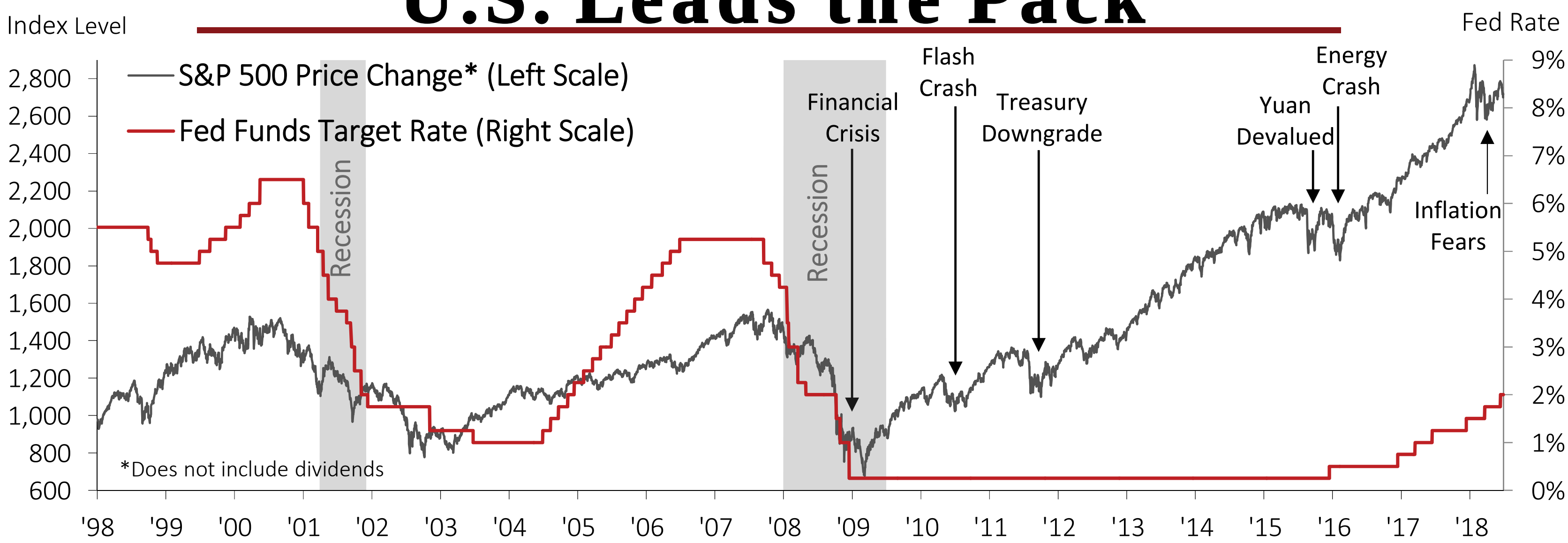
Capital Market Review

June 30, 2018

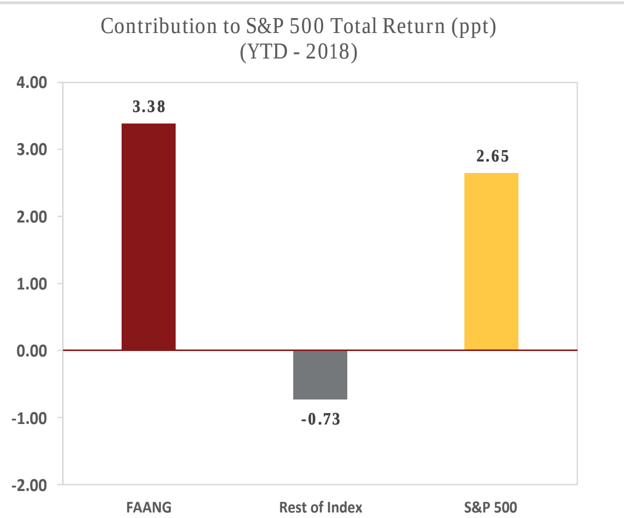



DeMarche

U.S. Leads the Pack

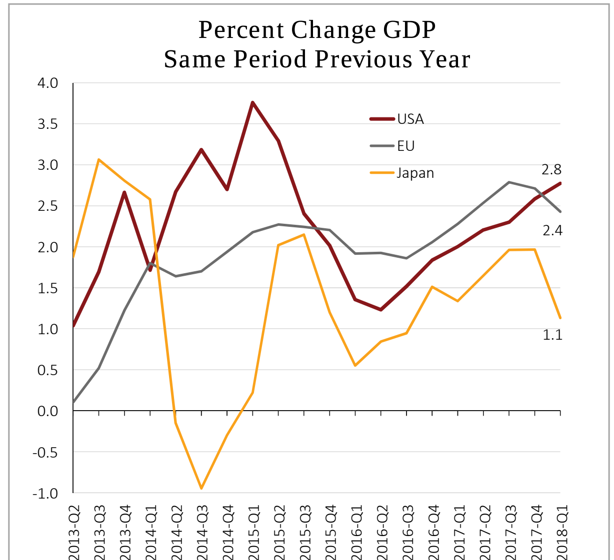


Source: Standard & Poor's, St. Louis Federal Reserve



Note: FAANG = FB, AAPL, AMZN, NFLX, GOOG/GOOGL
Source: S&P, BofA Merrill Lynch

U.S. stocks remained resilient this quarter and outperformed international stocks despite what looked like trouble brewing. However, the resiliency of the U.S. market has largely been driven by five stocks. As seen to the left, strong