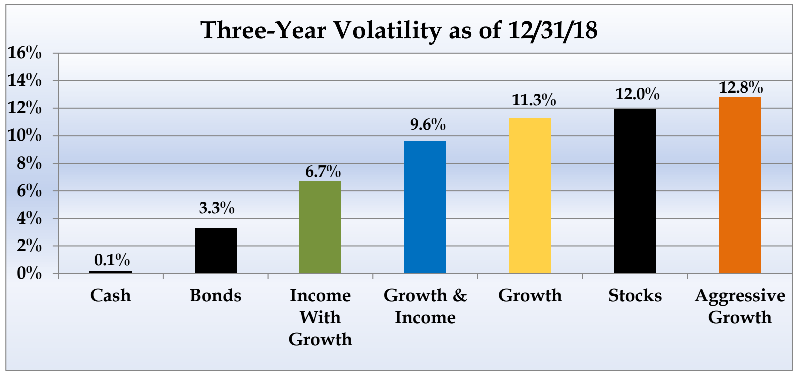
Asset Allocation Quarterly
First Quarter 2019

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 shown in black for reference in the accompanying chart.



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.*

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 consideration for the amount of risk taken to pursue these returns.

As the table below exhibits, return variance among asset classes from quarter to quarter can change dramatically. Over the past three years, we have witnessed healthy gains from U.S. equities, punctuated by sizable retreats, most notably in the past quarter. Similarly, bonds have generally enjoyed solid returns, though long-term bonds recorded a substantial loss two years ago and have also struggled recently. Foreign and emerging market equities were propelled by favorable valuations and a weaker U.S. dollar in 2017 only to be subjected to a strengthening dollar through much of the past year.

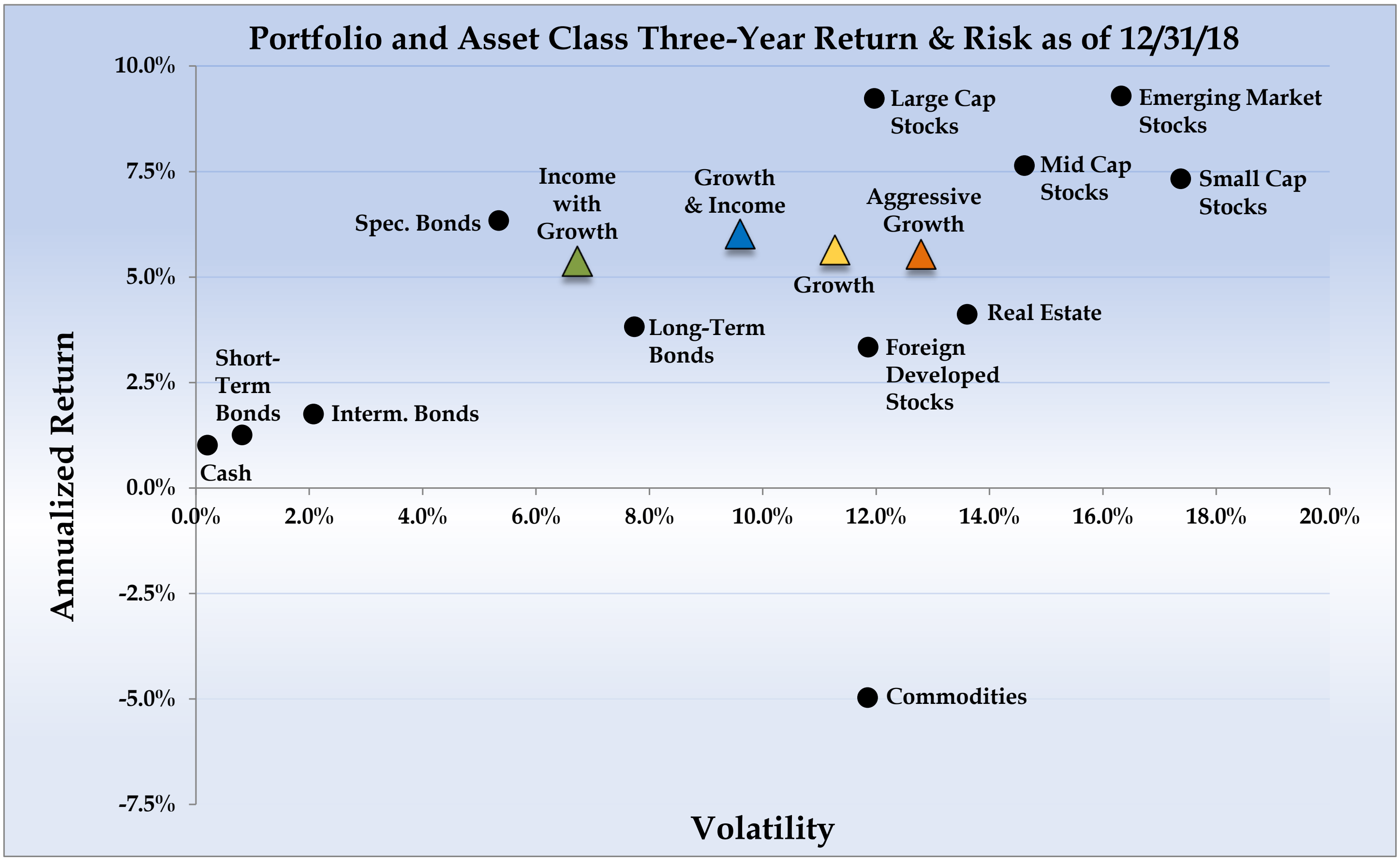
The Confluence asset allocation portfolios are structured across an array of risk profiles, where the more conservative lean against potential volatility and accept more muted, though steadier, returns, while the more aggressive accept inherent volatility in the pursuit of potentially higher returns.

