Quarterly Update 4th Quarter 2018

Review of the Markets

- Global equity markets posted steep declines in the fourth quarter. The U.S. underperformed the broad international indices as concerns mounted that an aggressive Federal Reserve (Fed) could steer the U.S. economy into recession. The inversion of yields on the 2-year and 5-year U.S. treasury notes was a strong message sent by investors that the Fed is approaching the tipping point.
- While non-U.S. equity markets outperformed for the quarter, economic growth in developed markets continues to decelerate and uncertainties over Brexit has reached new heights. Emerging markets were able to escape with single digit losses as U.S recession fears brought down yields and muffled the U.S. dollar's steady ascent.
- The risk off sentiment was evident given the bifurcated performance in the fixed income markets. As concerns mounted about a potential U.S. slowdown, credit spreads widened significantly. As yields drifted lower, higher quality issues saw modest gains while exposure to weaker credits experienced losses. A more stable dollar and lower U.S. yields contributed to the strong performance of Emerging Market Debt.

Our Views on Markets and Portfolios

- Despite the current correction in equity markets bringing valuations closer to long-term averages, given this point in the cycle we still believe above average long-term asset class return opportunities remain limited. We expect the current cycle will continue. However, the rate of growth will be lower in 2019.
- Our portfolios are positioned with low cost beta exposures to the broad global equity markets. We balance that with a fundamental focus on well capitalized quality companies. In the bond markets, we are growing increasing sensitive to credit while becoming more comfortable with duration. Alternatives holdings continue to include a mix of low cost beta and active alpha.
- We continue to invest in innovative technologies that are reshaping the global economy. The market is rewarding companies for efficient capital spending and R&D, and not just from financial engineering. Innovation in genetics, robotics, AI, nano-tech, clean-tech, bio-tech and ecommerce are focus areas.

Current Investment Strategy and Themes

- ***Market volatility increases as investors see signs the U.S. is approaching late cycle***
- ***Future growth impacted by global credit tightening, risks of eroding credit quality and increasing debt levels***
- ***Structure portfolios with low cost beta exposure plus innovative technologies that will effect global economies***

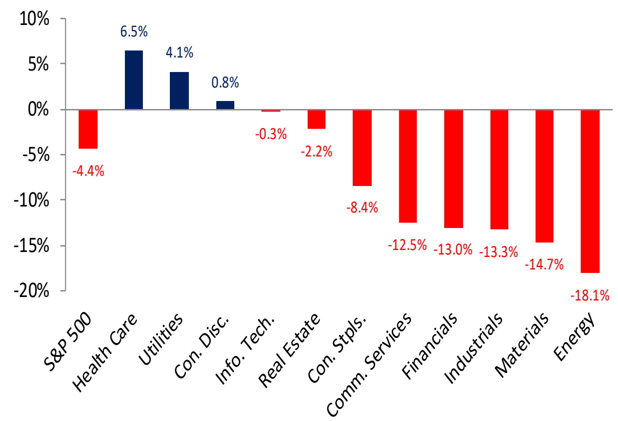
Key Market Indicators

Bullish | Favorable | Neutral | Cautious | Bearish

Equities	December 2018	4th Quarter 2018	2018	Current View
U.S. Large & Mid Cap	-9.03%	-13.52%	-4.38%	Cautious
U.S. Small Cap	-11.88%	-20.20%	-11.01%	Cautious
International	-4.85%	-12.54%	-13.79%	Neutral
Emerging Markets	-2.66%	-7.47%	-14.58%	Neutral
Fixed Income				
U.S. Aggregate	1.84%	1.64%	0.01%	Neutral
U.S. Government	2.13%	2.54%	0.88%	Neutral
U.S. Corporate	1.50%	0.01%	-2.11%	Neutral
U.S. High Yield	-2.14%	-4.53%	-2.08%	Cautious
Non-U.S. Developed	2.03%	0.78%	-2.26%	Cautious
Emg Market Debt	1.29%	2.65%	-6.90%	Bearish
Alternatives				
REITs	-8.23%	-6.73%	-4.62%	Favorable
Commodities	-6.12%	-8.60%	-8.91%	Bearish
Managed Futures	5.97%	3.58%	-4.40%	Cautious
Hedge Fund	-1.93%	-5.57%	-6.74%	Favorable

