

Notable 2Q Market Performance

	S&P 500 (Large Cap Stocks)	MSCI EAFE (International Developed Stocks)	MSCI Emerging Markets (EM Stocks)	Barclays Aggregate (Bonds)	10-Year Treasury (Bonds)	HFRI Hedge Fund Composite (Hedge Funds)	USD	WTI Crude Oil
2Q Return	3.43%	-0.97%	-7.86%	-0.16%	-0.28%	0.85%	5.00%	14.18%
YTD Return	2.65%	-2.37%	-6.51%	-1.62%	-2.67%	0.79%	2.55%	22.72%

2Q 2018 Market Commentary

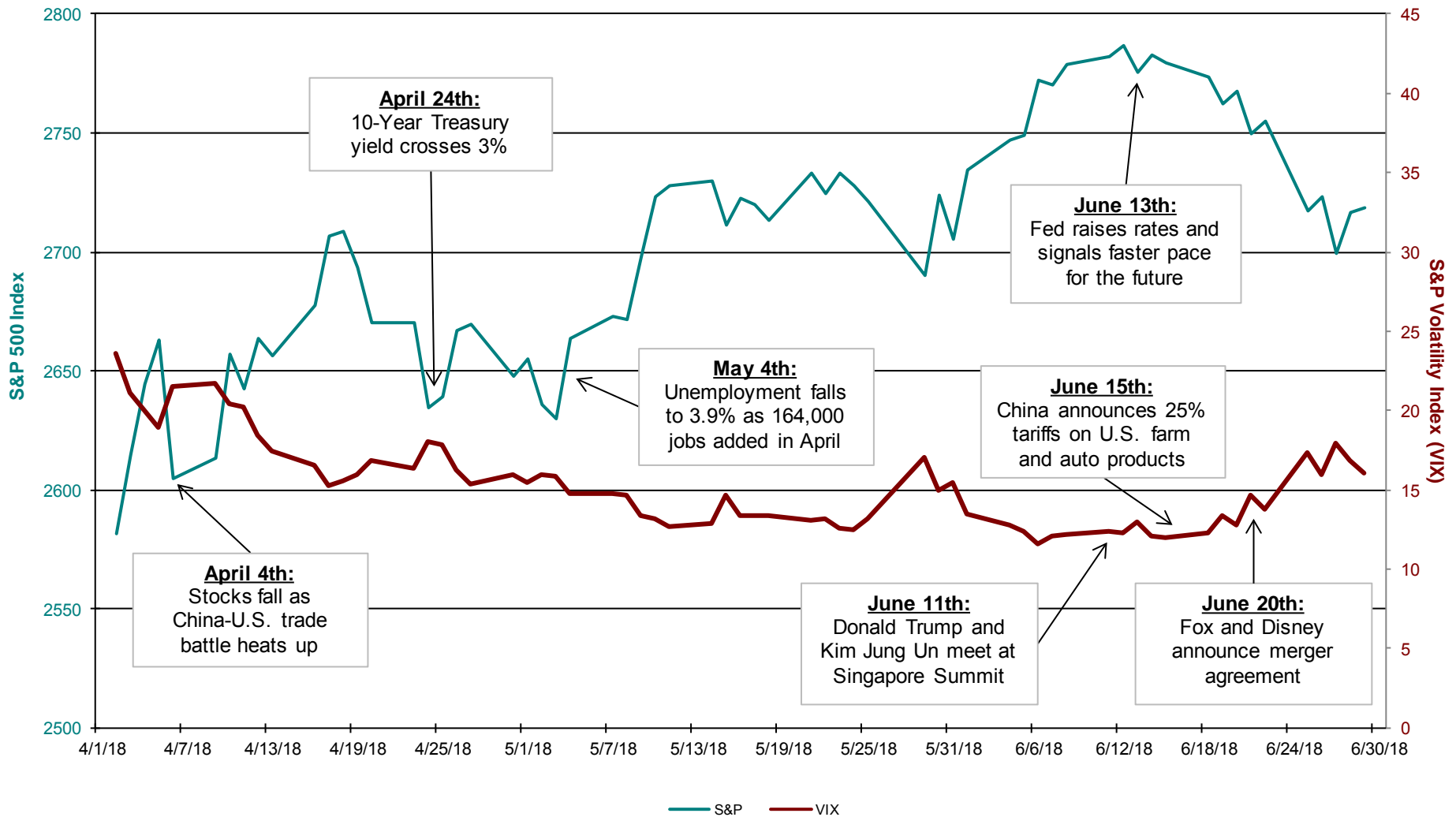
Non-U.S. risk assets lurched downward in June as fears of a protracted and pronounced trade war intensified. The Shanghai Composite index fell more than 20% from its 2-year high reached in late January. European stocks and bonds also declined as concerns that its fragile recovery could be overtaken by the region's significant exposure to international trade. In the US, where the business recovery continued apace, stocks made further advances, particularly shares of small cap companies that are less sensitive to trade-related actions.

