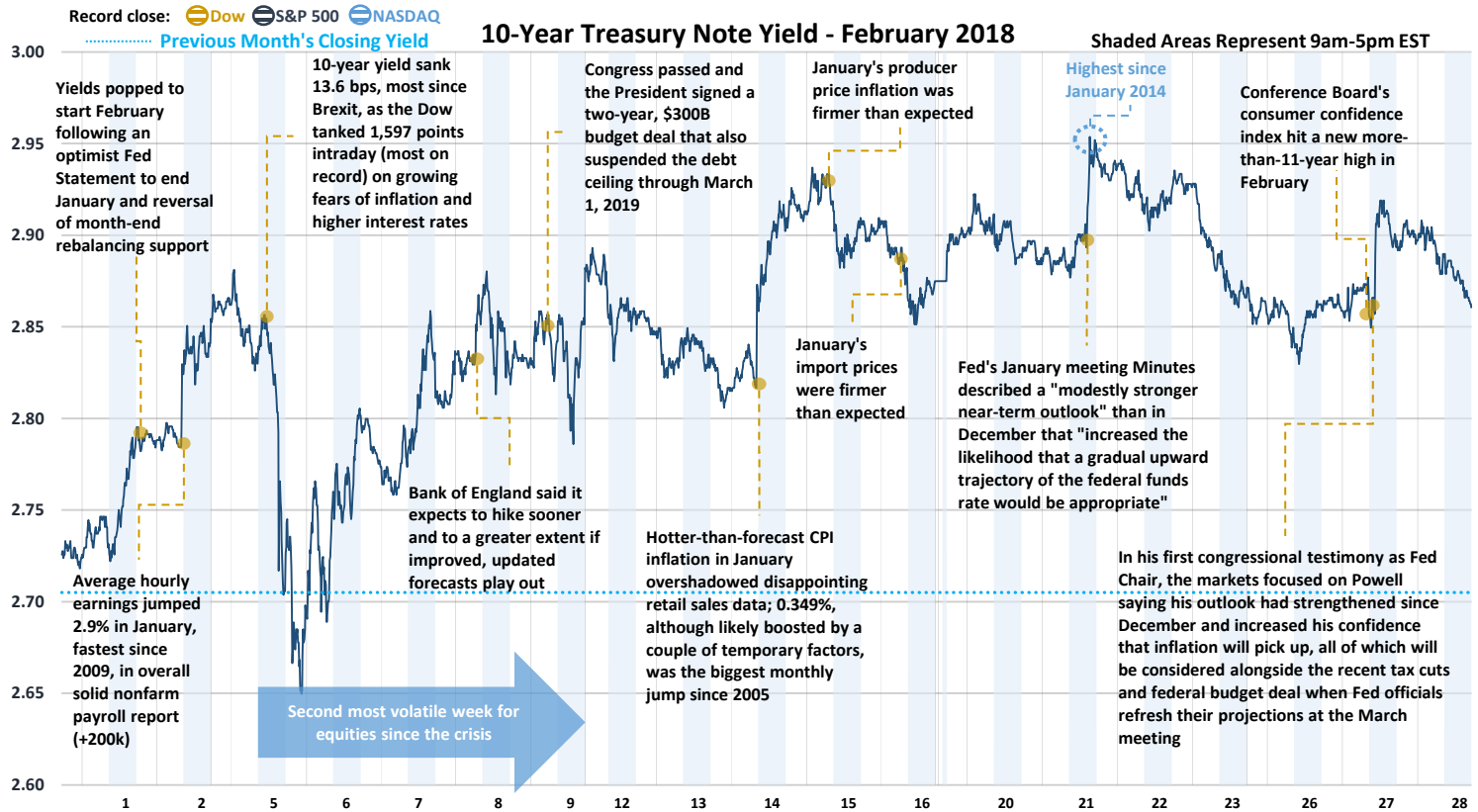


Monthly Review

February 2018

Fears of Inflation Fueling a Faster Fed Path and Higher Interest Rates Ends a Record Run for U.S. Stocks



