



Fort Washington Full Discretion Fixed Income

2Q17

Highlights

- Full Discretion Fixed Income returned 1.55% (gross) in the second quarter, outperforming the Bloomberg Barclays U.S. Aggregate Index by 10 basis points.
- The strategy's allocation to High Yield contributed to performance due to spread compression and a rally in the 5 – 10 year part of the curve.
- Within Investment Grade Corporates, positive selection effects drove outperformance. A large contribution of outperformance was generated from foreign sovereign and government related corporate securities.
- Positive security selection within Securitized Assets also contributed to returns as all major underlying sectors – ABS, CMBS, Agency and Non-Agency RMBS – experienced positive selection effects.
- Yield curve positioning detracted from performance as the team maintained biases of being long the 10-year part of the curve and short the 30-year part of the curve.
- The strategy held an allocation to TIPS throughout the quarter, which detracted from performance relative to the benchmark as inflation expectations eased.

Investment Professionals

**Timothy J. Policinski, CFA**

Managing Director  
Senior Portfolio Manager  
39 Years Experience

**Daniel J. Carter, CFA**

Vice President  
Senior Portfolio Manager  
21 Years Experience

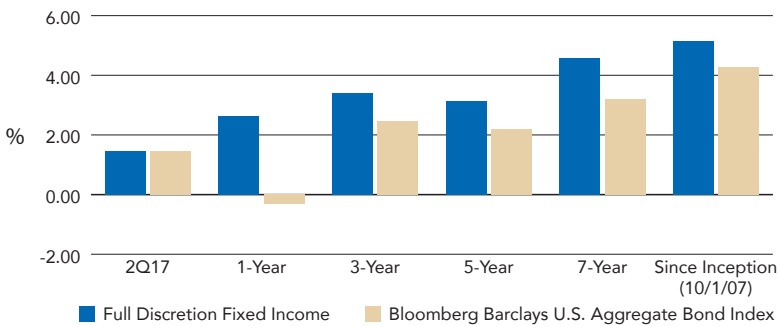
**Bradley D. Sikora**

Product Specialist – Fixed Income  
6 Years Experience

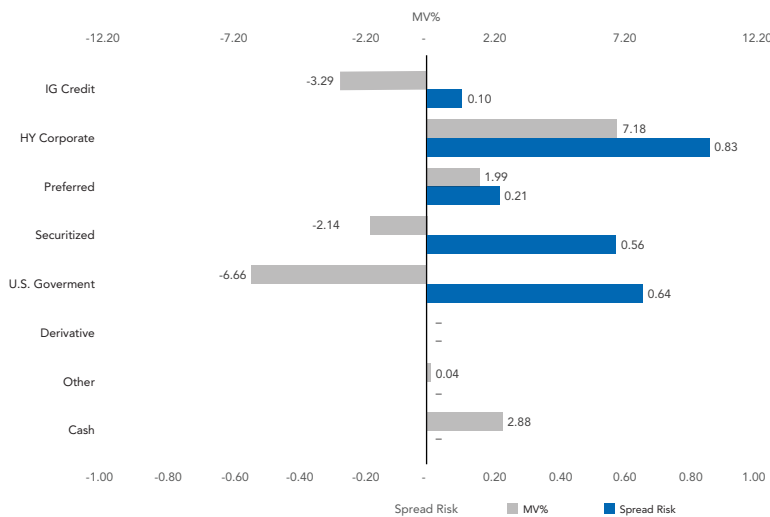
The two lead Portfolio Managers are supported by the dedicated research teams of Global Investment Grade Credit, Securitized Assets, Leveraged Credit, and Emerging Markets, as well as the Chief Economist and Chief Investment Officers.

Source: Fort Washington Investment Advisors. Past Performance is not indicative of future results.

Historical Performance (Annualized Net Return as of June 30, 2017)



Sector Analysis (Portfolio Exposure vs. Benchmark)



Source: Barclays Point. For illustrative purposes only; this illustrates the portfolio's allocation of dollars (grey) and risk (blue) compared to the benchmark. Information is subject to change at any time without notice. Index is the Barclays U.S. Aggregate Bond Index. This should not be considered investment advice or a recommendation of any strategy, product, or particular security. See disclosures for important information about derivatives. This supplemental information complements the Full Discretion Composite Presentation.

Current Risk Budget



## Market Overview

Economic fundamentals are solid yet not consistent with an increase from post-crisis trend growth (~2 – 2.5%). The labor market remains a bright spot and provides confidence that the U.S. consumer can continue to support overall economic growth. Second quarter growth tracked around 2.5%, which would put GDP for the first half of the year at roughly 2%.