The yield on the 10-year Treasury rose for the fourth consecutive quarter, briefly topping 3% before concerns about mounting trade tensions and slower global growth drove investors to the relative safety of government debt. Signs that inflation could accelerate, continued job gains for US workers and speculation that the Federal Reserve might raise rates four times this year, helped boost the yield to nearly a 7-year high of 3.11% in mid-May. Not surprisingly, the dollar strengthened 5% against its 16-currency basket. The rise in rates and the attendant gains in the dollar amplified struggles in the emerging markets as global investors began shifting assets away from developing markets to safer, higher yielding options. Countries that issue debt in dollars feel the brunt of rising yields since the dollar often rises in tandem with Treasury yields. The nascent trade war between the US and China exacerbates this trend and has likewise roiled most commodities. An important exception is oil. WTI crude soared 14% in Q2 as geopolitics weighed on supply, helping to drain inventories.

Domestic stocks still appear moderately attractive given reasonable valuations, strong earnings momentum and continued support in the form of loosening regulations, pro-business tax reform and the growing utilization of share buybacks in the face of excess corporate cash. Yes, the economy has become tighter as exemplified by the US jobless rate which fell to a 17-year low of 3.8% in May. But new entrants to the workforce — 213k joined in June — could help fuel ongoing growth for some time. And while market sentiment has become warier, we do not believe that the onset of a recession is approaching in the next year. Globally, the synchronized expansion is grinding down and we expect a more differentiated path for sub-markets. The risks for emerging markets have intensified a bit as have those for Europe with Chancellor Merkel's position weakening and Brexit-related concerns reentering the discussion.

In light of the opportunities and concerns discussed above, we are adjusting our model portfolio to modestly overweight US stocks and to underweight emerging markets equity while, to a lesser extent, lowering exposure to developed international stocks. With rates still likely to increase and with corporate credit spreads tight, fixed income is not yet a compelling investment. However, income-driven private lending to small-to-midsized companies remains attractive as long as the underwriting is disciplined and rigorous. Cash and very low duration bonds are viable holdings particularly now that the short end of the curve has made a meaningful move.

U.S. Stocks Recovered from the First Quarter Decline as the S&P 500 Finished +3.4% for the Quarter and +2.7 YTD; Fear of Trade War Continues to Loom



Source: Bloomberg, WSJ.com.

Domestic Capital Markets Snapshot: Small Caps Outperformed

U.S. Equity (S&P 500 +3.43%)

	Value	Blend	Growth
Large Cap	1.18	3.57	5.76
Mid Cap	2.41	2.82	3.16
Small Cap	8.30	7.75	7.23

U.S. Fixed Income (Barclays Agg -0.16%)

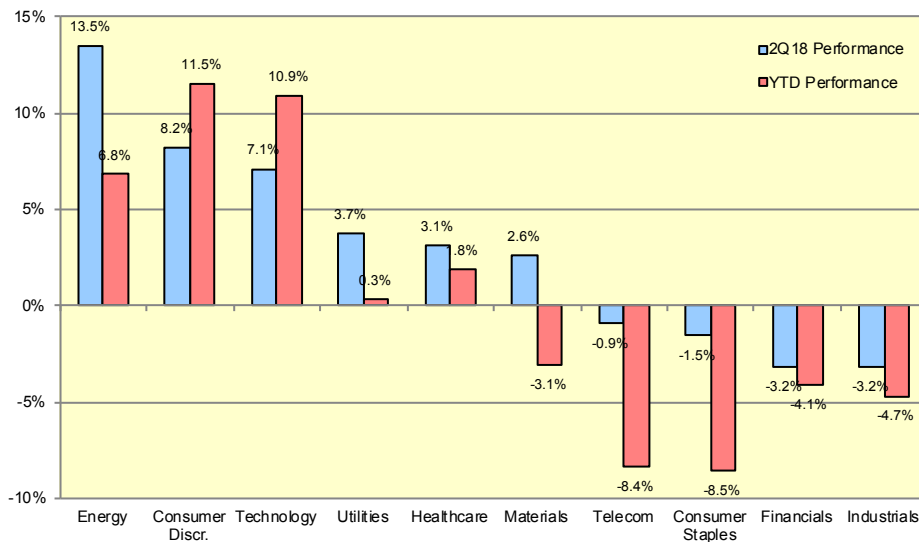
	Short Term	Intermediate	Long Term
Treasuries	0.21	0.06	0.31
Corporate	0.42	(0.08)	(2.65)
High Yield	N/A	1.10	(0.23)

