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GLOBAL INVESTMENTS

ECONOMIC AND STRATEGY COMMENTARIES

2Q 2017 Commentaries

- Economic Commentary
- Taxable Fixed Income Commentary
- Municipal Fixed Income Commentary
- Global Equity Income Commentary
- Theta Growth Commentary
- Large Cap Core Growth Commentary

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JUNE 30, 2017

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STEWARD FUNDS

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June 30, 2017

ECONOMIC COMMENTARY

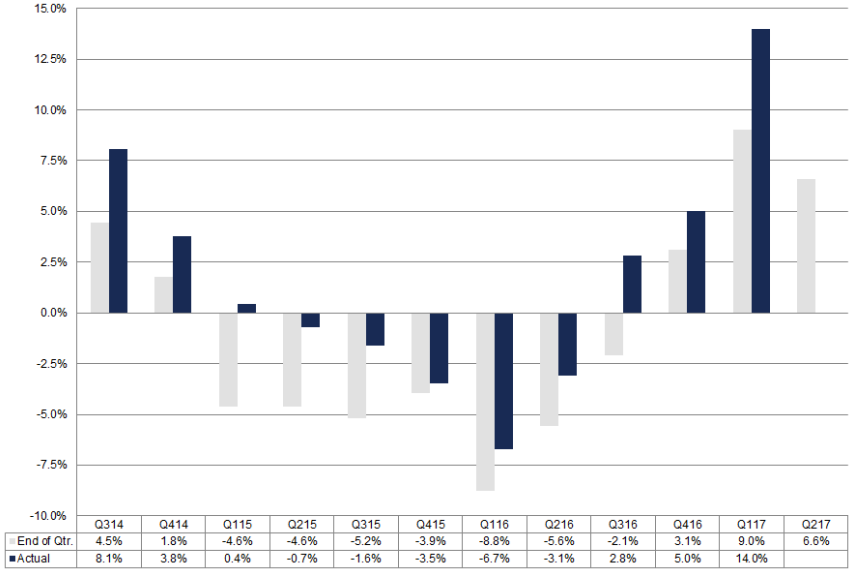
The rally in equities that began after the November 2016 election continued its upward charge in the second quarter with the S&P 500 gaining another 3.09%. For the year-to-date, the index was up a solid 9.34%. Investors are expecting stronger growth going forward from the administration's pro-growth agenda, but the time frame has been stretched from 2017 to 2018. A lot of questions remain as to just how much of the plan will be able to make it through the House and Senate gauntlets. Health care and tax reform seem to be having the most difficulty at this point. At the least, a significant reduction in regulations that impact corporate earnings should continue. This alone could be a significant driver of profits and perhaps stock prices as well.

Recent economic statistics presented investors with a mixed picture. We have had strong results from "soft" indicators such as consumer confidence, but weaker results from "hard" indicators such as gross domestic product. Automobile sales also slipped recently. One piece of hard data, the recently released ISM Manufacturing Index, posted a quite strong result with a reading of 57.8 for June. This was well above the consensus of 55.3 (readings above 50 indicate economic expansion). Especially of note, the manufacturing improvement was broad based. Fifteen of eighteen industries reported growth, and major measures of activity stayed above the key 50 level while new orders and production posted the largest gains for June. The new orders index this year has averaged the highest start to a year since 2004. The June ISM for non-manufacturing companies was just released and posted a solid 57.4, up 0.5 from May and ahead of the expectations of 57.1. This provides another good data point to confirm the economy is improving. Employment statistics continue to look strong. The June unemployment rate came in at 4.4%, up 0.1% from May. May was a 16-year low and essentially indicated full employment. The labor market appears to be tight and the JOLTS job openings report just hit 6.04 million, the highest level since the JOLTS report has been published. Such a high level indicates employers are having trouble finding qualified applicants which has been an issue for some time. As for the Federal Reserve, it raised its target range for the federal funds rate to 1.00%-1.25% and currently expects inflation to hit its target of 2% in 2018 and 2019.

- Investors are still looking for stronger growth going forward from the administration's pro-growth agenda, but the time frame has been stretched from 2017 to 2018.
- The ISM report indicated fifteen of eighteen industries reported growth, and major measures of activity stayed above the key 50 level while new orders and production posted the largest gains for June.
- The labor market appears to be tight and the JOLTS job openings report just hit 6.04 million, the highest level since the JOLTS report has been published.
- Revenue growth is projected to increase and already reported revenues for Q2 bolster that conviction.

