

Fixed income market update

June 2021

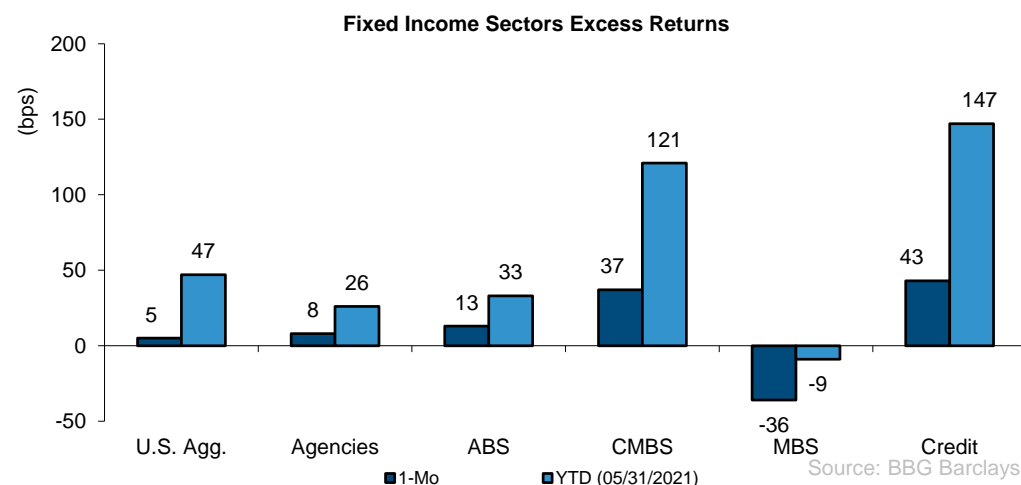
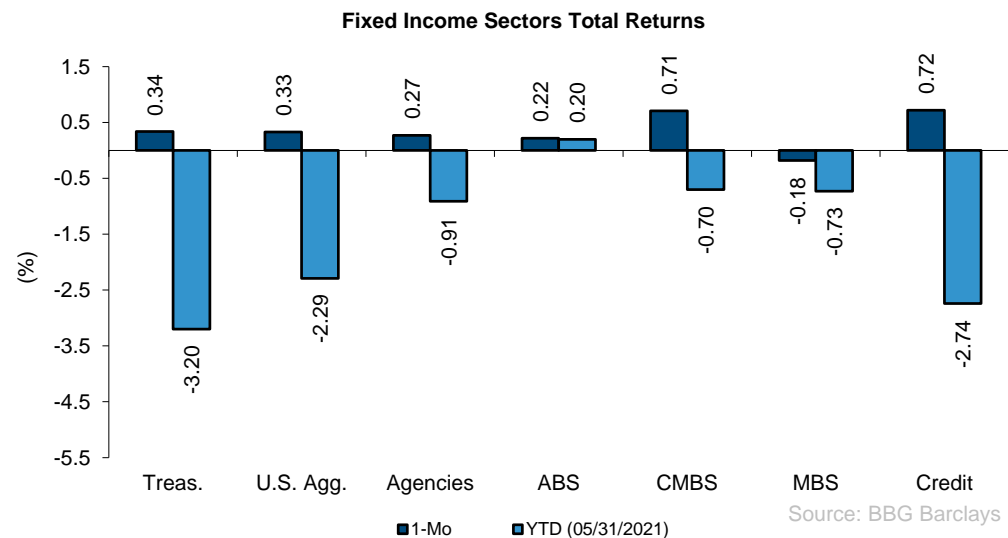
BMO Fixed Income

