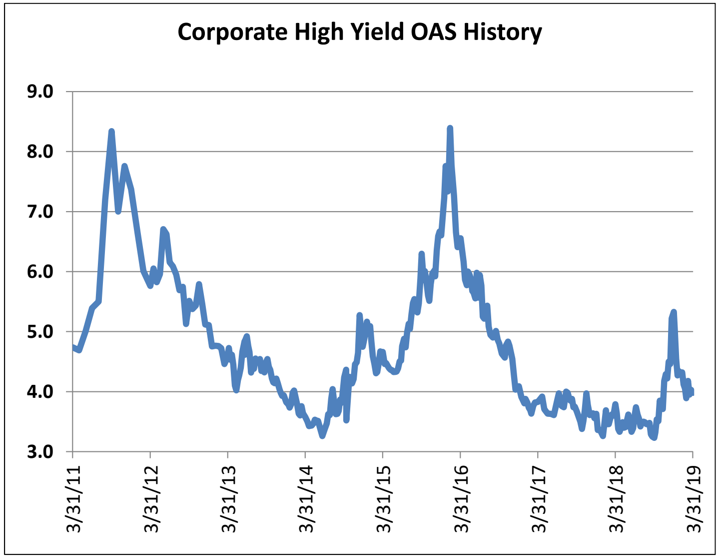
Market Review

Corporate Yield Spreads – March 2019

- As interest rates fell and equity markets recovered, corporate yield spreads tightened significantly in Q1, bucking the inverse relationship between interest rate risk and credit risk.
- Spread tightening was driven by the easier monetary policy and reversed the widening experienced in Q4 amid the sell off in risk assets.
- Continued strong economic conditions and corporate earnings continue to conflict with market sentiment that has implied significant deterioration in economic fundamentals
- Corporate credit conditions remain strong and risk of default has not risen to the degree that credit spreads have widened. Spreads may continue to grind lower as the year progresses.





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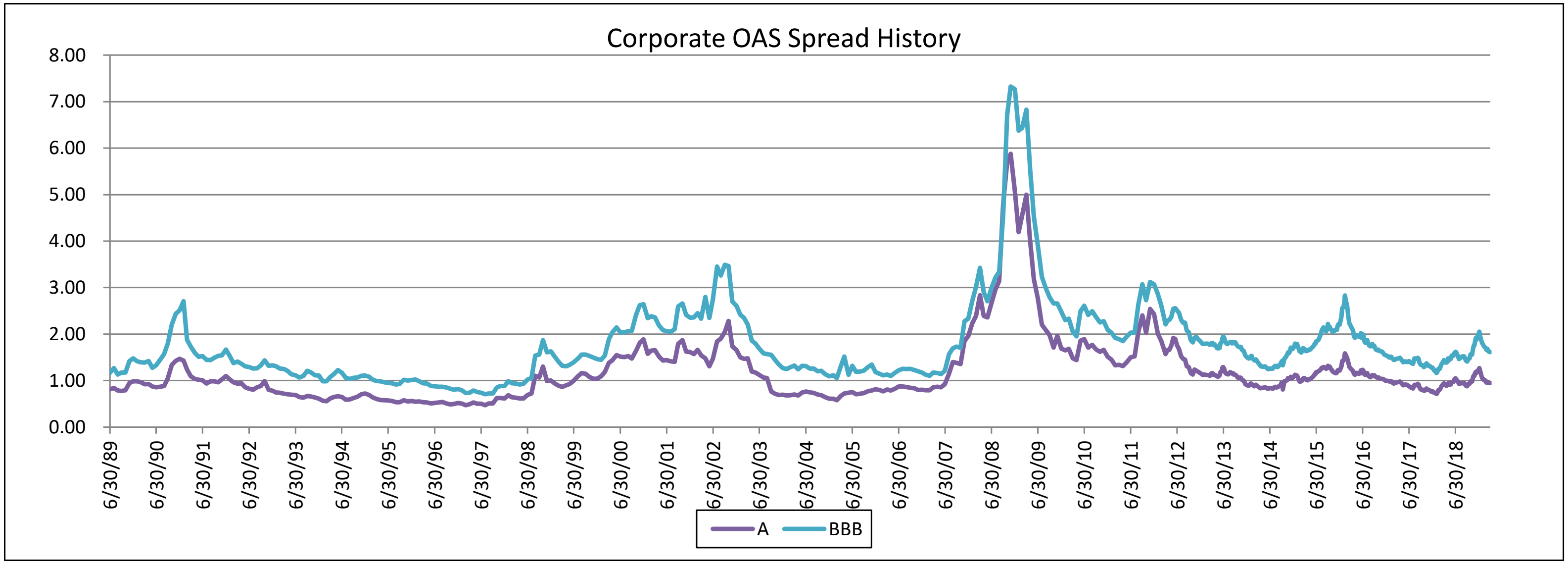
Market Review

Corporate Yield Spreads – March 2019

- When looking at corporate credit risk premiums on a longer term basis, it is useful to look at the mid to late 90's environment with similar policy and economic conditions.
- Steady policy after a recession induced extended monetary ease provided a solid economic foundation, and the economy progressed with steady growth and inflation.
- Credit spreads remained steady and moved tighter as credit risk remained low and investors craved additional income.