Economic Commentary

S&P 500: Estimated Earnings Growth at End of Qtr. vs Actual Growth



	Q314	Q414	Q115	Q215	Q315	Q415	Q116	Q216	Q316	Q416	Q117	Q217
End of Qtr.	4.5%	1.8%	-4.6%	-4.6%	-5.2%	-3.9%	-8.8%	-5.6%	-2.1%	3.1%	9.0%	6.6%
Actual	8.1%	3.8%	0.4%	-0.7%	-1.6%	-3.5%	-6.7%	-3.1%	2.8%	5.0%	14.0%	

Source: FactSet

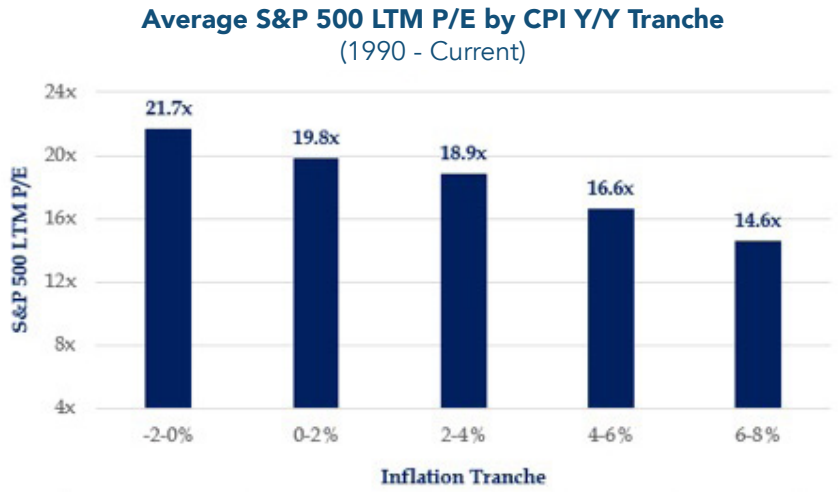
The corporate profits outlook for the second quarter now looks promising based on early reporting companies. The current estimate for second quarter earnings per share growth is an increase of 6.6%. As the chart above illustrates, these early estimates are often on the low side, so we could be in for something closer to double digit EPS growth.

Of course, the direction of equity prices is quite correlated with the direction of earnings. Revenue growth is also projected to increase, and already reported revenues for Q2 bolster that conviction. Nick Raich of "Earnings Scout" publication notes early reporters have posted revenue growth of 8.5%, so earnings are no longer just a cost-cutting story but also a growth story. Raich is quite encouraged by what he has seen thus far in Q2, and we share that sentiment. Second quarter earnings may, in fact, set a quarterly record in Q2 and Q3. So it looks as if we are transitioning from a Federal Reserve-driven market to an earnings-driven market at just the right time.

For the quarter, the stock market moved upwards through early June and then settled into a trading range between about 2400-2450 to close out the quarter. We remain constructive on equities for 2017, but the market has gone a long way without a significant pullback so we would not be surprised to see the market sell off between 5%-10% at some point in the next few months. That said, the indexes seem to be in a very positive position currently. The key indexes are "in gear," meaning they are moving up together and even hitting new highs, a very bullish sign. The S&P 500, Dow Industrials, NASDAQ, and the Advance/Line all hit new highs in June, and even the Dow Transports went on to hit a new high in early July. This is considered a very bullish occurrence by

Second quarter earnings may, in fact, set a quarterly record in Q2 and Q3, which looks as if we are transitioning from a Federal Reserve-driven market to an earnings-driven market just at the right time.

Economic Commentary



Source: Strategas

followers of "Dow Theory." The theory postulates that when the Industrials and Transports both make new highs, this indicates that both sectors of the economy are growing and that should be positive for stocks. If we do get a pullback, we would view it as a "healthy" development as it would allow earnings to catch up to stocks prices and improve the valuation numbers. As it stands, the S&P 500 is currently trading at a PE of around 18.5x, so it is a bit stretched by historical standards. However, we are in a period of unusually low interest rates and inflation which we refer to as a valuation "sweet spot". The chart above indicates markets can reach significantly higher levels during these periods, so we have a bit of a cushion as long as inflation remains tepid.

Additionally, the yield curve is still sending an encouraging message with a positive slope and spreads that have widened a bit recently, as well. If Washington can get its act together and pass some growth-inducing legislation such as tax reform (including repatriation of overseas profits), we could begin a new leg up on this bull market.

About Crossmark's 30 Year History
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CROSSMARK GLOBAL INVESTMENTS

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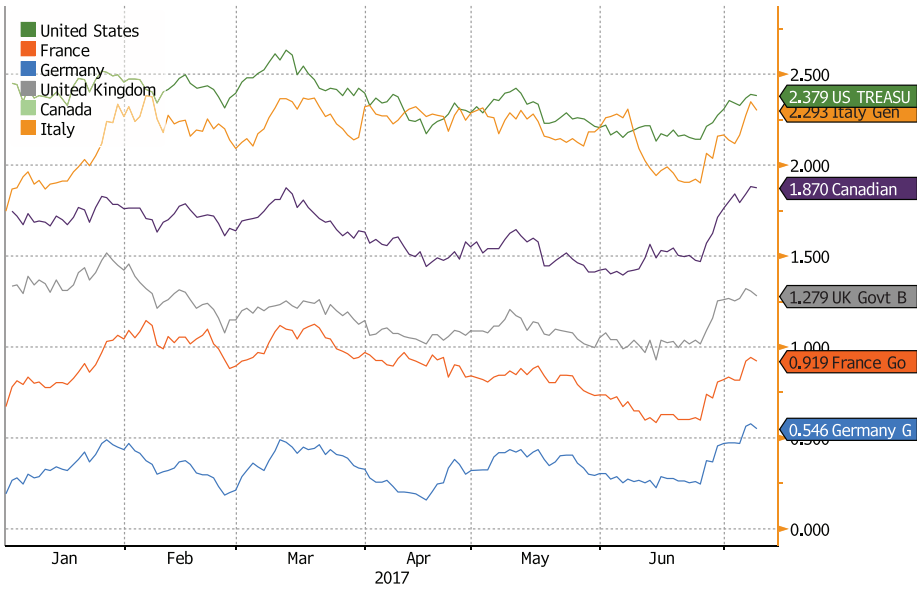
June 30, 2017