performance from Facebook, Amazon, Apple, Netflix, and Google propped the broader U.S. market into positive territory for 2018. Trade concerns have created daily headlines that have shaken markets worldwide. These concerns lead one to question the strength of global growth. And while the U.S. economy is steaming ahead, Europe and Japan are now underperforming growth expectations. The Fed continues tightening policy in response to U.S. economic growth.

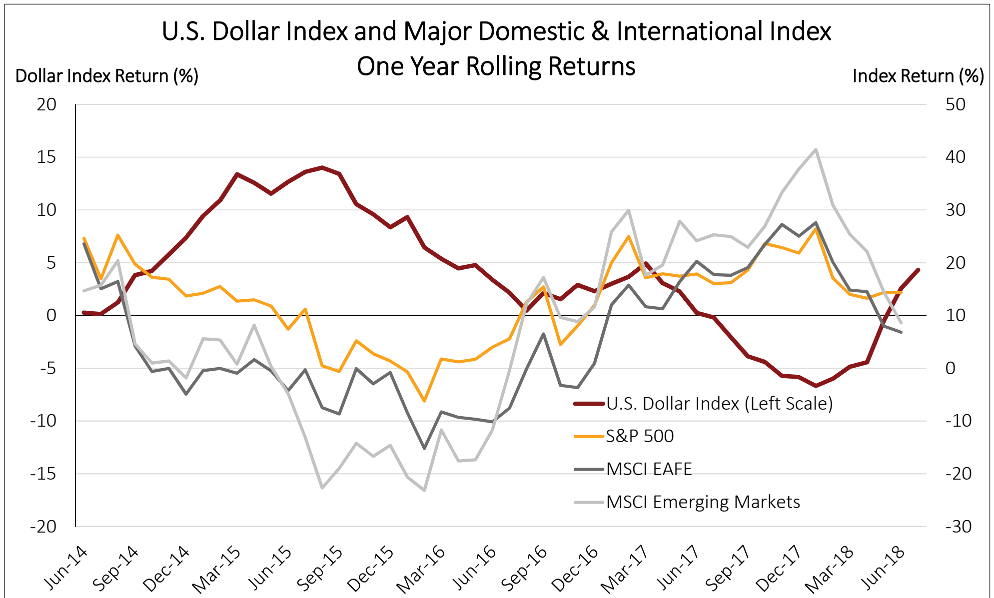


Source: OECD (Organisation for Economic Co-operation & Development)

