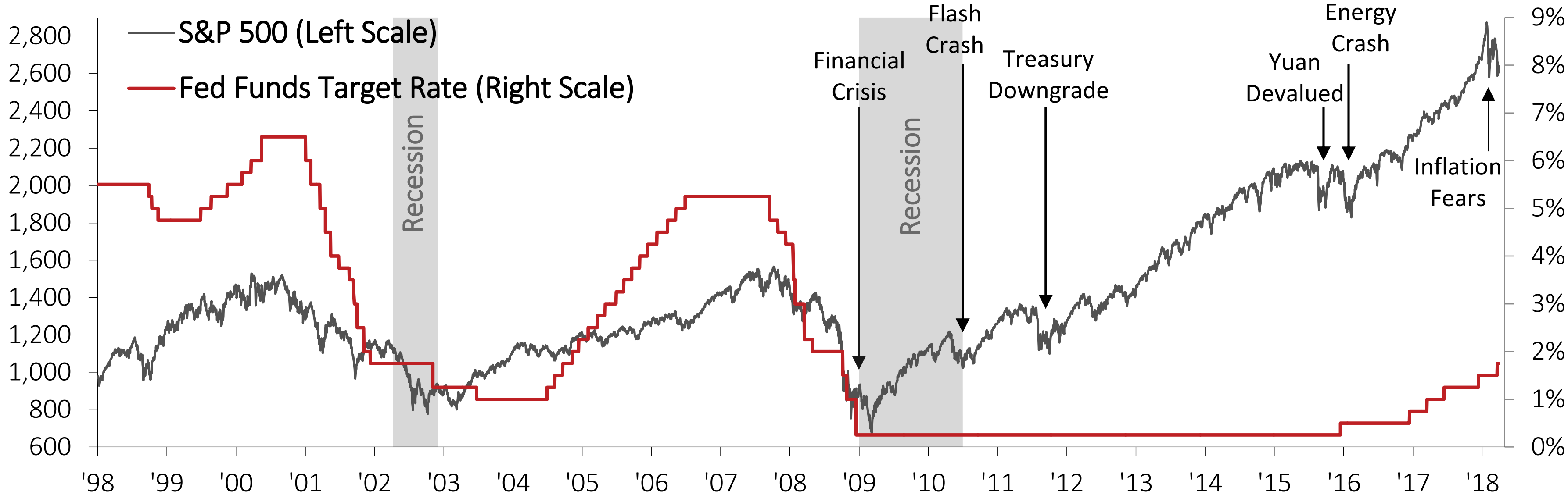
Capital Market Review

March 31, 2018

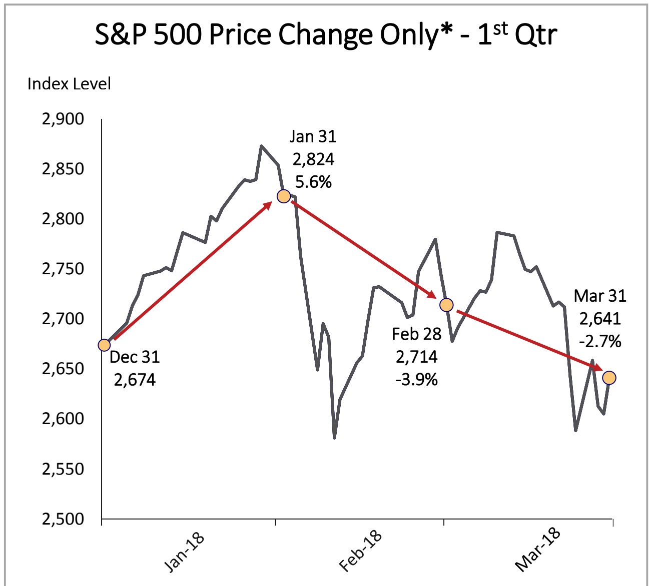



DeMarche

The Return of Volatility

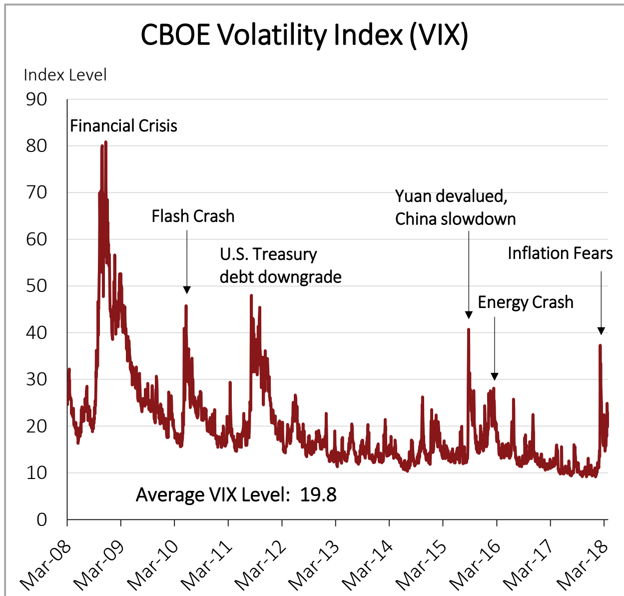


Source: Standard & Poor's, St. Louis Federal Reserve



*Source: Standard & Poor's *Does not include dividends.*

Volatility returned to the market during the quarter. Historically, the average level of volatility, as measured by the VIX Index, is 19.8. In truth, this makes 2017 an outlier year with an average VIX level of 11.1. When spikes in volatility have occurred in the past from financial or other global events, markets quickly settled back down. Volatility is not a code word for a "declining" market; instead, it is only a reflection of uncertainty that could produce both winners and losers. In the case of the first quarter, daily headlines about a "trade war", inflation