Managing a Fixed Income Portfolio in Today's Environment

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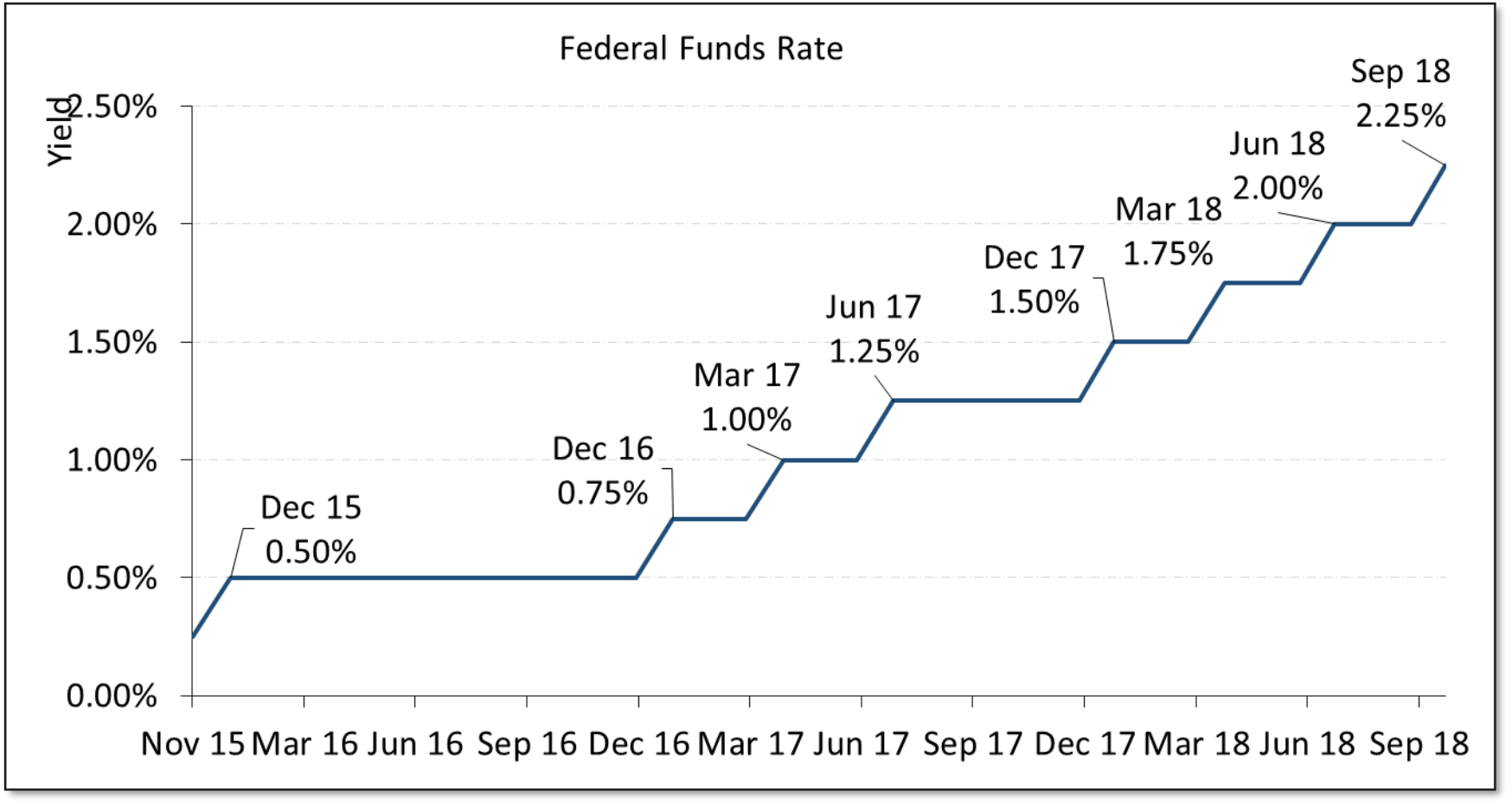
Federal Funds Rate Hike Scenarios

- The FOMC voted to increase the Federal Funds overnight rate to a range of 2.00% - 2.25% during the September 2018 meeting. This is was the eighth 0.25% rate hike during the current cycle.



Source: Bloomberg. See additional footnotes at the end of the presentation.

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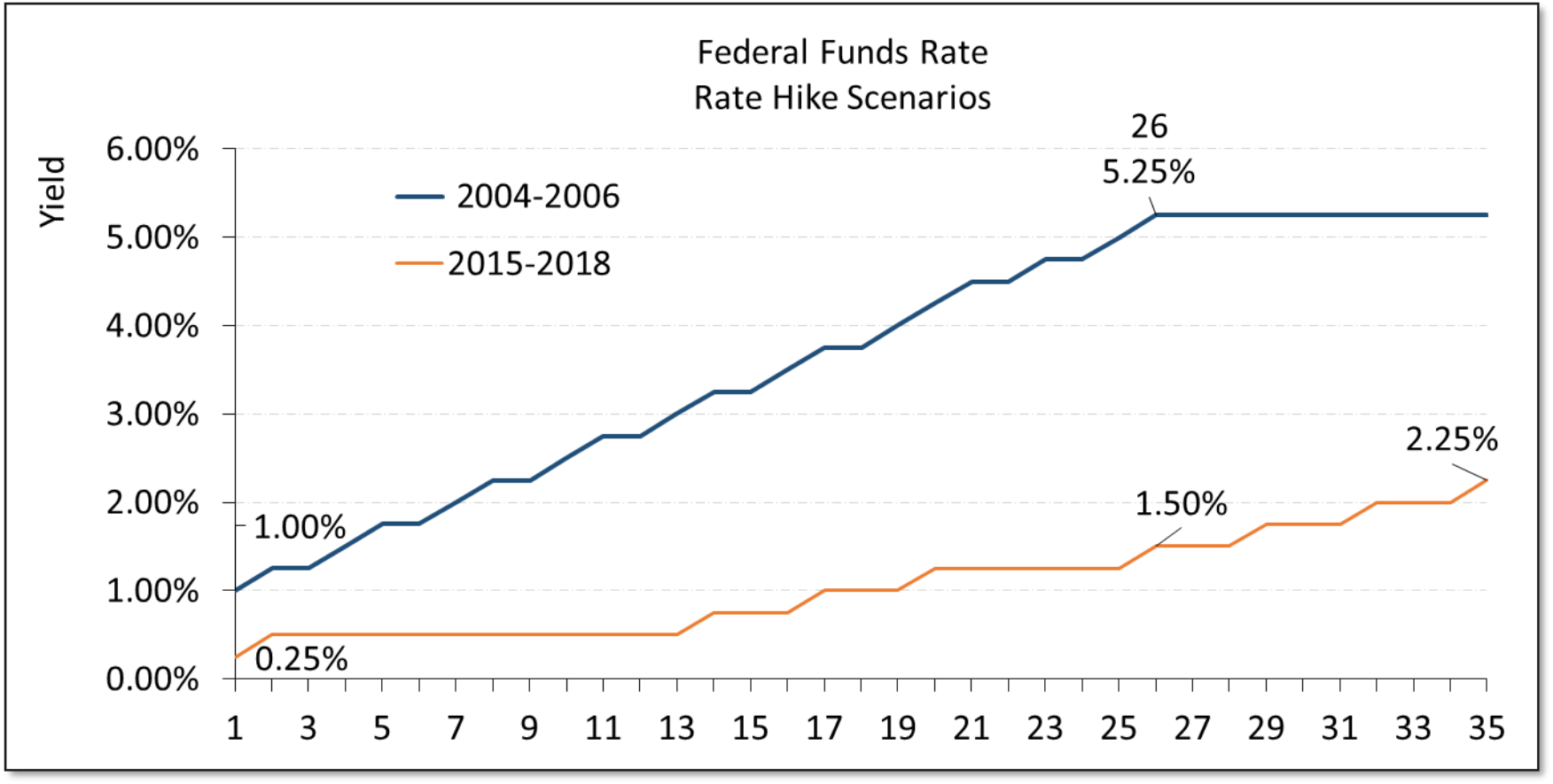
Federal Funds Rate Hike Scenarios

- The first 35 months of the current rate hike cycle has eight 0.25% increases compared to the 2004-2006 cycle which had 17 0.25% in the same time frame.



