Monthly Commentary

August 2017

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Overview

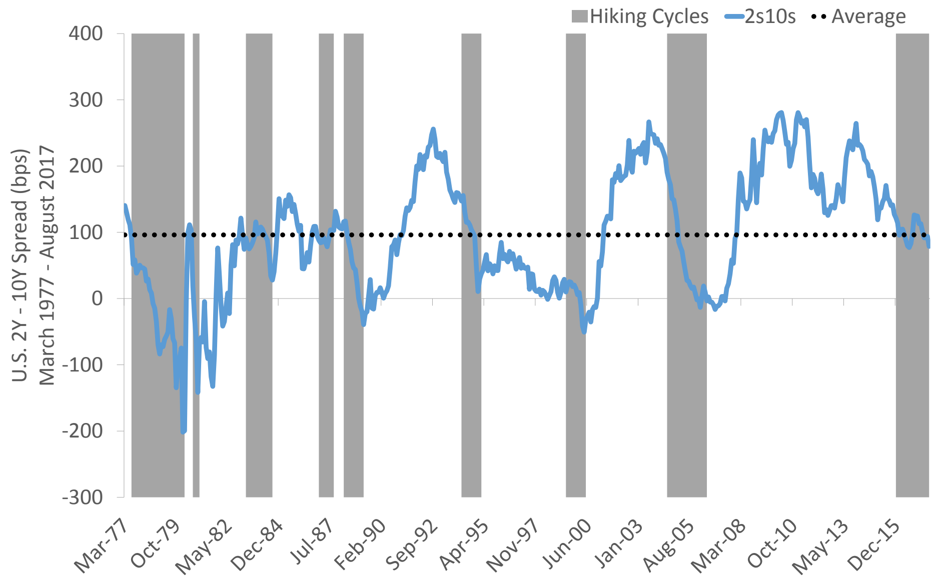
August was a relatively quiet month for the markets despite the news of North Korea successfully launching a missile over Japan and Hurricane Harvey hitting Texas. We continued to remain defensive within our portfolios mirroring our macro concerns around credit, interest rates and uncertainty in the global markets.

We continue to see little value in the front-end of the U.S. Treasury (UST) yield curve and remain tactically bearish on the longer-end. We believe that 10-year UST yields will continue to remain range bound, but are likely to move higher over the course of the next three months. Additionally, we remain bearish on European government bonds due to their long duration and lack of yield. In regards to credit, we maintain a higher credit quality bias.

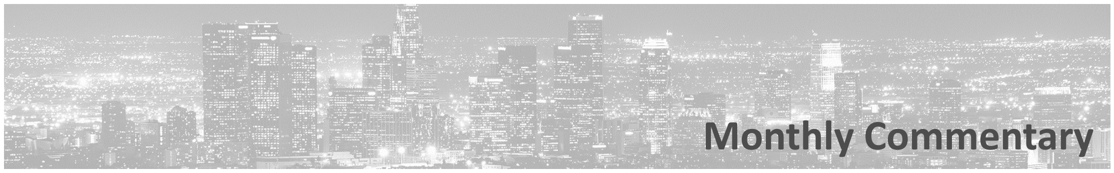
We do not predict a recession over the near-term, with none of our internal indicators signaling one. For example, one gauge we look at is the spread between the 10-year UST bond and the 2-year UST note. In a positive economic environment, the yield on the 10-year should be greater than the 2-year, creating a positive spread. Generally as the economic environment starts to deteriorate, spreads start to narrow and flatten. While spreads have been narrowing, we do not believe this level is close to signaling a recession. In fact, the chart, which depicts the spread between the 2 year UST note and 10 year UST bond, illustrates that the yield curve is near its historic average spread of 95 bps. Historically, recessions have not been triggered until this spread is at or below 0.

As we enter September, we are keeping an eye out for market moving events and catalysts that could create disruption within the credit markets. We believe our current positioning continues to favor defensive portfolios and remain cautious around chasing return.