Top Sectors

Bottom Sectors

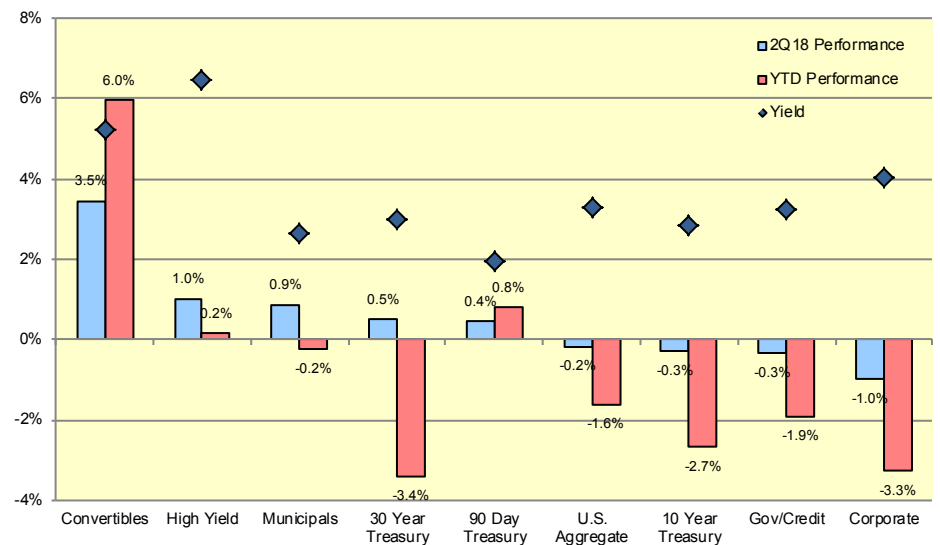
Source: Bloomberg; Barclays

S&P Sector Performance



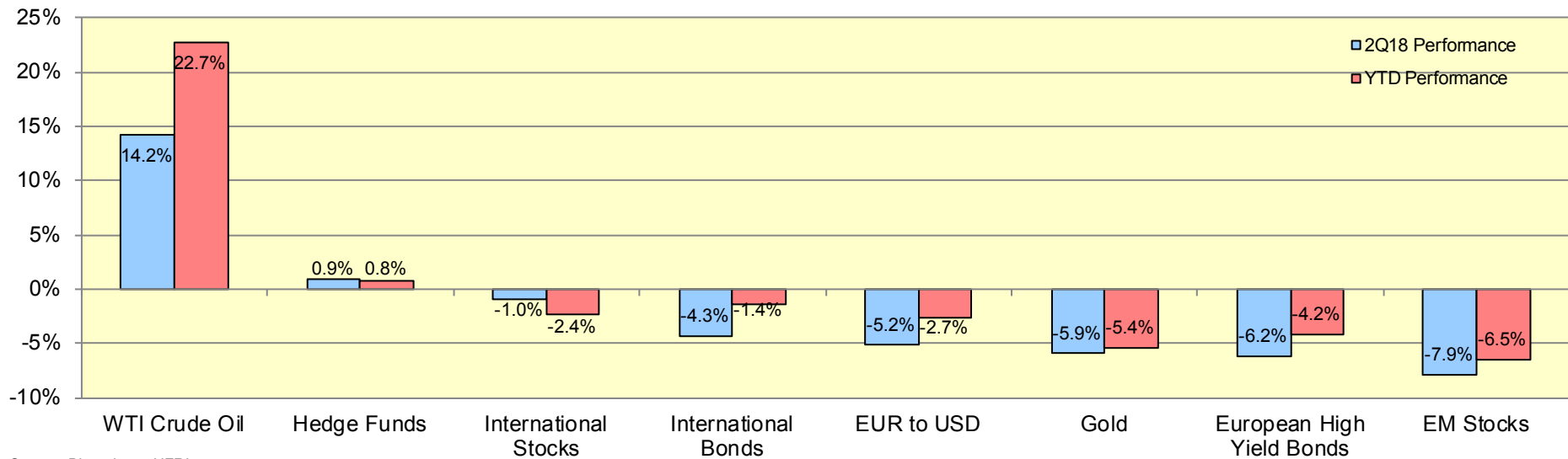
Source: Bloomberg

Domestic Fixed Income Performance



Source: Bloomberg, JP Morgan.

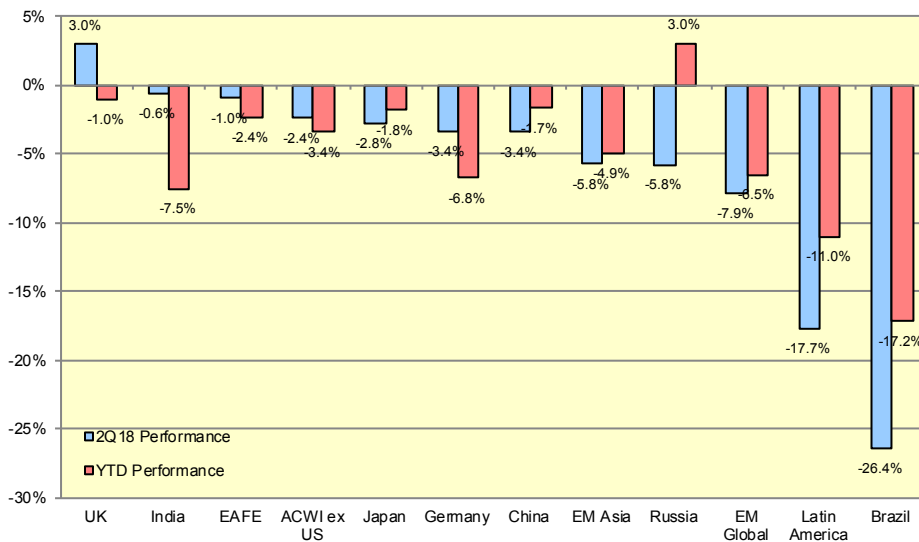
International Capital Markets Snapshot: Emerging Markets Underperformed



Source: Bloomberg, HFRI.

