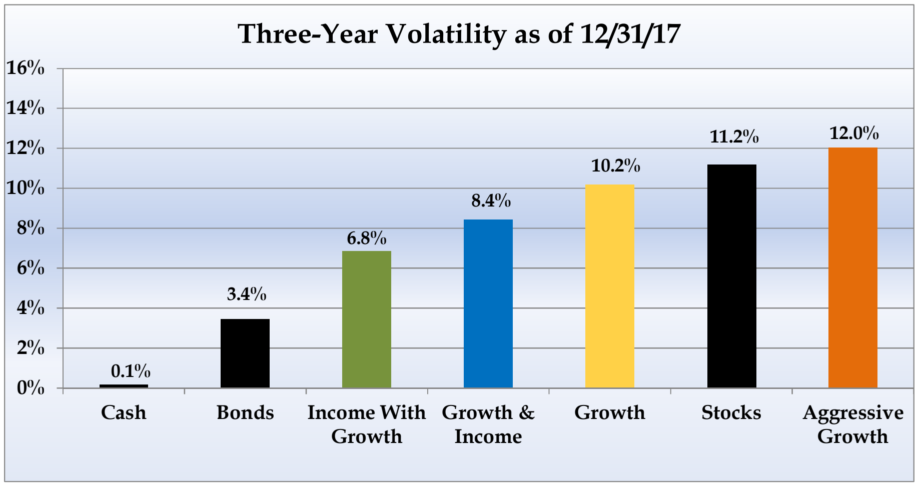
ASSET ALLOCATION QUARTERLY
First Quarter 2018

Asset allocation is a portfolio management process where various asset classes (stocks, bonds, commodities, etc.) are combined in one portfolio. Diversification helps to avoid having 'all eggs in one basket.' Risk and return are considered for the entire portfolio as opposed to evaluating individual securities or investments.

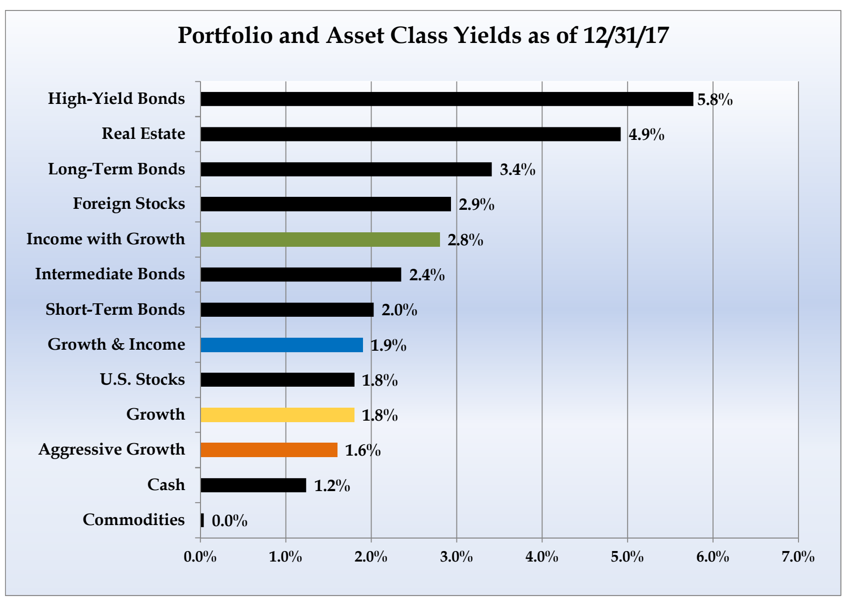


Source: Bloomberg, CIM. Cash is the ML 0-3 Month T-Bill Index; Bonds are the ML Domestic Master Index; Stocks are the S&P 500 Index. *See disclosures on page 6 for important details.