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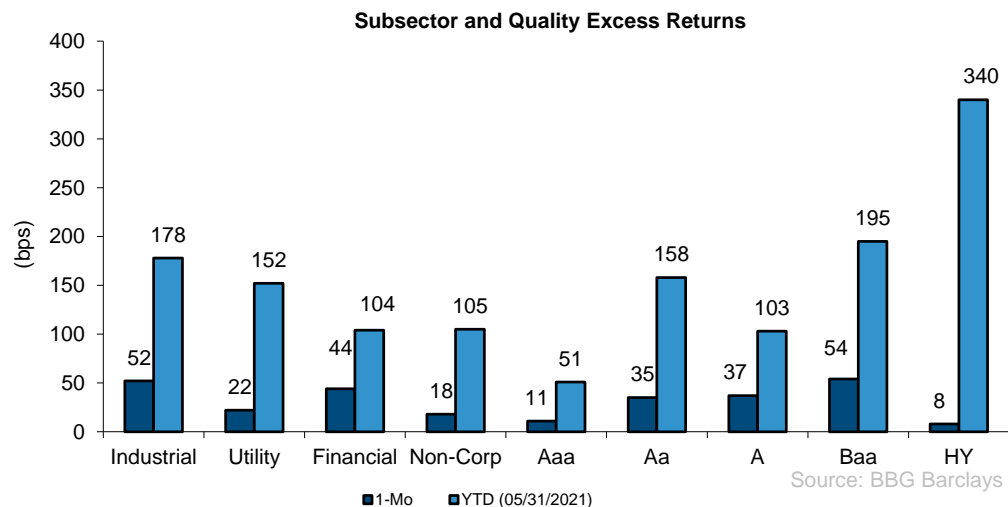
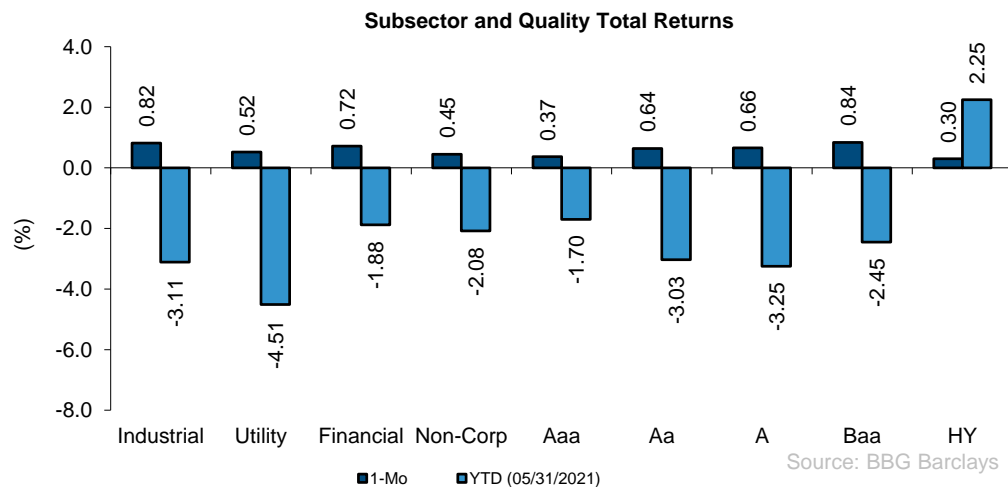
Fixed income market update

- For the month ended May 31, 2021, the Bloomberg Barclays U.S. Aggregate Bond Index returned 0.33%. Year to date, the index has returned -2.29%.
- U.S. Treasuries returned 0.34% during the month as the yield on the 10-year U.S. Treasury declined to 1.59% from 1.63% at the end of April. For the month, long Treasuries (+0.45%) outperformed intermediate Treasuries (+0.32%).
- Mortgage-backed securities (MBS) returned -0.18% during the month, underperforming Treasuries by 36 basis points on a duration-adjusted basis. The option adjusted spread (OAS) of the Bloomberg Barclays U.S. Mortgage Index widened 9 basis points during the month, ending the period at 16 basis points.



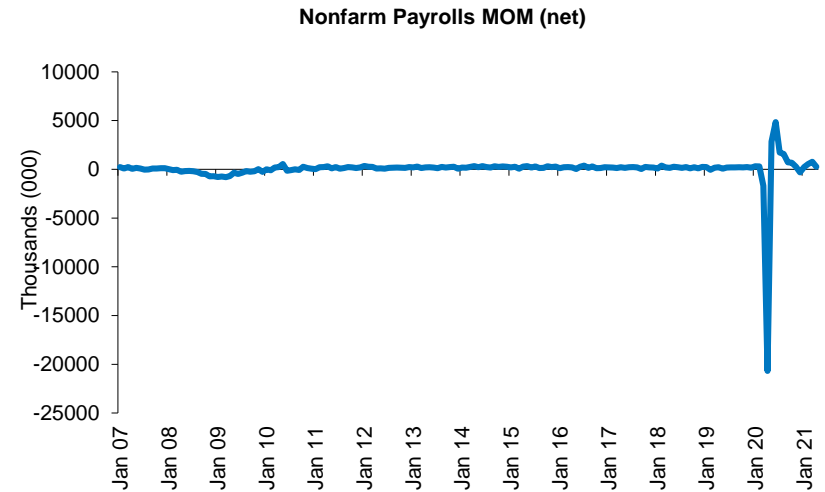
Fixed income market update (continued)