Spread Between 10-Year UST Bond & 2-Year UST Note (2s10s) and Fed Hiking Cycles
March 30, 1977 to August 31, 2017



Source: DoubleLine, Bloomberg



U.S. Government Securities

- The yield of the benchmark 10-year U.S. Treasury (UST) grinded down steadily in August, falling 17 bps from 2.29% to 2.12%. Several bullish factors contributed to the rally, which includes the weak Consumer Price Index (CPI) data, business leaders quitting Trump's advisory committee, as well as safe-haven demand sparked by the North Korea missile launch.
- According to the Bloomberg Barclays UST Index, the Treasuries market as a whole returned 1.1% for the month of August – the biggest monthly gain since June 2016 – extending the YTD return to 3.15%.
- The yield curve, as measured by the yield spread between 2-year and 30-year UST, flattened from 154 to 140.
- Treasury Inflation-Protected Securities (TIPS) breakevens declined amid CPI slowdown, a drop in oil prices and weakness in U.S. stocks. The 5-year breakeven approached 1.60%, ending the month at 1.65%.

U.S. Treasury Yield Curve

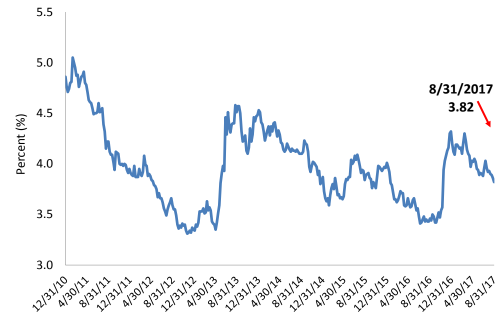
	7/31/2017	8/31/2017	Change
3 month	1.07%	0.99%	-0.08%
6 month	1.13%	1.07%	-0.06%
1 year	1.21%	1.22%	0.01%
2 year	1.35%	1.33%	-0.02%
3 year	1.51%	1.43%	-0.08%
5 year	1.84%	1.70%	-0.14%
10 year	2.29%	2.12%	-0.17%
30 year	2.90%	2.73%	-0.17%

Source: Bloomberg

Agency Mortgage-Backed Securities

- Prepayment speeds increased by about 9% month-over-month (MoM) owing primarily to a three-day increase in day count. Recent vintage (2015-2016) 3.5 and 4.0 cohorts experienced the highest increase in speeds while seasoned vintage 3.5 and 4.0 cohorts experienced a much smaller increase in speeds. If the prepayment experience of regions hit by Hurricanes Sandy and Matthew are any indication, we can expect homeowners in regions hit by Hurricanes Harvey and Irma to likely prepay slower by about 2-7 conditional prepayment rate (CPR).
- The 30-year Freddie Mac Commitment Rate continued to decline, in conjunction with the 10-year rate, and ended the month at 3.82%. The Mortgage Bankers Association (MBA) refinance rate remained largely unchanged.

Freddie Mac Commitment Rates
December 31, 2010 to August 31, 2017



Source: Bloomberg, DoubleLine

- Gross Agency MBS issuance was approximately $49 billion, bringing volume to $835 billion year-to-date (YTD).
- The Bloomberg Barclays U.S. MBS Index performed positively once again for the month with a return of 0.73%. The duration of the Index stood at 4.24 years as of month-end.
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Conditional Prepayment Rates (CPR) 2017	Sept	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	June	July	Aug
Fannie Mae (FNMA)	18.9%	17.9%	17.0%	15.1%	10.7%	8.6%	10.6%	9.7%	11.5%	12.3%	11.4%	12.4%
Freddie Mac (FHLMC)	18.6%	17.7%	16.6%	14.7%	10.4%	8.6%	13.6%	12.5%	14.5%	15.4%	14.8%	16.0%
Ginnie Mae (GNMA)	22.5%	21.7%	21.2%	18.5%	13.1%	11.8%	10.2%	9.6%	11.3%	12.1%	11.3%	12.2%

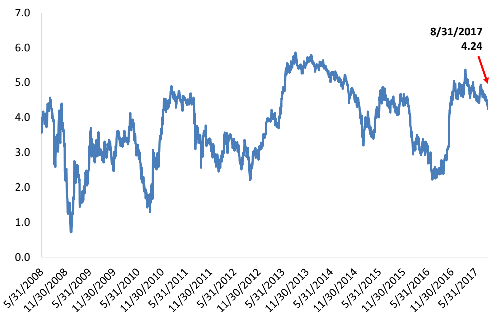
Bloomberg Barclays Capital U.S. MBS Index	6/30/2017	7/31/2017	8/31/2017	MoM Change
Average Dollar Price	$103.38	$103.63	$104.46	$0.83
Duration	4.72	4.66	4.24	-0.42

Bloomberg Barclays Capital U.S. Index Returns	6/30/2017	7/31/2017	8/31/2017
Aggregate	-0.10%	0.43%	0.90%
MBS	-0.40%	0.45%	0.73%
Corporate	0.26%	0.73%	0.84%
Treasury	-0.16%	0.17%	1.08%

Source: eMBS, Barclays Capital

dex stood at 4.24 years as of month-end.