and tech company privacy concerns have produced opportunities to reallocate and to rebalance. In fact, as earnings growth is expected to be strong this year, the S&P 500 is back to 16 times forward earnings, much more in line with the long-term averages.



Source: Federal Reserve of St. Louis

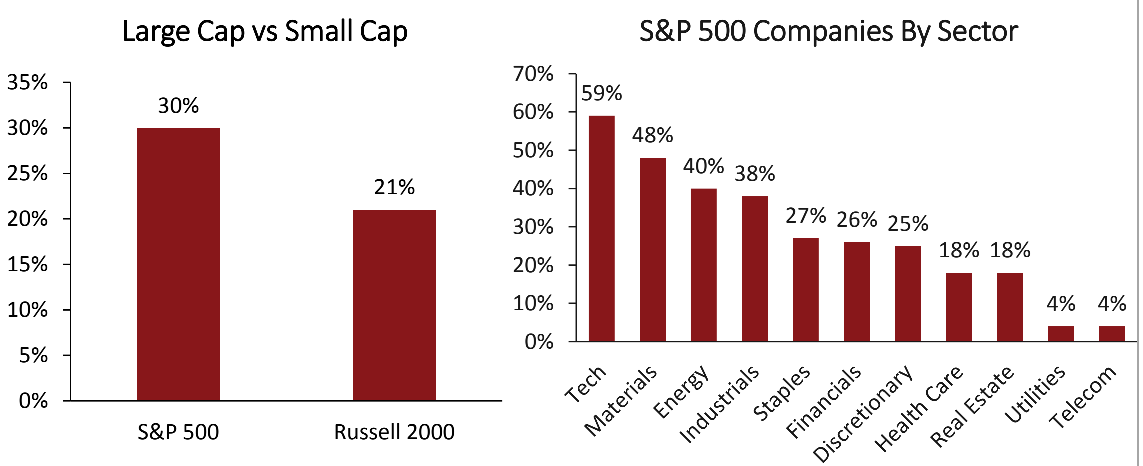
Broad Market Overview

INDEX	1st Qtr	1-YEAR	3-YEAR	5-YEAR	10-YEAR
MSCI World	-1.3	13.6	8.0	9.7	5.9
DeMarche World*	-0.7	14.4	8.1	9.5	5.7
DeMarche 3000	-0.8	13.3	9.1	10.9	7.4
Russell 3000	-0.6	13.8	10.2	13.0	9.6
S&P 500	-0.8	14.0	10.8	13.3	9.5
DeMarche International	-0.5	15.3	7.2	8.0	3.8
MSCI EAFE USD	-1.5	14.8	5.6	6.5	2.7
BlmBarc Aggregate	-1.5	1.2	1.2	1.8	3.6
Citigroup Non-US Gov't Bond	4.4	12.9	5.0	1.4	1.8
BlmBarc Global Aggregate	1.4	7.0	3.1	1.5	2.6
NCREIF (Private RE)	1.7	7.1	8.7	10.0	6.1
Bloomberg Commodity	-0.4	3.7	-3.2	-8.3	-7.7