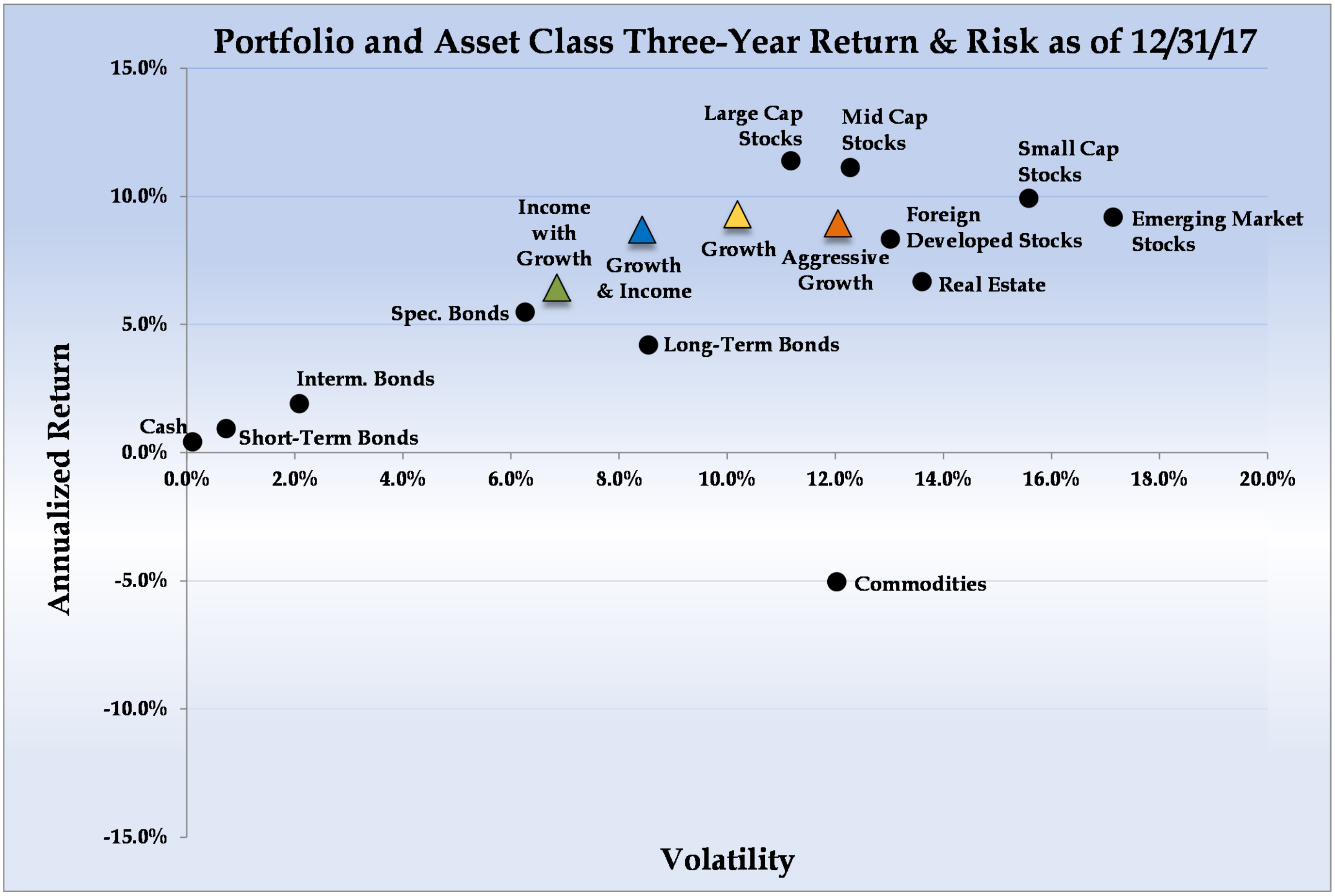
The Confluence asset allocation process is centered upon risk management. Our portfolios offer a broad spectrum of risk profiles, ranging from a fairly conservative posture in Income with Growth (green) to a more risk tolerant profile in Aggressive Growth (orange). The primary asset classes of cash, bonds and stocks are illustrated in the black bars for reference in the above chart.

We recognize that risk levels and return potential rise and fall over market and economic cycles. Therefore, we apply a dynamic process, one that evaluates the economy, interest rates, regulation, valuations and other investment variables in a forward-looking context. Although we seek return opportunities, we do so with a consideration for the amount of risk taken to pursue these returns.

For many investors, income is an important objective and we make it a priority in our income-oriented portfolios. However, we balance the income objective relative to our outlook for various asset classes. Often times, higher yields may not translate into attractive return/risk tradeoffs. This chart shows the recent gross yields of our portfolios, relative to several asset classes.



Source: Bloomberg, CIM. Portfolio yields are before fees. *See disclosures on page 6 for asset class composition and other important details.



Source: Bloomberg, CIM, using monthly data and gross returns. *See disclosures on page 6 for asset class benchmark details.

