



Portfolio Perspectives

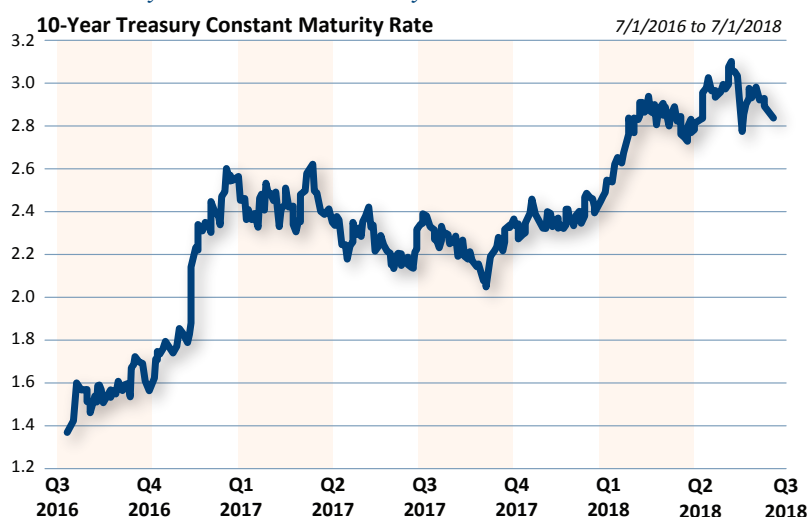
Two Years and Too Fast: Feeling the Impact of Rising Interest Rates

A Bond Manager's Worst Nightmare

For the majority of bond managers, the most difficult environment to navigate is a market where rates rise significantly and rapidly with very little in the means of coupon payment to offset the negative impact of raising rates.

The past two years have been just that — a bond manager's worst nightmare — a doubling of interest rates with an extremely low coupon at the onset.

Since July 6, 2016 (after Brexit), the yield on the 10-year Treasury has more than doubled, from 1.38% to 2.85% as of June 30, 2018.



Source: FRED, Board of Governors of the Federal Reserve System

A Bond Bear Market Is Not Like a Stock Bear Market

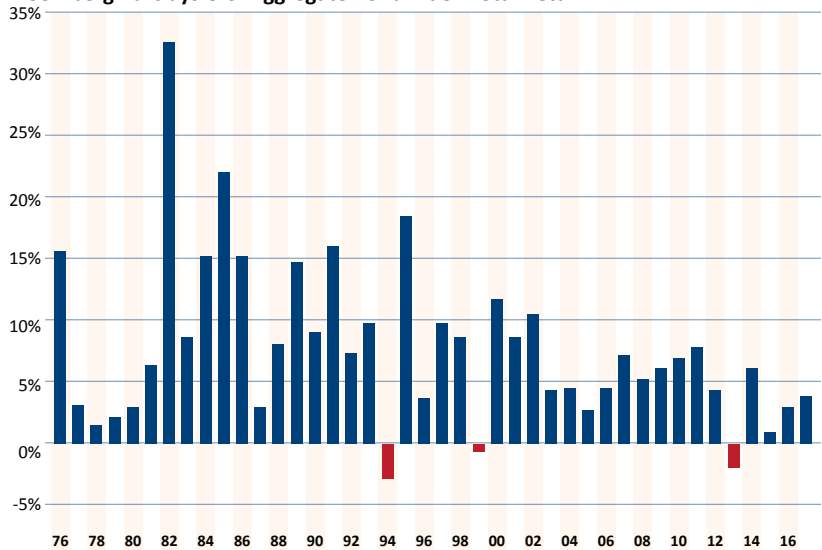
Since the inception of the Bloomberg Barclays Aggregate Bond Index on 1/1/1976, there have only been three calendar years with negative returns — 1994, 1999, and 2013. The worst of these years was 1994, a year in which the Fed raised the target on the Fed Funds rate six times for a total increase of 2.5%. Even in this environment, the Index was only down 2.92%.

What many investors don't take into consideration is that, even in difficult bond markets, bonds have historically not experienced the dramatic declines typical of an equity bear market. Stocks simply have greater volatility than bonds.

What's surprising to many, is that the Index had positive returns throughout the last half of the 1970s, a period when the yield on the 10-year Treasury went from 7.77% to 15.84%. The coupon

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Bloomberg Barclays U.S. Aggregate Bond Index Total Return



Source: Bloomberg

This is not a recommendation to buy or sell a particular security. Please see attached disclosures.

rate during that period was high enough to offset the principal decline associated with the increase in rates.

Not All Asset Classes React The Same to Rising Rates

Many investors ask, “Isn’t it difficult to make money in any asset class when interest rates are rising?” The answer is that not all asset classes react the same to rising rates. Over the past two years, equities have performed well, as have bonds that are more influenced by credit rather than interest rate risk.