*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 3/31	2018	2017	2016	2015	50 Year Average
GDP Annual Growth Rate	2.9	2.0	1.4	3.8	2.8
Unemployment	4.1	4.5	5.0	5.5	6.2
Inflation (CPI)	2.4	2.4	0.9	-0.1	4.1
10-Year Interest Rates	2.7	2.4	1.8	1.9	6.5

Exposure to Foreign Sales (%)



Source: WSJ

Source: WSJ

- Global equities turned negative for the quarter. Volatility returned with a vengeance in February, bruising both domestic and developed international stocks. Fears of inflation sparked profit-taking among domestic large cap stocks. Developed international stocks fell in response to purchasing managers' index (PMI) data that indicated softening growth. The PMI is a measure of the economic health of the manufacturing sector.

- Bonds were battered by inflation concerns as interest rates increased during the quarter. The Federal Reserve raised its benchmark rate once again in March to reach a target range of 1.50% to 1.75%. The 10-year Treasury bond yield increased from 2.40% to 2.74% during the quarter, resulting in a negative 2.4% return.

- The US dollar continued its weakening trend against global currencies. International bonds benefited as one unit of global currency can now purchase more US dollars. In addition, global rates generally were flat to lower in response to modest growth concerns and continued quantitative easing programs in Japan and the EU.

- The chart to the left shows the relative exposure of companies' earnings from sales overseas. Larger companies have more of a global presence than small companies, as one would expect. The second chart shows that technology companies generate over half of their earnings overseas. These companies could be more vulnerable to sales disruptions from the implications of a potential "trade war".

DeFact

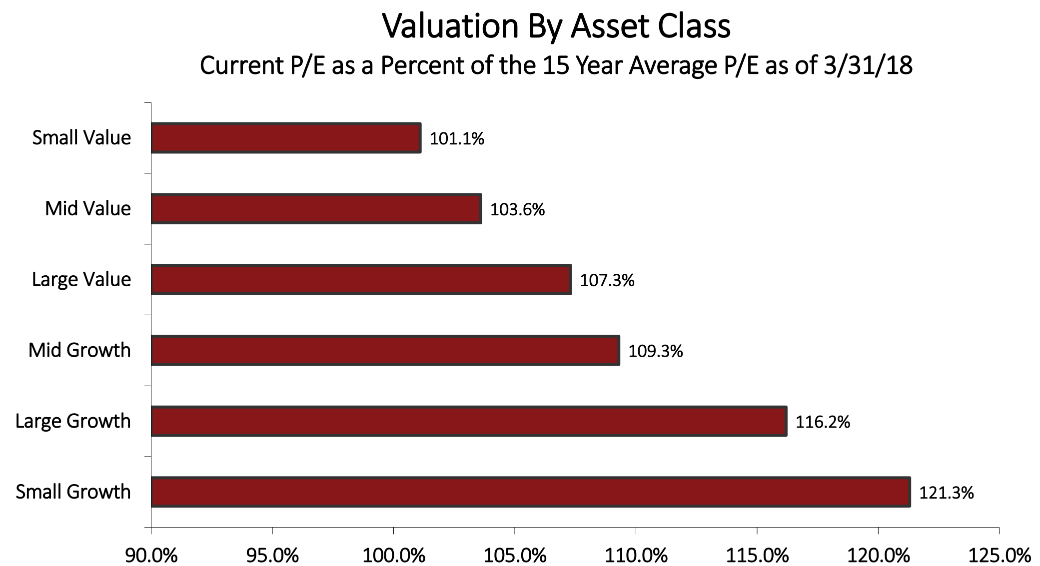
Volatility has returned. In 2017, the S&P 500 Index had only 10 trading days where the intraday price changed, either positively or negatively, by more than 1%, and none more than 2%. In the 1st quarter of 2018 alone, the S&P 500 Index experienced 34 trading days of such volatility: 20 days with a price change between 1% and 2%, 10 days between 2% and 3%, 1 day between 3% and 4%, and finally, 3 days above 4%.

