

Economic Outlook:

“Moderate” Recovery Prompts Further Fed Action

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Fed Raises Rates at March Meeting

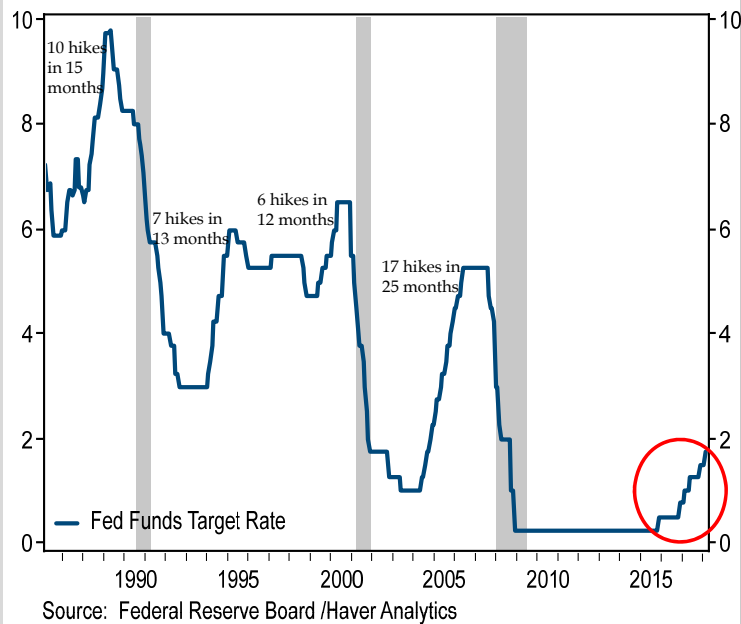
Historically Low Rates

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Fed raises rates 25bps to a range of 1.50% to 1.75% at latest March meeting, the sixth rate hike since liftoff in December 2015

Fed raised rates 25bps to a range of 1.25%-1.50% at December 2017 meeting, the third rate increase in 2017 (March & June)

Fed raised rates 25bps to 0.75% in December 2016 after seven consecutive meetings of unchanged policy



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Focus Shifts to "Normalize" Balance Sheet

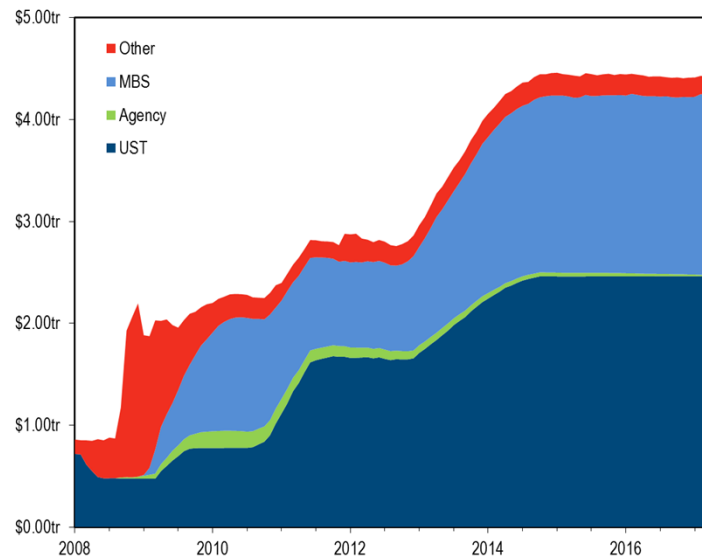
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UST: Cap of \$6bn per month increased by \$6bn every quarter until it reaches \$30bn in October 2018

2017 monthly avg. Fed purchases of UST: \$16.82bn

MBS: Cap of \$4bn per month increased by \$4bn every three months until it reaches \$20bn

2017 monthly avg. Fed purchases of MBS: \$25.07bn



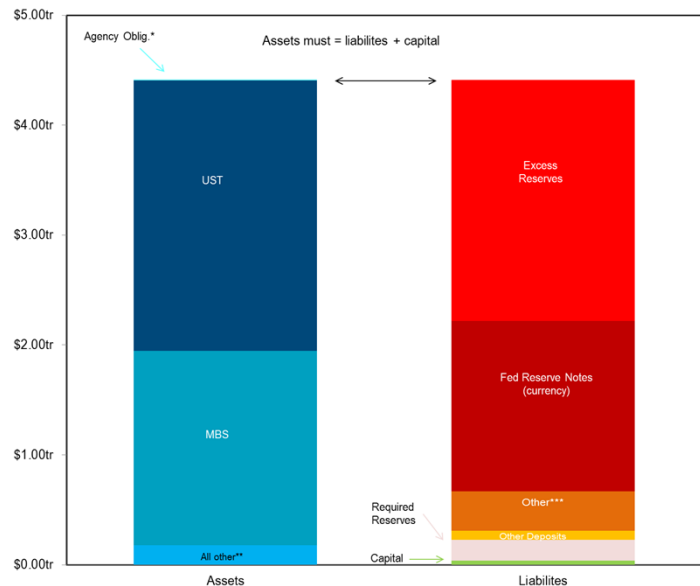
*Other includes discount window lending; lending to other institutions; assets of limited liability companies (LLCs) that have been consolidated onto the Federal Reserve's balance sheet, and foreign currency holdings associated with reciprocal currency arrangements with other central banks (foreign central bank liquidity swaps).

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Consolidated Balance Sheet

An increase on both sides of the Fed's balance sheet, as the Fed purchased bonds from primary dealers in reverse auctions but paid for them by essentially making a ledger notation in the dealers' reserve accounts

Essentially an equivalent impact had the Fed mandated purchases by the banks themselves



Source: Federal Reserve Board/Haver Analytics

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"Moderate" Growth

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GDP has Moderated

U.S. GDP in Q4 rose 2.9% following a 3.2% rise in Q3

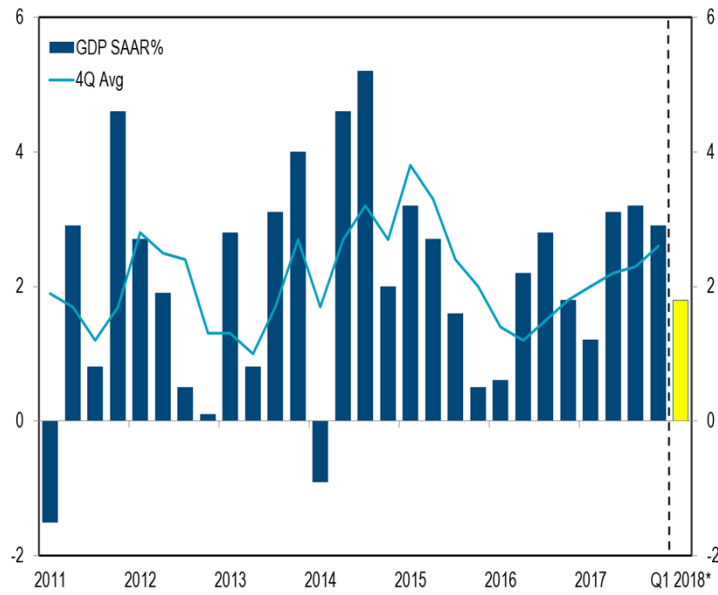
California GDP rose 3.4% in Q3, a four-quarter high*

