

Ellwood's Capital Markets Committee

Investment Outlook

2019

CAPITAL MARKETS VIEWS

Ellwood seeks to evaluate the risk and return potential for a range of asset classes within the anticipated investment environment. While we expect economic growth to remain positive, we view the U.S. to be in the later stages of the economic cycle. In this environment, we must be mindful that economic conditions could change rapidly and so portfolio positioning during 2019 is more oriented around risk management.

This is evident within fixed income, as our growing concern about the credit cycle leads us to bias portfolios towards higher quality securities. Additionally, Ellwood client portfolios have generally been

positioned with less interest rate risk (duration) for several years, and it is worth reconsidering this underweight duration during this coming year. We also view low volatility hedge funds as a way to remain exposed to attractively priced risk assets but with a low beta profile.

We see attractive opportunities in emerging markets and favor exposure to both equities and debt strategies—although with a watchful eye on China, which is showing decelerating growth trends. Our view on U.S. equities is balanced between upside potential and downside risk. Ellwood's optimism

regarding international developed markets has waned, as we have lower conviction that we will see positive catalysts—particularly in Europe.

Ellwood anticipates inflation to be range-bound around the Federal Reserve's 2% target so minimal opportunistic exposure to real (inflation-sensitive) assets is warranted. Finally, within private markets, we recommend that investors should commit to 2019 vintage year funds at levels that maintain stable exposures throughout the economic cycle.

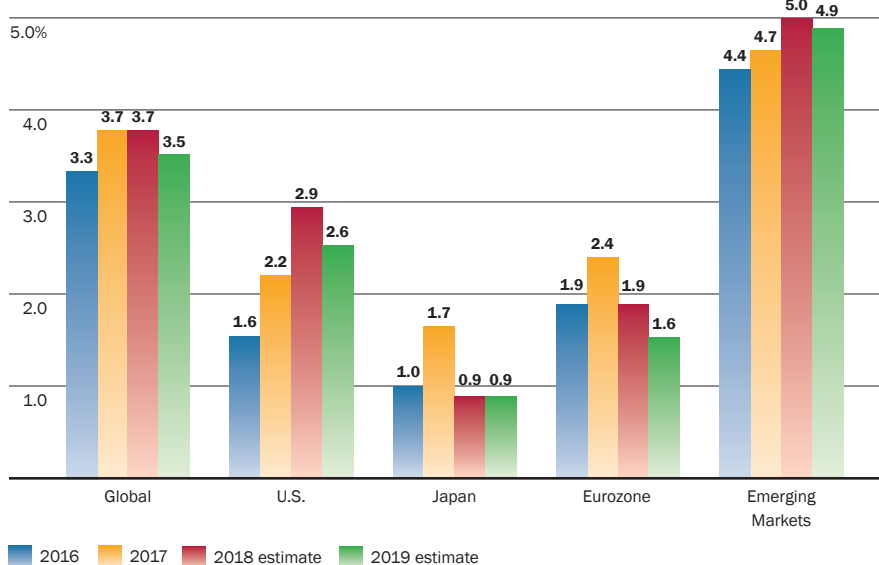
	Cautious View	Neutral	Favorable View
U.S. Equity		●	
International Developed Market Equity		●	
Emerging Markets Equity			●
Investment Grade Fixed Income		●	
International Developed Fixed Income	●		
Emerging Market Debt			●
High Yield Bonds		●	
Leveraged Loans		●	
Directional Hedge Funds		●	
Low Volatility Hedge Funds			●
Inflation Sensitive Assets		●	
Private Equity		●	
Private Credit		●	
Private Real Estate		●	

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ECONOMIC GROWTH

Global GDP growth is projected to remain steady at 3.7% in 2018 amongst mixed results across regions with the U.S. and emerging markets growing while Japan and the Eurozone are decelerating. As shown to the right, market consensus GDP growth estimates across regions are expecting slower, but positive, global growth rates in 2019. Ellwood expresses a similar view and anticipates global growth to decrease from its above trend levels of the past two years. The unwinding of monetary policy stimulus and the impacts of trade policy uncertainty are the primary drivers of this projected decline. As highlighted in the risks section, the outcomes in negotiations between the U.S. and China, and the UK and Europe, could lead to improving (or deteriorating) global growth estimates.

