CLS's WEEKLY 3

What You Need To Know About the Markets

DECEMBER 11, 2018

1. Diagnosing the latest sell-off
2. Global does better when it matters
3. Keep calm and stay invested

Market Performance

Equities	LAST WEEK	QTD	YTD '18
Global Equity Market[1]	-3.43%	-9.36%	-5.89%
Total U.S. Market[2]	-5.53%	-14.45%	-4.60%
Domestic Large-Cap Equity[3]	-4.55%	-9.27%	+0.32%
Domestic Small-Cap Equity[4]	-5.53%	-14.45%	-4.60%
International Equity[5]	-2.06%	-9.18%	-11.98%
Developed International Equity[6]	-2.26%	-10.15%	-11.44%
Emerging Market Equity[7]	-1.33%	-6.21%	-13.41%
Diversified Alternatives[8]	-1.04%	-2.46%	-1.80%
Fixed Income	**LAST WEEK**	**QTD**	**YTD '18**
U.S. Investment Grade Bonds[9]	+0.85%	+0.65%	-0.95%
Cash Equivalent[10]	+0.04%	+0.41%	+1.67%
Commodities	**LAST WEEK**	**QTD**	**YTD '18**
Commodity[11]	+1.17%	-1.57%	-3.56%

[1]MSCI ACWI Index [2]Russell 3000 Index [3]S&P 500 Index [4]Russell 2000 Index [5]MSCI ACWI ex-U.S. Index [6]MSCI EAFE Index [7]MSCI Emerging Markets Index [8]Morningstar Diversified Alternatives Index [9]Bloomberg Barclays Capital U.S. Aggregate Bond Index [10]Bloomberg Barclays Capital 1-3 Month U.S. Treasury Bill Index [11]Bloomberg Commodity Index As of 12/7/2018

Week in Review

Stocks were modestly lower last week. U.S. stocks, as defined by the Russell 3000 Index, lost more than 4%. International stocks fared better. Developed stocks fell more than 2%, and emerging market stocks lost just over 1%.

Bonds were modestly higher as the 10-year U.S. Treasury yield moved lower by 16 basis points to yield 2.85%.

Diagnosing the Latest U.S. Stock Sell-Off

After last week's sell-off, most equity markets are negative on the year, and U.S. stocks are flat. So, what exactly happened, and what should investors expect going forward? Based on our own assessment, there are three concerns that the market is weighing.

1. Bond investors are concerned about future economic growth: Bond investors clearly have priced in increased odds of the U.S. economy slowing, sending bond yields lower. In fact, there was much talk of a slight inversion of the yield chart last week. Despite this, there isn't enough data that would suggest that a slowdown or recession is imminent. In many ways, bonds may be overbought relative to where rates are likely to go if the U.S. Federal Reserve (Fed) still sees signs of inflation on the horizon.

2. Equity investors are looking for signs around U.S. trade talks with China: After a strong rally on the news of a pause in tensions over trade with China, investors spent the week reassessing whether or not anything will come of the next round of talks. Much of this was complicated by the CFO of China's largest smartphone manufacturer, Huawei, being arrested and extradited to the U.S. for violating U.S. sanctions on Iran. We expect that ongoing uncertainty related to U.S.-China trade talks will continue to weigh on stocks for the foreseeable future.

3. All investors are assessing increased market volatility: Equity investors are trying to decide what to make of recent market volatility, which has certainly been higher than in previous months (or years for that matter). Investors should remember that volatility is returning to more normal levels after being fairly muted for the last few years.

Joe Smith, CFA

Deputy Chief Investment Officer

Joe Smith specializes in quantitative research, risk management, and ETF due diligence. He serves as Senior Market Strategist for the CLS AdvisorOne International Equity Fund, CLS's Thematic Growth Strategy, and CLS's Core Plus ETF Strategy.