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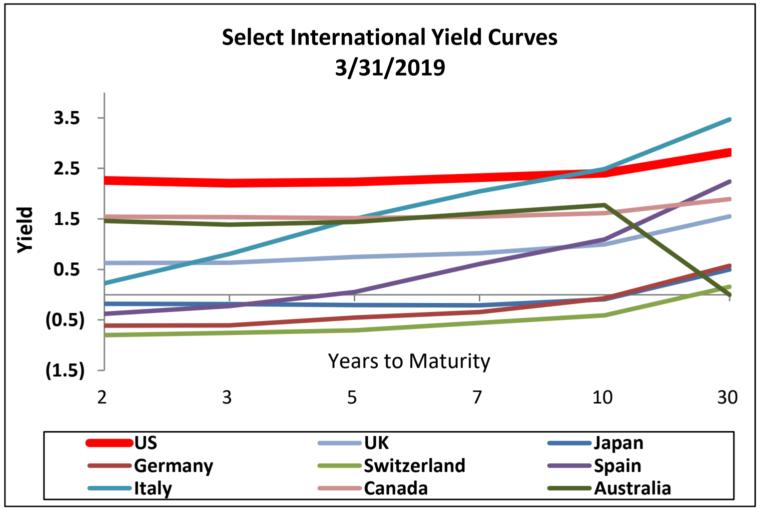
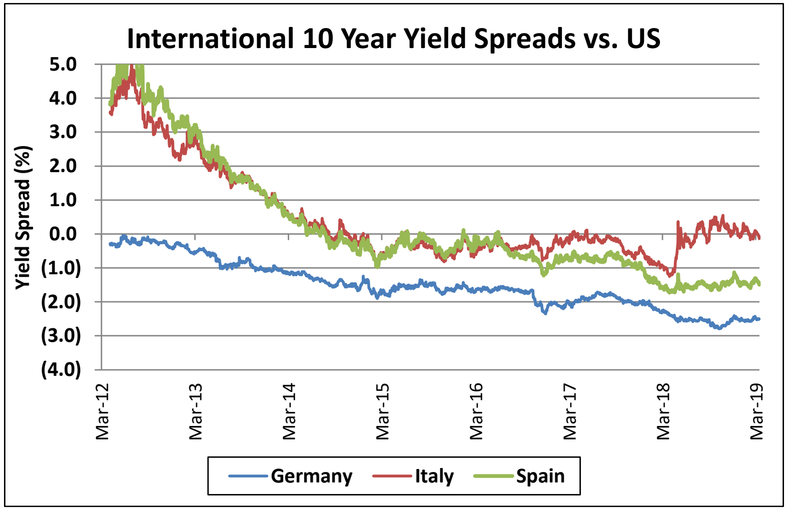
Market Review

International Yield Curves– March 2019

- The US continues as one of the highest yielding developed countries and the yield spread over Europe remained wide in Q4. German 10 year rates went below 0%.
- The European Central Bank and Bank of Japan continue aggressive easy monetary policy with negative rates in Europe and a targeted 0% ten year rate in Japan.
- Political events in Italy and their budget discussions with the EU have kept Italian yields relatively high.





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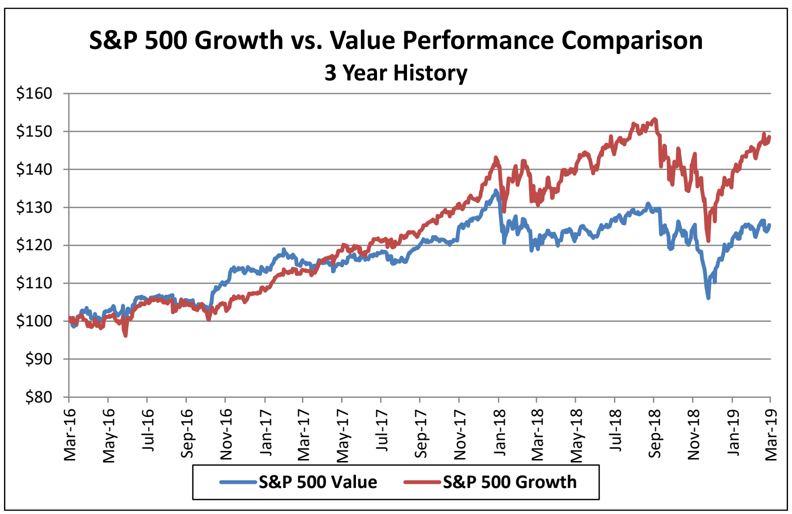
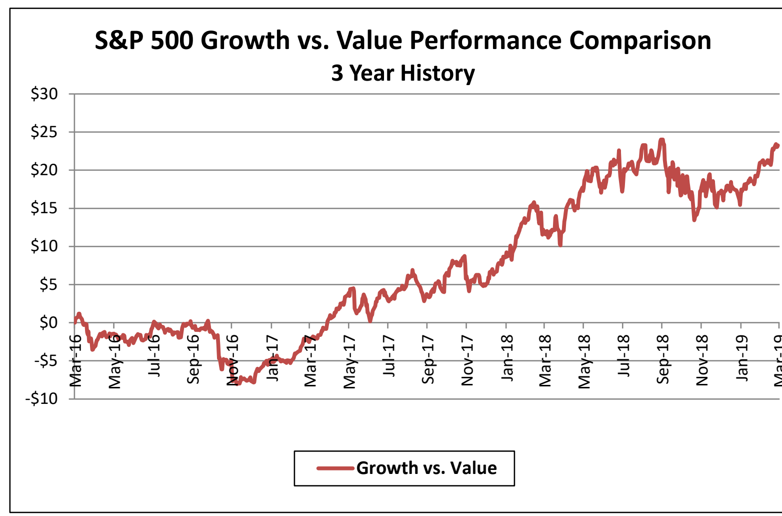
Market Review

Equity Market Returns - March 2019

- In the equity markets, Growth has outpaced Value reflecting innovation and high expectations of business investment going forward.
- The equity market recovery had growth stocks resuming their leadership roll after giving way to value stocks during the market correction.
- Dividend paying value stocks have been challenged by higher interest rates, but regained ground as rates fell. High dividend payers are doing well given the still low rate environment, but growth is doing a bit better.





