PATHSTONE

MARKET FLASH REPORT

June 2018

KEY TAKEAWAYS

- Markets remained volatile in the second quarter as news headlines were dominated by geopolitics. A strong U.S. economy and increased trade tensions helped lead U.S. small caps upward, outperforming their large cap peers. Non-U.S. equities were negatively impacted from trade rhetoric and political tensions. Additionally a stronger U.S. dollar worried investors in EM assets, which were some of the worst performing assets over the quarter.
- The Fed hiked rates for the second time this year by 0.25% in June. Continued strength of the U.S. economy and firmer inflation supported the rate increase. The median estimate by the Federal Reserve is for two additional hikes this year followed by three next year. The Fed remains committed to steady policy normalization.
- Overseas, monetary policy from the ECB and BOJ remains stimulative. The ECB signaled their intent to wind down their Asset Purchase Program by the end of the year. However interest rates will be held at zero through at least the end of next summer.
- The 10-year Treasury yield curve continues to flatten. Many investors are keeping close watch for the slope to turn negative, which historically has been a strong indicator of forthcoming recession. For now the U.S. economy remains on solid ground and a recession doesn't appear on the near-term horizon.

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INDEX PERFORMANCE (as of 6/30/18)

Equity	Quarter	One-Year	Three-Year
U.S. Large Cap	3.4%	14.4%	11.9%
U.S. Small Cap	7.8%	17.6%	11.0%
Developed Non-U.S.	-1.2%	6.8%	4.9%
Emerging Market	-8.0%	8.2%	5.6%
Real Assets			
Real Estate	2.7%	6.6%	6.8%
Commodities	0.4%	7.4%	-4.5%
Natural Resource Equities	12.1%	19.8%	3.3%
Fixed Income			
Core Plus			
U.S. High Yield Debt	1.0%	2.6%	5.5%
Emerging Market Debt	-10.4%	-2.3%	2.0%
Core Bonds			
U.S. Aggregate Bonds	-0.2%	-0.4%	1.7%
U.S. Treasuries	0.1%	-0.7%	1.0%
U.S. Municipal Bonds	0.8%	0.6%	1.9%

Month-End Values/Yields	Current	Prior Month	One-Year Ago
CBOE Volatility Index	16.1	15.4	11.2
10-Year Treasury Yield	2.9%	2.8%	2.3%

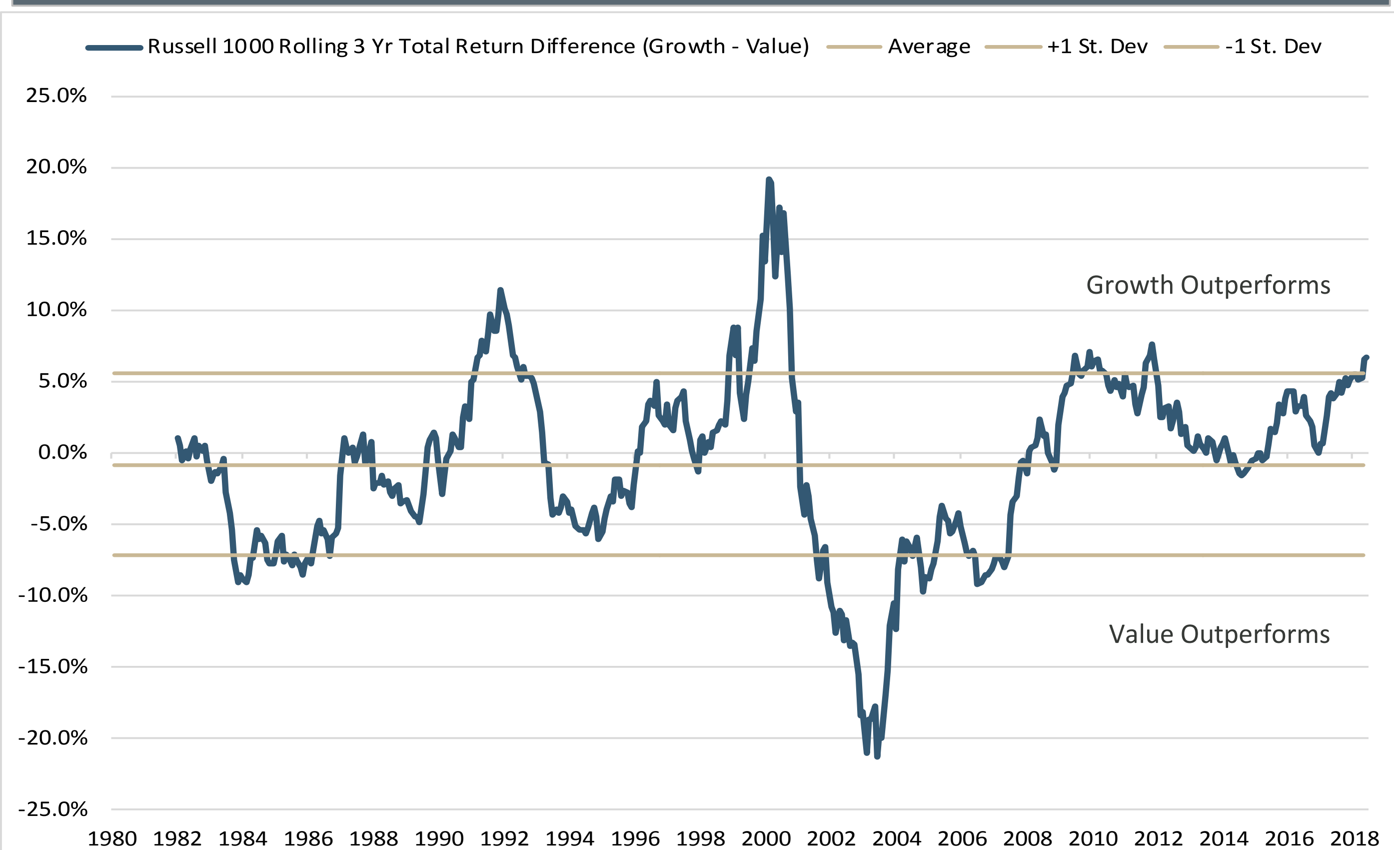
Sources: Bloomberg, Morningstar, treasury.gov.

