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Strategy & Outlook
February 2018

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Economic and Market Recap
January 31, 2017

Equity Markets		
Index	**January**	**One-Year**
S&P 500	5.72%	26.40%
Russell 3000	5.27%	25.15%
Russell Mid Cap	3.76%	20.06%
Russell 2000	2.61%	17.16%
EAFE	5.02%	27.60%
Emerging Markets	8.33%	41.01%

Fixed Income and Commodities		
Security	**1/31/2018**	**12/31/2017**
2 Year UST	2.13%	1.91%
10 Year UST	2.73%	2.43%
"BBB" Corporate	3.71%	3.54%
Yield Spread (bps)	98	111
Gold / oz.	$1,343	$1,297
Oil (WTI) / barrel	$64.70	$59.80

Economics and Currency		
Economic Data	**1/31/2018**	**12/31/2017**
GDP Growth (1)	2.60%	2.40%
Core CPI (1)	2.42%	2.21%
Unemployment Rate	4.1%	4.1%
YOY Wage Increase	2.9%	2.1%
Participation Rate	62.7%	62.7%
Euro, per $	€ 0.81	€ 0.84

(1) Lastest quarter ending 12/31/17.

Employment data as of January, 2018

Economy

- The U.S. economy continues to build momentum – initial 4Q GDP posted a 2.6% increase versus year-ago increase of 1.6%.
- The employment picture continues to improve as the unemployment rate remained at 4.1% in January, and wages experienced an increase of 2.9%.

Equity Markets

- U.S. equity markets experienced one of is strongest starts to the year with the S&P jumping 5.7% in January.
- Recent gains in equity markets have been led by technology, health care, and consumer discretionary stocks.

International

- International markets started the year strong with EAFE jumping over 5% and Emerging Markets surging 8.3%.
- Global economies continue to show signs of synchronized growth across all regions.

Fixed Income Markets

- Corporate yield spreads tightened in January as yields rose across the maturity spectrum.
- The yield curve remained relatively flat in January as the spread between the 10 year and 2 year Treasury hovered around 60 basis points..

Chart Sources: Russell, S&P, FactSet, Barclays, CRB, MSCI

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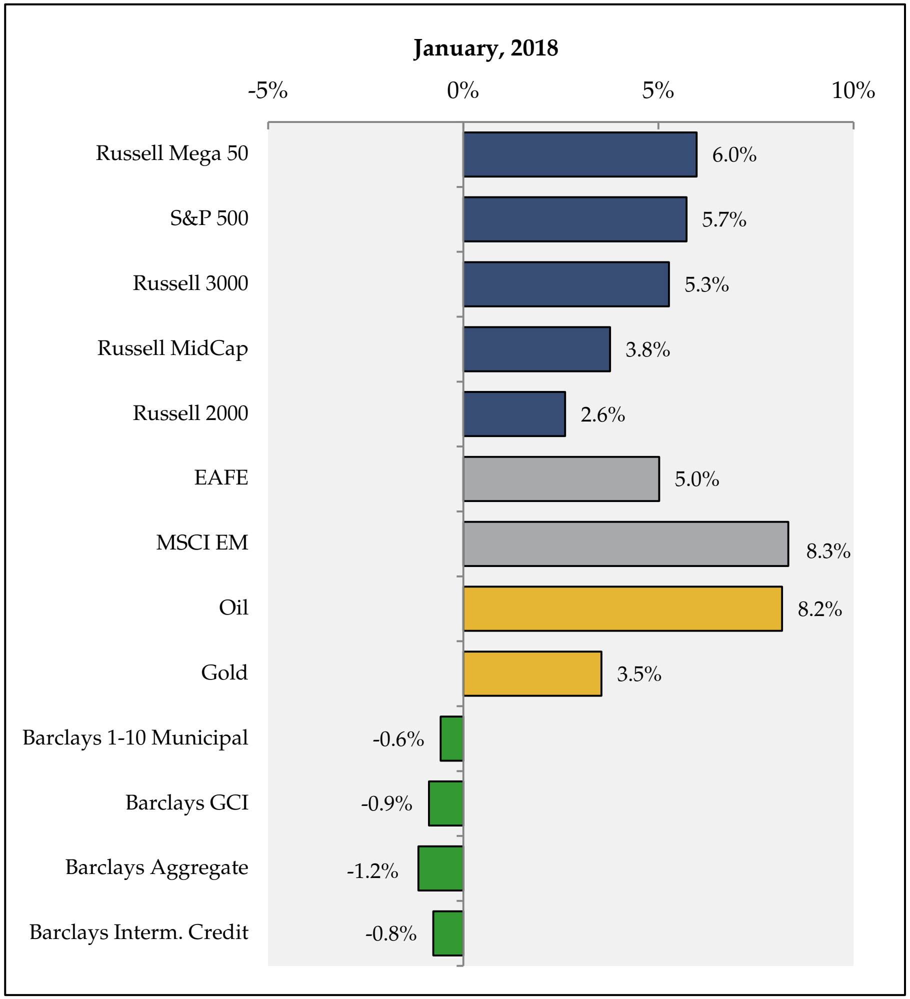
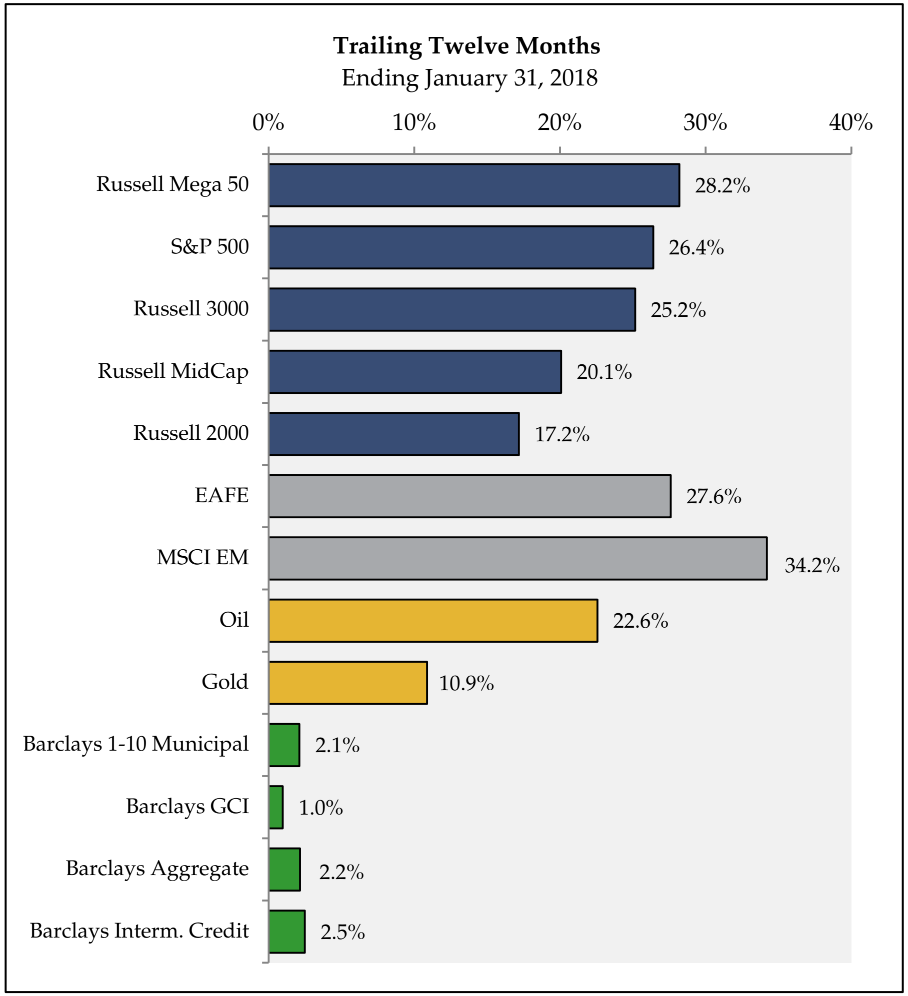
Major Market Returns