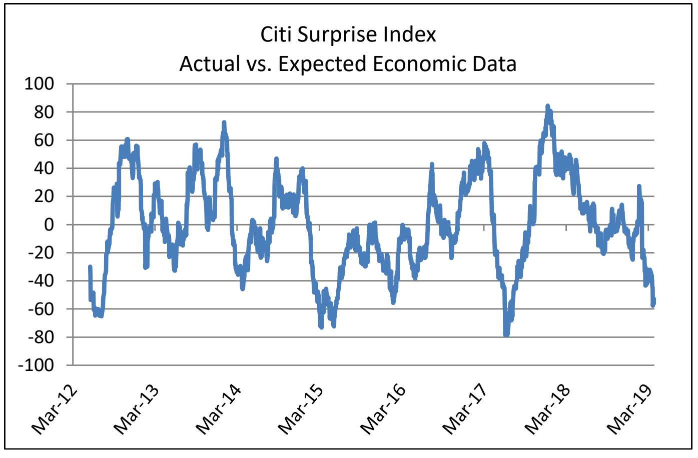
Economic Environment

March 2019

- The Citi economic surprise index plumbed to its lower levels as it typically has in Q1. Additionally, the partial government shutdown provided for delayed and partial economic data releases that should improve.

- There is a preoccupation with the moderation in economic growth around the globe, particularly in China and Europe, that is an ongoing discussion at the Fed and in the markets.

- Moving forward, economic data have begun to improve and should improve further on an absolute basis and relative to market expectations.

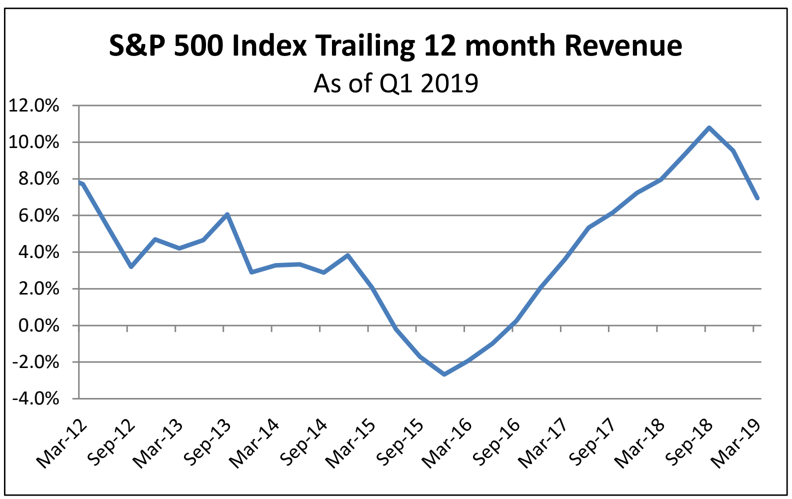


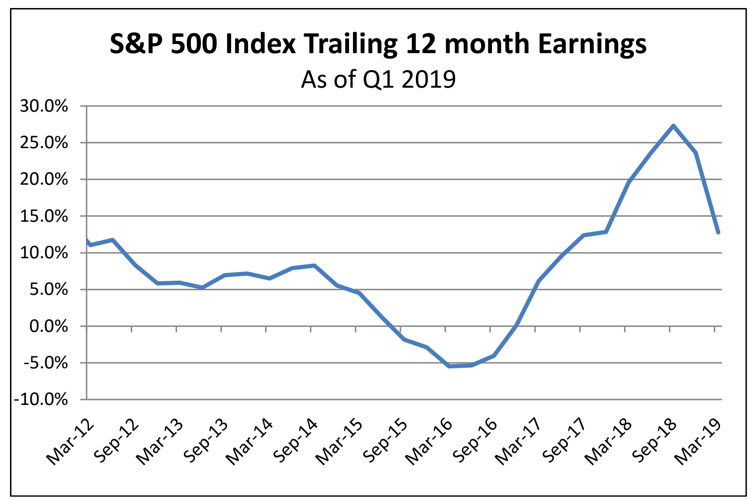
GDP YoY % Change			
	Current (Q1)	One Year Ago	Change
US	3.00	2.50	0.50
Eurozone	1.10	2.70	(1.60)
Germany	0.60	2.80	(2.20)
France	1.00	2.80	(1.80)
Italy	0.03	1.67	(1.64)
UK	1.40	1.60	(0.20)
Canada	1.10	3.40	(2.30)
Mexico	1.71	1.48	0.23
Australia	2.30	2.40	(0.10)
Japan	0.30	2.40	(2.10)
China	6.40	6.70	(0.30)
Russia	2.70	0.90	1.80
Brazil	1.07	2.18	(1.11)

Inflation YoY % Change			
	Current	One Year Ago	Change
US	1.90	2.40	(0.50)
Eurozone	1.40	1.40	0.00
Germany	1.30	1.50	(0.20)
France	1.10	1.60	(0.50)
Italy	1.00	0.80	0.20
UK	1.90	2.50	(0.60)
Canada	1.50	2.30	(0.80)
Mexico	4.00	5.04	(1.04)
Australia	1.80	1.90	(0.10)
Japan	0.20	1.10	(0.90)
China	1.50	2.10	(0.60)
Russia	5.30	2.40	2.90
Brazil	4.58	2.68	1.90

Economic Environment
March 2019

- Top line revenue growth has remained strong, and has flowed through to earnings, particularly on the heels of the recent tax package.
- Top line revenues may continue to grow given the economic backdrop, however cost pressures including labor, and the first quarter after the Tax cut will make year over Year comparisons more difficult.
- The stronger dollar and trade tensions may pressure multinationals due to more expensive exports and currency conversions back to the US Dollar.
- Bank earnings will be of interest given the recent interest rate environment. Loan growth should be supportive.