- Credit securities returned 0.72% for the month, outperforming Treasuries by 43 basis points on a duration-adjusted basis. The OAS of the Bloomberg Barclays U.S. Credit Index ended the period at 79 bps, 4 basis points tighter than at the end of April.
- For the month, industrials delivered 52 basis points of excess return on a duration-adjusted basis, outperforming financials, utilities and non-corporates by 8, 30, and 34 basis points, respectively.
- BBB rated securities were the best performing investment grade quality segment during the month, delivering 54 basis points of excess return and outperforming AAA, AA and A rated securities by 43, 19 and 17 basis points of excess return, respectively. High yield delivered 8 basis points of excess return for the month.

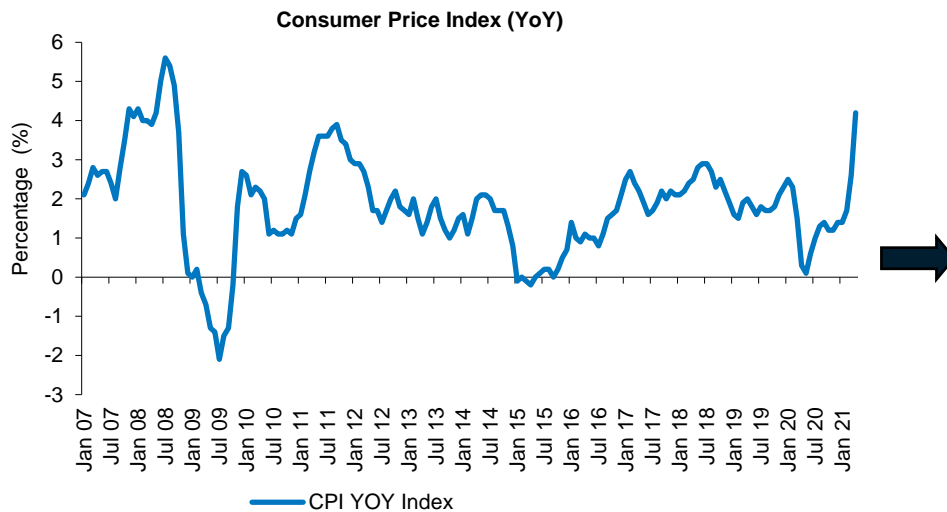


Economic update

Payrolls rose by 266,000, significantly below expectations of 1,000,000 new jobs. The unemployment rate, which had been projected to fall from 6.0% to 5.8%, rose to 6.1%. Underemployment continued to come down, declining from 10.7% to 10.4% and participation rose 0.2% to 61.7%. At the same time, the Department of Labor's Job Openings and Labor Turnover Survey showed over 8 million available positions. Arguing the disappointing new jobs figures were the result of excessive government support, over 20 states ended participation in the Federal government's extended unemployment benefits program.



Source: Bureau of Labor Statistics



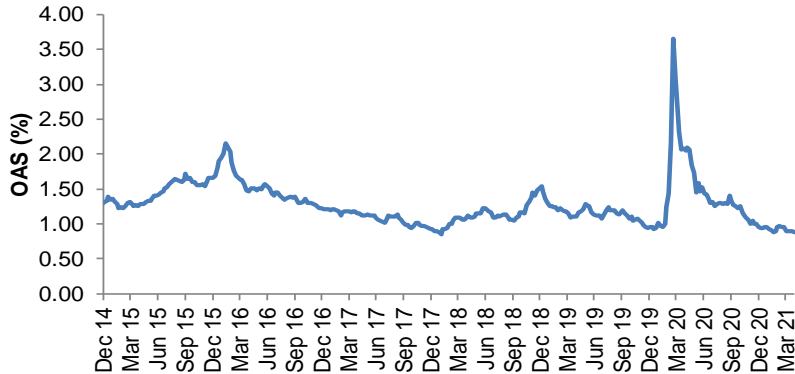
Source: Bureau of Labor Statistics



The consumer price index (CPI) rose 0.8% in April and 4.2% for the trailing 12 months, the largest increase since 2008. Projections for inflation have increased given the year over year comparison with the early stages of the pandemic in 2020, but the recent realized inflation meaningfully exceeded even the higher estimates. Core CPI, which excludes food and energy, rose 3.0% for the trailing year vs. estimates of 2.3%. The monthly increase in Core CPI of 0.9% was the largest monthly increase since 1981. Core PCE rose 0.7% for the month and 3.1% for the trailing year.