Prior to joining CLS in 2015, Mr. Smith worked at Russell Investments where he served as an Analyst responsible for asset allocation research, portfolio construction, optimization design, and risk management research. He later joined Russell ETFs as Manager of ETF Product Development and Research, a role in which he developed quantitative indexing strategies implemented as ETFs. Mr. Smith also worked for Charles Schwab Investment Management as a Senior Product Specialist supporting product management activities for the Schwab ETFs fund family. In addition, he worked for CLS during the summer of 2014 as an Investment Analyst.

Mr. Smith received his Bachelor of Science degree in Economics from the University of Washington. He later received his Master of Business Administration from the Tepper School of Business at Carnegie Mellon University.

Mr. Smith holds the Chartered Financial Analyst (CFA) designation and is a member of the CFA Society of San Francisco, Pittsburgh, and Nebraska. He is also a member of the Society of Quantitative Analysts and the Quantitative Work Alliance for Applied Finance, Education, and Wisdom.

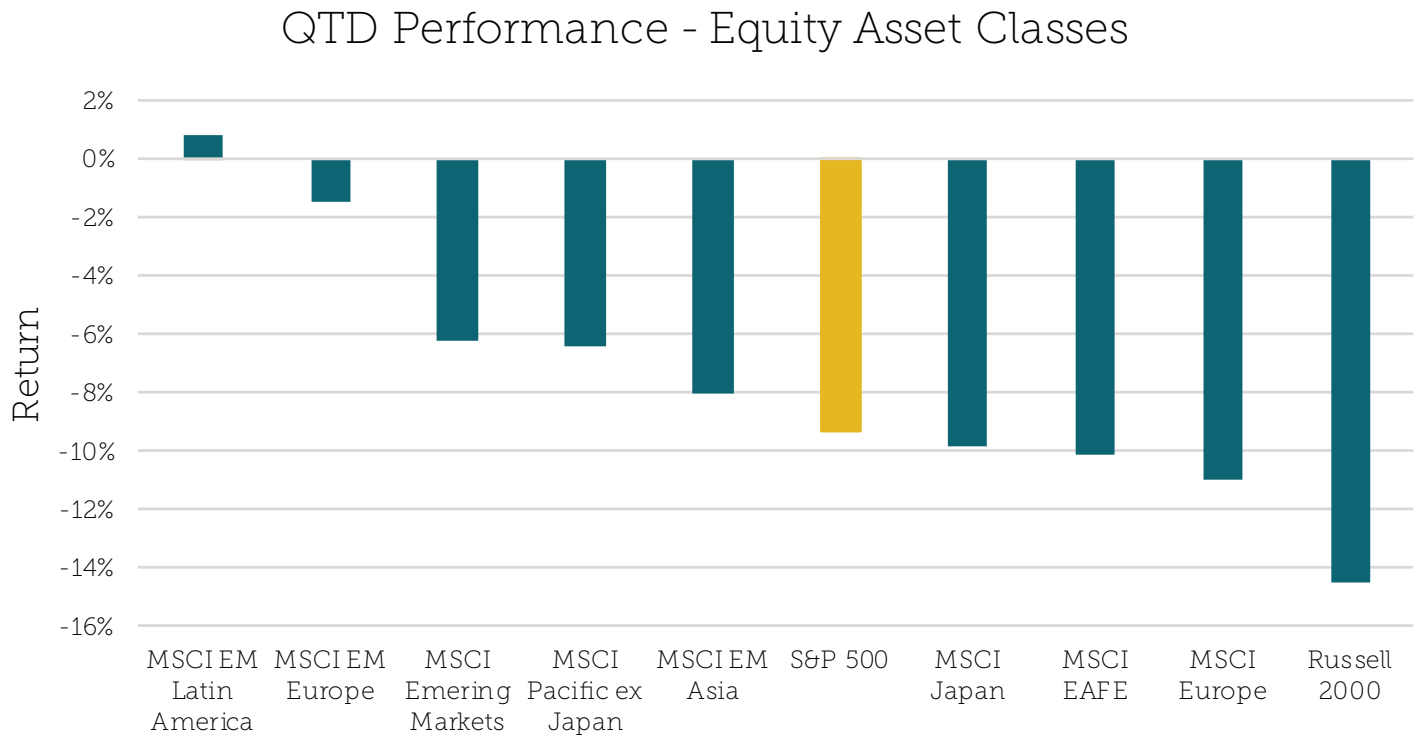
Did you know? In grad school, Joe spent 40 days in nine countries.

