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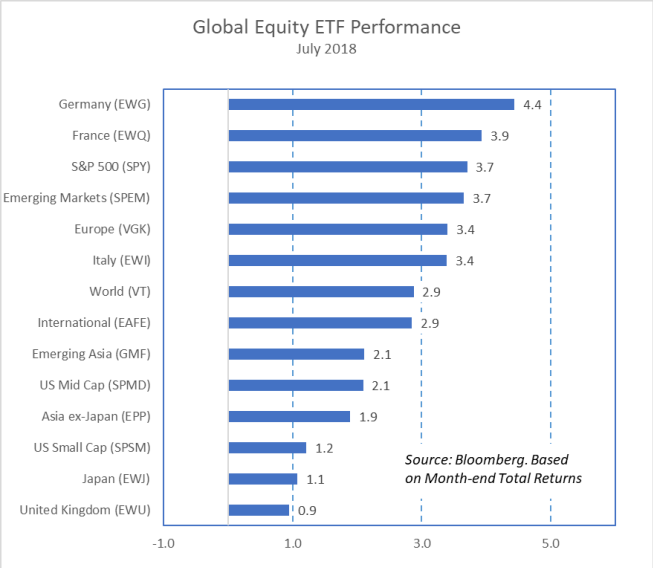
JULY 2018 CAPITAL MARKET REVIEW

July was a "risk on" month as global equities rallied with key European bourses leading the way. Emerging market debt and U.S. corporate bonds outperformed while the broad U.S. bond market was virtually unchanged. A decline in the U.S. dollar provided a boost for non-dollar fixed income.



Equity Markets*

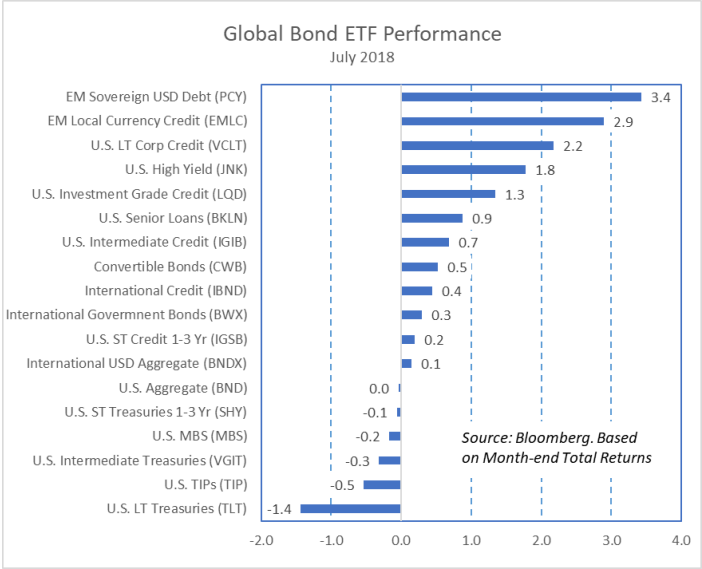
July was a solid month for global equities which advanced by nearly 3%. Key European markets rebounded with Germany and France leading the way, advancing 4.4% and 3.9%, respectively. U.S. Large Caps and Emerging Markets also outperformed broad global equities, both climbing 3.7% for the month.

Overall, Asia lagged most of the western world but still posted attractive results. Emerging Asia rose 2.1% and Developed Asia ex-Japan advanced 1.9%. Japanese equities rose 1.1% for the month.

Bond Markets*

Overall, U.S. bond market returns were flat during July. However, corporate credit rallied in unison with equities, although not as strongly. Safe haven U.S. Treasuries declined in price with long-term Treasuries contracting 1.4% as the yield on the benchmark 10-year Treasury bond rose from 2.86% to 2.96% by month end.

Emerging market debt, both in U.S. dollar and local currency terms, led global bonds, advancing 3.4% and 2.9%, respectively. International bonds were also aided by U.S. dollar weakness as the Bloomberg Dollar Index declined 0.56% during July.



