APPLETON PARTNERS, INC.

CORONAVIRUS & THE FIXED INCOME MARKETS

CORONAVIRUS & RISK

Fear of the Coronavirus has swept the globe in recent days, leading to a flight to quality that shook equity markets and caused Treasury and tax-exempt yields to fall to record lows. A sharp expected slowdown in global trade, travel and overall economic growth resulted in investors fleeing risk assets at the end of February in favor of the safety of cash and bonds.

Many factors surrounding Coronavirus remain highly uncertain and we have no way of knowing the ultimate magnitude or duration of this health crisis. Like everyone else, we are following developments closely and wanted to share our thinking.

CENTRAL BANK RESPONSE

US equity markets opened March on a highly positive note (S&P 500 +4.60% on 3/2) after suffering through several volatile trading days to close February. The market's rebound was influenced by expectations of renewed Central Bank accommodation. Many analysts expect a coordinated global central bank response, although the G7 taking no immediate action steps on March 3rd somewhat tempered those hopes prior to the Fed announcing a 0.50% Fed Funds cut.

While the effectiveness of monetary policy during a healthcare crisis is uncertain, we were not surprised to see the Fed be aggressive. We also anticipate growth in the Fed's balance sheet. Policy response is aimed at bolstering confidence and ensuring markets maintain ample liquidity and credit availability.

MUNICIPALS: CALM AMID THE STORM

As recent events have unfolded, municipals rallied along with Treasuries, reinforcing the important hedge municipals can offer as part of a diversified asset allocation strategy. During February, the S&P 500 fell by 8.23%, whereas the Bloomberg Barclays Managed Money Short/Intermediate Index produced a positive 0.66% return. Despite today's extremely low nominal yields, the value of minimal correlation to equities, relative price stability, and tax-advantaged income should not be discounted.

MAINTAIN CREDIT VIGILANCE

We are cautious on credit and see a risk of spreads widening among lower quality tax-exempt names. Strong technical factors marked by surging retail demand ($93.6 billion in net mutual fund flows in 2019, plus $23.6 billion YTD) coupled with constrained supply have kept municipal spreads very tight across the quality spectrum. Last week's flight to quality did not alter that dynamic as lower grade issues rallied in synch with higher quality bonds.

Even in the face of record low yields, we do not recommend going "down in quality". The risk premium is low and certain issuers could face credit stress should the economic implications of today's healthcare crisis worsen. Our municipal research team is assessing potential sector and issuer specific credit impact. The accompanying chart summarizes a few high-level thoughts.

Sector	Potential Impact
State and Local Governments	• Short-term liquidity challenges associated with costs to contain, treat and recover from widespread infection • Longer-term liquidity challenges of this nature are likely to be alleviated by state and federal aid • Densely populated areas assume greater risk of accelerated virus spread than sparsely populated regions • Regions heavily reliant on tourism are most at-risk of a decline in economic activity
Special Tax	• Fear of contagion could reduce economic activity, thereby constraining sales and use tax revenues • Special Tax Bonds secured by narrower revenue streams, particularly those associated with tourism and recreation, could face credit challenges
Transportation	• Airports, mass transit and toll roads are susceptible to declines in economic activity, demand and revenues • Reduced global trade would likely hit ports most acutely. While minimum guaranteed payments cover short-term disruptions, a prolonged downturn in trade would negatively impact credit profiles of companies making these payments
Healthcare	• A short-term surge in demand would positively impact revenue • Under a prolonged virus scenario, increased funding from state, federal and non-profit organizations to healthcare entities is likely

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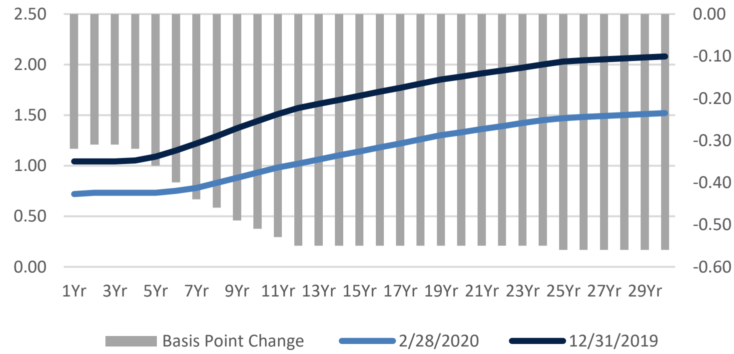
Duration & Curve Positioning

Our portfolios are defensively positioned by nature in terms of duration and curve exposure, credit, coupon and call structures. In our Intermediate strategy, duration targets remain in a 4.60 to 4.70-year range and we feel the 6 to 12Yr portion of the AAA municipal curve still offers the greatest value. The spread differential between 1 and 10-Year issues was 15 basis points on March 2nd versus only 1 basis point between 1 and 5 years. Beyond 12 years the curve also flattens out.

While greater clarity and comfort concerning the ultimate impact of Coronavirus may cause yields to rise modestly off today's lows, we do not see rates moving significantly higher over the near-term.



Source: MMD

Bond Structure

We seek opportunities in dynamic markets and actively analyze bond structure. Assessing features such as coupons, call options or put clauses can identify pockets of relative value. For example, we have long gravitated towards premium bonds given their slightly lower durations than par bonds with similar maturity and call features due to the greater coupon and increased cash flows.

Corporate/Taxable Bonds

Unlike municipals, corporate high yield spreads widened considerably as global economic fears proliferated. High Yield OAS rose over the last week of February from 331 to 500 basis points, while "CCC"-rated corporate spreads (a quality rating we do not hold) exceeded 1,000 basis points over US Treasuries for the first time since August 2016. Investment grade spreads have held up significantly better, widening 27 basis points to 122 basis points by the end of February.

We are maintaining a high investment grade focus (our High Grade Intermediate Gov't/Credit composite has an AA-/Aa3 average credit quality) and have been transitioning up in quality in preparation for a scenario such as this. Along with diversified higher investment grade corporates, we have increased portfolio exposure to about 15-20% in taxable municipals, along with 15-20% in US Treasuries. Exposure to BBB rated credit accounts for less than 4% of our High Grade Intermediate Gov't/Credit composite.

As events move forward, several Appleton attributes are worth re-emphasizing:

- Quality and liquidity are central to all our investment strategies.
- Rigorous credit research stands behind our security selection. All bond holdings are assigned proprietary credit ratings and undergo ongoing credit surveillance.
- Our active strategies invest in what we see as the best opportunities at the time of purchase, rather than implementing a static model. This can be advantageous in volatile markets.
- Communication is essential and access to our portfolio managers and relationship team offers you an ability to speak directly with our senior personnel. Please do not hesitate to reach out.

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