Global Investors Do Better When it Matters

U.S. stocks arguably get all of the attention when things are good and when things are not so good. Many investors avoid international stocks because of their perceived higher risk and, frankly, lackluster returns relative to U.S. stocks over the past few years. Global investors, however, know that those same international stocks provide diversification - an important element to being successful in the long term.

This quarter has been no different. International stocks have once again reminded us not to put all of our eggs into one basket. Quarter-to-date performance for each major equity asset class through the end of last week shows that emerging market stocks and developed Asian stocks have been the best place to receive the most of that diversification benefit.

Emerging markets have continued to be an overweight that we favor in CLS portfolios because of their diversifying nature and above-average expected returns (as our CIO, Rusty Vanneman, highlighted in his most recent Weekly Three). The key point is that the advantages of being global have shined when needed most.



Sources: Morningstar Direct, MSCI, FTSE/Russell. Based on weekly performance from 9/30/2018 through 12/8/2018.

As human beings, we are driven by emotions and often compelled to take action to address them. Investing is no different, and times like these can make each of us feel we ought to "do something." However, those emotions can drive us to do the one thing that we all know to be damaging in the long term: sell low, buy high.

When the markets are volatile, it is important to remind ourselves of our intended goals and investment timelines and to consider whether or not anything has changed. For financial advisors, this doesn't necessarily mean considering a change in your clients' Risk Budget scores, but rather a conversation on why those scores are appropriate for their current situations and stated goals.

Another important consideration is to avoid checking account balances on a day-to-day basis if we don't have the stomach for it. Keep in mind that "unrealized" losses in any situation are just that — unrealized — until we choose to sell that security down the road. If we remain invested for the long haul, there can be a much lower chance that will be our final result when we choose to sell our investments.

Finally, many of our investment horizons are quite long, which means that all we should really do is put even more dollars to work. When markets head lower, they can present some of the best opportunities to pick up assets. Why? Simply put, investors are usually willing to sell them at meaningful discounts.

Some of the most important aspects to investing are patience and staying invested. We believe these are both key ingredients to longer-term investment success.

The MSCI ACWI Index captures large and mid cap stocks across developed markets and emerging markets countries. The index covers approximately 85% of the global investable equity opportunity set. The Russell 3000 Index is an unmanaged index considered representative of the U.S. stock market. The index is composed of the 3,000 largest U.S. stocks. The S&P 500 Index is an unmanaged index of 500-large capitalization companies. This index is widely used by professional investors as a performance benchmark for large-cap stocks. The Russell 2000 Index is an index comprised of the 2,000 smallest companies on the Russell 3000 Index and offers investors a benchmark for small-cap stocks. The MSCI ACWI ex U.S. Index (MSCI All-Countries World Index, excluding U.S.) is an index considered representative of stock markets of developed and emerging markets, excluding those of the U.S. The MSCI EAFE Index is an index which tracks performance of international equity securities in developed countries in Europe, Australia, Asia, and the Far East, excluding the U.S. and Canada. The MSCI Emerging Markets Index is an index which tracks performance of large and mid-cap firms across countries classified as emerging market countries. The Bloomberg Barclays Capital U.S. Aggregate Bond Index measures performance of the U.S. investment-grade bond market. The Bloomberg Barclays Capital 1-3 Month U.S. Treasury Bill Index includes all publicly issued zero-coupon U.S. Treasury Bills that have a remaining maturity of less than 3 months and more than 1 month, are rated investment grade, and have $250 million or more of outstanding face value. The Bloomberg Commodity Index is made up of exchange-traded futures on physical commodities and represents commodities that are weighted to account for economic significant and market liquidity. The Morningstar Diversified Alternatives Index is an index comprised of exchange traded funds (ETFs) in the ProShares lineup that use alternative and non-traditional strategies. An index is an unmanaged group of stocks considered to be representative of different segments of the stock market in general. You cannot invest directly in an index.

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