Market update

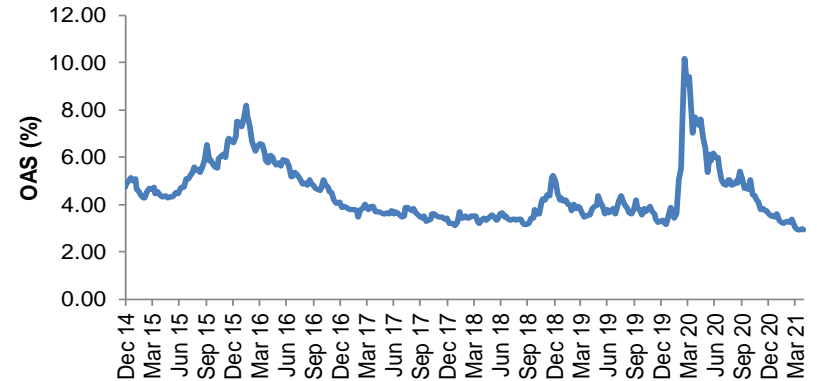
U.S. Investment Grade Corporate Spreads (weekly)



Source: Bloomberg Barclays

Corporate spreads continued to grind tighter during May, ending at the tightest level since early 2005.

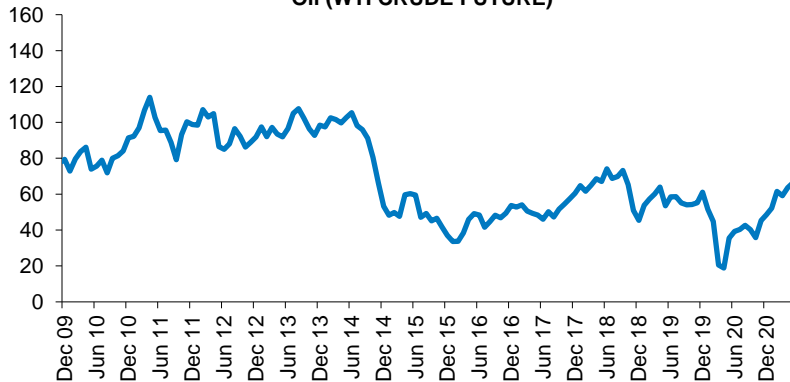
U.S. High Yield Corporate Spreads (weekly)



Source: Bloomberg Barclays

Since March 2020, high yield has delivered positive returns in 13 of the past 14 months. Issuance is running 90% above last year's record pace.

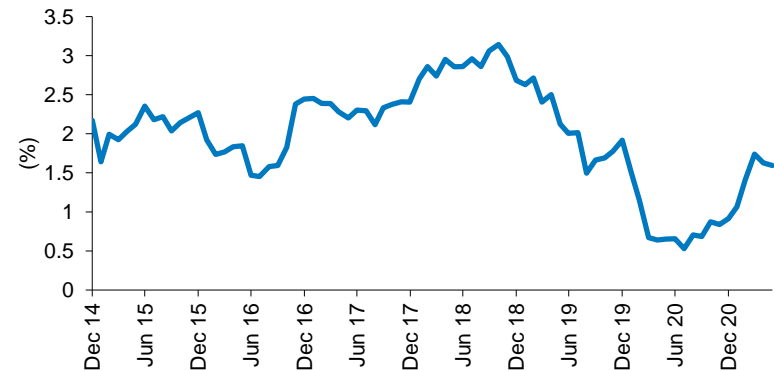
Oil (WTI CRUDE FUTURE)



Source: Bloomberg

Oil closed May above \$66 a barrel, its highest level in two years and more than triple its price from April 2020.

U.S. 10 Year Treasury Yields



Source: Bloomberg

After 10-year Treasury yields nearly doubled in the first quarter, rates declined modestly in both April and May.

News & nuggets

Economic growth:

- U.S. GDP estimates released in May showed the economy grew 6.4% in the first quarter, unchanged from the prior estimate and modestly below expectations. Consumer spending and business investment grew 11.3% and 10.8%, respectively; each were revised higher from the prior estimate, while inventory reduction deducted 2.8% vs. the 2.6% previously reported; inventory reduction is typically viewed as positive for future GDP reports as inventories will need to be rebuilt.

Earnings:

- First quarter earnings data has continued to improve. With 95% of companies reporting, first quarter corporate profits have grown 51.9% year over year (vs. 45.8% as of the end of April). These results have meaningfully exceeded expectations for the first quarter profits growth, which as of March 31, was for 23.8%. The second quarter is expected to be even stronger with profit growth of 59.9% and revenue growth of 18.9%. For the full year 2021, corporate earnings are projected to grow 33.7% with revenue growth of 11.8%.

