

2018 Capital Markets Review

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QTR. 4

Cash is King

Cash rarely tops any list of best performers, but against a backdrop of rising interest rates and collapsing stock prices, cash was king in 2018.

Market Turmoil

Heading into the final quarter, the S&P 500 (up +10.6% YTD) was poised to deliver its tenth consecutive calendar-year increase (including

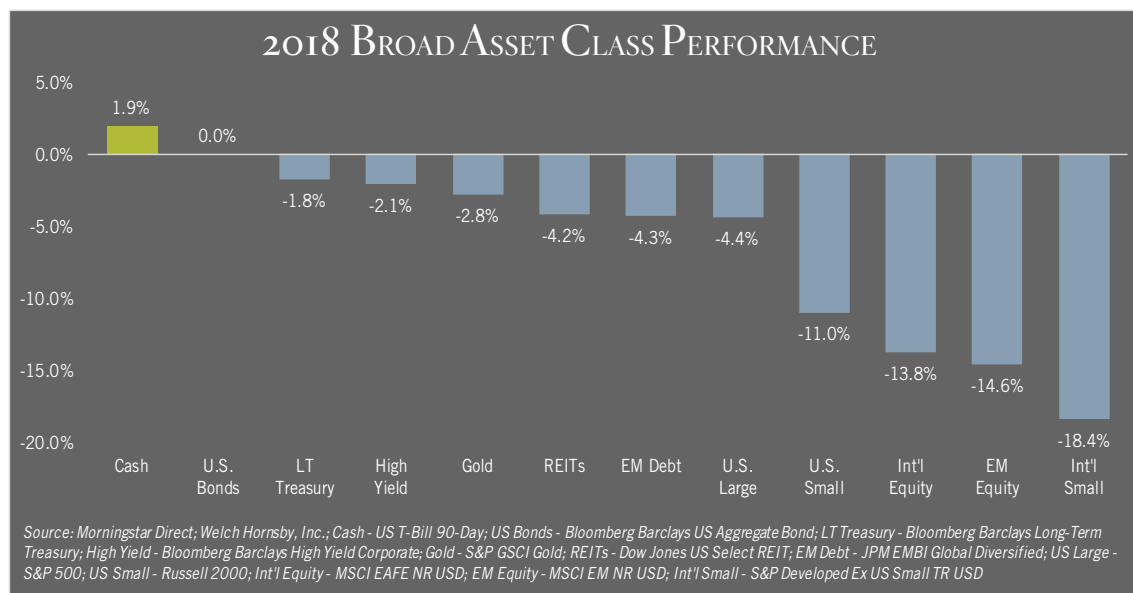
eight double-digit annual advances). However, the positive momentum ended abruptly as uncertainty surrounding multiple U.S. economic growth policies - monetary, fiscal and trade - elevated recession fears, sending stock markets sharply lower. The S&P 500 declined 13.5% over the final three months of 2018, resulting in a 4.4% loss for calendar year 2018.

Quarterly market collapses can be both emotionally and financially challenging, but rarely have

represented longer-term risks. Q4 2018 marked the twelfth double-digit quarterly decline in the last forty years. Reviewing the eleven previous sell-offs, on average the S&P 500 doubled over the subsequent five-years. The next five years may not look anything like the historical average, but often these market declines can be healthy for the stock market, reducing momentum driven risk-taking, excessive investor optimism and improving valuation metrics, providing a more stable foundation for future growth.

Digging deeper into the quarterly market turmoil, the extreme losses were felt across the capitalization spectrum, reaching 20% within smaller cap stocks. From a style standpoint, value modestly outpaced growth for the quarter, but no style box was left unscathed for the quarter or the year.

Reviewing sector results, seven of eleven sectors experienced quarterly declines greater than 10%. The only area that ended the quarter higher was the defensive Utilities sector, climbing 1.4%. On the opposite end of the spectrum, the Energy sector was crushed under the pressure of falling oil prices, declining 23.8% during the period.