Note: All returns in USD.

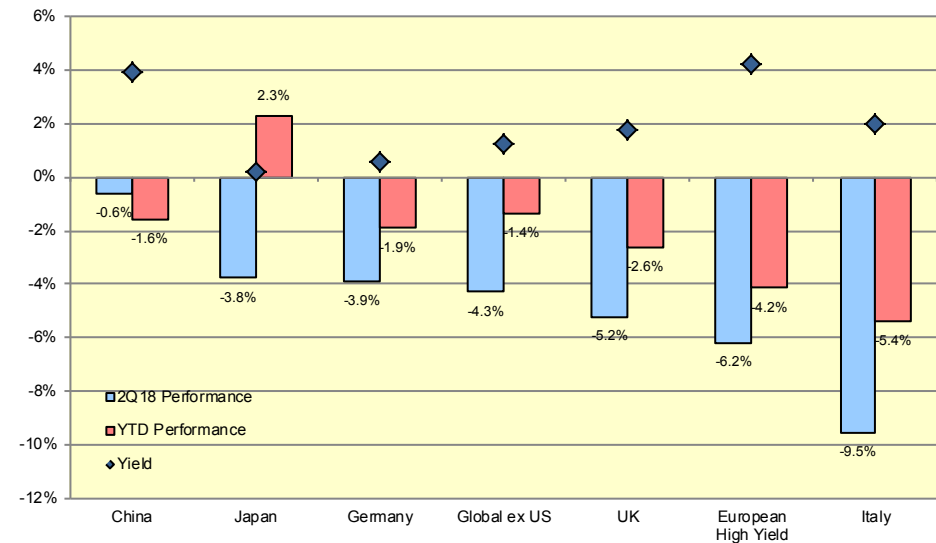
International Equity Performance



Source: Bloomberg

Note: All returns in USD.

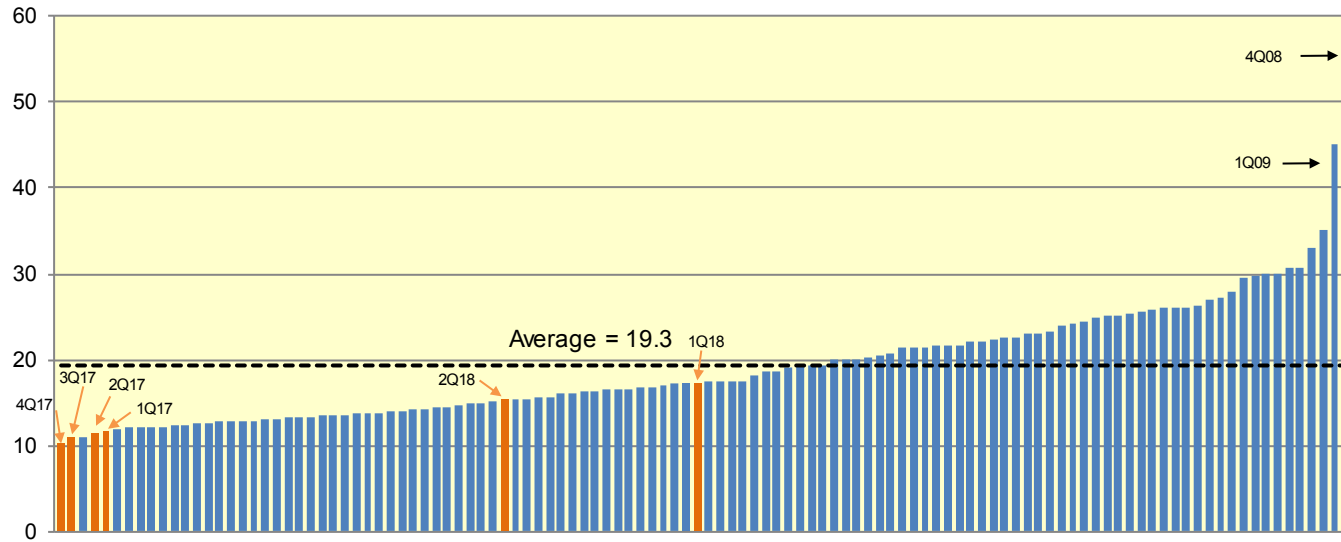
International Fixed Income Performance



Source: Bloomberg, JP Morgan. Country returns and yields represent those of Aggregate indices.