TAXABLE FIXED INCOME COMMENTARY

FIXED INCOME
INTERMEDIATE FIXED INCOME
CURRENT INCOME PORTFOLIO
INCOME OPPORTUNITY

It's summertime – which means we have maneuvered through the first half of the year with fixed income markets rallying for the majority of that time and spreads remaining contained. We began the year with the US 10yr treasury note yielding around 2.44% and hit a year-to-date low of 2.13% during the month of June before a brief bounce back to end the 2nd quarter at a 2.30%. The recent rebound was sparked by Mario Draghi's comment that perhaps it is time for the European Central Bank to look at removing some of their easing policies; a move that would more closely align the ECB with the recent actions by the Federal Reserve. The move to higher yields was seen not only in the U.S. but across Europe during the final month of the quarter, bringing yields back towards levels last seen at the beginning of the year.

Global 10yr Yields 2017



Source: Bloomberg

- The move to higher yields was seen not only in the U.S. but across Europe during the final month of the quarter, bringing yields back towards levels last seen at the beginning of the year.
- Markets have been driven more by macro factors than company specifics this year.
- For the month of June, all of our taxable fixed income product models outperformed their index as we began to see rates move higher and our income and allocation decisions providing positive contributions to return.

Taxable Fixed Income Commentary

Looking at the 2nd half of the year, there appears to be plenty of fodder to increase volatility in the markets including geopolitical issues with North Korea, domestic policy issues regarding healthcare, tax reform and infrastructure stimulus, along with continual guesses by the market on how the Federal Reserve will wind down its balance sheet and the path of future rate hikes. With these uncertainties looming, and the fact that markets have been driven more by macro factors than company specifics this year, Capstone continues to favor a more conservative, risk-averse fixed income portfolio. Our taxable products are structured with a shorter duration than the comparable indices to help reduce interest-rate risk, high-quality investments to counter credit risk, and large global issues to diminish liquidity risk. With an overweight to the investment-grade corporate allocation, we are able to focus on increased levels of income generation to buffer market value volatility and help support total return for the portfolios.

"Looking at the 2nd half of the year, there appears to be plenty of fodder to increase volatility in the markets including geopolitical issues with North Korea, domestic policy issues regarding healthcare, tax reform and infrastructure stimulus, along with continual guesses by the market on how the Federal Reserve will wind down its balance sheet and the path of future rate hikes."

For the month of June, all of our taxable fixed income product models outperformed their index as we began to see rates move higher and our income and allocation decisions providing positive contributions to return. For the Current Income Portfolio and the Income Opportunity Portfolio, exposure to different sectors including fixed-rate preferreds, high-yield corporates and REITs was an additional benefit with both portfolios outperforming for not only the month of June, but for the 2nd quarter and year-to-date. With additional volatility on the horizon, we will continue to utilize our four-step strategy focusing on duration, yield curve, sectors and security selection to help determine the most appropriate allocations within the fixed income products to meet the needs of our clients.

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June 30, 2017

MUNICIPAL FIXED INCOME COMMENTARY

Last month, Crossmark highlighted the bond trading desks and the media pushing a shortage of municipal bonds narrative with headlines similar to "Record-breaking Redemption Season Means Historic Cash Flurry." The information from the sources was accurate as to the total number of municipal bonds to be called and matured between June and September, but the current new issues that came to the market during June was greater than anticipated. Historically, June through August is weak for new issues coming to the market and the prices usually move higher for those investors focusing on total return only. In part, municipality and state fiscal years fall in June or July, so it is normal that new issuance will find a slower pace until fresh fiscal budgets are approved. It then takes a short period of time to implement the budgets. This narrative of a redemption bonanza is also based on the 10 year call protection used for most longer term bonds, and 2007 bond issuance in the market was the largest amount prior to the recession cutting into new issuance. In 2016, the 10 year Treasury hit a historical low of 1.42 percent the first week of July before municipalities and states began to take advantage of the low rates by bringing more issues to the market, until the 2016 election results pushed rates much higher. With yields moving lower in June, municipalities and states stepped up the pace of new issuance to begin addressing infrastructure needs across the country. While the argument stands that redemptions will be extra-large when compared to previous years, new issuance could outpace previous years as municipalities are servicing fewer bonds at much lower rate levels, so the capability to address projects is greater. As previously mentioned, patience and selectivity will be key during the summer months.

