MAPLE CAPITAL MANAGEMENT

FIXED INCOME COMMENTARY

July 6, 2020

KEY TAKEAWAYS

Bond markets were steady in June despite volatility in the equity markets, on-going pandemic news, and social unrest across the globe. The Fed has made it clear they will implement policy support as needed to keep the recovery on track. Looking forward, investors will continue to assess economic data for hints of hiccups in the recovery, especially as government programs start to be replaced with private income.

Key Rates (%)	Jun 30 2020	May 31 2020	Dec 31 2019
Treasury Yields			
2 Year	0.15	0.16	1.57
5 Year	0.29	0.30	1.69
10 Year	0.66	0.65	1.92
30 Year	1.41	1.41	2.39
Credit Yields			
BBB Industrial 10 Year	2.36	2.68	3.10
Muni Yields			
AAA 10 Year	0.86	0.82	1.48
Mortgage Backed Securities			
30 Year FNMA Current Coupon	1.57	1.65	2.71

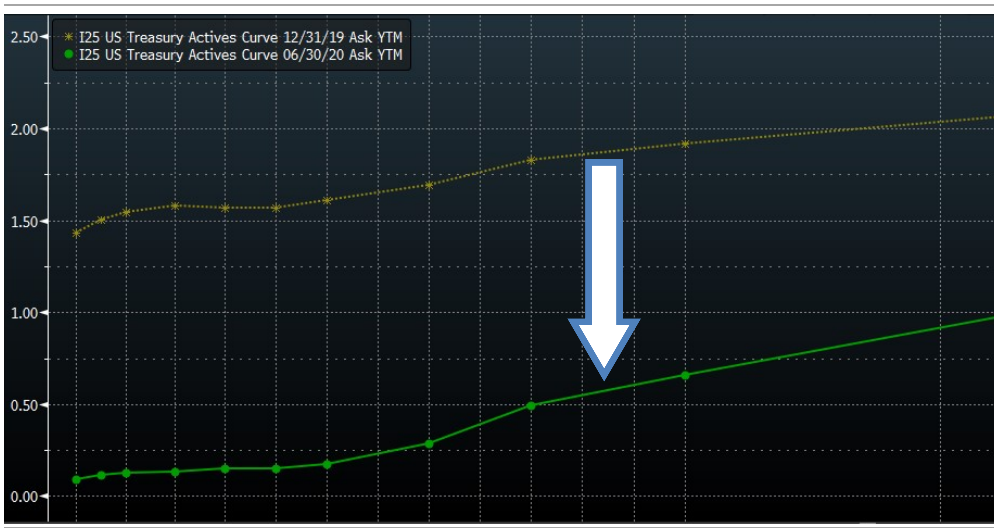
JUNE IN REVIEW

- The 10- year Treasury yield finished the month with a yield of 0.66%, up 1 bp month over month.
- Credit had a strong month, up 1.83% in June.
- Municipals were also strong as demand started to come back to the sector, up 0.82% in June.

Yield Curve Control in Action?

The bond market's steadiness in June was remarkable when considering the spike in equity market volatility, the on-going pandemic news, and the worldwide protests that broke out after the tragedy in Minneapolis. After the big drop in Treasury yields earlier this year (shown in Exhibit 1), during June bond yields changed very little -- 2 basis points or less -- as Fed Chair Powell's appearance on Capitol Hill signaled more policy support could be forthcoming if needed to keep the recovery on track. This stability in Treasury yields was accompanied by a further narrowing of corporate and municipal yield spreads, but some weakening of MBS, leaving the total return for the Bloomberg Barclays US Intermediate Aggregate Index at 0.41% for the month. The index yield* of just 0.98% implies very low go-forward monthly total return barring major changes in the yield curve. The prevailing level of rates leaves the distinct impression that the Fed is in firm control of Treasury yields (a policy known as Yield Curve Control whereby the Fed maintains effective control over the entire term structure) after making clear there is no plan to even think about raising rates until 2022.

