QUARTERLY 2Q17

TACTICAL ASSET ALLOCATION

- Indicators point to growth, but we expect the pace of improvement to slow
- Markets already pricing in the bulk of the "reflation trade's" bullish implications
- Low starting yields and elevated equity valuations weigh on return forecast
- Our "barometer" continues to suggest positive growth trends

The "reflation trade" that drove financial market behavior since the middle of last year lifted stocks and weighed on bond prices. This leaves us with an economy performing better and stock indices near records. Lower bond yields and higher equity valuations help lift short-term growth but also dampen our long-run return forecasts. In the months ahead, we expect to see the pace of improvement moderate compared to what we experienced over the past nine months.

Equity allocations in portfolios were increased last summer, and we continue to maintain a modest tactical tilt toward large capitalization domestic stocks over bonds and foreign equities.

Economy

The United States' economy settled into a 1.5 - 3.5% growth pattern in the years following the "Great Recession." Last year's growth of 1.6% fell right near the bottom end of that range. To focus on the full year misses an important aspect of the story because 2016 was a year of change. While the first half of the year was stagnant, the second half saw a marked improvement.

Global growth stabilized last summer, causing deflationary pressures to fade and confidence to strengthen. An upturn in business profits and a pickup in investment accompanied improving investor risk appetite throughout the second half of 2016. Our base case projection sees investment growing faster after the recent years' period of under-investment.

As stated in our *Viewpoint 2017*, we expect some modest upside to growth this year. We estimate growth in the United States will be near 2.8% this year with 3% global growth (see chart on page 3). Improved confidence, some tax relief, and fading global headwinds provide some lift to the outlook. Potential risks include elevated political risk, uncertainty around trade and immigration, and possible missteps by central banks attempting to unwind ultra-accommodative policy tools.

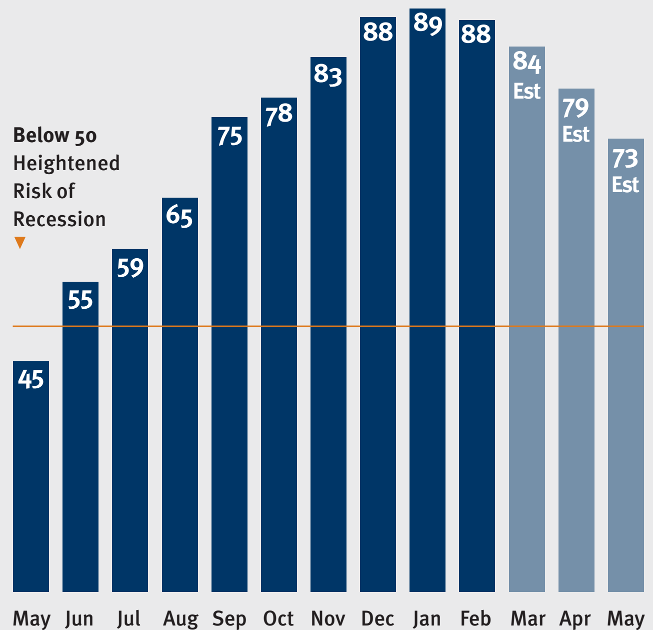
For now, most indicators seem to point toward improving economic conditions. Our WCA Fundamental Conditions Barometer (right) supports this observation. Should conditions remain supportive, we should expect stronger investment, productivity, and growth. We feel stocks would tend to outperform bonds in such an environment.

Equities

Stocks rose through the first quarter with the Dow Jones Industrial Average crossing above 20,000 for the first time in history. The Standard & Poors' 500 Index also set new records.

According to FactSet Research, the earnings outlook is beginning to brighten. Between mid-2015 and mid-2016, weakness in the global economy clouded the profit outlook, but analysts are once again expecting growth. For the first quarter and full year 2017, S&P 500 earnings are projected to rise roughly 9%. The energy sector accounts for much of the profit improvement. Energy sector earnings are forecast to swing to a $7.7 billion first-quarter gain from a $1.5 billion loss a year ago. Excluding energy, S&P 500 estimated profit growth slows to 5.2%.