INDEX	2nd Qtr	YTD	1-YEAR	3-YEAR	5-YEAR	10-YEAR
MSCI World	1.7	0.4	11.1	8.5	9.9	6.3
DeMarche World*	0.2	-0.5	9.4	7.9	9.5	5.9
DeMarche 3000	2.5	1.6	12.7	9.9	11.1	7.7
Russell 3000	3.9	3.2	14.8	11.6	13.3	10.2
S&P 500	3.4	2.6	14.4	11.9	13.4	10.2
DeMarche International	-2.6	-3.2	5.1	5.9	7.7	3.8
MSCI EAFE USD	-1.2	-2.7	6.8	4.9	6.4	2.8
BlmBarc Aggregate	-0.2	-1.6	-0.4	1.7	2.3	3.7
FTSE Non-US Gov't Bond	-5.1	-0.9	3.2	3.7	1.0	1.8
BlmBarc Global Aggregate	-2.8	-1.5	1.4	2.6	1.5	2.6
NCREIF (Private RE)	1.8	3.5	7.2	8.3	9.8	6.2
Bloomberg Commodity	0.4	0.0	7.3	-4.5	-6.4	-9.0

*Notes: Data are presented as percent returns. All 3, 5 and 10-year returns are annualized. *Does not include Canada or Brazil.*

Indicator Year Ending 6/30	2018	2017	2016	2015	50 Year Average
GDP Annual Growth Rate	2.8	2.1	1.3	3.3	2.8
Unemployment	4.0	4.3	4.9	5.3	6.2
Inflation (CPI)	2.9	1.6	1.0	0.1	4.1
10-Year Interest Rates	2.9	2.3	1.5	2.4	6.4



Source: Federal Reserve, S&P, MSCI

- The dollar strengthened against other currencies during the quarter in response to higher interest rates and good domestic GDP growth. At the beginning of the year, hopes for global growth continued in the wake of 2017's positive GDP expectations and international stocks outperforming the U.S. market. Despite the initial outlook, global growth is being reassessed while U.S. growth continues to chug along as the fed continues to increase rates.

- Stock returns were mixed in a jittery quarter. In stark contrast with U.S. stocks, International stocks continued to struggle, posting negative returns for both the quarter and the year to date. Trade tensions, a stronger dollar and slowing economic growth in developed markets were all contributing factors.

- Bond returns also struggled in the face of rising rates. Returns were negative again for the quarter. For the first time in five years, bond returns were negative for two quarters in a row (as measured by the Aggregate). Non-US bond returns were negatively impacted by the stronger dollar.

- The chart to the left shows the inverse relationship between the dollar and international returns. When the dollar strengthens (red line going up) the rolling returns of international stocks, while lagging, do show a negative trend. Interestingly, the return of the S&P 500 also tends to moderate when the dollar strengthens due primarily to the negative earnings impact of overseas revenues being translated into a stronger dollar.

