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ECONOMIC AND STRATEGY COMMENTARIES

4Q 2018 Commentaries

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

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December 31, 2018

ECONOMIC COMMENTARY

2018 has finally drawn to a close and we say good riddance. For the year, the S&P 500 closed down 4.39%. Not too horrible for a down year although it was the worst annual decline since 2008. However, for the fourth quarter, the index fell 13.52% and for December the decline was 9.03%, the worst December since 1931! The downside started at the beginning of October, as often seems to be the case, and ran through the last week of the year. Ten of eleven sectors were down for the quarter with utilities, the most defensive of sectors, posting a gain of 0.50%. Energy was the hardest hit sector, dragged down by falling oil prices which fell from $76 a barrel in October to $43 in December, down over 40%. Technology, the stellar performer for most of the year, fell 17.68% as the FAANGs stumbled badly for the period from not only high valuations but, suddenly, fears arose concerning fundamentals and business models. Apple Computer, which only joined the "four comma club" ($1 trillion market cap) last quarter, lost 37% from high to low in the fourth quarter and is back to only three commas for now. Much of the damage in December was probably due to tax selling where stocks with large losses are hit with seeming non-stop selling to lock in a tax loss prior to yearend. Sometimes these stocks will bounce in January in what is called the "January Effect."

Turning to the economy, the US economy continues to perform well with perhaps a bump or two in the road. The just released ISM Manufacturing survey for December came in at 54.1, below expectations of 57.5 but still a good reading indicating an expanding economy. Problematic however, are the two most forward-looking indices in the survey: new orders and production, which posted sizable declines. New orders declined 11 points to 51.1 and production fell 6.3 points to 54.3. The impact of tariffs undoubtedly had an impact on these numbers. The ISM Non-Manufacturing Survey declined to 57.6 versus expectations of 58.5. This is a minor decline and note that for 2018 the index averaged the highest reading since the series began in the late 1990s. Services growth was broad with 16 of 18 industries reporting expansion while only mining posted a decline. Obviously, services would be less impacted by tariffs. US employment statistics continue to look very strong. The December non-farm payrolls soared past the consensus, posting an increase of 312,000 versus expectations of 184,000. There were also revisions to past reports that added 58,000. The unemployment rate nudged up from 3.7% to 3.9% but that was due to an increase in the labor force of 419,000, a positive development. November's 3.7% rate was the lowest in almost 50 years. Average hourly

- For the year, the S&P closed down 4.39%.
- The US economy continues to perform well with perhaps a bump or two in the road.
- The just released ISM Manufacturing survey for December came in at 54.1, below expectations of 57.5 but still a good reading indicating an expanding economy.
- All told, the job market is in excellent shape.
- One potential problem has been interest rates which have been volatile as of late.

earnings rose 3.2% on a year/year basis. And the recent job openings data, known as JOLTS, while showing a slight decline, still shows there are more job openings than the number of people seeking work by about 800,000 (see chart below). All told, the job market is in excellent shape. One potential problem has been interest rates which have been volatile as of late. Rates surged in September through November as Fed Chairman Powell made a series of seemingly "hawkish" comments. But, as the stock market plunged, Powell and other Fed members changed their tone to a more "dovish" one. The ten year treasury interest rate had hit 3.24% in November but after Powell's comments rates started falling. By year end the 10 year rate was down to 2.68% and the speculation was for fewer than the three 2019 rate hikes previously expected. Some economists have speculated that the Fed may actually end up cutting rates in 2019. Lower rates would especially be a boon for the weak real estate market.

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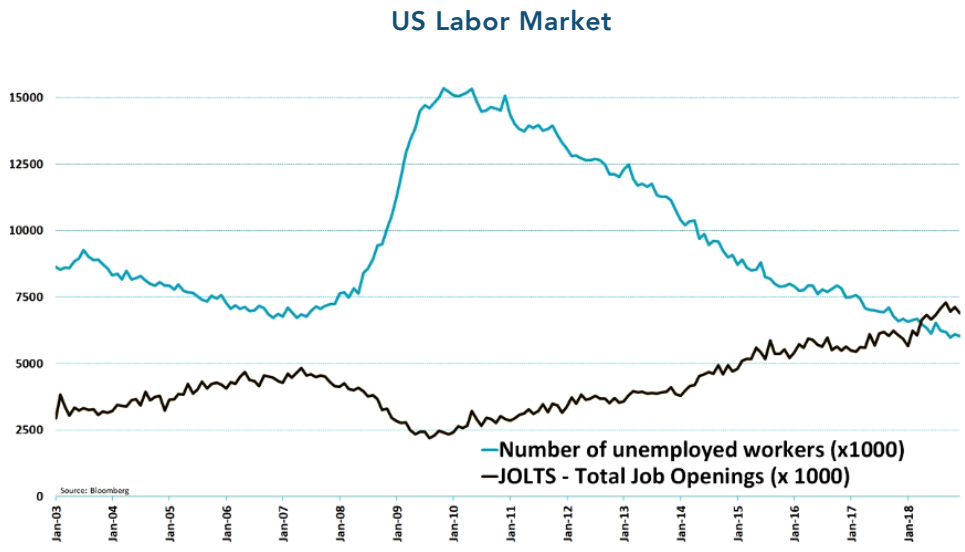

