Advisors Capital Management

2018 REVIEW AND OUTLOOK

Q3

INSIDE THIS ISSUE

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ACM Investment Committee
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Economic Commentary

Normally, this letter would begin by looking back at the behavior of the economy and markets over the prior quarter, but given the tumult in the market in October, it seems more appropriate to start the more recent developments since the end of the quarter. It has finally dawned on investors that interest rates are likely to rise more and faster than they had previously realized, something we have been expecting for some time. In combination with the uncertainties of a possible trade war with China, many investors became nervous and the market tumbled. Nonetheless, we still see a fundamentally sound economy, so we think the setback will prove to be another buying opportunity.

As I wrote recently, fear mongering remains rampant:

> Anytime the market takes a tumble, the Chicken Littles of the world come out to predict the coming stock market collapse. Because market corrections are quite common, they get this forecast right roughly one out of ten times, if that often.

Just this morning, a broadcast interview showed Peter Schiff, a perma-bear who has forecast the coming depression at least quarterly for a minimum of two decades, projecting gold prices would hit $5,000. He didn't mention that his firm sells gold and earns commissions on those sales. But this is great material for the 24/7 news cycle of business television.

We see the economy quite differently. The Fed is trying to maintain economic growth to enable more unemployed workers to find jobs, yet must raise interest rates to moderate the pace of growth so it doesn't overheat and cause inflation to take off. If they raise rates too much, the economy could go into recession. If they don't raise rates enough, inflation could surge. It's a delicate balancing act.

The typical person engages in such balancing acts every day.

Can you drive a car? Turn your car too much to the left and you'll go over the center line and hit an oncoming vehicle. Turn too much to the right and you could land in a ditch. Despite the narrow path for safety, almost all of us arrive at work each day and make it home at night. The Fed's job is a bit tougher, because there's a lot of fog, they don't know precisely where the edge of the road is located, and its car has somewhat imprecise steering. And to make it all nerve wracking, they have some critics screaming at them to steer more to the left, while others scream that they should be over to the right. In truth, they aren't paid enough for all the abuse they must take.

Economic Commentary

The good news is the economy is performing well and it is functionally like a super tanker that can't be turned easily.

Hiring remains very solid and wages are rising at a moderate pace. So households enjoy rising income to spend which boosts retail sales and forces compares to hire yet more workers. This makes for a classic self-reinforcing, self-perpetuating business cycle. Corporate profits are setting new records every quarter, belying the claims of the perma-bears that the markets are on a sugar high. As David Lieberman noted in a recent Investment Commentary, excluding the 5 FAANG stocks, the S&P 500 was recently trading at a mere 13.3 times 2019 earnings, a rather low valuation. It's all likely to continue until some serious economic imbalances disrupt the expansion. No doubt, that will happen someday.

But good news is not news for the broadcast media.

Only bad news qualifies as news. And there are economic and political issues that need to be addressed or could otherwise distract our driver so we end up in that proverbial ditch. The dispute over trade probably belongs at the top of the list. Trump is unilaterally imposing tariffs on imports, most especially on Chinese products, which could trigger a broader trade war and hurt global economic growth. Trump can push his tariff initiative too far, especially if the Chinese retaliate further, and this could create bigger economic problems for both nations. But neither side wants a recession, and both sets of economic advisors are aware of the risks. So there's no reason to assume things must necessarily spiral out of control. Trump played the same game with Mexico and Canada and that dispute was resolved even with a newly elected leftist nationalist as President of Mexico.

The S&P 500 was recently trading at a mere 13.3 times 2019 earnings, a rather low valuation.

Other issues could also prove disruptive.

Italy now has a populist government that wants to throw off the yoke of European fiscal austerity to promote more economic growth to the dismay of the E.U. government in Brussels. If the market loses confidence in Italian policies, the debt markets could close to Italian borrowers, and that could result in a worse financial crisis than hit Greece. So the Italian government must also engage in its own balancing act. And the U.K. must figure out Brexit. Or maybe they won't. But I'm quite confident that if no agreement is reached and there is a "hard" Brexit, the U.K. will not sink into the Atlantic Ocean.

Our markets (and we) must live with this cacophony.