Duration of Barclays U.S. MBS Index
June 1, 2008 to August 31, 2017



Source: Bloomberg, DoubleLine

Non-Agency MBS

- Spreads were flat during August as the non-Agency MBS sector continued to be supported by strong fundamentals and a positive technical environment.
- The impact of Hurricane Harvey on the non-Agency MBS market will vary depending on a security's underlying loan exposure to the Houston residential market. Credit Risk Transfer (CRT) experienced spread widening as some deals have exposure as high as 3% of their outstanding loan balance. Legacy spreads were firm as exposure ranged from about 10 to 60 basis points (bps).
- Fitch downgraded 348 bonds in August that are subject to trustee litigation from Wells Fargo. The downgrades come after Wells Fargo as trustee of 20 legacy deals held back approximately 17% of principal proceeds for lawsuits when the bonds were called in June. While some of the bonds were previously investment grade, all bonds are now below investment grade. Rating downgrades could expand to other trustees facing lawsuits from investors.
- There was $5.8 billion of legacy non-Agencies traded on bid lists during August compared to $4.2 billion during July. The increase in volume was primarily due to a Government-Sponsored Enterprise (GSE) list in the earlier part of the month.

Commercial MBS

- August private-label CMBS issuance volume decreased 17% MoM. Three conduit deals totaling $2.7 billion and 10 single-asset single-borrower (SASB) deals totaling $3.6 billion priced during the month. Private-label CMBS issuance volume is 38% YTD higher than for the same period in 2016. New issue volume has largely been driven by SASB deals, for which issuance is 130% higher than through the same period in 2016. Meanwhile, conduit issuance volume is up only 5% year-over-year (YoY).
- Secondary pension & investing (P&I) CMBS trading totaled $18.1 billion in August, increasing 30% MoM however slightly below the 2017 monthly average of $18.8 billion through July. Secondary market cash spreads were mixed with AAA LCFs (last cash flows) tightening by 3 bps to swaps +85 bps while BBBs widened by 25 bps to swaps +355 bps. CMBX spreads were also mixed alongside broader equity and credit markets, with AAA 2012-2016 reference indices tightening by an average of 2 bps, and BBBs widening by an average of 29 bps.
- The outstanding private label CMBS universe increased MoM by $3.5 billion or 0.8% to $442.4 billion in August, however net issuance is still down 8.7% YTD. This marked the second month in 2017 when net issuance has increased. The outstanding conduit universe increased to $329.8 billion, up $726 million MoM. Similarly, the outstanding SASB universe increased to $106.2 billion, up $2.1 billion MoM and 4.62% YoY. The CMBS delinquency rate decreased for the second month in a row, falling by 5 bps in August to 5.4%, following the 26 bps decrease in July. The delinquency rate still remains 76 bps higher than August 2016.

Asset-Backed Securities

- New issuance in Asset-Backed Securities (ABS) over the month of August remained strong as over $170 billion deals have been issued YTD. Auto ABS and credit card ABS constituted the bulk of that new issuance with $74 billion and $32 billion, respectively.
- Demand in secondary trading markets has also remained firm with spreads relatively unchanged MoM across all ABS sectors. With expectations for impending interest rate hikes, the demand has strongly concentrated in shorter duration trades.
- Investor appetite for more off-the-run opportunities remains robust as esoteric ABS deals continued to

make a push into the market at tighter spread levels. Deals within whole business, inventory receivables and aircraft receivables saw strong investor interest throughout the summer months.

- The consumer ABS sector resumed its march to higher valuations in the face of YTD weakening collateral performance; however, investors remained constructive given the current preference for shorter duration transactions and strong structural protections within the deals.
- The Barclays U.S. ABS Index returned 0.38% for the month of August and 1.80% YTD.