Source: Bloomberg

Turning to corporate profits, S&P 500 earnings were quite strong for the first three quarters in 2018 and fourth quarter earnings season, which begins shortly, is expected to produce another double-digit result. Current consensus for 4Q2018 is for growth of 11.4%. If accurate, it would be the fifth quarter in a row of double digit growth for the index. Of course, it will be the last quarter to be boosted by last year's tax cuts so growth is expected to fall back into single digits for 2019. Current FactSet consensus for 2019 is earnings growth of 7.4%, a fairly strong number given the tough comparison to 2018.

With the fourth quarter market pullback, equity valuations look much more attractive as we enter 2019. This has been the missing element for the last couple of years. At the end of the year, the S&P 500's 12 month forward PE had fallen to 14.1x, well below the five year average of 16.4x and the December 2017 high PE of 20.0x. Note that from the 2017 high, the index PE ratio has fallen about 30%. With the decent earnings growth anticipated for 2019 and somewhat less hawkish Federal Reserve, we have noted, the stage is being set for a strong upward bias for stocks. Of course, there are headwinds. We will have to deal with divided government now that the new Congress has been sworn in.

Economic Commentary

We are headed for gridlock but that is not necessarily a bad thing and history shows that markets often perform better during periods of divided government. Basically, it keeps politicians of both parties from creating too much economic mischief. From a technical perspective a lot of damage has been done to the charts so markets are not likely to go up in a straight line. That said, in late December we got into an extremely oversold condition followed by a very powerful positive volume surge. This can often mark at least a near-term bottom in stocks.

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About Crossmark's 30 Year History
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December 31, 2018

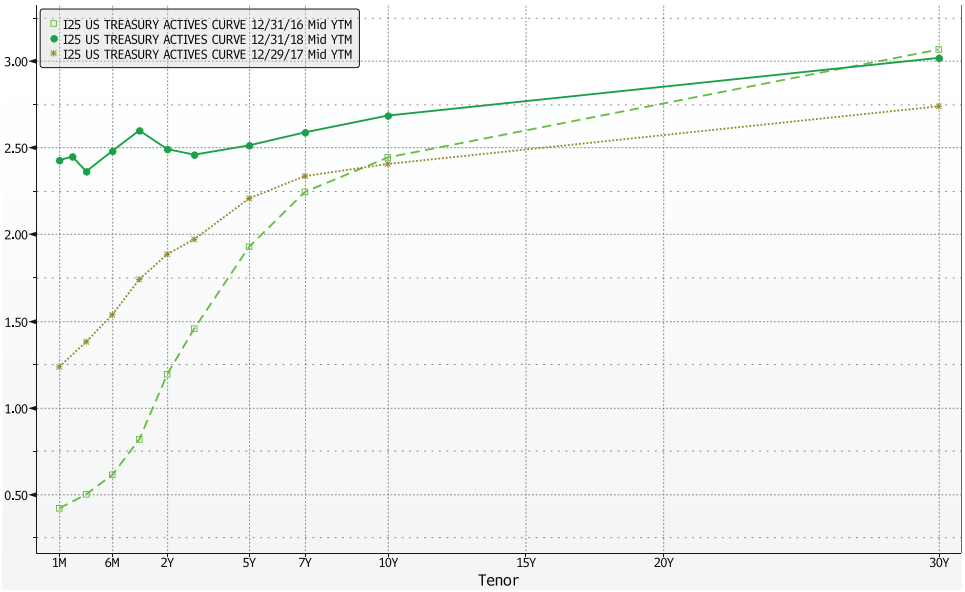
TAXABLE FIXED INCOME COMMENTARY

CORE FIXED INCOME
INTERMEDIATE FIXED INCOME
CURRENT INCOME PORTFOLIO
INCOME OPPORTUNITIES

Every new year we are faced with the concept of beginning anew. You hear sayings about turning over a new leaf, starting with a clean slate, setting new goals and we even sing about it with the traditional "Auld Lang Syne" which means "times gone by". But when we look at the markets as we turn the calendar from 2018 to 2019, it doesn't feel like a new beginning. On the contrary, it appears we have much more of the same – questions on what central banks will do, gridlock in Washington, slowing global growth concerns and continued talk of trade and tariff issues.

