INVESTMENT STRATEGY UPDATE - JULY 2018

High valuations imply low returns over an extended time period and/or large declines.

Allocation: Our overall allocation strategy is defensive because of high valuations of both stocks and bonds. High valuations imply low returns over an extended time period and/or large declines. Thus, we are generally maintaining an under-weighting of stocks. We have lowered bond allocations or reduced duration (interest rate risk) by an equivalent amount because of the risk of losses from rising interest rates and the Federal Reserve's policies. Finally, higher cash yields make cash a more viable alternative to bonds, if rates rise.

Stock Market Gauge: Our stock market gauge is composed of 5 measures: valuation, financial conditions, trend, earnings, and sentiment. High valuation and optimistic sentiment have been negative factors for some time. Earnings have been quite strong, which is a positive. While our model began April close to a sell level, improved trend and financial condition measures pushed the gauge back to a neutral rating of 3.0. Our research indicates that a sell signal (below 2.4) should be confirmed by a couple of weeks at this level.

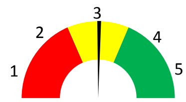
Value Stocks: The reflation narrative, a focus on the acceleration of growth as well as an increase in interest rates, should benefit value stocks that are concentrated in financials, energy, and more economically sensitive companies. Financials and energy companies should benefit the most from the new tax act, since they have high corporate tax rates. Financials also benefit from higher interest rates and stock market values. Finally, our analysis of past periods suggests that value stocks can out-perform growth stocks because of the extreme valuation difference.

Quality Stocks: Quality stocks represent ballast in the stock portfolio. They probably will not out-perform unless stocks correct. With increased volatility, a likely peak in the rate of earnings growth, and increased global uncertainty, the chances of a correction have increased. Furthermore, consumer staples, which represent a significant portion of quality stocks, have declined this year, making them more attractive investments.

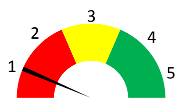
International Stocks: International stocks have under-performed U.S. stocks for an extended period, resulting in a large valuation gap, as we have illustrated in the past. The U.S. stock market recovered earlier than foreign markets because the U.S. undertook stimulus efforts before the rest of the developed world. Also, more successful economic policies tended to support a higher Dollar. Prospectively, higher relative growth overseas should support foreign stocks and currencies. The Dollar appreciation this year makes foreign stocks more attractive, presently.

Bonds: Strong growth, no recession in sight, and above expectation inflation imply a hostile environment for bonds. The 1st quarter represented a significant change in bond market sentiment. During the second quarter, the benchmark 10 year treasury rose above 3.0%, breaking perceived resistance to higher rates. Although rates have retreated from these higher levels, inflationary trends are entrenched. Therefore, we expect the trend of higher rates to continue. We are targeting a duration of 5 years, more defensive than taxable benchmarks.

