CROSSMARK GLOBAL INVESTMENTS

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COVERED CALL INCOME COMMENTARY

Second Quarter Review 2018

Volatility, which returned to the markets with a vengeance in the first quarter, persisted through much of April. Global headlines continued to play a major role within the markets. The potential for a trade war with China and escalating tensions between the U.S. and Russia were two of the main culprits worth watching. Earnings season for Q1 started and so far exceeded investor expectations. Many investors still remain somewhat cautious that the current pace of growth will at some point give way to accelerated inflation which in turn could lead to tighter monetary policy from the Fed. The Fed is still expected to announce two more rate increases prior to the end of 2018. All of these potential events play a part in the resurgence in volatility. The Covered Call Income team took advantage of the swings in volatility by strategically placing trades to enhance income as well as resetting the delta of the portfolio. April proved to be another important month in regards to selling covered calls.

Volatility continued to plague the markets in May due in large part to heightened political risk. Global trade issues and the off again on again summit with North Korea still caused uncertainties within the global markets. Italy's new populist government added to more market concerns towards the end of the month. Despite the significant intra-month swings, the ongoing strength of global growth was evident in corporate earnings. The positive effects of tax cuts contributed to a strong Q1 earnings season in the US and fears about a more aggressive pace of Fed tightening eased over the month May. The Fed is still expected to increase interest rates by a quarter of a percentage point at its June meeting, however the recent rhetoric has been more along the dovish side of expectations, a considerable change from prior communications.

The month of June continued to see the markets engulfed in trade policy rhetoric. One day the U.S. and China are headed for an all out trade war to the next day the Trump administration pulls back and decides against harsh measures against China. Tariffs and ongoing trade disputes will likely add to increased volatility within the markets. The consensus with investors is a potential trade war, which will have a negative effect on both U.S. and China that results in weaker economic growth, lack of consumer confidence and higher inflation. There seems to be quite a bit of posturing on both sides which is part of trade negotiations. Canada and Mexico have also entered the trade battle in recent weeks imposing tariffs of their own. The Federal Reserve didn't seem too concerned about the trade wars as rates were raised again as expected with the Fed

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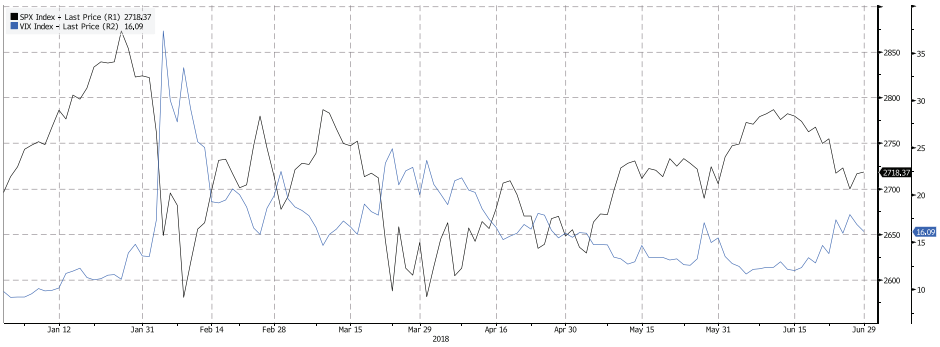
expressing few concerns that the disputes would impact U.S. growth in a meaningful way. The FOMC also upped its forecast for rate hikes this year from three to four.

VIX vs S&P 500



Source: Bloomberg

The Covered Call Income strategy slightly lagged the primary benchmark of the S&P Covered Call Index in April and May. The S&P made a decision at the end of May to discontinue support for the primary benchmark of the S&P Covered Call Index. The Crossmark Investment Committee made a decision to revert back to the BXM as the primary benchmark for the Covered Call Income strategy starting in June. The BXM was the original benchmark for the strategy since inception in August of 2005. June proved to be a rough month for active management strategies and the covered call income strategy lagged the BXM for the month and the quarter. However, the covered call income team took advantage of the swings in volatility by strategically placing trades to enhance income as well as resetting the delta of the portfolio. From an attribution standpoint, the strategy was affected in the following ways in regards to the S&P 500 sector breakdown:

Positive Attribution:	Negative Attribution:
Energy	Consumer Staples
Consumer Discretionary	Financials
Technology	Industrials

Looking ahead to Q3

As long as there are ongoing political issues surrounding the markets, volatility is not going anywhere. Volatility is healthy for the markets and advantageous to covered call strategies.

As it stands right now, the summer months ahead look to be fairly volatile if the last couple of months are any indication. Trade policy will be the talk of the markets as the rhetoric on both sides' ramps up. Earnings season kicks off in the middle of July and looks to be an important one with everything surrounding the markets currently. The markets have continued to push forward and the U.S. economy, for now, remains healthy. Stay tuned.

The Covered Call Income team took advantage of the swings in volatility by strategically placing trades to enhance income as well as resetting the delta of the portfolio.

Covered Call Income Commentary

Top 10 Model Holdings [1]	Weight
1. Microsoft Corp.	4.25%
2. Visa, Inc.	3.81%
3. PayPal Holdings, Inc.	3.59%
4. Abbott Labs	3.51%
5. Nike, Inc.	3.44%
6. Activision Blizzard, Inc.	3.29%
7. Valero Energy Corp.	3.19%
8. Pfizer, Inc.	3.13%
9. Gilead Sciences, Inc.	3.06%
10. Emerson Elec. Co.	2.98%
Total of Portfolio	34.25%

[1] Model Portfolios are based on a hypothetical account managed during the current quarter. Actual characteristics and income may differ materially from model. As of 6/30/2018.

Definitions:
"Up and Out" – This occurs when the original call option is repurchased and another call option is sold. The new option is sold with a higher strike price and a later expiration date than the original option.

"Rolling Down" – This involves buying back the current call option and selling another call option with the same expiration date. The only difference between the two call options is the strike price. In this case, the new option has a lower strike price.

"At-the-Money" – Options with a strike price, or exercise price, equal to the price of the underlying asset. Theoretically, these options have a delta around 50%.

"In-the-Money" – Options with a strike price, or exercise price, lower than the price of the underlying asset. These options have a theoretical delta greater than 50%.

"Out-of-the-Money" – Options with a strike price, or exercise price, greater than the price of the underlying asset. These options have a theoretical delta less than 50%.

"Delta" – One of the "Greeks" derived from the Black-Scholes model for option pricing. Theoretically, it states how much the price of the option will change given a $1 change in the price of the underlying asset. It is also commonly referred to as the "hedge ratio."

Covered Call Income strategy is designed for investors who want equity market participation with enhanced income potential. This approach is appropriate for investors looking for higher yields, capital appreciation and reduced risk levels.

Writing calls on securities held in the portfolio maximizes the gains that can be realized if the price of a stock increases, and investing in equity securities involves market risk, including the possible loss of principal.

About Crossmark's 30 Year History
Crossmark Global Investments is an innovative investment management firm. The firm provides a full suite of investment management solutions to institutional investors, financial advisors and the clients they serve. We have a multi-decade legacy of specializing in responsible investment strategies for clients. Founded in 1987, the firm is headquartered in Houston, Texas.

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