Intermediate Fixed Income Composite

First Quarter 2017 | Commentary

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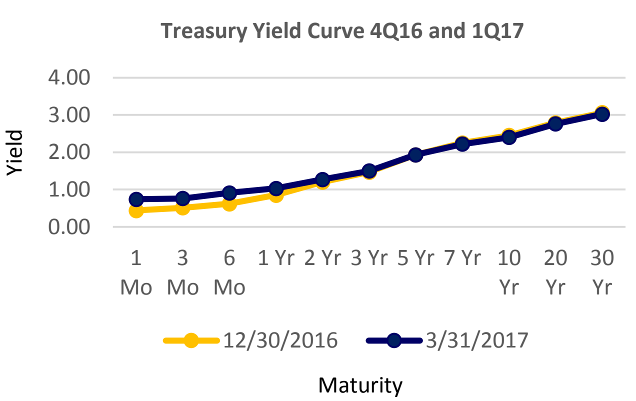
Market Commentary

The equity markets rallied in the first quarter of 2017 on expectations that President Trump will follow through with his campaign promises to boost the US economy. The S&P 500 posted a 6.1% total return for the quarter and hit an all-time intra-day high in March. In addition to the optimism displayed by the market for Trump's presidency, economic data came in strong with the ADP and Non-Farm numbers beating expectations for January and February. The unemployment rate dropped to 4.7% in February in conjunction with a slight increase in the participation rate. Global equity markets showed strong performance with the MSCI Emerging Market index boasting an 11.5% return for the first quarter.

As anticipated, the Federal Reserve raised the Federal Funds rate to 0.75% to 1.00% in March. Despite the rate hike, the yield curve flattened, leaving longer term interest rates a few basis points lower, while shorter term rates increased. The Bloomberg Barclays U.S. Aggregate posted a 0.82% return lead by the Corporate Investment Grade sector which returned 1.22% for the quarter. With the drop in yield on the long end of the yield curve, longer duration securities outperformed.

Commodity and currency markets were mixed during the quarter. Energy prices declined; crude oil (as measured by West Texas Intermediate or WTI) was down nearly 6% and natural gas down over 16%. The poor performance in the energy space is mainly attributable to higher crude inventories and uncertainty of the continued cooperation from OPEC members. The US Dollar dropped while the Japanese Yen strengthened against a basket of major currencies. Precious metals showed strong gains helped by a weaker US dollar, with SPOT gold up 8.9% and SPOT silver up 14.7%.



Source: Bloomberg

Portfolio Commentary

In the first quarter of 2017, the Composite returned 0.74% (gross of fees) and 0.65% (net of fees), underperforming the Bloomberg Barclays U.S. Aggregate Bond Index ("Benchmark") return of 0.82%.

The Composite's largest sector, agency commercial mortgage-backed securities (CMBS) (38.8% of the Composite), returned 0.6%, underperforming the U.S. Government subsector return of 0.68%. The higher income profile positively impacted returns, but it was not enough to overcome the relative underperformance of Swaps vs. Treasuries.

The Composite's second largest sector, single family agency mortgage-backed securities (29.0% of the Composite), returned 0.50% in the quarter, outperforming the U.S. MBS sector return of 0.47%. The sector exhibited slower prepayments while generating higher income relative to the Benchmark MBS sector.

The third major sector in the Composite, taxable municipal bonds (20.8% of the Composite), underperformed the U.S. Credit sector, returning 0.50% compared to 1.30%. Corporate spreads tightened by 5 basis points ('bps') while taxable municipal spreads widened by 5 bps. The lower income profile (Yield-to-worst YTW: 2.73% vs. 3.23%) also negatively impacted relative returns during the quarter.

The Composite's risk/return data continues to exhibit a superior profile compared to the benchmark. For the 5-year period ending March 31, 2017, the Composite's standard deviation (volatility of monthly returns) is 2.41% versus the benchmark's standard deviation of 2.88%. The Composite's Beta and Alpha is 0.80 and 0.45%, respectively.

As of March 31, 2017 the Composite's YTW is 2.89%, which once again is above the Benchmark's YTW of 2.61%. We feel the Composite is fundamentally well positioned given its lower duration (interest rate risk) compared to the benchmark and its higher concentration in agency and government guaranteed securities.

The portfolio management team does not anticipate any changes to its current asset allocation weightings.

Sources: Barclay's Live, Bloomberg PORT, eVestment Alliance

MSCI Emerging Market: Morgan Stanley Capital International (MSCI) Emerging Market Index. The MSCI Emerging Markets Index consists of 23 countries representing 10% of world market capitalization and is available for a number of regions, market segments/sizes and covers approximately 85% of the free float-adjusted market capitalization in each of the 23 countries.

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Bonds and bond funds are subject to interest rate risk and will decline in value as interest rates rise. Past performance does not guarantee future results. This performance report should not be construed as a recommendation to purchase or sell any particular securities held in composite accounts. Market conditions can vary widely over time and can result in a loss of portfolio value. The results portrayed included the reinvestment of dividends, interests and other earnings. The index information presented herein does not reflect the impact of fees; you cannot invest directly in an index.

Gross returns in this presentation do not include effect of management fees. If included, returns would be lower. Gross returns will be reduced by management fees. For example, a 1% annual fee from an account with a ten-year annualized growth rate of 10% will produce a net result of 8.95%. Actual performance results may vary from this example. Sector attribution is presented on a gross only basis and does not reflect the deduction of management fees. For a more detailed description of fees and expenses, see Form ADV Part 2A.

As of 3/31/17, the average annual gross returns for the Intermediate Fixed Income Composite for 1-year, 5-year, 10-year and since inception (8/30/99) were 0.12% ; 2.32%; 4.20%; and 5.12%. As of 3/31/17, the average annual net returns for the Intermediate Fixed Income Composite for 1-year, 5-year, 10-year and since inception (8/30/99) were -0.21%; 2.01%; 3.87%; and 4.71%.