MARKET COMMENTARY & OUTLOOK

Third Quarter, 2018

LAMCO

LAMCO ADVISORY SERVICES, INC.

Major Themes

As we move towards the end of the year there are a few major themes playing out on the world stage that will drive markets in the short term and shape longer term results:

1. Increasing short-term U.S. Interest rates and the general shift toward global quantitative tightening
2. Tariffs/trade
3. International relations (North Korea, China, Iran, Turkey, EU, Saudi Arabia, etc.)
4. Brexit

Economic Statistics

	Current	One Year Ago
Real GDP Growth (Annl. % Change From Prior Qtr.)	3.00%	2.34%
Unemployment Rate	3.70%	4.20%
Labor Force Participation Rate	62.70%	63.00%
Core CPI (Year-Over-Year)	2.17%	1.70%
Real Personal Income Growth (Year-over-Year)	2.39%	2.93%
10 Year Treasury Rate	3.00%	2.20%

Data Source: Federal Reserve, LAMCO Advisory

Economy

As the economy continued its second longest expansion in U.S. history, there are indicators that show growth can continue through the remainder of this year and into 2019. Household debt is in much better shape than it was at the start of the Great Recession. Housing starts have recovered over a longer historical perspective (i.e., over the last 10 years) and appear stable around long-term averages. More recent data show they have flattened and new starts have tapered off, but they are currently hovering around long term averages. Prices however were still trending upward over the last several years. Additionally, manufacturing and corporate earnings are strong. Unemployment is at the lowest level since 1969 and wage growth continues to trend higher, albeit at a much slower pace than job growth.

While there are a lot of positives, there are areas of concern which bear consideration. The Federal deficit level which has grown by 17% in 2018 calling into question the aggressive fiscal policy enacted during the later stages of the economic expansion. Historically, sound tenets of economic policy would dictate that such action should have come earlier in the downturn. Current deficit levels at this stage are unprecedented.

U.S. retail sales started to show signs of some weakness toward the end of the third quarter by increasing less than expected, 0.1% vs. expected 0.7%. However, the impact from Hurricane Florence, which hit mid-September, seems to have weighed negatively on the numbers. Vehicle sales, while volatile during the quarter ended on a strong note at 17.4 million, which was above the long-term average of 15.7.

Consumer prices remain in check for the most part, helped by a stronger dollar and declining energy prices. Although we are seeing some upward price pressure, inflation is still running at about 2.3%. This is slightly ahead of the Fed target of 2%, but the Fed has indicated they are willing to let inflation run for a “temporary period” ahead of target.

Rising oil prices continue to be a major focus in the commodity space. U.S. sanctions against Iran are scheduled to take full effect in November and may impact prices, but U.S. inventories are at their highest in more than 18 months which should dampen any near-term effects.

Trade/Tariffs

Trade tensions with Mexico, Canada and Europe have showed signs of easing yet tensions with China show no sign of letting up. Clearly trade wars in the historical sense are generally not a good thing. While U.S. trade tensions on multiple fronts and the current tariff battle is a stress on markets, it has not yet flourished into what we would classify as a global trade war. Generally, to date, the tariffs and trade disruptions we have seen have had an impact on supply chains, rattled confidence and put pressure on prices of various goods, both domestically and internationally.

Additionally, during the quarter, we saw the North American Free Trade Agreement (NAFTA) effectively come to an end. It has been essentially replaced with the U.S.-Mexico-Canada Agreement or USMCA. Indications are that the roughly $1.2 trillion in trade between the partners will not change dramatically. Overall, the U.S. should see a boost to manufacturing and jobs as a result.