~DeMarche

Domestic Equities

INDEX	1st Qtr	1-YEAR	3-YEAR	5-YEAR	10-YEAR
DeMarche Growth	1.0	19.0	11.4	13.6	8.9
DeMarche Value	-3.2	6.3	6.1	7.6	5.5
DeMarche Aggressive	-0.5	12.1	3.1	8.1	5.6
DeMarche Defensive	-0.9	13.4	9.7	11.1	7.5
DeMarche Large Cap	-0.8	13.8	9.3	10.8	6.6
Large Cap Growth	1.3	20.4	12.2	14.0	8.6
Large Cap Value	-3.4	6.2	5.8	7.1	4.3
DeMarche Small Cap	-1.1	11.4	8.9	11.8	10.1
Small Cap Growth	0.4	13.5	7.9	11.9	9.2
Small Cap Value	-2.2	9.8	9.5	11.7	10.6
S&P 500	-0.8	14.0	10.8	13.3	9.5
S&P Mid-Cap 400	-0.8	11.0	9.0	12.0	10.9
S&P Small-Cap 600	0.6	12.7	10.8	13.6	11.4
Russell 1000	-0.7	14.0	10.4	13.2	9.6
Russell 1000 Growth	1.4	21.3	12.9	15.5	11.3
Russell 1000 Value	-2.8	6.9	7.9	10.8	7.8
Russell 2000	-0.1	11.8	8.4	11.5	9.8
Russell 2000 Growth	2.3	18.6	8.8	12.9	11.0
Russell 2000 Value	-2.6	5.1	7.9	10.0	8.6

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



Source: JP Morgan, Forward P/E ratios calculated and provided by FactSet Market Aggregates

- Growth stock returns continued to trounce value stocks for the quarter and for the one-year period. Growth stocks were led by the technology sector with a 3.5% return for the quarter, outpacing all others. The technology-heavy NASDAQ index reached an all-time high on March 12, before falling over 8% to finish the quarter. Large growth companies (FAANG stocks) were negatively impacted by trade war and data privacy concerns.

- Small cap growth outperformed small cap value stocks by a wide margin again this quarter. Small cap healthcare stocks drove the outperformance by returning over 12% for the quarter. Interestingly, small cap technology returns were slightly negative. Healthcare and technology each make up about 25% of the small cap growth index.

- Value stocks, both large and small, suffered in the quarter. Financials make up the largest part of the large and small cap indexes, and that sector was negative for the quarter. The real estate (REIT) sector holds a 10% weight in the small cap value index and was negatively impacted by increasing interest rates.

- Small cap stocks outperformed large cap stocks for the second time in three quarters and have closed the return gap versus large cap stocks over the past 12 months. Small cap stocks have less international exposure in terms of foreign sales than large cap stocks, so they may be less exposed to the negative aspects of a trade war.

- The chart to the left shows just how extended growth stock valuations have become compared to 15 year averages. Even with the volatility of the past few months, growth stocks (both large and small) look over-valued. Value stocks, particularly small stocks, seem to be more “in-line” with longer term valuations.

DeFact

Earnings on domestic stocks are expected to remain strong in 2018, boosted by the tax overhaul and a growing global economy. Given the market’s recent pullback and surging earnings expectations, the forward P/E ratio of the market has dropped from 18.6 at the peak of the S&P 500 in late January to about 16 times at the end of the quarter. That is the lowest multiple since June 2016.

