PRIVATE WEALTH SERVICES GROUP

Our Thinking

Overview

After a period of relative calm in the stock market which dominated in 2017, volatility returned in the first quarter of 2018, with the market posting its first quarterly loss since 3rd quarter, 2015. 2018 volatility has been attributed to (1) worries of increased inflation/recession; (2) a protectionist shift in U.S. trade policy, including tariffs and a trade "skirmish" with China; and (3) the prospect of greater regulatory scrutiny over large technology companies.

When volatility rises, it is natural to pause and reflect more intensely on forward-looking views. As shared in past "Our Thinking" publications, we remain constructive on equities over the medium to long term. We consider a further 5-10% "correction" still possible, and we would view such a move as a buying opportunity. Furthermore, we believe the Federal Reserve (Fed) will continue to raise its benchmark Federal Funds rate at a measured pace; and that inflation will remain in check. Looking beyond the events of the past quarter, we expect rates to continue rising, albeit slowly, over the next couple years. We view the risk of recession in the near term as low.

The Economy

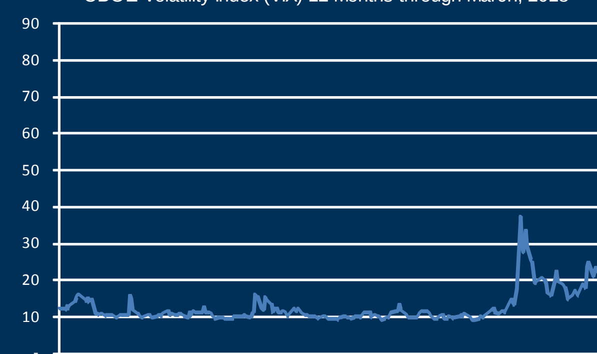
In the first quarter of 2018, the U.S. macroeconomic landscape remained strong as the economy continued its gradual progression through the business cycle and on the heels of the recent passing of the tax legislation in 2017. Most U.S. economic indicators reflect a period of "Goldilocks" with glimpses of late-cycle trends emerging.

Typically, the late cycle is characterized by a tight labor market which often leads to higher wages, and thereby, lower profit margins and earnings. These higher wages also lead to higher inflation forcing the Fed to tighten monetary policy which eventually leads to tighter credit conditions.

Volatility Returns

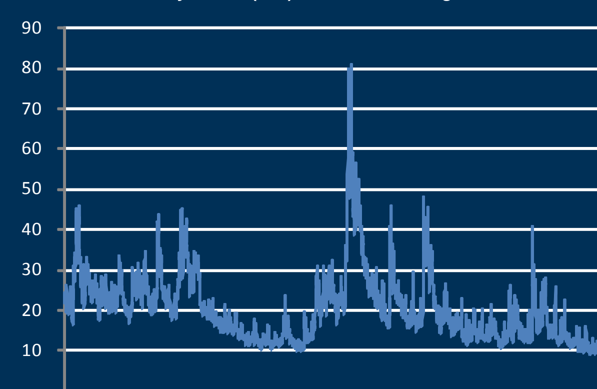
The two graphs below present the CBOE Volatility Index (often referenced by its ticker symbol "VIX") over 20 years and the last year. A popular measure of the expectation of the stock market's volatility as implied by S&P 500 index options, VIX is calculated and published by the Chicago Board Options Exchange (CBOE). The analysis shows that this recent increase in volatility is below the highs of the past, but there was a meaningful increase in first quarter 2018 relative to the calmer period in 2017.

CBOE Volatility Index (VIX) 12 Months through March, 2018



Source: S&P Capital IQ

CBOE Volatility Index (VIX) 20 Years through March, 2018



Source: S&P Capital IQ

STIFEL

During the 1st quarter, employment growth continued at a moderate pace while the Fed noted in its March 7 Beige Book publication that "labor market tightness and brisk demand for qualified workers" is starting to translate to an increase in hourly wages. For the first time in recent discussion about labor, the language around wage increases was upgraded from "modest" to "moderate." The unemployment rate has held at 4.1% for the last 6 months.