US Equity Market

Observations

- The third quarter equity markets continued to plow forward with the S&P 500 generating nearly an 8% return. That strong showing by stocks helped propel the year-to-date return to 10.6%.
- Small cap stocks couldn't keep pace during the quarter, but have fared better on a year-to-date basis, returning 11.5%.
- Growth stocks continue to outperform value stocks by a wide margin; however, valuations on the growth side have become more expensive and less attractive than their value counterparts. Overall though, even with the run the stock market has experienced, it is still somewhat fairly valued by forward P/E values based on the last 25 years. As an interesting side note, during the third quarter the current bull market run in the US stock market became the longest in history.
- Though markets have been volatile into the fourth quarter, we expect the momentum from the third quarter to carry forward as we move toward the end of the year.
- Fiscal stimulus from tax cuts and deregulation continue to outweigh slowing pressure from rising interest rates and mild increases in inflation.
- Corporate earnings continued to be robust with intense stock buybacks in play, putting further upward pressure on stock prices. Although earnings may begin to decelerate, they should remain positive through year end.
- From a sector perspective, consumer discretionary, technology and healthcare stocks have been major drivers of returns year-to-date for the period ended September 30.

Major US Market Averages

	Q3 2018	YTD	1 Year	3 Year	5 Year	2017	2016	2015
Russell 3000 Index	7.1%	10.6%	17.6%	17.1%	13.5%	21.1%	12.7%	0.5%
FTSE RAFI US 3000 Index	5.9%	6.7%	13.6%	15.6%	12.0%	16.2%	18.1%	-2.7%
Russell 3000 Equal Weighted	3.1%	10.3%	14.5%	17.3%	11.0%	15.6%	21.6%	-6.2%
S&P 500 Index	7.7%	10.6%	17.9%	17.3%	14.0%	21.8%	12.0%	1.4%
Russell Mid Cap Index	5.0%	7.5%	14.0%	14.5%	11.7%	18.5%	13.8%	-2.4%
Russell 2000 Index	3.6%	11.5%	15.2%	17.1%	11.1%	14.7%	21.3%	-4.4%
NASDAQ 100	8.6%	20.2%	28.9%	23.6%	20.3%	33.0%	7.3%	9.8%

Russell 3000 Style & Cap Summary

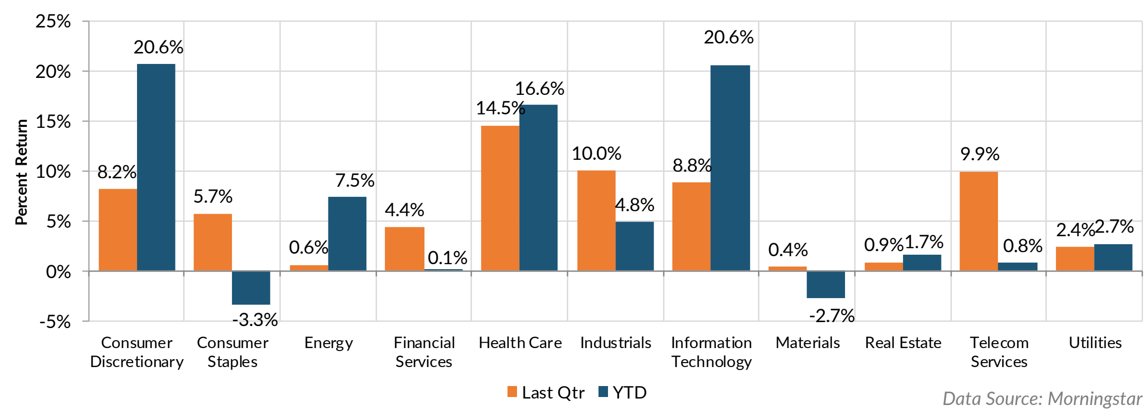
Third Quarter Results

	Mo.	Qtr	Value		Core		Growth	
Large	July		4.59%		3.83%		3.17%	
	Aug	Q3	1.54%	6.94%	3.58%	8.38%	5.38%	9.64%
	Sep		0.69%		0.78%		0.85%	
Mid	July		2.72%		2.49%		2.15%	
	Aug	Q3	1.36%	3.30%	3.11%	5.00%	5.76%	7.57%
	Sep		-0.79%		-0.64%		-0.43%	
Small	July		1.77%		1.74%		1.72%	
	Aug	Q3	2.38%	1.60%	4.31%	3.58%	6.23%	5.52%
	Sep		-2.48%		-2.41%		-2.34%	