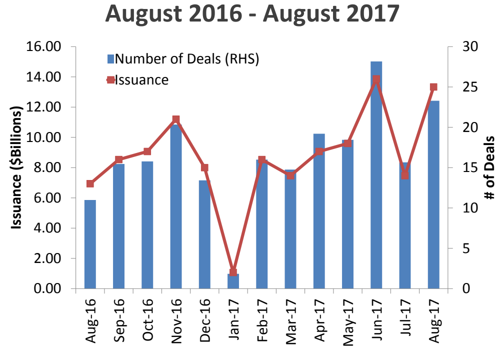
Investment Grade Credit

- Positive technicals were not enough to keep spreads from widening in August. Spreads widened at the beginning of the month from 98 bps, touching 106 bps on August 11th, to end the month at 104 bps. The rally in the U.S. Treasury market more than offset spread widening and the Bloomberg Barclays U.S. Credit Index ended up 0.84% for the month. Spreads are in 14 bps YTD and the Index is up 5.31%.
- The front-loaded heavy new issuance and geopolitical risks pushed spreads out early in the month despite record flows into Investment Grade (IG) mutual funds and exchange-traded funds (ETF). Flows continued in August at a rate of $15.5 billion, bringing YTD flows to $216.1 billion. New issuance of $102.8 billion, mostly in the first two weeks of the month, was only slightly below the $118.1 billion issued in August of 2016. There were several large deals this month, including $17.25 billion of U.S. Dollar (USD)-denominated British American Tobacco bonds to fund the acquisition of Reynolds America and $16 billion by Amazon to fund the Whole Foods acquisition.
- Metals & Mining was one of the best performing sectors, up 1.73%, benefiting from a rally in Commodities, especially Copper. Utilities, up 1.55%, Local Authority, up 1.55%, and Sovereigns, up 1.89%, outperformed, benefitting from the rally in U.S. Treasuries, especially at the long-end of the curve.

Collateralized Loan Obligations

- August was the second busiest month this year for CLO issuance with a total of $12.42 billion issued across 25 deals. This brought YTD issuance up to $73.27 billion across 132 deals. At the beginning of the year, the market expected Risk Retention implementation to hamper CLO total issuance. The CLO new issue market has surpassed the 2017 total issuance expectation and expectations have been revised up to $90 billion as managers and investors have found a new normal in this Risk Retention environment.

U.S. CLO Monthly Issuance
August 2016 - August 2017



Source: S&P Capital IQ
*RHS = Right Hand Side

- Unlike the busy primary market, the CLO secondary market was fairly quiet which was expected during the last month of summer. Prices and spreads were relatively unchanged for the month.

Bank Loans

- The S&P/LSTA Leveraged Loan Index posted a total return of -0.04% in August, the second negative reading in the last three months. After a very strong return in July, a heavy new issue calendar led to a softer technical environment in August.
- There was limited return dispersion across the ratings classes: CCC-rated names declined 0.12%, B-rated names declined 0.10%, and BB-rated names declined 0.01%.
- The worst performing sector was Oil & Gas, which posted -1.97% due to a sell-off in oil. The best returning sectors were Utilities and Forest Products, which returned 0.60% and 0.91%, respectively.

High Yield

- August consisted of two halves in High Yield (HY). Initially, heavy new-issue supply and negative headlines related to escalating geopolitical tensions, the Barcelona terrorist attacks and political fallout from the Charlottesville riots pushed spreads wider. Then mid-month, HY bond prices recovered as deal issuance slowed and political concerns dissipated somewhat. HY issuance roughly doubled in August from July, with $19.8 billion of new supply spread across 35 tranches, versus $10.2 billion across 21 tranches one month earlier, according to Leveraged Commentary & Data (LCD) data. Despite a slowdown for deal flow in the second half, the month also produced the highest issuance total for an August since 2012.

- Total returns for the month were slightly negative at -0.12% for the Citi High-Yield Market Capped Index; however, the CCC-rated portion returned -1.39%. Mutual fund outflows totaled $3.3 billion, marking the largest monthly outflow since March, which saw $8.1 billion in outflows, and extending YTD net outflows to $9.2 billion, according to JP Morgan.