As we take a look back on the journey through 2018, we see that the anticipated rise in rates we spoke about a year ago came to fruition as yields moved to their multi-year highs at the beginning of November with the US 2yr Treasury reaching a yield of 2.96% and the 10yr climbing to 3.25%. The more conservative positioning within our fixed income products was advantageous during this time as we reduced our interest rate risk with shorter durations versus the comparable indices and maintained a high level of income that helped drive outperformance relative to the indices.

U.S. Treasury Yield Curve 2018



Source: Bloomberg

- We reduced our interest rate risk with shorter durations versus the comparable indices and maintained a high level of income that helped drive outperformance relative to the indices.
- We do anticipate increased volatility as the path of future Fed Fund rate hikes is determined.
- We are taking opportunities to shift our duration slightly out the yield curve as appropriate although maintaining our reduced interest rate exposure overall.

We also witnessed the yield curve flattening from around 55bps in January down to less than 20bps between the 2yr and 10yr treasury notes as we begin the new year leading many to fear a recession is near. The flattening yield curve combined with the other concerns looming in the market (trade, slower growth, etc.) developed into a fear that the Federal Reserve was too optimistic and the belief that the Federal Open Market Committee would make a policy mistake pushing the economy into recession sooner than originally anticipated. As these concerns grew, we saw the yield curve begin to shift downward and ended the year with the US 2yr Treasury at 2.49% and the 10yr note at 2.68% - a shift of roughly 50bps at the end of the 4th quarter. Although declining yields means market values increase for our fixed income holdings, our shorter duration resulted in a smaller increase as compared to the indices and an underperformance for 4Q18. However, the positive contributions from our duration positioning and income levels allowed the Core Fixed Income, Fixed Income Intermediate and Fixed Income Corporate models to outperform their indices for the year 2018. Although the preferred allocation was stronger the last month of the year, it did serve as a drag on performance in the Current Income Portfolio for the year 2018 with all other sectors providing positive contributions.

As we enter 2019, our 4 step investment process which includes decisions on duration, yield curve positioning, sector and security selection remains steadfast and we continually update our strategy based on this process. Unfortunately, we don't have a crystal ball to see exactly what central banks around the world will do over the coming quarters, but we do anticipate increased volatility as the path of future Fed Fund rate hikes is determined. We are taking opportunities to shift our duration slightly out the yield curve as appropriate although maintaining our reduced interest rate exposure overall.

So even though we may not be starting with a clean slate or new beginnings here in 2019 as it relates to the markets, we are always here to answer your questions and discuss our economic outlook. Although we can't control the markets, we can control our own lives, so I want to leave you with one of my favorite New Year's quotes:

Be at war with your vices, at peace with your neighbors, and let every new year find you a better man. – Benjamin Franklin

Happy New Year!

It appears we have much more of the same – questions on what central banks will do, gridlock in Washington, slowing global growth concerns and continued talk of trade and tariff issues.

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December 31, 2018

MUNICIPAL FIXED INCOME COMMENTARY

There's been twelve consecutive weeks of selling in municipal bond mutual funds. The final week of the year brought mixed results with net buying in long maturities and high yield while intermediate term investment grade endured net selling. Technically, intermediate municipal bond funds recorded thirteen consecutive weeks of selling. Interestingly, the Treasury market staged a rally of epic proportions in December primarily aided from domestic and global equity volatility. Staggering to see the yields bounce all over the spectrum during 2018 as the Federal Open Market Committee (FOMC) remained steady with four 25 basis point increases to short-term Federal Fund Rates. The ten year Treasury saw yields beginning around 2.43 percent then change to above 3.20 percent in the first quarter, to below 2.70 percent during the summer, another run above 3.24 percent in October/November then down to finish the year around 2.69 percent. That is more volatility than witnessed in the fixed income markets for many years and one can expect 2019 to usher in similar possibilities. Investors will probably reverse the course of liquidating municipal bonds to being net buyers.