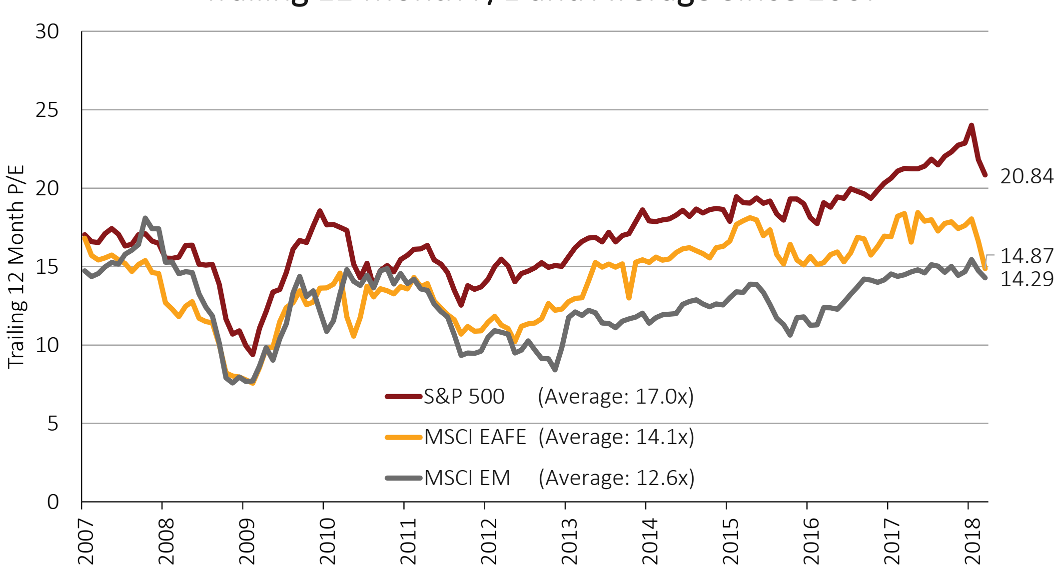
~DeMarche, WSJ

International Equities

INDEX	1st Qtr	1-YEAR	3-YEAR	5-YEAR	10-YEAR
DeMarche Int'l	-0.5	15.3	7.2	8.0	3.8
Growth	-0.4	15.8	5.6	6.5	3.6
Value	-0.7	15.5	7.0	8.3	3.4
DeMarche Int'l Small Cap	-0.5	15.5	7.5	9.2	6.4
DeMarche EM	-1.3	20.5	5.5	6.2	3.3
MSCI EAFE Local	-4.3	5.3	3.4	8.5	4.5
MSCI EAFE USD	-1.5	14.8	5.6	6.5	2.7
Growth	-1.0	17.5	6.7	7.1	3.4
Value	-2.0	12.2	4.3	5.8	2.0
MSCI Japan	0.8	19.6	8.4	8.9	4.1
MSCI AC Asia-ex Japan	0.7	25.8	9.2	8.2	5.5
MSCI Germany	-3.6	13.6	4.7	7.8	2.7
MSCI France	0.3	20.4	8.9	8.9	2.0
MSCI UK	-3.9	11.9	3.1	3.9	2.3
MSCI EAFE Small Cap	0.2	23.5	12.3	11.1	6.5
MSCI EM	1.4	24.9	8.8	5.0	3.0
MSCI All Country-ex US	-1.2	16.5	6.2	5.9	2.7

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

Trailing 12 Month P/E and Average Since 2007



Source: Morningstar Direct, DeMarche

- The US dollar continued its weakening trend against other currencies in the quarter. The trend is observed in the 3- and 12-month returns for developed stocks and, to a lesser extent, in 3-year returns. International developed stocks underperformed domestic stocks for the second quarter in a row, but they are still slightly ahead for the trailing 12 months at 14.8% for MSCI EAFE-USD vs. 14% for S&P 500.

- Emerging market stocks posted positive returns for the quarter and are now ahead of domestic stock returns by over 10% for the trailing 12 months. Earnings growth expectations are rising faster in the emerging markets than in any other region. Emerging market stocks suffered in the second half of March, on trade concerns, but the sell-off was less pronounced than other markets.

- Believe it or not, invoking Article 50 by the British to start the "Brexit" process is now a year old. The UK is scheduled to leave the EU on March 29, 2019. UK stocks have had the weakest five-year returns among developed and emerging markets. In addition, four stocks (HSBC, BP, Royal Dutch A & B), which have struggled globally over the past five years, make up over 22% of the UK index. The same four UK stocks make up 4% of the MSCI EAFE.