WCA FUNDAMENTAL CONDITIONS BAROMETER



We regularly assess changes in fundamental conditions to help guide near-term asset allocation decisions. Analysis incorporates approximately 30 forward-looking indicators in categories ranging from Credit and Capital Markets to U.S. Economic Conditions and Foreign Conditions. From each category of data, we create three diffusion-style sub-indices that measure the trends in the underlying data. Sustained improvement that is spread across a wide variety of observations will produce index readings above 50 (potentially favoring stocks), while readings below 50 would indicate potential deterioration (potentially favoring bonds). The WCA Fundamental Conditions Index combines the three underlying categories into a single summary measure. This measure can be thought of as a "barometer" for changes in fundamental conditions.

At 17.5 times forecast earnings of $134.50, the multiple paid to own stocks is higher than the 10-year average multiple of 14 times. Unattractive available yields on cash and bonds partly explain why investors may be willing to pay higher prices to own equities. Looking ahead, we expect somewhat lower equity returns to account for today's elevated equity valuations.

Cash returns from equities contribute to investment performance. Dividends and stock repurchases are the most common ways companies return cash to investors. For the S&P 500, we expect to see dividends near $425 billion and net buybacks of $550 billion this year. These estimates translate into a current dividend yield near 2% and a "buyback yield" near 2.8% for a total "cash yield" of 4.8% for the S&P 500. We continue to expect long-run returns from equities to fall short of historic returns. Still, equities should provide higher returns than Treasury bonds or cash in our view.

Fixed Income

The case for higher rates continues to strengthen. We are at full employment with inflation measures in the area of 2%. The economy is close to potential output. Tax cuts and infrastructure spending remain part of the President's economic agenda. Real interest rates are still negative, and the Federal Reserve's balance sheet remains near $4.5 trillion. Inflation priced into the TIPS market rose to 2% as the year-over-year change in the consumer price index increased to 2.7%.

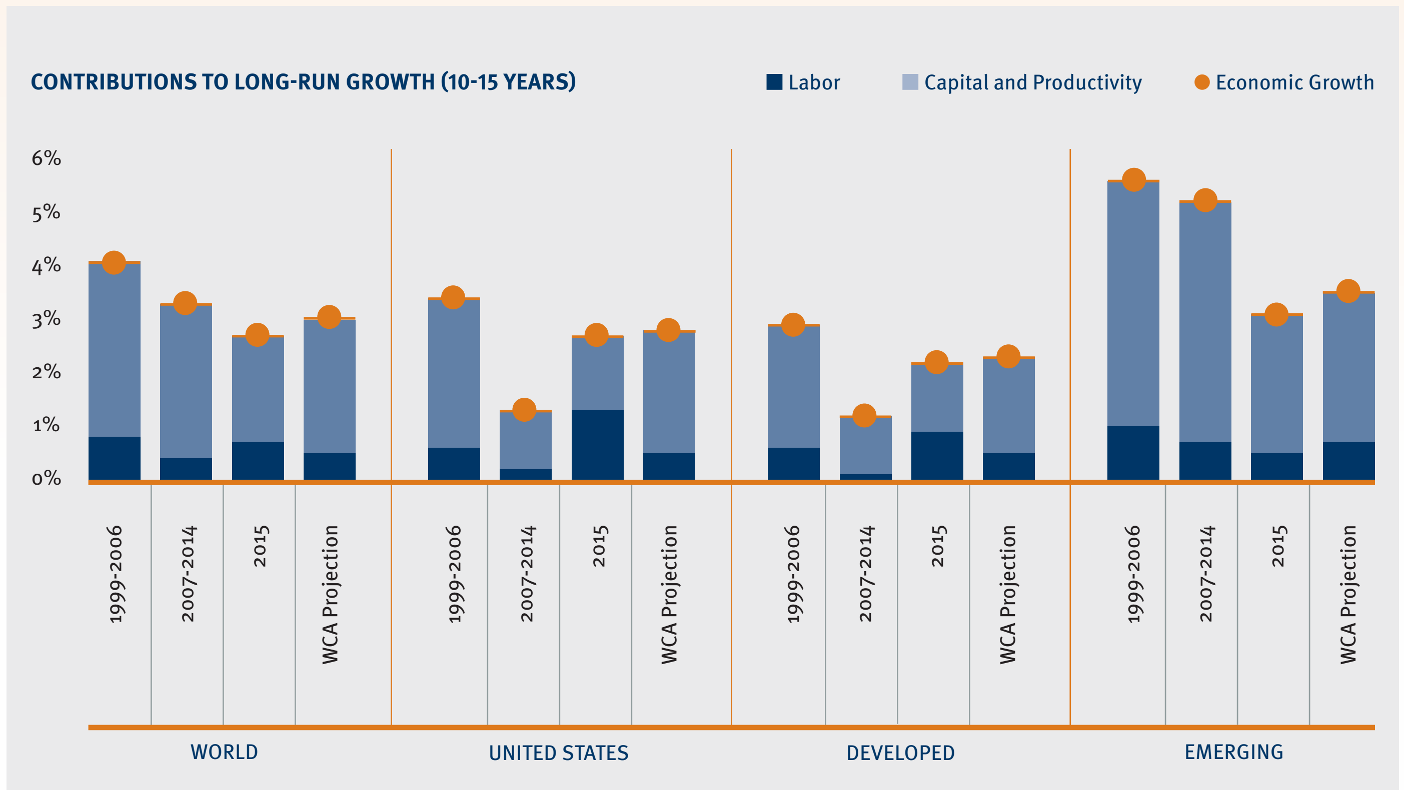
Given these factors, it makes sense for the Fed to get ahead of shifting market expectations. If expectations for growth and inflation ratchet higher, then the Fed could end up chasing interest rates rather than leading them. This would damage the central bank's credibility and dampen the effectiveness of future policy actions. It is important, therefore, for the Fed to avoid being perceived as complacent on rates.