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FOMC Dot Plot – September 2018

- FOMC Members are undecided on the path of long term rates.

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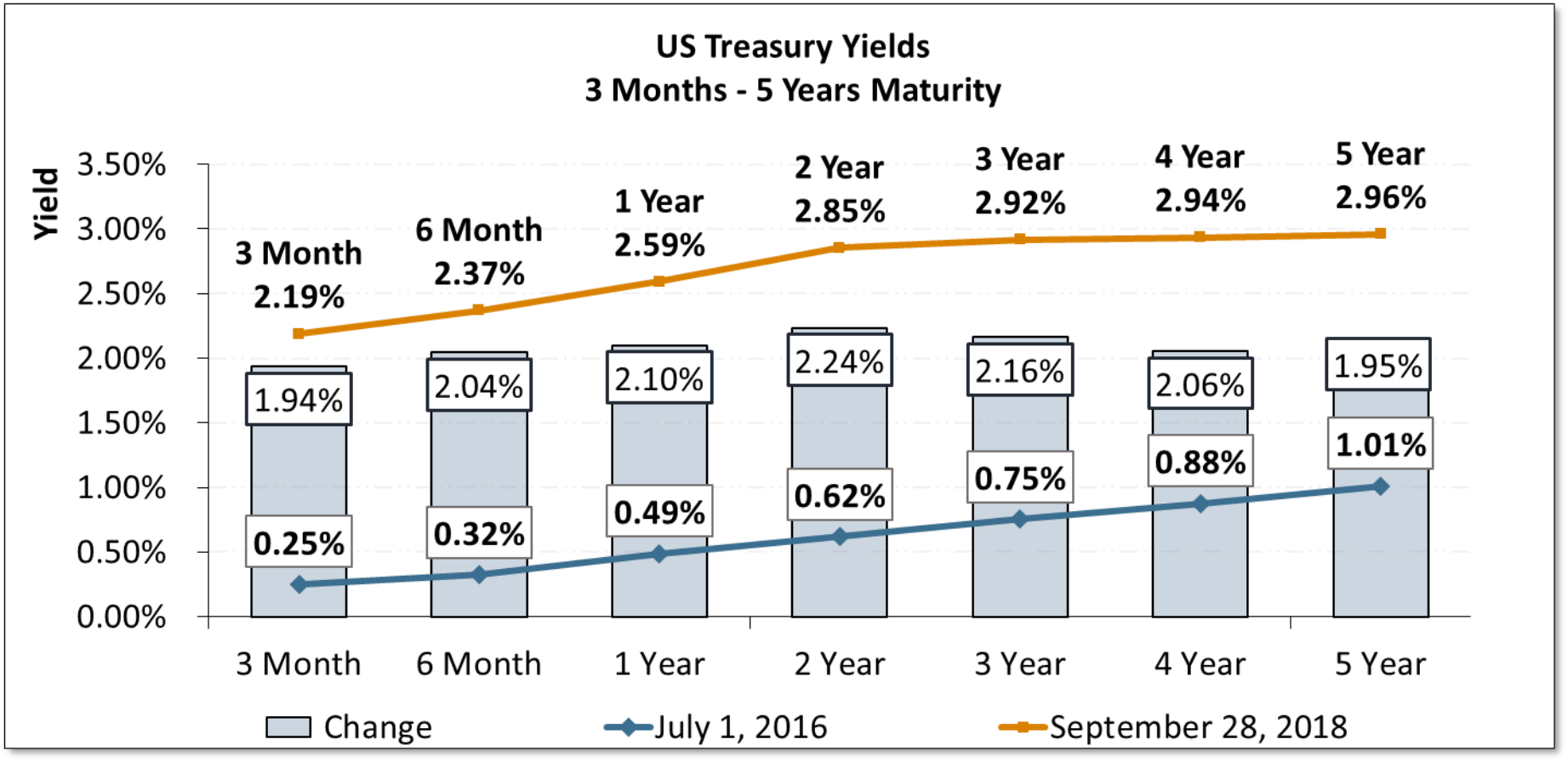
Yields are up to 200 Basis Points higher since 2016

- Interest rates continued the increasing, yet flattening trend, as shorter term maturities experienced larger increases in rates as compared to long term maturities.



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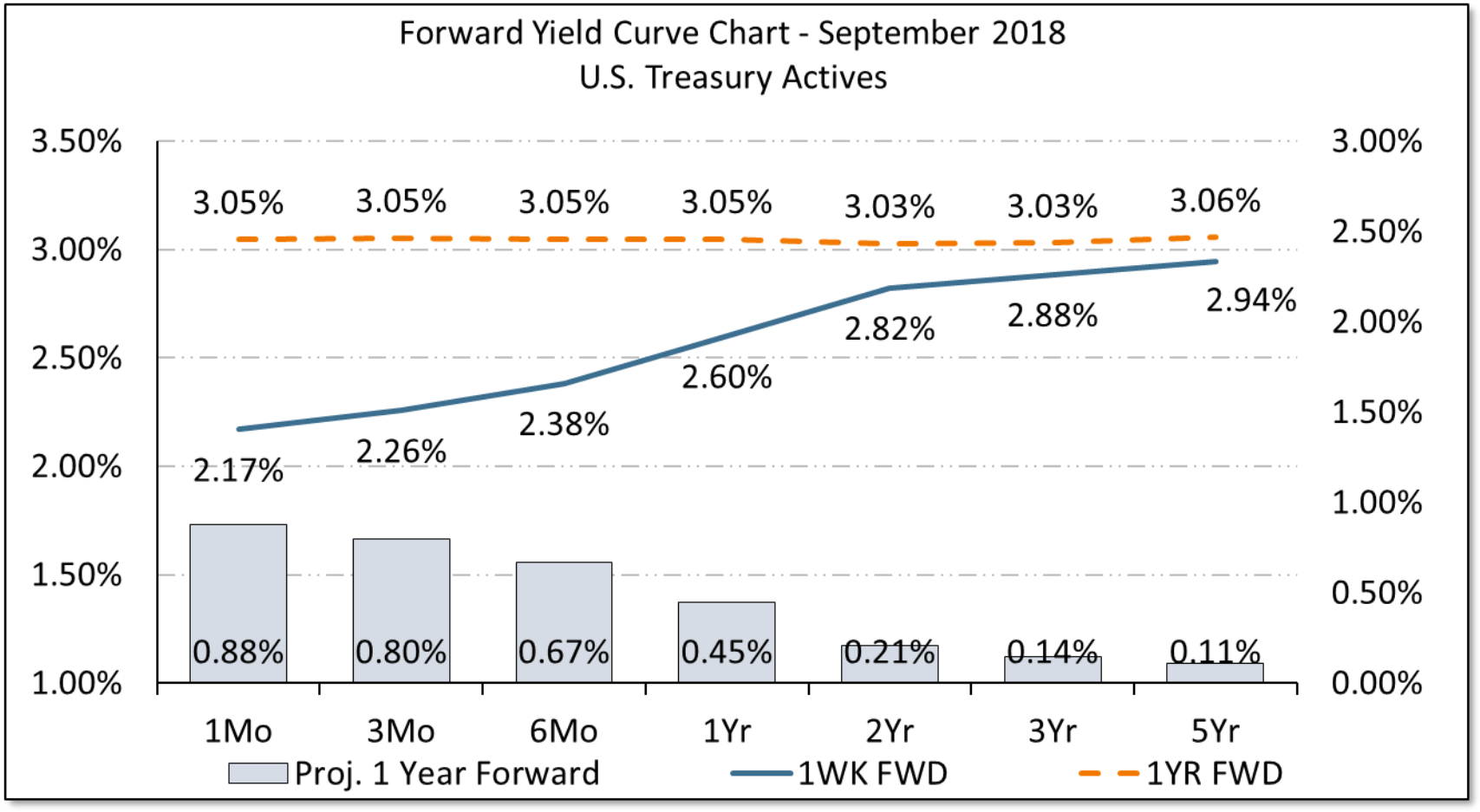
Forward Yield Curves

- Are we headed to an inverted yield curve?