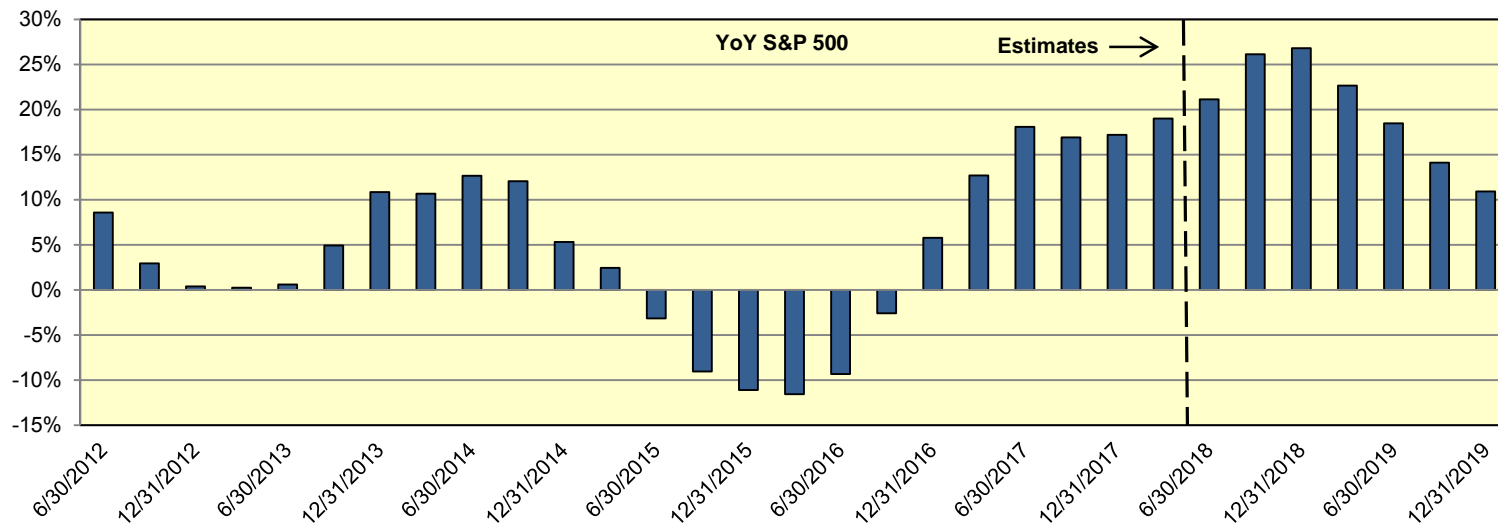
Note: All returns in USD.

Volatility Has Returned to Normal Levels...



Note: Data dates back to inception of the VIX (1Q 1990).
Source: Cambridge, Bloomberg.

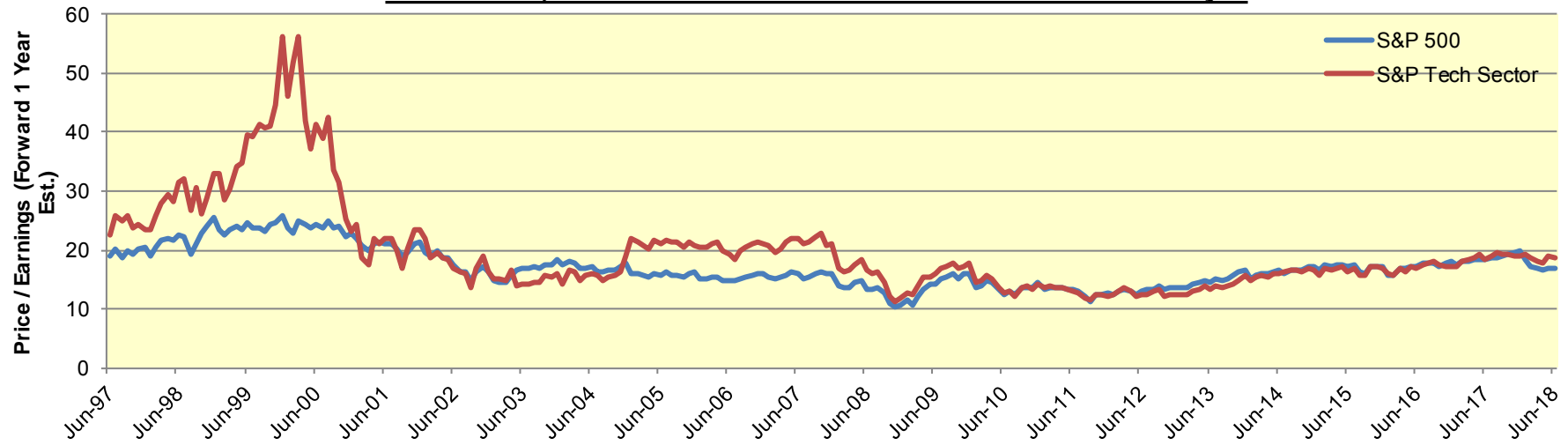
...And Earnings Should Continue to Grow Heading into 2019



Source: S&P Dow Jones Indices.