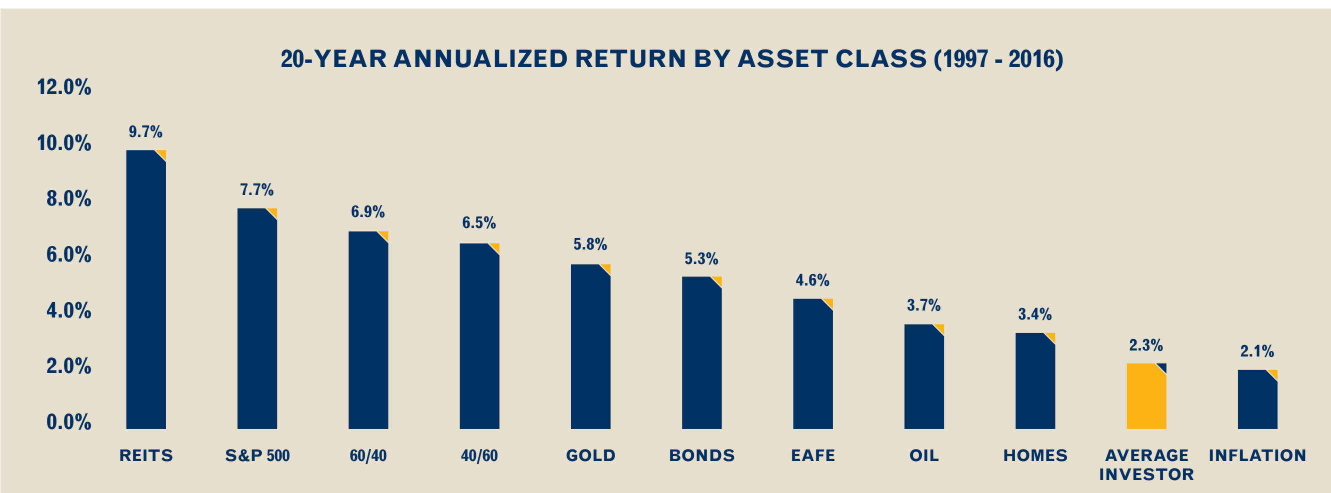
But as long as economic growth remains solid, interest rate increases stay moderate , and corporate profits keep rising, there is every reason to think stock prices will continue moving higher. While the market today is carrying an extra helping of fear, that fear is actually helpful in keeping everything on track. It is fear of the

Economic Commentary

unknown, not to mention memories of what happened in 2008, that has induced investors to pull more than one quarter of one trillion dollars out of stocks and stock mutual and ETF funds over the past decade, while pouring $8.2 trillion into bond and money market funds of all types. This a tragedy, since it is highly damaging to the long term financial health of the typical household. The stock market has fully recovered and more since the darkest days of 2008 and set new highs, but many investors haven't participated because they were frightened by the experience. This turns some investors into buyers when the market pulls back, as it did to start the fourth quarter, and that likely helps to keep the market from heading into a more pronounced decline at a time when corporate profit growth remains strong and the broader market remains relatively inexpensive, as now.

We continue our effort to educate our investors.

Stocks perform far better than bonds over the long run, albeit with vastly more volatility. Investors must choose the blend that meets their investment objectives at a volatility level they can tolerate. There is no one answer suitable for everyone. We are all different. And that's why we customize our investment holdings so we can construct a blend for each client. If your risk appetite changes or your investment needs change, we can modify that mix to adapt to your changing needs. The key is creating a good plan and sticking to it. We're here to help.



SOURCE: Dalbar Inc. Indexes used are as follows: REITS: NAREIT Equity REIT Index, EAFE: MSCI EAFE, Oil: WTI Index, Bonds: Barclays U.S. Aggregate Index, Homes: median sale price of existing single-family homes, Gold: USD/troy oz, Inflation: CPI. 60/40: A balanced portfolio with 60% invested in S&P 500 Index and 40% invested in high quality U.S. fixed income, represented by the Barclays U.S. Aggregate Index. The portfolio is rebalanced annually. Average asset allocation investor return is based on an analysis by Dalbar Inc., which utilizes the net of aggregate mutual fund sales, redemptions and exchanges each month as a measure of investor behavior. Returns are annualized (and total return where applicable) and represent the 20-year period ending 12/31/14 to match Dalbar's most recent analysis. – U.S. Data are as of March 31, 2016.

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ADVISORS CAPITAL MANAGEMENT

INVESTMENT PHILOSOPHY + STRATEGY

Founded in 1998, ACM views the markets with a two tiered process, utilizing a top-down view of the business cycle, coupled with a bottom-up, fundamental value based analysis.

Market Focus: Fixed Income

Since most investment grade issuances have a relatively high duration, interest rate movements are the primary driver of total return.

The Fixed Income market has become an increasingly popular topic of discussion as interest rates continue to rise.

Investors are finally starting to believe that the Fed's planned interest rate hikes will likely happen. Given the recent economic data and current economic outlook, we continue to believe interest rates are likely to remain on an upward trajectory for the foreseeable future.

Interest rates increased approximately 0.20% to 0.30% across all maturities along the Treasury curve in the third quarter.

This caused duration to continue to be a headwind for many fixed income benchmarks as rates continued to rise. Credit spreads, on the other hand, tightened across the credit spectrum, especially in high yield. Overall, third quarter performance in fixed income markets was inversely related to credit ratings: CCC-rated credit was the best performer and AAA-rated credit was the worst performer. Investment grade bonds enjoyed their first positive quarter of 2018 as credit spreads compressed—putting upward pressure on bond prices—and that offset the majority of the downward price effect of interest rate increases. Consequently, interest earned in the quarter more than compensated investors for the slight decline in bond prices. Investment grade spreads fell almost to their 10-year lows at quarter end, but spreads are still within approximately 0.2% of their 3- and 5-year averages. High yield spreads, by contrast, were only 0.05% off their 10-year lows and approximately 1.3% below the 3- and 5-year averages. High yield spreads are running out of room to tighten, and, unsurprisingly, spreads widened as the fourth quarter got underway.