U.S. GDP for the fourth quarter of 2017 was revised to a final reading of 2.9%, up from 2.5%. This upward revision was due to higher inventory levels and higher consumer spending – a positive, as consumption drives roughly two-thirds of GDP. However, in the first quarter, what we witnessed was a reversal in retail spending. Headline and core retail sales have now declined for three months in a row. Nevertheless, the U.S. economy is still expected to perform well this year, bolstered by both tax legislation and fiscal stimulus. As of April 2, the Atlanta Fed's estimate of first quarter GDP is 2.3%.

Economic data outside the U.S. also remains robust. In the Eurozone, the composite PMI fell to 55.3 in March, marking a second consecutive decline from its 12 year high in January. Although the PMI has trended lower over the past two months, a reading above 50 signals expansion in manufacturing activity. Overall in 2017, euro zone GDP rose 2.5%, the fastest growth rate since 2007. In the Asia-Pacific region, Japan's economy continued to expand, in the latest March estimate fourth quarter GDP was revised up to 0.4%, versus median economist estimates for 0.2%. This marked eight straight quarters of growth – the longest growth run in the past 28 years.

The Federal Reserve

In March, the Federal Reserve's Open Market Committee voted to increase the federal funds rate target range to 1.50% - 1.75%. This marked the sixth rate increase since the Fed began raising rates in December, 2015. The economic projections were slightly more hawkish than the market anticipated. The widely tracked "dot plot" now implies a third hike in 2019 and two hikes in 2020. This increases the cumulative hikes forecasted by the FOMC between 2018 and 2020 from 6 ¾ to 8. This is probably a result of its stronger growth forecast, indicated by the upward revision to 2019 real GDP.

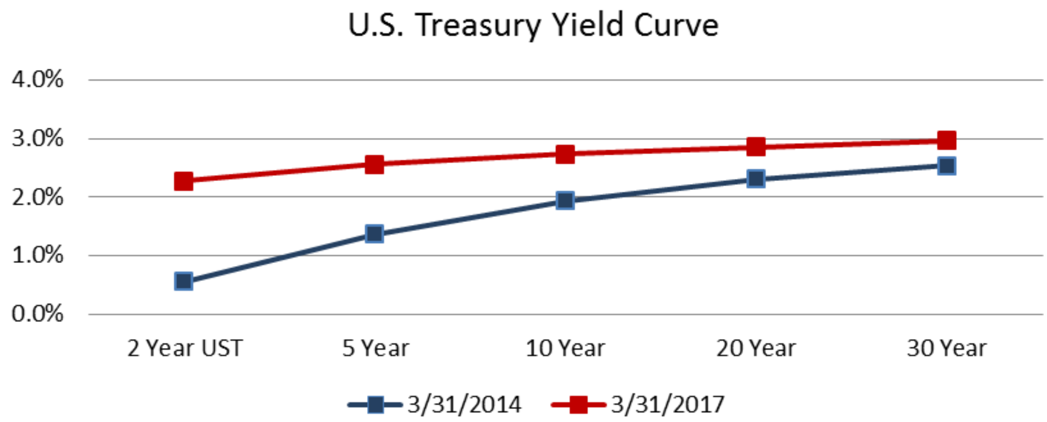
Another economic projection worth noting is the Fed's core PCE inflation forecast. Recently the media has discussed the possibility of the Fed falling "behind the curve," if inflation was to meaningfully pick up. This is, in part, what led to the sell-off in February after the employment report sparked concerns about faster than expected rises in wage and price inflation. While inflation is expected to inch higher, we don't foresee rapidly rising inflation. The Fed projected a modest overshoot of their inflation target (2%) and projected 2.1% in 2019 and 2020. This is likely a result of additional fiscal stimulus and a weaker dollar serving as tailwinds.

Newly appointed Fed Chairman Jerome Powell emphasized that the Fed will remain data dependent when setting policy and we continue to believe that future hikes will be at a measured pace.

Interest Rates

U.S. Treasury yields rose across the curve as expectations of inflation, interest rates, and growth moved higher. The Treasury curve continued to flatten modestly in the quarter, with the shorter end of the curve impacted by a rate hike and substantial bill issuance in March. The U.S. 10-year increased from 2.41% to start the year to as high as 2.95% in February before settling at 2.74% at the end of the quarter. Two-year yields increased from 1.89% to 2.27%. The 2-year to 10-year spread narrowed from 52 basis points to 47 basis points.