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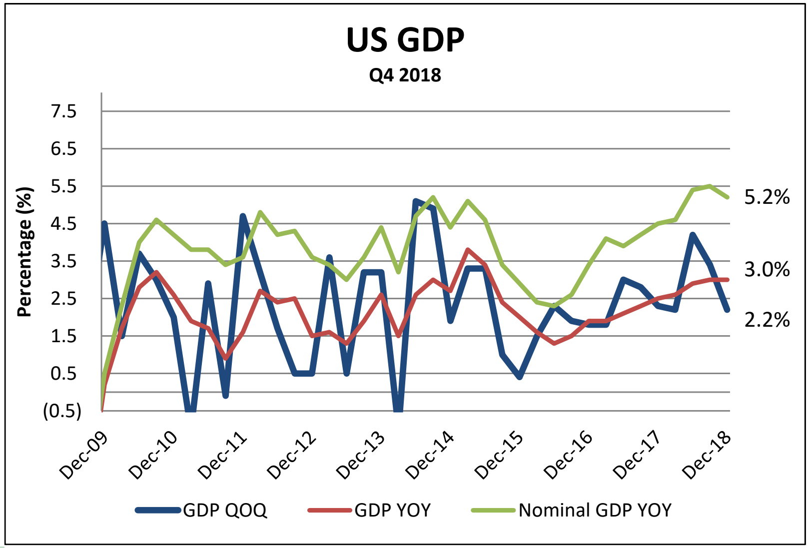
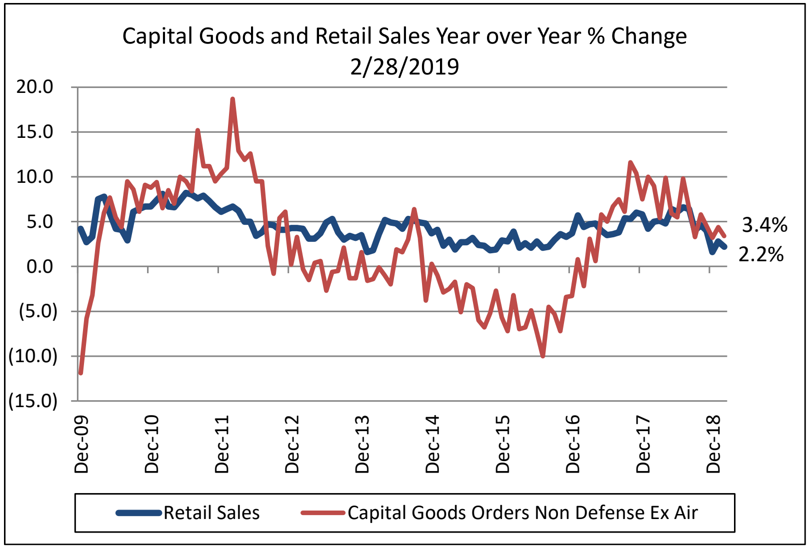
Economic Environment

March 2019

- Economic activity has been maintaining strong growth, in excess of a 3% pace year over year.
- Nominal GDP is running at just over 5% year over year, with rising inflation.
- Consumption and investment has decelerated from the time of the initial tax cut, but remains solid and supported as aggregate income continues to grow and the tax cut is permanent.
- Recent readings on consumption and investment reflect the usual first quarter moderation.





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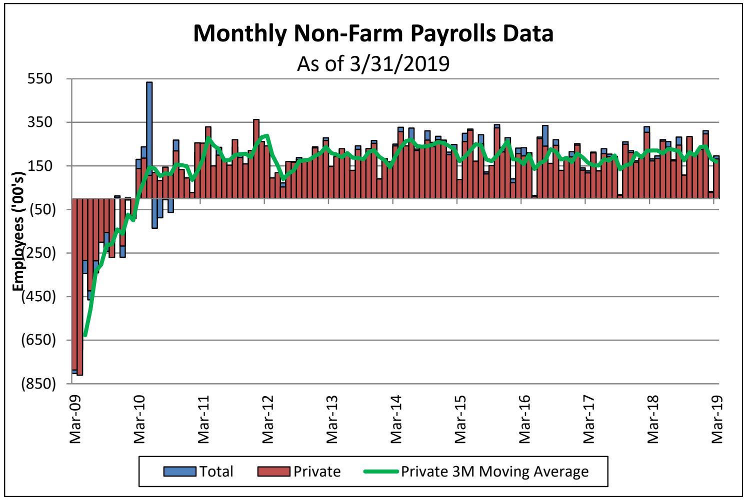
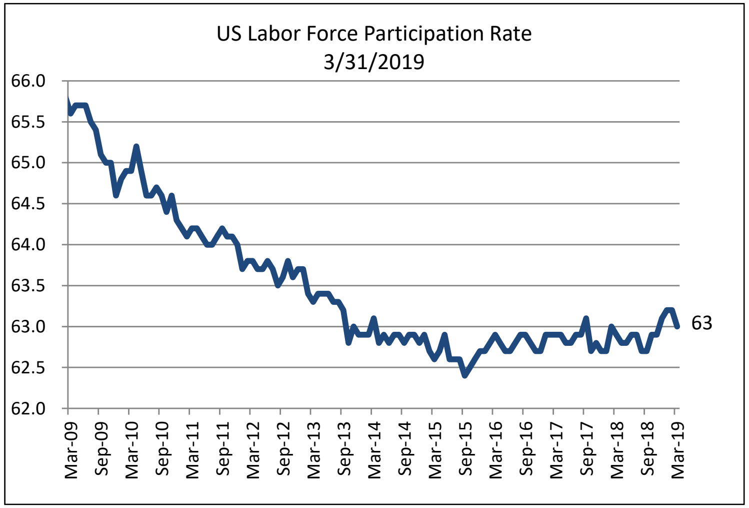
Economic Environment