U.S. growth in 2017 averaged 2.6%

4Q avg U.S. GDP: 2.6% in Q4 vs. 2.3% in Q3

2015 avg growth: 2.0%
2016 avg growth: 1.9%
2017 avg growth: 2.6%

*Data as of Q3 2017

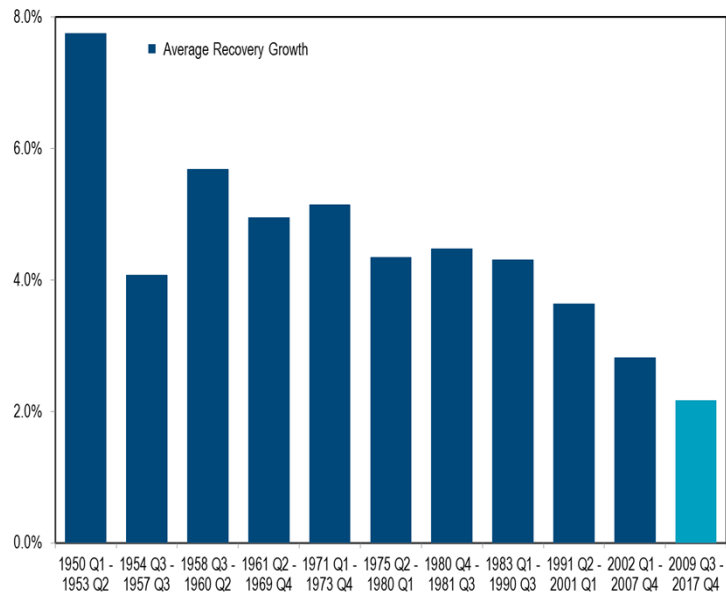


Source: Bureau of Economic Analysis/ Haver Analytics

*Atlanta Fed GDPNow Forecast

Average Growth vs. Previous Recoveries

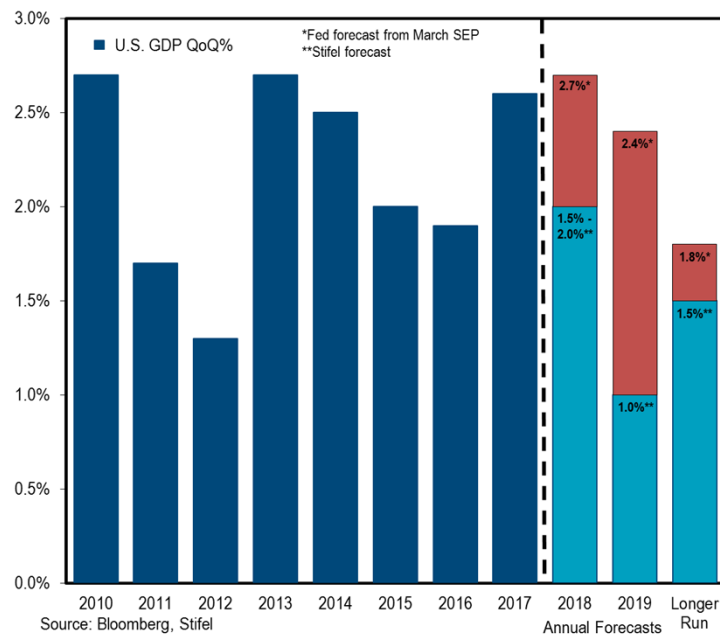
2.2% average growth in the U.S. since the Great Recession, the lowest average growth rate compared to previous recoveries



Source: NBER/ Haver Analytics

GDP Forecast

The Fed increased its 2018 GDP forecast to **2.7%** from 2.5% and its 2019 GDP forecast to **2.4%** from 2.1% in the latest March SEP



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"Strong" Job Gains

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Job Growth Continues Downward Trend

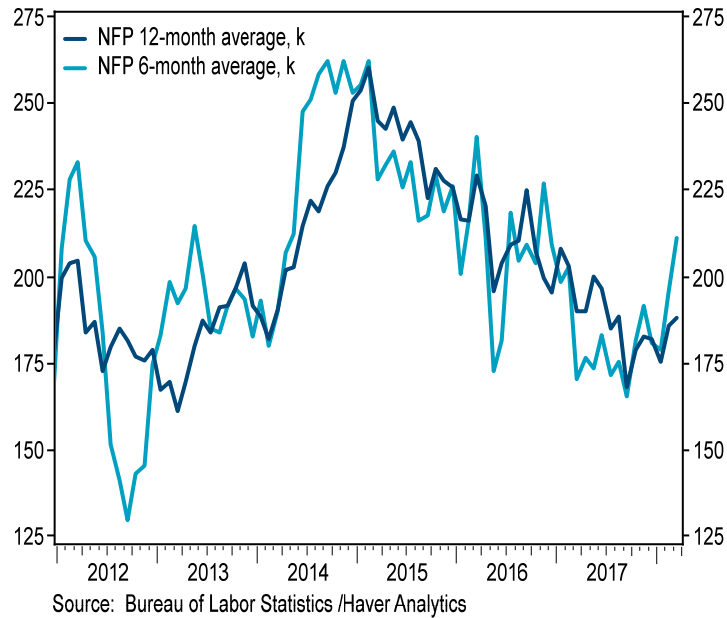
90 consecutive months of positive payroll growth

March payrolls rose **103k**, a six-month low, and following a 326k gain in February

12-month average rose from 186k to **188k** in March, a seven-month high

Above 200k in April, June, August, October & November 2017

On a 6-month average basis, the trend has slowed from 250k in 2014 to 232k in 2015 to 203k in 2016 to 169k in 2017

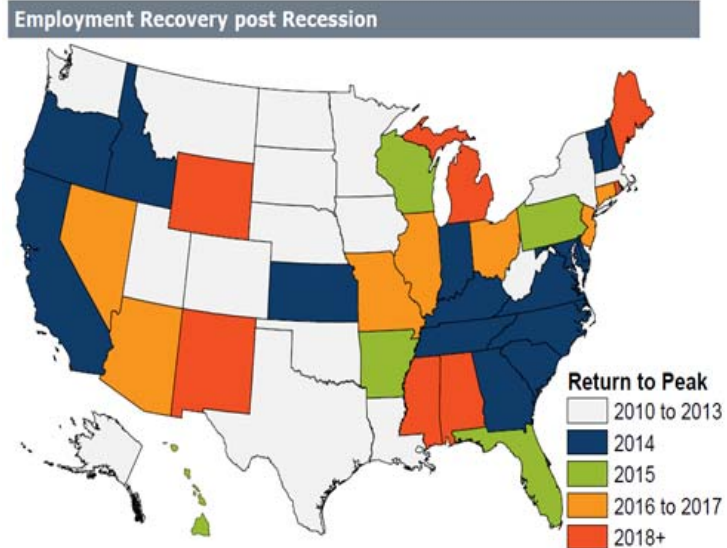


Uneven Growth Across States

The recovery has been notably uneven across state lines

States in the Central Plains were among the earliest states to reach and surpass their previous peaks in employment

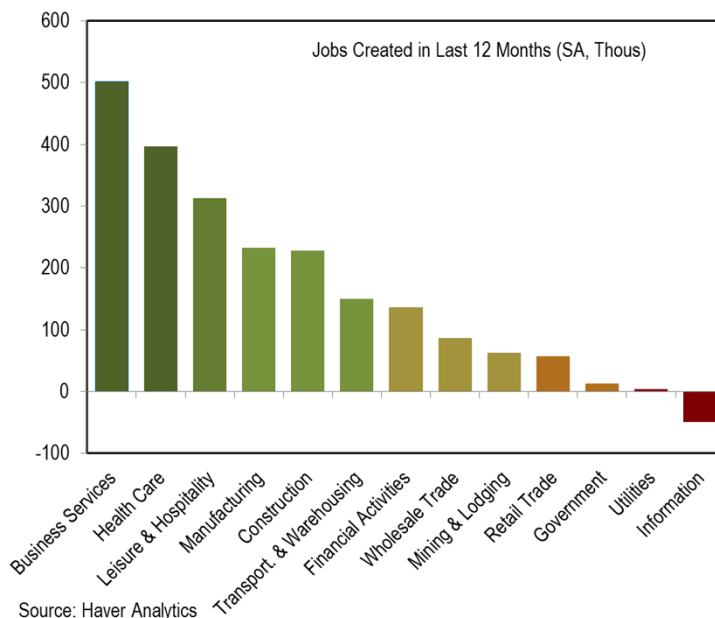
Several states in the Deep South and West are among the slowest labor markets to recover



Uneven Growth Across Industries

While certain sectors clearly remain at the forefront of such *"improvement,"* other sectors, such as retail, for example, have emerged as a source of weakness with job creation slowing noticeably

Business services has experienced the most robust growth, adding nearly 500k payrolls in the past 12 months, while information services has been the worst performing sector, shedding more than 62k jobs over the past 12 months