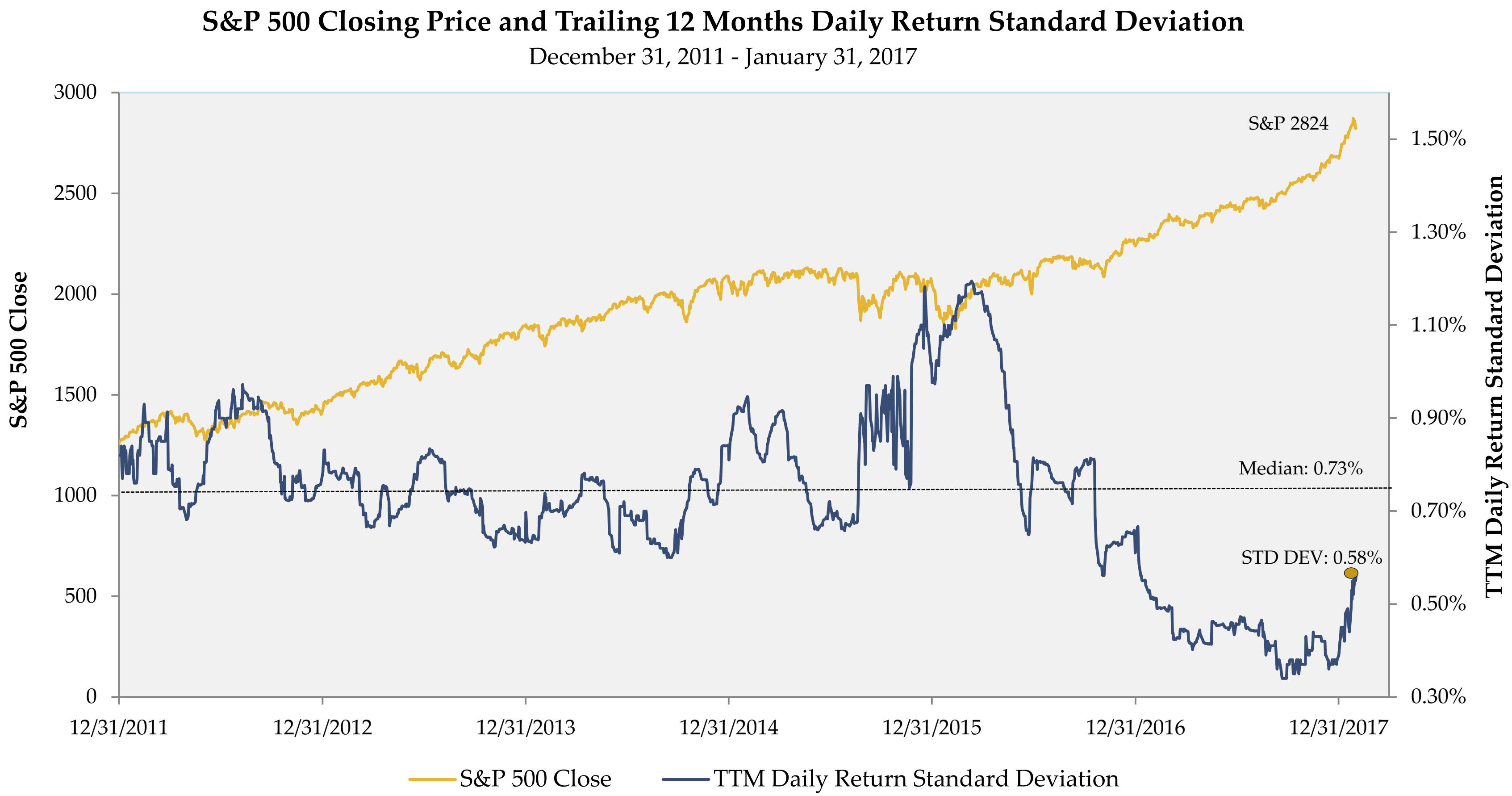




- Equity markets started the year strong with all major indices up solidly in January. This helped push all global indices significantly higher for the past year.
- Bond prices dropped in January as rates rose but, remain in positive territory for the trailing twelve months.

BBG: Bloomberg Barclays Index
Data as of 1/31/2018. Source: Russell, S&P, Barclays, FactSet, MSCI.

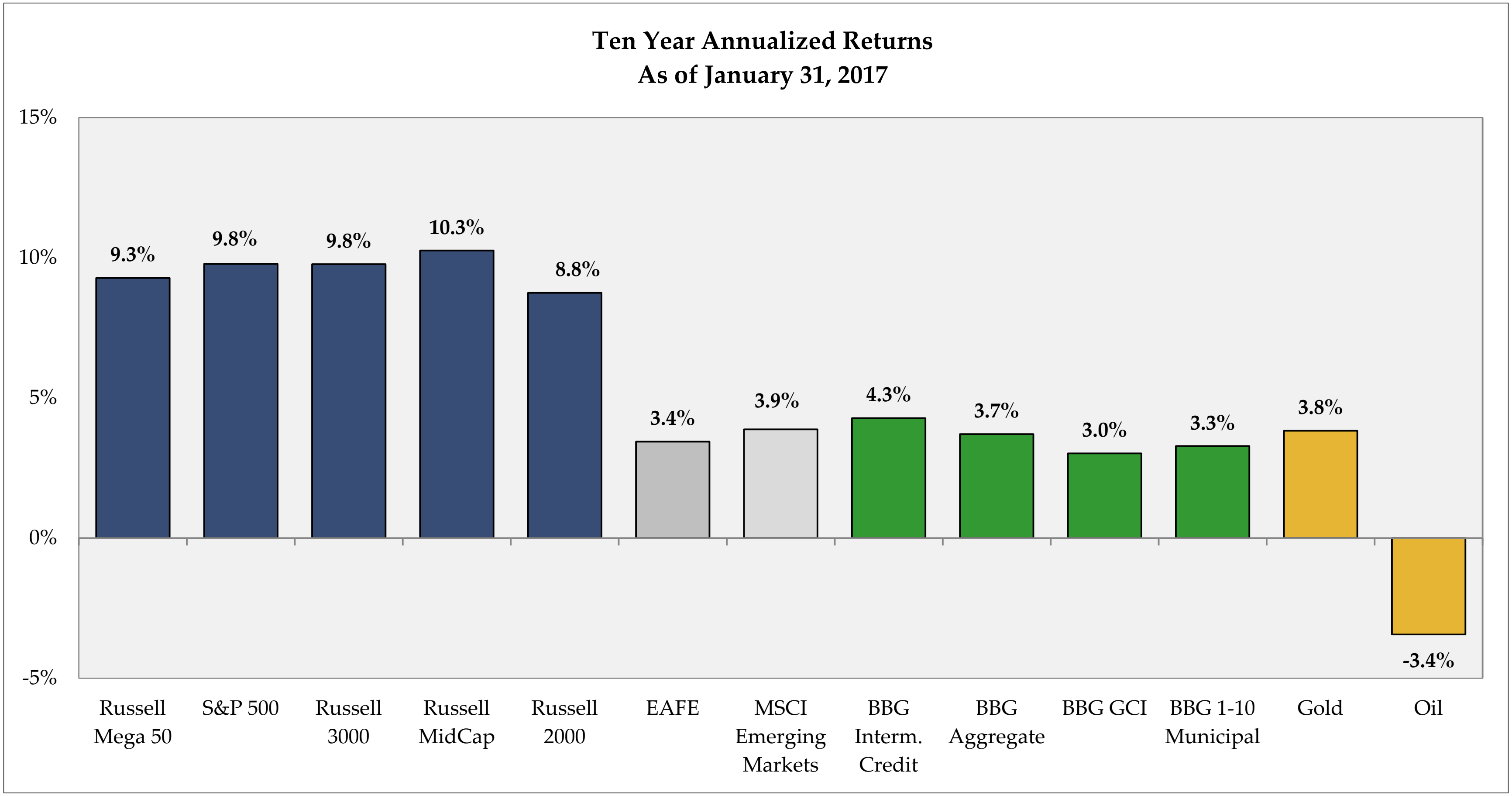
Equity Market Volatility



- After hitting all time lows in 2017 market volatility is increasing with short term market swings as measured by standard deviation of daily returns rising significantly in January.