Rising Rates Disrupted a Record Stock Run as a Pop in Hourly Earnings, Faster CPI, and More Optimistic Fed Raised Market Probability of More Gradual Rate Increases

Markets: Market volatility, essentially absent in 2017, re-emerged as a hotter-than-expected January hourly earnings number followed an optimistic Fed Statement and sent yields climbing. Fears of faster inflation forcing the Fed to do more spooked equities, sending the major indexes on their biggest intraday point drop in history and second most volatile week since the financial crisis. In just five days, the Dow and S&P both dipped into a technical correction, down more than 10% from their most recent peak, before partially recovering even as several other inflation indicators, including the January CPI report, proved firmer than expected. Finally, Minutes from the January Fed meeting described a better-than-expected near-term outlook than in December, a message echoed by Chair Powell's personal outlook in his first semi-annual congressional testimony. When the final tick printed, the S&P had fallen 3.9% and the Dow had lost 4.3%, the worst month in two years for both indexes. On a total return basis, the S&P snapped a 15-month positive streak (since the election), the longest in the index's history. The 2-year yield rose 10.9 bps to 2.25% as Fed Funds futures priced in a 100% chance of three 2018 hikes for the first time. The 5-year yield finished up 12.6 bps at 2.64% while the 10-year yield added 15.6 bps to 2.86%.

Consumer: Personal consumption in 4Q17 held at 3.8% after first revisions but January's data showed a weak start to 2018. Headline retail sales were negatively impacted by another soft month for autos and core sales that were unchanged from a negatively revised December (and November). After adjusting the nominal series for inflation, real activity was even weaker. On a more positive note, the labor data – whether it be total hiring (+200k), low unemployment (unchanged at 4.1%), earnings growth (2.9% YoY, fastest since 2009), or initial jobless claims (lowest 4-week moving average since 1973) – remained supportive of the consumer. In addition, the Conference Board's confidence index reached its strongest level since 2000, indicating the slowdown in January more likely represented a pause rather than a sustained pullback.

Private Investment: Business spending disappointed to start 2018 as capital goods orders fell unexpectedly and shipments rose less than forecast while manufacturing output came up short of estimates. However, the survey data was more optimistic. The ISM Manufacturing PMI touched its fifth best level since 2004 (fourth best in the last six months) and the Non-manufacturing PMI rose unexpectedly to its highest level since August 2005. In addition, and similar to the consumer, improved small business confidence stood in contrast to weaker spending. Save stronger starts and permits data, residential activity also disappointed: new home sales (-7.8%), existing home sales (-3.2%), and pending home sales (-4.7%). Nonetheless, prices continued their trek higher at a faster-than-6% pace.

External Trade: After weighing on 4Q17 growth, trade continued to look weak to start 2018. The advanced goods trade data showed weaker trade flows and a wider-than-expected deficit, as exports dropped more than imports. Despite continued weakness in the Dollar, trade remains an area of concern for 1Q growth.

Inflation: Inflation was the economic story in February as a pop in hourly earnings was followed by a firmer-than-expected CPI print and several additional secondary inflation reports that topped estimates. Core CPI rose 0.349% MoM, the fastest pace since 2005, keeping the 1.8% YoY rate from dipping to 1.7% as was expected.

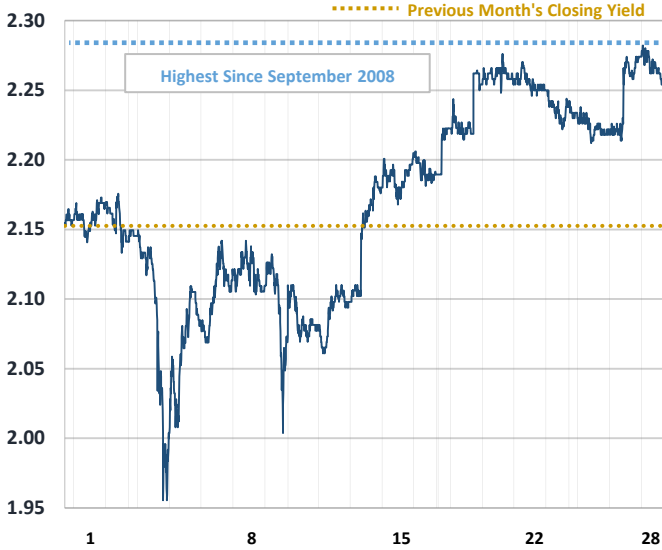
Monetary Policy: January's Fed Minutes described a "modestly stronger near-term outlook" than in December that "increased the likelihood that a gradual upward trajectory of the federal funds rate would be appropriate." This optimism was echoed by Jay Powell in his first congressional testimony as Fed Chair. Powell indicated that his personal outlook had strengthened since December and could affect his updated projections come March. Neither the ECB nor the BoJ met but the Bank of England said they may hike sooner and to a greater extent than previously thought if the improvements in their updated forecasts play out.