There will likely be a January Effect in 2019 as fewer municipal bonds will be issued than what will mature, be called, and interest paid to investors. In short form definition, there will be "more buyers than sellers" and that will potentially drive pricing higher in the short-term to begin 2019. An influence to the dropping yields, including the equity market volatility to the downside in December as well as the Fed Fund futures posting a less than 15 percent chance of a rate hike in 2019 seems to have pushed municipal bond buyers to the sideline for the time being. Interesting that in 4Q18, everyone was convinced, and supported by FOMC guidance, there would be four interest rate hikes in 2019 and two rate hikes in 2020. It is interesting how a short period of time can change perception of anticipating two rate hikes to a current discussion of zero rate hikes going forward. In fact, some discussion has been centered as to when and how soon the FOMC will be dropping short-term Fed Fund rates. In 2018 when the FOMC was giving guidance of four rate hikes in 2019 and two in 2020, the Crossmark Global Investments Senior Portfolio Manager for Municipal Fixed Income speculated that the guidance might be aggressive and publically suggested two rate hikes in 2019 and possibly zero in 2020. Fast forward to the end of 2018 and some financial writers are producing articles outlining why there will be zero short-term Fed Fund rate hikes in 2019 and possible cuts due to deteriorating economic fundamentals. FOMC guidance sounds logical for 2019 which could produce more pronounced volatility in pricing especially as we approach each FOMC meeting. Should the FOMC include one or two rate hikes in 2019, the market could adjust in a violent fashion. Crossmark Global Investments is anticipating

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- There will likely be a January Effect in 2019 as fewer municipal bonds will be issued than what will mature, be called, and interest paid to investors.
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States collected more than $1 Trillion in tax revenue in fiscal 2018, which is a record.

trading in the municipal bond portfolios entrusted to us at a slower pace to begin the year, allowing some cash to build coupled with selective purchases in the best portion of the yield curve, then aggressively purchasing when volatility peaks and most individuals are selling.

The December FOMC meeting was about as dovish as possible, although the equity market might have interpreted the message as hawkish, driving equity values lower. FOMC signaled very clearly that if financial conditions deteriorate nationally or globally then they might not raise rates in 2019. However, FOMC base case at year end was to raise rates twice in 2019 and once in 2020 regardless of various factors, including but not limited to, Trump tweets at wee hours of the morning. There is also a media concern of the Quantitative Tightening and how this might increase the yields on the long end of the curve. At this time, there is no evidence Quantitative Tightening is having an effect, probably because it will take a substantial period of time to organically allow maturities to occur instead of actual selling of portions of the portfolio in the open market. At the end of each quarter going forward, the FOMC will perform their dot-plots and be tight fisted with information in order to not get backed into a corner and be forced to change course to their message and guidance. Therefore, it should have been unrealistic to expect the FOMC to signal the end of the current tightening cycle. Everyone wants immediate gratification but be aware that one may not get it on their predetermined time schedule.

To round out the year end commentary on a positive note, states collected more than $1 Trillion in tax revenue in fiscal 2018, which is a record, according to a report by the Tax Policy Center. The total increased by 4.8 percent from 2017. It is anticipated the states will refrain from immediately spending this windfall increase. Some will be placed in underfunded pensions and infrastructure investments, but don't be surprised if most of this is carried over for a rainy day.

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 7 to 15 year range with a call feature between 2020 and 2024. Crossmark Global Investments 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.

Crossmark Global Investments is anticipating trading in the municipal bond portfolios entrusted to us at a slower pace to begin the year, allowing some cash to build coupled with selective purchases in the best portion of the yield curve, then aggressively purchasing when volatility peaks and most individuals are selling.

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December 31, 2018

GLOBAL EQUITY INCOME COMMENTARY

Performance

The fourth quarter ended with a significant downturn in returns that was broad based throughout the developed markets and affected all equity styles. This erased all of the equity market gains attained previously during the year. The Global Equity Income benchmarks of the S&P Global 1200 and the S&P 500 ended the quarter with returns of –12.91% and –13.52% respectively. For global dividend index comparison purposes, the MSCI World High Dividend Yield Index returned –8.54%.

Factors Affecting Performance

Despite the recent sharp downturn in the equity markets, the economic front is still poised for sustained growth albeit a slightly slower rate. Recent sales and jobless claims in the U.S. surprised favorably further supporting the 2.5% forecast for Q4 real GDP growth. The Fed has continued to increase its funds rate target during the quarter however they have signaled at their last meeting that further increases will be less than previously anticipated for 2019. Trade policy could potentially still be a headwind going forward despite a temporary reprieve with China as additional tariffs have been postponed. Canada's economic growth has been slowing slightly due to slumping oil prices and higher interest rates which should continue to impact further into next year. Moving overseas, the Euro area has had a hit to growth with weak data reported by France in the face of a wave of street protests. The French government announced a package that is expected to calm protests and restore growth in the next quarter. In the UK, slow progress is being made towards Brexit. The prime minister has a difficult task of convincing a majority of the MPs that the deal she negotiated with the EU is in their best interests. Global economic growth is projected to come it at 3.7% for 2018. Forecasts for 2019 by the International Monetary Fund and the Organization for Economic Cooperation and Development have recently been lowered from 3.7% to 3.5%.