- International stocks, both developed and emerging, look more "fairly" valued than domestic stocks. The drawdowns in the quarter brought domestic stocks (as measured by the S&P 500) down to valuations not seen since 2016. Developed international stocks are dominated by energy (Royal Dutch, Total, and BP) consumer staples (Nestle), and healthcare (Novartis). Technology stocks, which typically garner a higher P/E ratio are missing. Interestingly, the EM index is dominated by technology stocks, whose top four stocks make up almost 17% of the index. The implication is that the P/E of EM stocks may become "out of line" with its history as tech gains market share.

DeFact

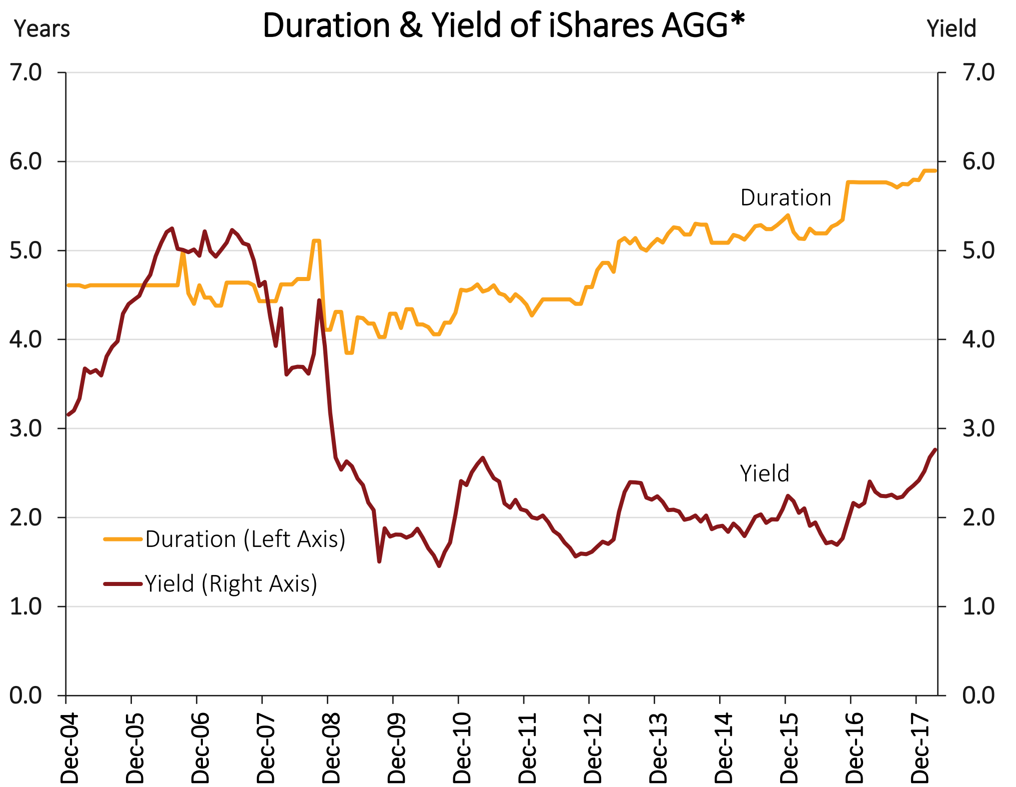
China's central bank guided the yuan to its strongest level in more than 2.5 years. The yuan appreciated more than 3% versus the US dollar during the quarter. China tries to manage its currency within a stable band versus other currencies, but it is struggling to maintain that level versus the U.S. dollar. A stronger yuan makes Chinese goods more expensive in US dollar terms, which may aid in easing trade pressures between China and the US.