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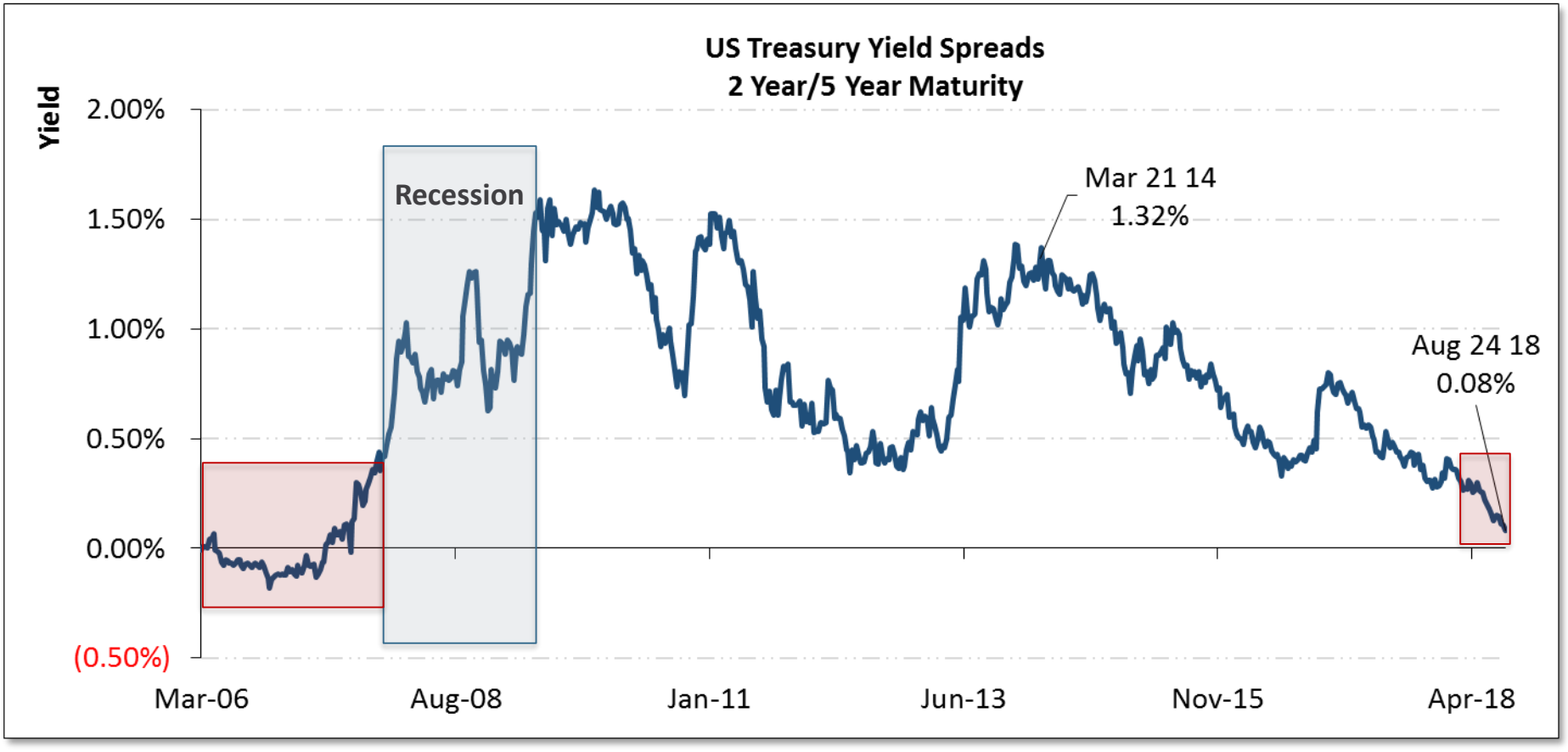
Spreads Narrow as the Yield Curve Continues to Flatten

- Spreads between maturities greater than two years continue to narrow approaching levels seen last seen in 2006 - 2007.



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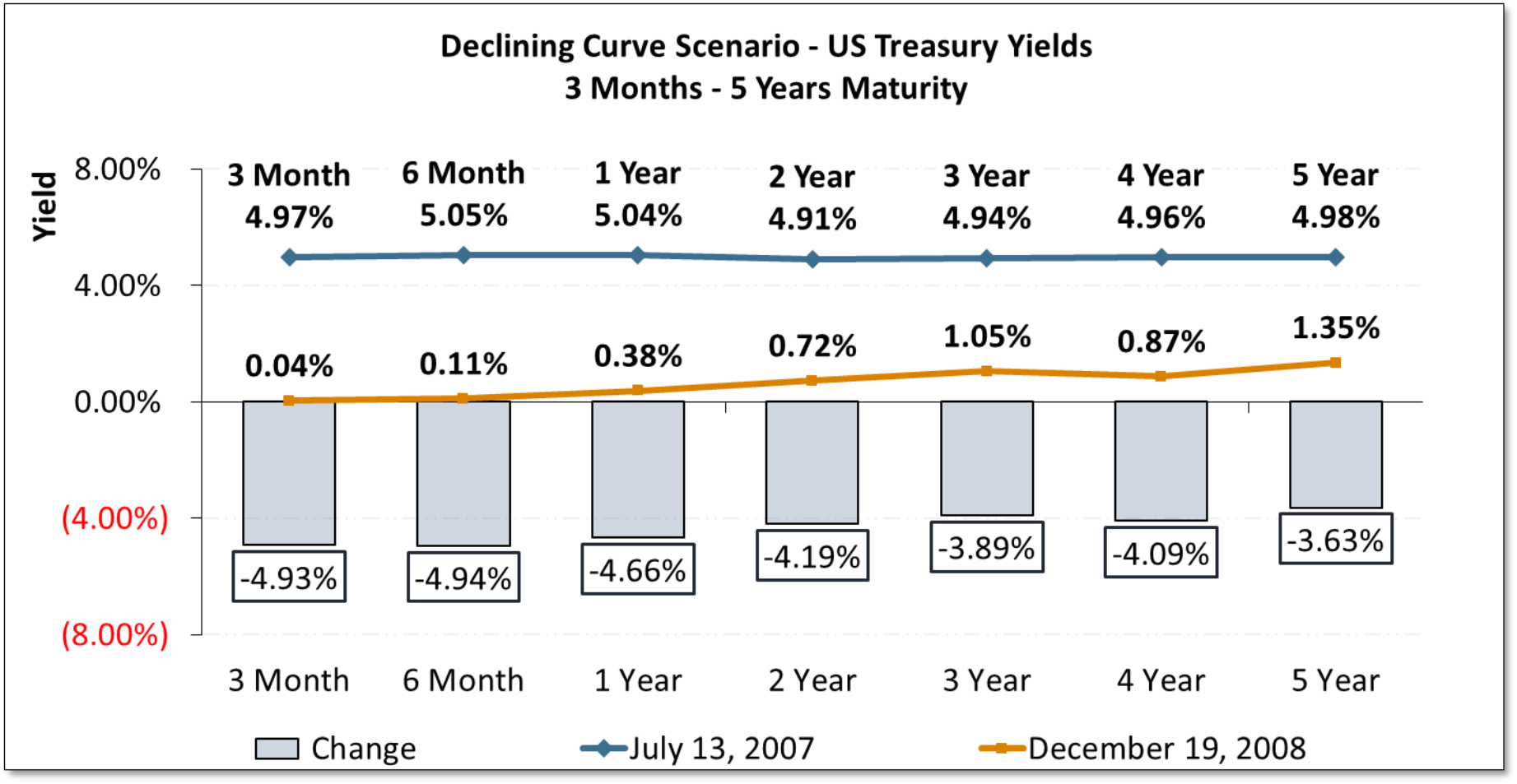
Declining Interest Rate Environment