Employment – Monthly Payrolls – March 2019

- With the exception of a low payroll number in February, Non-Farm payrolls have maintained solid gains and maintained a steady and healthy pace with 3 month average near 200k.
- The labor participation rate has continued to improve, with as many people entering the workforce as are getting hired. In Q1, there continued to be more jobs available than job seekers.
- The nature of the job gains has been broad based across economic sectors, except for Government.
- Wages have continued to rise.





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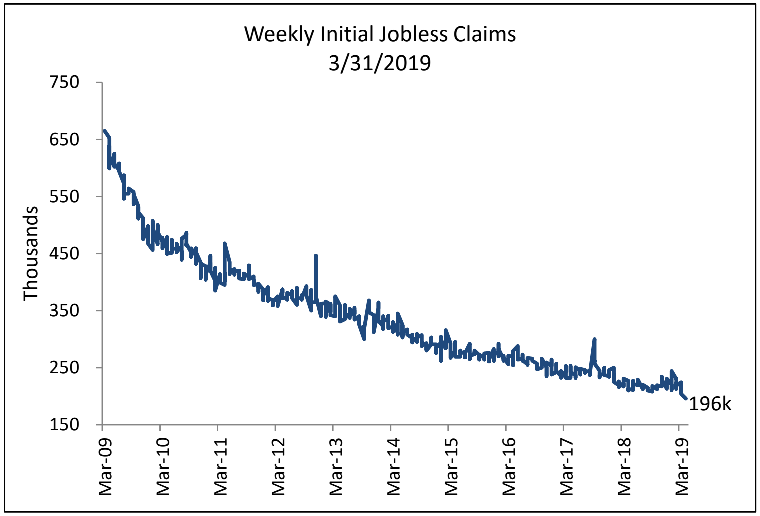
Economic Environment

Employment – Monthly Payrolls – March 2019

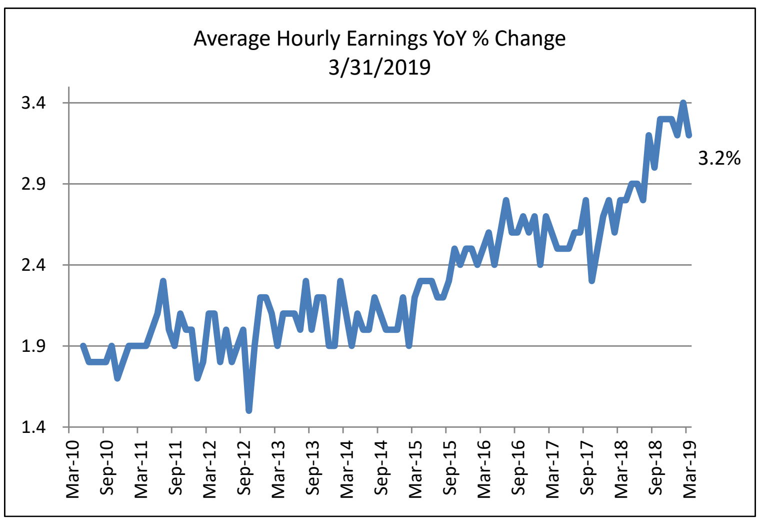
- The unemployment rate is maintaining a steady rate below 4% despite the considerable additions to the labor force.
- Although the labor participation rate has continued to improve, with as many people entering the workforce as are getting hired, it is still relatively low, suggesting room for many more entrants.
- Weekly initial unemployment claims have just moved below 200,000, lowest since the 1969, showing the strength of the employment environment in that there are few layoffs.