Source: Morningstar Data as of 12/31/2018

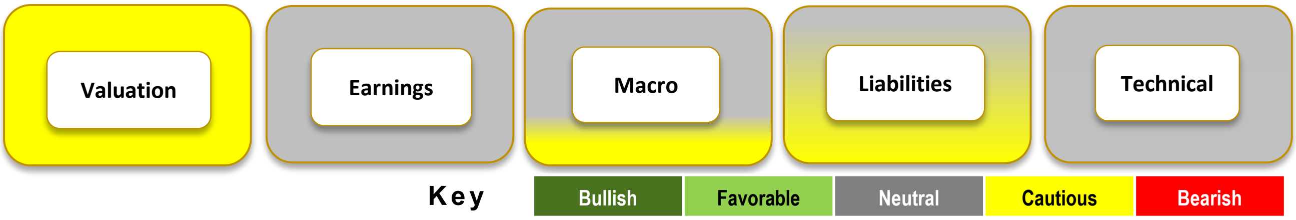
S&P 500 Sector 2018 Returns (%)



Source: Morningstar

Risk Examination

A quarterly update on our views of the complex risk factors in global markets



Valuation

- We continue to believe equities and long-dated bonds are trading slightly above fair value, with fixed income to a higher degree.
- Our view on equity valuation is based on actual and expected revenue growth and not exclusively earnings growth.
- Short-term Treasury Bills and Note yields now surpass the yield on the stock market, a signal that could trigger a reversal by risk averse investors out of equities into bonds.

Earnings

- We continue to believe earnings forecasts may be over-optimistic due to the strong momentum bias built into consensus forecasts and there could be a higher likelihood of downward earnings revisions as we head further into 2019.
- We place more importance on actual revenues and forecasted revenue growth rather than earnings growth, that can be measured several ways all of which can disguise true profitability measures.

Macroeconomic

- The consensus view is that the next U.S. economic recession will arrive during 2020.
- When factoring the current path of real economic output, productivity and the behavior of the yield curve, we are most concerned that an aggressive Federal Reserve may invert the yield curve, causing a U.S. recession to arrive much sooner than current expectations.
- Interest rate risk and inflation risk should remain tame unless central banks make the policy mistake of raising rates too quickly and too far.

Liabilities

- The decline in oil prices and accelerating wage growth could be a potential boost to the U.S. Consumer. However, a lower savings rate and increasing debt levels bear watching.
- Debt growth in the corporate sector has mushroomed over the last several years due to the low cost of capital. While interest coverage stands at higher levels than the financial crisis, higher interest rates and an economic slowdown could result in higher rates of credit default.
- Debt growth in the public sector has accelerated with no offset to pay for that growth. Infrastructure is still broken and real economic growth remains below the long-term average.

Technical

- While the performance gap between value and momentum contracted during the fourth quarter, price momentum continues to lead the market .
- Higher volatility was seen in both the equity and fixed income markets as the two major asset classes traded in tandem earlier in the quarter, reducing the benefits of diversification. The continued flow into passive and/or systematically managed low cost ETFs has also created the potential for a liquidity crisis down the road when market sentiment does shift toward the bearish side.

2019 Scenarios

Our assessment of potential macro scenarios

	Black Swan	**Ordinary Correction**	**Slow and Choppy**	**Upside Surprise**
Economy / Geopolitical	▪ N. Korea or Iran conflict leads to military intervention ▪ Populist movement accelerates ▪ Major cyber attack	▪ Valuation contraction ▪ Economic recession ▪ Central bank policy error ▪ Trade policy error	▪ Continued slow slog ▪ Below trend real economic growth ▪ Low inflation ▪ Limited or no fiscal response	▪ Productivity gains ▪ Earnings and growth increases ▪ Political cooperation on infrastructure and pro-growth policies
Markets	▪ Sharp sell-off across risk assets ▪ Elevated correlations suggest reduced diversification benefit	▪ Equities decline between 10-20% (risk off) ▪ Higher quality bonds gain modestly	▪ Equity markets choppy but grind higher ▪ Interest rates only modestly higher ▪ Quality may matter	▪ Stocks and most risk assets head higher ▪ Bond returns challenged by threat of higher rates
Focus	▪ Flight to quality: U.S. Treasuries, U.S. Dollar, Crypto Currencies & Gold benefit	▪ Bonds outperform stocks ▪ Diversified factor equity exposure with defensive tilt	▪ Faster growth economies and segments, with attractive valuations	▪ Fully invested, but highly diversified
Prospects	**< 10%**	**25%**	**45%**	**20%**

