CROSSMARK GLOBAL INVESTMENTS

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March 2018

MONTHLY COMMENTARIES

Monthly Commentaries Overview

Is it just us or did the shortest month of the year, February, just feel like one of the longest in recent market memory? In looking at a longer-term chart of equity market prices on a month-end closing basis, one would be wondering what all the fuss is about. Even in the pre-Feb'18 low realized and implied volatility environment, a -3.9% decline in the S&P 500 over a 1-month period doesn't appear overly dramatic (an average of just -0.1% per day). A daily chart, however, might argue otherwise. As discussed throughout our Covered Call Income, Large Cap Core Growth commentaries (see page 3), the S&P 500 corrected nearly ~10% in the first week or so before rebounding ~5% off early February lows to finish the month at the aforementioned -3.9%.

U.S. Treasury yields shared a similar volatile path in early February. U.S. 10-year Treasury yields started the month a little above 2.7%, peaked around 2.95% in conjunction with the equity sell-off, but have now "developed a pretty strong range between 2.80-2.90%" as stated in our Taxable Fixed Income commentary. The markets' wild ride came just in time for rodeo season here in Texas with the start of the Houston Livestock Show and Rodeo. Certainly, the Taxable Fixed Income commentary is spot on with its analogous comparison to the February ride in the markets – It feels like volatility has finally graduated from Mutton Bustin'[1] to the real deal (bull riding). Despite the volatile markets, both our Taxable and Municipal fixed income performance in February outperformed their comparable benchmarks as they've long been positioned for rising rates in shorter duration securities. Additionally, according to our Municipal Fixed Income manager, as the 10-year US Treasury rates continue "Flirting With Three" (3%), "we will seek opportunities to purchase intermediate maturities with a longer call feature than what has been focused on in previous quarters." This is something our Taxable Fixed Income team will also be strategically considering as opportunities arise… opportunities which could be created from sustained volatility.

Taxable Fixed Commentary

Every year around this time in Houston, the city celebrates the world's largest livestock show and rodeo with three weeks of animals, food, concerts, food, carnivals, food, fun and more food. The Houston Livestock Show and Rodeo provides year-round educational support to the community and has committed more than $450 million to Texas youth since 1932. One of my children's favorite parts is the carnival, especially the rides that spin you all around – no thank you; I will wait at the exit point for them to come off the ride. If you were in the markets during the month of February, you probably felt like you were on one of those rides as well.

1 http://www.rodeohouston.com/Get-Involved/Competitors/Mutton-Bustin

With the release of the jobs report on the first Friday in February, investors' fears took off like a roller coaster and fears of inflation and being caught on the wrong side of volatility drove the markets to record swings over the following days. Once we all stepped back and took a breath, the fixed income markets developed a pretty strong range between 2.80-2.90% for the U.S. 10yr Treasury note. The move higher in yields during both January and February have moderated as the markets await additional signs of whether inflation is shifting higher, which would give the Federal Reserve support to move forward with three or possibly four rate hikes this year.

The taxable fixed income portfolios are positioned with a reduced sensitivity to interest rate movements and therefore outperformed their comparable indices for the month of February and year to date for 2018. Reduced interest rate risk coupled with higher levels of income were positive contributors to performance and were factors in helping to reduce market value volatility as compared to the index. With U.S. 10 -year Treasury yields moving closer to the currently neutral rate of approximately 3.0%, we will take opportunities to invest slightly further out the yield curve than we have over the past few quarters and capture increased yield levels. We still have many factors that could continue to cause volatility in the markets and we will be closely watching and assessing our strategy to make any portfolio shifts we deem appropriate. Stay focused on the fundamentals, and if you are ever in Houston during February and March, come rodeo with us!

Municipal Fixed Income Commentary

Flirting With Three might sound like a television sitcom while also describing February interest rates for the 10 year Treasury. With the 10-year Treasury rate coming excitingly close to 3 percent, fixed income markets suffered price declines across the board. The municipal bond market again decoupled from normal fixed income market activity by holding prices better than other sectors as new issuance was decidedly smaller than previous February periods. The rush to bring bonds to the market before year-end Tax Reform reduced activity to a trickle this month, which helped to cushion the pricing of municipal bonds. Interestingly, while rising interest rates historically damper inflows to municipal bond mutual funds, this time the inflows remained positive for the month, also contributing to less inventory for investors.

Tax Reform eliminated, for the time being, advance refunding, a key tactic used by local and State governments to refinance tens of billions of dollars of municipal bond debt every year. With this elimination, Bloomberg reports that new issuance of municipal bonds is down 38 percent for 2018 from a year earlier. Historically, the pace of issuance should pick up in March and April so there is some relief on the horizon to low inventory and slightly higher pricing than where it should be based on the current interest rate levels. The team at Crossmark Global Investments remains disciplined on the negotiation of pricing for the benefit of the client, especially when spreads widen as volume is muted as experienced in February.