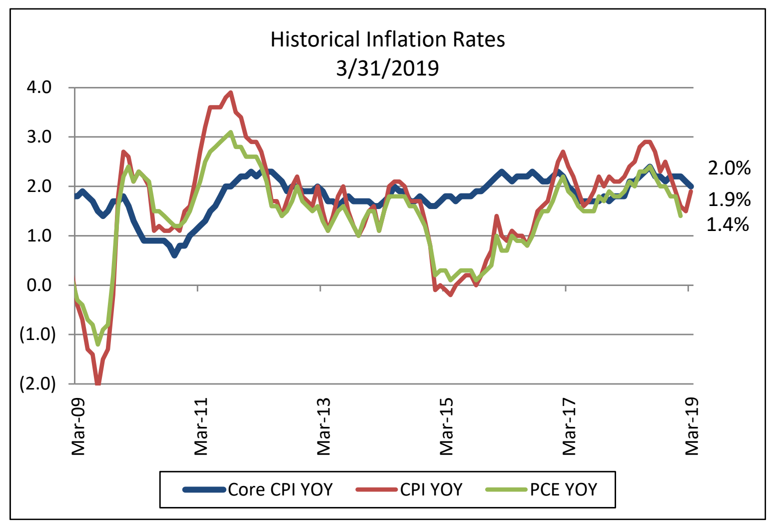


Economic Environment

Employment and Inflation – March 2019

- Average hourly earnings have continued to move higher, evidence of tighter labor market.
- All key inflation measures have reached the Feds targeted 2% level, including core measures that exclude food and energy, and are maintaining that range.
- The YOY Personal Consumption Expenditure Index (PCE), the Feds favored inflation gauge, also reached the target area of 2%, but has recently dipped.





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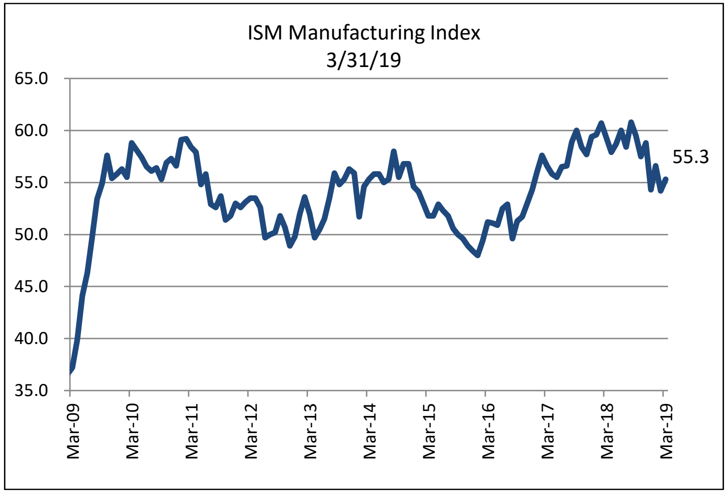
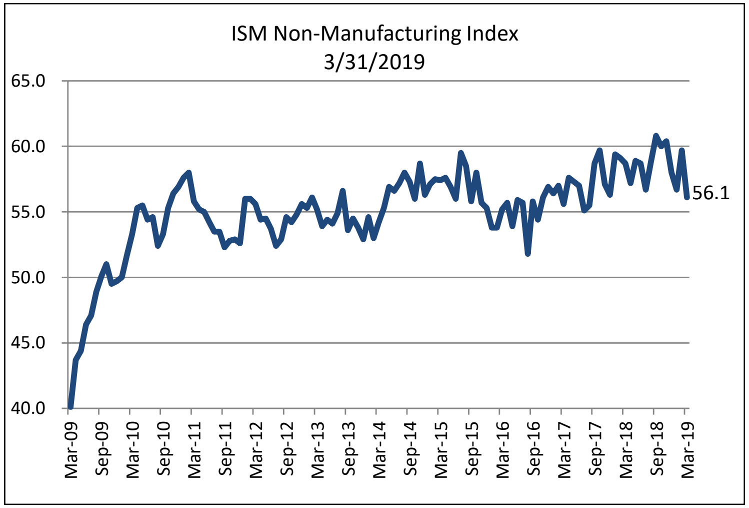
Economic Environment

Investment – March 2019

- Consumption, services, and manufacturing activity have recently moderated from a high rate.
- The manufacturing sector, as measured by the manufacturing purchasing manager index has moderated slightly but remains in a solid growth level of activity including orders, employment, and pricing.
- The Non Manufacturing index has also remained at a strong level, coming off a new record high in Q4.
- The 50 level is what divides expansion/contraction.





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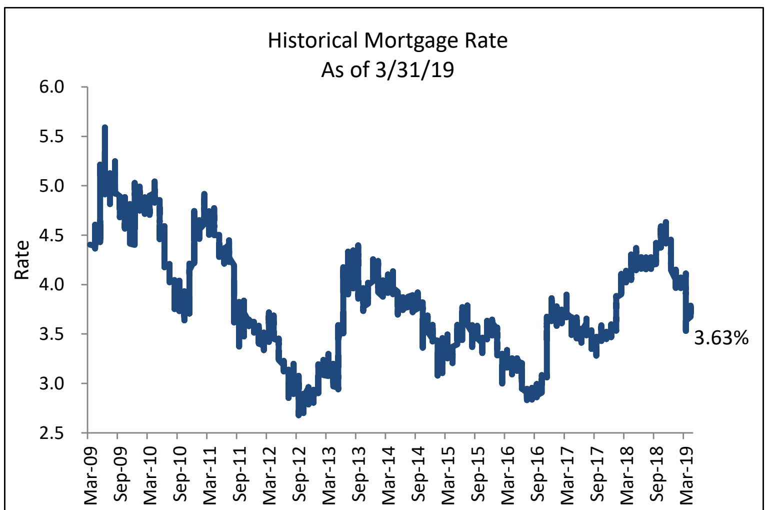
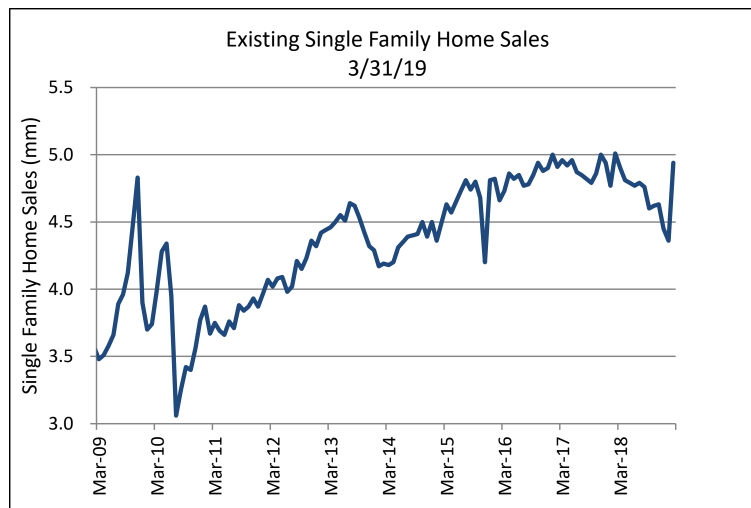
Economic Environment