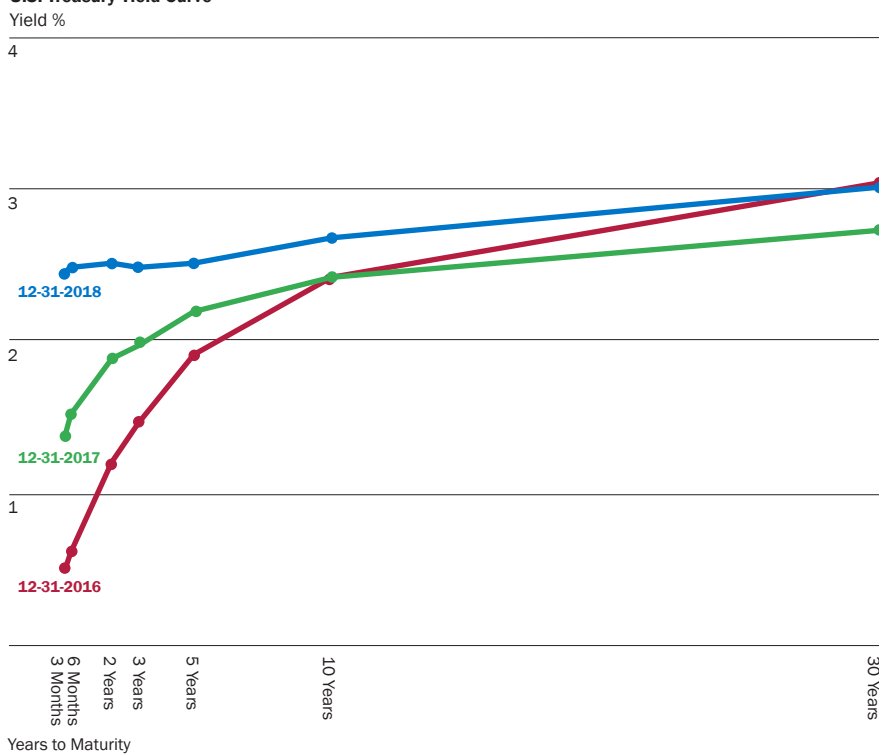
Global Consensus GDP Forecasts



MONETARY POLICY

The Federal Open Market Committee (FOMC) raised the Fed Funds rate four times in 2018, the largest annual increase since 2006.¹ Investors were caught off guard as markets placed only a 5%² probability on four rate increases going into the year. The current Fed Funds rate target of 2.25–2.50% is now much closer to the Federal Reserve’s projected long term target rate of approximately 2.50–3.00%. Recent statements from Chairman Jerome Powell indicate a somewhat softer stance with a willingness to be patient and flexible going forward and that rates were just below their neutral range. As such, Ellwood expects that the FOMC will slow their pace of rate increases with an anticipated one to two rate hikes in 2019.

U.S. Treasury Yield Curve



The yield curve flattened in 2018, raising concerns about an inverted yield curve (short rates above long rates) which has historically preceded recessions. While there are several reasons why “this time could be different”, Ellwood continues to believe that an inversion in the yield curve could present a meaningful risk to markets.

1. Federal Reserve: <https://www.federalreserve.gov/monetarypolicy/openmarket.htm>
 2. CME Group: <https://www.cmegroup.com/trading/interest-rates/countdown-to-fomc.html>