PORTFOLIO AND ASSET CLASS COMMENTARY

This chart illustrates the return and volatility for a variety of asset classes, as well as the composite performance for our asset allocation portfolios. It reveals how different kinds of asset classes and our portfolios have performed over the rolling three-year period ending December 31, 2017.

In a continuation from last year, the strategies positioned for lower volatility have also experienced more muted returns. Using standard deviation as a measure of risk, the volatility cadence has proceeded in a stepwise progression from the more conservative Income with Growth strategy through Aggressive Growth. The annualized returns followed in accordance with their respective volatilities, with the sole exception of Aggressive Growth, which fell slightly shy of the returns compiled by the Growth strategy. Lower returns recorded by U.S. small cap equities, where the Aggressive Growth strategy had an express overweight, were responsible for this relative lag.

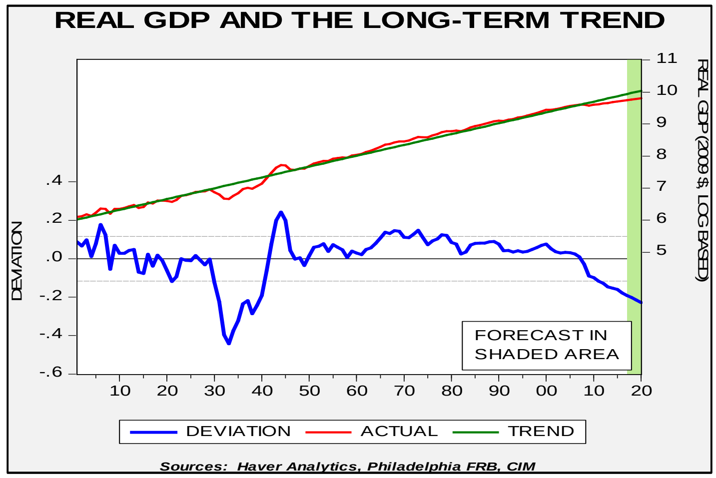
Accommodative monetary policies and an increase in investor risk appetites have prevailed over this time period. This environment is framed by the asset classes in the chart above and underscores the notion that equities have been amply rewarded relative to bonds. In the Confluence strategies where income is an objective, equity allocations remain high by historical standards. Although elevating the volatility, the exposures have assisted in capturing higher returns. While the long-term bond exposures in the income-oriented strategies have been regularly trimmed each quarter since mid-2016, the duration has exceeded that of the broader bond market indices and has proven beneficial to the portfolios. Non-U.S. equities were absent during the U.S. dollar rally from mid-2013 through the end of 2016 to the benefit of all strategies. However, our expectations for a softer U.S. dollar and favorable valuations abroad led us to add non-U.S. positions in mid-2017 to all strategies in risk-adjusted proportions, which subsequently had a positive impact on returns.

The positive economic landscape over the past three years is reflected in the chart above. Our outlook is for a continued favorable environment for risk assets given the ramifications of the recently passed tax legislation combined with positive business and investor sentiment. Although our forecast harbors solid expectations, we regularly reassess signals that could change our macroeconomic outlook and expected returns and volatility for each asset class. We remain cognizant that sentiment may shift, Fed actions may lead to a policy mistake and/or geopolitical risk may become elevated. Consequently, we regularly evaluate the risk exposures for all the strategies given our perception of the environment over our three-year forecast period, and any changes that might occur to the economic outlook would cause us to adopt a more risk-averse posture for the strategies.

FIRST QUARTER 2018 ASSET ALLOCATION OUTLOOK

- **The passage of the Tax Cuts and Jobs Act of 2017 significantly increased our earnings forecast for the S&P 500 for 2018 from $129.82 to $144.84.**
- **We do not expect major changes to economic growth stemming from the tax legislation.**
- **Fed policy should continue to tighten through increases in the fed funds rate and a reduction in the size of the Fed's balance sheet.**
- **An increased federal deficit factors into our outlook for softness of the U.S. dollar versus other currencies.**
- **We initiate a laddered structure for bonds in strategies where income is a factor.**
- **Overall equity exposures remain elevated across all strategies relative to historic allocations.**
- **Our sector and industry outlooks favor a growth style bias at 60%.**

ECONOMIC VIEWPOINTS



The most significant domestic economic news since last quarter was the passage of tax reform legislation in December, known colloquially as the Tax Cuts and Jobs Act of 2017. While the implications for corporate profitability and a rising federal deficit are substantial and will certainly affect financial markets, our analysis supports the notion that the effects on economic growth will be minimal. Throughout this expansion, GDP has remained beneath its long-term trend, with average real growth of 2.2%.