Mortgage Rates and Housing – March 2019

- The recent drop in interest rates has brought mortgage rates down with it, about 1% from their highs of last year.
- After years of significant price increases, home price increases have begun to moderate.
- The strong jobs market has provided a foundation for new household formation.
- Higher income, lower home prices, increased inventory, and lower interest rates have let to an increase in home purchases.





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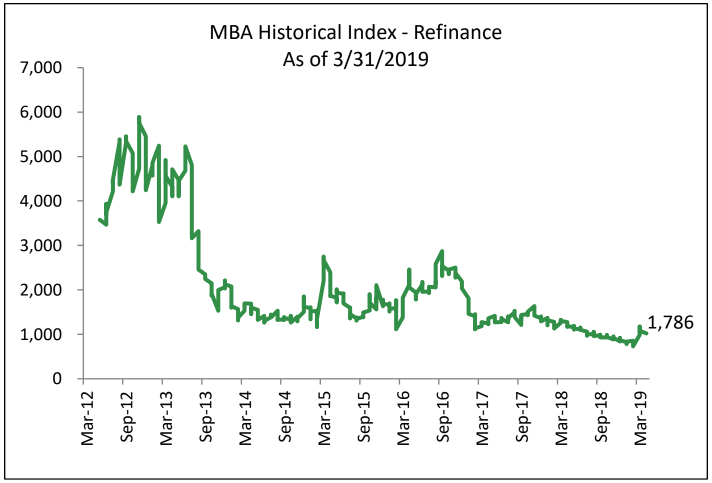
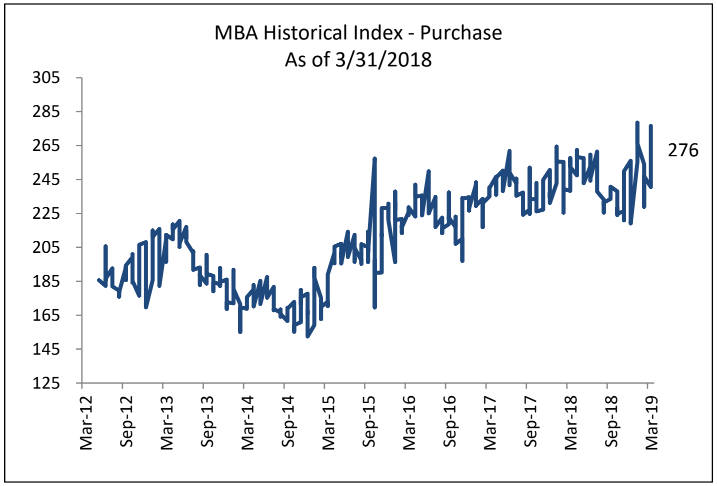
Economic Environment

Mortgage Rates and Housing – March 2019

- The drop in rates has spurred greater mortgage activity with an uptick in refinance activity and continued gains in home purchases.
- The renewed activity in housing, thanks to moderation in prices, an increase inventory and lower rates, will also have ripple effects to purchases of household goods.
- The recent impact of rates on housing may give the Fed more incentive to continue to talk rates down to further spur activity in housing.





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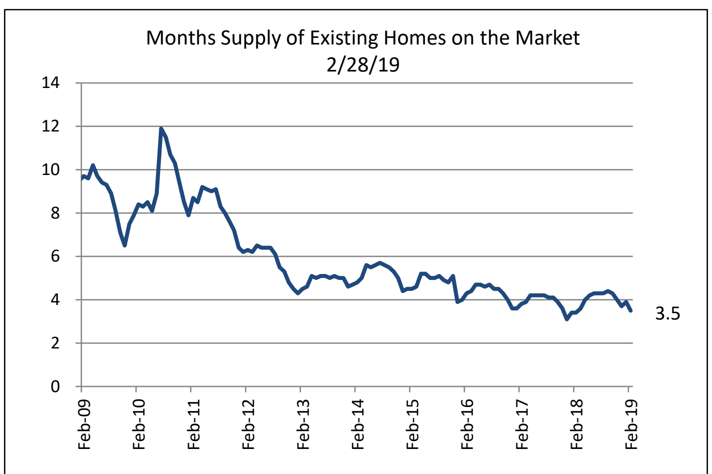
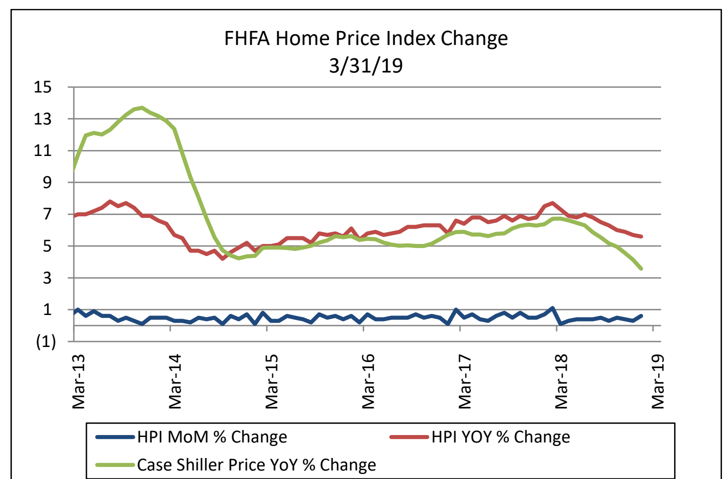
Economic Environment