State and municipality austerity measures will continue into fiscal 2018 as revenue growth is anemic but infrastructure need is growing. Through April 2017, of 35 states reviewed, the average growth of revenue is 1.80 percent, much lower than projected. At some point, maybe in the remaining months of 2017, job growth, low unemployment and the need to hire more quality workers might fuel wage hikes and improve revenue streams for state coffers. If this proves to be the case, then budget expansion to begin addressing infrastructure could dominate FY19 budgets. Fifteen

- With yields moving lower in June, municipalities and states stepped up the pace of new issuance to begin addressing the infrastructure needs across the country.
- State and municipality austerity measures will continue into fiscal 2018 as revenue growth is anemic but infrastructure need is growing.
- Fifteen states are struggling to finish up next year's budgets as the slow growth in revenues are forcing the municipalities to determine what is needed instead of what is nice-to-have for communities.
- Volatility will continue as unknown structures for tax reform, new issuance projections and bond redemptions are discussed ahead of reality.

states are struggling to finish up next year's budgets as the slow growth in revenues are forcing the municipalities to determine what is needed instead of what is nice-to-have for communities.

Streets, highways and toll roads have been in the news for years highlighting the need for infrastructure repair, shovel ready jobs, poor road conditions and the general feeling that states and cities are not doing enough, or working fast enough, to keep up with transportation needs. Toll roads have a cycle of revenue growth and usually account for faster repair efforts as the possibility to increase toll costs takes less time and effort than budgeting for a county road. Toll road bonds take a beating when the economy is in recession as fewer drivers pay the tolls. For a positive information cycle for toll roads, one needs to look no further than AAA study of travel growth over the past two years. The study showed that over 39.1 million people traveled more than 50 miles from their homes over Memorial Day. 88.1 percent drove to their destination which is an increase of 2.4 percent over 2016. On an annual basis, total vehicle miles increased 2.2 percent. The largest mileage gains were in North Carolina at 6.4 percent and Michigan at 7.5 percent. This traffic growth has been consistent while at the same time, toll systems have had regular or annual increases. The leverage in additional travel coupled with higher toll fees are allowing toll facilities to improve their infrastructure much faster than a non-toll facility.

Pennsylvania toll rate increases have been occurring annually since 2008, with the most recent increase being 6 percent for fiscal years 2017 through 2020. Even with the higher tolls and regular increases, the Pennsylvania toll usage is up 0.43 percent. Unless the growth in traffic improves to 1.26 percent that is needed for payments and maintain coverage levels, one can expect annual increases to continue. Vehicular travel looks to remain robust as fuels costs are currently low.

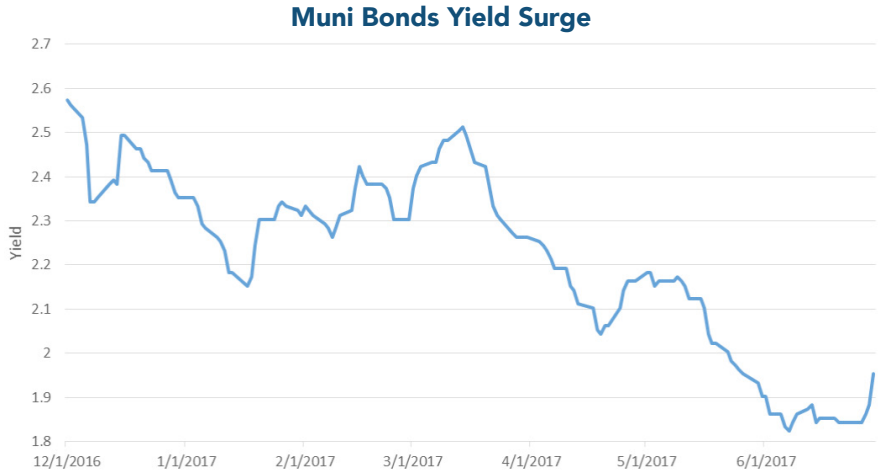
Speaking of tax increases, California increased the sales tax on a pack of cigarettes from 87 cents to $2.87 in an attempt to increase revenues for the state. While the revenues increased initially, it was most likely from cigarette users stockpiling ahead of the tax increase. The state has found revenue on cigarettes to be down 64 percent over last year. History continues to repeat as over-taxing a specific area will influence user habits. The cigarette tax windfall California was expecting just became a disappointment.

Municipal bond mutual funds witnessed one of the largest outflows of the year in the last week of June as $891 million was redeemed. Volatility will continue as unknown structures to tax reform, new issuance projections and bond redemptions become discussed ahead of reality. The graph on the following page shows bond yields surging at the end of 2Q17, defiantly against institutional projections. As volatility will continue in the markets, Crossmark will take advantage of trimming where needed when rates are low and adding aggressively, while extending duration when rates spike higher.

While the argument stands that redemptions will be extra-large when compared to previous years, new issuance could outpace previous years as municipalities are servicing fewer bonds at much lower rate levels so the capability to address projects is greater.

Municipal Fixed Income Commentary

Crossmark Global Investments continues to find value in the municipal secondary market with bonds rated A or better involved with essential services like water, sewer, power, streets, highways, school education and general obligations. The ideal maturities on the yield curve have moved to the 10 to 20 year range with a call feature between 2019 and 2026. Crossmark continues to hold a shorter duration than the Barclay's Quality Municipal Index with a focus on higher quality municipalities. Crossmark Global Investments continues to use municipal bond market volatility to opportunistically manage the portfolios entrusted to us.