Quarterly Asset Class Returns as of 12/31/18

	Q1 2016	Q2 2016	Q3 2016	Q4 2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	Q1 2018	Q2 2018	Q3 2018	Q4 2018
Cash	0.07%	0.07%	0.10%	0.09%	0.10%	0.20%	0.26%	0.28%	0.35%	0.45%	0.49%	0.56%
U.S. Short-Term Bonds	0.98%	0.66%	0.03%	-0.38%	0.39%	0.30%	0.34%	-0.18%	-0.19%	0.29%	0.35%	1.17%
U.S. Intermediate-Term Bonds	4.05%	2.72%	0.46%	-3.91%	1.26%	1.67%	0.94%	0.03%	-1.86%	-0.38%	0.21%	1.97%
U.S. Long-Term Bonds	7.33%	6.49%	0.90%	-8.37%	1.76%	4.17%	1.46%	2.66%	-3.46%	-1.23%	-0.67%	1.25%
Speculative Grade Bonds	3.25%	5.88%	5.49%	1.88%	2.71%	2.14%	2.04%	0.41%	-0.91%	1.00%	2.44%	-4.67%
REITs	6.00%	6.96%	-1.43%	-2.89%	1.16%	1.52%	0.94%	1.51%	-8.20%	10.04%	1.23%	-6.73%
U.S. Large Cap Stocks	1.35%	2.46%	3.85%	3.82%	6.07%	3.09%	4.48%	6.64%	-0.76%	3.43%	7.71%	-13.52%
U.S. Mid-Cap Stocks	3.78%	3.99%	4.14%	7.42%	3.94%	1.97%	3.22%	6.25%	-0.77%	4.29%	3.86%	-17.28%
U.S. Small Cap Stocks	-1.52%	3.79%	9.05%	8.83%	2.47%	2.46%	5.67%	3.34%	-0.08%	7.75%	3.58%	-20.20%
Non-U.S. Developed Stocks	-3.01%	-1.46%	6.43%	-0.71%	7.25%	6.12%	5.40%	4.23%	-1.53%	-1.24%	1.35%	-12.54%
Emerging Market Stocks	5.71%	0.66%	9.03%	-4.16%	11.45%	6.27%	7.89%	7.44%	1.42%	-7.96%	-1.09%	-7.47%
Commodities	-2.50%	12.67%	-4.15%	5.76%	-5.05%	-5.46%	7.22%	9.90%	2.19%	8.00%	1.34%	-22.94%

Source: Morningstar Direct, CIM.*

*This information is presented as supplemental information to the disclosures required by GIPS® standards.
See page 6 for asset class composition/benchmark details and other important disclosures.