Investment grade indices have struggled in 2018 with many indices down approximately 2.2-2.3% through the end of the third quarter.

Since most investment grade issuances have a relatively high duration, interest rate movements are the primary driver of total return. Given the relatively high quality of many investment grade issuers, the vast majority of yield in investment grade is dependent upon the market rate of interest, rather than credit spreads. To provide some context, approximately 70-90% of the yield on investment grade securities is driven by market interest rates, and only 10-30% of yield is driven by individual company credit quality. High yield returns, on the other hand, are approximately 45-60% based on market interest rates and approximately 40-55%, credit spreads.

Market Focus: Fixed Income

Additionally, investment grade companies typically issue longer-term debt with an average duration of 7.2 years while high yield debt has much shorter maturity of approximately 3.9 years. Therefore, investment grade's very high interest rate sensitivity and long duration explain the negative performance year-to-date of many investment grade indices.

Shorter dated Treasury yields rose a bit more than longer dated issuances during 3Q:

the difference between the 10-year and 2-year Treasury tightened to an extremely low 0.24%. The 10-year versus 2-year spread tightened by a full 1% since the beginning of 2017. To put this in context, note that the two year has risen 1.63% since the beginning of 2017, while the 10-year has risen 0.62% over the same period. The magnitude of the increases and the current level of the 2-year Treasury correspond reasonably well with the Fed's currently planned interest rate increases. The increase in the 10-year, however, still seems a bit too muted given the anticipated Fed rate increases over the next few years, the Fed's long-term Fed Funds rate estimate of 3%, and the currently projected economic trends. We expect long-term interest rates to rise more than the market is currently anticipating.

Interest rates have been moving higher since December 2015.

Going forward, we can expect further rate increases into 2020. According to its base-case scenario, the Fed is likely to increase the Federal Funds rate by an additional 0.25% in 4Q and another 0.75% in 2019. This would push the Fed Funds rate to 3.0%-3.25% by the end of 2019. The current economic fundamentals support such rate increases. GDP growth has been in the 2-3+% range for the past five quarters and is expected by the Fed to be greater than 3% in 2018 and 2.5% in 2019. Also, Core PCE inflation has picked up and has finally reached the Fed's 2.0% target after several years below 2.0%. Correspondingly, wage growth has been gaining momentum, nearing 3% in recent reports, as a very tight labor market pushed the unemployment rate down to 3.7%. The Fed expects to continue to see the unemployment rate decline thru 2019, which may very well accelerate wage-based inflation pressures.

Subsequent to the third quarter's end, we got a taste of the potential long-term interest rate increases should economic data remain as positive as we expect.

A strong employment report during the first week of October pushed the 10-year Treasury yield to a level not seen since 2011. While the 2- year Treasury roughly reflects the Fed's expected rate increase path, the 10-year has more room for increases, based on current and projections of economic fundamentals. Given this view, we continue to believe it is prudent to keep duration in fixed income relatively low.

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One size does not fit all.

Advisors Capital Management provides private accounts with security selection that is tailored to each client's personal objectives.

One size does not fit all. Our individually tailored portfolios are designed specifically for the client, using individual securities and thoughtfully managed in our all cap value style.

Advisors Capital
Management

Small/Mid Cap Update

U.S. small and mid-cap stocks gained +4.70% in the third quarter as measured by the Russell 2500 Index. The Small/Mid Cap strategy outperformed this comparative index with the average account returning +7.24%, net of all fees. Companies delivering faster earnings growth continue to outperform companies trading at lower multiples to earnings and book value The Russell 2500 Growth Index returned +7.17% versus +2.67% for the Value Index.

Two Index sectors achieved double-digit returns in the three months ending September. Information Technology (+10.57%), boosted by Software and Services, and Health Care (+10.33%) propelled by Health Care Equipment and Services led sector results. The portfolio participated in these areas. In Information Technology, new holding, Paycom Software, positively impacted performance. This payroll system-as-a-service provider continues to impressively grow revenues and earnings as the company takes market share from the traditional HR software system providers. Index sector Consumer Staples pulled back in the period which favored more cyclical-type companies. However, we achieved a positive return in this segment through the advance of Casey's General Stores. The Midwest convenience store operator has lagged. Earnings over the last two years have generally failed to meet expectations. This reflected the impact from weaker farm economies and lack of tangible benefits from an aggressive expansion plan. Investors delighted in the recent earnings report, however, with both margins and sales in the key grocery/prepared food areas exceeding projections. Strong performances were also registered by long-time holding John Bean Technologies and new position Ollie's Bargain Outlet Holdings. John Bean reported record orders in both of its divisions, FoodTech and AeroTech. The company confirmed continued double-digit revenue and earnings growth for 2018. Ollie's "extreme value" mantra resonates with customers and membership (Ollie's Army) continues to grow. The company posted impressive growth in the latest earnings report.