Company earnings as represented by the S&P 500 have posted another stellar performance with a 26% growth rate for the third quarter topping both previous quarters. Earnings growth for the full year of 2018 continues to be projected at a very healthy 20%. The energy sector continues to lead the group despite the recent sharp decline in oil prices with an estimated growth rate of 109%. All sectors are still projected to have positive growth rates for the year.

CROSSMARK STEWARD GLOBAL EQUITY INCOME FUND
Institutional (SGISX)

BEST GLOBAL EQUITY INCOME FUND AWARD WINNER
FOR 5-YEAR PERIOD

2018
THOMSON REUTERS
LIPPER FUND AWARDS
UNITED STATES
FOURTH CONSECUTIVE YEAR

Thomson Reuters recognized the Crossmark Steward Global Equity Income Fund at the U.S. Lipper Fund Awards on February 27, 2018 for delivering consistently strong risk-adjusted performance relative to its peers in the Global Equity Income Funds category for the three-year and five-year periods ending 11/30/2017. The number of peer funds included in the category was 36 for the three-year category and 31 for the five-year category. Each award was based on the Fund achieving the highest Lipper Leader for Consistent Return (Effective Return Net of Expenses) value over the stated time period.

Global Equity Income Commentary

The Global Equity Income strategy outperformed the S&P Global 1200 but underperformed the MSCI World High Dividend Yield Index for the fourth quarter. This completes another year of outperformance by the strategy against both benchmarks. The portfolio equity allocation at the end of the period was 61% U.S. and 39% international. Positive relative performance was led by McDonald's Corp. +6.80% which announced solid third quarter results. This represented 13 consecutive quarters of positive global comparable sales. In addition, the company has made substantial progress modernizing restaurants around the world and they remain confident that their current strategy will drive long-term profits and growth. Smith & Nephew +1.53% reported numbers that were in-line with analyst consensus and confirmed the outlook for the fiscal year. Guidance looking forward included an acceleration of growth from the slower first half of the year and a better margin expansion forecast even without the benefit of a pending favorable legal settlement. ResMed Inc. -0.94% achieved solid global revenue growth over the past several quarters which was led by sales of sleep devices, respiratory care devices, mask systems and software solutions. The company has outperformed its industry and has done impressively well across all of its geographical regions. Recent analyst upgrades cite a favorable outlook for 2019 based upon new product launches and a positive impact from recent M&A activity.

Negative contributors to relative performance included Valero Energy Corp. –33.44%. The company sold off due to the sharp decline of oil prices as well as a buyback of all outstanding units of Valero Energy Partners at a premium. The company however is still posting good results and its continuing investments in ethanol and its Diamond Green Diesel joint venture should position it well in the green energy space moving forward. Shares of China Petroleum & Chemical Corp. –29.71% slid on reports from various financial media that the company may have suffered transaction losses in its crude oil and petrochemical products trading business. The company disclosed that the business unit did incur some losses during certain crude oil transactions due to the oil price drop however they were not significant. Financial reports however indicated improved performance in four core business segments with significant cost savings and efficiency enhancements. Overall, the effectiveness of the methodology and quantitative screens for stock selection continue to perform as designed and are meeting or exceeding expectations.

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 the ability to maintain a higher yield, increase dividends over time and generate significant earnings. These companies also represent a broad spectrum of the global economy. The objective of this strategy is to provide current dividend income and the potential for capital appreciation at lower than overall market risk.

Despite the recent sharp downturn in the equity markets, the economic front is still poised for sustained growth albeit a slightly slower rate.

Global Equity Income Commentary

Top 10 Model Holdings [1]

Microsoft Corp.
McDonald's Corp.
Unilever N V
Intel Corp.
Taiwan Semiconductor Mfg Co.
Pepsico, Inc.
Smith & Nephew plc
ResMed, Inc.
Medtronic plc
Verizon Communications

% of Total Portfolio: 23%

[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 12/31/2018.

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December 31, 2018

COVERED CALL INCOME COMMENTARY

Fourth Quarter Review

October turned out to be downright scary for the markets as stocks had their worst month of performance since September of 2011. Volatility came back with a vengeance, which should not have come as that big of a surprise given the fact that interest rates continued to rise, Fed uncertainty was still high, trade negotiations with China continue to persist and mid-term elections were rapidly approaching. The higher volatility that investors are experiencing seemed likely to persist and did it ever. Sounds pretty unnerving. However, the markets entered what has been a historically strong seasonal period. The months of November and December of mid-term election years have been quite strong as history has shown. The broader fundamentals of the markets still remained favorable in October with Corporate earnings up again over 20%, profit margins remained close to historical highs, and sales growth continued to run at a pace not seen in several years. All of those factors seemed to indicate healthy tailwinds for the markets.