Source: Bloomberg, CIM, using monthly data and gross returns.*

Portfolio and Asset Class Commentary

The chart above depicts the returns and risk, as measured by the volatility of returns, for 12 asset classes as well as the composite performance for our asset allocation portfolios over the three-year period ending December 31, 2018. While positive returns have been generated by 11 of the 12 primary asset classes over the course of the full 36 months, the annualized returns mask quarter-to-quarter volatilities, the most pronounced of which occurred in the most recent quarter for all equities. As a result, volatility, as measured by standard deviation, was much higher for equities than bonds.

As one would expect, the returns and risks of the Confluence portfolios, represented by the colored triangles, were predominantly influenced by their respective exposures to the major asset classes of bonds and stocks. Given the performances of the bond and stock markets over the past three years, the Confluence Income with Growth portfolio, which had the largest exposure to bonds, exhibited the lowest level of return, yet with a lesser degree of volatility. The Growth and Aggressive Growth portfolios were allocated almost exclusively to stocks over the past three years and, consequently, risk was elevated for both.

Another significant influence was the allocation of each portfolio to sub-asset classes within equities and bonds. As an example, Large Cap Stocks and Foreign Developed Stocks had a wide differential of return, yet with roughly equivalent volatility. The aggregation of the stock/bond mix and the shifting exposures to sub-asset classes within the respective mix led to the location of each portfolio along the return/risk continuum. While the four Confluence portfolios all conformed to the expectation of higher volatility with the greater assumption of risk, the returns of the Growth and Aggressive Growth portfolios fell shy of the return of the Growth & Income portfolio due to the equity market correction that occurred in the latest quarter. Although the exposure to equities proved to be a headwind over the past three months, we believe the allocations are risk-appropriate and are expected to produce returns commensurate with the higher level of risk in our forecast of continued U.S. economic growth.

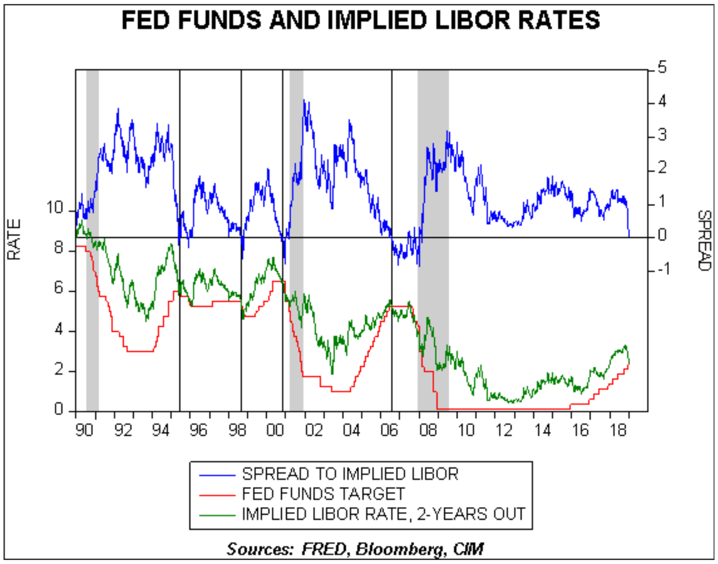
Our cyclical forecast is for a continuation of a positive economic environment, albeit with more subdued growth, which should reward risk assets. We regularly reassess and review data that can affect our macroeconomic outlook and should we find a shift in market sentiment, an increase in the potential for a policy mistake by the Fed, a higher probability for a recessionary environment, a pronounced disruption to global trade and/or magnified geopolitical risk then we will naturally adopt a more risk-averse posture for all of the portfolios.