Data as of 1/31/2018. Source: S&P, FactSet,

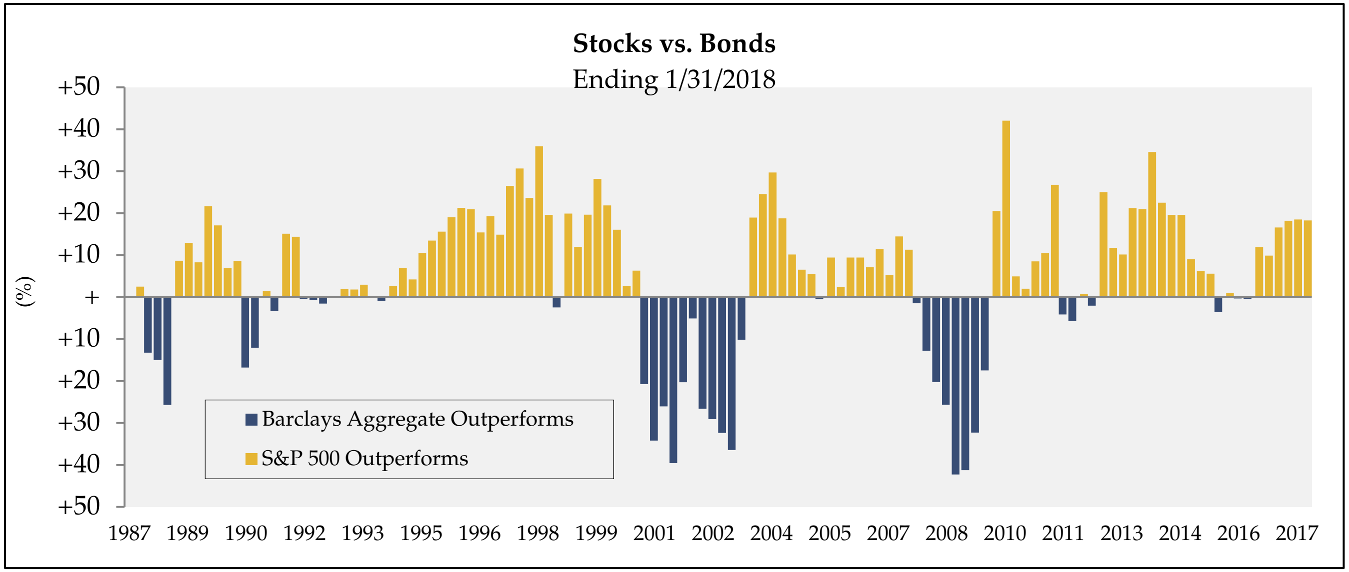
Long Term Market Returns



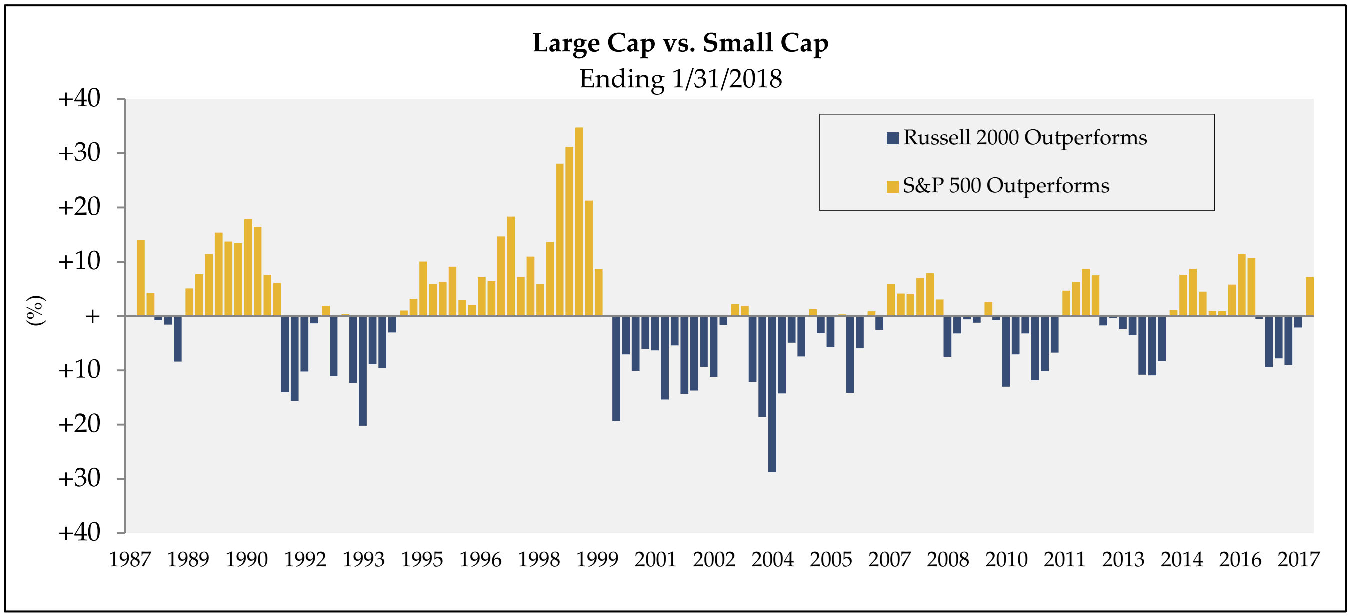
- Despite periods of volatility and uncertainty, long term rates of return for financial assets have been positive. However, oil prices have declined.
- Annual compounded returns for equities over the trailing ten years are solidly in positive territory despite the more than 50% market drop during the financial crisis of 2008-2009 – further supporting a focus on the long term.

BBG: Bloomberg Barclays Index
Data as of 1/31/2018. Source: Russell, S&P, Barclays, FactSet, MSCI.

Market Leadership: Year-Over-Year Returns



- Stock returns relative to bonds diverge dramatically over market cycles. The equity rally in 2017 created a significant return dispersion in stocks versus bonds on a year-over-year basis. This further supports the benefits of asset class diversification.