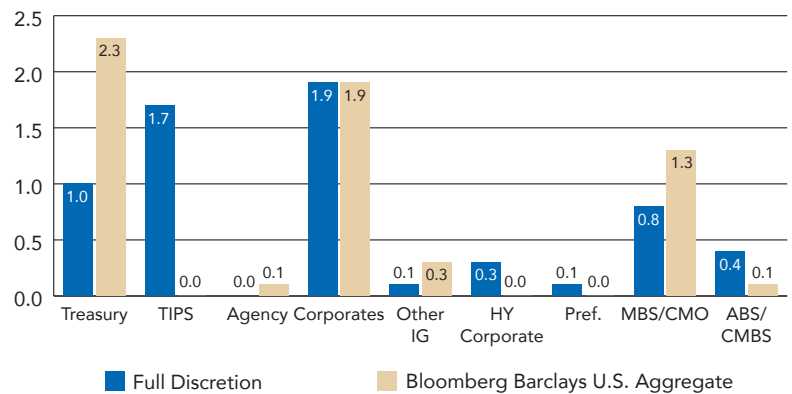
Broad financial conditions remain easy and supportive of risk assets and growth. Credit spreads tightened marginally over the quarter and near post crisis tights. Global central bank policy is generally accommodative, but has taken a recent hawkish turn in some developed economies. Market expectations of Fed rate hikes remain shallow with U.S. data showing no sign of acceleration, particularly inflation data which has been especially weak. Main risks are hawkish Central Banks might tighten conditions too quickly as accommodation is removed.

## Portfolio Statistics

### Characteristics

	Full Discretion Composite	Bloomberg Barclays U.S. Aggregate
Effective Duration	6.35	6.01
Yield to Worst	2.83	2.55
Effective Maturity	10.96	8.27
Average Quality	AA3/A1	AA1/AA2

### Contribution to Duration



Source: Barclays POINT, Bloomberg. Sector and duration allocation are subject to change at any time. Quality distribution subject to change. See the appendix for important information about derivatives. This supplemental information complements the Full Discretion Fixed Income Composite Presentation.

## Portfolio Activity

The team made several tactical shifts to interest rate exposure, yet generally maintained a duration-neutral bias versus the benchmark. Our economic outlook points to higher interest rates over the medium and long term with the upside risk in nominal yields squarely related to inflation and inflation expectations. Due to attractive valuations of TIPS in terms of expected inflation vs. realized inflation, we will likely maintain an allocation to TIPS as a cheap option on future inflation.

The team maintained its overweight bias to the 10-year part of the curve during the quarter. This part of the curve remained relatively attractive to other maturities.

Spreads remain close to post-crisis tights and still modestly attractive given our economic outlook coupled with accommodative financial conditions. As a result, the team maintained a slight overweight to risk assets, holding the Risk Budget target at 30% of max. The allocation of risk to High Yield, Investment Grade Corporate Bonds, and Securitized Assets was generally unchanged.

## Outlook

Factor	Outlook	Comments
Financial Conditions	Slightly Positive	<ul style="list-style-type: none"> <li>• Credit spreads marginally tighter since last month – remain near post-crisis tights</li> <li>• Global Central Bank policy generally accommodative but has taken hawkish turn in some developed economies, including the U.S.</li> <li>• Market expectations of Fed rate hikes remain shallow as U.S. data showings no signs of acceleration – inflation data has been especially weak</li> <li>• Risks: Hawkish Central Banks create risk of tightening conditions too quickly as accommodation is removed</li> </ul>
Economic Growth	Slightly Positive	<ul style="list-style-type: none"> <li>• Recent data has indicated no pickup from the post-crisis trend of ~2% growth</li> <li>• Economic survey data has declined, and no meaningful pickup in hard data</li> <li>• Labor market remains solid which should support overall economic growth</li> <li>• Inflation has moderated from prior trend. Uncertainty as to whether the weakness is “transitory”</li> </ul>
Valuations	Credit: Neutral	<ul style="list-style-type: none"> <li>• At year to date tights – additional tightening opportunity without higher rates moderate at best</li> <li>• M&amp;A deleveraging on target; overall leverage modestly declining providing chance for BBB’s to tighten further</li> </ul>
	Rates: Neutral	<ul style="list-style-type: none"> <li>• Near-term and medium-term: market pricing in ~17 bps of 2017 rate hikes and +30 bps in 2018. Market expectations have remained shallow due to uninspiring economic data, particularly inflation.</li> <li>• Long-term: inflation expectations remain subdued. Upside risk to nominal yields squarely related to inflation and inflation expectations</li> </ul>
Market Sentiment	Negative	<ul style="list-style-type: none"> <li>• Equity market sentiment is at bullish extremes</li> <li>• Open interest in 10-Year Treasury futures contracts remains at high levels</li> </ul>
<b>Macro Summary</b>	<b>Position</b>	
Risk Budget	30%	<ul style="list-style-type: none"> <li>• Broad financial conditions remain stable at easy levels – supportive of growth and risk assets. Economic fundamentals are solid yet not consistent with an increase from post-crisis trend. <b>Recession risk is low and anticipated default rate has been reduced significantly.</b> Valuations have adjusted to the more positive outlook. Summary: Still comfortable with modest overweight to risk assets.</li> </ul>

Source: Fort Washington. This is for informational purposes only and should not be construed as investment advice. Outlook reflects subjective judgments and assumptions subject to change without notice. Unexpected events may occur, there can be no assurance that developments will transpire as forecast. Past performance is not indicative of future results.