Key trades during the quarter included sales of Interpublic Group (IPG) and Ritchie Bros Auctioneers (RBA). IPG faces industry pressures as clients question the effectiveness of online media spend, and

Small/Mid Cap Update

geopolitical turmoil makes traditional purchasers more reticent to increase ad budgets. RBA is a good company with solid management and has been successful consolidating a fragmented auctioning industry, but margins have faded with the purchase of online auction company IronPlanet and we question the company's growth opportunity in this part of the economic cycle. Buys included Paycom Software (PAYC), Ollie's Bargain Outlet Holdings (OLLI), mentioned above, and RBC Bearings (ROLL). ROLL excels in providing high-end precision bearings/products to the aerospace, defense, and industrial markets. Clients trust the company's product dependability and appreciate.

In terms of outlook we note U.S. equities, in general, and smaller cap companies, in particular, have been very strong performers over the last five years.

In terms of outlook we note U.S. equities, in general, and smaller cap companies, in particular, have been very strong performers over the last five years. While knowing future returns cannot continue at that pace, we highlight the quality and strong businesses of the Small/Mid Cap holdings. The Portfolio's average company generates 16.61% return on invested capital over the last 12 months compared to 5.49% for the average company in the Russell 2500. Our companies, on average, have less than 50% of the debt load, and reflect premium free cash generation growth compared to the comparative index, yet valuation is comparable. We think these metrics should prove beneficial as we enter a later stage of the economic cycle.

Growth Review

For most of this year, growth and momentum stocks have been outperforming value investments, and, as value managers, our Growth strategy has underperformed. While we never like to lag the market, the secular drivers that motivated our selection of stocks remain in place and we have been topping up positions to take advantage of sell-offs where cash allows. We followed this strategy with companies that were negative in 2017 (Quorvo and Ciena) and both stocks have delivered double-digit returns since. We expect several headwinds to abate in coming quarters and anticipate that this and our averaging down will enable Growth to outperform under a number of scenarios.

The largest headwind for several Growth stocks has been the lengthy turmoil over U.S. trade policy. While the administration is right to try to push China to change policies forcing U.S. companies to share critical intellectual property, the resulting tariffs (on both sides) have reduced near-term outlooks for profits for several of the companies in the strategy. We continue to maintain these positions because the structural drivers remain solid and trade policy is a cloud which eventually will lift. Some of these companies are supplying key components or services to industries that are becoming larger parts of the global economy and our selections include companies with a growing role in that expansion (AVGO, BIDU, CIEN, JD, MTSI, and QRVO). Some of the multi-year drivers involve the expansion of data network infrastructure essential to the growing use of the internet, while others are leveraged to the more sophisticated electronic systems powering conventional, hybrid, and electric cars and trucks (BWA, NXPI). There are long runways of growth ahead for these companies.

We are also seeing a controversial cyclical pullback in semiconductor and semiconductor capital equipment suppliers. In decades past, the semi cycle was tied closely to Intel's release of new chips for PCs and servers since those systems drove the majority of all chip demand. This is not so today because of the much greater diversity of chip end markets, yet many have based this quarter's outlook on those past trends. The secular growth drivers for semis remain firmly in place as data centers continue to expand, cars rely more on advanced electronics, and the world readies the move

Growth Review

to 5G cellular technology. Nevertheless, the majority is assuming cyclical factors will outweigh secular (growth) factors—at least for this quarter and maybe next. The timing of the eventual shift in perceptions back to the dominance of secular drivers remains difficult to assess—it could happen with this quarter's earnings reports, or it may take another quarter or two. Because this shift can happen at any time, we have been topping up select semi positions so as to position portfolios to benefit as much as possible when the turn occurs.

Consumer Discretionary delivered mixed results with trade policy fears pulling down BWA, PII and JD, while economic strength boosted TJX and WSM. We had identified TJX as a company with the potential to outgrow its peers and to provide buoyancy in case of a market pullback; performance here has been solid.

Our Industrial allocations (led by XPO, LLL, AAL, and RTN) outperformed during the quarter as defense and transportation company shares rebounded sharply. We continue to see defense companies serving two purposes in the portfolio: they offer the potential for secular appreciation since global defense spending is on the rise and offer some cyclical protection against geopolitical turmoil. We also saw strong recovery in Materials as our two packaging companies moved higher (BLL and BERY).

While the S&P 500 was trading at 16.8 times forward earnings, our blended price-to-earnings ratio in Growth, trading at 14.5x

Overall, U.S. and global economic fundamentals remain supportive of our specific investments in the Growth strategy. While the S&P 500 was trading at 16.8 times forward earnings, our blended price-to-earnings ratio in Growth, trading at 14.5x, remained well below the market's multiple as we focus exposure on growth opportunities at a reasonable price. We anticipate that trade policy will remain in turmoil for some time to come, but expect that deeper, secular drivers will allow our selections to deliver above-segment earnings growth—the key driver of valuations—for several years to come.

Core Dividend Update

The Private Core Dividend Composite rose 4.95% in the third quarter, though it underperformed its benchmark as lagging performance in Information Technology and Industrials outweighed superior returns in Communication Services, Financials and Consumer Staples. While the economic fundamentals remain solid, several headwinds are holding back valuations across multiple sectors. In addition to some investors taking risk off the table, we are seeing uncertainty surrounding trade policy, interest rates, and the U.S. housing expansion adversely impact investor perceptions. Even in the face of these risks, earnings growth remains well above historical averages as the global economy enjoys growth of 3.7% and as several industries remain in the midst of multiyear expansions.