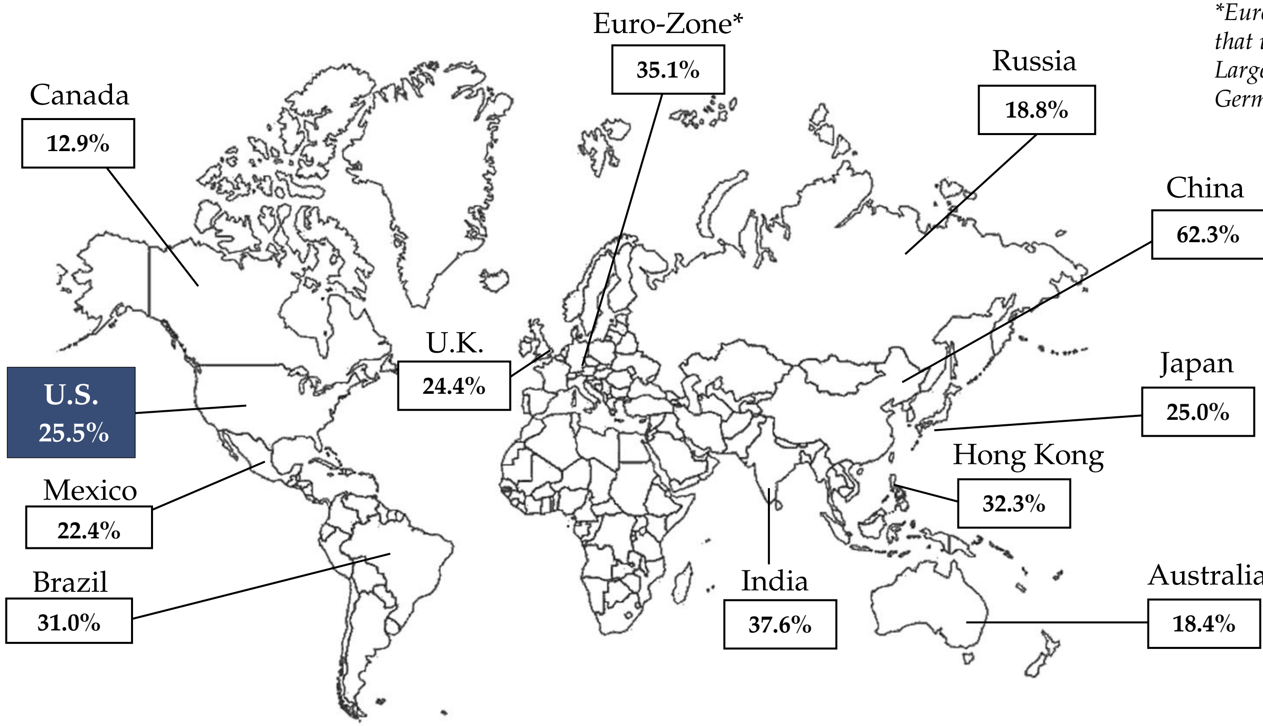


- There can be significant dispersion of returns within U.S. equity markets. This confirms our belief in equity asset class diversification. After a period of underperformance versus small caps, large cap stocks have begun to outperform.

Data as of 1/31/2018. Source for both charts: eVestment Analytics.

Global Equity Market Returns

Trailing 12 Months Ending January 31, 2018



**Eurozone comprised of 17 countries that use the Euro as its currency. Largest constituents include Germany, France and Italy.*

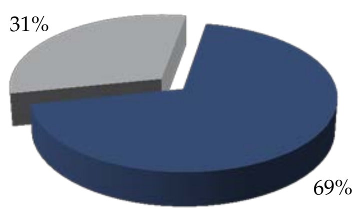
- All major equity markets are in positive territory over the past year – many emerging markets have surged following a prolonged period of underperformance.
- Global economies are showing signs of improvement; however, they continue to confront political and economic uncertainty – this should push volatility higher.

Source: MSCI

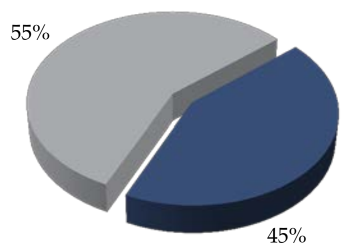
Global Perspective

Global Market Capitalization Breakdown (U.S. vs. Non-U.S.)

1970



2017*

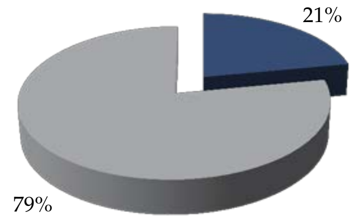


Source: International Monetary Fund (IMF), Russell Investments
** Preliminary*

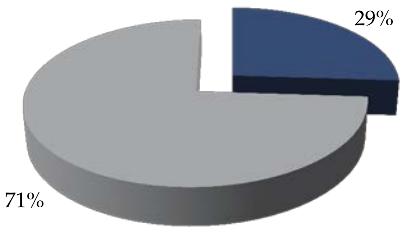
- International markets continue to grow with over half of the world's market capitalization traded outside of the U.S.

Global GDP and Corporate Location (U.S. vs. Non-U.S.)

Percentage of Global GDP

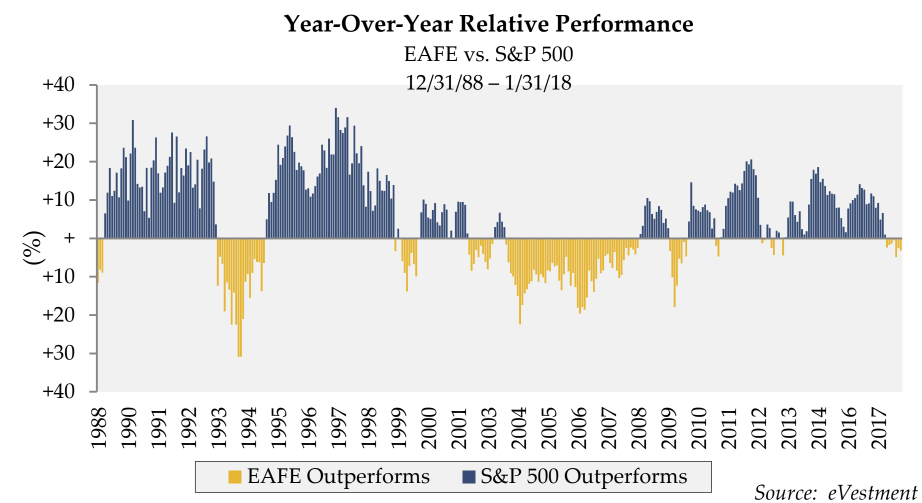


Publicly Traded Companies by Location



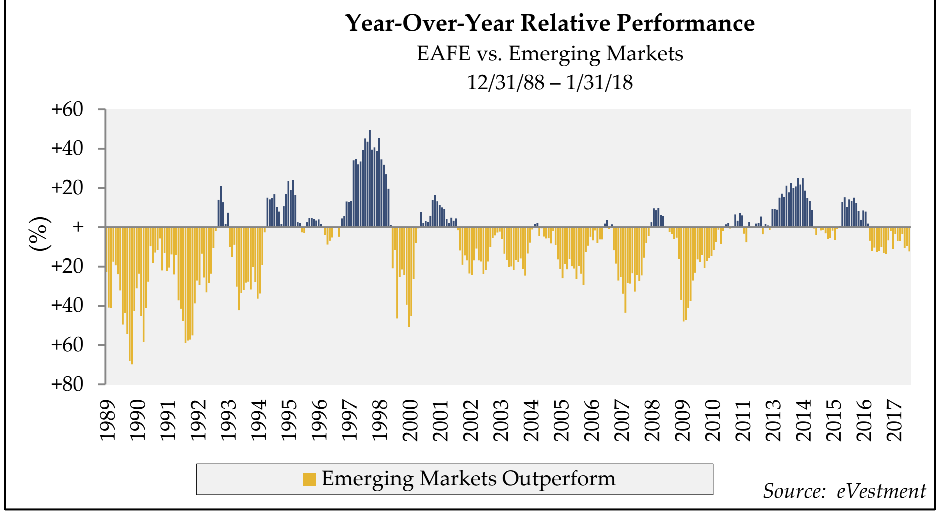
Source: International Monetary Fund (IMF), MSCI for most recent period ending 12/31/17

- International economies represent two-thirds of global GDP with the majority of publicly traded companies based outside of the U.S.



Source: eVestment

- International markets move in cycles with periods of underperformance versus U.S. markets followed by periods of outperformance.

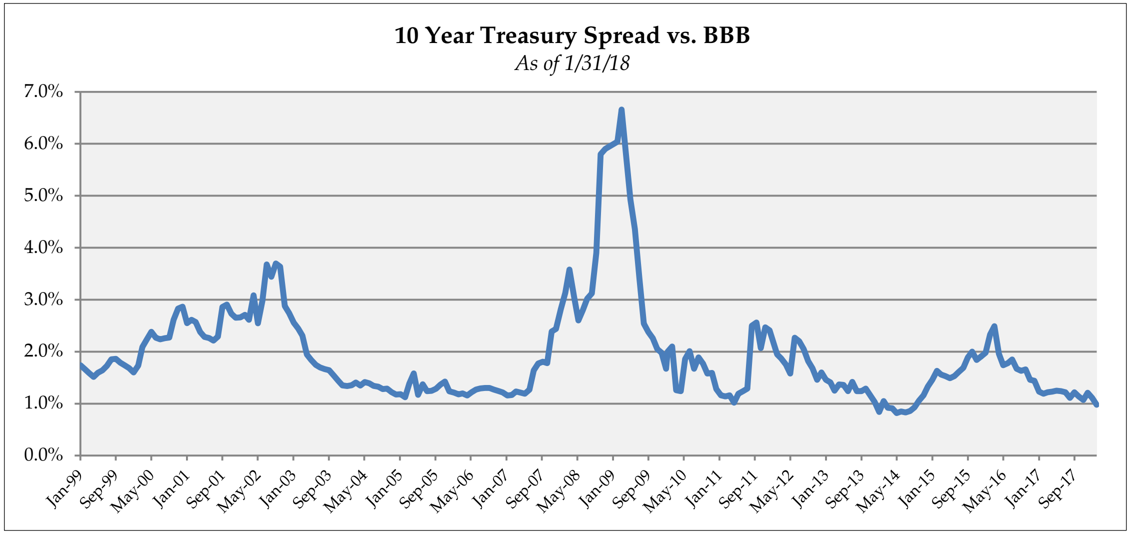


Source: eVestment

- Emerging Markets have the advantage of higher growth rates – however, there are prolonged periods where developed markets generate higher returns.