Source: Bloomberg

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June 30, 2017

GLOBAL EQUITY INCOME COMMENTARY

Performance

The second quarter continued its momentum from the beginning of the year with equity markets moving higher as valuations increased. The Global Equity Income benchmarks of the S&P Global 1200 and the S&P 500 ended the quarter with returns of 4.31% and 3.09% respectively. For dividend income comparison purposes, the MSCI World High Dividend Yield Index returned 3.20%.

Factors Affecting Performance

U.S. economic growth was somewhat lackluster in the first quarter of 2017 but is expected to pick up in coming months. The anticipation for the administration's proposals on healthcare reform, trade policy and tax reform has been subdued as the challenge of getting a consensus through both the House and Senate becomes more apparent. While most of these policies would have a positive impact on the equity markets, there is also a degree of uncertainty associated with the final details of these bills and how they would be implemented. The Federal Reserve, confident that the economy has sufficient momentum, hiked rates in June and signaled that it intends to raise them again this year while also starting the process of reducing its balance sheet. In Canada, the economy's momentum remains strong, and real GDP growth is expected to pick up in the next few months. The Bank of Canada should now be in a position to potentially raise interest rates later this year. Overseas, the UK is beginning its Brexit negotiations, and the Bank of England has set its policy to cushion the economy from potential weaker demand. In the Eurozone, economic growth is picking up steam and unemployment is falling, however, wage growth remains weak.

Earnings growth has improved significantly in 2017. For the first quarter as represented by the S&P 500, earnings increased by 13.8% over the previous quarter. Estimated earnings growth for the full year of 2017 is now estimated to increase by 10%. The energy sector, after experiencing steep declines from low oil prices, is now estimated to rebound and have earnings growth of 268% for the full year.

2015 • 2016 • 2017
LIPPER BEST
STEWARD GLOBAL EQUITY INCOME FUND
Institutional (SGISX)
AWARD WINNER
FOR 5-YEAR PERIOD

WINNER OF THE 2017
THOMSON REUTERS
LIPPER FUND AWARDS
UNITED STATES
THIRD CONSECUTIVE YEAR

The U.S. Lipper Fund Awards recognized The Fund on March 31, 2015, March 22, 2016 and March 23, 2017 for delivering consistently strong risk-adjusted performance, relative to its peers, for the 5-year period. Chosen out of 66 others in 2015, 80 others in 2016, and 22 others in 2017, the Fund achieved the highest Lipper Leader for Consistent Return (Effective Return Net of Expenses) value over an individual time period in its classification.

Global Equity Income Commentary

The Global Equity Income strategy outperformed the S&P Global 1200, S&P 500 and the MSCI World High Dividend Yield Index in the second quarter of 2017. The portfolio equity allocation at the end of the quarter was 57% U.S. and 43% international. The largest positive contributor was McDonald's Corp. +18.90% as shares climbed on a strong first quarter earnings report. The results exceeded analyst expectations driven by the recently introduced all day breakfast items, Big Mac platform expansion and increased beverage offerings. Quest Diagnostics Inc. +13.73% shares soared after it delivered one of its finest quarterly earnings reports in the four years since the current CEO has led the company. Earnings easily beat consensus analyst estimates, and the company also raised its 2017 guidance reflecting a higher than expected tax benefit. Shares of InterContinental Hotels Group plc +14.22% shares rose on first quarter results which revealed a positive outlook across all of the company's regions except in the Middle East due to low oil prices. Management remained confident in the outlook for 2017 and their ability to deliver sustainable growth into the future.

Contributors to relative negative performance included International Business Machines Corp. –10.80% as shares dropped on its mediocre quarterly results. Revenue, earnings and margins declined as the company is increasing its investments in R&D which are not yet translating to profits. Expectations are optimistic for a turnaround in the near future. Shares of Analog Devices, Inc. –4.54% fell on an analyst downgrade that stated the company's optimistic outlook is already reflected in the current share price and viewed future guidance as more mixed than positive. This came after the company reported quarter results that beat analyst consensus on both earnings and revenue. Overall, the methodology has performed very well for the quarter and will continue to seek high quality dividend paying companies that can provide solid performance over the long term.

Global Equity Income Strategy

The Global Equity Income strategy pursues its objective through the investment in U.S. and non-U.S. dividend-paying stocks that have demonstrated above median yield, a positive trend in dividends and favorable earnings growth. These companies also represent a broad spectrum of the global economy. The objective of this strategy is to provide current income and the potential for capital appreciation at lower than overall market risk.

