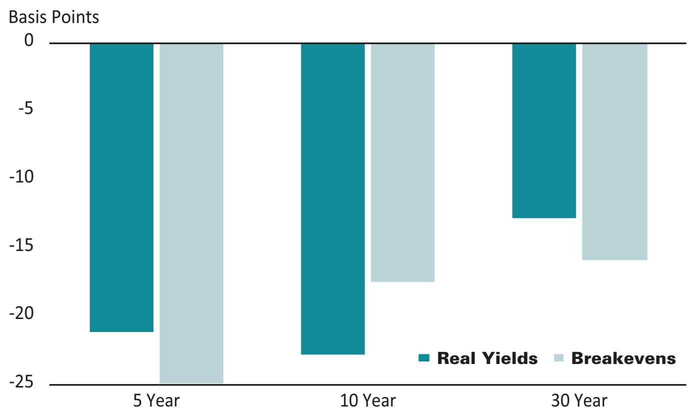
BBH Inflation-Indexed Securities

Quarterly Strategy Update / 2Q 2019

Easing Ahead

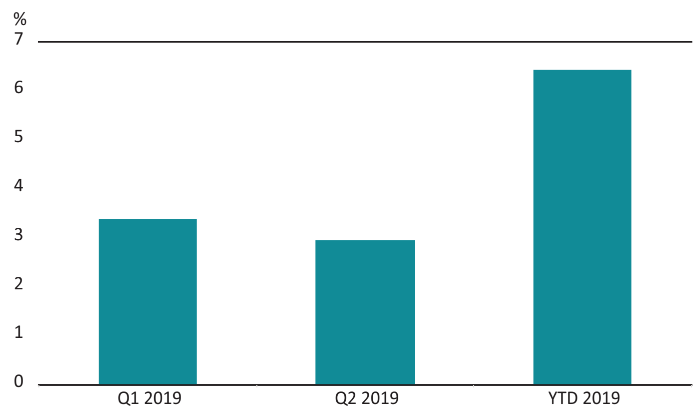
A highlight of the quarter came near the end of June when the Federal Reserve (Fed) signaled easier policy ahead. As argued below, the Fed's inability to raise inflation above target for almost a decade has been a constant frustration. From that perspective, inflation markets welcomed a policy shift aimed at raising inflation expectations with a strong rally in break-even inflation rates *(breakevens),* reversing a downward trend that had prevailed for most of the quarter.

Quarterly Change 2019



Data reported as of June 30, 2019
Sources: Bloomberg and BBH Analysis

TIPS Absolute Returns 2019



Past performance does not guarantee future results
Data reported quarterly from March 31, 2019 to June 30, 2019
Sources: BofAML and BBH Analysis

For the quarter, the real yield curve at the 5-, 10-, and 30-year maturities rallied 20, 25, and 15 basis points[1], respectively. The full-maturity TIPS benchmark returned 3%, bringing the year-to-date absolute return to 6.4%. Breakeven inflation rates at the 5-, 10-, and 30-year tenors decreased 25, 20, and 15 basis points, respectively.

In terms of performance, our accounts finished the quarter ahead of a strong market by 8 to 12 basis points. Consistent with the seasonal steepening bias we see in TIPS, we kept a duration overweight in the intermediate part of the curve and an underweight in the long part of the curve. This *real yield curve* steepener contributed to performance, especially after the Fed's policy statement in June. Our overall long-duration position also contributed to relative performance given the decline in real rates mentioned above.

Although breakevens regained some ground in the second half of June, they were down for the quarter. This caused our long-breakeven position to detract from performance. TIPS struggled as geopolitical uncertainties and unresolved trade disputes continue to drive investors toward nominal Treasuries.

The economy grew at an annualized rate of 3.2% in the first quarter of 2019 and it is estimated to have grown at 1%-2% in the second quarter. The current expansion – now 10 years in length – is the longest stretch of uninterrupted growth since 1854. Labor markets remain strong with unemployment at 3.7%, and more than a million new jobs have been added this year. Wage growth has now stayed on a healthy trajectory of at least 3% per year for eleven consecutive months.

Broad measures of inflation remain a concern for the Fed in an otherwise robust economy. At the end of May, headline Consumer Price Index (CPI) stood at 1.8%, Core CPI at 2%, and Core Personal Consumption Expenditure (PCE), the Fed's preferred inflation gauge, at 1.6%. Following the Federal Open Market Committee (FOMC) meeting in early May, Chair Powell attempted to downplay low inflation, citing "transitory" factors and pointed at the Dallas Fed Trimmed Mean running close to 2%.