**The returns cited reflect total return performance of exchange traded funds listed in the corresponding bar charts*

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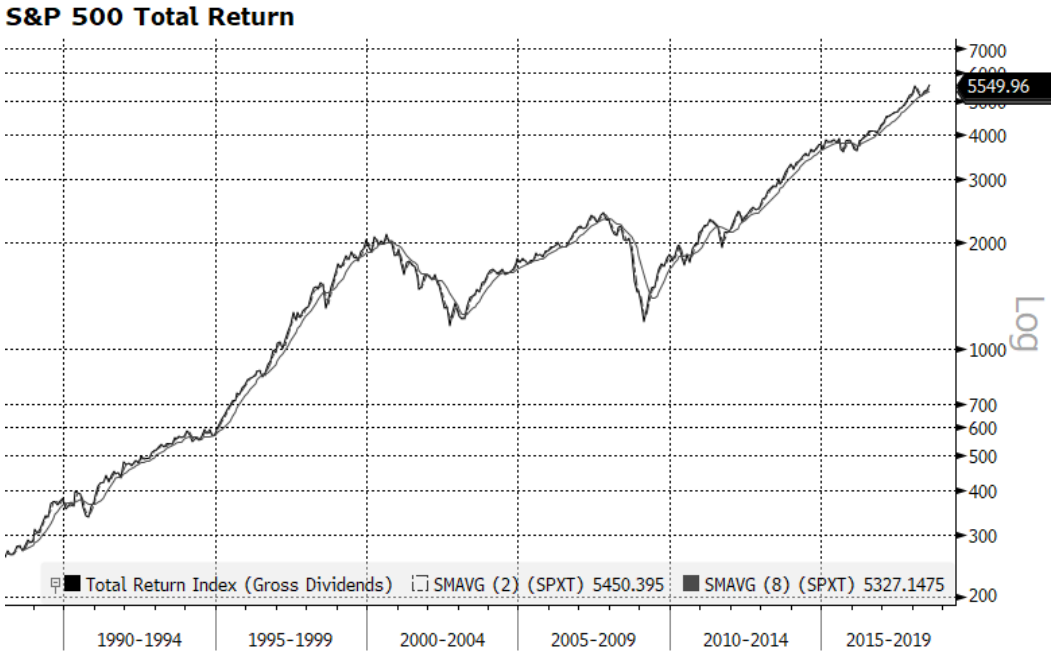
U.S. STOCKS AT A PIVOTABLE POINT

As July came to an end, turbulence returned to U.S. equity markets as several leading social media companies announced disappointing results. However, according to Bloomberg and Bianco Research, approximately 85% of S&P 500 index members have exceeded expectations this earnings season yet the market reaction has been muted to some extent. Investors may be concerned about the length of the current bull market and its ability to climb higher even despite positive U.S. corporate results. This is understandable given how far the S&P 500 has risen since the financial crisis.

However, we would point out that the S&P 500 measured on a total return basis including gross dividends (pictured below in log scale) had a longer and steeper ascent from the late 1980s until the Technology bubble burst in 2000. During the tail end of that period the market was also driven by the Technology sector as it has been in the current cycle, but valuations were bloated as earnings in many cases were weak or non-existent. We are mindful of current valuation metrics and we believe that the overall market can advance further if earnings continue to be robust.

From a market psychology perspective, the last week of the month brought good news—on July 26th, the S&P 500 total return index closed at an all-time high of 5,607.99 which exceeded the January 25th previous high by nearly two points. This may well prove to be a critical point in time for investors.



Source: Standard & Poor's, Bloomberg

See the WCM website for more market commentary or contact us with any questions.

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PORTFOLIO POSITIONING

In terms of overall positioning, we maintain a preference for U.S. equities and cash. Outside the U.S., we also have a favorable view of Asia ex-Japan and Emerging Asia. Our commitments to these equity markets are primarily funded from non-U.S. bonds. Within fixed income, we are underweight the U.S. with a preference for specific sectors including convertible bonds and preferred securities. Our portfolios maintain lower duration than the benchmark. We eliminated our non-U.S. bond exposure earlier in the year. We are overweight cash at the expense of fixed income.

RISK OUTLOOK

Economic activity generally remains robust at home; however, much of the rest of the world appears to be slowing. The following are key risks we are monitoring:

- The U.S economy accelerated to a 4.1% pace of growth in the second quarter, the fastest since 2014. There is some doubt that this pace can be maintained as fiscal stimulus fades and impending tariffs take effect. Higher than expected growth could force the U.S. Federal Reserve to increase the pace of interest rate increases in the second half of 2018 and beyond. Any unexpected upward pressure on interest rates could rattle markets.
- It is still early days in Italy as its new populist coalition government consisting of the Five Star Movement and the far-right League parties begin to govern. There is still concern that euro-skepticism could force an exit from the euro and EU and investors continue to focus on Italy's sovereign debt levels now surpassing 130% of GDP (well beyond EU budget rules) and the limitations that imposes fiscal flexibility.
- As referenced above, ongoing international trade disputes and tariffs among the U.S.'s closest allies, and critically China, may continue to contribute to market uncertainty.
- Britain's exit from the European Union has been a long, arduous process. A disruptive "hard" Brexit could derail economic and trade relationships with the other members of the Union. That could cause Prime Minister Theresa May to lose already weakened support and potentially force her from office.