Geopolitical events continued to move the markets over most of the month of November. The U.S. mid-term elections produced an outcome that most everyone expected as the Democrats took control of the House of Representatives with the Republicans increasing their hold on the senate. Risk off sentiment within the markets prevailed through most of the month as the U.S. administrations approach to global trade continued to be quite hostile. The most important meeting at the G-20 event turned out to be a dinner between President Xi of China and President Trump as the two world leaders sat down to discuss quite a few topics but none more important than the issues surrounding trade. Any whisper of good news coming out of that dinner meeting would have the markets off to the races again. All one had to do was look at S&P futures on Sunday night to determine how global equity investors thought of how the meeting went between the leaders of the world's two largest economies. As far as the Fed goes, the markets did not have to wait until the December meeting to receive some good news from Fed Chair Powell. Chairman Powell's comments indicated a more meaningful dovish tone which was drastically different than anything he had stated publically in the past several months. As with the Trump/Xi dinner, the markets again reacted favorably.

The final month of 2018 was not a December to remember from a market standpoint. Investors had to contend with rising U.S. central bank rates, the ongoing trade conflict between the U.S. and China, weaker Chinese growth and continued rising geopolitical concerns. Also, the Treasury yield curve inverted, a further sign investors are worried the economy is slowing. The yield curve doesn't cause a recession, but it expresses concerns the Fed has raised rates too high and too fast and will have to cut in the near future. After a few near misses, the S&P 500 finally entered into a correction in the middle of the month,

- Risk off sentiment within the markets prevailed as the U.S. administrations approach to global trade continued to be quite hostile.
- The last week of the month saw wild swings in the global stock markets as shifts in sentiment pushed the markets sharply higher and lower without much rationale.
- Overall, the Covered Call Income strategy outperformed both the BXM and S&P 500 index for the 4th quarter.

meaning the index closed more than 10% below its previous all-time high. The S&P 500 index played chicken with these levels earlier but had always rallied enough at the close to stay above the 10% threshold. Global markets continued to decline as the Fed raised rates and lowered expectations for future rate hikes but investors expressed dismay with the rhetoric coming from the Fed. The last week of the month saw wild swings in the global stock markets as shifts in sentiment pushed the markets sharply higher and lower without much rationale.

Consider these records for the market during the last week of trading:

- Investors experienced the worst Christmas Eve on record and the markets were only open half of the day.
- The day after Christmas saw the Dow set a record for the largest single-day point gain.
- On Thursday the 27th, the Dow moved from 600pts down to 250pts up making it the largest single-day rally in the Index's history.

Can you imagine what the markets would have done on Christmas Day had they been open?

VIX vs S&P 500 YTD

Source: Bloomberg

The Covered Call Income strategy outperformed the primary benchmark of the BXM in October and December and slightly lagged the BXM for the month of November. Overall, the Covered Call Income strategy outperformed both the BXM and S&P 500 index for the 4th quarter. The option overlay on the Covered Call Income strategy was a boost from an attribution standpoint as well for the quarter. The premiums from the call options sold plus dividends received from the underlying stocks enabled income generated to hit over 3% for the quarter. The Covered Call Income strategy utilizes a sector neutral approach to the S&P 500 sector weights. Taking this approach takes quite a bit of risk off the table. From an attribution standpoint, the strategy was affected in the following ways for the quarter:

- Consumer staples, healthcare and utilities were sectors that produced a positive attribution to the strategy. Stocks held in the strategy that individually performed well for the quarter within these sectors included: WMT, KO, ABT and EXC.
- Consumer discretionary, technology, financials and energy were the sectors that lagged from an attribution standpoint. Stocks held in the strategy that contributed to negative attributions included: HAL, TXT and ATVI.

Covered Call Income: Looking ahead to 2019

We have no reason to expect markets to become less volatile over the near term. The fact the markets ended the year on a positive note might add some momentum heading into the New Year. The core issues of slowing growth, what actions the Fed will take in 2019, U.S. and China trade and Brexit will continue to produce a high level of uncertainty in the markets which will in turn provide for more volatility. Look for the Crossmark Covered Call Income team to strategically place trades in order to generate additional income while using volatility to the strategies advantage. Bucket your seatbelts as we head into 2019.

Chairman Powell's comments indicated a more meaningful dovish tone which was drastically different than anything he had stated publically in the past several months.