Year To Date Results

	Value	Core	Growth
Large	4.36%	11.69%	18.23%
Mid	3.13%	7.46%	13.38%
Small	7.14%	11.51%	15.76%

S&P 500 Sector Performance



Data Source: Morningstar

US Equity Market

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Dividend Yield [a]

	Avg. Weight %	Return %	Contribution to Return %
Dividend Yield [0.48 - 1.70)	25.55%	10.19%	2.59%
Dividend Yield [1.70 - 2.72)	27.21%	7.79%	2.13%
Dividend Yield [0.00 - 0.48)	21.25%	7.64%	1.63%
Dividend Yield [2.72 - 33.58]	25.59%	5.24%	1.37%
Attribution Total	**99.60%**		**7.71%**

*Avg. Weight excludes cash (0.29%)

Capitalization [a]

	Avg. Weight %	Return %	Contribution to Return %
Mega Cap (>$85 Billion)	45.30%	9.72%	4.37%
Large Cap ($18 Billion -$85 Billion)	28.89%	6.22%	1.82%
Mid Cap ($3 Billion - $18 Billion)	18.05%	4.48%	0.82%
Small Cap ($700 Million - $3 Billion)	6.42%	2.69%	0.17%
Micro Cap (< $700 Million)	0.07%	0.85%	0.00%
Unclassified	0.98%	-5.42%	-0.06%
Total	**99.71%**		**7.12%**

Valuation [a]

	Avg. Weight %	Return %	Contribution to Return %
Fairly Valued	39.19%	11.64%	4.50%
Overvalued	17.94%	10.31%	1.85%
Undervalued	42.36%	3.12%	1.35%
Unclassified	0.11%	14.40%	0.01%
Attribution Total	**99.60%**		**7.71%**

*Avg. Weight excludes cash (0.29%)

(a) = ishares Russell 3000 ETF
(b) = SPDR S&P 500 ETF

Data Source for all data in tables: Morningstar Direct

Top Weights [b]

	Weight	Return	Contribution
Apple Inc	4.20%	22.38%	0.88%
Microsoft Corp	3.43%	16.43%	0.54%
Amazon.com Inc	3.12%	17.84%	0.53%
Facebook Inc A	1.80%	-15.37%	-0.31%
Berkshire Hathaway Inc B	1.63%	14.71%	0.23%
JPMorgan Chase & Co	1.59%	8.88%	0.14%
Alphabet Inc Class C	1.50%	6.98%	0.10%
Alphabet Inc A	1.49%	6.90%	0.10%
Johnson & Johnson	1.47%	14.63%	0.21%
Exxon Mobil Corp	1.43%	3.83%	0.06%

Top Contributors [b]

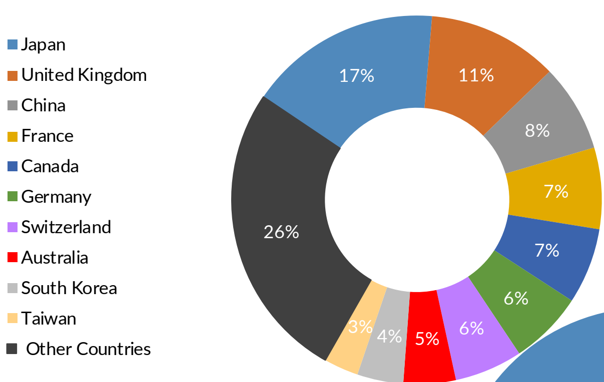
	Weight	Return	Contribution
Apple Inc	4.20%	22.38%	0.88%
Microsoft Corp	3.43%	16.43%	0.54%
Amazon.com Inc	3.12%	17.84%	0.53%
Berkshire Hathaway Inc B	1.63%	14.71%	0.23%
Pfizer Inc	0.98%	22.51%	0.21%
Johnson & Johnson	1.47%	14.63%	0.21%
Visa Inc Class A	1.05%	13.49%	0.14%
JPMorgan Chase & Co	1.59%	8.88%	0.14%
Merck & Co Inc	0.74%	17.67%	0.13%
Cisco Systems Inc	0.87%	13.94%	0.12%