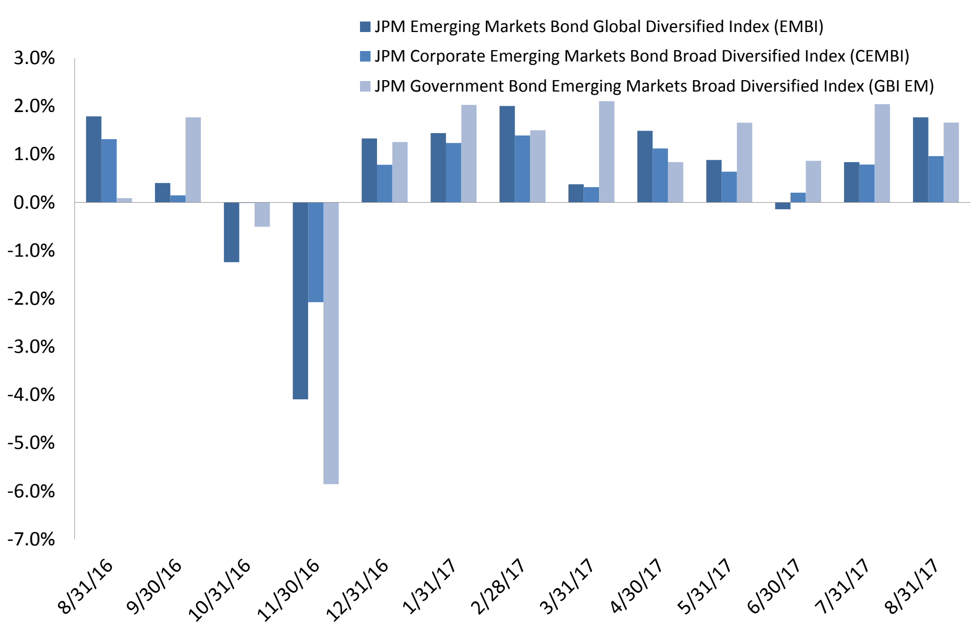
Commodities

- In August 2017 the broad commodity market was mixed with the Bloomberg Commodity Index (BCOM) rallying 0.31% while the S&P Goldman Sachs Commodity Index (GSCI) declined by 0.86%.
- The Energy sector declined by 0.37% in August with Hurricane Harvey driving unleaded gasoline up 12.57% while WTI crude declined 6.18%. The Precious Metals sector rallied 3.87% with Gold up 3.83% and Silver up 4.16%. Industrial Metals was the best performing sector in August, rallying 8.54%; Copper was up 6.41%. Agriculture declined by 7.51% with the worst performer being Wheat and the best performer being Cotton, with returns of -13.68% and 3.01%, respectively. Livestock declined by 5.51% with lean hogs and live cattle declining 7.00% and 5.85%, respectively.

Emerging Markets

- Emerging Market (EM) sovereign and corporate external bonds posted positive performance in the month of August. Despite a backdrop of heightened geopolitical tension, external conditions remained generally favorable for the EM fixed income asset class with continued investor appetite for higher-yielding EM debt.
- The August return for the JP Morgan Emerging Markets Bond Index Global Diversified (EMBI GD) was driven by a flattening of the UST curve. Credit spreads were relatively unchanged over the month, with the spread over UST tightening 4 bps to 300 bps.
- Primary election results in Argentina were seen as favorable for President Macri's Cambiemos party, leading to a rally in the bonds and the currency. The Chilean Peso was a notable outperformer during the month, driven by the strong rise in copper prices.
- We expect that headwinds over the remainder of the year could materialize from rising UST yields, Federal Reserve (Fed) rates hikes, European Central Bank (ECB) tapering,

JP Morgan Emerging Markets Bond Index Performance
August 31, 2016 to August 31, 2017



Source: JP Morgan

German elections, early Italian elections, and Brexit negotiations, as well as policy risk stemming from the U.S., Europe, and China.

International Sovereign

- Global government bonds posted positive returns in the month of July supported by both declining yields against a backdrop of heightened geopolitical tensions, as well as foreign currency gains against the USD as the U.S. administration's economic agenda remained stalled.
- The USD, as indicated by the USD Index (DXY), fell for a sixth consecutive month. Although U.S. second-quarter Gross Domestic Product (GDP) growth was revised up to 3.0% and retail sales data were strong, inflation continued to remain subdued, keeping a lid on USD strength. U.S. Federal Reserve (Fed) Chair Janet Yellen's lack of monetary policy details at the Jackson Hole symposium was seen as dovish by some market participants.
- The Euro rose over the month against a backdrop of positive economic data in Europe and expectations from some market participants of monetary tapering talks commencing in the fall. ECB President Draghi avoided making comments on Euro strength at the Jackson Hole symposium, reinforcing Euro strength.
- The Japanese Yen rallied against the USD this month benefiting from its safe haven status as geopolitical tensions flared with North Korea firing a missile over Japan around the end of the month. Bank of Japan (BoJ) Governor Kuroda said in an interview at Jackson Hole that the BoJ would continue extremely accommodative policy for some time.