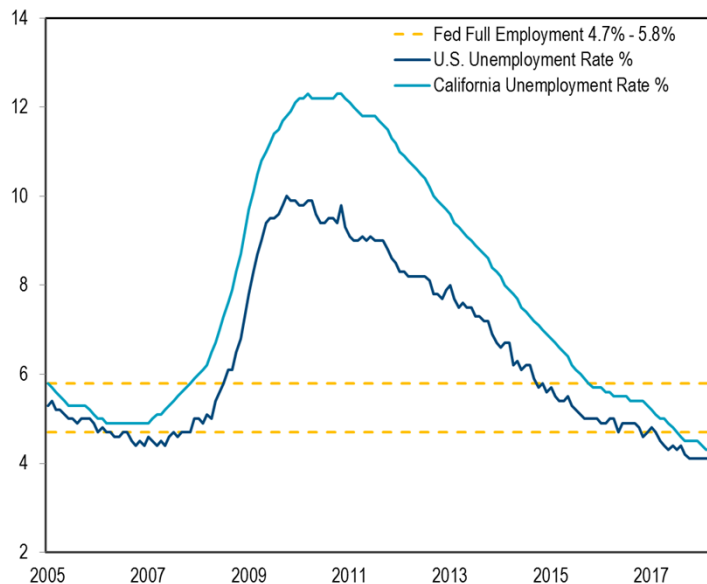
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Unemployment at 4.1%; California 4.3%

Unemployment remained at **4.1%** in March for the sixth consecutive month, the lowest since December 2000

The unemployment rate has been well within the Fed's full employment range since October 2014 and now falling below the Fed's target range since March 2017

California unemployment rate at an all-time low of **4.3%** as of February, further below the 12.3% peak in March 2010



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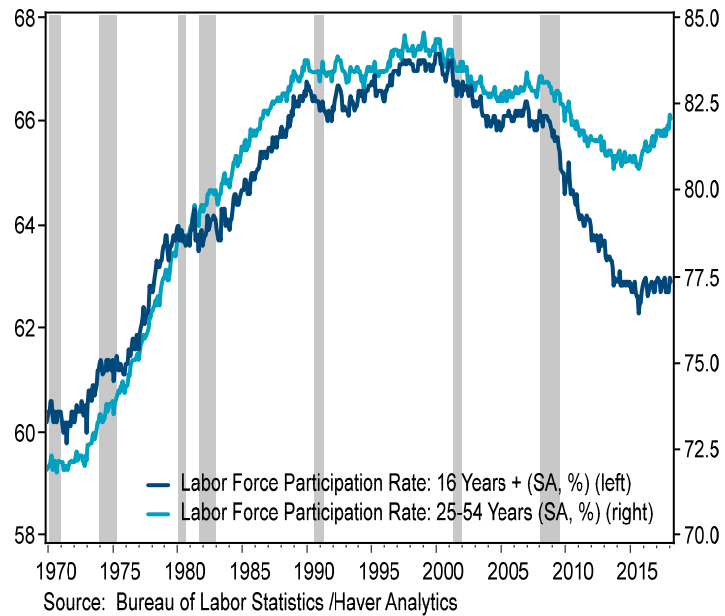
Participation Rate Still Low

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Participation rate at a multi-decade low, **62.9%** in March

The prime-age participation rate while improved from a low of 80.6% in September 2015, remains depressed at **82.1%** in March, a multi-decade low

20-55 year olds account for the majority of the decline in the labor force, **8.0m** Americans (only 59% of working age population)



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Gains in Household Spending Have
"Moderated"

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Retail Sales Lose Momentum

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March sales rose **0.6%**, the largest monthly increase since November

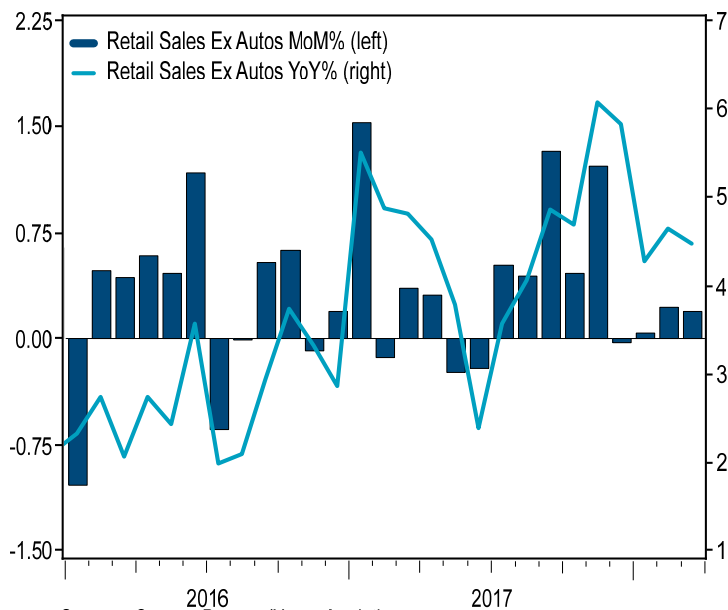
Y/Y sales rose **4.5%** vs. 4.1% in February

Excluding autos, sales rose 0.2% in March and 4.5% Y/Y, down from 4.7% in February

Control group* March sales rose 0.4% Y/Y up **3.8%** in March following a 4.1% increase in February

Six months of flat or negative sales since end of Q1 2017

*Control group excludes auto, building materials, & gas stations sales



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Consumer Credit

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Consumer credit rose by \$10.60 billion in February, a five-month low, and following a \$15.59 billion increase in January

The six-month average fell from \$18.29 billion to \$17.78 billion in February, a three-month low

On an annual basis, total outstanding revolving credit, which primarily reflect credit cards, rose just 0.2% in February, the lowest monthly reading since November 2013



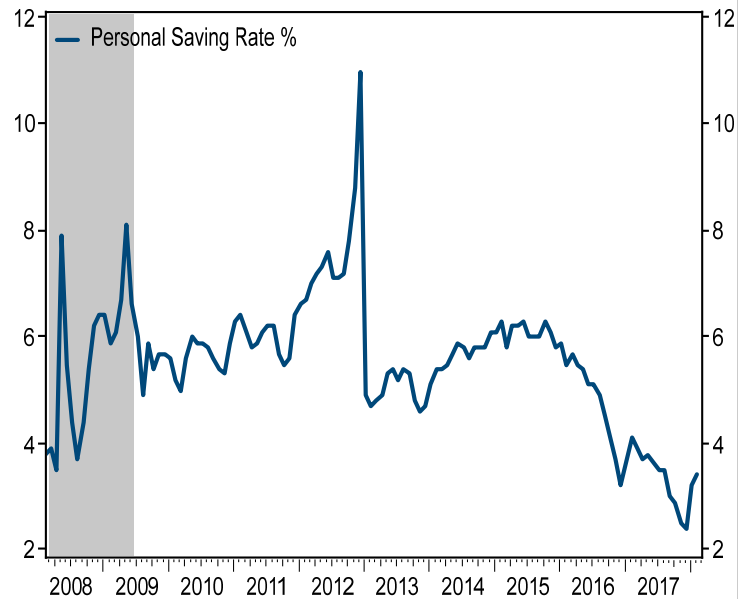
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Savings on the Decline

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The personal savings rate is at **3.4%** as of February, up from 3.2% reported in January and a six-month high

The savings rate averaged 6.0% 2009-2015 and 4.1% thereafter



Source: Bureau of Economic Analysis /Haver Analytics

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Gas Prices Give Muted Boost

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March price of **\$2.59** near 2009 low

\$2.56 six-month average vs. **\$2.76** long-term average

Down **\$1.10** and **30%** from a peak monthly average of \$3.69 in June 2014 (star)

Gas prices are up **13%** from **\$2.30** a year ago and 44% from 2016 low

According to the Energy Information Administration, average retail gas prices reached \$2.70 a gallon in the first week of April, the highest since 2015



Source: Haver Analytics

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Avg. Hourly Earnings Edging Higher

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Wages rose 0.3% in March, following a 0.1% rise in February

Up 2.7% Y/Y as of March, a two-month high

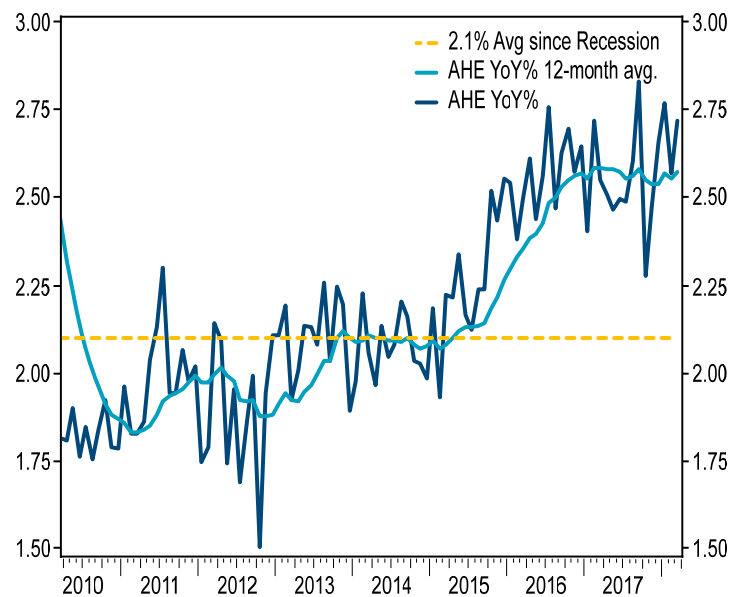
2.7% 12-month average in March

2.7% 3-month average in March

Wages in California rose 0.2% in February and 2.6% over the past 12 months, down from a recent peak of 4.9% in July 2017

"Regarding wage growth at the national level, several participants noted a modest increase, but most still described the pace of wage gains as moderate."