Consumer Staples was once again led higher by Chef's Warehouse, which climbed nearly 30% in 3Q and was recently sold near its all-time high. The solid economic outlook around the globe helped the cruise line companies, Royal Caribbean (RCL) and Norwegian (NCLH), which both climbed over 20% in the quarter. The Health Care sector was the leading contributor in Core, led by double-digit returns in Express Scripts (ESRX), Thermo Fisher (TMO), Anthem (ANTM), and Cardinal Health (CAH). Our selections in the S&P 500's new Communications Services sector helped Core outperform as Disney (DIS), Alphabet's Google (GOOG), and Cinemark (CMK). And while our Industrial segment underperformed, our recent additions to defense industry stocks (LMT and NOC) helped offset declines in home builder suppliers.

Supplies used for home construction and renovation did poorly during 3Q, and both Owens Corning (OC) and Top Build (BLD) were two of the worst four performers for the quarter in Private Core. While there are fears about the impact of higher rates on home builders and home goods, the inventory of homes on the market remains very low at only 4.3 months of supply available nationally. More homes must be built to absorb population growth, and with existing home supply so low, new supply must be made available to accommodate the demand. Interest rates, wage inflation, and tariffs may drive the cost of building higher, but until this demand is met home prices will continue to appreciate. This will eventually motivate builders to produce the supply needed. The reality is better than the stock price movements would suggest:

Core Dividend Update

single-family housing starts were up nearly 13% in August 2018 versus 2017. And although that growth slowed in September, the number of new houses being built remains near post-recession highs. In addition, people are spending on their current homes, and are likely to continue to do so even as new home building slows, and this has helped another Core holding, Lowe's (LOW), to perform well (up over 20% in 3Q). We took advantage of this weakness among home builder suppliers to add to our positions in BLD, MAS and OC.

Performance was also adversely affected by trade policy concerns in the auto industry. General Motors (GM) hasn't performed well, but is becoming an historically cheap stock. Its unfunded pension obligations continue to improve rapidly, something which will free up a lot of cash flow within another year or two. This would allow GM to increase its dividend, buy back shares, or invest in additional growth. The company has significant losses coming from its self-driving vehicle segment, known as "Cruise," which are hurting current earnings but should eventually become a major contributor to earnings. Its "Cruise" segment has grown to become the number two competitor to Google's self-driving endeavors and the investment by Softbank shows how far it has come. The Cruise operation alone was recently valued at $11 billion after an investment by Softbank. This investment values "Cruise" at over 20% of the entire market cap of GM. Tariffs may go either way at this point, and it remains to be seen how policy discussions will play out, but China is not ready to replace foreign automobiles with domestic brands because the domestic brands don't have the reputation of those abroad. Finally, the stock remains among the cheapest in the entire S&P 500 even though the company produces very high cash flow. It is worth being patient and collecting a dividend of nearly 5% while we wait for even more cash flow to be unlocked.

> Even in the face of these risks, earnings growth remains well above historical averages as the global economy enjoys growth of 3.7%.

Income with Growth Update

The Income with Growth composites delivered healthy returns last quarter. We are continuing to source income generation for clients from a diversified selection of equities—with larger shares from energy, financials, and REITs—and from a narrow set of bonds and preferred stock. Gross yields for the strategies remain north of 6%.

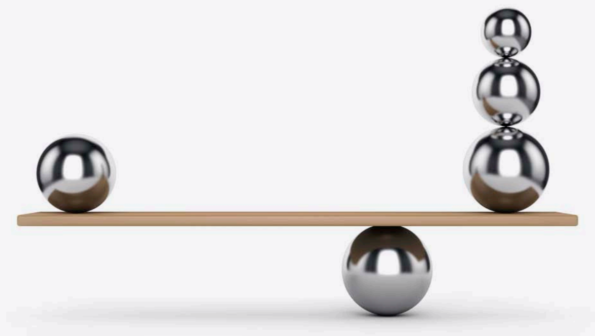
Leading the gains for the quarter was the energy sector where a transformation from Master Limited Partnerships to C-Corporations remains underway. This transformation improves the abilities of these companies to finance future capacity expansion and this is likely to alleviate a chief concern among potential investors. This has also broadened ownership and lifted the stocks. Underlying demand for new pipelines remains strong in the U.S. where limited take-away capacity continues to constrain the ability of exploration and development companies (as well as the integrated suppliers) to bring more oil and gas to market. A multi-year pipeline buildout—and now with more secure financing—is likely to remain a key driver of value in this sector. We expect the positive relative performance to continue.

Business development companies and commercial mortgage REITs also delivered solid results in Q3 as rising interest rates boosted both groups. We see far greater risk in residential REITs—because of the longer-term nature of the underlying mortgages and risks of early repayment—and continue to avoid those stocks. Information Technology also helped as Qualcomm and Cisco delivered double-digit returns. During the quarter, we allocated additional funds into big pharma, specifically focusing on companies with the ability to generate long-term growth through biotech investments. We expect this to play out nicely over time.