Tech Bubble Round Two? The Numbers Say Otherwise

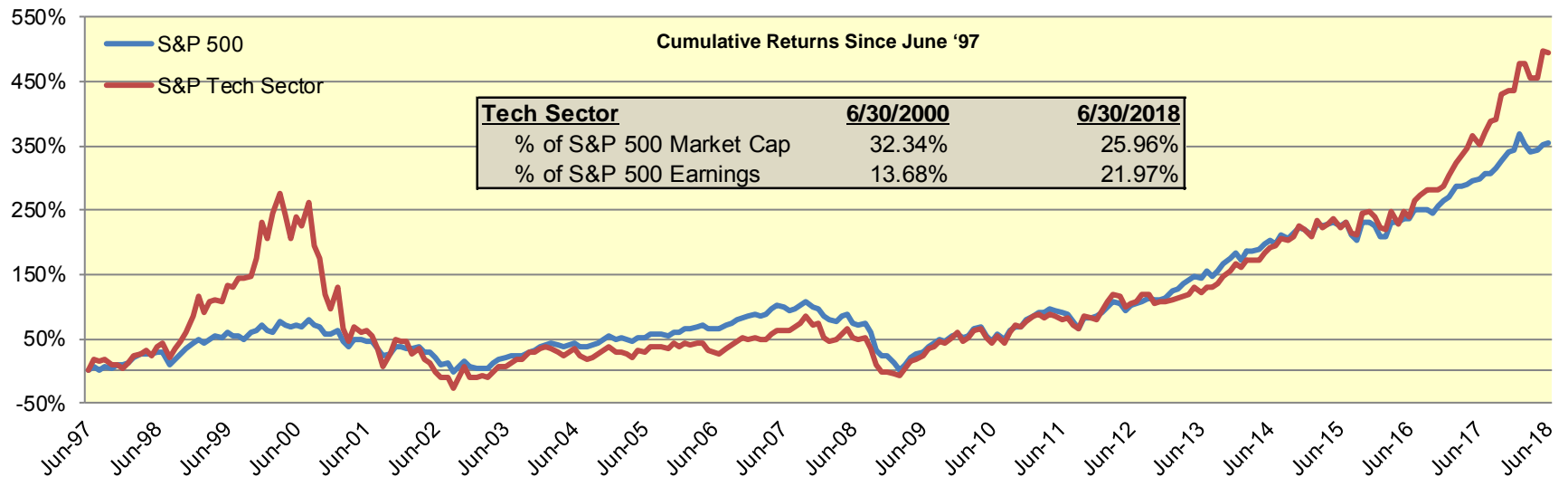
Unlike 2000, Tech Valuations are In Line with the Market Today...



Note: Excludes negative earnings.

Source: Bloomberg.

...As are Representative Earnings Even While the Tech Sector Outperforms



Source: Bloomberg, S&P Dow Jones Indices.

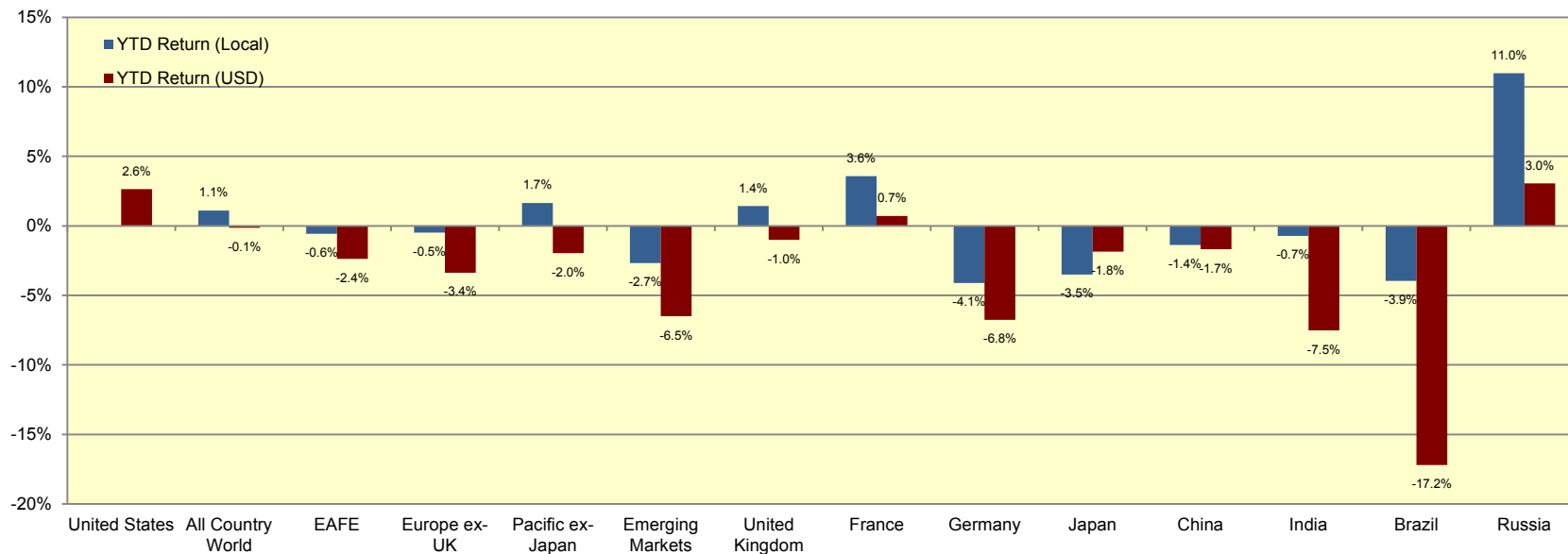
The Dollar Began to Strengthen During the Second Quarter...



Note: Adjusted for inflation. The US Dollar Index is comprised of a basket of currencies of the trading partners of the United States.

Source: BIS.