CAPITALIZATION AND STYLE PERFORMANCE

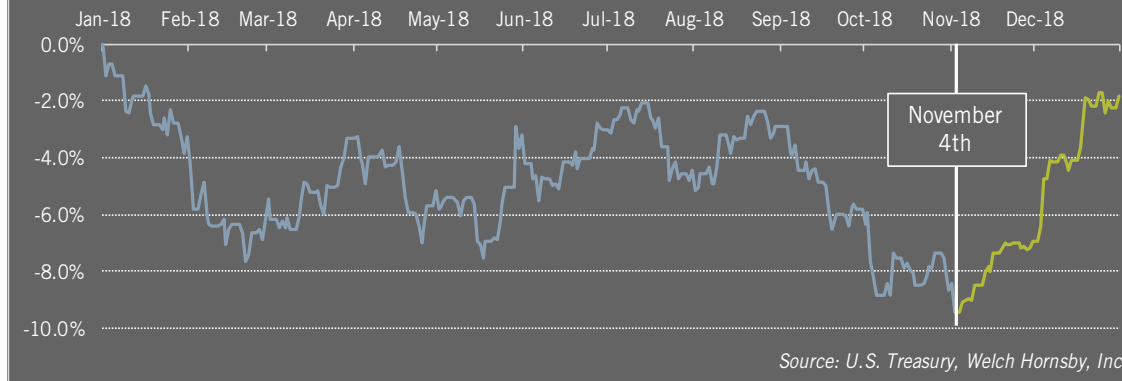
		4Q 2018	2018	
		Value	Core	Growth
Large		-11.7%	-13.8%	-15.9%
		-8.3%	-4.8%	-1.5%
Mid		-15.0%	-15.4%	-16.0%
		-12.3%	-9.1%	-4.8%
Small		-18.7%	-20.2%	-21.7%
		-12.9%	-11.0%	-9.3%

Source: Morningstar Direct, Russell Indices

Outside the U.S., foreign markets paralleled U.S. markets down, but unlike their domestic counterparts, they did not start the quarter with a cushion of YTD positive returns to insulate against market declines. Thus, while the quarterly market sell-off turned a good year for U.S. stocks into a bad year, the market rout turned a bad year for foreign markets into a significant market correction. Losses exceeded 10% for the quarter and year across most of Europe and the Asia-Pacific region with very few country-level exceptions. In aggregate, developed non-U.S. markets declined 12.5% for the quarter and 13.8% for the year, as measured by the MSCI EAFE Index.

BLOOMBERG BARCLAYS LONG-TERM U.S. TREASURY INDEX

Cumulative Year-to-Date Performance



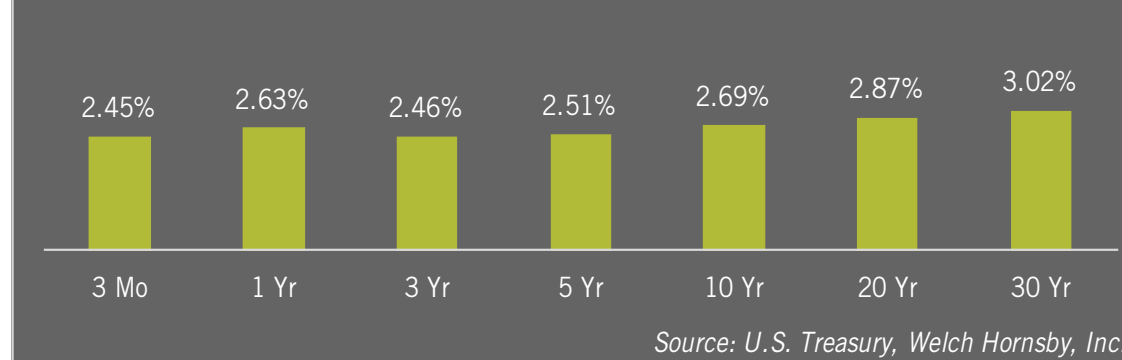
Fixed Income Review

Short-term rates moved steadily higher throughout 2018 as the Federal Reserve continued their rate normalization process, raising the Fed Funds rate four times. Longer-term yields followed short rates higher much of the year, creating significant headwinds for long duration fixed income strategies. By early November, the Bloomberg Barclays Long-Term Treasury Index had lost approximately 9.5%

year-to-date. However, as fears of a recession climbed, yields declined resulting in a dramatic year-end rally.