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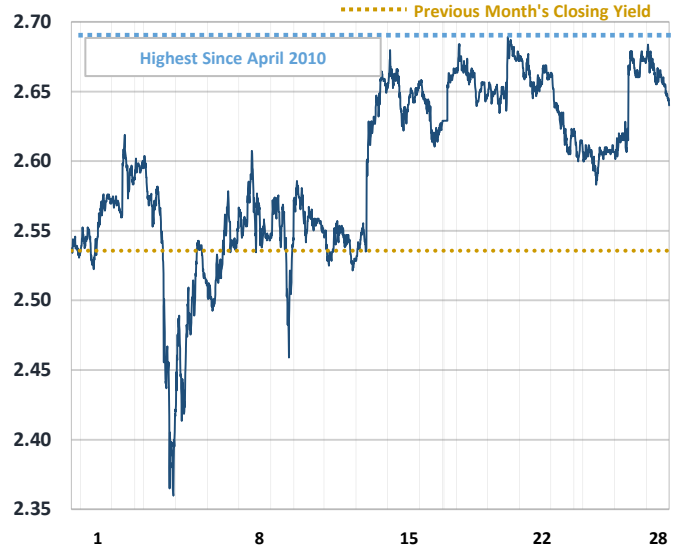
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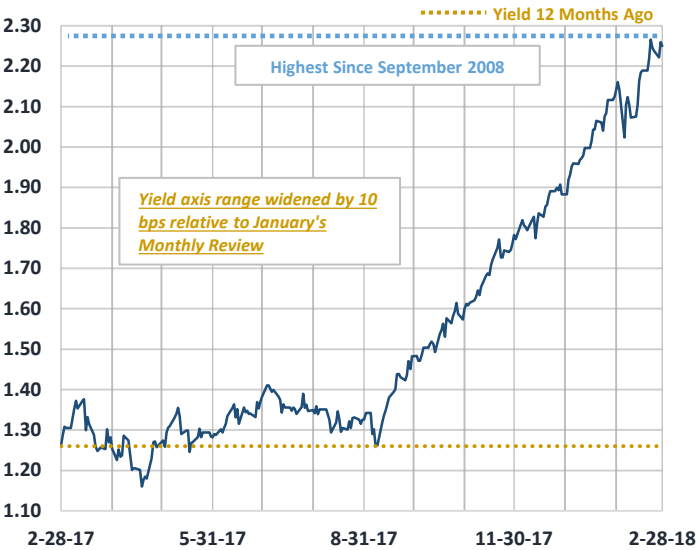
2-Year Treasury Note Yield - February 2018