-March 21st FOMC Meeting Minutes



Source: Bureau of Labor Statistics /Haver Analytics

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Trump Tax Bump

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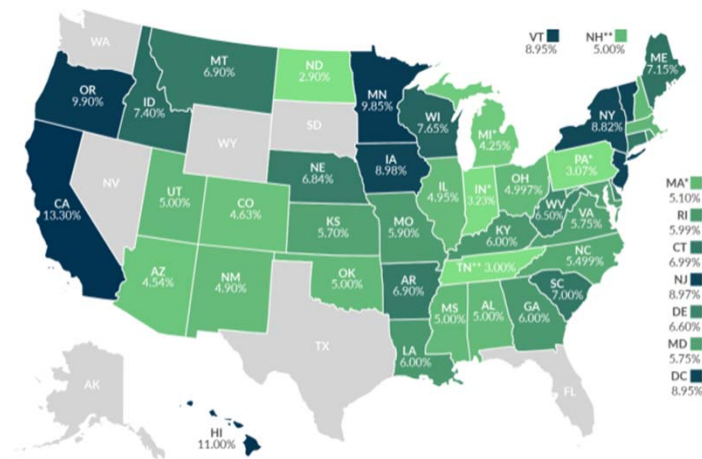
Americans' after-tax income is on the rise, thanks to the administration's Tax Cuts and Jobs Act, but for many, the increase made little difference

According to a Bankrate poll, nearly 75% of Americans say they didn't notice a change in their take-home after-tax pay post tax reform

Furthermore, while the Trump tax cut helped alleviate the federal burden, for many individuals and households, taxes were already on the rise as state and local governments grapple to finance rising deficits

How High Are Income Tax Rates in Your State?

Top State Marginal Individual Income Tax Rates, 2018



Note: (*) State has a flat income tax. (**) State only taxes interest and dividends income. Map shows top marginal rates: the maximum statutory rate in each state. This map does not show effective marginal tax rates, which would include the effects of phase-outs of various tax preferences. Local income taxes are not included.

Source: Tax Foundation; state tax statutes, forms, and instructions; Bloomberg BNA.

Top State Marginal Individual Income Tax Rate
Lower Higher

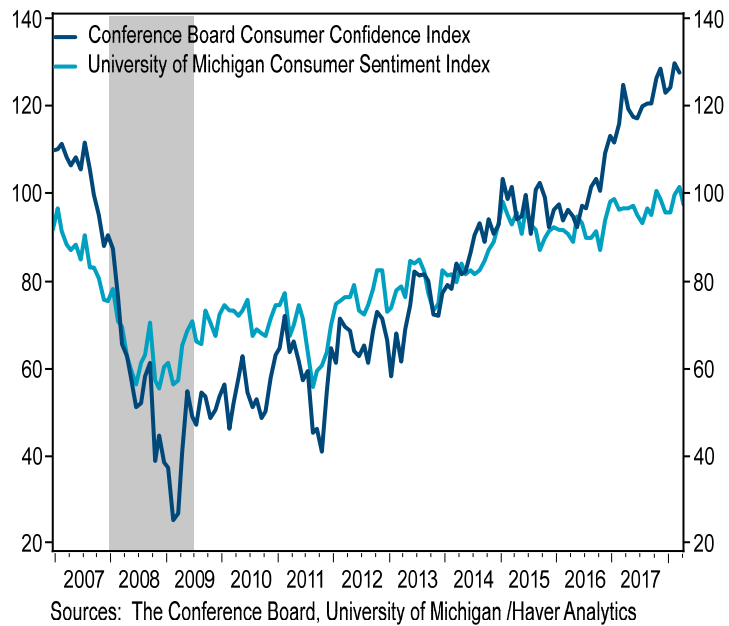
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Consumer Confidence Peaks

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In March, the Conference Board Consumer Confidence Index fell from 130.0, an eighteen-year high, to 127.7, a two-month low

Additionally, the University of Michigan Consumer Sentiment Index declined from 101.4 to 97.8 in the preliminary April report, a three-month low



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**Gains in Business Investment Have
"Moderated"**

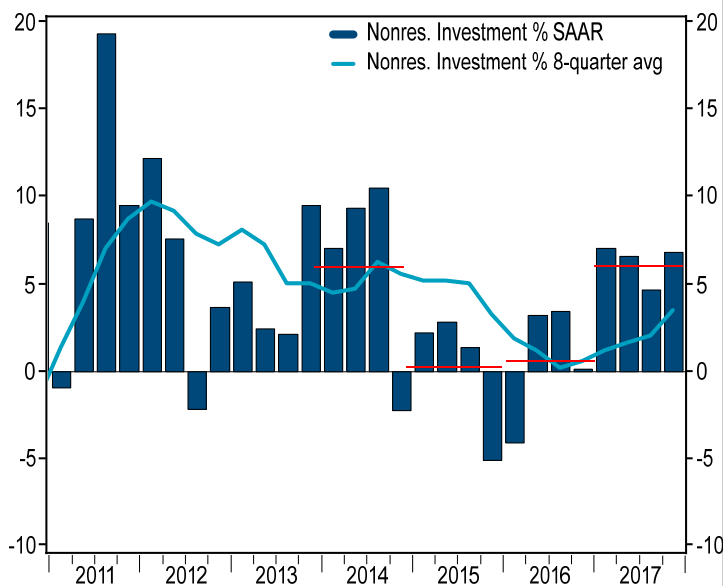
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Modest Business Investment

Nonresidential fixed investment fell 5.1% at the end of 2015, the largest quarterly decline since Q2 2009

Investment rose 6.2% in 2014, 0.4% in 2015, 0.7% in 2016 & 6.3% in 2017

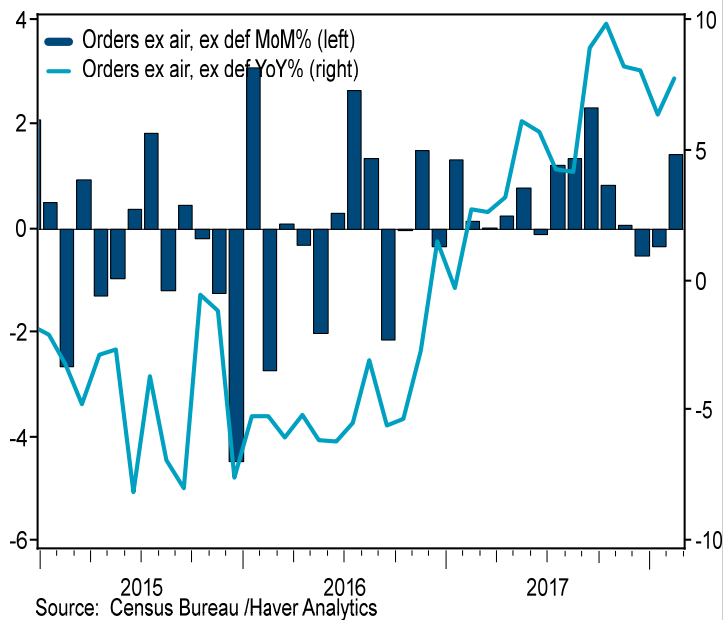
Investment rose **6.8%** in Q4 following a 4.7% rise in Q3 2017, thanks to an 11.6% increase in equipment and a 6.3% increase in structures investment in Q4