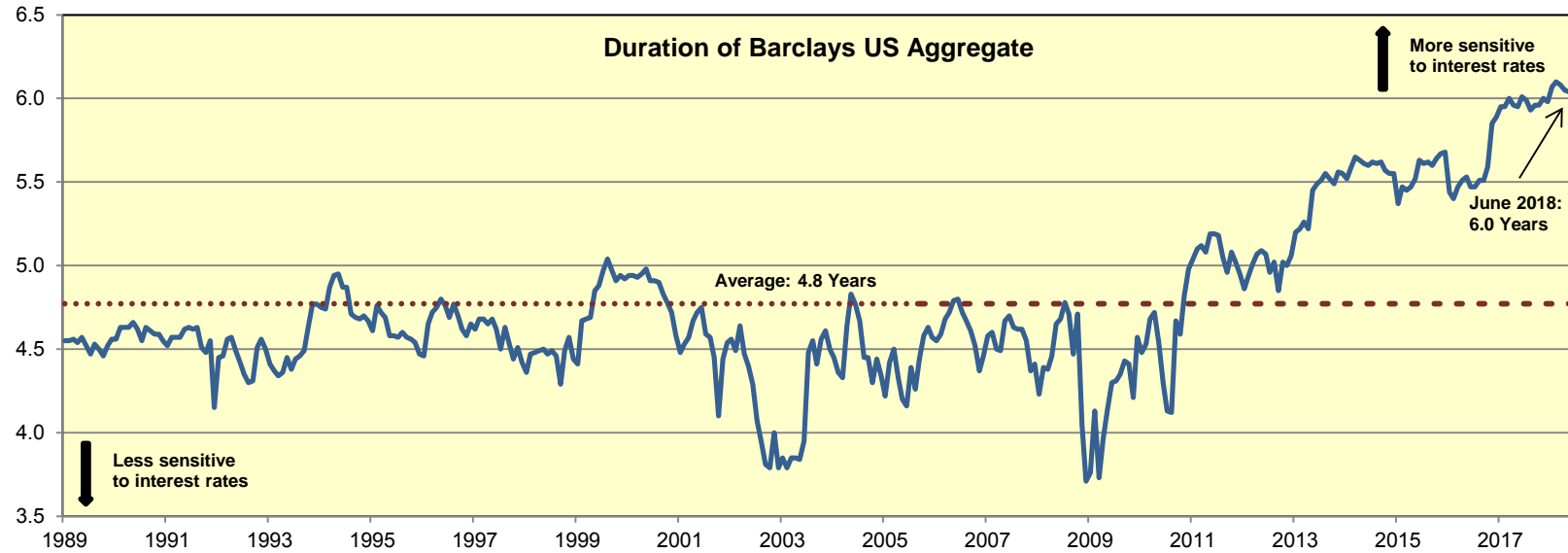
...One of the Reasons For Disappointing International/Emerging Market Returns



Source: Bloomberg, JP Morgan.

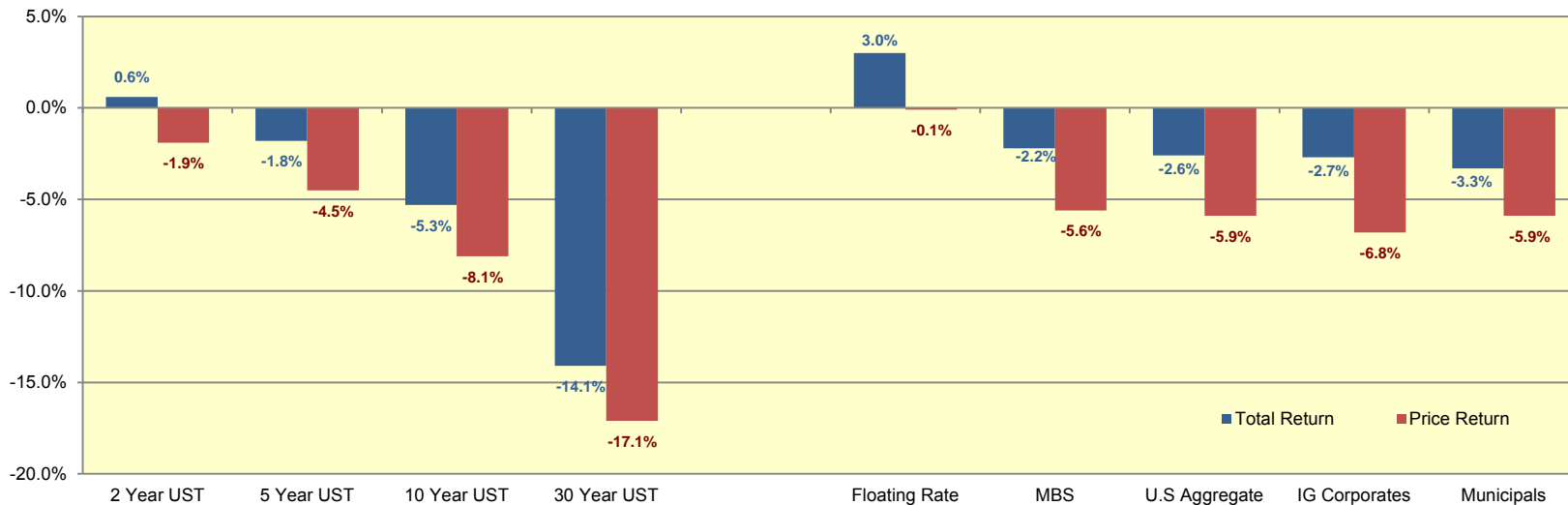
As Interest Rates Continue to Rise, Bonds Become Less Attractive

