Taxable Fixed Income Strategies

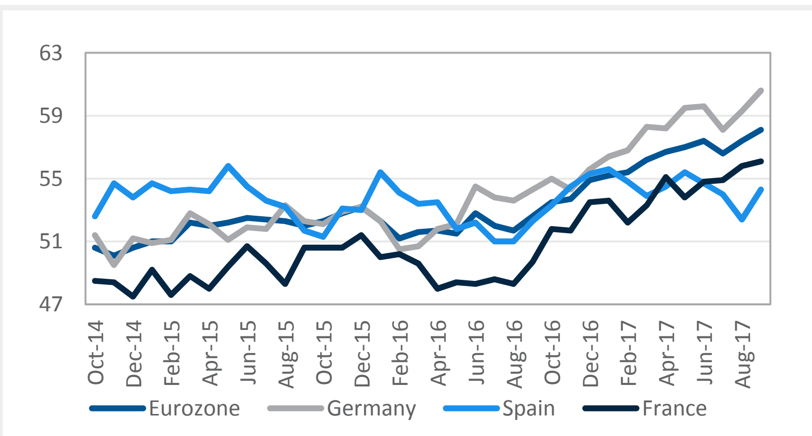
3Q 2017

Brian Meaney, CFA
Vice President, Portfolio Manager
Fixed Income Investments

The third quarter saw another positive performance period for stocks and bonds. US GDP growth recovered after a first quarter slowdown amid improving labor statistics and higher manufacturing surveys. Lawmakers have finally turned their sights on fiscal stimulus, bringing the stock market to all-time highs.

There is much for investors to cheer so far this year. Central bank policies remain accommodative and the pace of normalization is gradual. President Trump finally appears ready to make good on campaign promises for fiscal stimulus. Break-up fears of the Eurozone have receded after elections in Netherlands, France and Germany produced leaders preaching a united Europe. Unemployment is falling and corporate profits are robust. Global growth is in sync for the first time in many years.

PURCHASING MANAGERS INDEX, BY COUNTRY



Source: Bloomberg, as of August 2017.

The Federal Reserve has taken note of the improving economy. After much discussion, the committee decided at its September meeting to gradually reduce its purchase of Treasury bonds and mortgage securities. The size of the Fed balance sheet has skyrocketed since the financial crisis to support growth and ease monetary conditions when the policy rate was zero. This degree of extraordinary support is no longer necessary with unemployment at 4.4% and other measures of slack declining. The Fed reiterated its desire to hike rates by a quarter point later this year and 3 more times in 2018. As the Fed is always carefully notes, there is no preset course for monetary policy and changes to their outlook are possible.

Market and Strategy Returns*

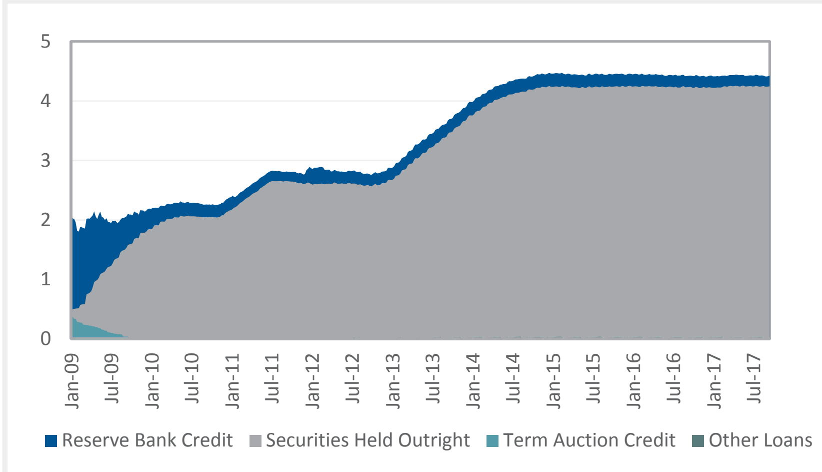
		3Q17	YTD
HGST	**Gross**	**0.36%**	**1.18%**
	Net	0.28%	0.91%
BBC US Gov/Cred 1-3Y		0.34%	1.06%
Ex BBB		0.30%	0.92%
HGCI	**Gross**	**0.76%**	**2.42%**
	Net	0.67%	2.15%
BBC Int. Agg		0.72%	2.34%
Ex. BBB/CMBS/ABS		0.66%	2.07%
Int Gov	**Gross**	**0.53%**	**1.93%**
	Net	0.45%	1.66%
BBC Int Gov		0.66%	1.20%
Corp 1-5	**Gross**	**0.74%**	**2.38%**
	Net	0.68%	2.19%
BBC 1-5 Corp		0.76%	2.65%
BBC Int. Treasury		0.34%	1.71%
BBC Int. TIPS		-0.70%	2.85%
BBC U.S. MBS		0.96%	2.32%
BBC Int. Corp		1.05%	3.75%
Industrials		1.01%	3.72%
Financials		1.11%	3.86%
BBC Muni 5 Year		0.68%	3.87%
ML High Yield		2.03%	7.05%
S&P 500		4.48%	14.24%