A big topic in 2017, the flattening yield curve remains in focus in 2018, as historically a flattening curve has been a harbinger to an economic downturn. While we continue to monitor the flattening of the curve and economic conditions, we don't believe that this is an indication of a future slowdown in growth in the near term. Conversely, we think that part of the flattening is due to strong demand for U.S. Treasuries as they have a more attractive yield than their international counterparts, which are yielding close to zero in many developed nations. Furthermore, we believe that the gradual reduction in the Fed's Treasury holdings along with a larger bond issuance will possibly lead to upside pressures at the long end of the cure.



Source: U.S. Treasury Website

The Equity Market - Earnings

Fourth quarter earnings recovered after the anomaly third quarter, which was a result of hurricanes Harvey and Irma. Approximately 75% of public companies reported earnings that surpassed Street expectations. (Historically, it is common for two-thirds of the index to beat the consensus analyst estimates.) The S&P 500 collectively posted a 14.5% increase in earnings versus the prior year. Energy, materials, and technology continued to post notable growth, up 112.6%, 32.0%, and 22.2%, respectively. For the full year 2017, S&P 500 earnings grew 12.8% and are expected to grow 19.7% in 2018. Analysts have been increasing their estimates of earnings per share to take into account the lower corporate tax rate. In fact, analysts have revised up the 1Q 2018 estimate by 5.4%, the largest increase since FactSet began tracking this statistic in 2002.

Investment Themes

The following table summarizes our thinking across various asset classes and regions.

Asset Class		View	Comments
Equity	U.S.	▼	We view U.S. Equity market valuations to be elevated, but not in a bubble. The S&P 500 trades at 16x earnings versus its 20-year average of 16x as of 3/31. The U.S. economy remains resilient, but in the latter stages of a cyclical bull market. Corporate tax cuts are expected to provide a boost for earnings, however, double-digit earnings growth will be more difficult to achieve on account of tougher comparisons. As we put new money to work, we lean toward non-U.S. markets. We consider a further correction still possible, which we would view as a potential buying opportunity.
	Europe	▲	The euro zone's economic growth outpaced the U.S. during the third quarter of 2017 and is on track for its best year since 2010. Improving economic growth, supportive fundamentals, and accomodative monetary policy from the ECB is expected to bode well for equities. We maintain our overweight, with a focus on larger, more established companies. Despite diminishing to some degree, political and policy risk may weigh on sentiment.
	Japan	▲	We've maintained a view that Japan will be the leader in Asia, so we are overweight here. Improving consumer consumption trends and a revamp in industrial production and investment have spurred growth in the economy. Connected to our themes of financials/banks, we've included Japanese banks in our non-U.S. Quality Dividend model.
	Asia ex-Japan	▼	We're keeping a close eye on Asia generally, and tilt toward Japan in the region, underweighting other countries.
	EM	▲	We are very measured investing in emerging markets, which alone can be quite volatile. We are modestly overweight in our diversified non-U.S. model and have modest exposure to Latin America in our non-U.S. Quality Dividend model.
	Themes	■	We remain focused on a number of themes: financials/banks, both in the U.S. and elsewhere; infrastructure, energy, healthcare, retail, and technology, including cyber security. Given the increasing pace of technological advancement, we are also focused on companies across industries that are impacted by the "Fourth Industrial Revolution."
Fixed Income	Duration/ Cash Flow Profile	▼	We see interest rates trending higher. Thus, we typically maintain a duration profile - a key measure of interest rate sensitivity - shorter than that of the market. For clients focused on cash flow, we are constructive to put money to work in a rising-rate environment.
	U.S. Government Bonds	▼	U.S. government bonds dampen credit risk and serve as an important tool to manage interest rate risk. In our taxable bond model, we maintain exposure here but are underweight, being constructive on other sectors of the bond market.
	U.S. Municipals	▲	Municipal bonds are our core exposure in fixed income. We typically invest in A- or AA-rated bonds, and prefer to hold to maturity. We currently invest in intermediate maturities, buying longer bonds only when we find the yield compelling.
	U.S. Credit	▲	In the taxable bond market, we are constructive on "credit" exposure - obtaining an extra yield to hold non-U.S. government bonds. This corresponds to our view that the economy continues to strengthen, benefiting corporate issuers.
	U.S. High Yield	■	In our taxable bond model, we will sometimes build a modest position in below-invesment-grade "high-yield" bonds. However, we see these as fully valued and have no exposure in the model.
	Themes	■	With an improving economy and a trend toward higher interest rates, our focus is on assessing the tradeoffs of maturity (how long to own a bond) and the cash flow/yield the bond provides. We like credit, especially short and intermediate credit exposure.