Corporate Investment Slows

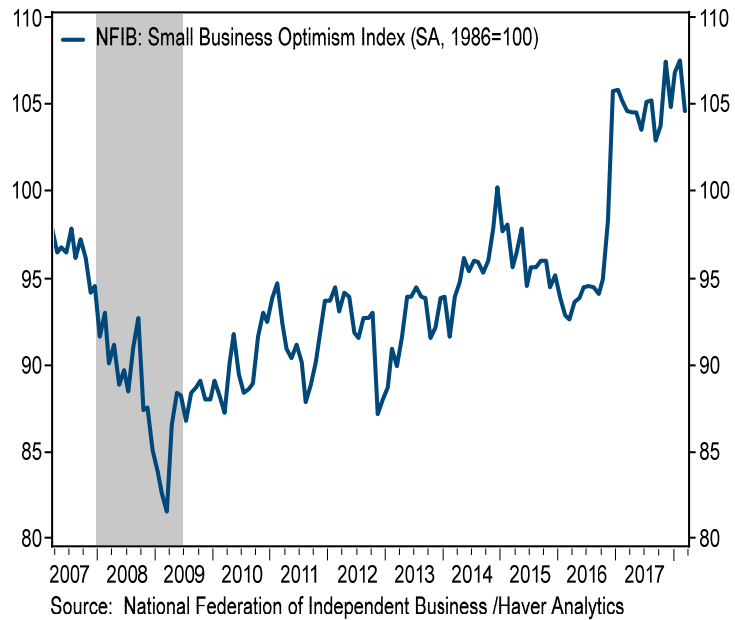
Capital goods excluding aircraft and defense – a proxy for business investment – increased 1.5% in February, a five-month high and following a 0.3% decline the month prior and a 0.5% drop in December

Year-over-year, business investment increased 7.7%, a two-month high, but down from a recent peak of 9.9% in October 2017



Small Business Confidence

The NFIB Small Business Optimism Index fell from 107.6 to **104.7** in March, a five-month low, but still up more than 12 points from a recent low in 2016

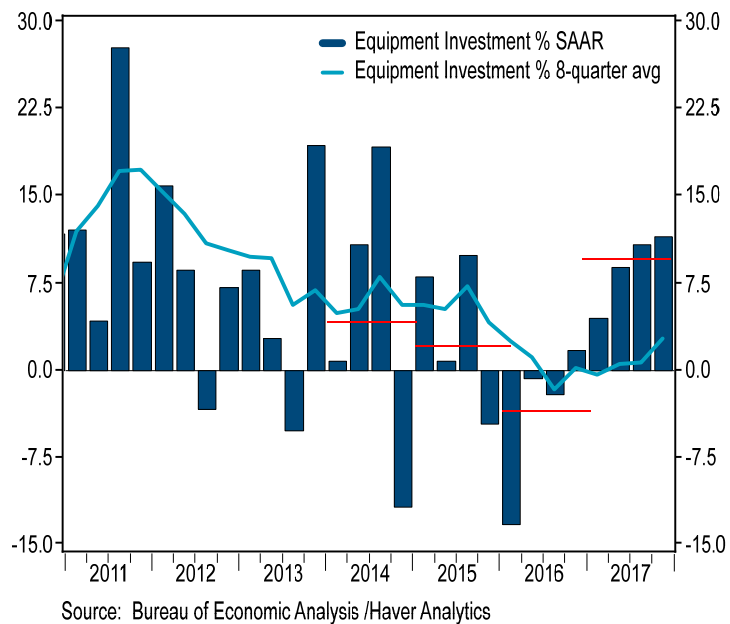


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Positive Equipment Investment

Equipment investment rose 4.8% in 2014, increased 3.6% in 2015, fell 3.5% in 2016 & rose 8.9% in 2017

Equipment investment rose **11.5%** in Q4, the highest since Q3 2014, and following a 10.8% rise in Q3 2017



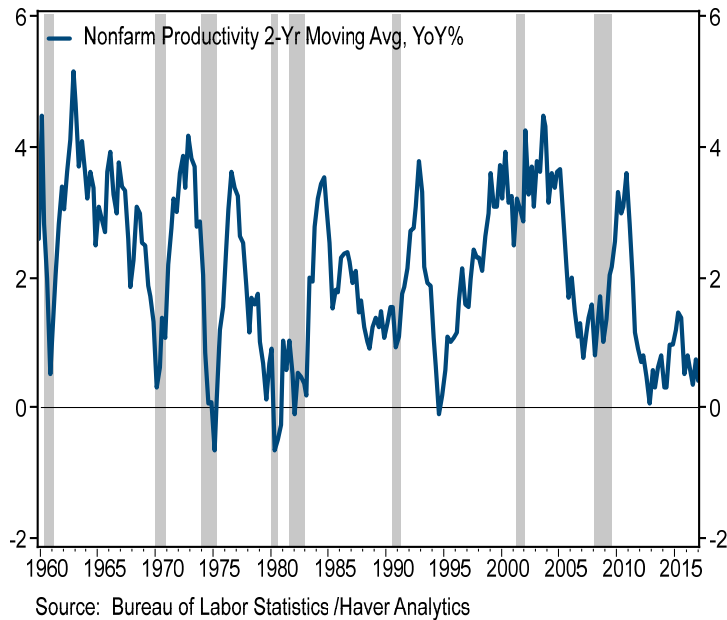
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Productivity Remains Weak

"Participants generally noted few signs of a broad-based pickup in wage growth in available data. With regard to how firms might use part of their tax savings to boost compensation, a few participants suggested that such a boost could be in the form of onetime bonuses or variable pay rather than a permanent increase in wage structures. It was noted that the pace of wage gains might not increase appreciably if productivity growth remains low."

-January 31st FOMC Meeting Minutes

Q4 productivity was **1.0%**, averaging **0.6%** in 2017 and **0.7%** over the past 5 years



Inflation Has Continued to "Run Below 2%" Target

"Inflation on a 12-month basis is expected to move up in coming months and to stabilize around the Committee's 2 percent objective over the medium term."

-March 21st FOMC Statement

Inflation Momentum: PPI & CPI

The PPI rose 0.3% in March, following a 0.2% rise the month prior

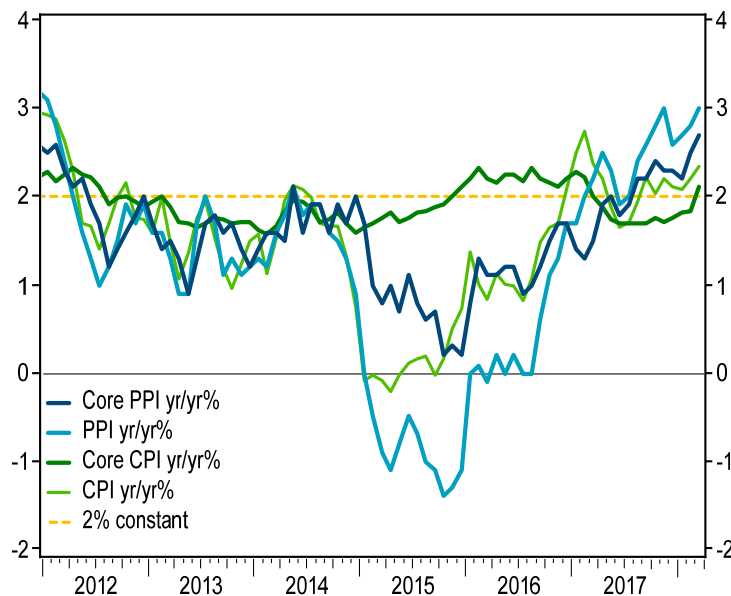
Year-over-year, headline producer prices rose 3.0% in March, a four-month high

The core PPI also rose 0.3% in March and increased 2.7% over the past 12 months, the highest since November 2011

The CPI fell 0.1% in March, the first monthly decline in ten months, and following a 0.2% increase the month prior

Year-over-year, headline consumer prices rose 2.4% in March, a one-year high

The core CPI rose 0.2% in March and 2.1% over the past 12 months, a thirteen-month high