This slower growth, combined with deregulation and globalization, has encouraged a low inflationary environment, both domestically as well as across developed countries. Our expectations for the year, which help frame our view of our three-year forecast period, is that the economy will remain on its trajectory of modest real GDP growth and inflation will be tame despite a low level of unemployment. Against this backdrop, we expect Fed policy to hold course in raising fed funds and possibly become slightly more hawkish given the changes to the FOMC voting roster. While the potential exists for a policy mistake by the Fed, even with such a mistake our analysis leads to the conclusion that it would not engender an effect until 2019.

Although our forecasts for GDP and inflation are sanguine, consumer and business sentiment remain elevated. The conflation of such high sentiment, tax changes and low inflation may lead to what many describe as a “melt-up” in the equity markets. Though fundamental metrics such as P/E or earnings yield underscore the notion that equities in general are fully valued, we note that such conditions may not only persist for an extended period of time, but can become even more pronounced. While this is not our base case, we view the odds as higher than normal.

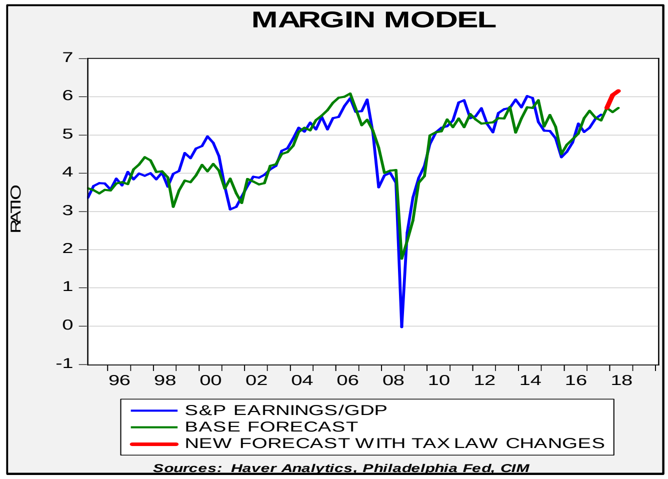
Beyond the U.S., a number of issues harbor some degree of uncertainty, notably the upcoming Italian election and its potential to further splinter the EU, the ECB’s tapering of its bond purchase program and China’s ongoing efforts to control credit growth. Despite these uncertainties, we are constructive on developed market economies. Moreover, based on purchasing power parity, which is a measure of exchange rate valuation based on relative inflation rates, we find the U.S. dollar remains overvalued relative to the euro, pound, yen and Canadian dollar. Regarding emerging economies, there is obviously a wide divergence of economic activity. Nevertheless, in the aggregate, emerging economies are helping to propel global growth and arguably the basket of emerging market currencies holds appeal relative to the U.S. dollar. For U.S.-based investors, a weakening dollar acts as a tailwind for foreign investing.

STOCK MARKET OUTLOOK

Based on our outlook for the economy and the effects of tax legislation, our expectations for U.S. equities are favorable. Our updated earnings forecast for the S&P 500 for 2018 is now $144.84, which represents an 11.6% increase over our previous forecast of $129.82 prior to the passage of the tax legislation.

On the accompanying chart on the next page, the blue line shows the ratio of total S&P 500 earnings to GDP and the green line is the forecast from our margin model. This includes productivity measures, global integration, several interest rate variables, corporate cash flow, the dollar and oil prices.

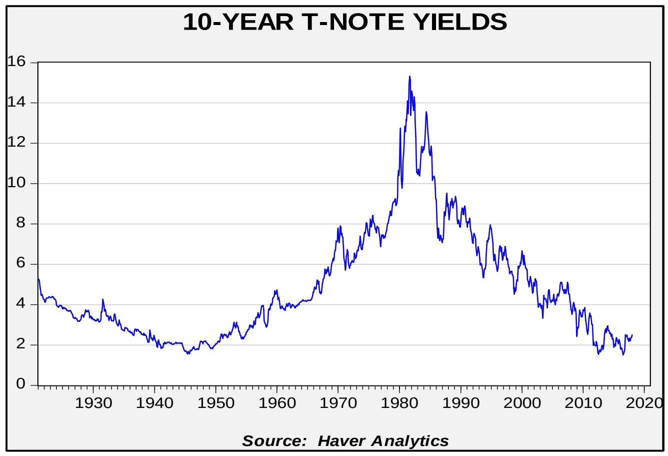
The red line shows our forecast impact of the new legislation. As the chart indicates, we are expecting a significant effect, with S&P 500 profits expected to exceed 6%, a record level.