▲ overweight ▼ underweight ■ neutral

Capital Markets Recap

During the first quarter, stocks were volatile, bonds posted negative returns, and commodities were mixed.

Global Stocks

Global equity markets continued their ascent to start the year. January was an extension of the prior year's rally as the market advanced on optimism from the recently enacted tax legislation. On January 26, the S&P 500 reached an all-time high of 2,872. However, after 15 months of positive returns, volatility returned in February. As mentioned above, the employment report at the start of the month spooked investors as it showed a surprise pickup in hourly wages. The market was quick to price in more aggressive Fed tightening and bond yields rose, causing the equity market to decline. The S&P 500 fell 8.6% in the first 6 trading days to start the month before rallying slightly to end the month down 3.7%. Volatility continued in March as concerns of a potential trade war surfaced and the S&P had 9 trading sessions where it moved more than 1%. (As a point of reference, the S&P had just 8 days where it traded more than 1% in either direction in all of 2017.) The S&P 500 Index finished the quarter with a decline of 0.8%. Going into the second quarter, we expect that volatility will remain as uncertainties remain related to (I) NAFTA, (ii) trade issues with China, and (iii) geopolitical tensions in regions such as Syria and North Korea.

The Information Technology sector was the best performing sector in the first quarter despite the recent sell-off. The sector ended the quarter up 3.5%. Telecom and Energy was the weakest, down 5.7% and 5.2%, respectively. Growth stocks once again outperformed value stocks, with the Russell 1000 Growth up 1.4% vs. the Russell 1000 Value down 2.8%. Small cap stocks, as represented by the Russell 2000 Index, outperformed large caps, finishing the quarter with a total return of -0.1%.

Emerging markets (EM) outperformed foreign developed markets to start the year as the concern surrounding trade tensions was less prevalent and a weaker U.S. dollar served as a headwind. In the first quarter the MSCI EM Index was up +1.4%. The MSCI EAFE Index, representing non-U.S. developed markets, was down -1.5%. Europe and Japan were weak due to worries about the path of U.S. interest rates and the tensions surrounding global trade.

Fixed Income

The first quarter of 2018 has been marked with a broad selloff across the fixed income markets. The rise in rates stalled in the second half as tariffs and geopolitical issues sparked a flight into fixed income and away from equities and risk assets. The yield on the 10-year Treasury rose to a high of 2.94% (up 54 basis points from the start of the year) and ended the quarter at 2.74%.The 2-year Treasury rose as high as 2.34% and closed the quarter up 38 basis points at 2.27%. The Barclays Aggregate Index, representing investment-grade taxable bonds, declined -1.5% for the quarter. The Barclays Muni Aggregate Index, representing investment-grade municipal bonds, declined 1.2% for the quarter. High yield bonds, as measured by the BofA ML U.S. High Yield Master II Index declined 0.9% for the quarter.

Commodities

The S&P Goldman Sachs Commodity index advanced 2.2% in the first quarter. The momentum in oil prices continued into 2018, however, prices were more volatile than previous quarters. West Texas Intermediate started the year at $60.42 per barrel and finished the quarter at $64.94, up 7.5%. Natural Gas saw a large spike in prices to start January, rising from $2.95 to $3.63, increasing 23%. Ultimately, prices declined and ended the quarter at $2.73. The spike was mostly attributed to a harsher-than-expected winter and below normal temperatures. Gold remained range bound at appreciated levels, relative to the recent low in December 2017. Gold was trading at $1,327.30 at the end of the quarter, up 1% from the start of the year.