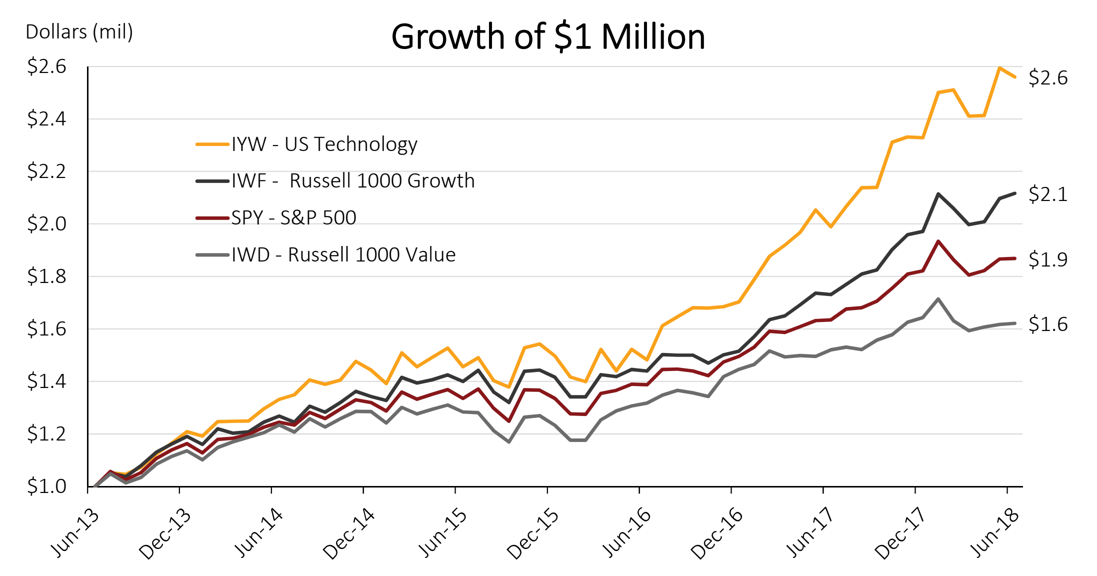
DeFact

The DJIA and the S&P 500 have diverged for the year due to international trade. The price return of the Dow is down 1.8% while the S&P 500 is up 1.7%, as Dow companies earn 44% of revenue overseas. The S&P 500 derives 30% of revenue from overseas. For example, 3M pulled the Dow down 157 points for the quarter after falling 10% and Caterpillar 8% decline shaved off an additional 81 points on an 8% drop. Both stocks derive 61% and 54%, respectively, of revenue from overseas.

WSJ

INDEX	2nd Qtr	YTD	1-YEAR	3-YEAR	5-YEAR	10-YEAR
DeMarche Growth	3.5	4.5	17.5	12.7	14.1	8.9
DeMarche Value	1.0	-2.3	6.5	6.3	7.4	6.4
DeMarche Aggressive	5.3	4.8	18.8	5.2	8.4	6.2
DeMarche Defensive	2.2	1.3	12.2	10.3	11.4	7.8
DeMarche Large Cap	2.2	1.5	12.6	9.9	11.0	7.0
Large Cap Growth	3.8	5.1	18.7	13.5	14.7	8.6
Large Cap Value	0.2	-3.2	5.1	5.5	6.7	5.1
DeMarche Small Cap	9.8	8.6	19.3	11.6	12.8	12.1
Small Cap Growth	8.3	8.8	18.1	9.9	12.9	10.5
Small Cap Value	10.8	8.4	20.3	12.8	12.7	13.1
S&P 500	3.4	2.6	14.4	11.9	13.4	10.2
S&P Mid-Cap 400	4.3	3.5	13.5	10.9	12.7	10.8
S&P Small-Cap 600	8.8	9.4	20.5	13.8	14.6	12.2
Russell 1000	3.6	2.9	14.5	11.6	13.4	10.2
Russell 1000 Growth	5.8	7.3	22.5	15.0	16.4	11.8
Russell 1000 Value	1.2	-1.7	6.8	8.3	10.3	8.5
Russell 2000	7.8	7.7	17.6	11.0	12.5	10.6
Russell 2000 Growth	7.2	9.7	21.9	10.6	13.6	11.2
Russell 2000 Value	8.3	5.4	13.1	11.2	11.2	9.9

Notes: Data are presented as percent returns. All 3, 5 and 10-year returns are annualized.



Source: BlackRock iShares

- Large cap growth stocks continue to trounce large cap value stocks. Technology stocks shined in the rocky quarter, reversing an 8% decline in the first quarter. Netflix led the so-called FAANG stocks, up 32.5% in the quarter. Facebook was up 21.6%, Amazon was up 17.4% as trade concerns did not impact large tech, as some investors feared. But it is concerning that technology stocks have high exposure to foreign revenue and, therefore, can be negatively impacted by currency swings.

- Small cap stocks outperformed large cap for the quarter, six months and year. International trade and currency swings impact small cap companies to a lesser degree than large cap companies because smaller companies tend to generate a smaller percentage of revenue overseas.

- In the second quarter, small cap value stocks rebounded and outperformed small cap growth, but still lag for the past six and 12 months. Small cap energy stocks have endured a volatile year so far, but for the second quarter are up over 24% as oil prices soared in the second quarter. The largest sectors in the small cap value universe, financials and REITs, also performed strongly, reversing their first quarter decline.

- Over longer time periods, the divergence between growth and value is made clear when we dig deeper into the returns of technology stocks. Over the past five years, tech stocks have significantly outperformed broader market indexes. Just this year, Amazon, Netflix and Microsoft together are responsible for 71 percent of S&P 500 returns and for 78 percent of Nasdaq 100 returns.