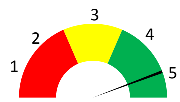
STOCK MARKET DASHBOARD



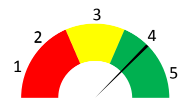
Overall Market Gauge
3.0



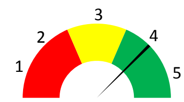
Valuation



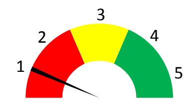
Earnings



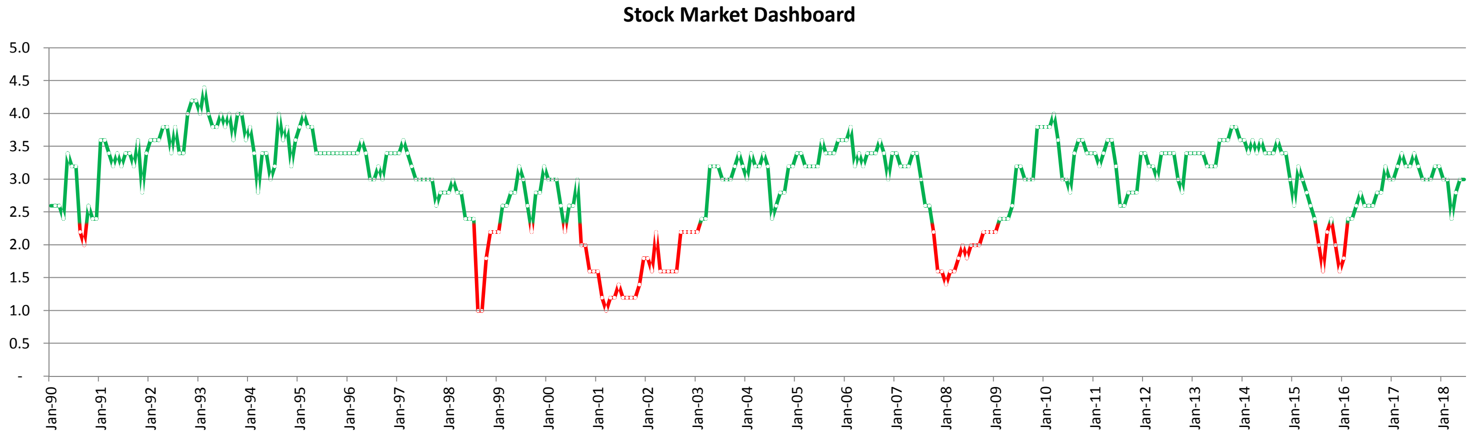
Momentum



Liquidity



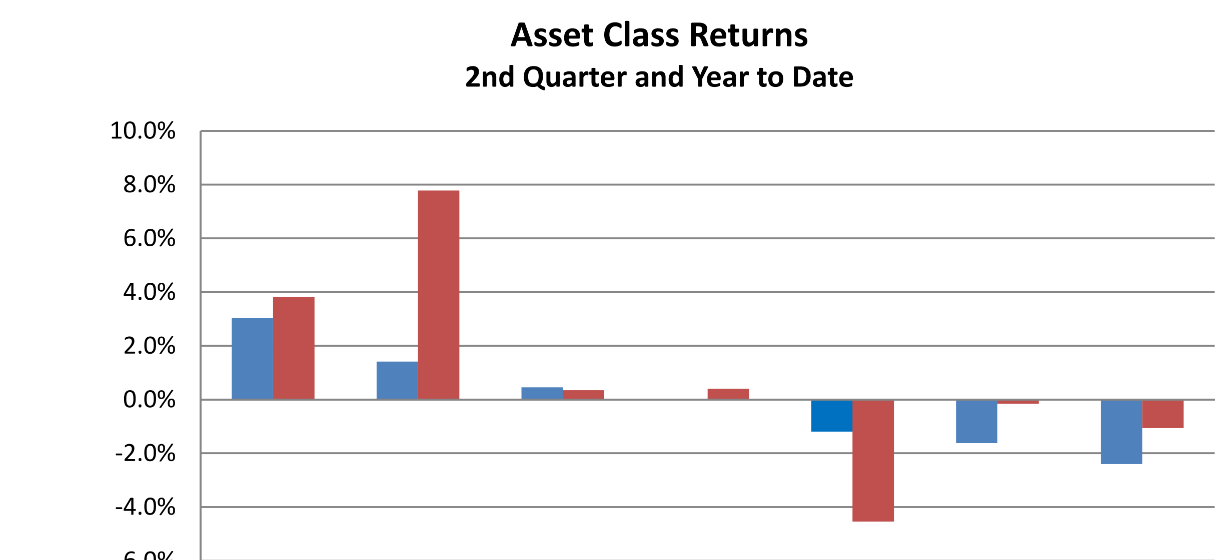
Sentiment



CAPITAL MARKET REVIEW

Asset Class Performance

In the second quarter, stocks bounced back from their first quarter losses. The strength in the U.S. Dollar dragged down international stocks and bonds with foreign currency losses. Bonds faced a headwind from rising rates, and cash yields approached 2%. Rising steel and energy prices pushed commodities slightly higher.