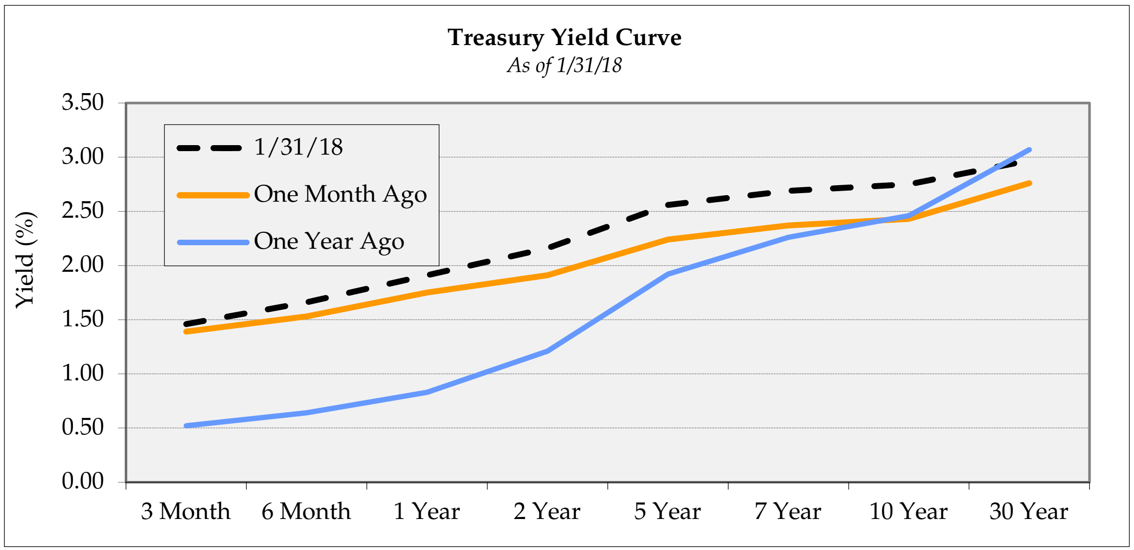
As of 01/31/2018. Source: FactSet.

Fixed Income Markets: Trailing 12 Months



Source: Bloomberg; Barclays Capital

- The BBB-rated corporate yield spread versus Treasuries ended January at 98 bps. However, BBB yields have fallen by over 13 bps for the year.

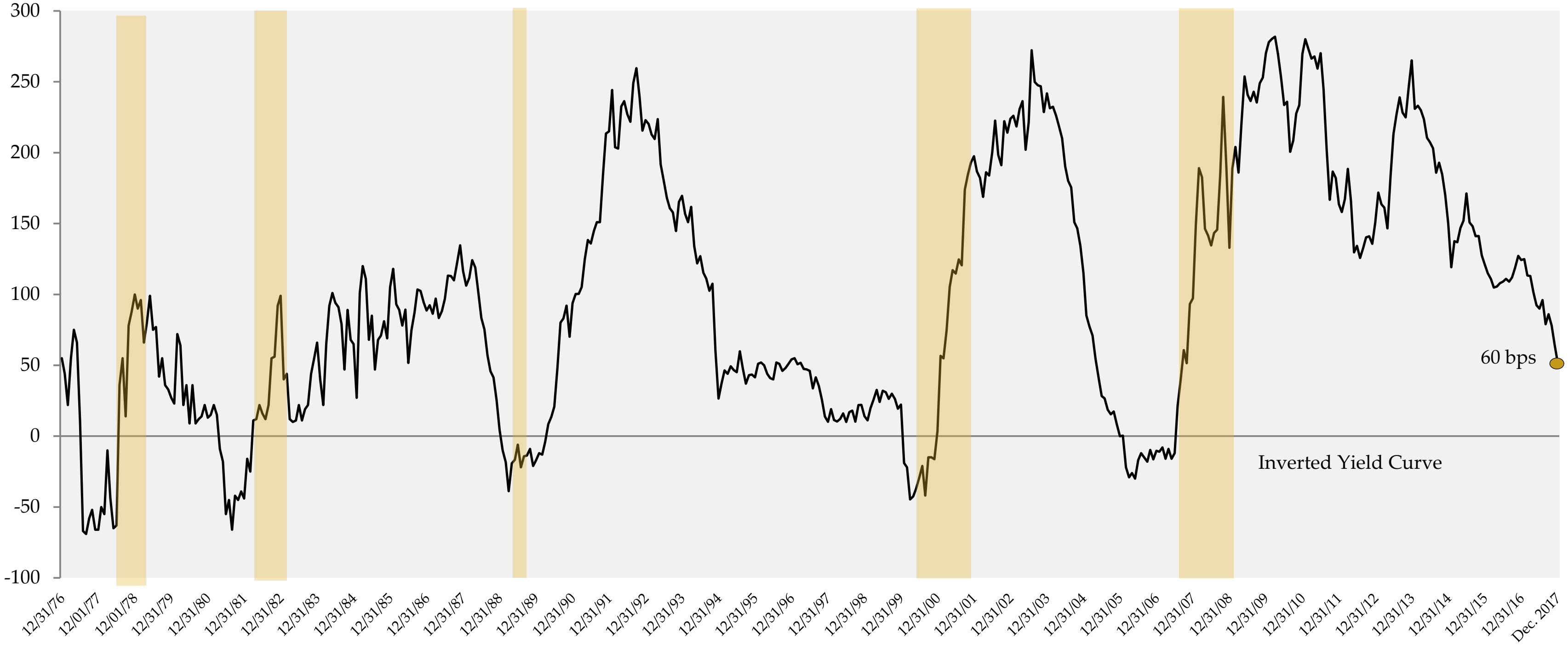


- The yield curve flattened in 2017 as short term rates moved higher while long term rates have declined.
- The 10 year Treasury bond yield closed January at 2.73% - down from 2.43% at the beginning of 2018.

Source: FactSet

Fixed Income Markets: Trailing 12 Months

Treasury Yield Curve
10-Year vs. 2 Year Spread (Basis Points)
12/31/76 - 1/31/2018



- The yield curve remained unchanged in January after flattening significantly in 2017. The yield spread between 10-year and 2-year Treasuries is at levels last seen in 2007.
- A flat yield curve signals a slowdown in economic growth while an "inverted" yield curve indicates a recession on the horizon. The yield curve has inverted five times in the past forty years, all of which were followed by a recession.
- Recent flattening in the yield curve is not cause for alarm at this time; however, it is important to pay close attention to where it moves from its current level.

As of 1/31/2018. Source: Factset

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Our Current Market View and Strategy

U.S. Equity Markets

Strengths

- Economic growth is expected to get a boost from the new tax law, which will lower corporate and individual tax rates.
- Valuations are historically high – but not at historic extremes, and earnings growth is improving.
- Corporate balance sheets are very strong – high cash and low debt levels should add stability and confidence.
- Despite strong gains in 2017 fundamentals continue to support our positive market outlook.

Concerns

- A substantial rise in market turbulence following a long period of record low volatility has begun and is expected to persist.
- Uncertainty over the timing and pace of the Fed's shift in monetary policy under new Fed leadership.
- Geopolitical risk - especially with recent developments in the Middle East and North Korea, and continuation of uncertainty in Russian Mid East policy.