## Full Discretion Composite Performance and Disclosures

	2Q17	YTD	12/31/16	12/31/15	12/31/14	12/31/13	12/31/12	12/31/11	12/31/10	12/31/09	12/31/08	12/31/07 <sup>1</sup>
Full Discretion Fixed Income (Gross)	1.55%	2.85%	6.62%	1.11%	5.26%	-0.93%	6.78%	10.09%	9.54%	15.64%	-3.99%	2.43%
Full Discretion Fixed Income (Net)	1.46%	2.66%	6.16%	0.71%	4.84%	-1.38%	6.30%	9.60%	9.05%	15.11%	-3.99%	2.43%
Bloomberg Barclays U.S. Aggregate	1.45%	2.27%	2.65%	0.55%	5.97%	-2.03%	4.22%	7.84%	6.54%	5.93%	5.24%	3.00%
Full Discretion Fixed Income 3-Year Annual Standard Deviation <sup>2</sup>	—	—	3.03%	3.07%	2.99%	3.06%	2.49%	3.00%	—	—	—	—
Bloomberg Barclays Aggregate 3-Year Annual Standard Deviation <sup>2</sup>	—	—	2.98%	2.88%	2.63%	2.71%	2.38%	2.78%	—	—	—	—
Dispersion <sup>3</sup>	—	—	—	—	—	—	—	—	—	—	—	—
Number of Accounts	≤5	≤5	≤5	≤5	≤5	≤5	≤5	≤5	≤5	≤5	≤5	≤5
Composite Assets (\$ millions)	\$640.9	\$640.9	\$606.9	\$310.4	\$308.9	\$293.4	\$297.5	\$276.2	\$251.0	\$229.0	\$199.5	\$207.7
Composite % of Firm Assets	1.36%	1.36%	1.33%	0.72%	0.69%	0.67%	0.70%	0.73%	0.69%	0.77%	0.80%	0.76%

Composite inception date: 10/01/07 and Composite creation date: 07/01/15.

<sup>1</sup>2007 returns are partial-year returns, reflecting the composite inception date of 10/01/07. <sup>2</sup>The 3-Year annualized ex-post standard deviation is calculated using monthly returns to measure the average deviations of returns from its mean. <sup>3</sup>Dispersion is not calculated for years in which the composite contains five portfolios or less. Dispersion is calculated as the equal weighted standard deviation of quarterly returns for those portfolios held in the composite during the full measurement period.

Past performance is not indicative of future results.

Fort Washington's Full Discretion Fixed Income strategy uses explicit measures of value and risk as a guide to investment decisions. Combined with intensive fundamental research, the portfolio management team believes this provides the best opportunity for excess return.

The Full Discretion Composite includes all fixed income accounts above \$50MM with the ability to invest in High Yield (at least 30%) and have the unrestricted ability to invest in Investment Grade Securities across all durations relative to the Bloomberg-Barclays U.S. Aggregate. Accounts within this composite may also have the ability to hold derivatives. These investments, whether or not traded on an established market, include but are not limited to options, notional principal contracts, futures or forward contracts, VIX futures; and options on futures, forward contracts, or debt obligations. Investments made in derivatives are used in line with the portfolio's risk exposure, allowing for the portfolio to reduce its exposure to an existing position or increase exposure within the portfolio's guidelines. Derivatives involve risks in addition to the risks of underlying securities, including liquidity, interest rate, market, credit, and management. Investing in derivatives could lose more than the amount invested.

Effective 10/22/15, the Full Discretion Fixed Income fee is 0.40% for the first \$100 million and 0.35% for amounts in excess of \$100 million for separate accounts, and 0.40% for the commingled vehicle. The benchmark for this composite is the Bloomberg Barclays U.S. Aggregate Bond Index. This benchmark covers the USD-denominated, investment grade, fixed-rate, and taxable areas of the bond market.

Portfolios in this composite include cash, cash equivalents, investment securities, interest and dividends. Cash is maintained, within each separately managed account segment, in accordance with our asset allocation ratio. The U.S. dollar is the base currency. The specific securities identified and described do not represent all of the securities purchased, sold, or recommended.

Returns are presented gross and net of management fees and include the reinvestment of all income. Gross returns will be reduced by investment advisory fees and other expenses that may be incurred in the management of the account. Net of fee performance was calculated using the actual management fees charged. Individual portfolio returns are calculated on a daily valuation basis. Past performance is not indicative of future results.

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Fort Washington claims compliance with the Global Investment Performance Standards (GIPS<sup>®</sup>) and has prepared and presented this report in compliance with the GIPS Standards. Fort Washington has been independently verified for the periods 7/1/94 - 12/31/15. A copy of the verification reports are available upon request. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request. To receive a complete list and description of composites, contact Fort Washington by phone at (888) 244-8167, in writing at 303 Broadway, Suite 1200, Cincinnati, Ohio 45202, or online at FortWashington.com.



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