- Interest rates fell as much as 500 basis points (5.00%) in the short end of the yield curve during the Great Recession.



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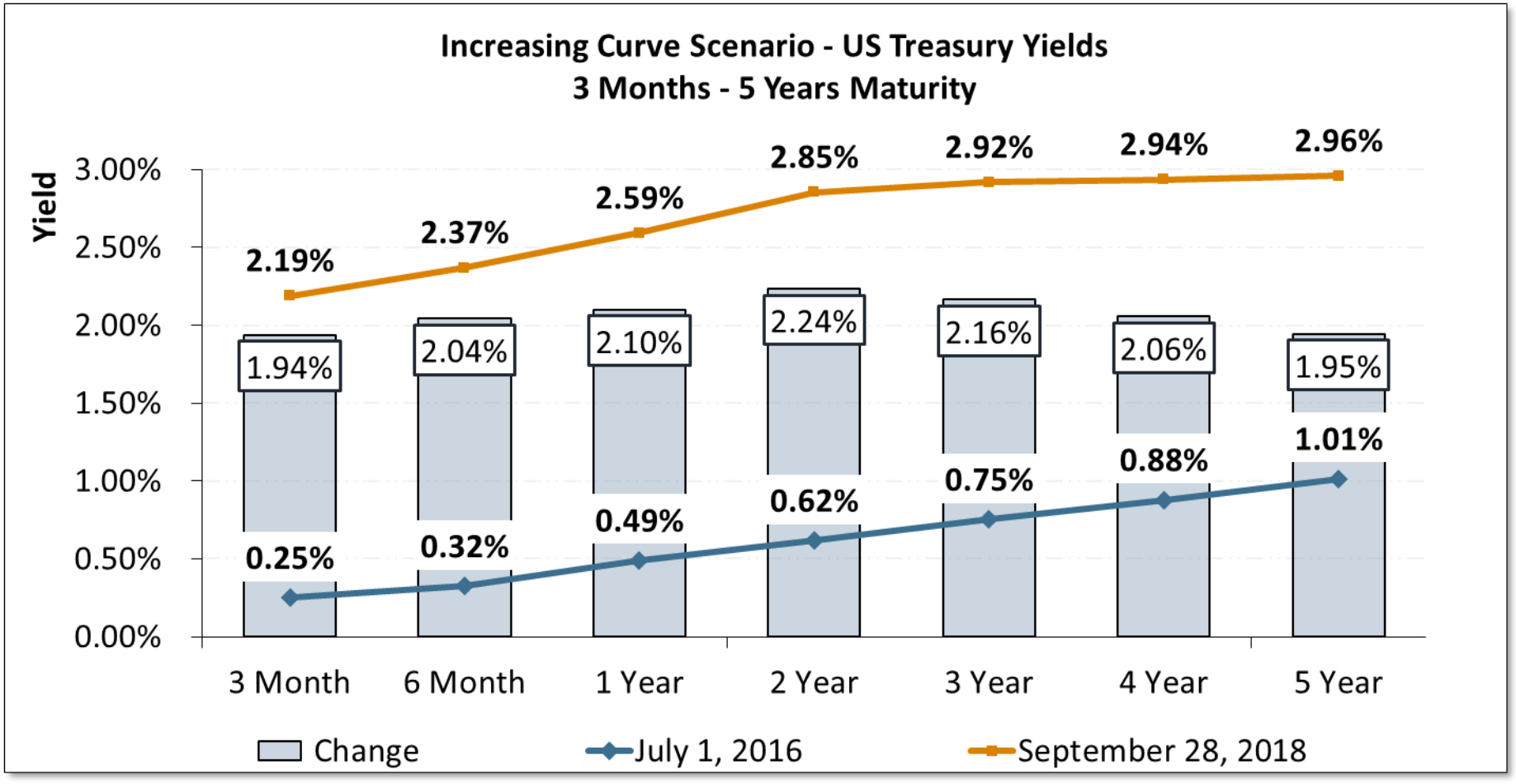
Increasing Interest Rate Environment

- Interest rates have increased by more than 200 basis points (2.00%) since the Brexit vote in late June 2016.



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Fixed Income Investment Maturity Structure and Risks

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Risks Defined

- **Market Risk**: the price volatility associated with an investment determined primarily by remaining time to maturity.

- **Credit Risk**: Risk of default or decline in security value due to Issuer financial conditions

- **Reinvestment Risk**: Interest and/or Principal will be reinvested at a lower rate of return than the current interest rate

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Historical Performance and Yield Curve Analysis