*Please see important disclosures at the end of this commentary for strategy and market definitions.
Sources: Bloomberg Barclays (BBC), Bloomberg as September 30, 2017.

Past performance is not a guarantee of future results. Inherent in any investment is the potential for loss.

The Fed's actions were well telegraphed and markets responded with a shrug. We think of the balance sheet announcement (and gradual rate hikes) as a small shift and expect central banks to stick to the lower rates for longer playbook. It makes sense to stay patient rather than be preemptive until more evidence of the recovery is presented. The recovery has seen many false starts, and dovish policy serves as an insurance policy to support growth. Slow normalizing of policy justifies keeping portfolio durations neutral to slightly longer than benchmark.

FEDERAL RESERVE BALANCE SHEEET, TRILLIONS ($)

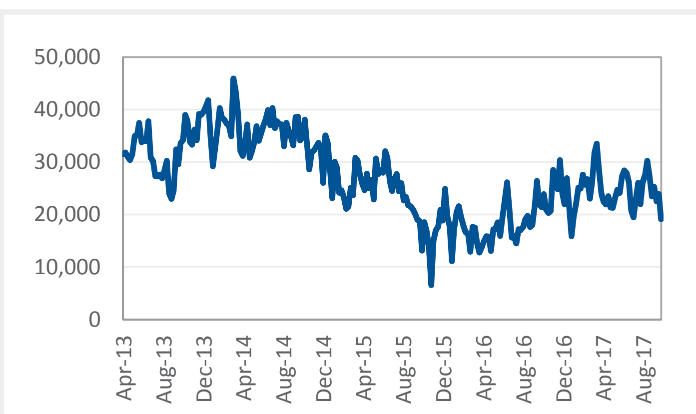


Source: United States Federal Reserve, as of 9/21/17.

Chair Yellen's term expires in February and media reports are heating up over whether she continues in the post or President Trump goes in another direction. If Yellen is not reappointed, then a less dovish Chair is likely. Among the known contenders, all possess impressive resumes and extensive policy experience. Whoever is Fed chair will likely to take a wait-and-see approach to gauge the impact of balance sheet adjustment and possible fiscal stimulus. We don't see the next Fed chair being disruptive for these reasons, provided they retain political independence and clearly communicate to markets.

We increased our exposure to Treasury Inflation Protected securities during the period. This is not a play on runaway inflation, rather we are positioned for modest change in market-implied inflation expectations. Looking at forward looking indicators such as manufacturing surveys and commodities, we believe markets are too pessimistic about the Fed reaching its 2% target. Inflation has softened but we agree with the Fed that this is transitory. Inflation is a lagging indicator of economic growth. As a general rule, inflation lags GDP by 12-18 months meaning the inflation undershoot seen this year is a product of the late 2015/early 2016 slowdown. With GDP back above 2%, inflation should pick up as well. TIPS are the asset class best positioned to outperform in that scenario.

PRIMARY DEALER INVENTORIES, CORPORATE SECURITIES



Source: Federal Reserve Bank of New York, as of 9/27/17.