< < < Downside < < < | **> > > Upside > > >**

Risks

Downside:
- Diverging central bank policies; mishandled rate normalization; Social inequality leads to social unrest
- Protectionism policies
- Lone wolf terrorism and cyber attacks
- Recession or sharp global slowdown
- High geopolitical risk leads to major conflict

Upside:
- Central banks thread policy needle
- Trade talks turn productive
- Confidence builds, corporate investment resumes
- Economic and productivity growth trend around 3.0%
- Swift and comprehensive fiscal action

Asset Class Positioning

PORTFOLIO SEGMENT / SEGMENT OBJECTIVE	SEGMENT CONSTITUENTS	SEGMENT COMMENTS
Equity *Low-Cost, Systematic, and Factor Exposure*	▪ Global Systematic Equity Beta exposure; both market cap and factor weighted ▪ Diversified factor exposure with emphasis on multi-factor and a slight tilt toward quality	▪ Favor higher quality equities ▪ Favor higher growth regions and sectors with attractive valuations ▪ Longer term, market driven by value, but in shorter-term growth and momentum can and have dominated
Fixed Income *Seeks to Preserve Capital and Generate Income*	▪ Broad, Core Plus Exposure ▪ Active, Multi-Sector Fixed Income ▪ Actively-managed Mortgage Backed Securities ▪ Short-to-Intermediate High Quality Credit ▪ Shorter duration high yield	▪ Favor intermediate duration or less ▪ Favor quality credit over rates ▪ Selective, short duration high yield ▪ Issuer selection critical ▪ BBB segment is crowded
Opportunistic *Reflecting Ideas Based on 12-24 Month Proprietary Forecasts*	▪ Active Beta Emerging Mkt Equity ▪ Regional Developed Mkt non-U.S. Equity with Focus on Asia and Europe ▪ Global Technology ▪ Basket of Innovation	▪ Reflects Palladiem's shorter term model (value and momentum) ▪ Sectors and themes have growth potential and attractive valuations relative to broad market ▪ Seeking participation in select themes with attractive return potential
Alternative *Anticipated Risk Mitigation with Alpha Opportunities*	▪ Global Macro ▪ Hedged Equity ▪ Long/Short Credit ▪ Merger Arbitrage	▪ Given elevated risks to traditional, long-only exposures (especially equities), favor moderate allocations to non-correlated alternative strategies ▪ Favor transparency, low cost, and daily liquidity ▪ Favor global macro, long/short equity, and long/short credit strategies for lower correlation and diversification potential (look to de-risk long equity exposure)

All investments are subject to risk, including the loss of principal. For additional information about the Palladiem Investment Portfolios, please refer to the Disclosures at the end of this report.

Important Disclosures

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Genesis and Palladiem have discretion to change allocations to styles and vehicles at any time.

Index definitions:

“U.S. Large Cap” represented by the S&P 500 Index.
“U.S. Small Cap” represented by the Russell 2000 Index.
“International” represented by the MSCI Europe, Australasia, Far East (EAFE) Net Return Index.
“Emerging” represented by the MSCI Emerging Markets Net Return Index.
“U.S. Aggregate” represented by the Bloomberg Barclays U.S. Aggregate Bond Index.
“U.S. Government” represented by the Bloomberg Barclays U.S. Government Bond Index.
“U.S. Corporate” represented by the Bloomberg Barclays U.S. Credit Bond Index.
“U.S. High Yield” represented by the Bloomberg Barclays U.S. Corporate High Yield Index.
“Non-U.S. Developed” represented by the S&P International Treasury ex U.S. Index.
“Emerging Market Debt” represented by the JP Morgan GBI-EM Global Core Index
“REITs” represented by the FTSE North American Real Estate Investment Trust (REIT) Equity REITs Index.
“Commodities” represented by the Dow Jones Commodity Index .
“Managed Futures” represented by the Credit Suisse Managed Futures Index.
“Global Macro” represented by the Credit Suisse Global Macro Index.

Direct investment in an index is not possible.

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