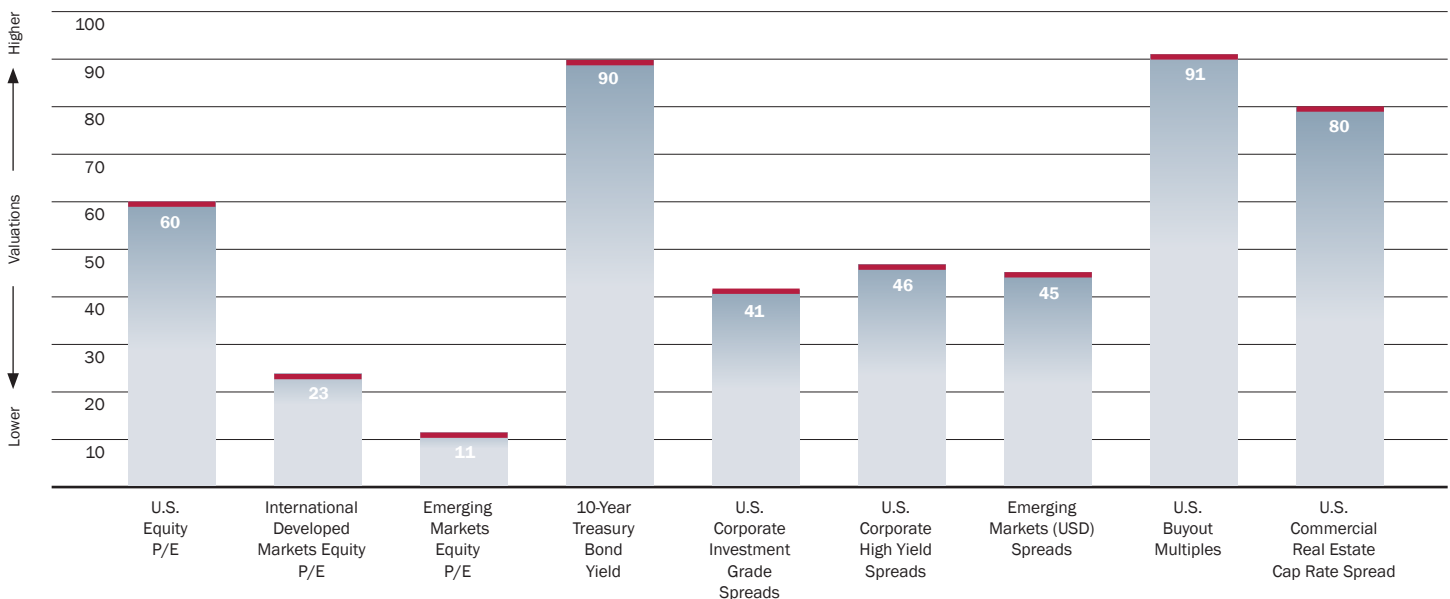
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ASSET CLASS VALUATIONS

A silver lining to the market sell off in late 2018 comes in the form of lower valuations across most asset classes. Whereas U.S. equity market valuations were in the top quartile relative to recent history entering 2018, market multiples are now meaningfully lower. Equity valuations are even more attractive outside the U.S. where developed market and emerging market

price-to-earnings ratios remain substantially below the U.S. and well below long-term averages. Higher interest rates and wider credit spreads lead to an improved picture for fixed income valuations as well. While valuations are notoriously a weak signal for predicting short-term returns, more reasonable valuations alleviate some of the asymmetric downside risk within markets.

Asset Class Valuation Percentile Ranks



The most recent data point available for each asset class is compared to the longest available historical observations, with its percentile ranking shown from lowest valuation (1) to highest valuation (100).

Source: MSCI, U.S. Department of the Treasury; Bloomberg Finance, LP; Pitchbook Data Inc.; National Council of Real Estate Investment Fiduciaries. See footnotes for index information.

RISKS TO THE OUTLOOK

Ellwood monitors a range of leading economic cycle indicators (including measures of economic activity, employment, credit conditions, spreads and liquidity) to evaluate the expected trajectory of economic growth. While the majority of indicators are positive as of this writing, we must remain vigilant as several are trending towards levels that create some unease over the sustainability of economic growth as we move forward.

In contemplating factors that could tilt our outlook to be more optimistic or downbeat, trade tensions between the U.S. and China top our list. We think a resolution, in some form of an updated trade deal, could have a meaningful positive impact on market sentiment. Conversely, a continuation of tensions between the world's two largest economies will build additional levels of uncertainty into the market.