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June 30, 2017

THETA/GROWTH A COVERED CALL STRATEGY COMMENTARY

Second Quarter Performance Summary 2017

After taking a slight breather in April, the U.S. equity markets continued its upward trend in May. June was a different story as the markets traded off for the balance of the month. Neither the equity markets nor the bond markets reacted well to speeches that suggested the ECB could soon begin reducing its quantitative easing (QE) purchases, and the Bank of England might raise interest rates at some point this year. The two primary benchmarks for the Theta Growth strategy are the S&P 500 Covered Call Index (SPXCC) and the CBOE S&P 500 Buy Write Index (BXM). As the markets took a breather in April, Theta Growth model slightly outperformed the return of .86% for the SPXCC and was flat against the BXM. In May, as the markets continued to rally, Theta Growth model slightly underperformed the return of .98% for the SPXCC and underperformed the return of 1.78% for the BXM. The markets stalled a bit as the calendar flipped to June with the Theta Growth model outperforming the return of .33% for the SPXCC and outperforming the return of .35% for the BXM. Overall for the second quarter Theta Growth model outperformed the return of 2.19% for the SPXCC and was a few basis points behind the return of 3.07% for the BXM. The S&P 500 gained another 3.09% for the second quarter and is up 9.49% since the beginning of the year. Theta Growth is designed to outperform in flat to declining markets and will lag in quick rallying markets.

The S&P 500 – What Sectors Worked and What Did not Work in Q2 2017

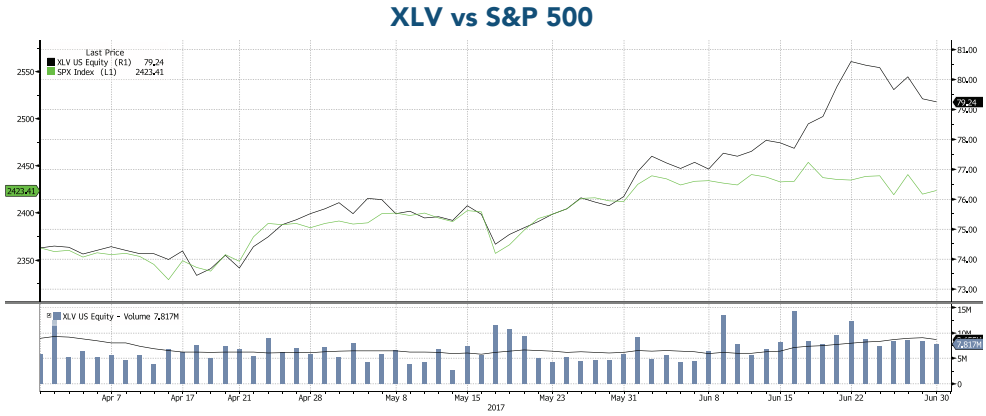
VIX vs S&P 500

Source: Bloomberg

- After taking a slight breather in April, the U.S. equity markets continued its upward trend in May. June was a different story as the markets traded off for the balance of the month.
- The Healthcare sector broke out in the second quarter as it the led the way with a return of 6.98%.
- Neither the equity markets nor the bond markets reacted well to speeches that suggested the ECB could soon begin reducing its quantitative easing (QE) purchases and the Bank of England might raise interest rates at some point this year.

Theta/Growth Commentary

The Healthcare sector broke out in the second quarter as it the led the way with a return of 6.98%. The Industrial sector was up 5.18% for the quarter followed by Financials up 4.36%. The Material and Technology sectors were up 3.15% and 3.06% respectively. The Energy sector was the big loser again for the second quarter as it returned -6.50%. The Energy sector is down -12.70% for 2017 following its banner year of 2016 when it was up 28.02%. The Consumer Discretionary, Utility and Consumer Staples sectors all had positive performance for the second quarter.



Source: Bloomberg

Best and Worst Trades/Performers Q2 2017

The following section provides a closer look at a few of the best and worst trades/performers of the quarter.

Best Trade/Performer

1. A slight underweight to the Energy sector as that was the worst performing S&P 500 sector for the quarter down -6.50%.
2. The individual Healthcare names in the Theta Growth portfolio had strong second quarters as the Healthcare sector was the best performing S&P 500 sector up 6.98%. Medtronic (MDT) was up 10.16% followed by Abbot Labs (ABT) up 10.12% and Gilead Sciences (GILD) up 5.35% for the second quarter.
3. Nike Corp. (NKE) had a great earnings announcement on the last day of the quarter and was up 10.96% on June 30th which resulted in a positive return of 6.23% for the quarter.
4. PayPal Holdings (PYPL) continued its strong 2017 with a solid return of 24.75% for the second quarter.
5. Kroger (KR) was sold from Theta Growth on April 25th and was down -13.21%. After another poor earnings announcement from Kroger, the stock was down another -21.59% after it was sold from the portfolio.

Worst Trade/Performer

1. After a banner first quarter up 16.15%, Lowes Cos. (LOW) was down -5.30% for the second quarter.
2. Verizon Comm. (VZ) continued to perform poorly in 2017 as it was down another -7.30% for the second quarter.
3. A slight underweight to the Healthcare sector was a drag on performance as that sector was the best performer for the quarter up 6.98%.

Theta/Growth Commentary

Looking ahead to the Second Quarter of 2017

As we begin the third quarter of 2017, historically September and August are the worst performing months of the year in relation to the S&P 500 index. Keeping this in mind, the potential for market volatility in the third quarter and the rest of the year definitely exists. One of the key questions for the balance of the year will be the extent to which equity and bond markets can withstand a gradual reduction in monetary stimulus which has been very supportive to markets over the past several years. Mario Draghi's recent speech on QE was one of the most market-moving events of the second quarter, with both bonds and equities selling off. The announcement of quantitative tightening from the Fed combined with the announcement of a reduction in QE from Mario Draghi and the ECB could very well be the events that trigger a potential pullback in the markets.