We are positive on the long-term outlook for U.S. equities. We expect positive earnings growth, low inflation, and strong corporate balance sheets will help stocks move higher over the next several years. In addition, the U.S.'s position as a global economic leader should continue to attract capital. The pro-business shift in Washington adds opportunity for an additional boost in growth – however, uncertainty over timing and pace of change will persist. Despite historically low volatility in 2017 we expect volatility to increase as issues around fiscal and monetary policy heat up.

International Equity Markets

Strengths

- Unique investment opportunities in various regions exist as non-U.S. markets now represent over 50% of global capitalization – our emphasis is currently on developed markets vs. emerging markets due to more rapid improvement in underlying fundamentals in EAFE economies.
- Expect higher than U.S. growth in many non-U.S. economies over the next three to five years.
- Recent positive performance versus the U.S. has been driven by improving fundamentals – which should allow this trend to continue.

Concerns

- Despite recent positive relative returns, emerging market growth expectations have slowed in recent quarters causing investor concerns and increased volatility in their equity markets.
- Geopolitical, economic, social, and military unrest and uncertainty in Europe , as well as the Middle East and North Korea.

Our view towards international equities has turned more positive. Valuation and improving fundamentals are encouraging. We want to have an active exposure to these markets in the current environment. We believe global economic and financial markets continue to be a cornerstone of a diversified portfolio. Our current bias is towards developed markets versus emerging markets due great acceleration in economic growth expected in Europe, Japan, and other developed markets. However, we have exposure to both markets.

Fixed Income Markets

Strengths

- Changes to monetary policy through the Fed's interest rate policies is expected to be gradual over the next year.
- Corporate credit fundamentals are strong and improving.
- Growing pressure to reduce government debt and spending.
- Continued low inflationary pressures.

Concerns

- Fed's successful execution of rate hikes over the next year.
- Rising concerns over a possible uptick in inflation driven by improving economic conditions and rising wage pressures.
- Risk associated with emerging market debt, China and India economic growth concerns, and pervasive geopolitical unrest.

We are positioning our portfolios more defensively by maintaining short to neutral maturity positions relative to benchmarks and focusing on higher coupon bonds. We believe the improving economy is expected to eventually put upward pressure on long term rates. We favor overweighting high quality corporate bonds relative to Treasury and Agency securities. Our high quality bias is expected to provide enhanced liquidity during this transition period. Municipal bonds have been attractively priced relative to taxable securities for the past several years – however, recently that relationship has become more normalized.

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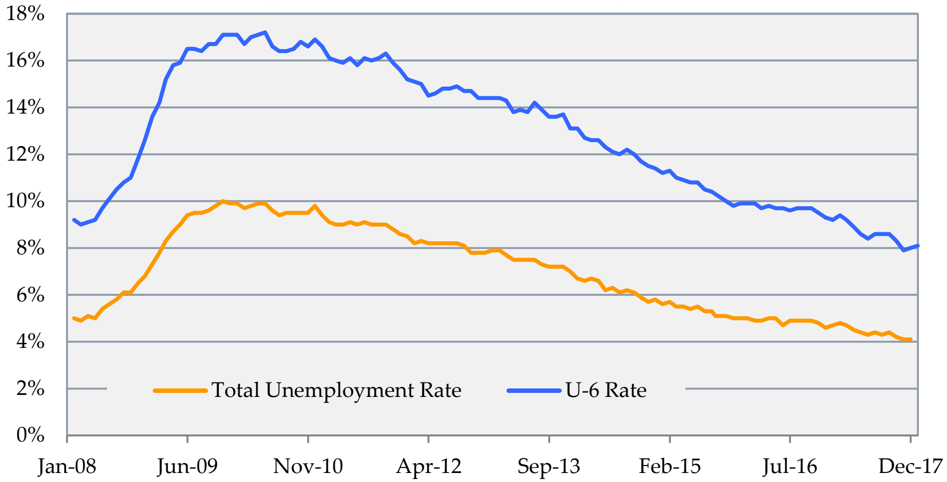
Dashboard of Labor Market Indicators

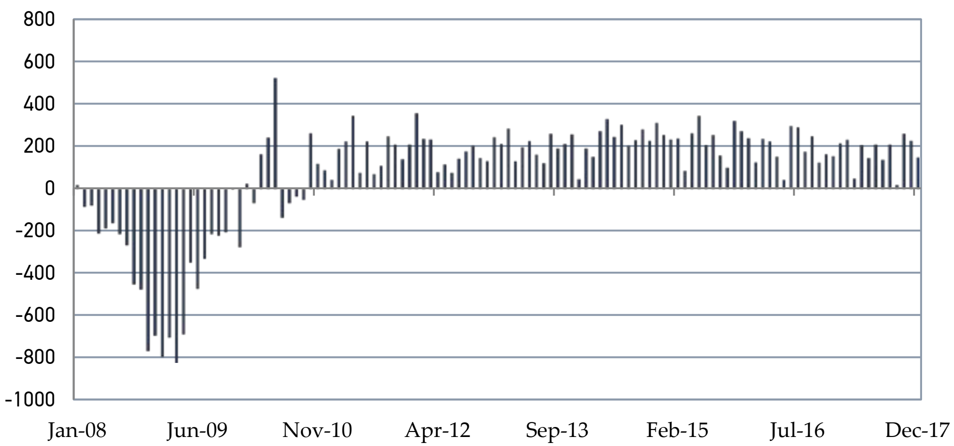
Unemployment and Underemployment (U-6)



Percent of Unemployed Considered Long-Term

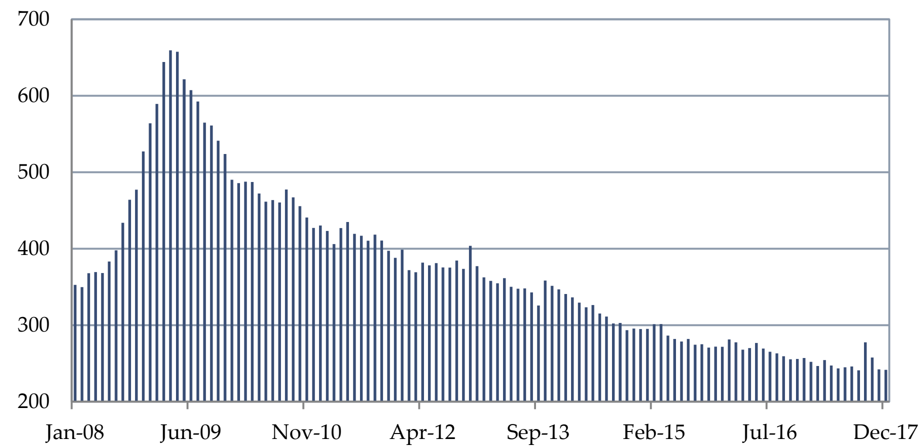
Thousands

NonFarm Payrolls MoM Change



Thousands

Initial Jobless Claims



- Labor markets continue to improve into 2018 as the unemployment for January remained at 4.1%, and wages rose a meaningful 2.9% across several economic sectors.

Data as of 1.31.2018. Sources: Bureau of Labor Statistics, Department of Labor.