Top Detractors [b]

	Weight	Return	Contribution
Facebook Inc A	1.80%	-15.37%	-0.31%
General Electric Co	0.46%	-16.26%	-0.08%
Wells Fargo & Co	1.03%	-4.50%	-0.05%
Twitter Inc	0.10%	-34.83%	-0.04%
Intel Corp	0.94%	-4.29%	-0.04%
Micron Technology Inc	0.24%	-13.75%	-0.04%
Schlumberger Ltd	0.37%	-8.38%	-0.03%
Netflix Inc	0.65%	-4.42%	-0.03%
Applied Materials Inc	0.18%	-15.93%	-0.03%
General Motors Co	0.19%	-13.60%	-0.03%

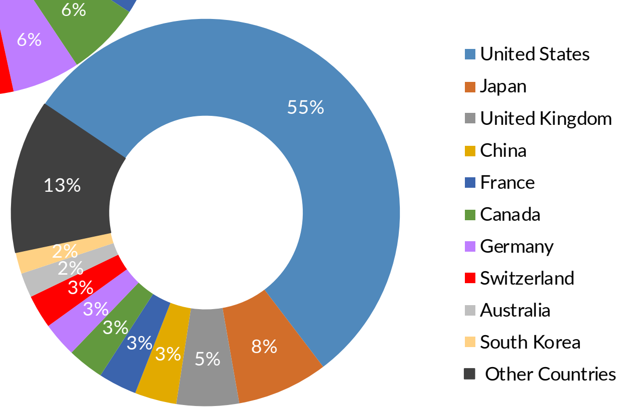
Observations

Europe has had a weak showing this year, down around 2.5%. However, projected GDP growth for the year remains slightly above 2%, driven in large part by consumers. The most critical point, from an economic perspective in Europe, continues to center around Brexit. With talks continuing to stall between the UK and EU, focus has been on establishing a backstop, but no one can seem to agree on how it will work. The backstop is essentially a safety net to ensure that, no matter what happens with the UK/EU – deal or no deal - there won't be restrictions (i.e., boarder checks and restrictions) in Ireland. The deadline for Brexit as a whole, between the UK and the EU is set for March 29, 2019. Failure to come to a resolution would be troublesome to say the least for Europe as a whole, but especially for the UK economy. China, while dealing with trade pressure with the U.S., has also been intentionally slowing it's economy in an effort to move towards a more consumer driven structure. The World Bank expects China's growth rate will moderate to a 6.5% rate this year and then slow further to 6.3%. In 2017, China's GDP growth was 6.9%. Markets are more interconnected on a world scale than ever before and gradual increases in U.S. interest rates are tightening financial conditions globally. This has been particularly evident in emerging markets where higher US rates create an environment of competition for capital. Emerging markets have been in a selloff mode for 2018. Year-to-date through September 30, EM lost 7.7% as measured by the MSCI EM Index. However, the pullback has made valuations in the space very attractive. With continued strong fundamentals, EM presents unique opportunities, particularly in Asia, for skilled investment managers.



Country Weights

MSCI All Country World Index (Ex. USA)



MSCI All Country World Index

Data Source: Morningstar and iShares ETFs as the representative index proxies. Weights are average for Q4.