Market Returns						
Equity	**1 Month**	**YTD**	**1 Year**	**3 Years**	**5 Years**	**10 Years**
Dow Jones Industrial Average	-3.6%	-2.0%	19.4%	13.5%	13.3%	9.9%
S&P 500	-2.5%	-0.8%	14.0%	10.8%	13.3%	9.5%
Russell 1000	-2.3%	-0.7%	14.0%	10.4%	13.2%	9.6%
Russell 2000	1.3%	-0.1%	11.8%	8.4%	11.5%	9.8%
Russell 3000	0.3%	-0.7%	13.1%	9.4%	12.9%	9.2%
MSCI AC World Index	-2.1%	-1.0%	14.9%	8.1%	9.2%	5.6%
MSCI All Country ex USA	-1.8%	-1.2%	16.5%	6.2%	5.9%	2.7%
MSCI EAFE	-1.8%	-1.5%	14.8%	5.6%	6.5%	2.7%
Fixed Income						
Barclays Aggregate	0.6%	-1.5%	1.2%	1.2%	1.8%	3.6%
Barclays U.S. Muni Bond	0.4%	-1.1%	2.7%	2.3%	2.7%	4.4%
Barclays VLI High Yield	-0.7%	-1.2%	3.0%	4.4%	4.4%	8.0%
Other						
S&P Goldman Sachs Commodity	2.2%	2.2%	13.8%	-4.2%	-11.9%	-10.8%
Dow Jones US Select REIT	3.9%	-7.4%	-3.7%	0.7%	6.0%	6.0%

Source: Morningstar. Past performance is no guarantee of future results.

As of March 31, 2018. Periods greater than one year are annualized.

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There are special considerations associated with international investing, including the risk of currency fluctuations and political and economic events. Investing in emerging markets may involve greater risk and volatility than investing in more developed countries. Due to their narrow focus, sector-based investments typically exhibit greater volatility. When investing in bonds, it is important to note that as interest rates rise, bond prices will fall. High yield bonds have greater credit risk than higher quality bonds. Small company stocks are typically more volatile and carry additional risks, since smaller companies generally are not as well established as larger companies. The risk of loss in trading commodities can be substantial. You should therefore carefully consider whether such trading is suitable for you in light of your financial condition. The high degree of leverage that is often obtainable in commodity trading can work against you as well as for you. The use of leverage can lead to large losses as well as gains. Changes in market conditions or a company's financial condition may impact a company's ability to continue to pay dividends, and companies may also choose to discontinue dividend payments.

Exchange Traded Funds (ETFs) are subject to market risk, including the possible loss of principal, and may trade for less than their net asset value. ETFs trade like a stock, and there will be brokerage commissions associated with buying and selling exchange traded funds unless trading occurs in a fee-based account. Investors should consider an ETF's investment objective, risks, charges, and expenses carefully before investing. The prospectus, which contains this and other important information, is available from your Financial Advisor and should be read carefully before investing.