Infrastructure

- Infrastructure spending took center stage again in Washington as President Trump addressed Congress on government bureaucracy and regulation slowing large scale infrastructure projects that are seeking approval. Much of the President's comments focused on reducing the time it takes to approve infrastructure projects and did not address funding for these assets/projects.
- Despite Washington's languid pace in the area of infrastructure, the private debt markets have seen brisk issuance volume in this space both domestically and internationally. August saw projects in the area of utility grade solar, aviation, traditional power utilities and rail transport. Spreads continued to compress, albeit, at a decreasing rate and investor demand continued to grow.

U.S. Equities

- August was a continuation of the "maximum complacency" environment of the previous months, as seen in the S&P 500 for the month. The S&P 500 set an all-time new high early in the month and after recovering from modest declines mid-month ended August essentially unchanged (up 0.3%).
- These benign returns, however, belied the return of volatility, albeit moderate, to the U.S. equity markets. In August, the CBOE SPX Volatility Index (VIX) reached its highs for 2018 after establishing an all-time low below nine in late July. We continue to believe the markets are overly complacent, given historically high corporate margins and stock multiples at a time when the Fed is raising rates and tapering its balance sheet.
- In August, the Technology sector remained a leadership sector in the S&P 500, gaining almost three percent for the month. Energy was the weakest sector, and following a 5.5% decline in August is now down over fifteen percent in 2017. The August weakness in Financials is also noteworthy, down 1.6%, as this had been a leadership sector following the 2016 Presidential election.

Global Equities

- Global equities managed a positive return in August with the Morgan Stanley Capital International All-Country World Index (MSCI ACWI) up 0.44% during the month. U.S. equities produced positive gains with the S&P 500 and Dow Jones 0.31% and 0.65%, respectively. The Russell 2000 and Nasdaq Composite were mixed, -1.27% and 1.43%, respectively.
- In Europe, equities underperformed global equities with the

Eurostoxx 50 down 0.71% during the month. Core European equities declined with the DAX returning -0.52% and CAC returning -0.16%. In the periphery, the FTSEMIB was 0.85% and IBEX -1.76%. UK equities, as measured by the FTSE 100, outperformed returning 1.65%.

- Asian equities were mixed in August. Chinese equities, as measured by the Shanghai Composite, performed well returning 2.79%. Japanese equities, as measured by the Nikkei, declined 1.34%. Korean equities, as measured by the KOSPI, declined 1.64%.
- EM equities outperformed developed markets with MSCI EM Index returning 2.27%. Brazil's Ibovespa gained 7.46%. Russian equities, as measured by MSCI Russia Index, gained 8.14%.

Bloomberg Barclays U.S. Credit Index—The US Credit component of the U.S. Government/Credit Index. This index consists of publically-issued U.S. corporate and specified foreign debentures and secured notes that meet the specified maturity, liquidity, and quality requirements. To qualify, bonds must be SEC-registered. The US Credit Index is the same as the former US Corporate Investment Grade Index.

Bloomberg Barclays U.S. MBS Index—An index that measures the performance of investment grade fixed-rate mortgage-backed pass-through securities of the Government-Sponsored Enterprises (GSEs): Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC).

Bloomberg Commodity Index (BCOM) - An index calculated on an excess return basis that reflects commodity futures price movements. The index rebalances annually weighted 2/3 by trading volume and 1/3 by world production and weight-caps are applied at the commodity, sector and group level for diversification. Roll period typically occurs from 6th-10th business day based on the roll schedule.

Citi High-Yield Cash-Pay Capped Index -This index represents the cash-pay securities of the Citigroup High-Yield Market Capped Index, which represents a modified version of the High Yield Market Index by delaying the entry of fallen angel issues and capping the par value of individual issuers at $5 billion par amount outstanding.

Cotation Assistee en Continu 40 (CAC) - The CAC 40 Index which is a French stock market index. It tracks 40 of the largest French stocks on the Paris Bourse, or stock exchange.

Consumer Price Index (CPI) - A measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. The CPI is calculated by taking price changes for each item in the predetermined basket of goods and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living.