You cannot invest directly in an index; therefore, performance returns do not reflect any management fees. Returns of the indices include the reinvestment of all dividends and income, as reported by the commercial databases involved.

REGIONAL COMMENTARY

- One theme that has been prevalent in markets this year, particularly within the U.S., is the dominance of growth companies over value. The Russell 1000 Growth index has returned +7.3% so far this year compared to -1.7% for the Russell 1000 Value index.
- Growth companies can be defined to include firms whose share prices have higher price-to-book ratios and higher expected earnings growth rates. Value companies on the other hand are defined as firms whose shares have lower price-to-book ratios and lower expected earnings growth rates. As a result, the growth index tends to be more heavily weighted to technology and consumer discretionary sectors. The value index is more heavily weighted to financials, energy, and utilities.
- Looking at the historical total returns, the recent strength of the growth index has been helped by technology and specifically the FAANG companies, which have propelled the return differential slightly above a one standard deviation historical difference.
- As you can see in the below graph, the leader between these two styles comes and goes in cycles, and particularly can be driven by investor sentiment between the different sectors. Knowing when these tides will turn can be difficult to pinpoint. From a valuation standpoint, forward looking price-to-earnings ratios for both styles are right around their historical averages. Meaning despite Growth's strength, neither index looks too overvalued or undervalued relative to their own histories.

Rolling Three Year Return Differential
Russell 1000 Growth vs. Value



Sources: Bloomberg, Russell Indices.

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DISCLOSURE

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U.S. Large Cap Equity is represented by the S&P 500 Index, with dividends reinvested. U.S. Small Cap Equity is represented by the Russell 2000 Index. Developed Non-U.S. Equity is represented by the MSCI EAFE Index. Emerging Market Equity is represented by the MSCI EM Index. Real Estate is represented by the S&P Global Property Index. Commodities are represented by the DJ UBS Commodity Index. Natural Resource Equities are represented by the S&P North American Natural Resources Index. U.S. High Yield Debt is represented by the Bloomberg Barclays U.S. Corporate High Yield Index. Emerging Market Debt is represented by the JPM GMI-EM Global Diversified Index. U.S. Aggregate Bonds is represented by the Bloomberg Barclays U.S. Aggregate Bond Index. U.S. Treasuries is represented by the Bloomberg Barclays U.S. Treasury Index. U.S. Municipal Bonds is represented by the Bloomberg Barclays Municipal 1-10yr Index.