At the Fed's last two meetings in early May and mid-June, the federal funds rate was left unchanged at 2.5% as had been expected by most market participants. But the Fed's policy stance has since shifted based on the potential economic fallout from broadening trade disputes as well as from inflation

[1] Basis point is a unit that is equal to 1/100th of 1% and is used to denote the change in price or yield of a financial instrument.

measures undershooting Fed targets. The Fed will deny any policy impact from the President's unrelenting calls for renewed ease, but this has had some impact on the Fed's abrupt shift in policy since the end of last year. In his recent Congressional testimony, Chair Powell guided investors to expect an ease at the upcoming July 31st meeting. June's Summary of Economic Projections (SEP) shows seven FOMC members expect two cuts in 2019, compared to none of the members expecting a cut in March's SEP.

The Fed's SEP released after the June meeting shows a decline in inflation forecasts. The forecast for PCE inflation was reduced from 1.8% to 1.5%, and that of Core PCE was lowered by 0.2% to 1.8%. Since there were no forecasted growth problems and the data continue to suggest that the U.S. economy remains on solid footing, we believe that low inflation and low inflation expectations are the driving forces behind policy easing.

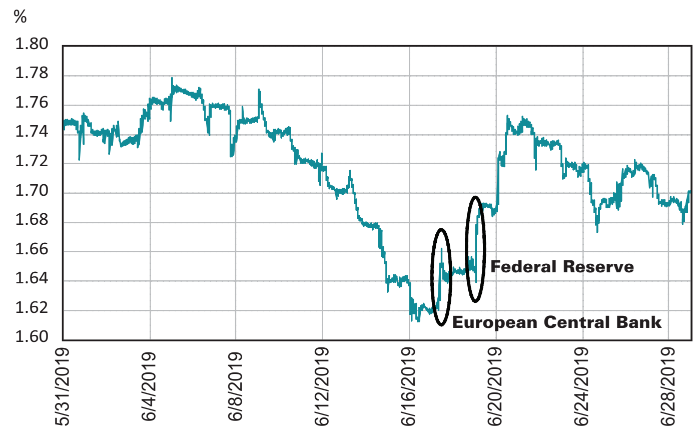
We should add that the Fed is not the only major central bank signaling policy accommodation amid concerns of low inflation. On June 18th, at the European Central Bank's (ECB) annual forum, President Mario Draghi stated that "additional stimulus will be required" if the economic outlook does not improve.

In general, when central banks intend to lower rates, the objective is to lower real rates, which is equivalent to reducing funding costs or increasing inflation expectations. Inflation markets responded with a strong rally. For instance, 10-year breakevens jumped almost 15 basis points in response to the ECB and Fed policy announcements, reversing the trend of falling breakevens observed throughout the quarter.

Ongoing trade uncertainties, and the desire to obtain more clarity before changing policy, ultimately dissuaded the Fed from cutting rates in June. For now, investors expect three rate cuts in the second half of the year – one more than the Fed itself. With central banks around the world gravitating towards lower rates, we do not need above-average inflation for TIPS to perform well. Improved auction demand and positive flows into TIPS-related products after eight consecutive months of outflows are already helping.

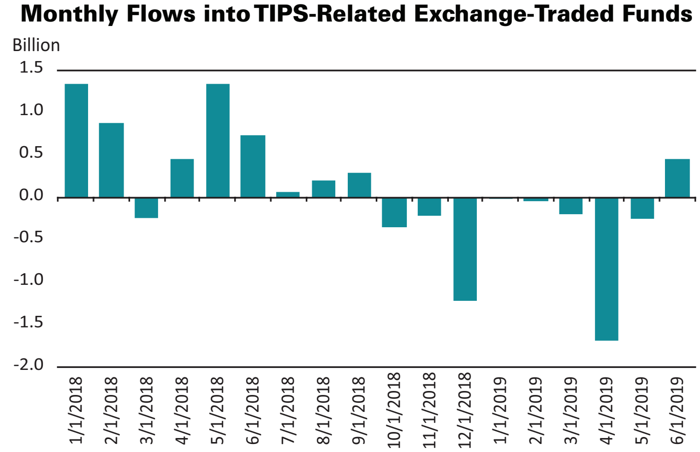
The Fed is on a path of easier policy amid the longest economic expansion on record. We think this is an expression of genuine concern about below-target inflation for too long. With breakeven rates 25-to-50 basis points below realized inflation, this is a welcome development that supports already attractive TIPS valuations. We look forward to capitalizing on the opportunities we find with our time-tested investment strategies.