Crossmark Global Investment's Municipal Bond Portfolios are shorter duration resulting in a reduced sensitivity to interest rate movements and therefore outperformed the comparable indices for the month of February and year to date for 2018. With 10 year Treasury yields flirting 3.0 percent, we will seek opportunities to purchase intermediate maturities with a longer call feature than what has been focused on in previous quarters. This activity will continue as interest rates inch higher. There could be many factors that continue to cause volatility in the markets and we will be closely watching for opportunities in the markets to make any portfolio shifts deemed to be appropriate.

Covered Call Income Commentary

Covered Call Income: February in Review

The first month of 2018 was a continuation of the 2017 rally as markets across the board were all up in January. Unfortunately, February could not have been worse for the markets following a global sell-off at the beginning of the month. Volatility made an all-important appearance following historically low levels over the past several years. The market sell-off that mostly defined the month of February can be explained by a rapid change in investor sentiment over new concerns that the Fed will tighten monetary policy faster than previously anticipated in response to signs of growing inflation, which can deter growth and earnings. All that being said, the global economy continues to show growth, corporate earnings are still strong, and the potential growth catalyst provided by the end of 2017 tax legislation is already coming to fruition in the U.S. The issues other than Fed policy that could potentially derail the growth of the markets are still the usual suspects that have been in the discussion since President Trump was elected: political and geo-political events with North Korea leading the way, ongoing political and legal issues within the Administration, and quite possibly trade and currency battles. A losing month of February ended a 10-month winning streak, the longest such streak since 1959. The good news is that March is typically one of the better performing months of the year.

After starting 2018 on a positive note with January producing another positive month, the Covered Call Income strategy traded off with the markets in February but still outpaced the strategies primary benchmark of the S&P 500 Covered Call Index. All sectors of the S&P 500 were down across the board in February. For the month, the markets were led by the technology, utility, financial and consumer discretionary sectors, with those being down the least for the month. The Covered Call Income strategy benefitted from a slight overweight to both the Technology and Financial sectors. The energy sector was the worst performing sector for the month. Volatility finally showed up in February as the VIX swung violently over the first few weeks of the month. 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. Even though the markets traded off, February proved to be an important month in regards to selling covered calls.

Covered Call Income: Looking Ahead

After a February to forget, stocks are entering the month of March, which is historically one of the better performing months of the year. February, on the other hand, is the third worst performing month going all the way back to 1945. Coming into the year, investor sentiment was strong and that carried over to January. February seemed to rile up investors with the thought of inflation and the Fed raising rates faster than anticipated. In Fed Chair Powell's first public comments, the rhetoric did not change from his policies to those of his predecessor Fed Chair Yellen. However, the markets quickly sold off with investors almost looking for any reason to sell. Volatility is healthy for the markets and good for covered calls. The markets have seen rates move higher over the past several years and have been able to handle as well as continuing to move to record highs. The consensus view still remains that the Fed will look to raise rates 3-4 times in 2018. Continued earnings and revenue growth coupled with low but rising rates and low but rising volatility look to make for a positive market environment for the rest of the first quarter and into the second quarter.

Large Cap Core Growth Commentary

The post-election record-breaking stock market rally finally ended with a bang! The S&P 500 dropped just over 10% on a closing basis during the selloff and the Dow Industrials actually dropped over 3,000 points during the turmoil. The markets settled down a little bit with the S&P 500 ending February down 3.69% on a total return basis. The Russell 1000 Growth Index, our benchmark, fell 2.62%. The Russell index was supported a bit by the strong weighting of Facebook, Amazon, Netflix and Google/Alphabet (collectively known as the FANG stocks) in the index. They performed relatively well during the selloff and subsequent bounce. Volatility, which had been so low in 2017, skyrocketed to just over 50 from the recent low of 12.50. It settled back to about 20 at the close of the month. For the month, our Large Cap Core Growth model outperformed the S&P 500 but lagged the Russell 1000 Growth.

For our Large Cap Core Model, our best performing industries were financials and technology, with gains of 0.15% and -0.01%, respectively. You know it's been a tough month when your two best sectors show such paltry returns. Conversely, our lagging sectors were energy, down 11.74%, and telecommunications, down 11.71%. As for individual securities, Cisco Systems won the month with a total return of 7.80%, followed by Apple, which rose 6.81%. Cisco reported strong results for the quarter and benefited from several analyst upgrades. Apple rose as investors became more optimistic about 2018. Laggings stocks included Celgene, the biotech company, after the FDA gave a "refusal to file" notice on one of the company's key future drugs. Exxon-Mobil was also weak as oil prices declined through much of February.

Adjustments to the model included trimming our Thor Industries position as industry demand appeared to weaken and we initiated a new position in Tapestry, previously known as Coach.

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. 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 Steward Global Equity Income Fund - named Lipper's "Best Global Equity Income Fund" for the last four consecutive years.

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Thompson 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.

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