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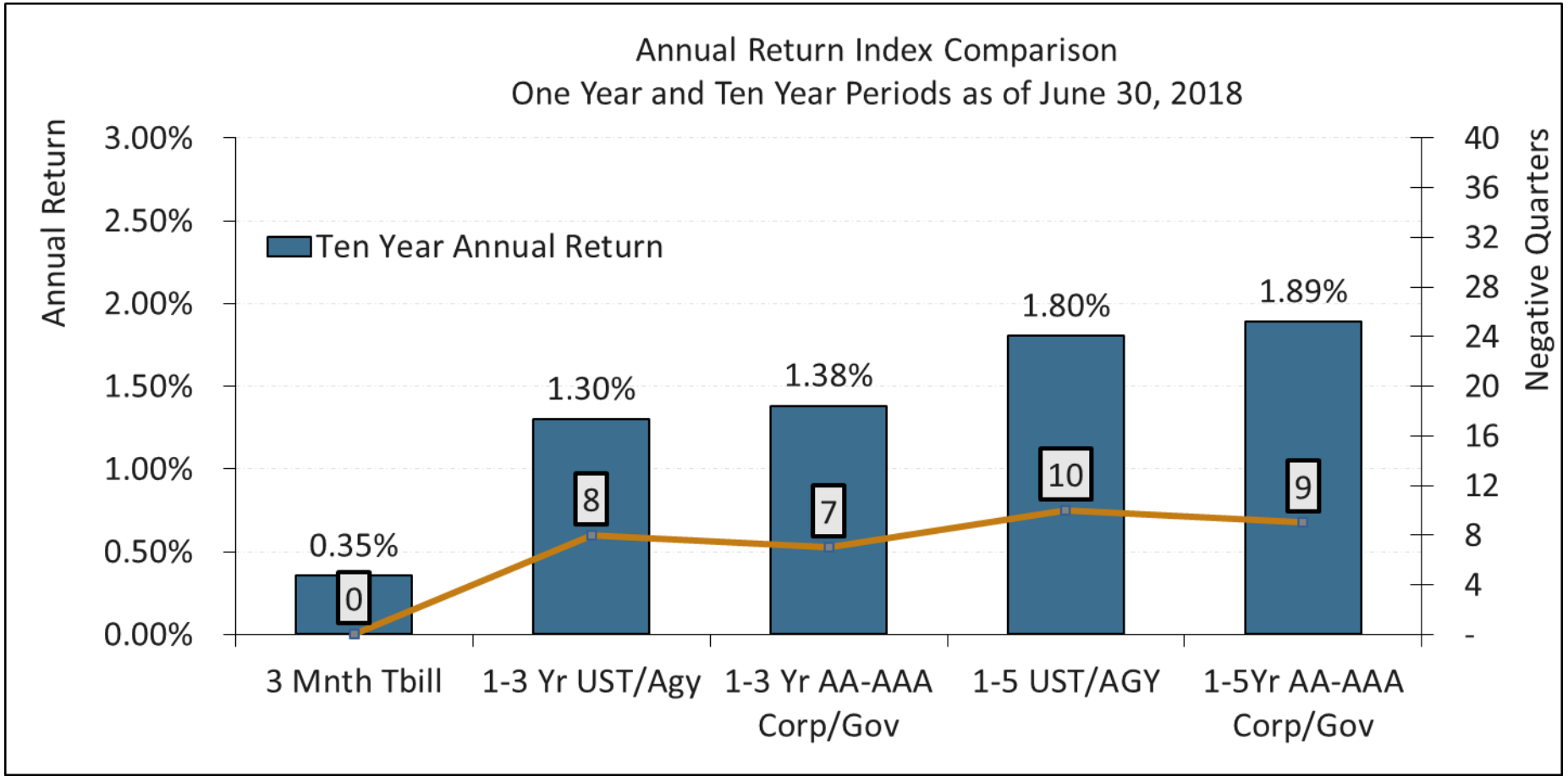
Historical Total Return – 10 Year Analysis

- Historically, longer duration investment programs have provided higher returns compared to shorter duration investment strategies, although with higher volatility.



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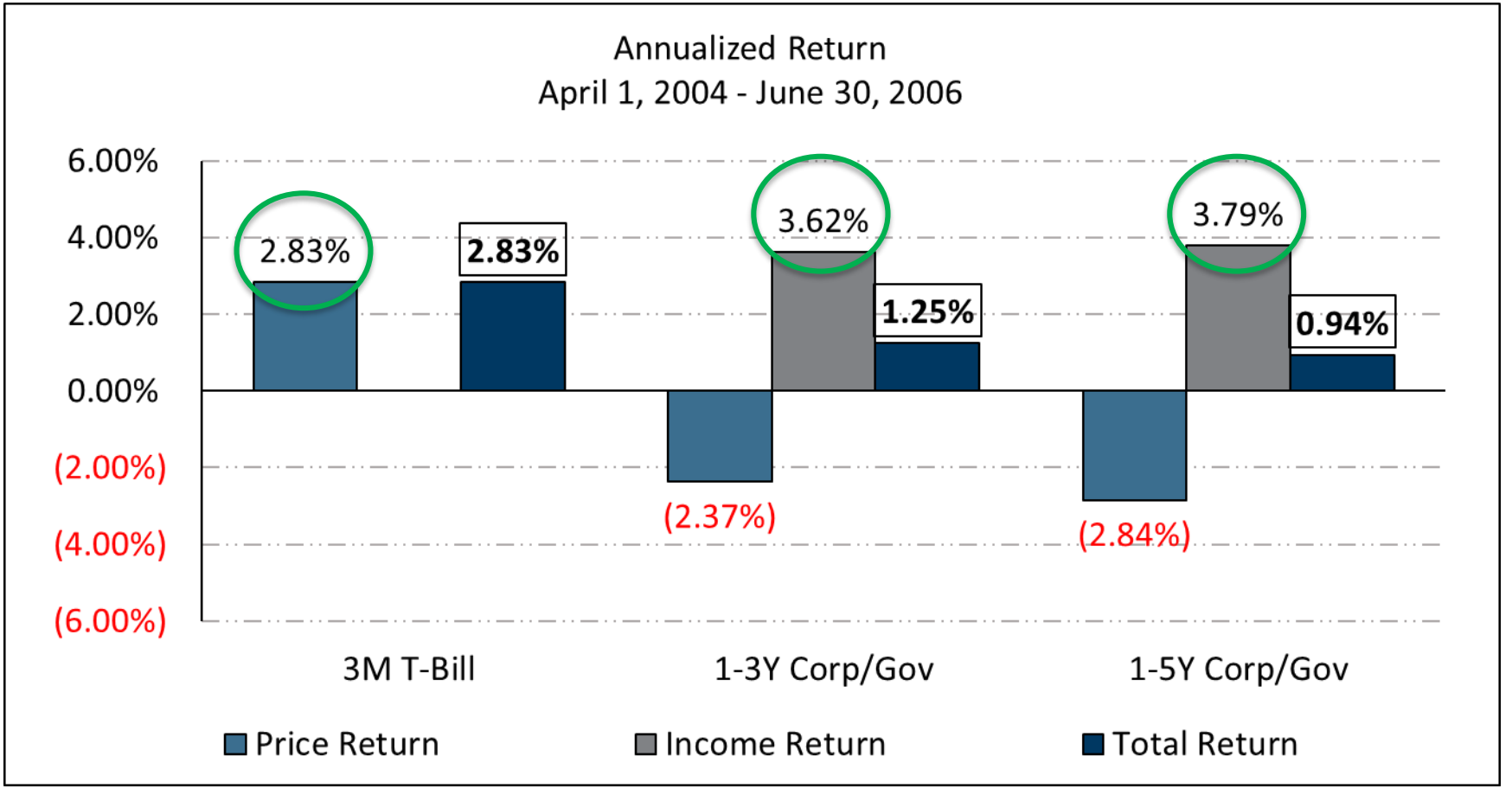
Historical Performance **Rising** Interest Rate Environment

- In a rising interest rate environment, short duration strategies may outperform long duration strategies as a result of the impact on the price return component of total return.