By continuing to raise the short-term rate as they did at their March meeting, the central bank lessens perception they are "behind the curve." Higher short-rates also helps restore some "dry powder" to the Fed's arsenal of crisis-fighting tools. In the event of an unexpected crisis or recession, the Fed will be better able to respond if policy rates are higher than they are today. Higher short-term rates would also provide some much-needed relief to yield-starved savers.

Looking further afield in fixed income markets, little has changed since our January report. The yield curve flattened somewhat, and corporate spreads remained steady.

Summary

The economy is performing much better compared to a year ago. A turnaround that began last summer lifted equity valuations and led the Fed to resume rate increases. Our WCA Fundamental Conditions Barometer remains above 50, indicating a lessened likelihood of a recession in the near term (see chart). Our forecast remains positive given the recent trends, but we do envision some moderation in the months ahead. We will continue to watch changing conditions and make tactical adjustments as warranted.

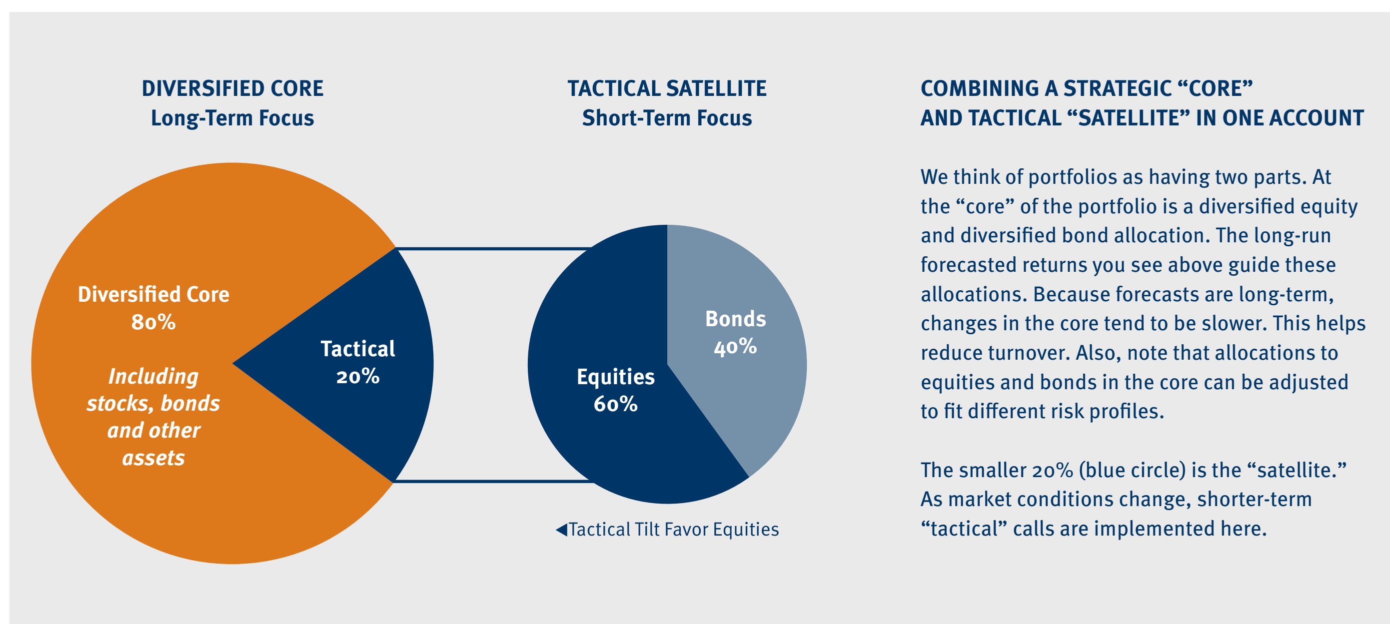


Source: Conference Board, WCA.

ASSET CLASS	10-15 YR VIEW RETURN	VOLATILITY	UNDERWEIGHT	NEUTRAL	OVERWEIGHT
BONDS					
Core Bonds	2.8%	4.4%	■ Tactical		
1-3 Year Treasury Bond	2.0%	1.0%		■ Core	
Mortgage-Backed Securities	2.3%	2.5%		■ Core	
Intermediate Government/Credit	2.3%	2.4%		■ Core	
20+ Year Treasury Bond	2.3%	11.4%	■ Core		