Our new forecast is aggressive and is supportive of the continuation of elevated equity exposures across all strategies relative to our historic allocations. With lower corporate tax rates, cash flow will be higher and, combined with repatriated overseas cash, we expect increased dividends, share buybacks and acquisitions, which should be favorable for the stock market.

Given our overall outlook for equities, we have moved to a 60% tilt toward growth and 40% to value. In U.S. large caps, we overweight technology, energy, financials and materials. Mid-cap and small cap equities have the same tilt toward growth and are both overweight in the more growth-oriented strategies. Outside the U.S., we retain our historic maximum exposure owing to our expectations of continued softness in the U.S. dollar exchange rate.

BOND MARKET OUTLOOK



The rise in Treasury yields since the passage of the tax legislation in December has led many commentators to suggest that a bear market in bonds has developed. Though we tend to agree with this assessment, we believe that a secular bear market commenced in 2016 and the prospect is for a *gradual* increase in rates over not only our forecast period of three years, but likely beyond. The operative word in the previous sentence is gradual as historically problems engendered by bond bear markets take years to manifest. As the top chart on the right illustrates, the last secular bond bear market that began in 1945 took over two decades, when yields rose above 5% in the late 1960s, for rising rates to have an adverse impact on financial markets.

For a longer term perspective, the lower chart on the right displays the interest rate of U.K. Consols beginning in 1701. What is notable is that both bull and bear markets for bonds endure for long periods of time. Though the British bond bear market following WWII had enormous magnitude, the length was actually fairly normal. For a more detailed analysis of the potential causes and implications of a bear market in bonds, please refer to our *Asset Allocation Weekly* report (1/19/18).

Over the forecast period, we envision the terminal fed funds rate to be in the range of 2.25% to 2.75%, given the anticipated composition of the Fed's voting roster. As noted above, we expect a gradual rise in rates over time and, accordingly, have created a laddered core in strategies with income as an investment objective. Bond ladders offer a degree of defense against rising rates through capturing the rolling yield while also allowing maturing issues to be deployed at the longer rungs of the ladder, benefiting from yield advantage. Although the yield curve has flattened and we expect a degree of continued flattening, we still forecast a positively sloped curve that should inure to the benefit of a laddered approach.

Through the use of bond ladders, we lessen the overall duration slightly and maintain the concentration in the intermediate segment of the yield curve. Regarding sectors, spreads for both investment grade and speculative grade corporate bonds remain near post-recession tight levels. Accordingly, Treasuries are attractive and we maintain a lower exposure to speculative grade bonds.

OTHER MARKETS

Exposures to commodities are typically helpful during conditions of rapid economic growth and/or surging inflation expectations. As these conditions are absent from our forecast, the strategies have no allocations to commodities.

First Quarter 2018	Income With Growth		Growth & Income		Growth		Aggressive Growth	
	Current	Change	Current	Change	Current	Change	Current	Change
Cash	2%	-	2%	-	2%	-	2%	-
Short Term Bonds	3%	-	5%	-	-	-	-	-
Intermediate Term Bonds	22%	5%	10%	-	-	(5%)	-	-
Long Term Bonds	15%	-	5%	-	-	-	-	-
Speculative Grade Bonds	7%	-	5%	-	-	-	-	-
Real Estate	10%	(10%)	-	-	5%	-	-	-
U.S. Large Cap Stocks	27%	5%	30%	-	40%	-	-	-
U.S. Mid Cap Stocks	-	-	15%	-	15%	-	25%	-
U.S. Small Cap Stocks	-	-	13%	-	8%	-	35%	(5%)
Foreign Developed Country Stocks	14%	-	10%	-	15%	-	13%	-
Emerging Market Stocks	-	-	5%	-	15%	5%	25%	5%
Commodities	-	-	-	-	-	-	-	-
Total	*100%*		*100%*		*100%*		*100%*	

INCOME WITH GROWTH

The one allocation change this quarter in Income with Growth is a reduction in the REIT exposure, which was split equally between intermediate-term bonds and large cap equities. Through the implementation of a laddered bond core, we reduce the overall duration by nearly 0.5 years. We increase Treasuries in the longer duration segment and introduce MBS in the intermediate segment. Among equities, all large cap for this model, we now have a 60% tilt toward growth in the U.S. exposures based on our expectations of continued momentum from last year.