Mortgage Rates and Housing – March 2019

- The continued robust rise in home prices reduced inventory and began to price many out of the market, slowing the pace of home purchases.
- The slowdown in home purchases had an impact on pricing, and while prices did not decline, the pace of appreciation slowed, and inventories rose.
- The strength of the employment environment, more homes for sale, moderation in prices, and a drop in mortgage rates has spurred activity in the housing market again.





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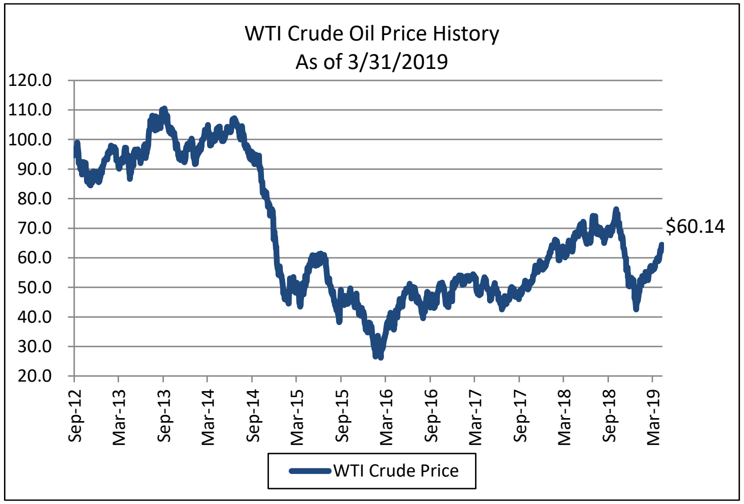
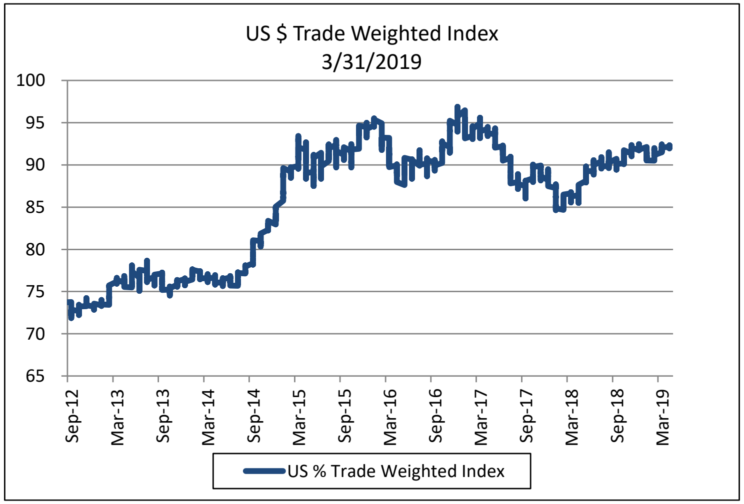
Economic Environment
March 2019

- The dynamics of reduced supply and increased demand have helped boost a recovery in the price of oil.
- Offsetting the significant increase in US oil production, OPEC continues to curb production. Together with sanctions the supply of oil has recently been reduced, helping boost prices.
- The dollar has stabilized in a range recently after a period of appreciation.
- The direction the dollar takes will have implications for emerging markets, earnings of multinational corporate earnings, and trade.





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Market Environment Summary
March 2019

- The Federal Reserve made a significant reversal of monetary policy from tightening to easing in an effort to reverse the adverse reaction to their December rate hike. Risk assets including Equities, High Yield bonds, and emerging markets responded with a full recovery from their December correction.
- Interest rates fell significantly in response to a move to neutral rate policy and a halt to unwinding the balance sheet, effectively stimulating the economy. The Fed has since continued to talk rates down, discussing the risk of global economic slowing– particularly in China and Europe, impacting the US Economy. They continue to discuss the lack of inflation limiting the need to hike.
- Intermediate term interest rates fell below the Fed Funds rate, explicitly pricing in the probability of a Fed rate cut during 2019. Technical factors and Fed policy have helped push rates artificially low.
- Despite the moderation abroad, moderation in Q1 US economic statistics, and the implications of the rate environment, the US economy is on solid footing. A Fed ease in 2019 is unlikely.
- The recovery in equity markets is again being led by growth stocks including technology and consumer cyclicals, and High Yield and deeper credit corporate risk premiums have tightened considerably, pointing to healthy economic and corporate environment.
- Strong employment and income together with lower taxes, stronger corporate investment and earnings may enable the economy and equity markets to continue to march higher, with interest rates moderating at higher levels.
- Many of the risks evident in the first quarter such as a Trade agreement with China and a government shutdown have faded away or improved. Volatility should subside over the next quarter.