INSIGHTS & OBSERVATIONS

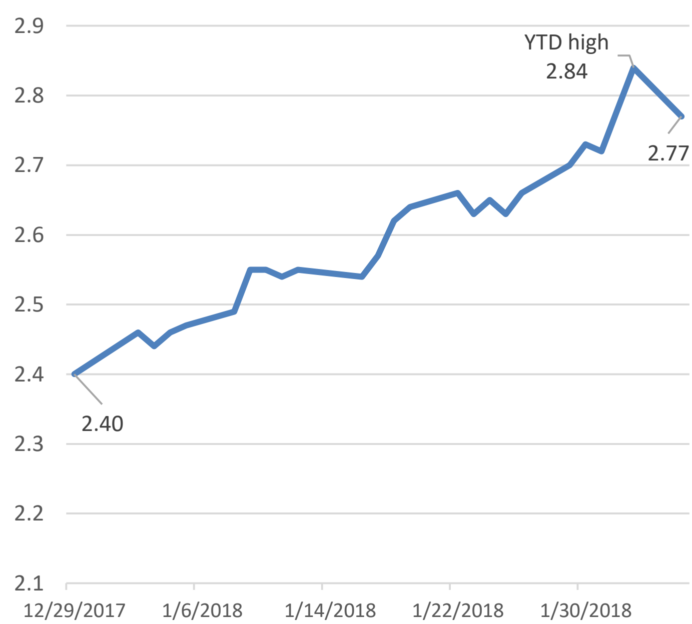
ECONOMIC, PUBLIC POLICY, AND FED DEVELOPMENTS

- The January jobs report released on February 2nd exceeded expectations with the economy adding 200,000 jobs. Perhaps of greater note, wages increased by 2.9%, fueling a spike in the 10Yr to 2.89% before Treasuries rallied back in the face of sharp equity market declines. What may have been overlooked though, was a 0.2% drop in the average January work week, as well as steady productivity growth. ***In our view, this speaks to an expectation of a range bound but modestly rising 10Yr, not a surge in inflation or Treasury yields.***
- The Federal Reserve had previously adjourned Janet Yellen's final meeting as Chairperson by ***holding short-term rates steady at 1.25-1.50%.*** However, given signs that inflation is moving towards and possibly above the Fed's target of 2%, the implied probability of a hike in March had risen to over 99% before dropping sharply to the low 80s in the midst of a sudden equity sell off. ***We expect 2 to 3 short-term rate increases this year and are not in the camp that foresees more hawkish Fed action.***
- The dollar fell by more than 1% on January 24th after Treasury Secretary Mnuchin indicated that a weak dollar was positive for US trade. He and Commerce Secretary Wilbur Ross subsequently walked back the comments. Nonetheless, ***at month end the dollar remained near three-year lows after a long ascend, having fallen 9.9% over the course of 2017***, the largest calendar year decline since 2014**.**
- Barring a currency war, which we do not anticipate despite recent Administration comments, the dollar may have been oversold of late and anticipated stability would mitigate some inflation concerns, in part given the impact on energy prices.
- In the face of a steady rise in Treasury yields, ***the steepness of the curve increased in January***, as the spread between the 2Yr and 10Yr rose from 51 to 67 basis points. The curve steepened somewhat more before the Treasury's decision to upsize February's shorter maturity auctions, citing a larger-than-expected funding gap after the passage of the December tax bill. ***Generally speaking, we continue to see the greatest value in the 6 to 9Yr portion of the curve.***
- Tax cuts were also cited when the CBO shortened its estimation of the length of time the Treasury can continue to operate using extraordinary measures before breaching the debt ceiling. The wall has now been pushed up from early April to mid-March. Despite much brinkmanship, Congress has always managed to raise the debt ceiling before breaching it. ***We expect them to do so again, but the underlying political dynamics could be a source of considerable volatility***, particularly given recently high levels of yield and equity market turbulence.