Covered Call Income Commentary

Top 10 Model Holdings [1]

Abbott Labs
Exxon Mobil Corp.
Visa, Inc.
Coca Cola Co.
Intel Corp.
Oracle Systems Corp.
Exelon Corp.
Nike, Inc.
Cisco Systems, Inc.
United Technologies Corp.

% of Total Portfolio: 36%

[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 12/31/2018.

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. Investing in equity securities involves market risk, including the possible loss of principal.

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 Global Investments is an innovative investment management firm. We provide a full suite of investment management solutions to institutional investors, financial advisors and the clients we serve. We have a multi-decade legacy of specializing in values based investment strategies for clients. Founded in 1987, the firm is headquartered in Houston, Texas and manages approximately $4.5 billion in AUM.

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December 31, 2018

LARGE CAP CORE GROWTH COMMENTARY

2018 has finally drawn to a close and we say good riddance. For the year, the S&P closed down 4.39%. Not too horrible for a down year although it was the worst annual decline since 2008. However, for the fourth quarter, the index fell 13.52% and for December the decline was 9.03%, the worst December since 1931! The Russell 1000 Growth Index, our benchmark, followed a similar path but was down 15.89% for the quarter and 8.60% for the month. The downside started at the beginning of October, as often seems to be the case, and ran through the last week of the year. Ten of eleven sectors were down for the quarter with utilities, the most defensive of sectors, posting a gain of 0.50%. Energy was the hardest hit sector, dragged down by falling oil prices which fell from $76 a barrel in October to $43 in December, down over 40%. Technology, the stellar performer for most of the year, fell 17.68% as the FAANGs stumbled badly for the period from not only high valuations but, suddenly, fears arose concerning fundamentals and business models. Apple Computer, which only joined the "four comma club" ($1 trillion market cap) last quarter, lost 37% from high to low in the fourth quarter and is back to only three commas for now. Much of the damage in December was probably due to tax selling where stocks with large losses are hit with seeming non-stop selling to lock in a tax loss prior to yearend. Sometimes these stocks will bounce in January in what is called the "January Effect."

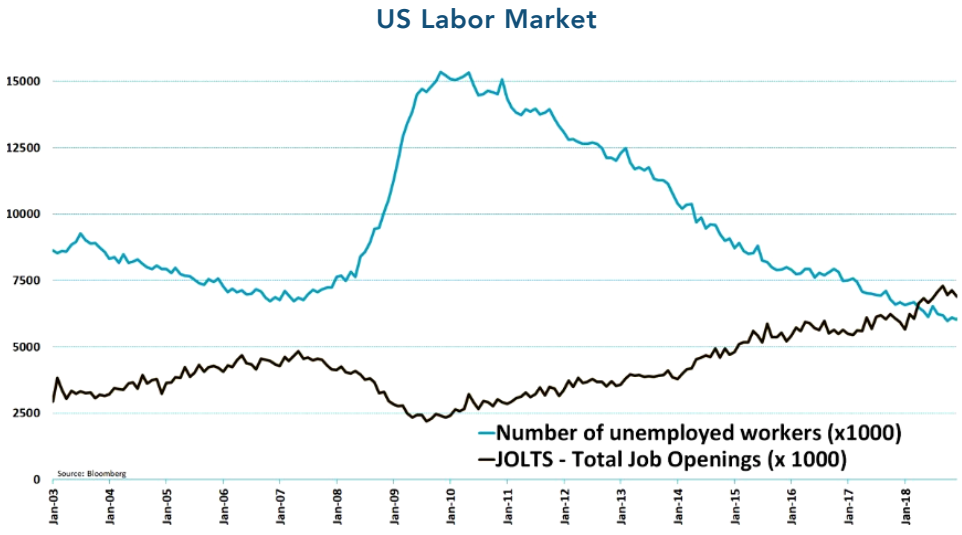
Our Large Cap Growth Model performed well in the fourth quarter. However, it lagged the Russell Growth Index for the year by just seven basis points. Posting a return of -1.58% versus the benchmark's return of -1.51%. The poor performance of the FANG-type stocks was a major factor for the quarter with the NYFANG Index falling 19.86% for the period. While the LCCG Model is fairly heavily weighted in technology stocks, it is less so in the very-high PE names and this really boosted our performance. Our top performing sectors for the fourth quarter were Materials which were down "only"5.73%, Staples which fell 6.83%, and Health Care, down 7.25%. Health Care and Staples are, of course, less affected by the economy so it is not surprising to see them near the top. Conversely, our poorer performing sectors were Energy, down 24.23%, Communication Services, which fell 20.63% and Technology, down 17.11%. As for individual stocks, Eli Lilly won the performance derby by gaining 8.39 %. The company gave good guidance and had excellent reports on Trulicity. Verizon, a defensive name, and Coca Cola also did well. Lagging names included Activision Blizzard, Square Inc., and Schlumberger.