First Quarter 2019 Asset Allocation Outlook

- **Our expectations are that the U.S. economy will continue to grow, albeit at a more modest pace of 2.7%**
- **While we anticipate the current economic expansion will become the longest on record this March, the risk of a downturn rises toward the end of our three-year forecast period**
- **We expect the Fed to suspend its recent string of rate increases and even pause its efforts to shrink its balance sheet**
- **Though unemployment remains low, the employment/population ratio indicates continued slack in the labor force, thereby blunting the full impact of wage growth on inflation**
- **We retain the high relative weightings to equities given economic health and expectations for continued GDP growth. However, our style guidance has shifted to 50/50 growth/value**
- **We eliminate exposures to equities outside the U.S. due to our expectations for a slowdown in global growth and difficulties in particular domiciles, notably continental Europe and the U.K.**

Economic Viewpoints

Despite sentiment indicators ticking down slightly over the past month, the U.S. economy continues to expand. A continuation of this expansion through March will lead it to become the longest on record. Though one often hears that the U.S. economy is in the latter innings of its growth cycle, which stretches back to June 2009, we believe the economy will grow into extra innings. The growth trajectory, however, should become more muted, with our forecast at 2.7% GDP growth for 2019.



Underpinning our forecast is not simply sentiment and growth, but our belief that the Fed will suspend its vector of raising the fed funds rate as well as its aggressive reduction of its balance sheet. Regarding the former, as the accompanying chart displays, the spread between two-year forward LIBOR and the fed funds target rate tightened dramatically over the past month. This chart illustrates the reason that recent rhetoric from members of the FOMC has been markedly dovish. Relative to the balance sheet, since October the Fed has been shrinking its holdings by $50 billion each month, or at an annual rate of $600 billion. While we think the Fed will allow the $385 billion maturing in 2019 and the $284 billion in 2020 to roll off, we don't anticipate outright sales of securities from its portfolio. In addition, we expect the Fed will reinvest prepayments on its agency mortgage-backed securities holdings back into the long end of its portfolio, principally in agency mortgage-backed securities. The potential for a hiatus on tightening by the Fed could conceivably be extended through the 2020 election season.

Worldwide, we are forecasting reduced global growth, especially in light of expected tightening by the European Central Bank and the Bank of Japan toward the back half of the year, as well as a slowing of growth rates from China and economic challenges facing Britain and continental Europe. Although we expect weakness in the U.S. dollar relative to other major currencies, which would be beneficial for U.S.-based investors, the challenges and diminished growth offset near-term advantages of exposure to non-U.S. equities.

Stock Market Outlook

While the growth in profitability for U.S. corporations will slow relative to last year's torrid pace stemming from corporate tax reform, growth will nevertheless be positive. Confluence's estimate for S&P earnings in 2019 is $160.93, representing a 4.2% increase over our estimate for the full year of 2018.[1] The most significant influence will be market sentiment as reflected in the price to earnings [P/E] ratio. The equity market correction in the fourth quarter of 2018 caused the trailing P/E on the S&P 500 to decline to 17.2x by the end of the year. Our base case, given the Fed's posture and the prospect for market sentiment to improve, is a rebound to a P/E of 18.6x. The spike in retail money market balances to over $1.15 trillion provides further buying potential for equities among retail investors, buoying our favorable outlook.

Regarding style and sectors, our former tilt to growth that existed for nearly two years has been brought back to an equal split between growth and value. This is due principally to our more muted forecast for GDP growth and complemented by the relatively extreme valuation differentials between growth and value equities. As an example, based upon year-end 2018 prices, the P/E for the S&P 500 Value Index stood at 13.5x as compared to the 22.3x for the S&P 500 Growth Index. Similarly, the price-to-book [P/B] ratio was 2.0x for value versus 4.6x for growth. While the sizable valuation differential can persist for an extended period, especially as markets advance, we find it prudent to eliminate the overweight to growth. Among sectors, we retain the prior overweights to Energy and Materials, while the former overweight to Financials is replaced by an overweight to Healthcare.

Among capitalizations, our bias is an overweight to both mid-caps and small caps due to more attractive traditional fundamental valuation measures of P/E and P/B. Moreover, the IRS's finalization of rules announced on 12/18/2018 regarding repatriation of foreign earnings of foreign subsidiaries of U.S. companies should prove beneficial for prices of companies classified as mid-cap and small cap as well as in the lower strata of large cap, by virtue of increased M&A activity. Accordingly, all of our asset allocation portfolios have historically high levels of equity exposure and in the portfolios where it is risk appropriate we include express overweights to mid-cap and small cap equities.