Dollar Price Action (DXY Index)
12/1/2017 to present

Source: US Dollar Index, ICE, Bloomberg

10 Year Treasury - Year to Date (%)



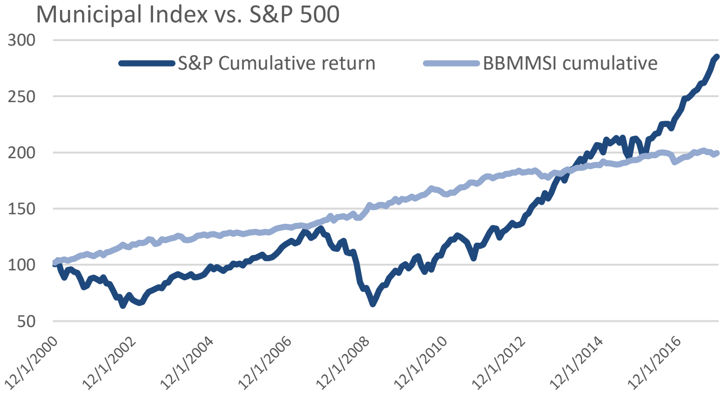
Source: Bloomberg

FROM THE TRADING DESK

MUNICIPAL MARKETS

- With the S&P 500 declining suddenly by 10% soon after the February 6 open, and equity volatility, as measured by the CBEO Volatility index, spiking to its highest levels in several years, asset allocation has resurfaced as a top-of-mind consideration. While the tax-advantaged income attributes of municipal securities are well understood, the ability of the asset class to enhance portfolio efficiency should not be overlooked. As the accompanying chart reveals, ***high quality municipals have historically provided portfolio stability in "risk-off" environments.***

Bloomberg Barclays Managed Money Short/Int. Municipal Index vs. S&P 500



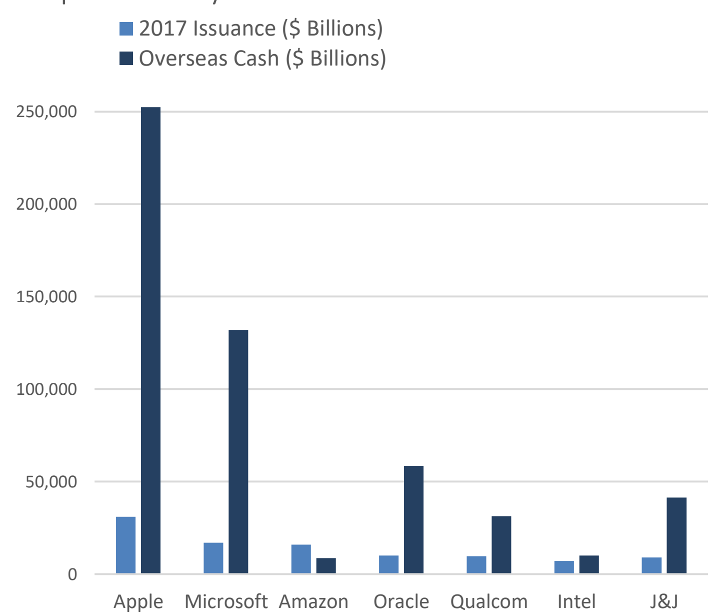
Source: Bloomberg and S&P

- January was a notable month in "Muni-land" as ***the curve steepened dramatically, with 2Yrs to 10Yrs increasing to 80 basis points from 42 basis points***. This move was largely attributed to a yield spike in Treasuries, coupled with a choppy environment on the long end of the curve after some banks and insurance companies reduced their longer maturity exposure given new tax rates. According to the Bloomberg Barclays Index, Munis booked their worst January performance since 1981. ***Relative value has since improved in our opinion, in large part given "risk-off" Treasury demand.***
- As expected, Muni issuance was down nearly 60% in January relative to the prior month due to a pre-tax reform December surge and sharply lower January pre-refunding issuance. ***The year opened with monthly issuance of $16.1 billion, the lowest month since 2011***. While one might expect reduced issuance and robust demand to support performance, otherwise known as the January Effect, this was not the case for the reasons highlighted above. ***Nonetheless, we anticipate net negative issuance in February.***

CORPORATE MARKETS

- As we turn the corner into 2018, ***the new Trump tax laws have seemingly sidelined many issuers of Investment Grade Corporate debt.*** More specifically, the $120.275 billion issued last month was 33% less than last year's record breaking January when uncertainty surrounding the new Trump Administration fueled a rush to market. This year it appears that lack of issuance is tied to the new US tax code which allows corporations to repatriate cash held overseas at a much lower rate of 15.5% vs. the previous 35%.
- The accompanying chart shows the amount of bonds issued by several prominent corporations during 2017 relative to their overseas cash. ***We see the short-term issuance impact and a resulting supply and demand imbalance helping to keep spreads in a tight trading range throughout 2018.***
- An eventual spread widening trend will likely require a significant catalyst, such as economic dislocation and an associated flight to Treasuries. That scenario does not seem likely in the near term.
- ***Longer-term, we feel the market will maintain an appetite for high quality credit as issuance eventually picks up, limiting the impact on credit spreads.***