For example, high yield bonds were up 7.54% per year while treasuries, which are only influenced by changes in interest rates, were down 1.49% per year.

U.S. Equity	2 Years (Annualized)
S&P 500	16.12%
Russell 1000	16.27%
Russell 2000	21.03%
Russell 3000	16.63%
Russell 1000 Value	11.06%
Russell 1000 Growth	21.46%
International Equity	
MSCI Emerging Market	16.12%
MSCI World ex US Index	13.67%
Fixed Income	
BBgBarc U.S. Aggregate Bond	-0.36%
BBgBarc U.S. Treasury	-1.49%
BBgBarc U.S. Corporate	0.72%
BBgBarc U.S. Corporate High Yield	7.54%
BBgBarc Municipal 5-Year Bond	0.53%

We believe the best way to navigate these challenging markets is to take an active and tactical approach. Putting all of this together, we currently favor credit over interest rate risk and believe that these conditions should support a stable or narrowing credit spread and help corporates outperform treasuries.

With interest rates doubling from a very low standing point, we believe the biggest challenges facing bonds are behind us.

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The S&P 500 measures the performance of the 500 leading companies in leading industries of the U.S. economy, capturing 75% of U.S. equities.

The Russell 1000 Index measures the performance of the large-cap segment of the U.S. equity universe. It is a subset of the Russell 3000® Index and includes approximately 1000 of the largest securities based on a combination of their market cap and current index membership. The Russell 1000 represents approximately 92% of the U.S. market.

The Russell 2000 Index measures the performance of the 2000 smallest U.S. companies based on total market capitalization in the Russell 3000, which represents approximately 11% of Russell 3000 total market capitalization.

The Russell 3000 Index measures the performance of the 3000 largest U.S. companies based on total market capitalization, which represents approximately 98% of the investable U.S. equity market. The S&P 500 measures the performance of the 500 leading companies in leading industries of the U.S. economy, capturing 75% of U.S. equities.

The Russell 1000 Value Index measures the performance of the large-cap value segment of the U.S. equity universe. It includes those Russell 1000 Index companies with lower price-to-book ratios and lower forecasted growth values.

The Russell 1000 Growth Index measures the performance of the large-cap growth segment of the U.S. equity universe. It includes those Russell 1000 Index companies with higher price-to-book ratios and higher forecasted growth values.

The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets. The MSCI Emerging Markets Index consists of the following 21 emerging market country indices: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand, and Turkey.

The MSCI World ex US Index is a market capitalization-weighted index designed to measure equity performance in 22 global developed markets, excluding the United States. The benchmark for this composite is used because the MSCI World Ex US Net Index is generally representative of international equities. Index returns reflect the reinvestment of income and other earnings and are provided to represent the investment environment during the time period shown.

BBgBarc U.S. Aggregate Bond Index covers the U.S. investment-grade fixed-rate bond market, including government and credit securities, agency mortgage pass-through securities, asset-backed securities and commercial mortgage-based securities. To qualify for inclusion, a bond or security must have at least one year to final maturity, and be rated investment grade Baa3 or better, dollar denominated, non-convertible, fixed rate and publicly issued. The BBgBarc U.S. Aggregate Bond Index is generally representative of broad based U.S. fixed income. Index returns reflect the reinvestment of income and other earnings, are provided to represent the investment environment during the time period shown and are not covered by the report of independent verifiers.

The BBgBarc US Treasury Index measures US dollar-denominated, fixed-rate, nominal debt issued by the US Treasury. Treasury bills are excluded by the maturity constraint, but are part of a separate Short Treasury Index. Index returns reflect the reinvestment of income and other earnings, are provided to represent the investment environment during the time period shown and are not covered by the report of independent verifiers.

The BBgBarc U.S. Corporate High-Yield Index covers the U.S. dollar-denominated, non-investment grade, fixed-rate, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody’s, Fitch, and S&P is Ba1/BB+/BB+ or below. Index returns reflect the reinvestment of income and other earnings, are provided to represent the investment environment shown, and are not covered by the report of independent verifiers.

The BBgBarc 5-Year Municipal Bond Index is the 5 Year (4-6) component of the Municipal Bond index. It is a rules-based, market-value-weighted index engineered for the tax-exempt bond market. The index tracks general obligation bonds, revenue bonds, insured bonds, and pre-refunded bonds rated Baa3/BBB- or higher by at least two of the ratings agencies.

The indices shown are for informational purposes only and are not reflective of any investment. As it is not possible to invest in the indices, the data shown does not reflect or compare features of an actual investment, such as its objectives, costs and expenses, liquidity, safety, guarantees or insurance, fluctuation of principal or return, or tax features.

The volatility (beta) of an account may be more or less than that of an index.

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