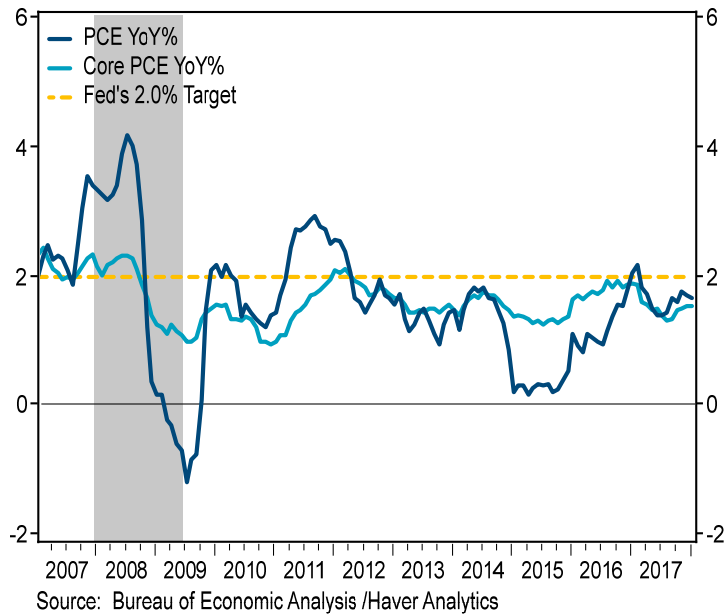


Decline in Inflation Momentum: PCE

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The PCE rose **0.4%** in January and rose **1.7%** year-over-year for the third consecutive month, below the recent peak of 2.2% in February 2017, the first +2% reading since April 2012

The core PCE rose **0.3%** in January and rose **1.5%** year-over-year for the third consecutive month, down from a peak of 1.8% in January 2017



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"A few participants cautioned that, despite increases in market-based measures of inflation compensation in recent months and the stabilization of some survey measures of inflation expectations, the levels of these indicators remained too low to be consistent with the Committee's 2 percent inflation objective."

"Downside risks included the possibilities that longer-term inflation expectations may have edged lower or that the run of low core inflation readings last year could prove to be more persistent than the staff expected."

—March 21st FOMC Meeting Minutes

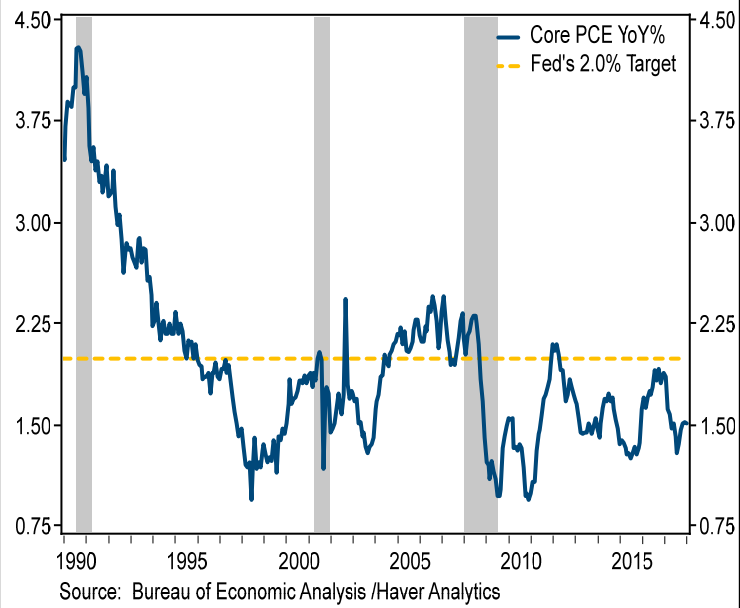
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Core Inflation Low for Decades

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The core PCE rose 1.6% in February, an eleven-month high

Inflation has been under 2% for 21 of 25 years



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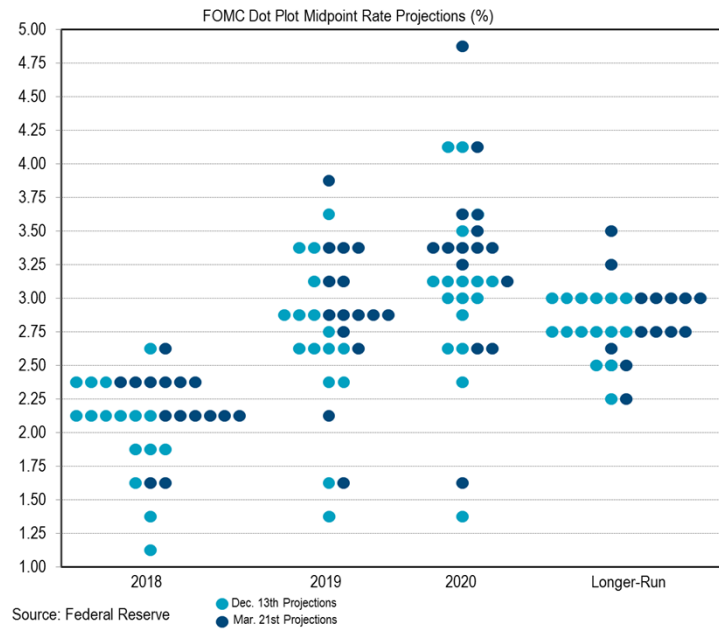
Forward Guidance

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Fed Dot Plot Shows Three Hikes in 2018

The Fed continues to forecast three (two additional hikes after March 21st move) in 2018

Median Consensus:
2018: 2.1%
2019: 2.9%
2020: 3.4%
Longer-Run: 2.9%



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"We've made one decision at this meeting and that decision was to raise the Federal funds rate by 25 basis points."

—Chairman Jerome Powell, March 21st Press Conference

"All participants saw some further firming of the stance of monetary policy as likely to be warranted...Participants expressed a range of views on the amount of policy tightening that would likely be required over the medium term to achieve the Committee's goals."

—March 21st FOMC Meeting Minutes

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The Fed Continues to Expect a “Gradual” Rise in Rates

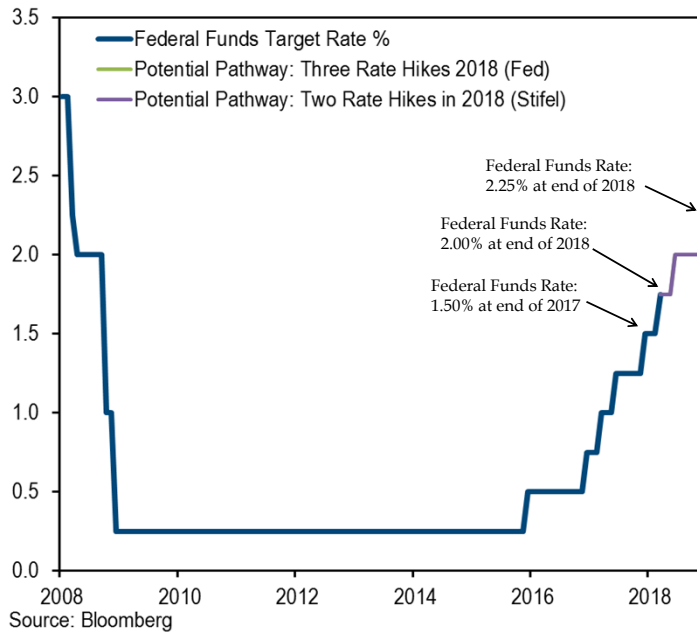
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Buoyed by the expectation of firmer growth and prices to come, the majority of Fed officials anticipate three additional rate hikes in 2018, the same number reported in the December SEP

Fed may be “overselling” future hikes

In December 2014, the Fed’s median consensus for rate hikes in 2015 was 4 and we had 1 and in 2016 it was 4 and we had 1

Finally, in 2017 the Fed forecasted 3 hikes and we had 3 hikes



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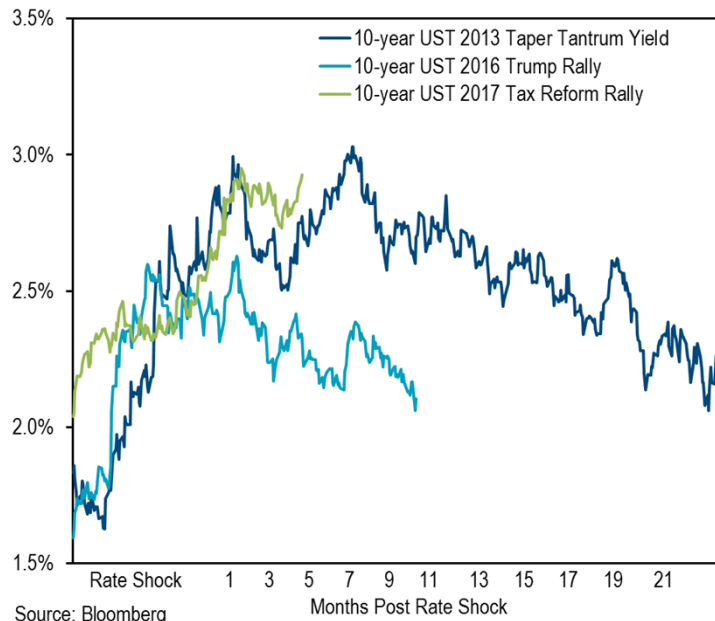
Market Optimism