In contrast to our sanguine view of U.S. equities, we find that the risks outweigh the potential for non-U.S. equities. Though comparative valuations are attractive, the expectations for a slowdown in global growth combined with complications stemming from the EU and Britain lead us to a cautious near-term stance. Brexit, Italy's budget plans, a new head of the ECB, a new German Chancellor and elections in the European Parliament conspire to make us cautious on overseas exposure. While a weaker U.S. dollar would be a tailwind for U.S.-based investors, we are more comfortable avoiding non-U.S. equities for at least the first portion of the year.

[1] The earnings estimates are based on Standard & Poor's methodology for determining S&P earnings, which differs from Thompson/Reuters I/B/E/S by 7%.

Bond Market Outlook

Our premise for the Fed's suspension of tightening for a period of time, perhaps stretching through the 2020 election cycle, naturally leads to the expectation that short rates will be anchored. What is murky is the continuation of the global appetite for yield, the initiation and pace of tightening by the ECB and BOJ and their potential effects on U.S. rates, and the domestic inflation outlook, especially with a more dovish Fed. Adding to this murkiness is the effect upon corporate spreads of $3 trillion of corporate debt maturing before 2022, coupled with the change in interest expense deductibility in 2022 from 30% of EBITDA to 30% EBIT. Given the uncertainties for the intermediate and long segments of the Treasury and corporate curves, we retain the laddered bond positioning we introduced a year ago. In addition, exposure to speculative grade bonds remains at historically low levels in the portfolios despite the sizable widening of spreads over the last quarter. Although speculative bonds are more attractively valued than they were three months ago, we are cautious about embedded risk.

Other Markets

We maintain the allocation to REITs in the more income-oriented portfolio due to attractive and improving dividend yields and the diversified income stream they afford. Relative to speculative bonds, we find the potential risk/reward to be superior in REITs.

We also retain the modest allocation to gold owing to the combination of its ability to offer a hedge against geopolitical risk and the safe haven it can afford during an uncertain climate for the U.S. dollar.

First Quarter 2019	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	24%	(8%)	5%	(5%)	-	-	-	-
Long Term Bonds	11%	-	5%	-	-	-	-	-
Speculative Grade Bonds	4%	-	-	-	-	-	-	-
Real Estate	10%	-	-	-	-	-	-	-
U.S. Large Cap Stocks	33%	7%	35%	5%	45%	5%	20%	20%
U.S. Mid Cap Stocks	10%	10%	30%	15%	25%	15%	38%	15%
U.S. Small Cap Stocks	-	-	15%	(5%)	23%	-	35%	-
Foreign Developed Country Stocks	-	(9%)	-	(10%)	-	(10%)	-	(10%)
Emerging Market Stocks	-	-	-	-	-	(10%)	-	(25%)
Commodities	3%	-	3%	-	5%	-	5%	-
Total	*100%*		*100%*		*100%*		*100%*	

See page 6 for disclosures and important details regarding portfolio allocations.

Income with Growth

We reduce the substantial overweight to intermediate-term bonds by 8% to 24% in favor of an increased weight to U.S. large cap equities and the introduction of a U.S. mid-cap equity position. The laddered maturity structure still occupies the majority of the bond exposure. Large caps now represent 33% of the portfolio and mid-caps are 10%. Our positive view on equities, especially with the Fed pausing its tightening efforts and valuations being much more compelling following last quarter's correction, leads to a historically high exposure to equities for the Income with Growth portfolio. However, this substantial equity allocation does not include non-U.S. equities, stemming from caution surrounding a number of issues being confronted in Europe in 2019. We maintain the modest 3% weighting to gold due to its potential to reduce overall portfolio risk accruing from geopolitical uncertainty and its attractiveness in the event of a decline in the value of the U.S. dollar.