5-Year Treasury Note Yield - February 2018



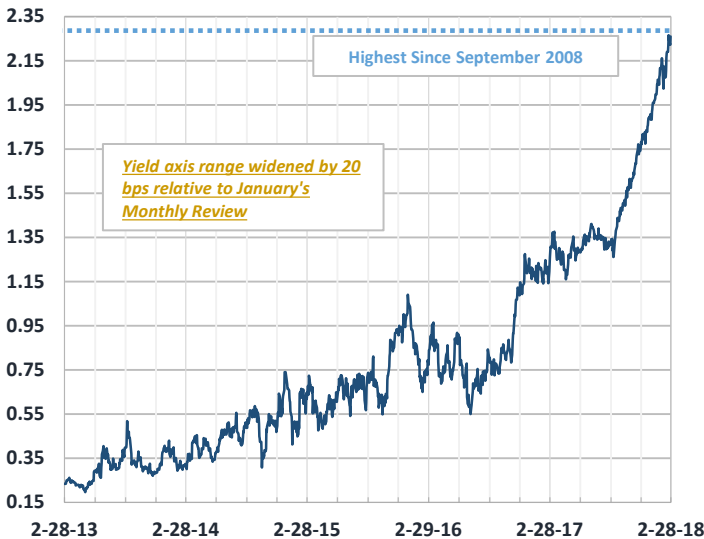
2-Year Treasury Note Yield - Last 12 Months



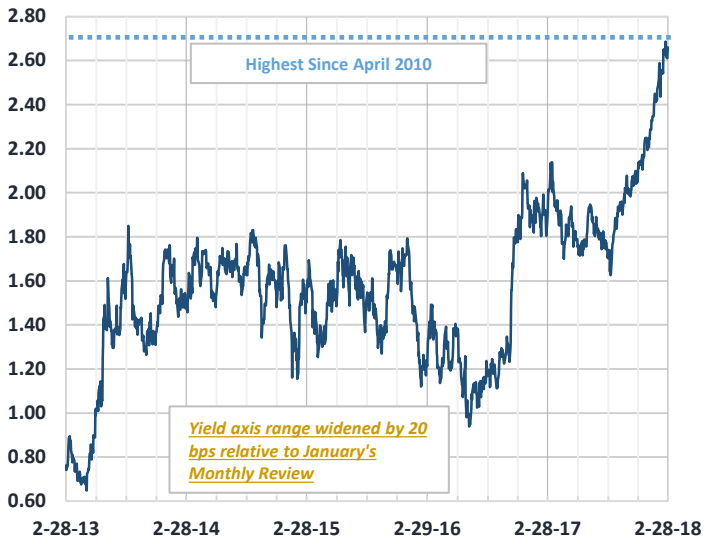
5-Year Treasury Note Yield - Last 12 Months



2-Year Treasury Note Yield - Last 5 Years



5-Year Treasury Note Yield - Last 5 Years

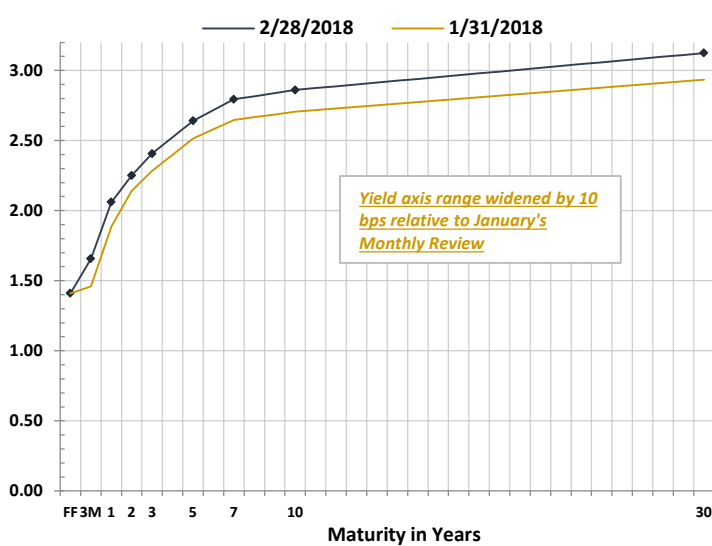


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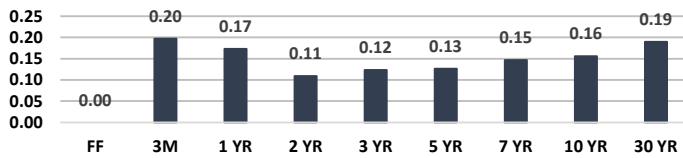
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Treasury Month-Over-Month



