Market Update

February 12, 2018

Equity Update: The Return of Volatility

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Oh what a difference a month makes! February has ushered in the return of volatility to a market that had all but forgotten what it felt like. Since the start of the month, we have seen the Volatility Index (the "VIX") spike from its January (and all of 2017) average of the low teens all the way to 50, now presently sitting at 29. In addition, over the last month the 10 Year Treasury Yield has moved from 2.55% to 2.83%. The S&P has declined 8.8%. All this action and we are only 7 trading days into the month! So what is going on?

This market pullback reminds us of the "Taper Tantrum" of May/June 2013. Recall that 2013 was a time of recovery in the US and Europe. The US economy was still mending after the great recession of 2008/09, and Europe was recovering from fears of the breakup of the European Union that took hold through 2011. GDP growth was at hand and we were slowly creating more jobs and getting back to work. The macro backdrop was positive. Then in May of 2013, the Fed announced its intention to "taper" the bond purchases that were part of its quantitative easing program, and out of the blue the VIX spiked, the 10 Year jumped and the S&P pulled back. Much hand wringing was done during those few weeks of market uncertainty, but in the end, macro fundamentals won out and the market marched higher, finishing the year 16% above the lows of the tantrum.

While there are of course differences between then and now – we are later in the economic cycle, for one – the similarities are what catch our attention. Then as now, global growth is at hand, companies are indicating mostly positive fundamentals and the macro picture is intact. Additionally, there is confusion about the Federal Reserve's intentions – then, it was a new taper program; this time, it is a new leader who the market doesn't yet know very well, Jerome Powell. The move in yields may be reflecting fears that the Fed will get it wrong….or, it may be reflective of a stronger growth environment.

What is more unique to 2018 is the concern that inflation has returned after so many years of deflation. Last week's jobs report showed rising wages which may have triggered this fear in a full employment scenario. We believe inflation is worth worrying about through the medium/long term, but we don't think it will run away at the very first sign of wage growth. There are still a lot of deflationary forces at work, technology first among them. Even in the face of inflationary fears, the price of oil has pulled back nearly 12% from recent highs. In addition, we can't forget that the rise of quantitative investing is probably a factor exacerbating this correction, since triggered selling is part of the 'algorithm' for some trading strategies.

Our best sense is to keep the faith and remain committed to the companies that we know well, and whose fundamentals are well positioned. We know that markets go up and down, and that remaining focused on the fundamentals is a winning long term formula. It is a benefit that this pullback is happening during earnings season when we have a chance to hear from management teams themselves about the state of things. In most cases, the news couldn't be more positive. We are excited at the ability to buy high quality companies at entry prices that meet our hurdle rate, a silver lining to the market volatility, and a necessary one for long term outperformance. Please feel free to reach out with specific concerns or questions.

Chilton Trust

Fixed Income Update: Interest Rate Risk in Focus as Equity Market Swoons

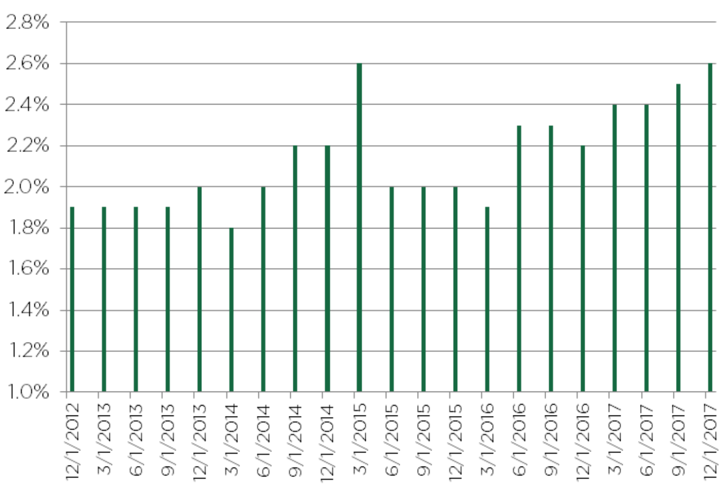
TIMOTHY W. A. HORAN

Executive Vice President & Chief Investment Officer - Fixed Income

As the stock market officially enters a "correction" (S&P 500 is down 11% since January 26), several long-nascent bond market concerns have begun to manifest, albeit to a degree that is currently moderate and manageable.