We maintained our overweight to corporates. Fiera purchases best of breed companies with strong operating performance, manageable debt loads, and businesses with high barriers to entry. Spreads have narrowed but valuations are still reasonable. Healthy company fundamentals, accommodative financial conditions and positive supply dynamics support our continued overweight (and underweight to government securities). Corporate tax reform has the potential to tighten spreads further. Republicans just released an outline calling for lower tax rates, and investment write-offs, among other changes. These proposed changes will affect industries differently, but at this stage is difficult to forecast what the final bill will include (or even pass).

Agency MBS remain a core holding in the strategies, providing a high quality source of income and liquidity. We were cautious leading up to the balance sheet announcement, but the decrease in purchases was in line with expectations. Investors can now focus on relative valuations rather than fear a large buyer like the Fed would dial back aggressively. Also with the market close to fully pricing a rate hike in December, mortgages are now better positioned than at the start of the quarter.

Tax-exempt municipals are the best performing sector in high quality bonds this year (even before the tax advantage). Municipals returns have surged as fears about tax reform stripping the exemption were overblown and at low supply . This pushed valuations to high levels. Municipal credit is strong at the broad level but valuations appeared stretched this summer as 5 year M/T ratios hit low 60s. Issuance historically picks up this time of year and we are watching closely for opportunities to re-enter the sector.

For clients interested in “core plus” strategies, Fiera has successfully implemented a closed end fund strategy to supplement our high grade offerings. “Core plus” strategies have a majority exposure to high quality, long term oriented bond investments with an opportunistic allocation to more aggressive asset classes. Below investment grade bonds are a common “plus” allocation in such strategies. Fiera Capital has developed a framework for clients to gain exposure to higher yielding asset classes (below investment grade bonds, emerging market debt) through closed end funds in a well-executed, risk managed, and diversified manner. Closed end funds now trade at attractive yields with the added benefit of discount to net asset value that open-end bond funds do not offer.

HIGH GRADE FIXED INCOME INVESTMENT TEAM

Jonathan E. Lewis
Chief Investment Officer

Miriam Legrand
Vice President, Corporate Credit

Brian Meaney, CFA
Vice President, Portfolio Manager

Lacey Greenwalt, CFA
Assistant Vice President, Portfolio Manager

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Allocations presented herein are as of the date noted and subject to change.

Strategy Definitions:

- High Grade Short Term (HGST) – utilizes the same investment themes and sector rotation methodology as the Core Intermediate strategy but focuses on shorter maturities, limiting the interest rate risk.
- Intermediate Government (Int Gov) – emphasizes government quality bonds, but in a diversified approach that looks beyond Treasuries to include to pre-refunded municipals, Treasury Inflation-Protected Securities and U.S. dollar denominated sovereign-supported issuers.
- High Grade Core Intermediate (HGCI) – relative return focused versus the Barclays Capital Intermediate Aggregate Index, which offers diversification benefits comparable to the Aggregate Index, but with what we believe to be favorable risk/return metrics.
- Corporate Index Replication (Corp 1-5) – seeks to provide the return and risk profile of a selected benchmark with fewer securities through a separately managed account. This is designed for clients interested in a specific asset class, but wishing to avoid the premium/discount issues of exchanged traded funds.

Index Definitions:

It is not possible to invest directly in an index. Investors pursuing a strategy similar to an index may experience higher or lower returns and will bear the cost of fees and expenses that will reduce returns.

