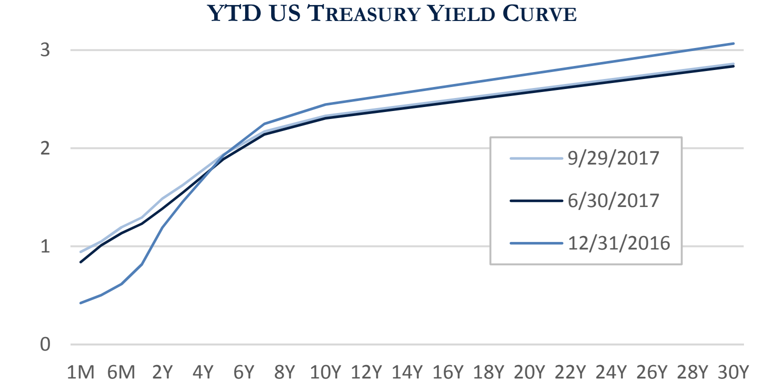
The dominant theme during the first half of 2017 was the disconnect between the worsening political gridlock in DC, and the remarkably calm markets. The third quarter proved no different, as the geopolitical environment managed to deteriorate further with tensions rapidly rising between the US and North Korea and a continuation of the Washington stalemate with no major legislative action passed into law this year. Yet, the markets remained relatively quiet for most of the quarter. There was a brief period where a flight-to-quality trade around Hurricanes Irma, Jose, and Maria drove yields lower over the first two months of the quarter; though, yields did quickly retrace before the quarter ended with the Fed's announcement of plans for a reduction in the balance sheet and the outline of the Trump tax plan.

The Fed's decision to begin a slow and measured balance sheet normalization in October was widely telegraphed, as was their decision to maintain the Fed Funds Rate at 1-1.25%; though, they did slightly lower forward guidance. The latter move was predicated on an unexpected slowdown in inflation (Core PCE fell to 1.29% in August, below the Fed's inflation target of 2%), which Chairperson Yellen has indicated she strongly believes is transitory in nature. The long-run forecast end cycle rate was lowered from 3.0% to 2.75%. Over the course of the quarter, the 10Yr Treasury stayed within a roughly 20bps range, closing virtually unchanged at 2.33%. Most of the moves in Treasury yields were focused 3Yrs and in, which contributed to the yield curve's continued bear flattening in 2017.

U.S FED FUNDS TARGET INTEREST RATE HISTORY

Date	Target	Survey	Direction	Change	Discount
9/20/2017	1.00-1.25%	1.00-1.25%	None	None	1.75%
7/26/2017	1.00-1.25%	1.00-1.25%	None	None	1.75%
6/14/2017	1.00-1.25%	1.00-1.25%	Tightening	0.25%	1.75%
5/3/2017	0.75-1.00%	0.75-1.00%	None	None	1.50%
3/15/2017	0.75-1.00%	0.75-1.00%	Tightening	0.25%	1.50%
2/1/2017	0.50-0.75%	0.50-0.75%	None	None	1.25%
12/14/2016	0.50-0.75%	0.50-0.75%	Tightening	0.25%	1.25%

YTD US TREASURY YIELD CURVE



Source: Bloomberg, API

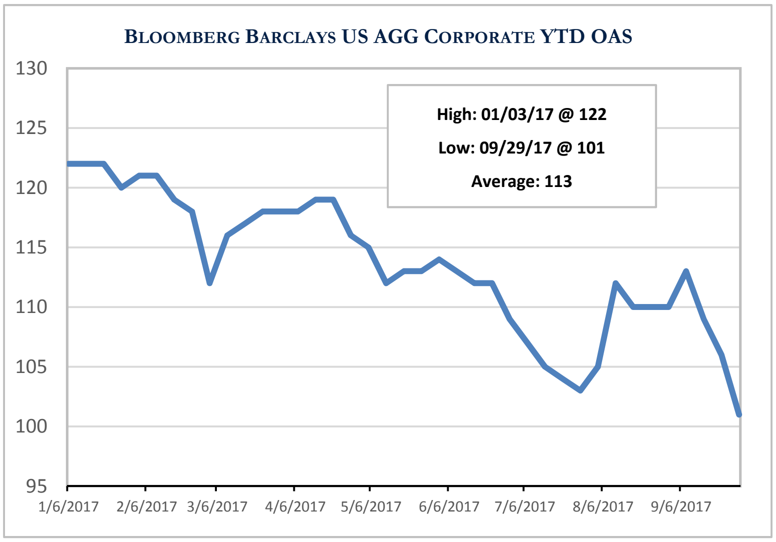
The first half of the quarter proved busy for investment grade corporate credit markets. July started off with a bang, as several major U.S. corporations (including JP Morgan, Wells Fargo, Citigroup, and Bank of America) emerged from earnings blackouts to issue a total of $31 billion in new debt. There was also a decent amount of merger and acquisition activity during the month, with AT&T issuing $22.5 billion worth of debt to fund the Time Warner acquisition. The deal was spread across 7 tranches, including $4.5 billion in 20Yrs, $5 billion in 32.5Yrs, and $2.5 billion in 41Yrs. Those longer maturities required a 10–15 basis point concession to comparables when priced. With that being said, the deal, which was the third largest deal to hit the Investment Grade Credit market, had orders for $65+ billion and was over-subscribed more than 2.8 times. Other notable deals for the month came from British American Tobacco and Amazon.