Deutsche Borse AG German Stock Index (DAX) - The German stock index, which represents 30 of the largest and most liquid German companies that trade on the Frankfurt Exchange.

Energy Select Sector Index - The Energy Select Sector Index includes companies from the following industries: oil, gas & consumable fuels and energy equipment & services.

Eurostoxx 50 Index - A stock index of Eurozone stocks designed by STOXX, an index provider owned by Deutsche Borse Group and SIX group, with the goal of providing a blue-chip representation of Supersector leaders in the Eurozone.

Financial Times Stock Exchange 100 (FTSE 100) - A capitalization-weighted index of the 100 most highly capitalized companies traded on the London Stock Exchange.

Financial Times Stock Exchange Milano Italia Borsa (FTSE MIB) - The benchmark stock market index for the Borsa Italiana, the Italian national stock exchange, which superseded the MIB-30 in September 2004. The index consists of the 40 most-traded stock classes on the exchange.

G-10 - A grouping of 10 countries identified by the World Trade Organization which are "vulnerable" to imports due to ongoing reform in the agricultural sector. This grouping includes Switzerland, Japan, South Korea, Taiwan, Liechtenstein, Israel, Norway, Iceland, Bulgaria and Mauritius.

Ibovespa - This accumulation index represents the present value of a portfolio begun on 2 January 1968, with a starting value of 100 and taking into account share price increases plus the reinvestment of all dividends, subscription rights and bonus stocks received.

Indice Bursatil Espanol (IBEX) - The official index of the Spanish Continuous Market. The index is comprised of the 35 most liquid stocks traded on the Continuous market. It is calculated, supervised and published by the Sociedad de Bolsas.

JP Morgan Corporate Emerging Markets Bond Broad Diversified Index (CEMBI) -This index is a market capitalization weighted index consisting of US-denominated Emerging Market corporate bonds. It is a liquid global corporate benchmark representing Asia, Latin America, Europe and the Middle East/Africa.

JP Morgan Government Bond Emerging Markets Broad Diversified Index (GBI EM) -This index is the first comprehensive, global local Emerging Markets index, and consists of regularly traded, liquid fixed-rate, domestic currency government bonds to which international investors can gain exposure.

JP Morgan Emerging Markets Bond Global Diversified Index (EMBI) -This index is uniquely-weighted version of the EMBI Global. It limits the weights of those index countries with larger debt stocks by only including specified portions of these countries' eligible current face amounts of debt outstanding. The countries covered in the EMBI Global Diversified are identical to those covered by EMBI Global.

Korea Composite Stock Price Index (Kospi) - A market capitalization weighted index of all common stocks traded on the Stock Market Division—previously, Korea Stock Exchange—of the Korea Exchange. It is the representative stock market index of South Korea, similar to the Dow Jones Industrial Average or S&P 500 in the United States.

Markit CMBX Index (CMBX) - A synthetic tradable index with 6 subindices referencing a basket of 25 commercial mortgage-backed securities offerings issued in 2012.

Morgan Stanley Capital International All Country World Index (MSCI ACWI) -A market-capitalization-weighted index designed to provide a broad measure of stock performance throughout the world, including both developed and emerging markets.

An investment cannot be made in an index.

MSCI Emerging Markets (MSCI EM)- An index that covers 23 Emerging Market countries and is designed to capture the large and mid-cap representation across those countries.

MSCI Russia Index - A free-float capitalization-weighted index used to track the equity market performance of Russian securities on the MICEX Stock Exchange.

Nikkei 225 Index - A price-weighted index comprised of Japan's top 225 blue-chip companies on the Tokyo Stock Exchange. The Nikkei is equivalent to the Dow Jones Industrial Average Index in the U.S.

Shanghai Composite Index - A capitalization-weighted index that tracks the daily performance of all A-shares and B-shares listed on the Shanghai Stock Exchange. The index was developed on December 19, 1990 with a base value of 100.

S&P Goldman Sachs Commodity Index (GSCI) - Standard & Poor's Goldman Sachs Commodity Index, or GSCI, is a composite index of commodity sector returns which represents a broadly diversified, unleveraged, long-only position in commodity futures.

S&P 500 Index - Standard & Poor's US 500 Index, a capitalized-weighted index of 500 stocks.

S&P/LSTA Leveraged Loan Index - An index designed to track the market-weighted performance of the largest institutional leveraged loans based on the market weightings, spreads and interest payments.

An investment cannot be made in an index.

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