DeFact

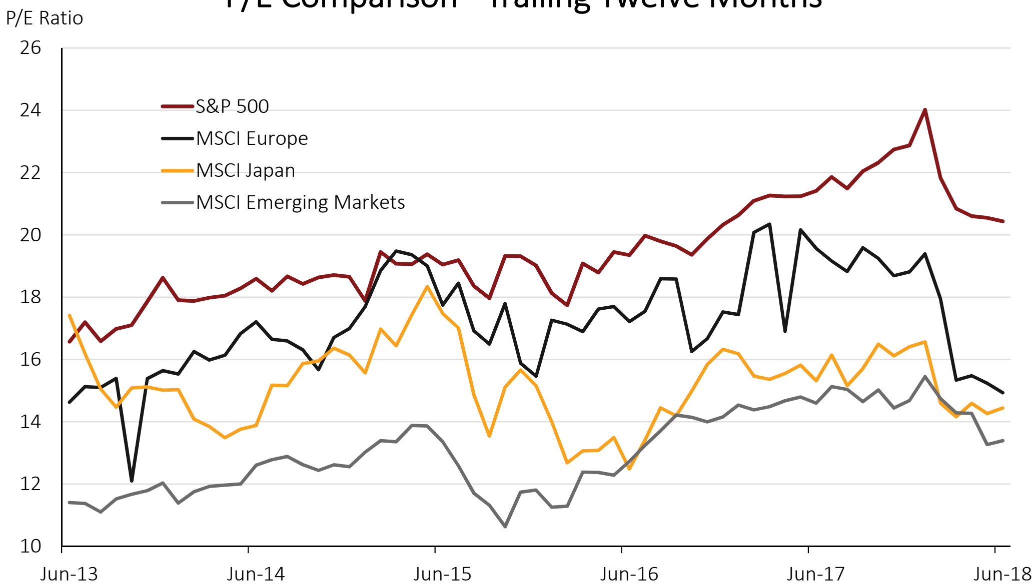
The tech sector's dominance in the S&P 500 is about to face a big test. In a realigning of companies within GICS (global industry classification standard), Facebook and Alphabet (Google) will join the new communication-services group and leave technology. Netflix and Comcast (now members of consumer discretionary) will also move to the communication-services group. The old telecom sector (with high yielding, slow growth Verizon, AT&T) will cease to exist in its current form as its members also join the communication-services group.

WSJ

INDEX	2nd Qtr	YTD	1-YEAR	3-YEAR	5-YEAR	10-YEAR
DeMarche Int'l	-2.6	-3.2	5.1	5.9	7.7	3.8
Growth	-1.9	-2.3	4.7	4.6	6.9	3.7
Value	-3.0	-3.7	6.4	5.4	7.4	3.5
DeMarche Int'l Small Cap	-4.2	-4.7	0.9	5.9	8.5	6.9
DeMarche EM	-8.1	-9.3	3.9	1.7	6.0	3.0
MSCI EAFE Local	3.5	-1.0	6.1	5.2	8.9	5.0
MSCI EAFE USD	-1.2	-2.7	6.8	4.9	6.4	2.8
Growth	0.1	-0.9	9.4	6.4	7.4	3.4
Value	-2.6	-4.6	4.3	3.3	5.4	2.2
MSCI Japan	-2.8	-2.0	10.5	6.2	7.4	3.5
MSCI AC Asia-ex Japan	-5.4	-4.8	9.9	7.0	8.2	5.8
MSCI Germany	-4.0	-7.4	2.5	5.3	6.4	2.5
MSCI France	-0.5	-0.1	9.9	8.7	8.2	2.3
MSCI UK	2.9	-1.0	10.0	3.1	4.9	2.7
MSCI EAFE Small Cap	-1.6	-1.3	12.4	10.1	11.3	6.8
MSCI EM	-8.0	-6.7	8.2	5.6	5.0	2.3
MSCI All Country-ex US	-2.6	-3.8	7.3	5.1	6.0	2.5

Notes: Data are presented as percent returns. All 3, 5 and 10-year returns are annualized.