Investment-Grade Corporate Bonds	2.9%	5.2%			■ Core
High-Yield Corporate Bonds	3.2%	8.6%			■ Core
EQUITY					
Domestic Equity	6.0%	15.5%			■ Tactical
Domestic Large Cap Value	5.5%	15.7%		■ Core	
Domestic Large Cap Growth	4.9%	14.3%		■ Core	
Foreign Developed Equity Markets	6.3%	17.4%			■ Core
Foreign Emerging Equity Markets	6.2%	20.4%	■ Core		
Gold	3.5%	15.7%	■ Core		
REITs	4.9%	22.3%		■ Core	

As of January 18, 2017. Past performance does not guarantee future results.

■ Core ■ Tactical



COMBINING A STRATEGIC "CORE" AND TACTICAL "SATELLITE" IN ONE ACCOUNT

We think of portfolios as having two parts. At the "core" of the portfolio is a diversified equity and diversified bond allocation. The long-run forecasted returns you see above guide these allocations. Because forecasts are long-term, changes in the core tend to be slower. This helps reduce turnover. Also, note that allocations to equities and bonds in the core can be adjusted to fit different risk profiles.

The smaller 20% (blue circle) is the "satellite." As market conditions change, shorter-term "tactical" calls are implemented here.

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Washington Crossing Advisors, LLC (“WCA”) is an SEC registered investment advisor and wholly owned subsidiary of Stifel Financial Corp. WCA helps supervise and manage over $1 billion in assets under advisement for individuals and institutions.

The team is managed by Kevin R. Caron and Chad A. Morganlander, who were among the first founding members of Washington Crossing Advisors.