EXHIBIT 1: US TREASURY ACTIVES CURVE—12/31/19 TO 6/30/20



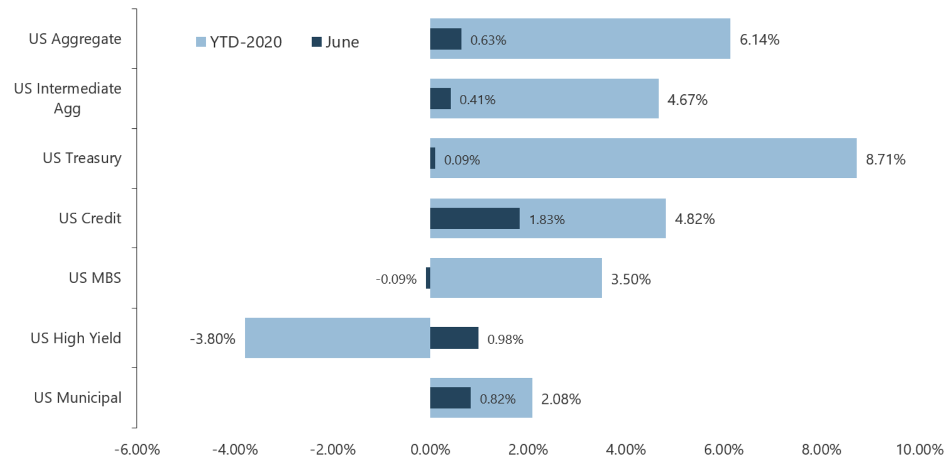
Source: Bloomberg Financial L.P.

The pandemic has introduced new and heightened risks that demand thought and analysis in terms of the impact on cash flow. Bond investors should be quite interested in cash flow due to the two simple goals from lending money: the promised income stream from regular "coupons" and the return of principal at maturity. When the government-mandated shutdowns were instituted, cash flow was disrupted for many corporate and municipal borrowers which is why the fiscal and monetary policy response was so powerful and broad. Cash flow is starting to return to many types of entities which has helped yield spreads on corporate and municipal bonds to improve dramatically from the wide levels witnessed in March and early April. Still, risk remains elevated and the compensation for taking risk remains quite low, so we believe caution is warranted and quality is key in selecting bond investments.

**YTW = Yield to Worst, a measure that incorporates all embedded options*

The big recovery in bonds engineered by the Fed's various programs continues to filter down to the broad economy by easing financial conditions, but access to bank credit for individuals and small businesses remains a concern. If disruptions to income streams are only temporary, obtaining credit should be possible, but many simply cannot yet define temporary. Now that the Fed has begun buying not only bond ETFs but individual bond issues as well, the trickle-down effect of instilling confidence in the system should continue to benefit all types of borrowers.

EXHIBIT 2: FIXED INCOME MARKET TOTAL RETURNS



Source: Bloomberg Financial L.P. and Barclays Securities

Incoming economic data remains quite difficult to assess due to the unusual, man-made nature of the downturn as opposed to the normal cyclical recession. While a rebound does appear to be unfolding as the lockdowns are lifted, the projections from economists are proving far less accurate than usual. This wide gap between expected and actual reflects the sheer scale of what has occurred --- there is just no context for what happened, particularly since it occurred so quickly and so broadly around the world. The lack of context also seems to be impacting economist forecasts which have generally been quite far off the mark versus actuals. Many economic reports are also susceptible to data integrity issues with workplaces not yet back to normal, government programs replacing private income, and forbearance policies in place on many types of loans. Regardless of the actual data, it seems safe to observe that things are bad but improving and will be improving for quite some time. With both the manufacturing and service sectors being impacted at the same time, and with some industries severely constrained, the recovery will be elongated.

We expect economic set-backs due to the highly fragmented and uneven lifting of lockdown measures, both here and abroad, as well as the uncertainty surrounding how renewed spikes in the pandemic will be handled. While we do not foresee another broad lockdown, it is likely that "business as usual" is not in the offing and some restrictions will remain in effect. Before the pandemic crisis, we had concerns that the longest recovery in history was soon susceptible to a mild recession due to structural and sectoral challenges. The slow growth of the working age population, high public sector debt, tepid business investment spending, and the unraveling of globalization were all contributing to the potential for malaise. The pandemic crisis only exacerbates many of these trends, so we are not expecting an economic boom to be unleashed.

Uncertainty is always pervasive but this moment in time feels much more uncertain than usual. Scientific questions concerning the pandemic, the global nature of the crisis, and the shifting government directives are all contributing to a highly challenging environment, all compounded by the upcoming election. We plan to continue balancing risk and reward in allocating your investment portfolio across the range of fixed income securities to provide the ballast and income you expect from your bond portfolio.

535 Stone Cutters Way, Montpelier, VT 05602 •
Tel: 802.229.2838 • Toll Free: 800.255.9946 Fax: 802.229.2837
533-D Johnson Ferry Rd • Suite 350 • Marietta, GA 30068 •
Tel: 770.693.7690 • Fax: 770.512.5176

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