

## CONCERN Over Inflation

Inflation swelled briefly in October, but appears to be slowing on a year-over-year basis. Many investors and analysts are keeping a close eye on inflation in light of recent interest rate activity by the Federal Reserve (Fed).

Current market-based forecasts suggest the Fed appears likely to increase the Fed Funds rate target at its meeting on December 18-19. Here's why it matters to your fixed income portfolio:

- Inflation is the primary driver of interest rate increases. The Fed increases rates to keep inflation in check. Higher expected inflation tends to lead to more interest rate increases.
- Interest rates and the prices on existing bonds are inversely related. Thus, as interest rates increase, the prices on existing bonds decrease.
- Generally speaking, as inflation expectations increase so do bond yields, particularly on the longer end of the curve, as bond investors will demand higher return to compensate for inflation risk.

When you add interest rate increases, volatility in oil prices and uncertainty over trade in China, these factors have resulted in a reduction of inflation expectations.

## THE BIG MOVE In Interest Rates

James Camp, CFA, Managing Director of Fixed Income at Eagle Asset Management, believes there is little risk of inflation coming unhinged.

"It's important that clients understand when they worry about interest rates that 'the worst' has already happened," Camp opined during a recent webinar. "Since 2016, we have seen a significant move for interest rates (see Figure 1). Many global sovereign debt yields were negative that year. We believe that would have been the time to panic. From a monetary policy standpoint, things seem to be more normalized now."

**FIGURE 1** The Big Move In Interest Rates Has Occurred  
Rising rates over 2 years lead to higher bond yields

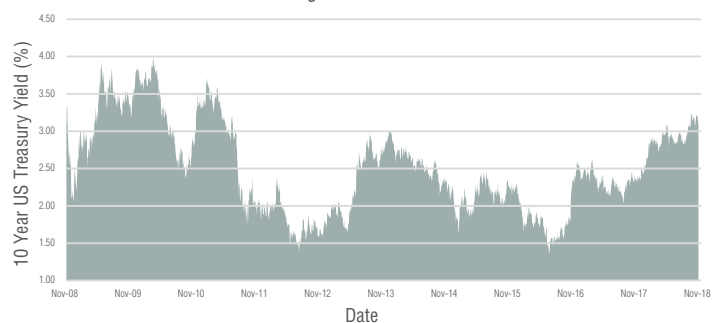


Well-anchored inflation appears to be reflected in the actions of central banks. The Fed has stopped its quantitative easing program and embarked on quantitative tightening – the raising of interest rates. Some analysts are concerned that other world banks tightening at the same time could cause a global quantitative tightening cycle, possibly weakening the economy. However, global inflation is low and the likelihood of world banks putting the brakes on monetary accommodation is also low.

A primary concern for Mr. Camp is that the Fed might be overly aggressive in raising interest rates several more times in 2019; however, the possibility of falling inflation suggests to Mr. Camp that the Fed lacks economic or market justification for aggressive hikes in the next year. Market odds are for one to two rate increases in 2019<sup>1</sup>, but Mr. Camp is wary of a Fed policy error.

## ATTRACTIVE Bond Yields

**FIGURE 2** Yields At Highest Level In Seven Years



For the time being, the Eagle Asset Management fixed income team is seeing a lessening of inflation expectations. The interest rate environment appears benign for the time being and bond yields are at their highest in seven years (see Figure 2), with future income prospects at historically attractive levels.

All investments are subject to risk and you may incur a profit or a loss. There is no assurance that any investment strategy will be successful. Asset allocation and diversification does not ensure a profit or protect against a loss. Past performance is not guarantee of future results.

<sup>1</sup> Bloomberg

## About Eagle Asset Management

Eagle Asset Management, an affiliate of Carillon Tower Advisers, provides a broad array of fundamental equity and fixed-income strategies designed to meet the long-term goals of institutional and individual investors. Eagle's multiple independent investment teams have the autonomy to pursue investment decisions guided by their individual philosophies and strategies.

## About Carillon Tower Advisers

Carillon Tower Advisers is a global asset-management company that combines the exceptional insight and agility of individual investment teams with the strength and stability of a full-service firm. Carillon Tower believes providing a lineup of institutional-class portfolio managers – spanning a wide range of disciplines and investing vehicles – is the best way to help investors seek their long-term financial goals.

## Disclosures

The information presented is for illustrative purposes only and should not be used as the sole basis for an investment decision. Past performance does not guarantee future results. This information is intended solely to report on investment strategies as reported by affiliates of Carillon Tower Advisers and estimates offered constitute individual portfolio managers' judgment and are subject to change without notice, as are statements of financial market trends, which are based on current market conditions. Under no circumstances does the information contained within represent a recommendation to buy, hold or sell any security and it should not be assumed that the securities transactions or holdings discussed were or will prove to be profitable. All holdings are subject to change daily.

Investing involves risk, including the possible loss of principal. This information is not intended to serve as investment, tax, legal or accounting advice. It should not be considered a recommendation to engage in or refrain from taking a particular course of action and is not an endorsement, recommendation or sponsorship of any securities, services or other investment property. It has been prepared for informational purposes only and you should consult your own investment, tax, legal and/or accounting advisors before engaging in any transaction. Any discussion of tax matters contained herein is not intended or written to be used, and cannot be used, for the purpose of avoiding any penalties that may be imposed under federal tax laws. The opinions expressed are those of the author(s) and do not necessarily reflect the views of the firm, its clients or any of its or their respective affiliates. Views expressed are as of the date indicated and may change based on market and other conditions. The accuracy of the content and its relevance to your particular circumstances is not guaranteed.

Many investors consider bonds to be "risk-free" investment vehicles. Historically, bonds have indeed provided less volatility and less risk of loss of capital than has equity investing. However, there are many factors which may affect the risk and return profile of a fixed-income portfolio. The two most prominent factors are interest-rate movements and the creditworthiness of the bond issuer. The risk of a change in the market value of the investment due to changes in interest rates is known as interest-rate risk. Interest-rate risk is subject to many variables but may be analyzed based on various data (e.g., effective duration). The risk that the issuer may default on interest and/or principal payments is often referred to as credit risk. Credit risk is typically measured by ratings issued by ratings agencies such as Moody's and Standard & Poor's. Bonds issued by the U.S. Government have significantly less risk of default than those issued by corporations and municipalities (see below for a discussion of the risk associated with convertible securities). However, the overall return on Government bonds tends to be less than these other types of fixed-income securities. Finally, reinvestment risk is the possibility that the proceeds of a maturing investment must be invested in a lower yielding security, all other things held constant, due to changes in the interest-rate environment. Investors should pay careful attention to the types of fixed-income securities which comprise their portfolio, and remember that, as with all investments, there is the risk of the loss of capital.

Contact us at [800.521.1195](tel:800.521.1195) or visit [eagleasset.com](http://eagleasset.com)

**EAGLE** | Asset  
Management  
AN AFFILIATE OF CARILLON TOWER ADVISERS