Washington Crossing Advisors’ views on investing and markets are regularly sought by national media outlets, including *CNBC*, *Bloomberg*, *Fox Business News*, *The Wall Street Journal*, *Forbes*, and *Reuters*.

Philosophy and Process

We believe that investments should be selected only after clear and quantified measures of value, risk, and potential reward have been made. Our investment approach combines top-down analysis of the macroeconomy with fundamentally rooted, bottom-up security analysis.

Description of Indices and Terms/ Disclosures

Description of Indices and Terms: All performance calculations of indices are calculated on a total return basis (reflecting reinvestment of dividends and other earnings). Indices are unmanaged, are not available for direct investment, and have no associated management fees.

Barclays Aggregate Bond Index: A composite of the Barclays Gov't/Corp Index, Mortgage-Backed Securities Index, and Asset-Backed Securities Index, including securities that are investment grade or better, have at least one year to maturity, and have an outstanding par value of at least $100 million.

S&P 500 Index: Capitalization-weighted composite of 500 stocks traded on the NYSE, AMEX, and NASDAQ; not the largest 500 stocks in U.S., but rather a blend of leading companies in leading industries in the U.S. economy; index comprised of 10 broad industrial sectors.

Dow Jones U.S. Select REIT: The Dow Jones U.S. Select REIT Index intends to measure the performance of publicly traded REITs and REIT-like securities. The index is a subset of the Dow Jones U.S. Select Real Estate Securities Index (RESI), which represents equity real estate investment trusts (REITs) and real estate operating companies (REOCs) traded in the U.S.

The ICE U.S. Treasury 1-3 Year Bond Index is a market value weighted index designed to measure the performance of U.S. dollar-denominated, fixed rate U.S. Treasury securities with minimum term to maturity greater than one year and less than or equal to three years.

Markit iBoxx USD Liquid High Yield Index consists of liquid USD high yield bonds, selected to provide a balanced representation of the broad USD high yield corporate bond universe.

The FTSE Developed All Cap ex U.S. Index is part of a range of indices designed to benchmark international investments. The index comprises large, mid and small cap stocks from developed markets excluding the U.S.

The FTSE Emerging Markets All Cap China A Inclusion Index is a market-capitalization weighted index representing the performance of large, mid and small cap stocks in Emerging markets. The index is comprised of approximately 3350 securities from 21 countries.

Moody's Baa Corporate Bond Index—An index comprised of industrial bonds rated Baa by Moody's with a minimum maturity of 20 years.

Consumer Price Index—A measure of the average change in prices over time for a basket of consumer goods.

Asset Allocation—Asset allocation does not ensure a profit or protect against loss.

International and Emerging Markets Investing—There are special considerations associated with international investing, including the risk of currency fluctuations and political and economic events. Investing in emerging markets may involve greater risk and volatility than investing in more developed countries.

Bonds and High Yield Bonds—When investing in bonds, it is important to note that as interest rates rise, bond prices will fall. High yield bonds have greater credit risk than higher quality bonds.

Commodities and Futures—The risk of loss in trading commodities and futures can be substantial. You should therefore carefully consider whether such trading is suitable for you in light of your financial condition. The high degree of leverage that is often obtainable in commodity trading can work against you as well as for you. The use of leverage can lead to large losses as well as gains.

Real Estate—When investing in real estate companies, property values can fall due to environmental, economic, or other reasons, and changes in interest rates can negatively impact the performance.

Score Disclosure: The Washington Crossing Advisors, LLC Stifel Conquest and Dynamic Strategies Portfolios require a $25,000 and $50,000 minimum investment, respectively. Strategies in the Stifel Score Program are proprietary products developed by Stifel. More information on the Score Program is included in the Stifel Consulting Services Disclosure Brochure and Part II of the Manager's Form ADV, which may be obtained from your Financial Advisor and which further outlines the fees, services, exclusions, and disclosures associated with this program. The information contained herein is believed to be reliable and representative of the portfolios available through Stifel; however, the accuracy of this information cannot be guaranteed. Investors should consider all terms and conditions before deciding whether the Score Program is appropriate for their needs.

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