1. Inflation concerns surface with the most recent indication being a 2.6% increase in the Employment Cost Index, continuing a steady, multi-year increase (Chart 1). However, broad-based pricing trends remain well-contained. For example, core Personal Consumption Expenditures registered just a 1.5% increase in the 4th quarter of 2017.

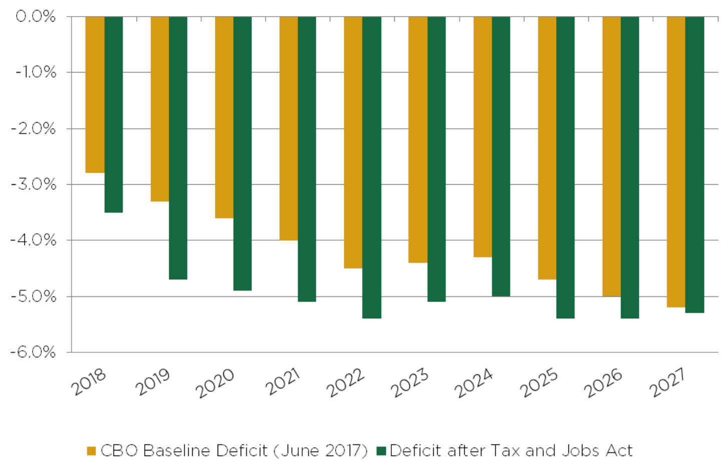
Chart 1: Employment Cost (% Change YoY)



Source: Bureau of Labor Statistics Employment Cost Civilian Workers YoY NSA

2. Federal fiscal deficit is expanding significantly, due in part to passage of the Tax Cuts & Jobs Act. The Congressional Budget Office projects the US budget deficit will increase by $1.5 trillion over the next 10 years, rising to an estimated -5.3% of GDP in 2027 versus -3.4% currently (Chart 2).

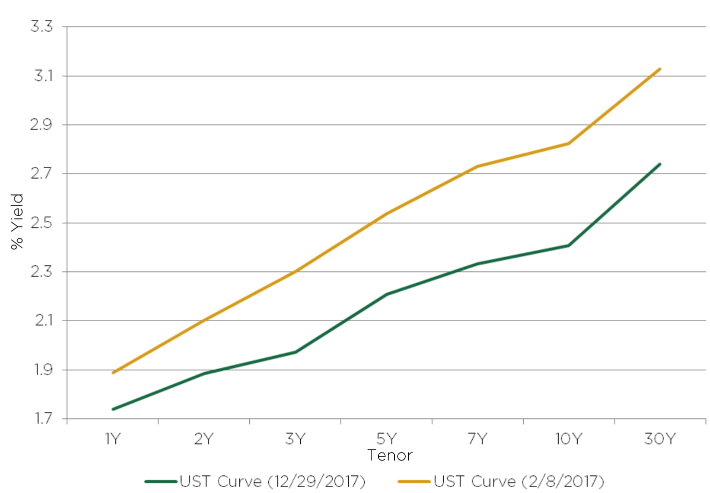
Chart 2: Federal Budget Deficit (% GDP)



Source: Congressional Budget Office

3. Fixed income yield curves have steepened year-to-date (Chart 3) with the 10 Year US Treasury note rising over 40 basis points (to current 2.83% yield) and the 30 Year bond up 34 basis points (3.15% yield). Meanwhile the 2 Year Treasury has increased just 22 basis points (2.09%), indicating a relative shift in market concern toward longer term issues like inflation and deficits versus short-term dynamics related to the Federal Reserve's interest rate tightening cycle. The same steepening dynamic has been witnessed in the municipal bond market as well.