The Fed raised rates again, as expected, and bond prices fell sharply as market rates moved higher. As corporations look at their balance sheets in light of fed movements, we sold some preferred stock in anticipation of the issues being called early. Funds were redeployed into other fixed income investments, but still with a very defensive orientation.

Balanced Update

Value investing remains the key driver of our investment selections in our Balanced strategies, and our selections are trading well below the market - at 14.1 times 12-month forward earnings, as compared to the S&P 500 multiple of 16.8 (as of the end of 3Q). We are seeing a few headwinds holding back near-term performance while leaving longer term drivers very much in place. Among these headwinds are ongoing trade tensions between the U.S. and China (and to a lesser extent, Europe), concerns regarding a possible slowdown in the U.S. housing market, fears concerning the broader consequences of rising interest rates, and controversy over cyclical versus secular dynamics in the technology sector.



Health Care and Information Technology were the largest contributors to equity returns last quarter. We saw 15% or greater increases from a variety of companies in the space. Info Tech was led higher by the large cap blue chips but also faced headwinds from concerns over a possible negative semiconductor cycle which caused LRCX and MCHP to trade lower after double-digit gains in 2017. We continue to see secular drivers in place—ultimately stronger than cyclical headwinds—and have topped up some positions in this group. LRCX reported its September quarter results recently and confirmed that September marked a trough, guided December sequentially higher, and helped dispel those cyclical concerns for the group.

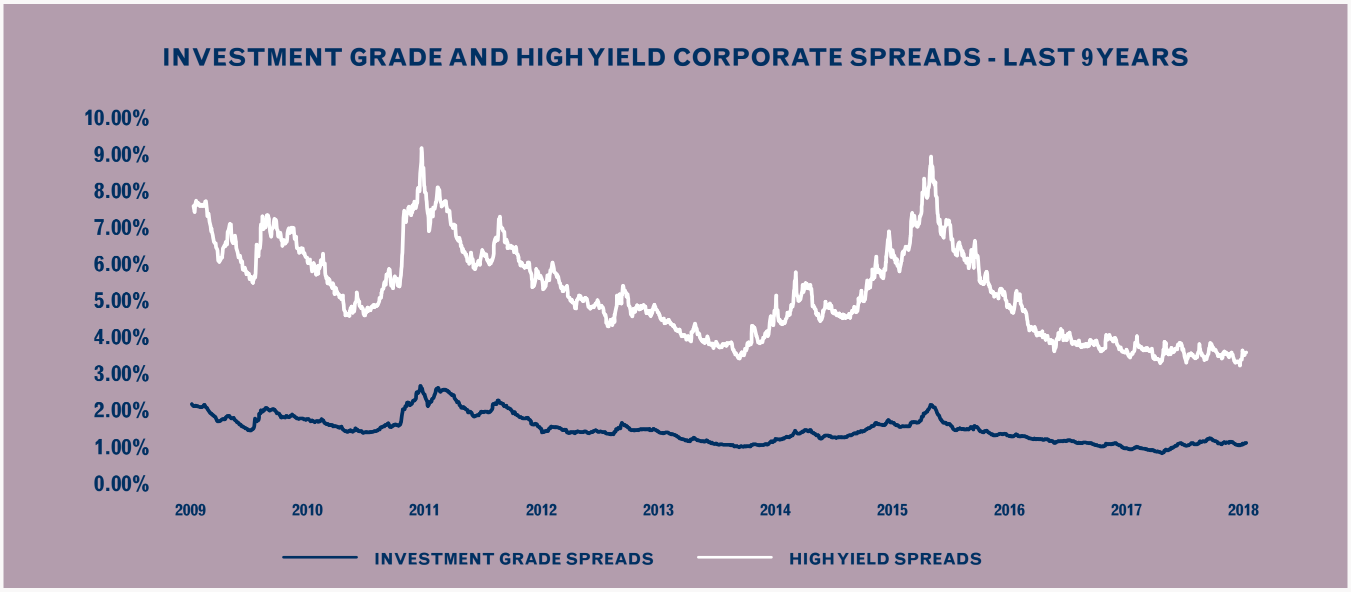
We also saw recovery in all the other sectors except Materials, where higher oil prices raised costs and undermined profits in the two chemical companies in portfolios. Each company (DWDP and LYB) is making changes to accommodate those cost headwinds and face strong end market growth drivers. Consumer Discretionary delivered mixed results, but ended higher overall. Our more defensive positions, TJX and DNKN, rose by double-digit percentages in the quarter, as did housing market stocks—LOW and WSM—but autos continue to suffer trade war woes and Macao gambling troubles undermined Las Vegas Sands.

On the fixed income side, our selections remain especially low in duration as rising market interest rates threaten to reduce principle values of longer-dated bonds. During the third quarter, our strategy produced the desired results as coupon payments on bond and preferred holdings more than offset the minor principle decline we saw in the fixed income holdings for the Balanced strategies.