One of the key questions for the balance of the year will be the extent to which equity and bond markets can withstand a gradual reduction in monetary stimulus which has been very supportive to markets over the past several years.

The Theta Growth team will continue to look for opportunities to increase income by strategically putting on option trades as the present themselves. Even with the VIX hitting a low of 9.75 on June 2nd, the Theta Growth strategy is still able to generate attractive income through the use of call options and dividends.

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."

About Crossmark's 30 Year History

Crossmark, previously Capstone Asset Management Company, is an independent investment advisor headquartered in Houston, Texas. Founded in 1987, Crossmark is in its 30th year of providing portfolio solutions for financial advisors and institutional investors with values-based, SRI and ESG values and factor-based strategies. Additionally, Crossmark is the exclusive manager of the Crossmark Steward Funds, which is a fund family that applies an overarching values-based screening methodology to its suite of equity and fixed income funds, including its award-winning Global Equity Income Fund- named Lipper's "Best Global Equity Income Fund" for the last three consecutive years. Crossmark manages approximately $5 billion in assets with clients nationwide.

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June 30, 2017

LARGE CAP CORE GROWTH COMMENTARY

The rally in equities that began after the November 2016 election continued its upward charge in the second quarter with the S&P 500 gaining another 3.09%. The Russell 1000 Growth Index, our benchmark, added 4.67%. For the year-to-date, the indexes were up 9.34% and 13.99%, respectively. The Russell index was aided by strong technology performance for most of the quarter. For the second quarter, our Large Cap Core Growth model handily beat the S&P 500 while lagging the Russell 1000 Growth by a few basis points. For the period, our best performing sectors were Consumer Discretionary, Industrials and Healthcare, so it was a mixed bag of cyclicals and defensive sectors. Lagging sectors were Telecom, Energy and Consumer Staples. Energy is also cyclical but performed poorly as the price of oil declined from the mid-$50's to the mid-$40's. Telecom and Consumer Staples also trailed as slow growers were shunned. Adjustments to the LCCG model for the three-month period included the purchase of Rockwell Collins, maker of communications equipment, Charles River Labs, provider of research tools for drug development, and Microchip Technology, which develops, manufactures, and sells semiconductor products for various embedded control applications. Sales included General Mills and TJX Companies.

Investors are still expecting stronger growth going forward due to the administration's pro-growth agenda, but the time frame has been stretched from 2017 to 2018. A lot of questions remain as to just how much of the agenda will make it through the House and Senate gauntlets. Health care and tax reform seem to be having the most difficulty at this point. At the least, a significant reduction in regulations that impact corporate earnings should continue, and that alone could be a significant driver of profits and perhaps stock prices as well.

Recent economic statistics presented investors with a mixed picture as far as the economy, with strong results from such "soft" indicators as consumer confidence but weaker results from "hard" indicators such as gross domestic product. Automobile sales also slipped recently. One piece of hard data, the just-released ISM Manufacturing Index, posted quite a strong result with a reading of 57.8 for June. This was well above the consensus of 55.3 (readings above 50 indicate economic expansion). Especially of

- The rally in equities that began after the November 2016 election continued its upward charge in the second quarter with the S&P 500 gaining another 3.09%.
- Investors are still looking for stronger growth going forward from the administration's pro-growth agenda but the time frame has been stretched from 2017 to 2018.
- A significant reduction in regulations that impact corporate earnings should continue and that alone could be significant driver of profits and perhaps stock prices as well.
- Employment statistics continue to look strong.
- The corporate profits outlook for the second quarter now looks promising based on early reporting companies .