Growth & Income

We eliminate the prior 10% positioning in non-U.S. equities as a result of our cautionary stance in Europe for the myriad issues they face in 2019. This position has been reallocated to U.S. large cap and mid-cap equities, which account for 35% and 30%, respectively, of the exposure in the Growth & Income portfolio. Additionally, a portion of the U.S. small cap equity exposure has been reallocated to U.S. mid-caps due to more attractive valuations and lower expected volatility for mid-caps. Within the bond sleeve of the portfolio, an overweight to the intermediate bond segment is brought to even-weight, while retaining the laddered maturity structure . We maintain a small weighting to gold as a hedge against geopolitical risk and the opportunity it affords against a potentially weaker U.S. dollar.

Growth

Exposure to non-U.S. equities is eliminated from the Growth portfolio this quarter, owing to the laundry list of concerns emanating from Europe. The 20% weight previously positioned outside of the U.S. has been reallocated to U.S. large cap and mid-cap equities. Within the large cap allocation, we replaced the overweight to the Financials sector with Healthcare as a result of a more favorable growth outlook for this sector, while maintaining overweights to the Energy and Materials sectors due to attractive valuations. We retain the 5% allocation to gold, which we believe has the potential to offer a hedge against geopolitical risk and holds attraction should the U.S. dollar experience weakness.

Aggressive Growth

Consistent with the other portfolios, we have removed all exposures to non-U.S. equities in the Aggressive Growth portfolio. The former exposure has been reallocated to U.S. large cap equities, which is a new position, and U.S. mid-cap equities. Concerns regarding a number of issues facing Europe over the next several quarters encouraged the elimination of non-U.S. positions given our anticipation of elevated risk. The introduction of a 20% exposure to large cap equities provides the ability to overweight certain sectors. Energy and Materials are overweight based upon attractive valuations and Healthcare is overweight due to growth prospects. We retain the 5% allocation to gold due to the hedge it provides against geopolitical risk and its return potential in the event of a decline in the value of the U.S. dollar.

Performance & Disclosures
as of 12/31/18

Strategy	Quarter	YTD	1 - Year	3 - Year	5 - Year	10 - Year	ITD
Income Taxable with Growth - Gross of Fees	-4.6%	-3.8%	-3.8%	5.4%	5.6%	8.5%	8.9%
Income Taxable with Growth - Net of Fees	-5.3%	-6.6%	-6.6%	2.2%	2.5%	5.3%	5.6%
Benchmark - 40% S&P 500 and 60% ML Bond Index	-4.5%	-1.5%	-1.5%	5.1%	5.1%	7.5%	7.7%
Growth and Income Taxable - Gross of Fees	-11.6%	-8.1%	-8.1%	6.0%	6.1%	9.3%	6.1%
Growth and Income Taxable - Net of Fees	-12.3%	-10.8%	-10.8%	2.9%	2.9%	6.0%	2.9%
Benchmark - 70% S&P 500 and 30% ML Bond Index	-9.1%	-2.8%	-2.8%	7.2%	6.8%	10.4%	7.7%
Growth - Gross of Fees	-13.2%	-10.1%	-10.1%	5.7%	6.1%	9.9%	5.8%
Growth - Net of Fees	-13.8%	-12.7%	-12.7%	2.5%	3.0%	6.6%	2.7%
Benchmark - S&P 500	-13.5%	-4.4%	-4.4%	9.2%	8.5%	13.1%	9.0%
Aggressive Growth - Gross of Fees	-13.5%	-11.1%	-11.1%	5.5%	4.7%	9.7%	5.7%
Aggressive Growth - Net of Fees	-14.2%	-13.7%	-13.7%	2.4%	1.6%	6.5%	2.6%
Benchmark - S&P 500	-13.5%	-4.4%	-4.4%	9.2%	8.5%	13.1%	9.1%

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 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. 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.

The asset allocations shown represent the individual ETFs used for the asset allocations in the model portfolios as of 1/15/2019 and do not represent the precise allocation of assets in an actual client account. Asset allocation in client accounts may vary based on individual client considerations and market fluctuations. The allocation of assets in the model portfolio may be changed from time to time due to market conditions and economic factors. The investments held by the portfolio are ETFs and are not guaranteed and do carry a risk of loss of principal. 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 but charge internal management fees; 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 thru 12/31/18. 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 (S&P GSCI Total Return).

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