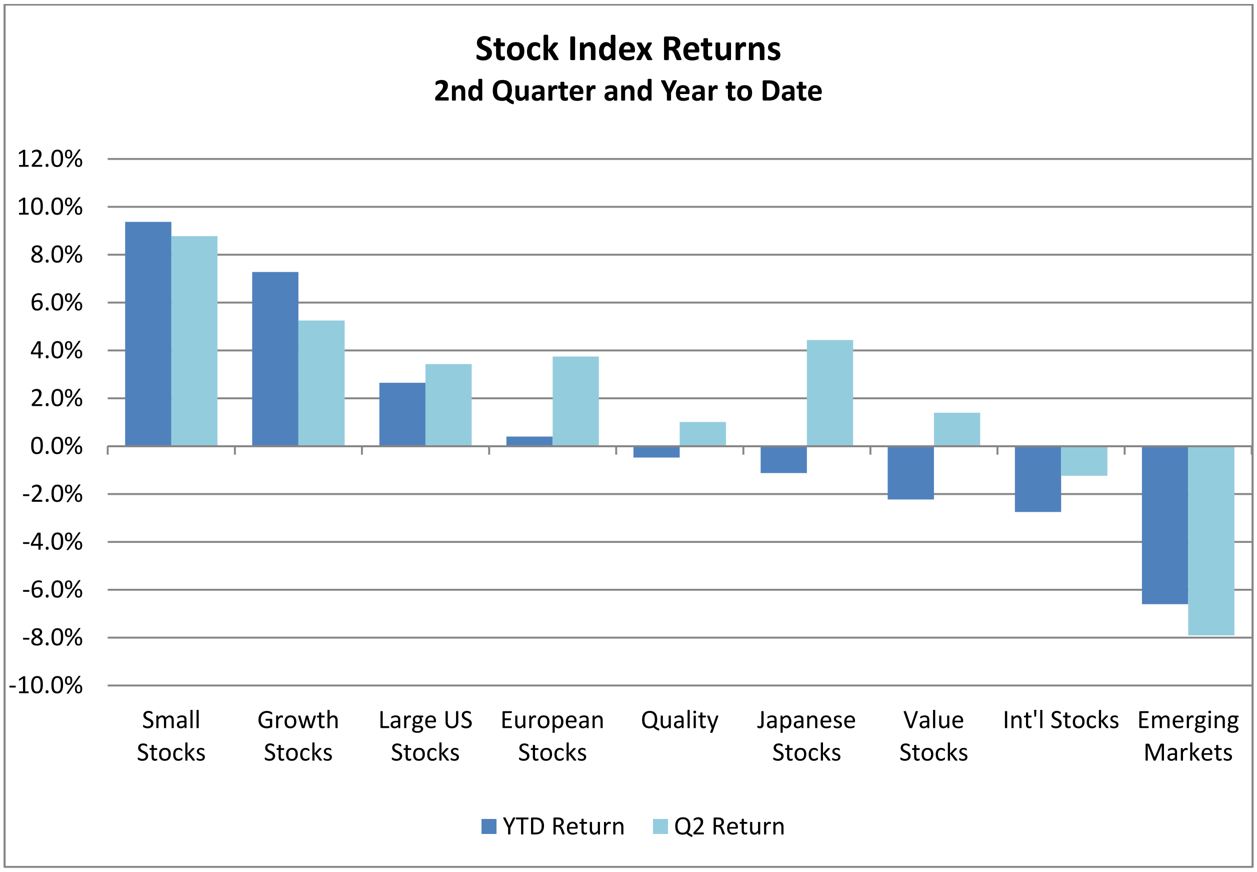


	US Stocks	Real Estate	Cash	Commodities	Int'l Bonds	US Bonds	Int'l Stocks
YTD Return	3.0%	1.4%	0.5%	0.0%	-1.2%	-1.6%	-2.4%
Q2 Return	3.8%	7.8%	0.4%	0.4%	-4.5%	-0.2%	-1.1%

CAPITAL MARKET REVIEW
(continued)

Stock Market Performance

U.S. stocks rallied in the second quarter, led by small company stocks and growth stocks. International stock returns were hurt by the rising Dollar, which offset local currency returns. Investors bid up the prices of small company stocks because these companies tend to be more domestically focused, whereas for multinational companies their overseas sales are worth less when the sales are reported in Dollars. Threats of a trade war and currency losses had a devastating effect on emerging market stocks. For example, China's stock index declined by 20% from the high into bear market territory.



CAPITAL MARKET REVIEW
(continued)

Bond Market Performance

Concern that a trade war could reduce growth (and the pressures on rates) allowed for rallies in some segments of the bond market, although the factors that pushed interest rates up in the first quarter, namely strong growth expectations, rising inflation worries, and increasing bond supply in relation to demand, remained in place. Treasury rates rose across all maturities, especially in shorter maturities. Corporate investment grade bonds fared poorly, declining more than treasury bonds. Municipal bonds benefited from continuing demand from investors and modest supply from issuers; rates declined across maturities, albeit by small amounts.