Repatriation May Slow Debt Issuance



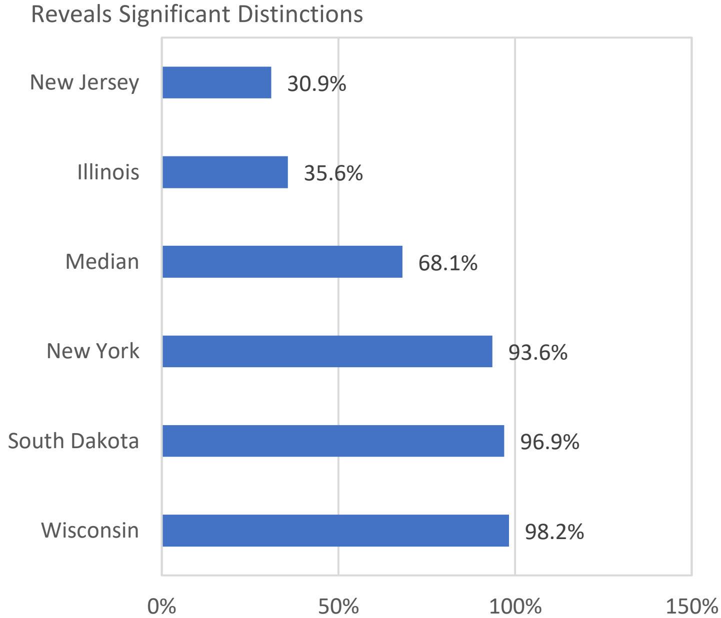
Source: Bloomberg

PUBLIC SECTOR WATCH

CREDIT COMMENTS

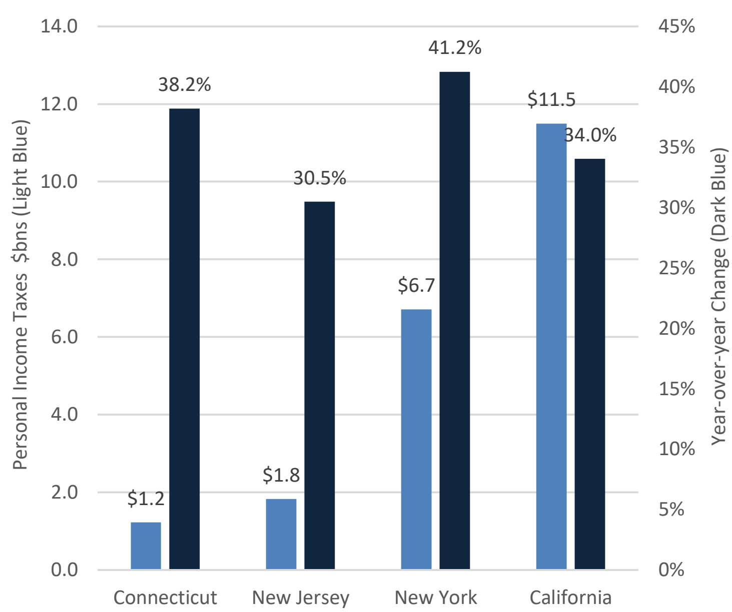
- We recently published a response to a Barron's column, "The Muni Market Time Bomb," published in the January 29th edition. In our judgment, although very real public finance challenges exist, greater context is needed. Woefully inadequate pension funding ratios are evident in certain cases, most notably states like Illinois and New Jersey, as well as cities such as Detroit and Hartford. However, ***acute case specific problems do not translate across the board either in pension funding status or credit quality*** as evidenced in the chart below. The health of municipal entities should not be painted with a broad brush, as ***credit quality is dependent on localized factors such as an issuer's tax base, economic vitality, and fiscal management.*** That's where security specific research comes into play. While we do not dispute the validity of concerns raised in Barron's, a much deeper look at individual issuers and securities, as well as an investment advisor's credit research capabilities, is warranted.
- Puerto Rico recently released a revised fiscal plan and, as expected, ***the Commonwealth does not anticipate making any debt service payments over the next five years.*** A mass exodus of the island's population has increased pressure on an already stressed economy. There is also a bill floating around Congress which would allow Puerto Rico and other US territories to terminate their public debt. ***We continue to view Puerto Rican debt issues as highly speculative*** given deep economic, political and demographic risk.
- State personal tax collection surged in December and January, as taxpayers rushed to take advantage of federal deductibility of state and local taxes before the new $10,000 cap was instituted. However, ***far from a windfall, these "strong" revenues reflect merely a change in timing, and we expect reductions in future months' receipts relative to budgets***. States that continue to budget conservatively and enjoy revenue diversity should weather tax reform well. That is where our credit focus remains.
- A number of states are also considering actions that would allow residents to circumvent the cap on state and local tax deductions. Officials, particularly in high-tax states, are exploring options to swap property taxes for charitable contributions, or to switch from income taxes to deductible employer payroll taxes. No state has yet enacted legislation and implementation hurdles are high. ***We believe the recent tax reform will acutely impact high earners in high-tax states, prompting continued demand for tax-advantaged strategies.***