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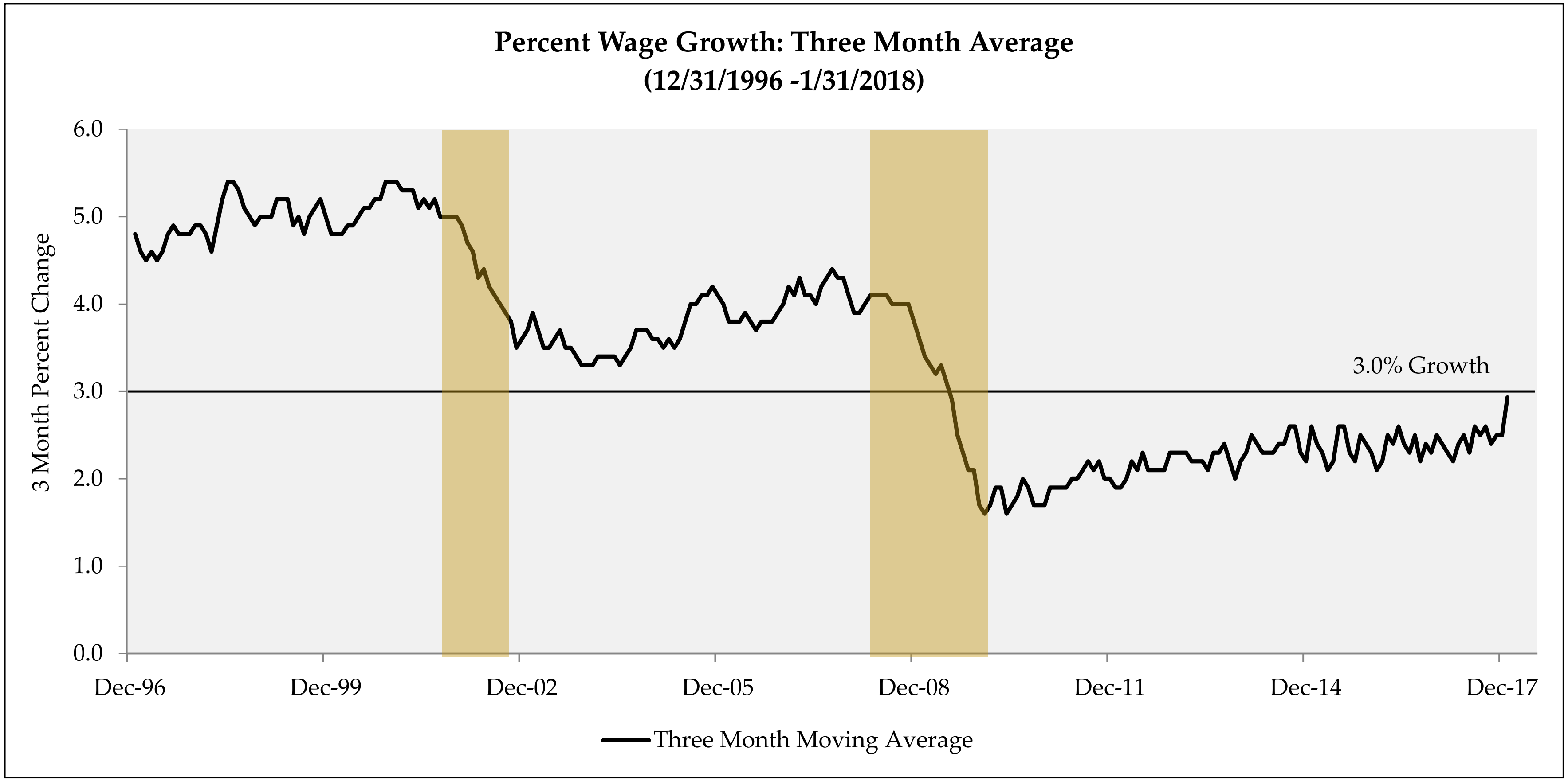
U.S. Wage Growth

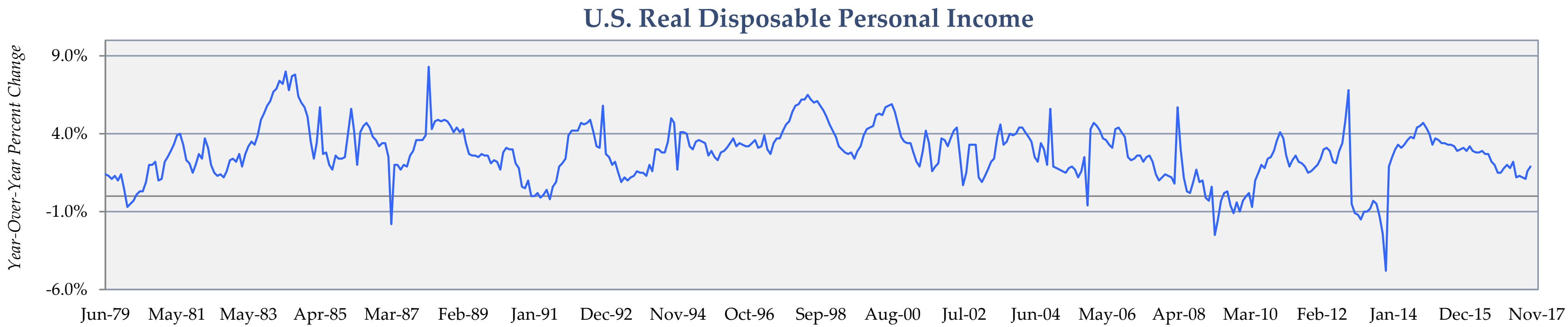


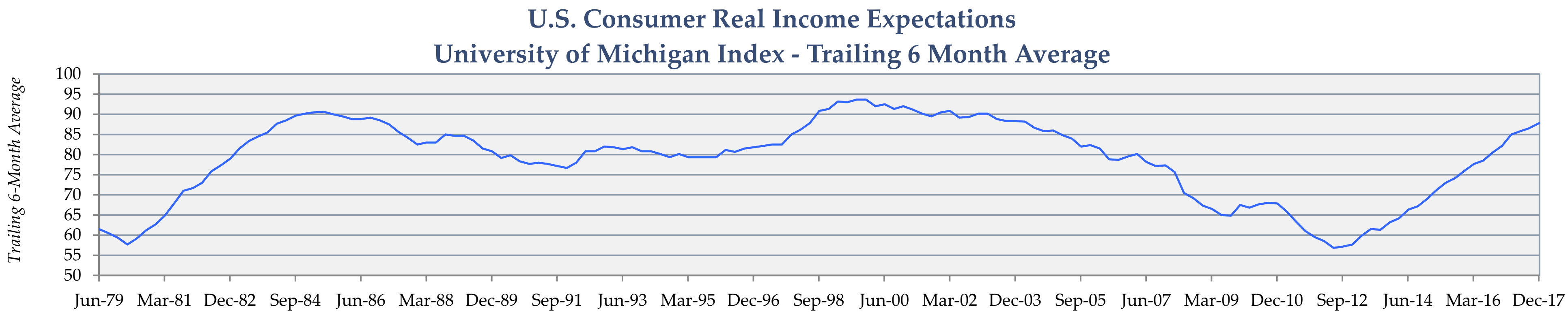
Shaded Areas = Recession

- Three month average wage growth has begun to move higher after years of stagnation.
- Tightening labor markets and the expanding global economy is putting upward pressure on wages. Upward wage pressures will eventually push inflation higher.

Data as of 1.31.2018. Source: US Department of Labor.