International Equity Market Performance

	Q3, 2018	YTD	1 Year	3 Year	5 Year
MSCI EAFE	1.42%	-0.98%	3.25%	3.25%	3.25%
MSCI EAFE Value	1.26%	-2.95%	0.24%	0.24%	0.24%
MSCI EAFE Growth	1.57%	0.95%	6.27%	6.27%	6.27%
MSCI EM	-0.95%	-7.39%	-0.44%	-0.44%	-0.44%
MSCI ACWI Ex. USA.	0.80%	-2.67%	2.25%	2.25%	2.25%

	Last Quarter			Year To Date		
	Local	USD	Impact Of US Dollar [a]	Local	USD	Impact Of US Dollar [a]
MSCI ACWI Ex USA	1.63%	0.80%	-0.83%	0.70%	-2.67%	-3.37%
MSCI Europe	1.24%	0.84%	-0.40%	1.33%	-1.89%	-3.22%
MSCI Europe Ex UK	1.88%	1.83%	-0.05%	1.40%	-1.60%	-3.00%
MSCI United Kingdom	-0.43%	-1.65%	-1.22%	0.99%	-2.65%	-3.64%
MSCI Pacific Ex Japan	0.66%	-0.53%	-1.19%	2.32%	-2.49%	-4.81%
MSCI Japan	6.46%	3.81%	-2.65%	2.74%	1.89%	-0.85%
MSCI France	3.41%	2.87%	-0.54%	7.11%	3.60%	-3.51%
MSCI Switzerland	5.55%	7.30%	1.75%	1.05%	0.81%	-0.24%
MSCI Germany	-0.05%	-0.57%	-0.52%	-4.16%	-7.29%	-3.13%
MSCI Canada	-0.78%	0.98%	1.76%	1.40%	-1.71%	-3.11%
MSCI China	-7.56%	-7.42%	0.14%	-8.84%	-8.98%	-0.14%
MSCI India	3.42%	-2.25%	-5.67%	2.67%	-9.60%	-12.27%
MSCI Brazil	10.21%	6.17%	-4.04%	5.86%	-12.07%	-17.93%
MSCI Russia	10.69%	6.60%	-4.09%	22.83%	9.84%	-12.99%

Assumes Gross Reinvestment Of Dividends

Data Source: Morningstar

(a) Impact of Dollar: For a US investor, a strengthening dollar has a negative impact on non-US asset returns when converted to US dollars since the conversion requires more of a foreign currency to purchase the more expensive US dollar. A weakening dollar has the opposite effect; the foreign currency can buy more US dollars.

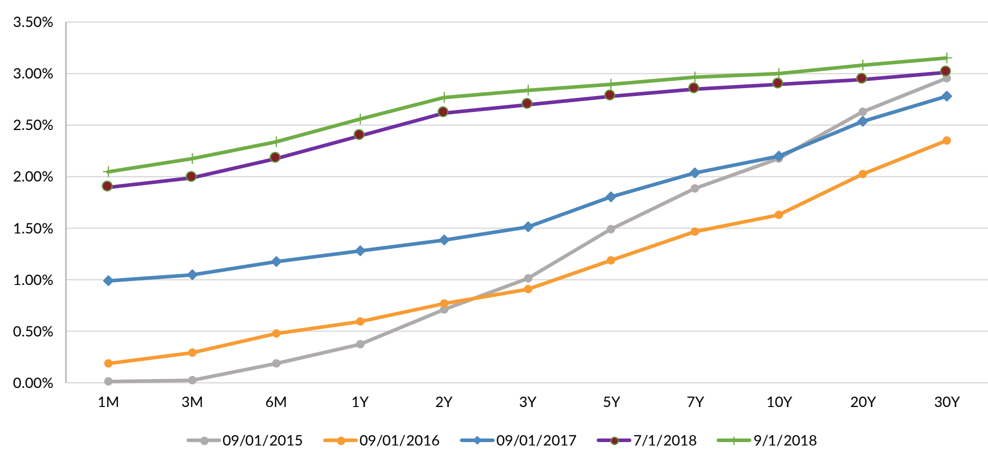
Observations

Indications are the Fed will continue to lift short term rates with a further rate increase this December and then again in March and June of 2019, unless the economy changes in a material way. At this expected pace, that would place the federal funds rate in a range between 2.75% and 3% by the middle of next year.