The allocation to non-U.S. developed markets remains elevated due to favorable valuations relative to U.S. counterparts combined with our expectations for further U.S. dollar softness relative to other currencies.

GROWTH & INCOME

The major asset class allocations are unchanged from last quarter and continue to reflect our historically high exposure to equities for the Growth & Income strategy. Within the bond sleeve, we institute a laddered core for the majority of the intermediate segment and maintain the prior weighting to mortgages. In the longer segment there is a heavier weight to Treasuries due to the fact that spread compression among corporate bonds lessens their attractiveness. We retain a small 5% allocation to speculative grade bonds.

As noted above, the equity exposure remains elevated due to our positive outlook and now has a 60% tilt toward growth. The structure of U.S. market capitalizations is unchanged from last quarter and we continue the exposures to mid-cap and small cap stocks. We also maintain the allocation to developed market equities due to our expectations of softness in the U.S. dollar exchange rate and the attendant benefits for U.S.-based investors.

GROWTH

The U.S. large cap allocation serves as the foundation of the Growth strategy. We retain a small allocation to REITs stemming from their ability to deliver differentiated returns and consequent diversification benefits. We maintain the elevated levels of mid-cap and small cap equities due to our favorable outlook for U.S. equities. Our overall posture for U.S. equities has a tilt of 60% toward growth as we expect a continuation of multiple expansion.

Our historically high exposure to non-U.S. equities is more elevated, having sourced a slight increase in emerging market equities from a small legacy allocation to intermediate bonds. This adjustment was driven by the attractive fundamental valuations for emerging market equities combined with our thesis for a softer U.S. dollar relative to a basket of emerging market currencies.

AGGRESSIVE GROWTH

Continuing the trajectory of the past several quarters, we increase the exposure to non-U.S. equities in the Aggressive Growth strategy by decreasing the U.S. small cap allocation and redeploying it in emerging market equities. The attractive valuation metrics for emerging market stocks combined with our expectation of higher currency valuations relative to the U.S. dollar encouraged our adjustment in this strategy. The developed foreign exposure retains a tilt toward Europe, where economic growth is strengthening.

We continue to exclude U.S. large cap equities in favor of mid-caps and small caps, which comprise the majority of the allocation. Their attractive valuations, ability to deliver higher growth and our expectations of advantages stemming from the tax bill led to the overweight exposure. The U.S. equity posture now tilts 60% toward growth.

Performance & Disclosures

As of 12/31/17

Strategy	Quarter	YTD	1 - Year	3 - Year	5- Year	ITD
Income Taxable with Growth - Gross of Fees	2.2%	10.5%	10.5%	6.4%	8.0%	10.4%
Income Taxable with Growth - Net of Fees	1.5%	7.2%	7.2%	3.3%	4.8%	7.1%
Benchmark - 40% S&P 500 and 60% ML Bond Index	2.9%	10.6%	10.6%	6.0%	7.5%	8.7%
Growth and Income Taxable - Gross of Fees	4.3%	15.5%	15.5%	8.7%	10.3%	7.7%
Growth and Income Taxable - Net of Fees	3.5%	12.1%	12.1%	5.5%	7.0%	4.5%
Benchmark - 70% S&P 500 and 30% ML Bond Index	4.7%	16.1%	16.1%	8.7%	11.6%	8.9%
Growth - Gross of Fees	5.1%	16.0%	16.0%	9.3%	12.0%	7.7%
Growth - Net of Fees	4.3%	12.5%	12.5%	6.1%	8.7%	4.5%
Benchmark - S&P 500	6.6%	21.8%	21.8%	11.4%	15.8%	10.6%
Aggressive Growth - Gross of Fees	4.8%	13.9%	13.9%	9.0%	11.9%	7.7%
Aggressive Growth - Net of Fees	4.0%	10.5%	10.5%	5.7%	8.6%	4.5%
Benchmark - S&P 500	6.6%	21.8%	21.8%	11.4%	15.8%	10.6%

ITD: Inception-to-Date. Inception: Income with Growth (12/1/08), Growth & Income (9/1/08), Growth (9/1/08), Aggressive Growth (8/1/08).

