

FIXED INCOME MARKET UPDATE

Third Quarter 2017

Despite intra-month rate volatility, the yield curve ended the quarter slightly flatter with minimally higher rates.

Treasury returns were slightly positive this quarter given the modest move higher in interest rates.

Investment-grade spreads were tighter in the third quarter with strong corporate earnings offsetting increased geopolitical risks. Strong equity performance aided corporate spread performance.

TREASURY YIELDS (%)¹

	Quarterly Change	9/30/17	8/31/17	7/31/17	6/30/17
90-Day T-Bills	0.04	1.05	0.99	1.07	1.01
2-year Treasury	0.10	1.48	1.33	1.35	1.38
5-year Treasury	0.04	1.93	1.70	1.84	1.89
10-year Treasury	0.03	2.33	2.12	2.30	2.30
30-year Treasury	0.02	2.86	2.73	2.90	2.84

TREASURY RETURNS (%)¹

	Duration (years)	Q3 17 Return	YTD
90-Day T-Bills	0.24	0.27	0.58
2-year Treasury	1.96	0.20	0.58
5-year Treasury	4.78	0.26	1.39
10-year Treasury	8.88	0.28	2.40
30-year Treasury	20.68	0.33	5.96
TIPS	6.01	0.86	1.72

INTEREST RATE SPREADS (basis points)¹

	Quarterly Change	9/30/17	8/31/17	7/31/17	6/30/17
5-year Swap Spread	1	8	6	7	7
10-year Swap Spread	-2	-4	-5	-5	-2
5-year Baa2 Industrial Spread	-4	82	91	82	86
10-year Baa2 Industrial Spread	-4	118	124	113	122
30-year Baa2 Industrial Spread	-2	131	135	123	133
MBS Current Coupon Spread	-10	63	71	68	73

Index returns were all positive this quarter given small changes in rates and tighter spreads.

BROAD MARKET RETURNS (%)¹

	Duration (years)	Q3 17 Return	Duration adj. vs. Treasuries	YTD Return	Duration adj. vs. Treasuries
U.S. Universal	5.75	1.01	0.58	3.67	1.44
Aggregate	5.96	0.85	0.41	3.14	0.84
Government/Credit	6.62	0.81	0.39	3.49	1.07

Sector returns were all positive in the quarter due to modest yield changes and the extra income cushion provided by spread sectors. Agency MBS and TIPs finally turned in strong performance in the third quarter.

INVESTMENT-GRADE SECTOR RETURNS (%)²

	Duration (years)	Q3 17 Return	Duration adj. vs. Treasuries	YTD Return	Duration adj. vs. Treasuries
Treasuries	6.19	0.38	--	2.26	--
U.S. Treasury TIPs	6.01	0.86	--	1.72	--
Agencies	3.91	0.41	0.05	2.07	0.57
Mortgage-Backed Securities	4.47	0.96	0.47	2.32	0.27
Asset-Backed Securities	2.21	0.42	0.14	1.56	0.68
Investment-Grade Corporates	7.55	1.34	0.87	5.19	2.42
Intermediate Corporates	4.47	1.05	0.66	3.75	1.98
Long Corporates	14.19	1.97	1.34	8.46	3.43

Credit sectors outperformed with BBB-rated sectors performing the best.

INVESTMENT-GRADE CREDIT QUALITY RETURNS (%)²

	Duration (years)	Q3 17 Return	Duration adj. vs. Treasuries	YTD Return	Duration adj. vs. Treasuries
Aaa	5.39	0.63	0.21	2.31	0.18
Aa	6.20	0.96	0.54	3.60	1.31
A	7.55	1.26	0.79	4.78	1.97
Baa	7.65	1.63	1.16	6.14	3.34

High-yield posted solid returns in the quarter with a difference between the best performing ratings category (Caa) and the worst (B) of only 0.75%, the lowest differential since mid-2014.

High-yield spreads tightened across all three high-yield rating categories in the third quarter.

The high-yield default rate ticked down in August both in total and on an ex-commodities basis.

The star outperformer during the third quarter was the U.S. Convertibles sector.

HIGH-YIELD SECTOR RETURNS (%)²

	Duration (years)	Q3 17 Return	Duration adj. vs. Treasuries	YTD Return	Duration adj. vs. Treasuries
High-Yield Corporates	3.78	1.98	1.60	7.00	5.35
Ba	4.36	2.01	1.62	6.90	5.09
B	3.42	1.75	1.38	6.11	4.50
Caa	3.11	2.50	2.17	9.26	7.89

HIGH-YIELD OPTION-ADJUSTED SPREADS (basis points)²

	Quarterly Change	9/30/17	8/31/17	7/31/17	6/30/17
High-Yield Option-Adjusted Spread	-18	347	378	352	364
BB Option-Adjusted Spread	-21	206	232	217	227
B Option-Adjusted Spread	-21	340	370	347	361
CCC Option-Adjusted Spread	-33	647	699	649	680

HIGH-YIELD DEFAULT RATES (1 month lag, basis points)³

	Quarterly Change	8/31/17	7/31/17	6/30/17	5/31/17
Number of Issuers in Default	-6	42	48	47	48
Issuer Default Rate	-0.53%	4.00%	4.56%	4.43%	4.53%
Number of Issuers in Default (ex-commodities)	1	24	29	26	23
Issuer Default Rate (ex-commodities)	0.14%	3.08%	3.73%	3.32%	2.94%

OTHER SECTOR RETURNS (%)^{1,2}

	Duration (years)	Q3 17 Return	Duration adj. vs. Treasuries	YTD Return	Duration adj. vs. Treasuries
Emerging Markets	5.09	2.69	2.29	8.77	6.85
Global Treasuries (Unhedged)	7.92	1.58	1.14	6.14	3.40
S&P Leveraged Loan Index	--	1.02	--	2.98	--
Wells Fargo Hybrid & Pref. Securities Aggregate Index	--	0.85	--	10.51	--
U.S. Convertibles	--	4.43	--	14.65	--

This update provides an overview of certain broad based Fixed Income benchmarks and does not include performance of the Denver Investments' Fixed Income styles. We have obtained this information from third parties that we consider to be reliable. Past performance does not guarantee future results.

¹Source: Bloomberg.

²Source: Barclays.

³Source: Bank of America Merrill Lynch.

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