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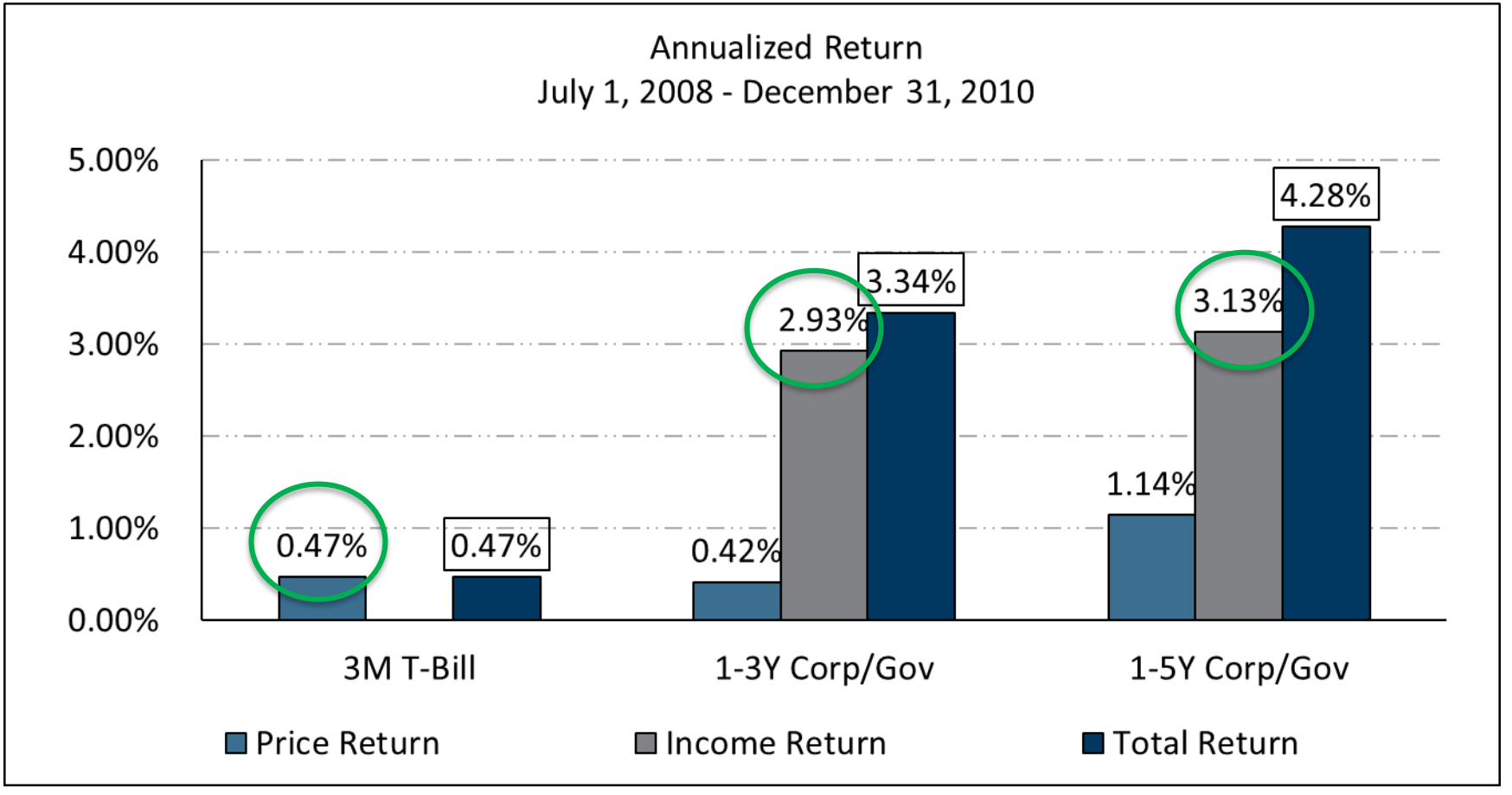
Historical Performance **Declining** Interest Rate Environment

- In a declining interest rate environment, long duration strategies may outperform short duration strategies as a result of the impact on the price return component of total return.



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Historical Performance **Rising** Interest Rate Environment

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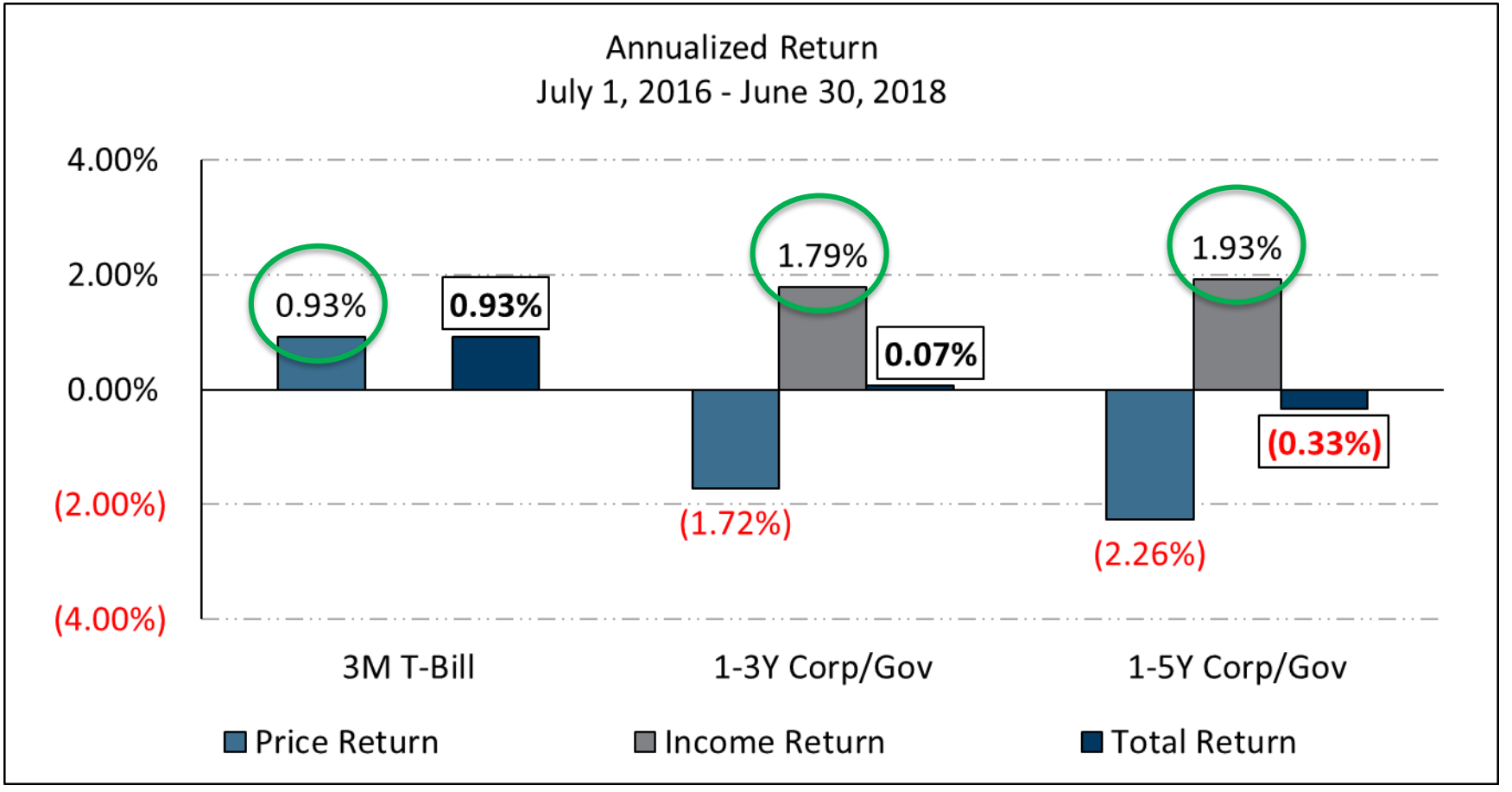