2016 State Pension Funding Status Reveals Significant Distinctions



Source: S&P, "U.S. State Pensions: Funded Ratios Declined Again in 2016," October 18, 2017

Tax Reform Drives Large December Tax Collections

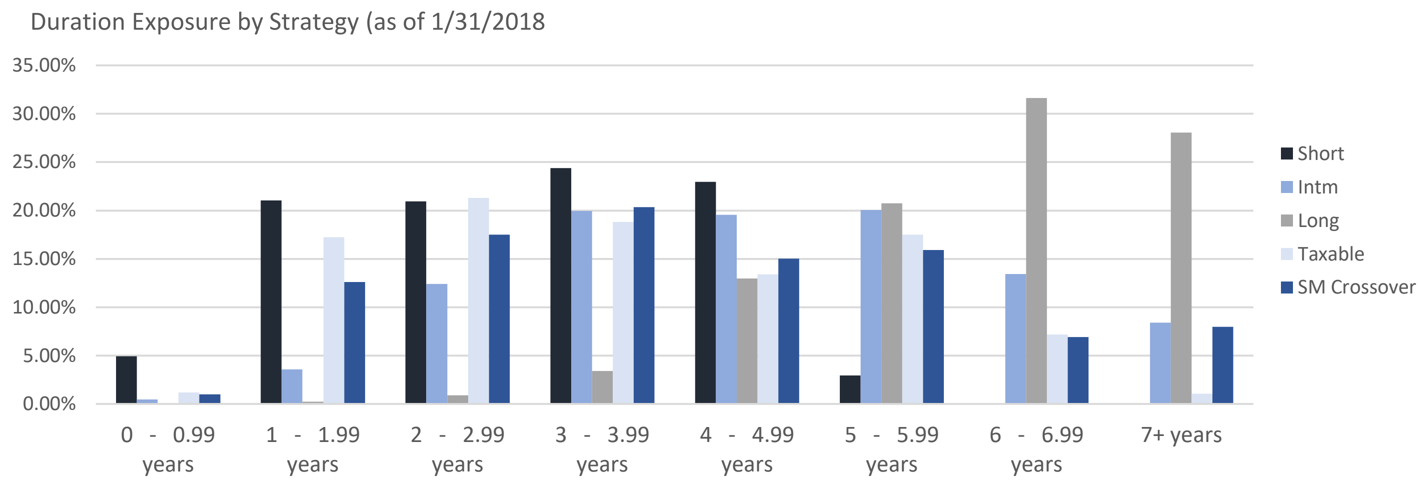


Source: California Controller's Office, New Jersey Office of Legislative Services, Connecticut Department of Revenue Services, New York Department of Taxation and Finance

STRATEGY OVERVIEW

PORTFOLIO POSITIONING (AS OF 1/31/2018)

	Short Municipal	Intermediate Municipal	Long Duration Municipal	Taxable Fixed Income	Strategic Muni Crossover
Average Modified Duration	2.89 years	4.55 years	6.06 years	3.68 years	4.00 years
Average Maturity	3.24 years	6.02 years	10.72 years	4.14 years	5.04 years
Yield to Worst	1.71%	2.02%	2.49%	2.68%	2.33%
Current Yield	4.28%	4.25%	4.21%	3.74%	4.19%
Average Quality	AA+	AA	AA	AA-	AA-



Source: Investortools Perform, Appleton Partners, Inc.

OUR PHILOSOPHY AND PROCESS

- Our objective is to preserve and grow your clients' capital in a tax efficient manner.
- Dynamic active management combined with an emphasis on liquidity affords us the flexibility to react to changes in the credit, interest rate, and yield curve environments.
- Dissecting the yield curve to target maturity exposure can help us capture value and capitalize on market inefficiencies as rate cycles change.
- Customized separate accounts are structured to meet your clients' evolving tax, liquidity, risk tolerance, and other unique needs.
- Intense credit research is applied within the liquid, high investment grade universe.
- Extensive fundamental, technical and economic analysis is utilized in making investment decisions.