- For the year, the S&P closed down 4.39%.
- The US economy continues to perform well with perhaps a bump or two in the road.
- The just released ISM Manufacturing survey for December came in at 54.1, below expectations of 57.5 but still a good reading indicating an expanding economy.
- All told, the job market is in excellent shape.
- One potential problem has been interest rates which have been volatile as of late.

Large Cap Core Growth Commentary

Our Large Cap Growth Model performed well in the fourth quarter. However, it lagged the Russell Growth Index for the year by just seven basis points. Posting a return of -1.58% versus the benchmark's return of -1.51%.

Turning to the economy, the US continues to perform well with perhaps a bump or two in the road. The just released ISM Manufacturing survey for December came in at 54.1, below expectations of 57.5 but still a good reading indicating an expanding economy. Problematic however, are the two most forward-looking indices in the survey: new orders and production, which posted sizable declines. New orders declined 11 points to 51.1 and production fell 6.3 points to 54.3. The impact of tariffs undoubtedly had an impact on these numbers. The ISM Non-Manufacturing Survey declined to 57.6 versus expectations of 58.5. This is a minor decline and note that for 2018 the index averaged the highest reading since the series began in the late 1990s. Services growth was broad with 16 of 18 industries reporting growth while only mining posted a decline. Obviously, services would be less impacted by tariffs. US employment statistics continue to look very strong. The December non-farm payrolls soared past the consensus, posting an increase of 312,000 versus expectations of 184,000. There were also revisions to past reports that added 58,000. The unemployment rate nudged up from 3.7% to 3.9% but that was due to an increase in the labor force of 419,000, a positive development. November's 3.7% rate was the lowest in almost 50 years. Average hourly earnings rose 3.2% on a year/year basis. And the recent job openings data, known as JOLTS, while showing a slight decline, still shows there are more job openings than the number of people seeking work by about 800,000. All told, the job market is in excellent shape. One potential problem has been interest rates which have been volatile as of late. Rates surged in September through November as Fed Chairman Powell made a series of seemingly "hawkish" comments. But, as the stock market plunged, Powell and other Fed members changed their tone to a more "dovish"one. The ten year treasury interest rate had hit 3.24% in November but after Powell's comments rates started falling. By year end the 10 year rate was down to 2.68% and the speculation was for fewer than the three 2019 rate hikes previously expected. Some economists have speculated that the Fed may actually end up cutting rates in 2019. Lower rates would especially be a boon for the weakening real estate market.



Source: Bloomberg

Turning to corporate profits, S&P 500 earnings were quite strong for the first three quarters in 2018 and fourth quarter earnings season, which begins shortly, is expected to produce another double-digit result. Current consensus for 4Q2018 is for growth of 11.4%. If accurate, it would be the fifth quarter in a row of double digit growth for the index. Of course, it will be the last quarter to be boosted by last year's tax cuts so growth is expected to fall back into single digits for 2019. Current FactSet consensus for 2019 is earnings growth of 7.4%, a fairly strong number given the tough comparison to 2018.

With the fourth quarter market pullback, equity valuations look much more attractive as we enter 2019. This has been the element that has been missing for the last couple of years. At the end of the year, the S&P 500's 12 month forward PE had fallen to 14.1x, well below the five year average of 16.4x and the December 2017 high PE of 20.0x. Note that from the 2017 high, the index PE ratio has fallen about 30%. With the decent earnings growth anticipated for 2019 and somewhat less hawkish Federal Reserve, we have noted the stage is being set for a strong upward bias for stocks. Of course there are headwinds. We will have to deal with divided

Large Cap Core Growth Commentary

government now that the new Congress has been sworn in. We are headed for gridlock but that is not necessarily a bad thing, and history shows that markets often perform better during periods of divided government. Basically, it keeps politicians of both parties from creating too much economic mischief. From a technical perspective a lot of damage has been done to the charts, so markets are not likely to go up in a straight line. That said, in late December we got into an extremely oversold condition followed by a very powerful positive volume surge. This can often mark at least a near-term bottom in stocks.

Top 10 Model Holdings [1]

Microsoft Corp.
Apple, Inc.
Alphabet Class C
Home Depot, Inc.
O'Reilly Automotive, Inc.
UnitedHealth Group, Inc.
JP Morgan Chase & Co.
CDW Corp.
Cisco Systems, Inc.
Texas Instruments, Inc.

% of Total Portfolio: 38%

[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 12/31/2018.

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