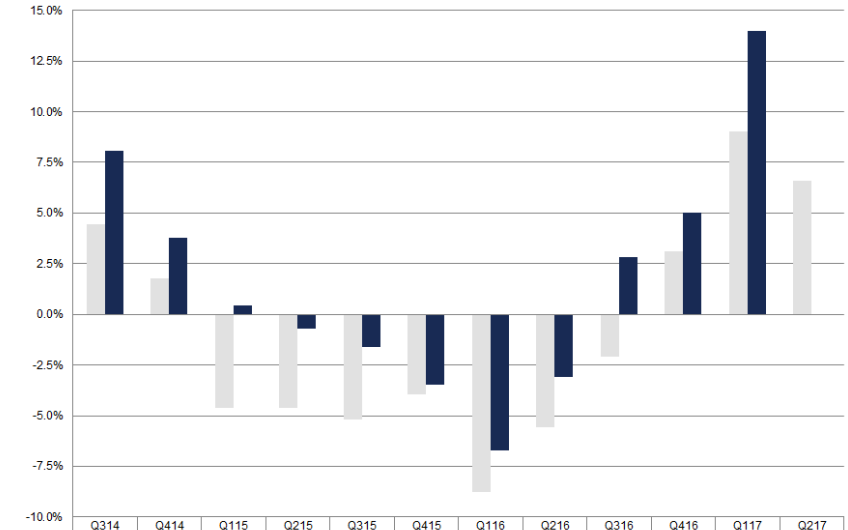
Large Cap Core Growth Commentary

note, the manufacturing improvement was broad based. Fifteen of eighteen industries reported growth, and major measures of activity stayed above the key 50 level while new orders and production posted the largest gains for June. The new orders index this year has averaged the highest start to a year since 2004. Another report, the June ISM for non-manufacturing companies, was also released and posted a solid 57.4, up 0.5 from May and ahead of the expectations of 57.1. This provides another good data point to confirm the economy is improving. Employment statistics continue to look strong. The June unemployment rate came in at 4.4%, up 0.1% from May. May was a 16-year low and essentially indicated full employment. The labor market appears to be tight, and the JOLTS job openings report just hit 6.04 million, the highest level since the JOLTS report has been published. Such a high level indicates employers are having trouble finding qualified applicants which has been an issue for some time. As for the Federal Reserve, it raised its target range for the federal funds rate to 1.00%-1.25% and currently expects inflation to hit its target of 2% in 2018 and 2019.

The corporate profits outlook for the second quarter now looks promising based on early reporting companies. The current estimate for second quarter earnings growth per share is for an increase of 6.6%. As the chart below illustrates, these early estimates are often on the low side, so we could be in for something closer to double digit growth.

Of course, the direction of equity prices is quite correlated with the direction of earnings. Revenue growth is also projected to increase, and already reported revenues for Q2 bolster that conviction. Nick Raich of the"Earnings Scout" publication notes that early reporters have posted revenue growth of 8.5%, so earnings are no longer just a cost-cutting story but also a growth story. Raich is quite encouraged by what he has seen thus far in Q2, and we share that sentiment. Second and third quarter earnings may set quarterly records. It, therefore, looks as if we are transitioning from a Federal Reserve-driven market to an earnings-driven market at just the right time.

S&P 500: Estimated Earnings Growth at End of Qtr. vs Actual Growth



	Q314	Q414	Q115	Q215	Q315	Q415	Q116	Q216	Q316	Q416	Q117	Q217
End of Qtr.	4.5%	1.8%	-4.6%	-4.6%	-5.2%	-3.9%	-8.8%	-5.6%	-2.1%	3.1%	9.0%	6.6%
Actual	8.1%	3.8%	0.4%	-0.7%	-1.6%	-3.5%	-6.7%	-3.1%	2.8%	5.0%	14.0%	

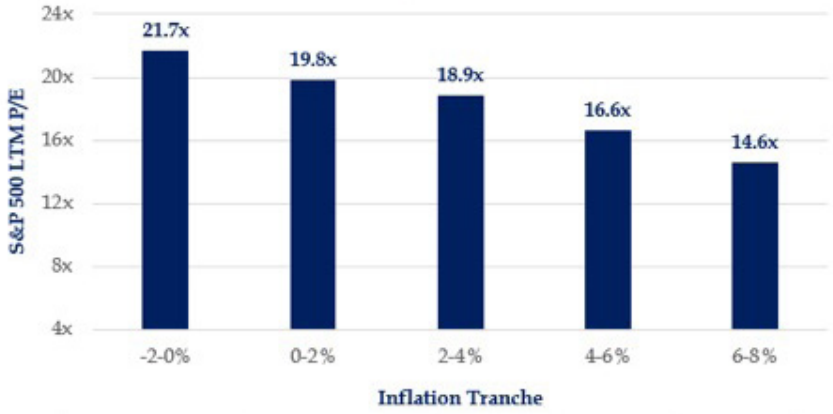
Source: FactSet

For the quarter, the stock market moved upwards through early June and then settled into a trading range of between about 2400-2450 to close out the quarter. We remain constructive on equities for 2017, but the market has gone a long way without a significant pullback so it would not be a surprise to see the market sell off between 5%-10% at some point in the next few months. That said, the indexes seem to be in a very positive position currently. The key indexes are "in gear," meaning they are moving up together and hitting new highs, a very bullish sign. The S&P 500, Dow Industrials, NASDAQ, and the Advance/Line all hit new highs in June. Even the Dow Transports went on to hit a new high in early July. This is considered a very bullish occurrence by followers of "Dow Theory." The theory postulates that when the Industrials and Transports both make new highs, indicating that both sectors of the economy are growing, then that should be positive for stocks. Actually, we would view a pullback as a "healthy" development as it would allow earnings to catch up to stocks prices and improve the valuation numbers. As it stands, the S&P 500 is currently trading at a PE of around 18.5x, so it is a bit stretched by historical standards. However, we are in a period of unusually low interest rates and inflation

which we refer to as a valuation "sweet spot". As the chart below indicates, markets can reach significantly higher levels during these periods so we have a bit of a cushion as long as inflation remains tepid.

Additionally, the yield curve is still sending an encouraging message with a positive slope and spreads that have widened a bit recently, as well. Now, if only Washington can get its act together and pass some growth-inducing legislation such as tax reform (including repatriation of overseas profits), we could possibly begin a new leg up on this bull market.

Average S&P 500 LTM P/E by CPI Y/Y Tranche
(1990 - Current)



Source: Strategas

Second and third quarter earnings may set quarterly records, and it looks as if we are transitioning from a Federal Reserve-driven market to an earnings-driven market just at the right time.

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