The **Dow Jones Industrial Average** is an index that shows how 30 large, publicly owned companies based in the United States have traded during a standard trading session in the stock market. The **Standard & Poor's 500 Index** is a capitalization-weighted index that is generally considered representative of the U.S. large capitalization market. The **Russell 1000 Index** measures the performance of the 1,000 largest companies in the **Russell 3000 Index**, which measures the performance of the 3,000 largest U.S. companies based on total market capitalization. The average market capitalization is approximately $11 billion, and the median market capitalization is approximately $3.5 billion. The **Russell 2000 Index** measures the performance of the 2,000 smallest companies in the broader **Russell 3000 Index**, which measures the performance of the 3,000 largest U.S. companies based on total market capitalization. The average market capitalization is approximately $490 million, and the median market capitalization is approximately $395 million. The Russell 3000 Index measures the performance of the 3,000 largest U.S. companies based on total market capitalization, which represents approximately 98% of the investable U.S. equity market. The average market capitalization is approximately $4 billion, and the median market capitalization is approximately $700 million. The **MSCI ACWI Index** is a free float-adjusted market capitalization-weighted index that is designed to measure the equity market performance of developed and emerging markets. The **MSCI World ex USA All Cap Index** captures large-, mid-, small-, and micro-cap representation across 22 of 23 Developed Markets (DM) countries (excluding the United States). With 8,138 constituents, the index covers approximately 99% of the free float-adjusted market capitalization in each country. The **MSCI EAFE Index** (Europe, Australasia, and the Far East) is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the U.S. and Canada. The **Barclays U.S. Aggregate Index** is comprised of the Barclays Capital U.S. Government/Credit Index and the Barclay Capital Mortgage-Backed Securities Index. All issues in the index are rated investment grade or higher, have at least one year to maturity, and have an outstanding par value of at least $100 million. The **Barclays U.S. Municipal Bond Index** covers the USD-denominated long-term, tax-exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds, and pre-refunded bonds. **BofA Merrill Lynch U.S. High Yield Master II Index** is a market value-weighted index of all domestic and yankee (bonds denominated in U.S. dollars and issued in the U.S. by foreign entities) high yield bonds, including deferred interest bonds and payment-in-kind securities. The **S&P GSCI** (formerly the Goldman Sachs Commodity Index) serves as a benchmark for investment in the commodity markets and as a measure of commodity performance over time. The index was originally developed by Goldman Sachs. In 2007, ownership transferred to Standard & Poor's, who currently own and publish it. Futures of the S&P GSCI use a multiple of 250. The **S&P GSCI** contains as many commodities as possible, with rules excluding certain commodities to maintain liquidity and investability in the underlying futures markets. The index currently comprises 24 commodities from all commodity sectors. The **Dow Jones U.S. Select REIT Index** intends to measure the performance of publicly traded REITs and REIT-like securities. The index is a subset of the Dow Jones U.S. Select Real Estate Securities Index (RESI), which represents equity real estate investment trusts (REITs) and real estate operating companies (REOCs) traded in the U.S. The indices are designed to serve as proxies for direct real estate investment, in part, by excluding companies whose performance may be driven by factors other than the value of real estate. **Euro STOXX 50® Index** represents the performance of the 50 largest companies among the 19 supersectors in terms of free-float market capitalization in 12 Eurozone countries. The index has a fixed number of components and is part of the STOXX blue-chip index family. The index captures about 60% of the free-float market cap of the EURO STOXX Total Market Index (TMI). **The Barclays U.S. Corporate Index** covers USD-denominated, investment grade, fixed rate, taxable securities sold by industrial, utility, and financial issuers. It includes publicly issued U.S. corporate and foreign debentures and secured notes that meet specified maturity, liquidity, and quality requirements. Securities in the index roll up to the U.S. Credit and U.S. Aggregate Indices. **The MSCI EM (Emerging Markets) Europe, Middle East and Africa Index** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the emerging market countries of Europe, the Middle East & Africa. **The Bloomberg Barclays US Corporate High Yield Bond Index** measures the USD-denominated, high yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below. Bonds from issuers with an emerging markets country of risk, based on Barclays EM country definition, are excluded.

Index returns include the reinvestment of dividends but do not include adjustments for brokerage, custodian, and advisory fees. Indices are unmanaged, do not reflect fees or expenses, and are not available for direct investment. Past performance is no guarantee of future results.

Models mentioned herein are within the Stifel Solutions Program, in which approved Financial Advisors manage their clients' assets on a discretionary basis through the consistent application of a pre-screened investment process. Since all investment decisions in a Solutions account are made by the Financial Advisor(s) on the client's behalf without having to receive prior approval, it enables the Financial Advisor(s) to quickly react to volatile market conditions in order to execute the investment strategy. It is also paramount that Solutions clients have detailed knowledge of their Financial Advisors' individual investment philosophy and decision-making process before entrusting him or her with their portfolio. There is no guarantee that the objectives of the portfolio strategy will be achieved. Investing involves risk, including the possible loss of principal. The Stifel Solutions Program has an annual asset-based fee, charged quarterly, that covers costs, including trade execution, custody, and performance reporting. There may be other costs associated with the Stifel Solutions Program, including but not limited to: exchange fees, transfer fees, interest expense, trade surcharges, and closing costs. Ask your Financial Advisor for a Disclosure Brochure, which further outlines the fees, services, exclusions, and disclosures associated with this program. You should consider all terms and conditions before deciding whether the Solutions Program is appropriate for your needs.

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