Fixed Income Update

Fixed Income portfolio performance was strong in the third quarter as the Composite delivered a total return of 0.95% versus the benchmark, the Barclays Aggregate Bond Index, which was up only 0.02%. The Composite's strong results were driven by the continued resilient performance of shorter dated fixed rate securities as well as the inclusion of a healthy mix of floating rate securities. Floating rate securities benefit the portfolio because coupons reset at higher rates every quarter as rates rise. This quarter, investor demand for such securities remained very strong and provided additional total return as floating rate bonds appreciated. More and more fixed income investors are realizing that duration doesn't pay and consequently have tried to lower the duration of their portfolios, driving up the demand for floaters.

Interest rates increased approximately 0.20% to 0.30% across all maturities along the Treasury curve. This caused duration to continue to be a headwind for many fixed income benchmarks as rates continued to rise. Credit spreads, on the other hand, tightened across the credit spectrum, especially in high yield. Overall, third quarter performance in fixed income markets was



SOURCE: ICE Benchmark Administration Limited (IBA), Federal Reserve Economic Data, myf.red/g/ll3d

Fixed Income Update

inversely related to credit ratings: CCC-rated credit was the best performer and AAA-rated credit was the worst performer. Investment grade bonds enjoyed their first positive quarter of 2018 as credit spreads compressed—putting upward pressure on bond prices—and that offset the majority of the downward price effect of interest rate increases. Consequently, interest earned in the quarter more than compensated investors for the slight decline in bond prices. Investment grade spreads fell almost to their 10-year lows at quarter end, but spreads are still within approximately 0.2% of their 3- and 5-year averages. High yield spreads, by contrast, were only 0.05% off their 10-year lows and approximately 1.3% below the 3- and 5-year averages. High yield spreads are running out of room to tighten, and, unsurprisingly, spreads widened as the fourth quarter got underway.

We remain focused on keeping duration low and credit quality relatively high while maintaining a healthy exposure to floating rate notes.

The Barclays Aggregate Bond Index, with its high duration, underperformed significantly as a result of the 0.20% increase in the 10-year Treasury rate in 3Q. For the year through 3Q, the Index is now down 1.6% as the duration effect on bond prices continues to more than offset higher interest payments. We expect this trend to continue since GDP growth has been strong—in the 2-3+% range for the past five quarters—and is expected by the Fed to be greater than 3% in 2018 and 2.5% in 2019. Also, Core PCE inflation has picked up and has finally reached the Fed's 2.0% target after several years below 2.0%. Correspondingly, wage growth has been gaining momentum, nearing 3% in recent reports, as a very tight labor market pushed the unemployment rate down to 3.7%. The Fed expects to continue to see the unemployment rate decline thru 2019, which may very well accelerate wage-based inflation pressures.

We remain focused on keeping duration low and credit quality relatively high while maintaining a healthy exposure to floating rate notes. The recent increase in interest rates has not only increased the yield on your current portfolio, but has also allowed us to reinvest proceeds from redemptions at even higher rates. Maintaining a relatively high quality credit mix will also allow us to reposition the portfolio if and when credit spreads widen out to more attractive levels. Overall, we remain optimistic about the near- and long-term outlook and potential opportunities in fixed income.

Global Growth Update

Global equities registered a positive return in the third quarter 2018 and the strategy significantly outperformed. Leading sectors in the MSCI index included Health Care (+11.46%), Information Technology (+10.50%), and Industrials (+6.66%). These three were the only sectors out of eleven that returned above the benchmark average. Three sectors finished the quarter with small negative returns – Communication Services (-0.65%), Materials (0.33%), and Real Estate (-0.28%). The Global Growth Portfolio managed positive returns in these sectors as well. HFF, a Dallas-based, commercial real estate broker contributed positively to our real estate allocation. The stock bounced back from a weak second quarter when investors expressed concerned about lighter volumes which turned out to be an issues of new business bookings being deferred versus a reflection of business fundamentals. In Communications Services, the Philippines-based Globe Telecom, jumped on strong earnings and less investor concern about a third mobile service entrant into the Philippines. The company may also change their business model to less capital intensity by selling and renting access to cell towers. The position in Givaudan, the Switzerland-based flavor and fragrance provider achieved a new all-time high at quarter end. The company benefits from the health and wellness trend helping its clients deliver healthier and yet tasty products.

Stocks providing the most positive impact to the portfolio included John Bean Technologies (JBT) and Veeva Systems (VEEV). John Bean reported record orders in both of its divisions, FoodTech and AeroTech. The company confirmed continued double-digit revenue and earnings growth for 2018. VEEV is a software system provider for Health Care and Consumer Products companies. VEEV's relatively new business model helps pharmaceutical companies better manage their drug pipeline through clinical trials and regulatory approval. Business has been better than management expected, and earnings guidance was again increased for the year.

Key sells during the quarter included Ambev (ABEV), Samsonite (SMSEY), Ritchie Bros Auctioneers (RBA), Interpublic Group (IPG), and WPP. RBA is a good company with solid management and has been successful consolidating a fragmented auctioning industry, but margins have faded with the purchase of online auction company IronPlanet and we question the company's growth opportunity in this part of the economic cycle. Media companies, Interpublic Group and WPP, face industry pressures as clients question the effectiveness of online media spend, and geopolitical turmoil makes traditional purchasers more reticent to increase ad budgets. WPP also suffered from management intrigue with a new CEO.

