MCDONNELL INVESTMENT MANAGEMENT

Fixed Income Market Commentary ✧ September 2015

Market Overview

Despite the sound and fury roiling global equity and currency markets, US rate markets ended the month of August little changed with most yields ending modestly lower across the curve and demonstrating a bias toward flattening. Intra-month volatility in Treasury yields was substantial as safe haven buying temporarily drove 10-year yields below 2%, but selling quickly materialized, some of which was attributed to the People's Bank of China (PBOC) liquidating Treasuries in an effort to boost the renminbi after it came under pressure following the surprise widening of its trading band versus the dollar. The mini-'devaluation' served as a catalyst for further share price selling as investors downgraded their growth outlook for China amid the maelstrom of developments.

The estimate for US growth during the second quarter was revised sharply higher to a respectable 3.7%, in part due to a build-up in inventories but also broader based gains in Consumption, Business Fixed Investment and Government Spending. While the pace of growth is expected to moderate going forward, it was nevertheless an encouraging development amidst the volatile moves occurring across the capital markets. Second half growth in the 2 ½ to 3% range would place full year GDP growth around 2 ½ %, roughly in line with 2014.

- Markets were roiled by a vicious correction in Chinese share markets with the added catalyst of a modest devaluation of the renminbi.
- New issuance in the corporate market ground to a halt amid heightened volatility and a second consecutive month of spread widening across the sector.
- Emerging Market (EM) currencies continued to weaken markedly against both the dollar and other Developed Market (DM) currencies.
- Commodity markets sunk to multi-year lows as fears of weakening demand from China and expanding energy output pressured prices broadly.

The municipal market moved mostly sideways and displayed considerably less volatility than the Treasury market amid the steep correction in equity markets. Municipals ended the month with modest outperformance versus Treasuries. New issue supply was quite healthy and remained in line with year-to-date trends, with the overall pace of volume running nearly 40% ahead of last year's pace with Refunding Issuance up at more than 70%. Mutual fund outflows were relatively heavy in both domestic equity and taxable bond funds, while municipal fund flows, though negative, were quite moderate.

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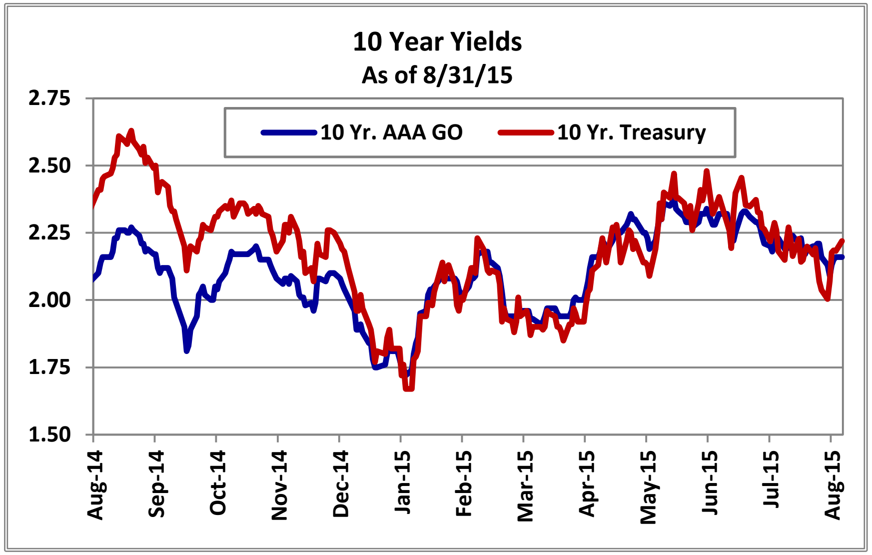

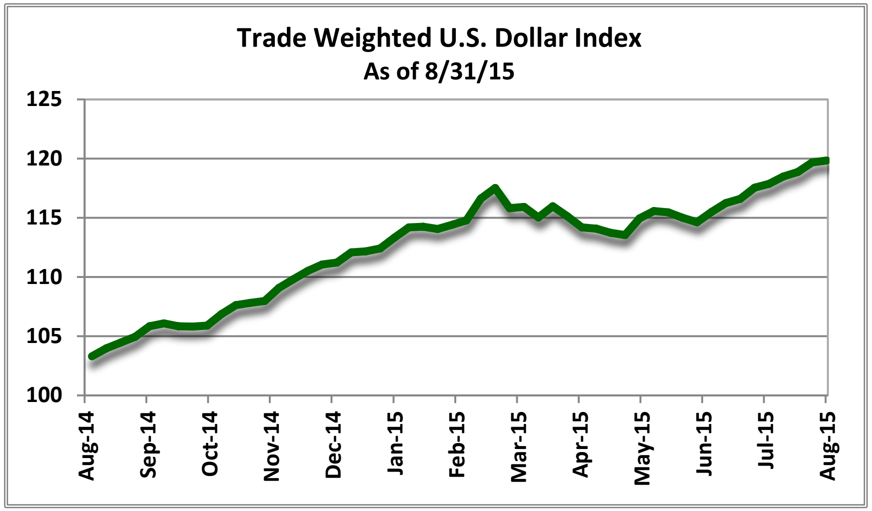

Sources: Municipal Market Data; Federal Reserve Bank.
Please refer to the Notes and Disclosures on the next page for additional information.