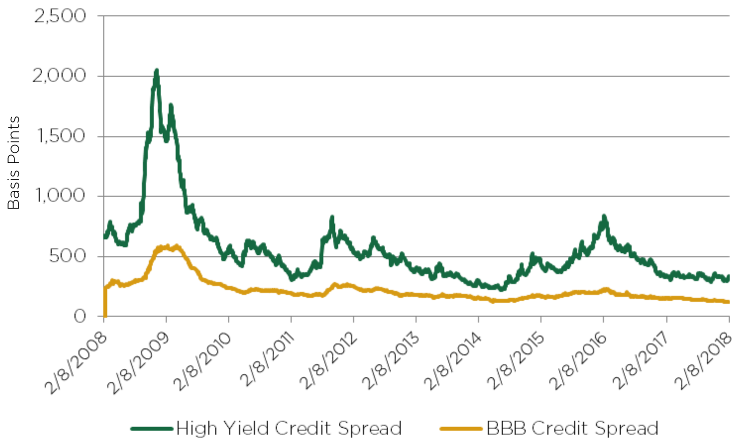
Chart 3: US Treasury Curves Steepening



Source: Bloomberg LP

4. Credit conditions however, remain sound. Credit spreads have widened modestly in the past week, in sympathy with the equity market sell-off. However, corporate credit fundamentals remain solid. Global economic activity remains strong with the JP Morgan Global Manufacturing PMI Index at close to a 7-year high. Even with the recent spread widening, investment grade and high yield credit spreads remain very tight on a multi-year basis (Chart 4) and market conditions remain healthy.

Chart 4: Credit Markets Remain Sound



Source: Bloomberg Intelligence

Conclusion

In short, we expect market volatility to pick up in the near term but we do not believe we are entering a more disruptive market cycle. Interest rate risk is increasingly in-focus, an expectation long anticipated by the market as the economy strengthened and the Federal Reserve normalized monetary policy. Thus far, it appears to represent a healthy repricing with interest rates remaining historically low and relative value for US taxable bond markets possibly enhanced in relation to lower-yielding bond markets in Europe and Japan. The municipal bond market faces a temporary weakness in demand as the tax reform bill reduced the incentive for banks and property & casualty insurance companies to hold municipal bonds. Both have been reducing municipal bond holdings year-to-date.

External Manager Update

LOUISA IVES

Managing Director & Head of Manager Research

During this drawdown and period of increased volatility, our external manager group has been in close contact with the managers with whom we partner. We derive great comfort in their experienced, calm approach to this recent market activity. Our external managers are actively focused on quality companies, and proactively positioning portfolios to take advantage of appropriate buying opportunities. Should you have any questions or concerns about a specific manager or our external managers in general, please don't hesitate to reach out.

Richard L. Chilton, Jr. is the founder, Chairman and Chief Investment Officer of Chilton Trust Company, which in April 2012 was the first company in eight years to be awarded a trust charter in Florida. Mr. Chilton also serves as the Chairman, CEO and Chief Investment Officer – Equities of Chilton Investment Services and is the founder, Chairman, CEO and Chief Investment Officer of Chilton Investment Company.

Since founding Chilton Investment Company in 1992, Mr. Chilton has built a team of investment professionals focused on building wealth in favorable markets and preserving capital in declining markets. Under Mr. Chilton's leadership, Chilton Investment Company has developed an investment approach committed to fundamental, bottom-up stock selection and disciplined portfolio management.

Prior to forming Chilton Investment Company, Mr. Chilton was a managing director of Allen Value Incorporated and a vice president and equity portfolio manager at Alliance Capital Management Corporation. Mr. Chilton began his career in the Mergers and Acquisitions group at Merrill Lynch and Company.