Bloomberg Barclays 1-3 Yr Gov/Credit is the 1-3 Yr component of the U.S. Government/Credit Index. The Government/Credit Index includes securities in the Government and Credit Indices. The Government Index includes treasuries (i.e., public obligations of the U.S. Treasury that have remaining maturities of more than one year) and agencies (i.e., publicly issued debt of U.S. Government agencies, quasi-federal corporations, and corporate or foreign debt guaranteed by the U.S. Government). The Credit Index includes publicly issued U.S. corporate and foreign debentures and secured notes that meet specified maturity, liquidity, and quality requirements. **Bloomberg Barclays Intermediate Aggregate Index** is the intermediate component of the US Aggregate Index. The Bloomberg Barclays U.S. Aggregate Index represents securities that are SEC-registered, taxable, and dollar denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities. These major sectors are subdivided into more specific indices that are calculated and reported on a regular basis. **Bloomberg Barclays U.S. Corporate Investment Grade Index** is a rules-based and market value weighted index of publicly issued U.S. corporate bonds. To be included in the index, bonds must be rated investment-grade (Baa3/BBB- or higher) by at least two of the following ratings agencies: Moody's, S&P, Fitch. Bonds in the Index must have at least one year to final maturity regardless of call features and have at least $250 million par amount outstanding. Bonds in the Index must be fixed rate, although it can carry a coupon that steps up or changes according to a predetermined schedule, must be dollar-denominated and non-convertible and must be publicly issued. **The Bloomberg Barclays 1-5 Corporate Index** is the 1-5 year component of the Corporate Index. **The Bloomberg Barclays Intermediate Corporate Index** is the Intermediate component of the Corporate Index. **Bloomberg Barclays Intermediate Corporate Industrial Index** is the Intermediate component of the Investment Grade Industrial Index. To be included in the index, bonds must be rated investment-grade (Baa3/BBB- or higher) by at least two of the following ratings agencies: Moody's, S&P, Fitch. Bonds in the Index must have at least one year to final maturity regardless of call features and have at least $250 million par amount outstanding. Bonds in the Index must be fixed rate, although it can carry a coupon that steps up or changes according to a predetermined schedule, must be dollar-denominated and non-convertible and must be publicly issued. Bonds in the Index must belong to the Industrial sector. **Bloomberg Barclays Intermediate Corporate Financial Institutions Index** is the Intermediate component of the Investment Grade Financial Institutions Index. To be included in the index, bonds must be rated investment-grade (Baa3/BBB- or higher) by at least two of the following ratings agencies: Moody's, S&P, Fitch. Bonds in the Index must have at least one year to final maturity regardless of call features and have at least $250 million par amount outstanding. Bonds in the Index must be fixed rate, although it can carry a coupon that steps up or changes according to a predetermined schedule, must be dollar-denominated and non-convertible and must be publicly issued. Bonds in the Index must belong to the Finance sector. **Bloomberg Barclays 5 Year Municipal Index** is the 5 Year component of the Municipal Bond Index. The Bloomberg Barclays Municipal Bond Index is a rules-based and market value weighted index engineered for the long-term tax-exempt bond market. To be included in the index, bonds must be rated investment-grade (Baa3/BBB- or higher) by at least two of the following ratings agencies: Moody's, S&P, Fitch. If only two of the three agencies rate the security, the lower rating is used to determine index eligibility. If only one of the three agencies rates a security, the rating must be investment-grade. They must have an outstanding par value of at least $7 million and be issued as part of transaction of at least $75 million. The bonds must be fixed rate, have a due date after December 31, 1990, and must be at least one year from maturity date. Remarketed issues, taxable municipal bonds, bonds with floating rates, and derivatives, are excluded from the benchmark. **Bloomberg Barclays US MBS is a component of the US Aggregate Index.** The MBS Index covers the mortgage-backed pass-through securities of Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC). The MBS Index is formed by grouping the universe of over 600,000 individual fixed rate MBS pools into approximately 3,500 generic aggregates. In other words, each aggregate is a proxy for the outstanding pools for a given agency, program, issue year, and coupon. The index maturity and liquidity criteria are then applied to these aggregates to determine which qualify for inclusion in the index. About 600 of these generic aggregates meet the criteria. The aggregates included in the index are priced daily using a matrix pricing routine based on trader price quotations by agency, program, coupon, and degree of seasoning. **The US Intermediate Treasury Index** represent the intermediate securities of the U.S. Treasury Index, which represents public obligations of the U.S. Treasury with a remaining maturity of one year or more. **The Bloomberg Barclays Intermediate TIPS Index** consists of securities in the intermediate maturity range of the Inflation-Protection securities issued by the U.S. Treasury.