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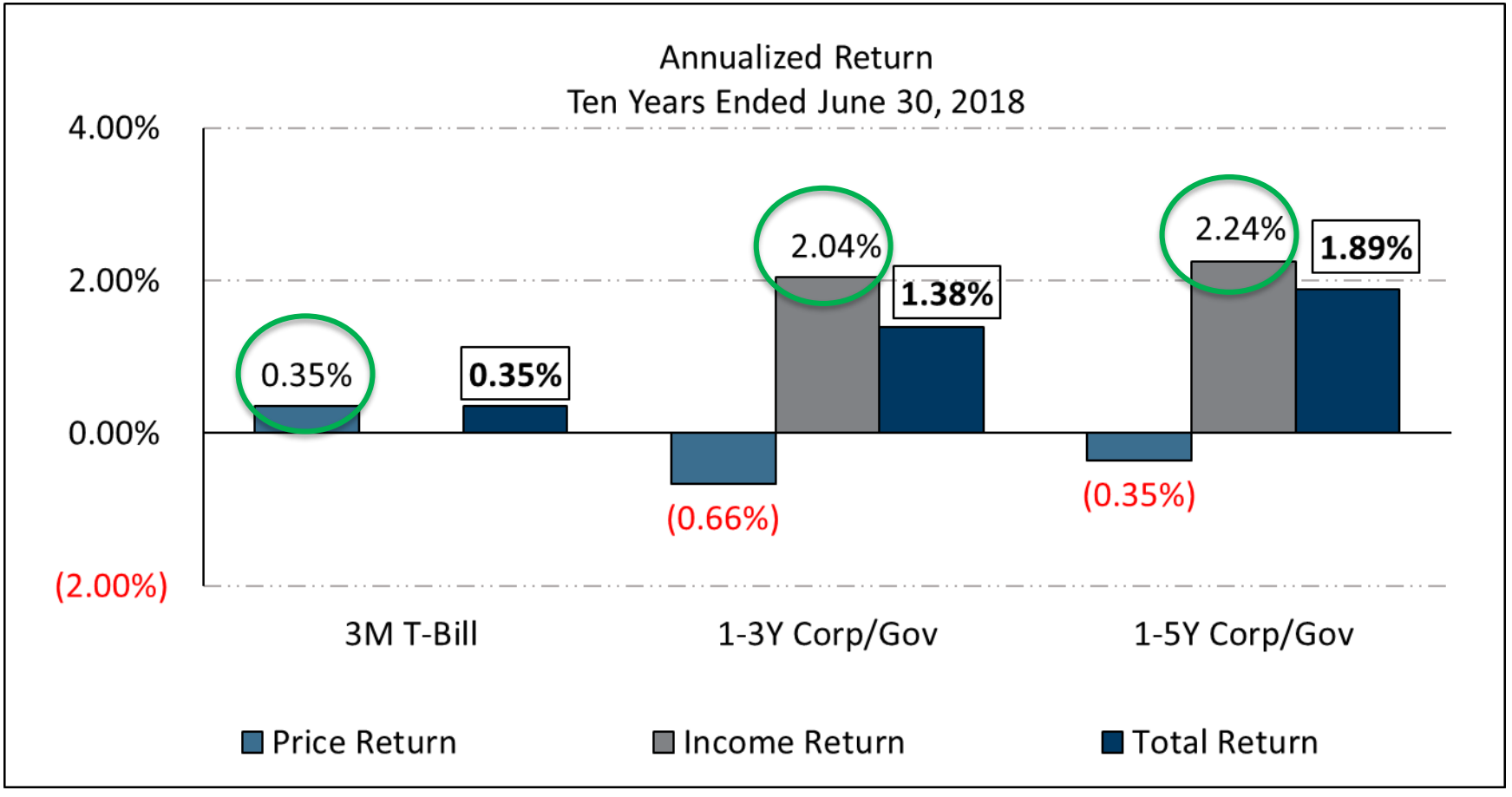

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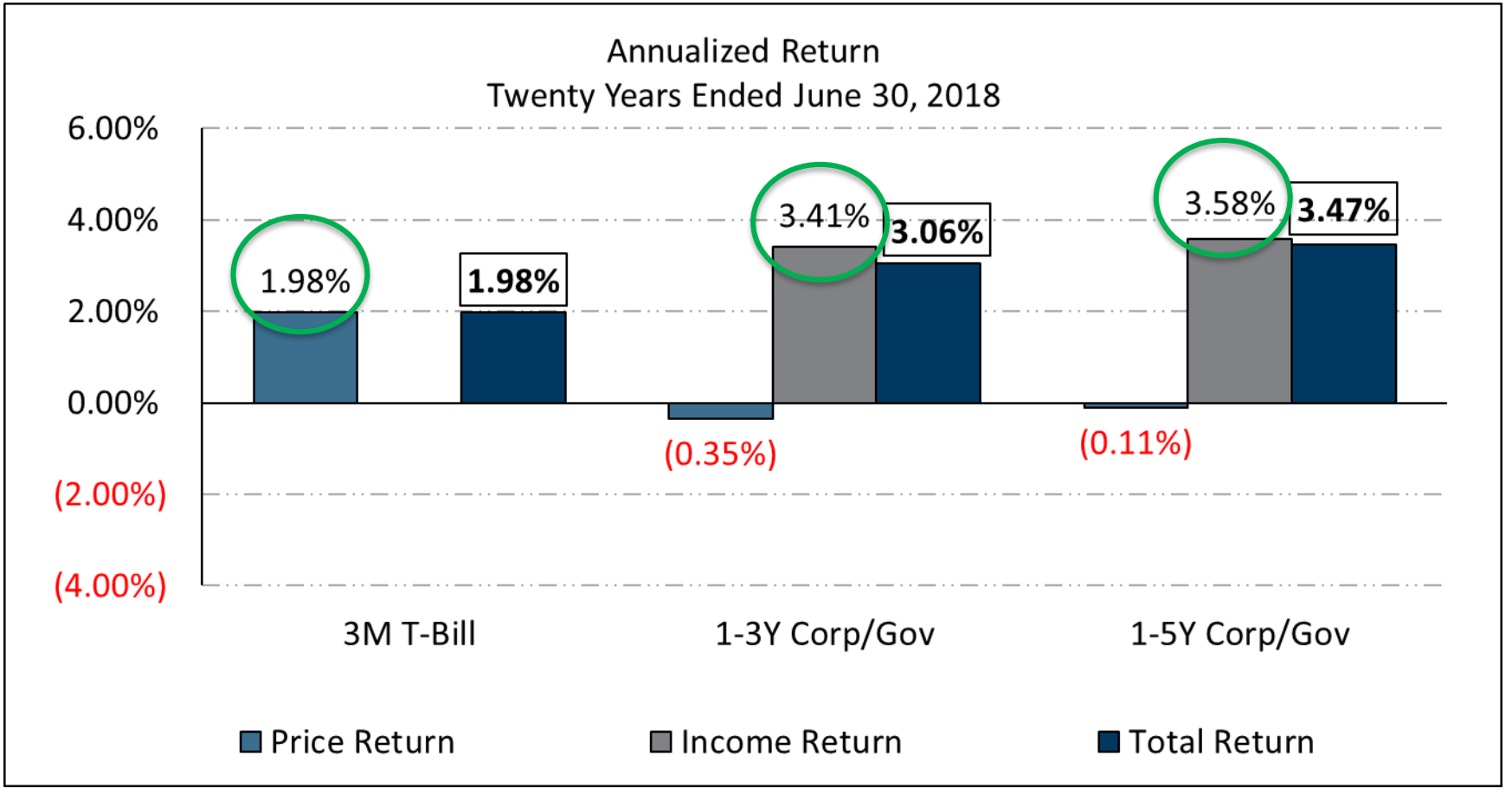
20 Year Historical Total Return: Price vs. Income Return

- Total return comprises income return and price return.