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During the Taper Tantrum of 2013 yields rose more than 100bps January to December before recapturing 79bps 35 months later

10-yr yield rose 80bps from November 1, 2016 to 2.63% on March 13, 2017, the highest since July 2014

10-yr rose 91bps from September 7, 2017 to 2.95% on February 21st, the highest since January 2014



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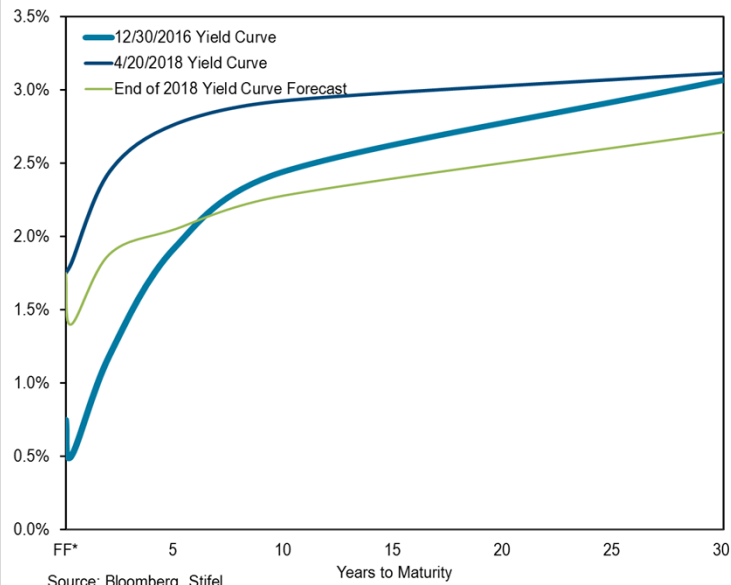
Yield Curve To Flatten Further

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2s10s spread of **124bps** prior to liftoff and down to **42bps** following the March 2018 FOMC meeting

With the 2-year up 125bps since the start of 2017 and the 10-year up 48bps, the spread of 48bps is near an eleven-year low

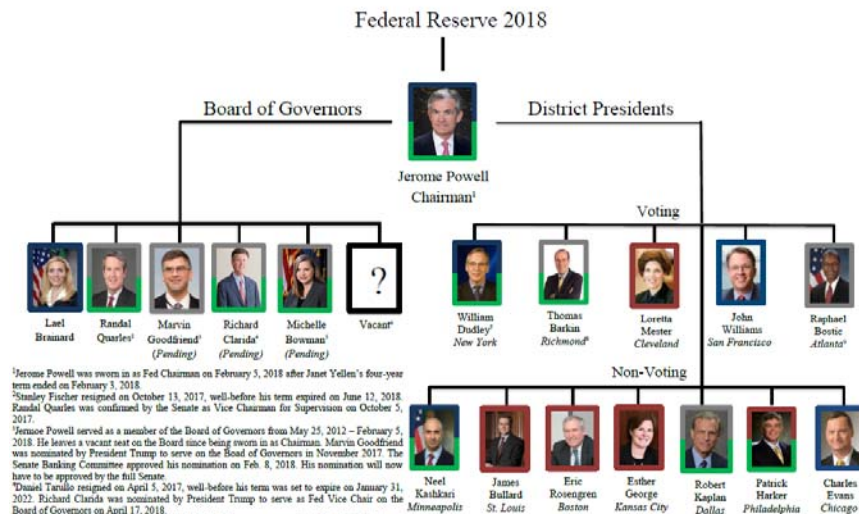
Projected to flatten to **40bps** by end of 2018



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Composition of the Fed

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¹Jerome Powell was sworn in as Fed Chairman on February 5, 2018 after Janet Yellen's four-year term ended on February 3, 2018.
²Randal Quarles resigned on October 13, 2017, well before his term expired on June 12, 2018. Randal Quarles was confirmed by the Senate as Vice Chairman for Supervision on October 5, 2017.
³Jerome Powell served as a member of the Board of Governors from May 25, 2012 – February 5, 2018. He leaves a vacant seat on the Board since being sworn in as Chairman. Marvin Goodfriend was nominated by President Trump to serve on the Board of Governors in November 2017. The Senate Banking Committee approved his nomination on Feb. 8, 2018. His nomination will now have to be approved by the full Senate.
⁴Daniel Tarullo resigned on April 5, 2017, well before his term was set to expire on January 31, 2022. Richard Clarida was nominated by President Trump to serve as Fed Vice Chair on the Board of Governors on April 17, 2018.
⁵Jeremy Stein resigned on May 28, 2014. Michelle Bowman was nominated by President Trump to serve on the Board of Governors on April 17, 2018.
⁶Sarah Bloom Raskin resigned on March 13, 2014.
⁷William Dudley will retire in mid-2018, about six months prior to the expiration of his term on January 2019. The New York Fed named San Francisco Fed President John Williams as its next president on April 3, 2018.
⁸Thomas Barkin began serving as the new Richmond Fed President on January 1, 2018 after Jeffrey Lacker resigned on April 4, 2017.
⁹Raphael Bostic took office on June 5, 2017 after Dennis Lockhart resigned on February 28, 2017.

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Wild Cards

"... a strong majority of participants viewed the prospect of retaliatory trade actions by other countries, as well as other issues and uncertainties associated with trade policies, as downside risks for the U.S. economy."

"A number of participants also suggested that uncertainty about whether all elements of the tax cuts would be made permanent, or about the implications of higher budget deficits for fiscal sustainability and real interest rates, represented sources of downside risk to the economic outlook."

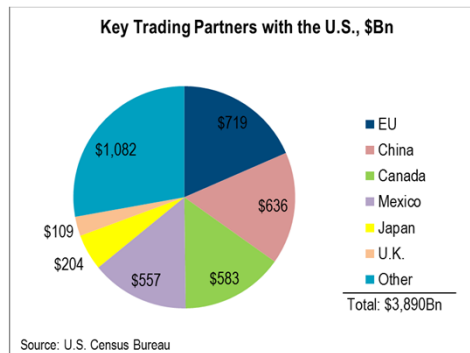
–March 21st FOMC Meeting Minutes

- “Fair” and “reciprocal” trading relationships, renegotiate trade deals that have left the U.S. disadvantaged; “America First” and protectionist policies defending American workers and their interests.
 - Tariffs on solar panels from China and washing machines from South Korea, totaling 30% and 20%, respectively
 - Tariffs on steel and aluminum, totaling 25% and 10%, respectively
 - Second-round retaliatory tariffs of 25% proposed on more than 1,300 types of Chinese goods totaling \$50Bn following China’s 25% tariff on 128 U.S.-made goods
 - \$100Bn in additional tariffs on China considered following China’s announcement of additional 25% tariff on 106 U.S.-made goods
 - China imposes temporary anti-dumping duties of 178.6% on U.S. sorghum imports (U.S. exports of sorghum to China amount to nearly \$1 billion a year)
- Renegotiate NAFTA, now in its seventh round.
- Reconsidering membership in the TPP. Partnering with other Asian countries would put pressure on the Chinese to end unfair trade practices.

Further restrictions on imported goods would expectedly hurt corporate America by reducing access to production materials, limiting accessibility to Chinese consumers and potentially rising costs should producers pass along price increases directly to shoppers

“Participants did not see the steel and aluminum tariffs, by themselves, as likely to have a significant effect on the national economic outlook...”