P/E Comparison - Trailing Twelve Months



Source: Morningstar Direct

- As mentioned before, the US dollar continued its strengthening trend against other currencies in the quarter. When the dollar strengthens, foreign currencies can buy fewer dollars, negatively impacting returns. International developed returns in five and 10 year periods reflect a stronger dollar, just like the second quarter returns.
- In addition, GDP growth across the globe has not lived up to expectations. The Chinese economy grew during the quarter at its slowest pace in over two years. And Europe and Japan have slower GDP growth than previous quarters.
- Emerging market stocks fell during the quarter. Many factors combined to jolt emerging markets including trade tensions, slower GDP growth and the stronger dollar. China currently makes up the largest percentage of the index and actually outperformed other countries despite losing almost 5% in the last week of the quarter. The laggards in the index were Brazil (down over 27%) and South Africa (down over 15%). Korea, the second largest index weight, was down but in line with the broader index.
- As interest rates have climbed, the dollar strengthened and geopolitical headlines roiled the markets, while earnings have continued to grow and valuations have improved. Large cap domestic stocks have decreased almost four points in P/E multiple as measured by trailing 12 months earnings. Emerging market stocks, which performed very well in 2017 as technology stocks have led the way, have also reversed its P/E trend. Dollar strength in the future could slow down earnings growth momentum, so it is wise to be cautious even in light of cheaper valuations.

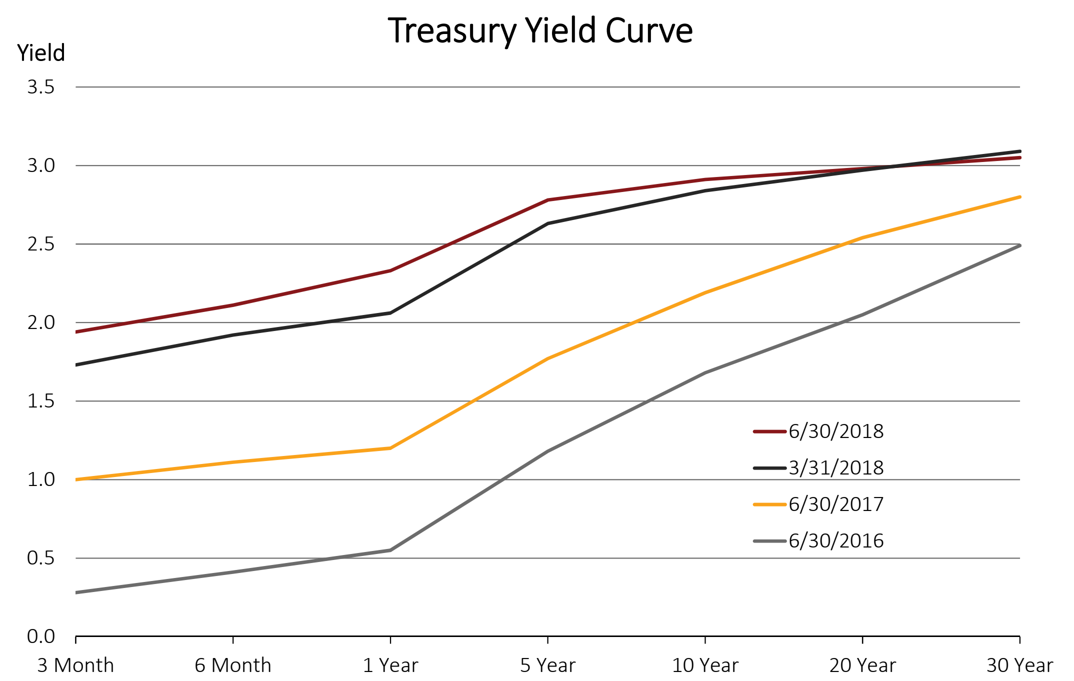
DeFact

Emerging markets continue to evolve as new countries gain status. Saudi Arabia will be reclassified as an emerging market in June 2019. It will represent 2.6% of the EM index with 32 securities. Also Argentina is to be reclassified from a frontier market to emerging market in June 2019. The number of emerging market countries currently stands at 24 and will increase to 26. Most recently, close to 230 China A shares debuted in the EM benchmark on June 1, 2018. Once A shares are fully included in the index, it is expected that China will make up over 42% of the index.