Confluence Investment Management LLC is an independent registered investment adviser. Past performance is not indicative of future results. The U.S. Dollar is the currency used to express performance. Returns are presented gross and net of all fees and include the reinvestment of all income.

[1]Net of fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly. This fee includes brokerage commissions, portfolio management, consulting services and custodial services. The Confluence fee schedule for this composite is as follows: 0.40% on the first $500,000; 0.35% on the next $500,000; and 0.30% over $1,000,000. There are no incentive fees. Clients pay an all-inclusive fee based on a percentage of assets under management. The collection of fees produces a compounding effect on the total rate of return net of fees. Bundled fee accounts make up 100% of the composite for all periods. Actual investment advisory fees incurred by clients may vary. Wrap fee schedules are provided by independent wrap sponsors and are available upon request from the respective wrap sponsor.

Each strategy is implemented using Exchange Traded Funds (ETFs) and the investment objective is the pursuit of nominal returns (yield and growth) in excess of inflation, subject to the limitations of the risk constraint for each strategy. The targeted risk constraint and appropriate investor risk tolerance for each strategy is as follows; Aggressive Growth (High), Growth (Average), Growth and Income Taxable (Moderate), and Income with Growth (Conservative). ML Bond Index consist of Merrill Lynch US Corporate, Government, and Mortgage Bond Index.

Confluence claims compliance with the Global Investment Performance Standards (GIPS®). A complete list of composite descriptions and/or a GIPS compliant presentation is available by contacting Marketing@confluenceim.com or calling (314) 743-5090.

There are investment risks in investing in these strategies. Each asset class has specific risks associated with it and no specific asset class can prevent a loss of capital in market downturns. In a rising interest rate environment, the value of fixed income securities generally declines. Speculative grade bonds are subject to greater risk of loss of principal and interest, including default risk, than higher-rated securities. Investments in international and emerging market securities include exposure to risks such as currency fluctuations, foreign taxes and regulations, and the potential for illiquid markets and political instability. The real estate asset class is a portfolio containing Real Estate Investment Trust (REIT) securities.

Confluence utilizes fixed income ETFs for the bond asset classes to deliver the income and lower volatility traditionally available from a diversified bond portfolio. Fixed income ETFs are not bonds, but are pro-rata interests in publicly traded bond funds. Investors should be aware there are limitations in utilizing fixed income ETFs, which are subject to market risk, including the possible loss of principal. There may be times when an ETF's performance may vary relative to its targeted benchmark. And while ETFs generally trade very close to their net asset values, during times of market disruption they can trade at discounts or premiums, directly affecting performance. Liquidity can vary depending upon market conditions. 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.

Information provided in this report is for educational and illustrative purposes only and should not be construed as individualized investment advice or a recommendation. The investment or strategy discussed may not be suitable for all investors. Investors must make their own decisions based on their specific investment objectives and financial circumstances. Opinions expressed are current as of the date shown and are subject to change.

*Benchmark return and volatility calculations utilize monthly data through 12/31/17. Investors cannot invest directly in an index. Past performance does not guarantee future performance. Asset class and benchmark index representation: cash (ML T-Bill); short-term bonds (ML 0-3 Year C/G); intermediate bonds (ML 3-5 Year C/G); long-term bonds (ML 10+ C/G); speculative grade or high yield bonds (ML High Yield Master); real estate (FTSE NAREIT Equity); large cap (S&P 500); mid cap (S&P MidCap 400); small cap (Russell 2000); foreign developed country (MSCI EAFE); emerging markets (MSCI Emerging Market); commodities (Dow Jones UBS Commodity). Yield chart data as of December 2017. Representations: U.S. stocks are the S&P 500; foreign stocks are the average of developed country and emerging markets.

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Confluence Investment Management LLC is an independent, SEC Registered Investment Advisor located in St. Louis, Missouri. We provide professional portfolio management and advisory services to institutional and individual clients. Our investment philosophy is based upon independent, fundamental research that evaluates global markets and economies, and continues all the way down to specific companies. Our portfolio management philosophy begins by addressing risk, and follows through by positioning clients to achieve income and growth objectives.