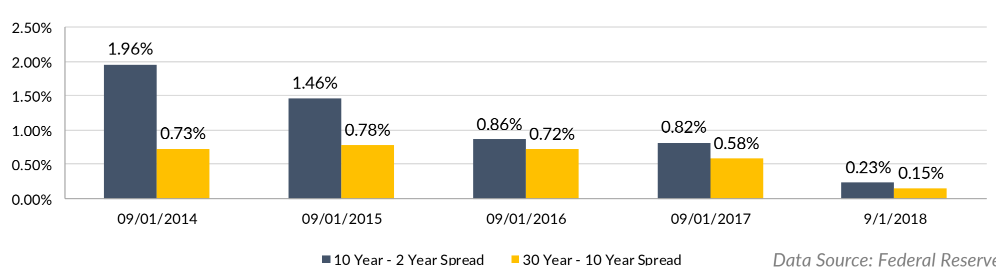
For bond investors, the focus has been on the yield curve and the risk of increasing short-term rates are having on its slope. Historically, an inverted slopping yield curve (where short-term interest rates are higher than long term rates) has been a precursor to economic recession. It is also important to note that the current environment of uncertainty around inflation pressures and the degree of economic growth is putting upward pressure on the long end of the curve. While the Fed has a fair amount of control over short term interest rates, long term rates are more a function of market forces. If long term rates continue to increase, and depending on the magnitude, we could see that have a negative effect on housing, as well as the stock market - something we will be watching closely.

High yield bonds have held up well so far in 2018 and typically do well in rising interest rate environments. However, they tend not to offer much this late in the credit cycle and yield spreads (i.e., difference in yield between high yield and treasury) are very tight.

Yield Curve



Spread Analysis



Data Source: Federal Reserve; LAMCO Advisory

Major Market Averages

	Q3, 2018	YTD	1 Year	3 Year
ICE BofAML US 3M Treasury Bill	0.49%	1.30%	1.59%	0.84%
Bloomberg Barclays US Govt/Credit 1-3 Yr	0.33%	0.41%	0.20%	0.73%
Bloomberg Barclays US Govt Interm	-0.11%	-0.78%	-1.18%	0.19%
Bloomberg Barclays US Govt/Credit Interm	0.21%	-0.76%	-0.96%	0.91%
Bloomberg Barclays US Govt/Credit	0.06%	-1.85%	-1.37%	1.45%
Bloomberg Barclays US Agg Interm	0.11%	-0.86%	-0.93%	0.95%
Bloomberg Barclays US Agg Bond	0.02%	-1.60%	-1.22%	1.31%
Bloomberg Barclays Global Agg Bond	-0.92%	-2.37%	-1.32%	1.98%
Bloomberg Barclays US Treasury	-0.59%	-1.67%	-1.62%	0.23%
Bloomberg Barclays US Treasury US TIPS	-0.82%	-0.84%	0.41%	2.04%
Bloomberg Barclays US Corporate IG	0.97%	-2.33%	-1.19%	3.12%
Bloomberg Barclays High Yield Corporate	2.40%	2.57%	3.05%	8.15%
Bloomberg Barclays Municipal	-0.15%	-0.40%	0.35%	2.24%
Bloomberg Barclays Municipal 7 Yr 6-8	-0.11%	-0.36%	-0.58%	1.61%

Credit Quality

B of A/Merril Lynch US Corporate AAA	0.11%	-3.11%	-1.45%	2.52%
B of A/Merril Lynch US Corporate AA	0.59%	-1.70%	-0.86%	2.21%
B of A/Merril Lynch US Corporate A	0.71%	-2.44%	-1.37%	2.50%
B of A/Merril Lynch US Corporate BBB	1.26%	-2.04%	-0.89%	3.99%
B of A/Merril Lynch US Corporate BB	2.36%	0.55%	0.89%	6.81%
B of A/Merril Lynch US Corporate B	2.41%	3.48%	3.87%	8.03%
B of A/Merril Lynch US Corp. CCC & Lower	2.85%	6.92%	7.70%	13.87%

Data Source: Morningstar

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