MSCI, CNBC

INDEX	2nd Qtr	YTD	1-YEAR	3-YEAR	5-YEAR	10-YEAR
BlmBarc 1-3 Gov Credit	0.3	0.1	0.2	0.7	0.8	1.7
BlmBarc Aggregate	-0.2	-1.6	-0.4	1.7	2.3	3.7
BlmBarc Gov Credit Long	-1.4	-5.0	-0.8	4.3	5.1	6.8
BlmBarc US TIPS	0.8	0.0	2.1	1.9	1.7	3.0
Merrill Lynch High Yield	1.0	0.1	2.5	5.5	5.5	8.0
CSFB Leveraged Loan (bank loans)	0.8	2.4	4.7	4.3	4.2	5.0
BlmBarc Global Aggregate	-2.8	-1.5	1.4	2.6	1.5	2.6
JPM Emerging Mkt Bond	-3.5	-5.2	-2.4	4.3	4.4	6.5

Notes: Data are presented as percent returns. All 3, 5 and 10-year returns are annualized.



Source: U.S. Federal Reserve

- Increases in interest rates proved to be a negative to bond returns. Long duration bonds were under pressure as longer term rates ticked up. The 10 year U.S. Treasury yield closed the quarter at 2.85%, up 12 basis points from the end of the first quarter.

- Corporate yield spreads remain tight to Treasuries which helped high yield bonds and bank loans returns for the quarter. If spreads widen to Treasuries, there is a negative impact to returns. The incremental yield provided from the credit spread cushioned corporate bond returns against interest rate increases. Longer term returns for high yield and bank loans have nicely outperformed BlmBarc Aggregate returns.

- Emerging market debt struggled against rising rates and a stronger dollar. The duration of the index is about 1.5 years longer than the BlmBarc Aggregate, so rate increases have a greater impact on returns. In addition, emerging market debt denominated in dollars is more difficult to repay as the dollar strengthens versus other currencies. Over longer time periods, emerging market debt has posted better returns than U.S. bonds due to the credit spread premium earned to compensate for the risk associated with emerging market countries.

- The chart to the left shows the dramatic flattening of the Treasury curve over the past two years. Short term rates have increased 150 basis points and longer term rates have increased only 50 basis points. The increase in rates have negatively impacted bond returns over this time frame. And a flattening curve is worth paying attention too as over the longer term, a flattening yield curve could signal a slowing economy.

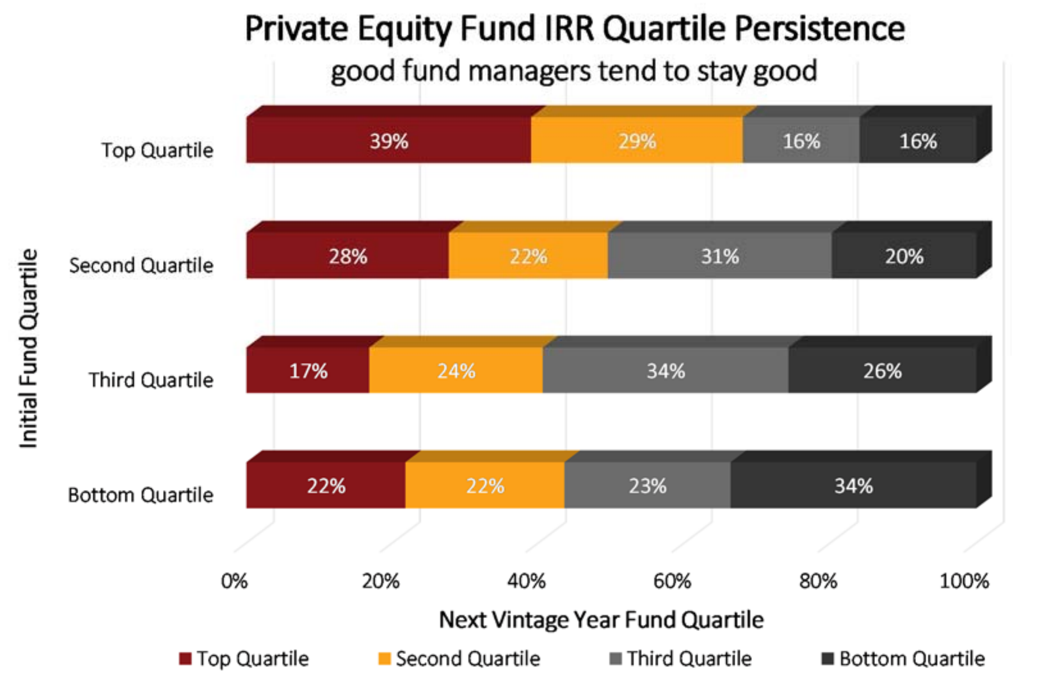
DeFact

The ballooning bank loan market is bigger than the high yield bond market for the first time in a decade, a sign of strong investor demand for debt that offers high returns as rates rise. The size of the market grew by $33 billion last month to $1.22 trillion, its fastest pace of growth in nearly four years. That pushed the amount of outstanding loans above the high yield bond market's $1.21 trillion.