-March 21st FOMC Meeting Minutes



Top 10 U.S. Imports from China			Top 10 U.S. Exports to China		
	Total Value 2017, \$Thous	% of Total		Total Value 2017, \$Thous	% of Total
1. Cell phones and other household goods, n.e.c.	70,394,367	13.9%	1. Civilian aircraft, engines, equipment, and parts	16,265,504	12.5%
2. Computers	45,520,475	9.0%	2. Soybeans	12,362,119	9.5%
3. Telecommunications equipment	33,481,948	6.6%	3. Passenger cars, new and used	10,525,593	8.1%
4. Computer accessories	31,611,573	6.3%	4. Semiconductors	6,076,819	4.7%
5. Toys, games, and sporting goods	26,773,048	5.3%	5. Industrial machines, other	5,441,908	4.2%
6. Apparel, textiles, nonwood or cotton	24,152,367	4.8%	6. Crude oil	4,434,408	3.4%
7. Furniture, household goods, etc.	20,667,323	4.1%	7. Plastic materials	4,004,303	3.1%
8. Other parts and accessories of vehicles	14,418,233	2.9%	8. Medicinal equipment	3,454,276	2.6%
9. Household appliances	14,146,304	2.8%	9. Pulpwood and woodpulp	3,394,968	2.6%
10. Electric apparatus	14,072,700	2.8%	10. Logs and lumber	3,179,211	2.4%
TOTAL IMPORTS FROM CHINA TO U.S.	505,597,065		TOTAL U.S. EXPORTS TO CHINA	130,369,530	

Source: U.S. Census Bureau *Data classified by 5-digit End-Use Code

Trump's Key Agenda Points

- A four pillar framework for immigration including a path to citizenship for Dreamers, building a “wall,” ending the visa lottery program and moving towards a merit-based immigration system.
- Repeal & reform the Affordable Care Act. (Graham-Cassidy).
- Infrastructure spending bill proposes \$200 billion in federal spending and \$1.3 trillion at the state and local level, totaling \$1.5 trillion to build roads, bridges, schools and airports “second to none.”
- Tax Cuts and Jobs Act

Tax Cuts and Jobs Act

	Prior to 2017 Reform	2017 Reform
Top Individual Tax Rate	39.6%	37%
Individual Tax Brackets	Seven (10%, 15%, 25%, 28%, 33%, 35% & 39.6%)	Seven (10%, 12%, 22%, 24%, 32%, 35% & 37%)
Child Tax Credit	\$1,000; 15% of earnings over \$3,000 are refundable	\$2,000; up to \$1,400 refundable
Personal Exemption	\$4,150 per taxpayer and dependent	Eliminates
Estate Tax	Top rate of 40% on estates above \$5.6 million	Increases threshold to estates above \$11.2 million
State & Local Tax Deduction	Income or sales and property taxes are deductible	All state and local tax deductions limited to \$10,000
Medical Expense Deduction	Can deduct out-of-pocket expenses in excess of 10% of adjusted gross income	Reduce the threshold to 7.5% of adjusted gross income for the tax years 2017 and 2018.
Student Loan Interest Rate Deduct.	Can deduct up to \$2,500	No change
Standard Deduction	\$6,500 / \$13,000 (singles/couples)	Nearly Doubles – \$12,000 / \$24,000 (singles/couples)
Mortgage Interest Rate Deduction	Can deduct interest payments on up to \$1 million of debt	Limited to payments on \$750,000 of debt
Charitable Donation Deductions	Able to deduct charitable contributions that are made to qualifying organizations	No change
Obamacare Individual Mandate	Penalty for not having health insurance	Repeals penalties starting in 2019
Alternative Minimum Tax	Alternative income tax calculation for businesses	Ends the AMT for corporations but keeps it for individuals, while boosting the exemption to \$500,000 for single taxpayers and \$1 million for couples
Corporate Rate	35%	21% in 2018
Top pass-through rate	Taxed at individual rates	20%, phasing out starting at \$315,000 of income for couples
New investment purchases	Complex rules for deducting over many years	Five years of full expensing, then phased out over five more years
Repatriation	The U.S. taxes multinationals on their global earnings at the corporate rate of 35%, but allows them to defer taxes on those foreign earnings until they bring them back to the U.S., or “repatriate” them	U.S. companies' overseas income held as cash would be subject to a 15.5% rate, while non-cash holdings would face an 8% rate; companies can make the payments in eight annual installments.

Trump Tax Cuts

- Tax relief for middle-class families as well as for businesses, especially small businesses. The simplicity of “postcard” tax filing and ending incentives to ship jobs, capital and tax revenue overseas. Broadening the tax base and providing greater “fairness” for all Americans by closing special interest tax breaks and loopholes.
- “Our expectation should be that we will continue to increase our dividend and our share buybacks next year and the year after that and the year after that.”
-Wells Fargo CEO Tim Sloan, December 18, 2017 CNN Money interview
- According to the Tax Foundation, the GOP tax plan **would increase the deficit by \$1.47 trillion over the next ten years.**
- The latest 2018 budget adds nearly \$300 billion in additional discretionary spending with increases in military and infrastructure.

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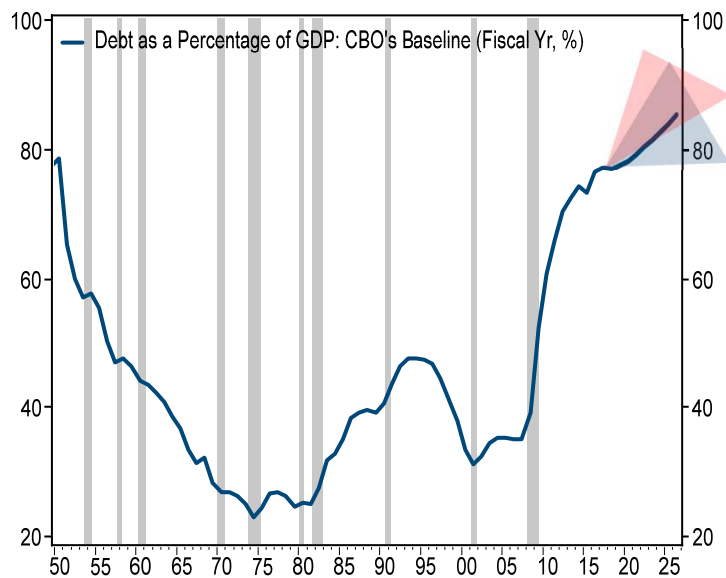
Debt Appetite Diminished

77% of GDP, the highest level relative to the size of the economy since 1950

1950s decade-long expansion posting over 4.5% GDP vs. stagnant 2%

According to the CBO, financing the debt coupled with rising interest rates would result in a four-fold increase

Federal interest outlays totaled more than **\$330b**



Source: Congressional Budget Office /Haver Analytics

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Positive Market Reaction: Equities Rally on Optimism

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After an initial fallout on election day, equities have since rebounded, pushing the Dow to a record high as of January 26th

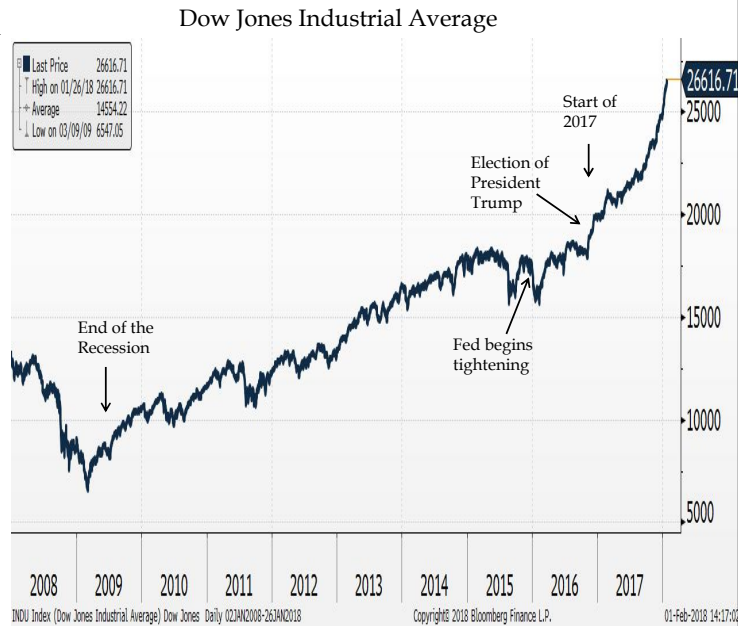
The Dow broke through 23,000 on an intraday basis for the first time on October 17th and closed above 23,000 on October 18th

The Dow closed above 25,000 for the first time on January 4th

The Dow closed down 1,175.21 pts (4.6%) on February 5th, marking the largest one-day point decline on record and following a 665.75 pt drop the prior trading day (Feb 2nd)

Equities had a wild ride throughout the first quarter, breaking a ten-month winning streak with more than 50 days of triple digit swings, 27 of which ended in the red

Since the start of 2017, however, the Dow is up 21% and up 31% since election day



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**Continued Moderation, Subdued Inflation,
and a Flatter Curve**

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Questions?

Disclosures

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