Key buys for the three-month period included Paycom Software (PAYC), Ollie's Bargain Outlet Holdings (OLLI), and RBC Bearings (ROLL). Drilling down, ROLL excels in providing high-end precision bearings/products to the aerospace, defense, and industrial markets. Clients trust the company's product dependability and appreciate ROLL's innovation and ability to deliver complex designs. Although operating in cyclical industries, Roll should benefit from several secular tailwinds including universal air travel growth and rising geopolitical tensions influencing defense budget spend.

Global Dividend Update

Global equities registered a positive return in the third quarter 2018. The MSCI All Country World Index Net advanced +4.28%. The Global Dividend Portfolio bettered the index result with the average account gaining +6.03%, net of all fees.

Leading sectors in the MSCI index included Health Care (+11.46%), Information Technology (+10.50%), and Industrials (+6.66%). These three were the only sectors out of eleven returning above the benchmark average. Three sectors finished the quarter with small negative returns – Communication Services (-0.65%), Materials (0.33%), and Real Estate (-0.28%). The Global Dividend Portfolio managed positive returns in these sectors. HFF, a Dallas-based, commercial real estate broker contributed positively to the portfolio's real estate segment. The stock bounced back from a weak second quarter when investors expressed concerned about lighter volumes which turned out to be a timing issue with new business bookings being deferred versus a reflection of business fundamentals. In Communications Services, the Philippines-based Globe Telecom, jumped on strong earnings and less investor concern about a third mobile service entrant into the Philippines. The company may also change their business model to less capital intensity by selling and renting access to cell towers. The portfolio's position in Givaudan, the Switzerland-based flavor and fragrance provider achieved a new all-time high at quarter end. The company benefits from the health and wellness trend helping its clients deliver healthier yet still-tasty products.

Lagging stocks during the quarter included Virtu. The U.S. market maker tends to do best in times of higher volatility, not lower volatility as seen in Q3. Japan-based, Zenkoku Hosho (ZNKKY), fell as investors fear the early year slowing of new mortgage guarantees. Due to the company's commanding position in the industry and the changing regulatory environment inducing banks to reduce their guarantee business we look for ZNKKY to continue to generate profitable growth. Best performing stocks included Grupo Aeroportuario del Centro Norte (OMAB) and Marine Harvest (MHGVY).

International ADR Update

International equities registered a positive return in the third quarter 2018. The quarter started off on a positive note with the MSCI Index up in July as generally positive economic data provided a short respite from trade war concerns. Foreign equities struggled the remainder of the quarter, however, losing most of the July gain in August before finishing with a mild gain in September. Foreign equities were influenced by generally weakening foreign currencies. Italian budget woes pressured the euro, more Brexit intrigue pounded the pound, and the yen lost ground on global trade fears. Further, a currency crisis in Turkey, Argentina, and South Africa set off a wave of investors selling emerging market assets and currencies to seek safe haven in the U.S. dollar. This hurt foreign equities, in general, and emerging market equities, in particular. Of note, equities trading at lower multiples to earnings and book value (Value Stocks) outperformed those companies delivering faster earnings growth (Growth Stocks) over the three-month period. Value had lagged Growth for six consecutive quarters through June 2018, accumulating to 1244 basis points before Value's Q3 outperformance of 205 basis points. This along with the resurgence of higher dividend yield helps explain your Portfolio's outperformance during the period.

In the benchmark, Energy, continuing the momentum from Q2, registered the strongest sector return, followed by Health Care and Information Technology. Interestingly, this was the identical trifecta from the second quarter. Lagging sectors included Consumer Discretionary, Communication Services and Real Estate. Angst towards China with the growing trade friction negatively impacted two holdings. Singapore-based China Yuchai, a leading truck engine manufacturer in China, and China Gas Holdings, a leading natural gas distributor in China, registered the weakest returns for Q3, but we believe the fundamentals remain sound for both companies. Grupo Aeroportuario del Centro Norte (OMAB) provided the biggest positive impact on the portfolio. The central Mexico airport operator stock price gained on news of the new United States-Mexico-Canada trade agreement, popularly known as NAFTA 2.0. Farmed salmon producer, Marine Harvest, also contributed to the portfolio results. Salmon prices remain strong, boosted by growing global demand, but limited supply.

Trading during the quarter included the sale of Ambev (ABEV) and Samsonite (SMSEY). Ambev, the Brazilian beer company, has seen deteriorating margins over the last several quarters, which will likely continue with Brazil real weakness. We note the difficult growth challenge with the company's parent, Anheuser Busch Inbev, likely limiting the ABEV's ability to expand outside Brazil. Also, very high market share limits ABEV's expansion within Brazil. Samsonite has seemingly delivered broad-based growth, but balance sheet analysis causes us concern as working capital and inventory marches continually higher, setting the company up for potentially sharp losses should growth slow. Although reviewing several names, we did not add a new position in the portfolio in the quarter. Thus, the cash position is elevated at the moment while we patiently wait for a better buying opportunity.

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