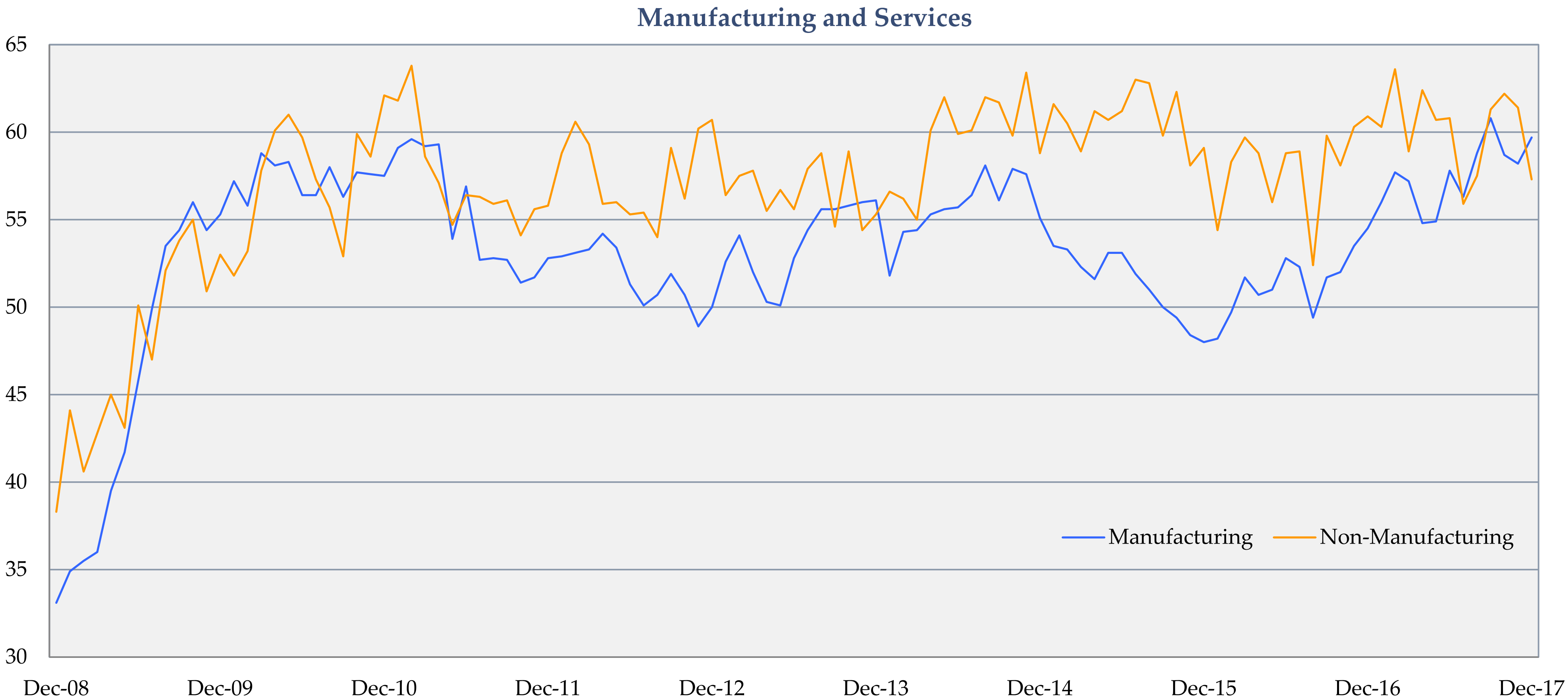
American Consumer on Solid Footing





- The consumer has seen continued growth of disposable income over the last two years and remains optimistic about future income growth.

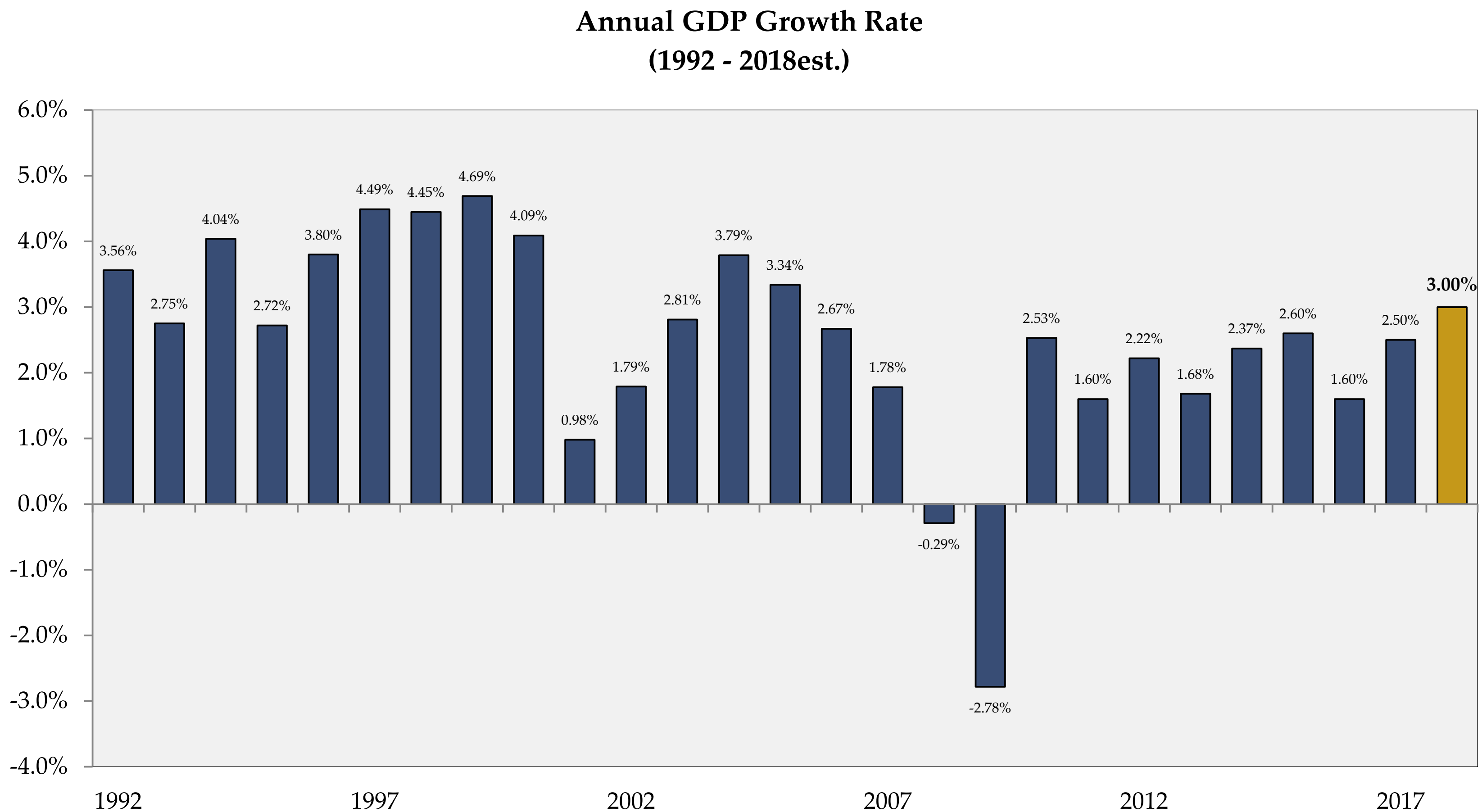
U.S. Real Disposable Personal Income data as of 12.31.2017. U.S. Consumer Real Income Expectations data as of 12.31.2017. Source: Bureau of Economic Analysis.



- ISM manufacturing as well as services activity indicators both remain solidly in expansionary territory.

Data as of 12.31.2017. Source: Institute for Supply Management.

Annual U.S. GDP Growth



- The U.S. economy is expected to expand by 3.0% in 2018 marking the first time since 2005 that calendar year growth has reached this level.

Data as of 1.31.2018. Source: US Department of Labor and Sterling Estimates.

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Economic Outlook

Strengths

- Signs of economic improvement continue – tax reform and regulatory rollbacks by the current administration should help drive higher growth in 2018.
- Consumer confidence and manufacturing are strengthening.
- Accelerating corporate profits and strong balance sheets continue to be positive.
- Global economies showing signs of modest improvement and stability
- Personal incomes growing and employment picture improving.
- Positive trend in leading economic indicators.

Concerns

- Washington "quagmire" may derail new administration's policies and stall the future execution of pro-business agenda.
- The Fed's pace and magnitude of interest rate increases adds monetary policy uncertainty.
- Investor complacency after a prolonged run in equity prices accompanied by low volatility.
- Global security concerns are rising with several terrorist incidences occurring and North Korea's nuclear weapons escalation.

Outlook

The combination of a modest improvement in housing, employment, and business spending should keep economic growth in positive territory over the next several quarters. Geopolitical concerns and uncertainty in Washington will overhang the economy, but should not derail economic momentum that began in late 2016. Improving corporate earnings, rising consumer confidence, and an uptick in capital spending should support positive future growth. For the full year 2017, we believe economic growth will have pushed higher to the 2.50%-2.75% range, up from the 1.7% rate of growth in 2016. Our view of 2018 calls for GDP growth in excess of 2017 - potentially reaching 3.0%. Overall, economic growth globally should continue well into 2018 at a pace greater than what has been experienced in recent years.

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