~WSJ, Merrill Lynch, Forbes

Fixed Income

INDEX	1st Qtr	1-YEAR	3-YEAR	5-YEAR	10-YEAR
BlmBarc 1-3 Gov Credit	-0.2	0.2	0.7	0.8	1.6
BlmBarc Aggregate	-1.5	1.2	1.2	1.8	3.6
BlmBarc Gov Credit Long	-3.6	5.1	2.1	4.1	6.8
BlmBarc US TIPS	-0.8	0.9	1.3	0.0	2.9
Merrill Lynch High Yield	-0.9	3.7	5.2	5.0	8.0
CSFB Leveraged Loan	1.6	4.6	4.3	4.2	5.4
BlmBarc Global Aggregate	1.4	7.0	3.1	1.5	2.6
JPM Emerging Mkt Bond	-1.8	3.3	5.5	3.9	6.8

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



*Source: Morningstar Direct, iShares AGG. *Data are net of fees and expenses of the ETF.*

- The Fed increased the top of the target range to 1.75%. The 10-year Treasury yield increased 34 basis points. The increase in rates along the curve negatively impacted bond returns.
- High yield bonds posted negative returns for the quarter. The higher coupon on high yield cushioned the blow of interest rate increases somewhat. Some credit spread widening also hurt returns. The yield on the index is now 6.2%, an increase of 50 basis points from year-end. Longer term returns (3- to 10-years) are more in-line with the yield spread one would expect over investment grade bonds.
- Bank loans posted positive returns for the quarter. Bank loans are predominately floating rate and have coupons that reset quarterly. This feature protects against rises in interest rates. One year returns are about 440 basis points over short duration investment grade bonds (as measured by the BlmBarc 1-3 Gov Credit) Returns in the 3- to 10-year range are slightly less robust at approximately 340 to 380 basis points over.
- The JPM Emerging Market Bond index has a duration about 1.5 years longer than the intermediate-term duration of the Bloomberg Barclays Aggregate Index at 7.4 years vs. 5.9 years. While the higher yield on EM debt and the weaker US dollar helped mitigate the effect of the longer duration, returns were still negative due to rising rates.
- The chart to the left shows the evolution of the Bloomberg Barclays Aggregate duration and yield as tracked by the iShares AGG ETF. The duration has extended due to longer term bond issuance. As of quarter end, the 30-day SEC yield increased to yield 2.76%. The increase in yields during the quarter and bond prices declined resulting in a negative 1.5% return for the quarter.

DeFact

CVS Health Corp. completed the third largest corporate bond sale on record to fund its acquisition of Aetna. The pharmacy giant issued $40 billion in investment grade debt. The longest portion of the offering, a 30-year bond, yielded 195 basis points above Treasuries (coupon of 5.05%) after the initial pricing at 215 basis points. S&P Global Ratings downgraded CVS one level to BBB following the announcement of the debt offering. The offering was three times over-subscribed.

~Bloomberg

Less Liquid Strategies

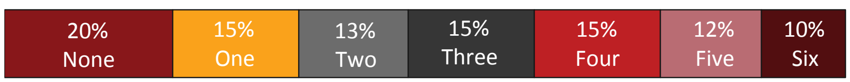
INDEX	1st Qtr	1-YEAR	3-YEAR	5-YEAR	10-YEAR
NCREIF Property (Private RE)	1.7	7.1	8.7	10.0	6.1
Apartment	1.5	6.4	8.0	9.0	6.1
Industrial	3.3	13.5	13.3	13.4	7.3
Office	1.8	6.6	7.7	9.2	4.9
Retail	0.7	4.8	8.4	10.5	7.5
NAREIT (Public RE)*	-6.7	-1.0	3.1	6.5	7.0
NCREIF Timberland	0.9	3.8	3.4	6.1	4.1
HFR FOF Composite	0.6	5.9	2.0	3.4	1.6
Conservative	0.4	3.3	1.6	2.9	1.3
Diversified	0.6	5.5	1.6	3.3	1.6
Strategic	0.5	7.7	2.7	4.0	1.8
Bloomberg Commodity	-0.4	3.7	-3.2	-8.3	-7.7