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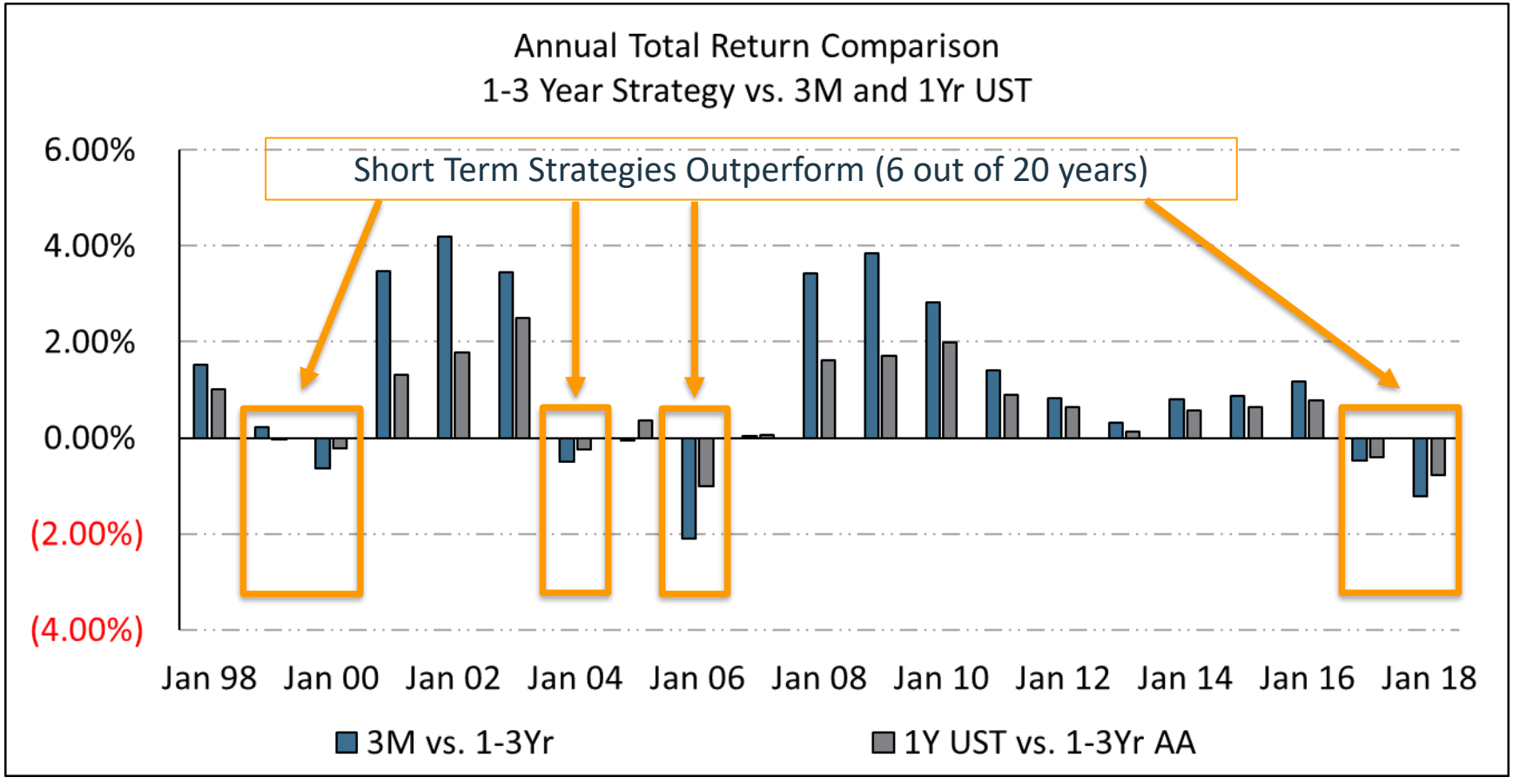
Annual Total Return Comparison

- Longer Term strategies have underperformed from a total return perspective for the last two years.



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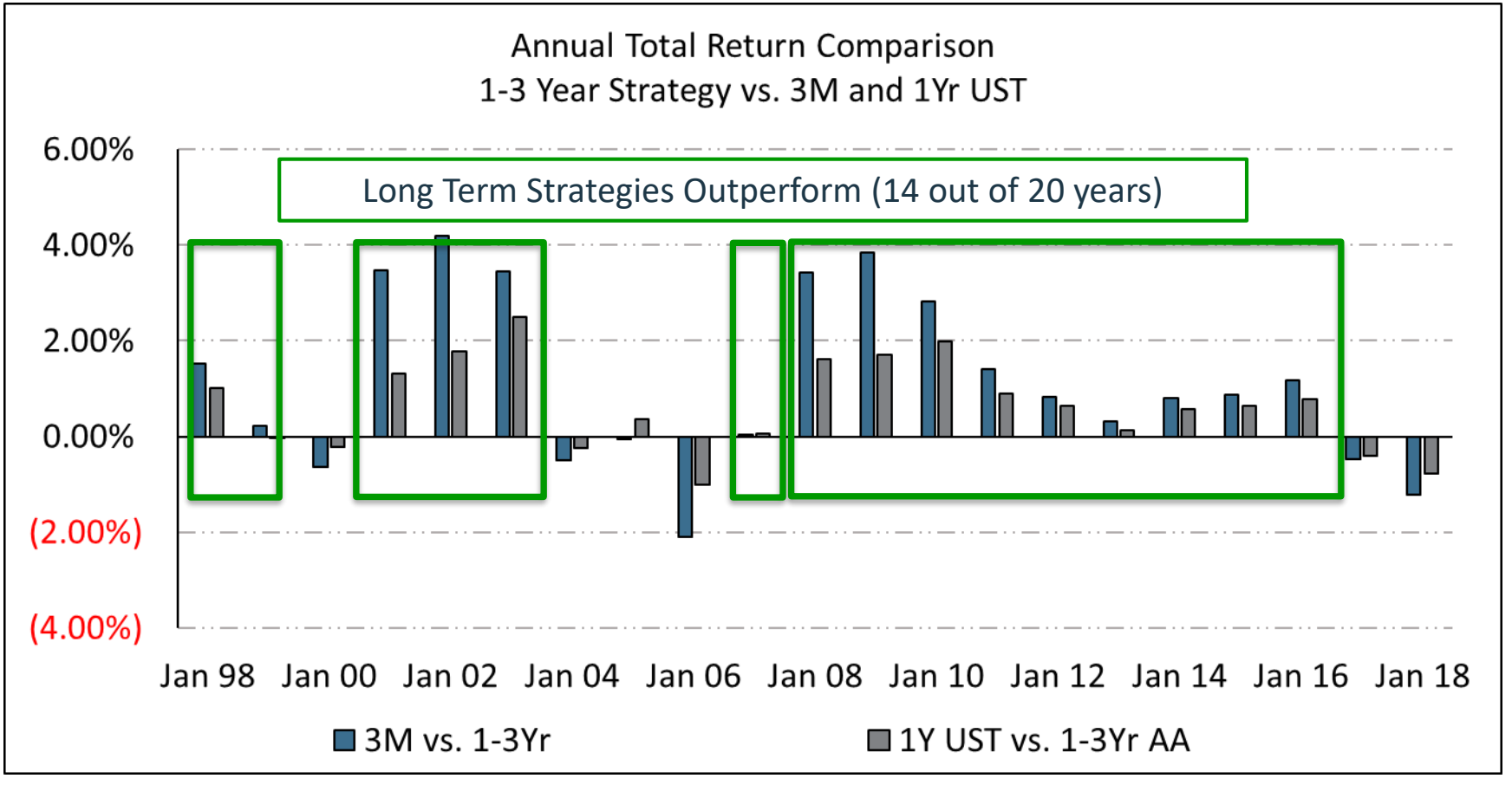

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Considerations for Investment Strategies

- **Market Timing**: Shifting investment strategies may result in loss of interest income, increase in market risk volatility, or both.
- **Multiple Duration Strategies**: Utilizing short and longer term maturity strategies may provide reduced overall risk during several interest rate cycles.
  - Liquidity options including DDA, LGIP, MMF, CP, Discount Notes*
  - Maturities between one and five years for reserves*
- **Consider Investment Risks:** All investments have risks
  - Market Risk
  - Liquidity Risk
  - Reinvestment Rate Risk

*Not a recommendation. All investments have a risk of loss. Only invest in permitted investments according to all applicable laws and as permitted by investment policy.

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