Mr. Chilton is a trustee of The Metropolitan Museum of Art and a trustee of the Classic American Homes Preservation Trust, both located in New York.

Mr. Chilton received his B.S. in Finance and Economics from Alfred University.

Jennifer L. Foster is an Executive Vice President, Co-Chief Investment Officer & Portfolio Manager– Equities with over 18 years of experience. Prior to taking on her role as Portfolio Manager in September 2012, Ms. Foster served as Chilton Investment Company's Director of Research for seven years. She also serves on the Chilton Investment Company Risk Management Committee, Board of Directors, and Executive Board. Preceding her tenure as Director of Research, Ms. Foster served for seven years as an equity analyst at Chilton covering the Software and Technology sectors.

Before joining Chilton, Ms. Foster worked at GE Capital as a financial analyst in several divisions of the company including commercial finance, commercial real estate, equipment leasing and corporate planning. Ms. Foster graduated summa cum laude with a B.A. in English from Boston College and earned an M.B.A. with distinction from Harvard Business School. She is a current trustee of St. Luke's School and the Calvin Coolidge Presidential Foundation.

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Timothy W.A. Horan is an Executive Vice President & Chief Investment Officer – Fixed Income. With over 30 years of experience, Mr. Horan is a specialist in fixed income investing, ranging from municipal and US taxable securities to international bonds and currencies. He leads a team of nine professionals managing client assets across a variety of strategies including intermediate liquidity, tax-advantaged, taxable, international and global.

Prior to joining Chilton Trust, Mr. Horan was a Managing Director at Morgan Stanley Smith Barney and served as MSSB's Chief Investment Officer of Fixed Income Investment Advisers, a division of MSSB, providing customized portfolio management to ultra-high net worth private clients, charities, endowments, foundations, and family offices, primarily in North America, the Caribbean and Latin America. Earlier, Mr. Horan led Morgan Stanley's Private Wealth Management Fixed Income business in London serving European, Middle Eastern and Swiss private bank clients. Mr. Horan also served on the Morgan Stanley Global Asset Allocation Committee. Before joining Morgan Stanley, Mr. Horan was Director of International Fixed Income at Lord Abbett & Co. He also held senior management positions in fixed income and foreign exchange portfolio management at Credit Suisse, Aubrey G. Lanston & Company, Inc. and Bankers Trust. At Bankers Trust, he helped pioneer the fixed income risk management frameworks. Mr. Horan began his career at the Federal Reserve. During the Volcker years, he was an Economist in the Sovereign Debt Unit at the New York Fed, working on the debt restructuring of Brazil, Mexico and Argentina. Following the Plaza Accord, he also served as a foreign exchange trader for the Federal Reserve Bank of New York. Mr. Horan earned an AB with honors in Economics and History from the University of Pennsylvania, Wharton-Sloan Program. He was an Andrew Mutch Scholar in Economics and Politics at the University of Edinburgh and holds a post graduate law degree from the University of Cambridge, where he was a Thouron Scholar.

Louisa Ives is a Managing Director, Head of Manager Research. Ms. Ives is responsible for external manager selection and due diligence for Chilton clients. Prior to joining Chilton Trust, Ms. Ives was a Managing Director at Chilton Investment Company, where she was a research analyst covering the financial services sector. She also served on the company's Board of Directors. Prior to joining Chilton, she worked as a Senior Associate at Coopers & Lybrand Consulting Group, reporting directly to the CEO, and as an Assistant Vice President at Chemical Bank in their Middle Market Lending Group. Ms. Ives graduated cum laude from St. Lawrence University with a B.A. in English Literature and earned an M.B.A from Harvard Business School. Ms. Ives serves on the boards of the North Haven, ME Casino (Yacht Club), The Project Y Theatre Company, and on the Investment Committee of Vinalhaven, ME Land Trust.

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