Interest Rate Sensitivity Remains at an Elevated Level



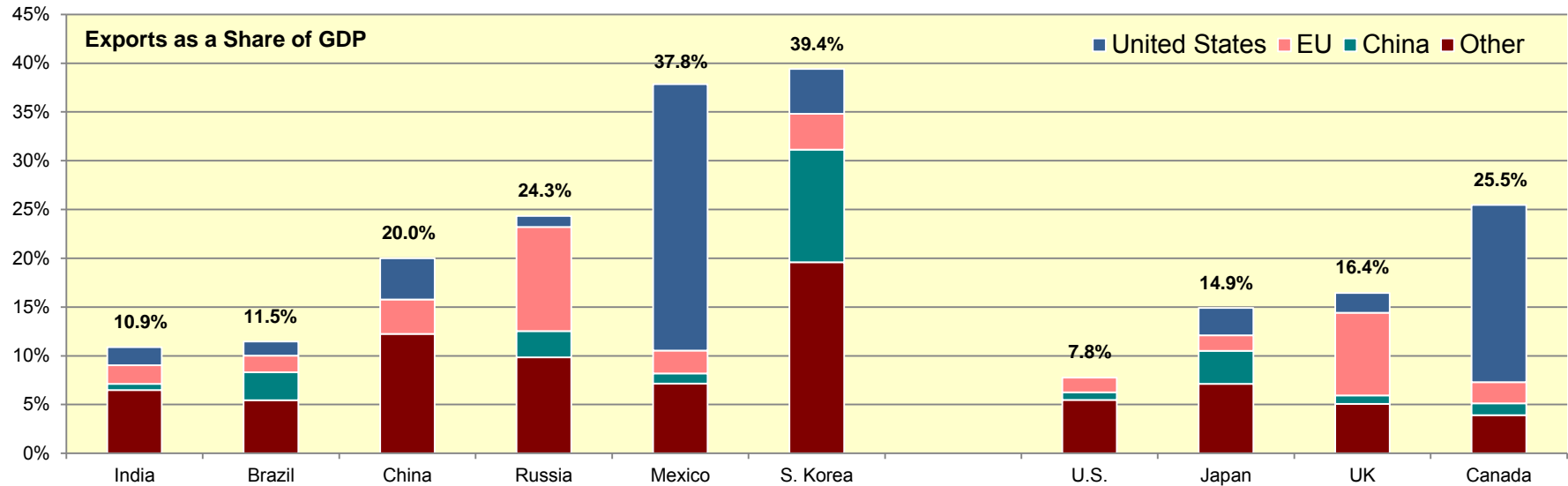
Source: Bloomberg, JP Morgan.

Bonds Don't Appear to be a Safe Bet in the Current Environment



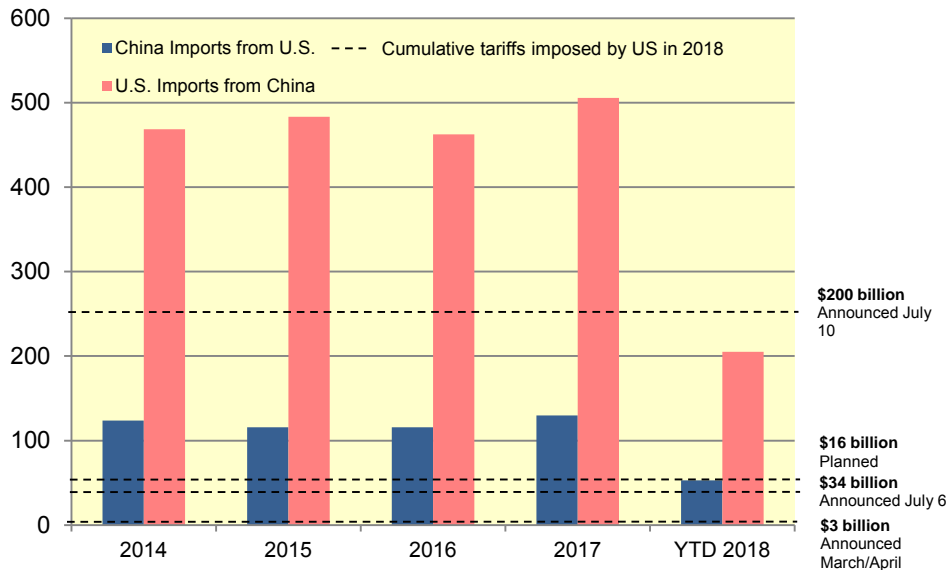
Source: JP Morgan.

On a Relative Basis, the US Trails in the Export Industry



Note: Data as of December 2017.
Source: Bloomberg, IMF, JP Morgan.

The US Has Out-Tariffed China—What Is China's Next Move?



Source: US Census Bureau, WSJ.

Small Cap Stocks Have Less Exposure to the Perils of a Trade War



Source: Bloomberg, WSJ.

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Past Performance is No Guarantee of Future Results