Intraday Levels of 10-Year Breakeven Inflation Rates



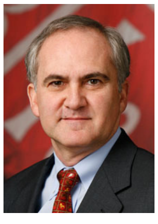
Data reported daily from May 31, 2019 to June 29, 2019
Sources: Bloomberg and BBH Analysis

Monthly Flows into TIPS-Related Exchange-Traded Funds



Data reported monthly from January 1, 2019 to June 1, 2019
Sources: Bloomberg and BBH Analysis

Sincerely,



James J. Evans, CFA
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Performance As of June 30, 2019							
	Total Returns		Average Annual Total Returns				
Composite/Benchmark	**3 Mo.***	**YTD**	**1 Yr.**	**3 Yr.**	**5 Yr.**	**10 Yr.**	**Since Inception**
BBH Inflation-Indexed Securities Composite (Gross of Fees)	2.97%	6.20%	4.90%	2.13%	1.97%	3.87%	5.71%
BBH Inflation-Indexed Securities Composite (Net of Fees)	2.93%	6.12%	4.75%	1.98%	1.82%	3.72%	5.51%
Bloomberg Barclays U.S. TIPS Index	2.86%	6.15%	4.84%	2.08%	1.76%	3.64%	5.29%

* Returns are not annualized.

Sources: BBH & Co. and Bloomberg

Past performance does not guarantee future results, and current performance may be lower or higher than the past performance data quoted. The investment return and principal value will fluctuate, and shares, when sold, may be worth more or less than the original cost.

For purpose of complying with the GIPS® standards, the firm is defined as Brown Brothers Harriman Investment Management ("IM"). IM is a division of Brown Brothers Harriman & Co. ("BBH"). IM claims compliance with the Global Investment Performance Standards (GIPS®). To receive a list of composite descriptions of IM and/or a presentation that complies with the GIPS standards, contact John W. Ackler at (212) 493-8247, or via email at john.ackler@bbh.com.

Gross of fee performance results for this composite do not reflect the deduction of investment advisory fees. Actual returns will be reduced by such fees. "Net" of fees performance results reflect the deduction of the maximum investment advisory fees. Performance calculated in U.S. dollars.

The Composite is comprised of fully discretionary, fee-paying domestic accounts over $10 million with an emphasis on U.S. inflation indexed securities. May invest up to approximately 25% outside of U.S. inflation indexed securities, and a duration of approximately 7-9 years. Accounts are benchmarked to the Bloomberg Barclays U.S. TIPS Index or equivalent. The Bloomberg Barclays 1-10 Year Municipal Blend Index is a market value-weighted index which covers the short and intermediate components of the Barclays Municipal Bond Index --an unmanaged, market value-weighted index which covers the U.S. investment-grade tax-exempt bond market. The 1-10 Year Municipal Blend index tracks tax-exempt municipal General Obligation, Revenue, Insured, and Prerefunded bonds with a minimum $5 million par amount outstanding, issued as part of a transaction of at least $50 million, and with a remaining maturity from 1 up to (but not including) 12 years. The index includes reinvestment of income.

RISKS

Investing in the bond market is subject to certain risks including market, interest-rate, issuer, credit, and inflation risk; investments may be worth more or less than the original cost when redeemed.

The U.S. Government guarantee applies only to the underlying securities of the fund's portfolio and not to the value of the fund's shares. U.S. Government Securities issued by government agencies, instrumentalities and government sponsored enterprises, are neither issued nor guaranteed by the U.S. Treasury nor backed by the full faith and credit of the United States.

International investing involves special risks including currency risk, increased volatility, political risks, and differences in auditing and other financial standards.

The Fund also invests in derivative instruments, investments whose values depend on the performance of the underlying security, assets, interest rate, index or currency and entail potentially higher volatility and risk of loss compared to traditional stock or bond investments.

The Fund may engage in certain investment activities that involve the use of leverage, which may magnify losses.