As the Federal Reserve moves interest rates to its projection of the neutral Fed Funds rate (the rate the Fed thinks will neither stimulate nor restrain economic growth), it will be challenged to navigate a market anxious about the impact of higher rates on the market and economy.

Finally, no outlook would be complete without mentioning the ongoing Brexit saga. The UK is scheduled to exit from the EU on March 29, and the threat of a no-deal, "hard Brexit" continues to weigh on European market sentiment. The only prediction we can make on macro events with binary outcomes like Brexit is not the outcome, but rather that volatility will remain at elevated levels.

Market conditions are fluid, and Ellwood will continue to process new information to determine if material modifications in our views are necessary.

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International Monetary Fund data source: <http://www.imf.org/external/ns/cs.aspx?id=28>.

Valuation Percentile Ranks chart index information. U.S. Equity P/E is P/E Trailing 12-Months EPS from 1970-2018 and is represented by the MSCI USA index; Int'l Developed Mkts P/E is P/E Trailing 12-Months EPS from 1970-2018 and is represented by the MSCI World ex USA index; Emerging Mkts Equity P/E is P/E Trailing 12-Months EPS from 1995-2018 and is represented by MSCI Emerging Markets Index; 10-Yr Treasury Bond Yield is 10-Year Treasury Constant Maturity Rate from 1962-2018 and is represented by the 10-Year Treasury Constant Maturity Rate; U.S. Corporate Inv Grade Spreads is option-adjusted spread from 1989-2018 and is represented by BloombergBarclays U.S. Corporate Investment Grade Index; U.S. Corporate High Yield Spreads is option-adjusted spread from 1994-2018 and is represented by the BloombergBarclays U.S. Corporate High Yield Index; Emerging Markets (USD) Spreads is option-adjusted spread from 2000-2018 and is represented by BloombergBarclays EM Hard Currency Aggregate Index; U.S. Buyout Multiples is implied EV/EBITDA median from 1995-2018 and is represented by United States, Deal Status: Completed, Deal Type - All Buyout Types; U.S. Commercial Real Estate Cap Rates is Current Value Cap Rates Equal Weighted from 1978-2018 and is represented by NCREIF Property Index.

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Bonds are subject to interest rate, price, and credit risks. Generally when interest rates rise, bond prices fall.

Investments in emerging markets may be less liquid and more volatile. Additional risks include currency fluctuations, and political instability.

Equity investments are more volatile than bonds and subject to greater risks. Small- and mid-cap stocks involve greater risk than large-cap stocks.

High-yield fixed income securities are subject to liquidity and credit risk, and tend to be more volatile than investment grade fixed income.

A real assets strategy is subject to the risk that its asset allocations may not achieve the desired risk-return characteristic, underperform other similar investment strategies or cause an investor to lose money. The risks of investing in REITs are similar to those associated with direct investments in real estate securities. Property values may fall due to increasing vacancies, declining rents resulting from economic, legal, tax, political or technological developments, lack of liquidity, limited diversification and sensitivity to certain economic factors such as interest rate changes and market recessions.

Bank Loans are subject to greater levels of credit risk and liquidity risk than certain other securities. Leveraged loans are considered predominately speculative with respect to the issuer's continuing ability to make principal payments. A downturn or period of risk aversion could adversely affect the market for leveraged loans and reduce an investor's ability to sell its securities.

Alternative investment products, such as hedge funds, private equity, venture capital, private credit, real estates and real assets, are speculative and involve risk. Only investors who understand, and are willing and financially able to assume, the risks of such an investment—including the risk of losing all or substantially all of their investment—should consider investing. Additional risks to consider before investing in alternative investment products include the fact that some products may use leverage that may increase the risk of investment loss, can be illiquid, may involve complex tax structures, and are subject to limited regulatory oversight. For a more detailed discussion of the risks involved with an investment in an alternative investment product, please review the offering materials for the relevant alternative investment product prior to making an investment.

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