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KEY EVENTS IN AUGUST

Week 1

- 8/1 U.S.: FOMC Rate Decision
- 8/2 U.K.: BOE Policy Targets
- 8/2 Japan: Nikkei Composite PMI
- 8/2 China: Caixin Composite PMI
- 8/3 U.S.: Employment Rate
- 8/3 U.S.: Markit Composite PMI
- 8/3 U.K.: Markit/CIPS Composite PMI
- 8/3 Eurozone: Markit Composite PMI
- 8/6 Eurozone: Sentix Investor Confidence

Week 2

- 8/8 China: Price Index Surveys
- 8/9 Eurozone: EC publishes economic bulletin
- 8/9 Japan: Q2 GDP
- 8/9-8/10 U.S.: Price Index Surveys
- 8/10 U.K.: GDP (June/Q2)
- 8/14 Eurozone: Q2 GDP
- 8/14 Eurozone: ZEW Expectations Survey
- 8/15 U.K.: Price Index Surveys

Week 3

- 8/16 U.S.: Housing Surveys
- 8/17 U.S.: Conf. Board Leading Indicators

Weeks 4&5

- 8/22 U.S.: FOMC Meeting Minutes
- 8/23 Eurozone: EC Consumer Confidence
- 8/23 Japan: Leading Indicators (June)
- 8/28 U.S.: Conf. Board Expectations Survey
- 8/29 Japan: Consumer Confidence
- 8/30 U.K.: GfK Consumer Confidence
- 8/30 Eurozone: EC Confidence Surveys
- 8/31 U.S.: Univ. of Michigan Sentiment Surveys

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It is important to remember that there are risks inherent in any investment and that there is no assurance that any money manager, fund, asset class, style, index or strategy will provide positive performance over time.

Diversification and strategic asset allocation do not guarantee a profit nor protect against a loss in declining markets. All investments are subject to risk, including the loss of principal.

The information contained herein is based upon the data available as of the date of this document and is subject to change at any time without notice.

Portfolios that invest in fixed income securities are subject to several general risks, including interest rate risk, credit risk, the risk of issuer default, liquidity risk and market risk. These risks can affect a security's price and yield to varying degrees, depending upon the nature of the instrument, and may occur from fluctuations in interest rates, a change to an issuer's individual situation or industry, or events in the financial markets. In general, a bond's yield is inversely related to its price. Bonds can lose their value as interest rates rise and an investor can lose principal. If sold prior to maturity, fixed income securities are subject to gains/losses based on the level of interest rates, market conditions and the credit quality of the issuer.

Foreign investments are subject to risks not ordinarily associated with domestic investments, such as currency, economic and political risks, and may follow different accounting standards than domestic investments. Investments in emerging or developing markets involve exposure to economic structures that are generally less diverse and mature, and to political systems that can be expected to have less stability than those of more developed countries. These securities may be less liquid and more volatile than investments in U.S. and longer-established non-U.S. markets.

An investment in small/mid-capitalization companies involves greater risk and price volatility than an investment in securities of larger capitalization, more established companies. Such securities may have limited marketability and the firms may have more limited product lines, markets and financial resources than larger, more established companies.

Portfolios that invest in real estate investment trusts (REITs) are subject to many of the risks associated with direct real estate ownership and, as such, may be adversely affected by declines in real estate values and general and local economic conditions.
Portfolios that invest a significant portion of assets in one sector, issuer, geographical area or industry, or in related industries, may involve greater risks, including greater potential for volatility, than more diversified portfolios.

Important Disclosures: Exchange-Traded Funds

Exchange-traded funds (ETFs) are investment vehicles that are legally classified as open-end investment companies or unit investment trusts (UITs) but differ from traditional open-end investment companies or UITs. ETF shares are bought and sold at market price (not net asset value) and are not individually redeemed from the fund. This can result in the fund trading at a premium or discount to its net asset value, which will affect an investor's value. Shares of certain ETFs have no or limited voting rights. ETFs are subject to risks similar to those of stocks.

ETFs included in portfolios may charge additional fees and expenses in addition to the advisory fee charged for the Selected Portfolio. These additional fees and expenses are disclosed in the respective fund/note prospectus. For complete details, please refer to the prospectus.

For additional information regarding advisory fees, please refer to the Fee Summary and/or Fee Detail pages (if included with this report) and the program sponsor's/each co-sponsor's Form ADV Part 2, Wrap Fee Brochure or other disclosure documents, which may be obtained through your advisor.

Certain ETFs have elected to be treated as partnerships for federal, state and local income tax purposes. Accordingly, investors in such ETFs will be taxed as a beneficial owner of an interest in a partnership. Tax information for such ETFs will be reported to investors on an IRS schedule K-1. Investors should consult with their tax advisors in determining the tax consequences of any investment, including the application of state, local or other tax laws and the possible effects of changes in federal or other tax laws.