This gluttony of supply extended into early September, which put pressure on spreads during a time credit markets were already feeling soft from risk-off sentiment spurred by deteriorating US/North Korea relations. Over $90 billion was issued in the first two weeks of the month, notably another $5 billion from Apple and $6.3 billion from Discovery Communications. September tends to be robust and, in this case, there seemed to be some urgency with political uncertainty and the prospects of a Fed hike looming. However, supply faded going into the last week of the quarter, and total new issuance over the quarter came in at $169.92 billion. Year-to-date volume hit $1.31 trillion, down 2% over the same period in 2016. With the decrease in supply and a rebound in investor confidence, credit spreads reversed the widening trend seen during the middle of the quarter. The Bloomberg Barclays US AGG Corporate Index OAS began the quarter at 109 and rose as high 113 on September 8th. Credit spreads rallied to year-to-date and multi-year tights, and the index closed out the quarter at 101.

The much-anticipated Trump tax plan announced at the end of September has the potential to put its mark on the taxable bond market, but not enough is known about the broader details to make concrete assessments on its effects. We have already seen that the initial response from the market has been positive, but there seems to be some concern due to the lack of any detail and the continuing political gridlock in Washington. One of the larger components of the tax plan is the potential for repatriation of the estimated $3 trillion in corporate cash that is overseas, which could bring in enough funds to help offset a corporate tax reduction. This repatriation could put pressure on Investment Grade corporate supply to the downside, although it is not clear that companies will buy back debt. Another issue is the possibility of limiting the deductibility of interest for corporations, which in theory could send companies striving to de-lever their balance sheets and potentially create a better corporate credit environment.

APPLETON PARTNERS, INC. ONE POST OFFICE SQ. BOSTON, MA 02109 TEL. 617.338.0700 WWW.APPLETONPARTNERS.COM

However, it is unclear that companies would then look to enact that action in the short term, as it would likely take quite some time to de-lever an already highly leveraged market. We will continue to monitor how the tax plan unfolds in order to determine the potential impacts on our market. Despite the lack of clarity, we expect demand for Investment Grade taxable bonds to remain strong. We believe this should be especially true for higher rated and less volatile names and sectors.



Source: Bloomberg

As we enter the final quarter of 2017, there are a number of major macro themes that we believe have potential to shape the remainder of the year. Inflation remains stubbornly low despite a labor market approaching full employment, and continued weakness here will likely prevent the Fed from hiking rates further. The steady escalation of rhetoric between the US and North Korea, with the real possibility of open military engagement, also bears watching. Lastly, we will continue to monitor developments regarding the Republican tax plan. In the wake of the Republican health care plan collapse, the market remained reassured by the belief that this would allow the party to pivot more quickly to tax reform. That pivot failed to materialize, and any further delay may begin to jeopardize the tax plan by occupying valuable legislative time. Overall, we see an economy little changed from the start of the year, with low unemployment, little inflation, and decent underlying growth. However, the longer political uncertainty weighs on the market, the more the possibility grows that something may at some point manage to shake the market's tranquility. We remain focused on the rhetoric coming out of DC on tax reform, and will continue to assess any market moving policy changes as they formulate.

As always, we welcome your comments and questions. Please contact us if there are any changes to your financial situation or investment objectives. Appleton is on Twitter: follow us at @AppletonPtnrs.