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

Institutional Investor Participation in Alternative Asset Classes

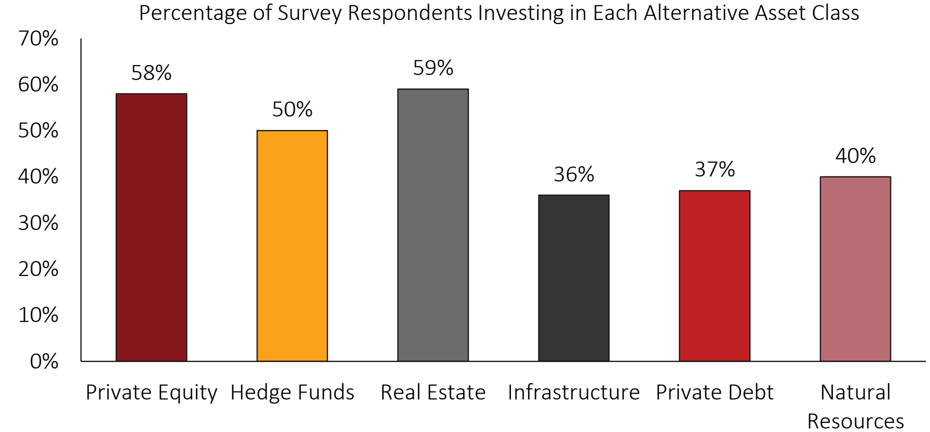
How Many Alternative Asset Classes Are Being Utilized?

Number of Alternative Asset Classes Invested In By Survey Respondents*



Which Alternative Asset Classes Are Being Utilized?

Percentage of Survey Respondents Investing in Each Alternative Asset Class



Source: Preqin.com; Preqin Investor Outlook: Alternative Assets H1 2018; December 2017 survey of 550 respondents

- Commodity prices fell for the quarter, driven lower by natural gas and industrial metals (copper, aluminum). Crude oil and grains posted positive returns and precious metals were flat to slightly negative. The best performing commodity sector was cocoa, posting a 35% return; the worst sector was lean hogs with a negative 20% return.

- REITs struggled in the quarter causing one-year returns to enter negative territory. REIT returns are negatively correlated to interest rate increases, thus when interest rates increased during the first quarter, prices fell. Over the longer term, REIT performance is in line with private real estate.

- Industrial properties, which are primarily warehouses, continue to be stellar performers with a return of 3.3% for the quarter while the retail sector return was only 0.7%. Online shopping could be the catalyst for both, increasing demand for “last mile” warehouse space (helping the industrial sector) and at the same time hurting many traditional retailers.

- Hedge funds continue to post modest results quarter after quarter. The positive returns this quarter mark the eighth positive quarter in a row. Composite returns were driven by equity hedge returns in both the event driven and long short strategies. Global macro strategies tended to struggle in the quarter with the sudden rise in volatility.

- Alternative assets classes continue to gain traction with institutional investors. The table to the left shows that while 80% of survey respondents have invested in alternatives, over 50% have three or more such investments.

DeFact

The research teams at Bloomberg New Energy Finance report renewable energy sources are set to represent “almost three-quarters of the $10.2 trillion the world will invest in new power-generating technology until 2040.” Even more significant, across the Asia Pacific region, including the Chinese and Indian economies, renewables will account for more than 60 percent of new energy investments, versus only 10 percent for coal and gas generation.

~Real Assets Advisor

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DeMarche Events

Month		Topic / Organization	Who	Where
May	3rd	The Evolving Landscape for Defined Contribution Plans	DeMarche Hosted Workshop	Minneapolis, MN
May	23rd	Expanding Investment Horizons with Alternatives	DeMarche Hosted Workshop	Chicago, IL

Industry Speaking Engagements

April	24th	Bitcoin and Other Cryptocurrencies-Investment Opportunities *Minneapolis MNAFP Regional Meeting*	Mark Andes Speaker	St. Paul, MN
May	24th	Strategies to Enhance Short-Term Yield for Operating Funds *Windy City Summit*	James Dykstal, CFA Speaker	Chicago, IL
June	12th	Markets Group	Don Lennard	Chicago, IL
Sept	12th	Markets Group	James Dykstal, CFA Markets Group Panelist	Minneapolis, MN
Oct	23rd	Markets Group	Travis Newman Markets Group Panelist	Atlanta, GA

Appearances and dates subject to change.