WSJ, Fitch

INDEX	2nd Qtr	YTD	1-YEAR	3-YEAR	5-YEAR	10-YEAR
NCREIF Property (Private RE)	1.8	3.5	7.2	8.3	9.8	6.2
Apartment	1.5	3.1	6.5	7.5	8.8	6.2
Industrial	3.6	6.9	14.1	13.3	13.4	7.6
Office	1.5	3.4	6.5	7.1	8.9	5.0
Retail	1.3	2.0	4.6	7.8	10.1	7.5
NAREIT (Public RE)**	8.3	1.1	4.8	9.2	9.0	8.5
NCREIF Timberland	0.5	1.4	3.6	3.4	6.0	4.0
HFR FOF Composite	0.8	1.0	5.5	2.0	3.5	1.4
Conservative	1.0	1.6	4.1	1.9	3.0	1.2
Diversified	0.8	0.9	5.4	1.8	3.3	1.5
Strategic	0.9	1.3	6.6	2.5	4.2	1.7
Bloomberg Commodity	0.4	0.0	7.3	-4.5	-6.4	-9.0

Notes: Data are presented as percent returns. All 3, 5 and 10-year returns are annualized.
**Lagged **Public RE is not a less liquid strategy. It is listed for comparative purposes.*



Source: PitchBook, PitchBook Benchmarks: Private Markets - 3Q2018, Data through September 30, 2017

- Commodity prices posted positive gains for the quarter. Oil prices in particular soared when OPEC and other major producers capped output. U.S. output stalled when production bottlenecks arose. Brent climbed 13% and West Texas Intermediate was up 14.2% for the quarter. Conversely, agricultural commodities suffered during the last few weeks of the quarter due to trade tensions, down almost 10% for the quarter.

- Hedge funds continue to post positive quarters. The positive returns this quarter marked the ninth quarter in a row, despite relative poor performance during June. Composite returns were led in the quarter by event driven strategies as speculative activity in Telecom and Media accelerated. Macro strategies lagged others due to trade tariff volatility.

- Based on a study by Pitchbook, performance persistence is observable in Private Equity funds. The chart to the left shows that when funds that deliver top-quartile performance, they are followed by above median performance in their successor fund 68% of the time. This suggests that investors are well–served to scrutinize past performance in order to determine if GPs demonstrate observable traits that can create a “feedback loop” making it more likely that strong performance will endure.

DeFact

Initial public offerings of companies in the U.S. are dwindling. Private equity funds have long held to a certain model: raise money to buy a business, then exit their bets by selling or going public in a decade or so. Now, some private equity firms want to hold onto their businesses. The trend toward long-term capital funds have broader implications. More and more companies can tap the private equity markets and delay plans for initial public offerings. About 200 companies went public in 2017, down from more than 800 in 1996. So far in 2018, the IPO market has seen about 100 companies go public.

WSJ, Dealogic

Directions Please

Navigating Crucial Decisions to Reach Your Investment Goals

2018 DeMarche Client Conference
September 12 – 14
Kansas City

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demarche.com/cc18

There's no autopilot for financial success. No roadmap exists to show you the single best route to reach your institutional investment goals and satisfy your fiduciary responsibility. While more than one route may get you to your destination, each has a unique set of characteristics including risk, volatility, liquidity and performance that determines whether it's right for you. But how do you know which direction to take when you're faced with so many investment decisions?

Using our forty-three years of experience as financial trailblazers, DeMarche works with each client to help find their direction among the myriad of financial paths and avoid the many pitfalls. That's why we have chosen 'Directions Please' as the 2018 DeMarche Client Conference theme.

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Institutional Investing Trends
- Alternative Investments and the role of real assets
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