Virus & Vaccine:

- As of the end of May, 51% of the U.S. population has received at least one dose, with 41% of the population fully vaccinated, up from 43% and 30%, respectively, at the end of April. Along with the increased vaccination of the population, COVID related restrictions continue to ease in the U.S.

Fiscal Policy:

- At the end of the month, President Biden proposed a \$6 trillion budget for next year, which includes spending for his proposed infrastructure plan and American Families Plan as well as tax increases for both individuals and corporations. Even with the tax hikes included, the budget would result in a \$1.8 trillion deficit next year and deficits of at least \$1.3 trillion through 2029.

Outlook and conclusions:

Monetary policy:

- Minutes from the April 27-28 meeting of the Federal Open Market Committee were released in May. Markets were looking for hints regarding prospective tapering of asset purchases at the April meeting; the minutes revealed that some members believed that “if the economy continued to make rapid progress toward the Committee’s goals, it might be appropriate at some point in upcoming meetings to begin discussing a plan for adjusting the pace of asset purchases.” Regarding inflation, the minutes noted that “after the transitory effects of these factors fade, participants generally expected measured inflation to ease.” The next FOMC meeting is scheduled for June 15-16.

Outlook:

- May was a conundrum for those seeking clarity on the post-COVID recovery. In May we witnessed significantly higher inflation than expected, including the highest monthly core inflation print in four decades, as well as a jobs report that underwhelmed projections so badly it shifted the narrative on unemployment policy. Despite these significant data points, however, it felt as though markets took no notice. Treasury rates, credit spreads and equities were nearly unchanged, with sentiment improving modestly even with these developments. The Fed minutes suggested a touch more flexibility on policy than had been interpreted from the prior meeting, though Fed members took pains to address and calm the burgeoning inflation concerns. The inflation and jobs reports created the potential for a disruption to sentiment, but other factors such as strong GDP numbers and corporate profits suggest the robust recovery carries on. Though overall spreads continue to look tight in both credit and securitized sectors, we do continue to see opportunities at the sub-sector and quality level as well as in security selection.

Fixed income returns as of May 31, 2021

Index Returns as of May 31, 2021				
	Total Return (%)		Excess Return (%)	
	Month-to-Date	Year-to-Date	Month-to-Date	Year-to-Date
U.S. Aggregate	0.33	-2.29	0.05	0.47
U.S. Treasury	0.34	-3.20	-	-
Intermediate	0.32	-1.07	-	-
Long	0.45	-11.10	-	-
TIPS	1.21	1.12	-	-
Agencies	0.27	-0.91	0.08	0.26
U.S. MBS	-0.18	-0.73	-0.36	-0.09
ABS	0.22	0.20	0.13	0.33
CMBS	0.71	-0.70	0.37	1.21
U.S. Credit	0.72	-2.74	0.43	1.47
Intermediate	0.54	-0.87	0.24	0.53
Long	1.05	-5.84	0.75	3.02
Industrial	0.82	-3.11	0.52	1.78
Utility	0.52	-4.51	0.22	1.52
Financial	0.72	-1.88	0.44	1.04
Non-Corporate	0.45	-2.08	0.18	1.05
Aaa	0.37	-1.70	0.11	0.51
Aa	0.64	-3.03	0.35	1.58
A	0.66	-3.25	0.37	1.03
Baa	0.84	-2.45	0.54	1.95
High Yield	0.30	2.25	0.08	3.40
Floating Rate Notes	0.11	0.39	0.10	0.35

Source: Bloomberg Barclays

Disclosures

All investments involve risk, including the possible loss of principal.

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The option-adjusted spread (OAS) is the measurement of the spread of a fixed-income security rate and the risk-free rate of return, which is adjusted to take into account an embedded option. Basis points (bps) represent 1/100th of a percent (for example: 50 bps equals 0.50%)

The Bloomberg Barclays US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. The Bloomberg Barclays US Mortgage Backed Securities (MBS) Index tracks fixed-rate agency mortgage backed pass-through securities guaranteed by Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC). Bloomberg Barclays U.S. Credit Index measures the investment grade, US dollar-denominated, fixed-rate, taxable corporate and government related bond markets. It is composed of the US Corporate Index and a non-corporate component that includes foreign agencies, sovereigns, supra-nationals and local authorities.

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