Month-Over-Month Change in Treasury Yields



Global Stock Performance

	Value	MTD Change	QTD Change	YTD Change
Dow Jones	25,029	-4.28% ↓	1.25% ↑	1.25% ↑
S&P 500	2,714	-3.89% ↓	1.50% ↑	1.50% ↑
Nasdaq	7,273	-1.87% ↓	5.35% ↑	5.35% ↑
Stoxx Europe 600	380	-4.00% ↓	-2.45% ↓	-2.45% ↓
China CSI 300	4,024	-5.90% ↓	-0.18% ↓	-0.18% ↓
Nikkei 225	22,068	-4.46% ↓	-3.06% ↓	-3.06% ↓

Global Sovereign Debt Performance

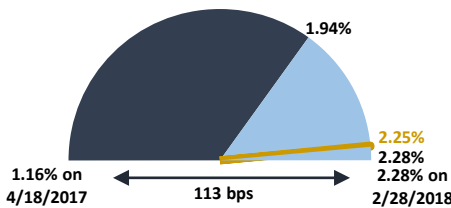
	Yield	MTD Change (in bps)	QTD Change (in bps)	YTD Change (in bps)
U.S. 2-year	2.25%	10.9 ↑	36.7 ↑	36.7 ↑
U.S. 5-year	2.64%	12.6 ↑	43.4 ↑	43.4 ↑
U.S. 10-year	2.86%	15.6 ↑	45.5 ↑	45.5 ↑
German 10-year	0.66%	-4.1 ↓	22.9 ↑	22.9 ↑
U.K. 10-year	1.50%	-0.9 ↓	31.1 ↑	31.1 ↑
French 10-year	0.92%	-5.0 ↓	13.3 ↑	13.3 ↑
Italian 10-year	1.97%	-5.5 ↓	-4.2 ↓	-4.2 ↓
Japanese 10-year	0.05%	-3.2 ↓	0.5 ↑	0.5 ↑

Commodity Performance

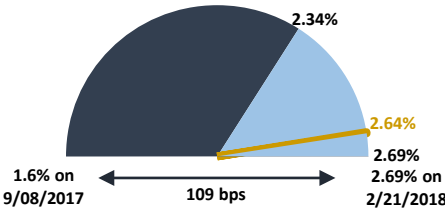
	Value	MTD Change	QTD Change	YTD Change
WTI Crude	\$ 61.64	-4.77% ↓	2.02% ↑	2.02% ↑
U.S. Dollar	90.61	1.66% ↑	-1.64% ↓	-1.64% ↓
Gold Spot	1,318	-1.99% ↓	1.18% ↑	1.18% ↑
Commodity Index	88.14	-1.85% ↓	-0.03% ↓	-0.03% ↓

Treasury Notes Intraday Ranges: 52-Week Yield Range / Monthly Yield Range / Last Traded Yield

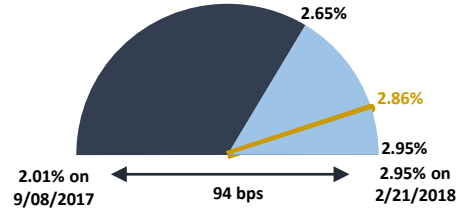
2-Year Treasury



5-Year Treasury



10-Year Treasury



Nonfarm Payrolls

January 200k +

Unemployment Rate

January 4.1% Unchanged +

Existing Home Sales MoM

January -3.2% -

Excepting stronger starts and permits, the housing data was a disappointment to start 2018

New Home Sales MoM

January -7.8% -

Core Retail Sales

January 0.0% -

Weak start to 2018, expected +0.4%

Consumer Confidence

February 130.8 +

Up 6.5 pts Highest since November 2000

ISM Non-Manufacturing

January 59.9 +3.9 pts + Strongest since August 2005

ISM Manufacturing

January 59.1 -0.2 pts + Fourth strongest in last six months, fifth strongest since 2004

Manufacturing Production

January 0.0% -

Core Capital Goods Orders

January -0.2% -

Trade Balance

December -53.1B -2.7B - Trade continued to look weak

Core PCE YoY

January 1.5% + Down 0.01%

As expected

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