By year-end, the Treasury yield curve had very little “curve”. The spread between ultra-long bonds and ultra-short bonds was less than 0.6%. Why would an investor accept significantly more interest rate risk for only 0.6% in premium? The investor expects the Federal Reserve to reverse course and lower, not

TREASURY YIELDS - DECEMBER 2018



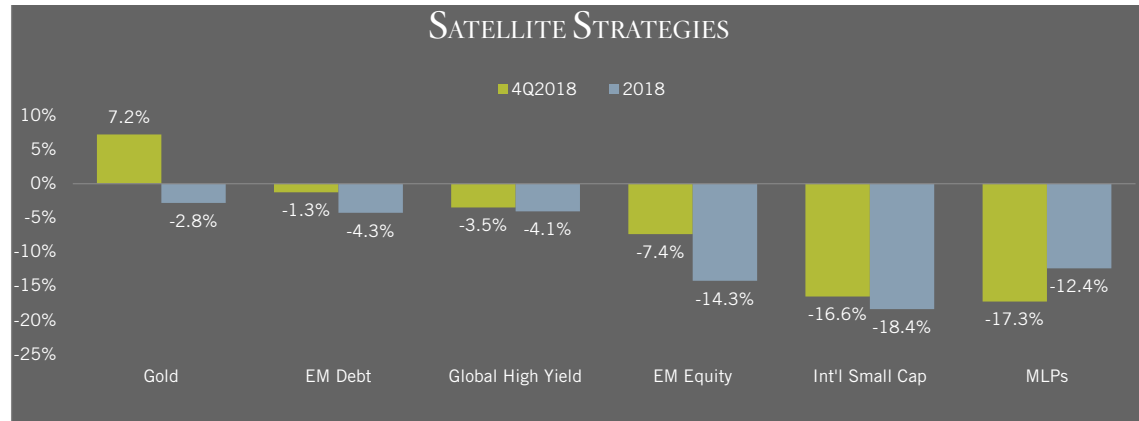
raise, rates. In fact, despite the Fed's projection for three additional rate hikes, the market has priced in no hikes in 2019 and a rate cut in 2020. Yields will likely continue to be volatile as market expectations and Federal Reserve projections reconcile.

Outside of the Treasury sector, spread performance was mixed during 2018. Corporate bonds lagged as investors demanded additional premium for perceived heightened credit risk, while agency mortgage-backed securities ended the year modestly higher. Against this extraordinary backdrop with yields and spreads rapidly changing, investment-grade bonds ended the year one basis point higher, as measured by the Bloomberg Barclays U.S. Aggregate Bond Index.

Finally, outside of the taxable bond market, municipal bonds held up relatively well, posting modest increases across most maturities as investor demand for tax-exempt income remained high.

Satellite Strategies

As market fear climbed, gold was the big winner during the fourth quarter, gaining 7.2% as measured by the S&P GSCI Gold Index. Outside of gold, losses were seen across the investment landscape. Hardest hit were MLPs which cratered under the weight of falling oil prices, tax-loss selling, and general market anxiety. For the year, performance dispersion was wide, but there were very few areas that avoided negative territory.



Source: Morningstar Direct, Welch Hornsby, Inc. - Emerging Mkt Equity: MSCI EM Index (\$); Global High Yield: Barclays Global High Yield TR (\$); MLPs - Alerian MLP TR (\$); Emerging Market Debt - JPM EMBI Global Diversified TR (\$); Int'l Small Cap: S&P Developed Ex US Small TR (\$); Gold - S&P GSCI Gold (\$)



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