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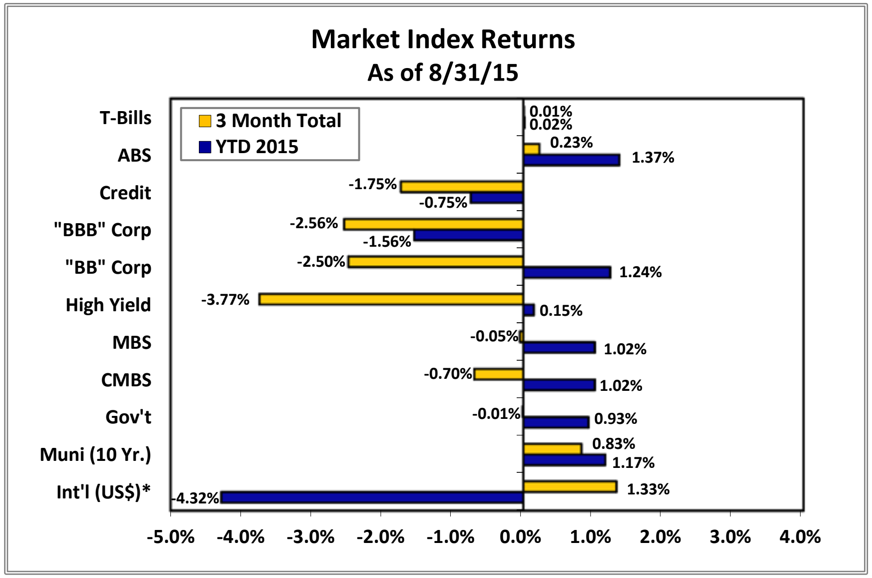
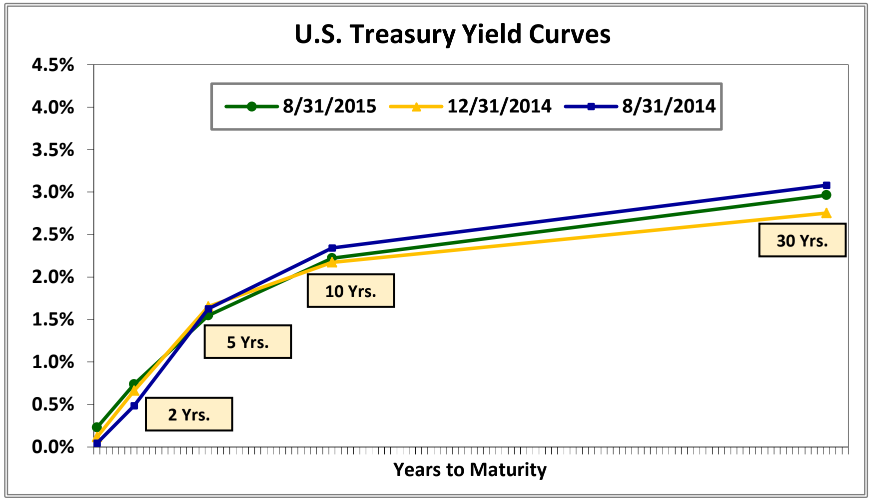
Market Overview *(Cont.)*

Taxable spread sectors were mixed with moderate outperformance across most structured product areas and sharp underperformance in credit, in general, and lower quality credit, in particular. One noteworthy occurrence during part of the month was the virtual shutdown of new issuance in the corporate market. Increased volatility and back to back months of spread widening seemed to give issuers pause. In addition, much refinancing has taken place amid favorable conditions and the need for issuers to tap the market amid a less advantageous environment was limited.

An open question facing investors is whether the Chinese share market volatility is symptomatic of deeper economic troubles or more benignly the result of forced liquidations by overleveraged investors. The behavior of related currency and commodity markets is not comforting however. It should give pause to even the most stalwart of growth optimists over the near-term outlook for the world's second largest economy. Should the sell-off resume, it will likely result in a ratcheting lower of both global growth and inflation estimates as we near 2016.

Looking ahead, conditions seem to favor a relatively range-bound US rate market amid steady domestic growth, little if any inflation and expectations of a gradualist monetary policy. The dominant source of potential volatility appears to revolve around the divergence of global growth prospects and the weakness of both EM and DM currencies versus the dollar. The environment of sub-par growth and deflationary tendencies abroad should augur for relatively benign conditions in US fixed-income markets over the medium term horizon.





All indices shown reflect Barclays Indices, except where noted.
*Sources: Barclays; *Merrill Lynch; Bloomberg.*
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