Global Income Strategy

Portfolio and Economic Commentary – 2nd Quarter 2018

Global Income Strategy Commentary

Our investment philosophy is predicated on a time-tested, three pronged approach providing solid risk adjusted returns to our investors for over two decades.

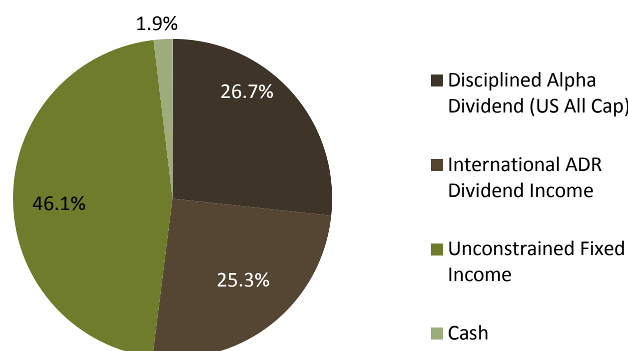
- We believe in the importance of getting paid immediately for the risks which are taken and focus on businesses which compensate our clients with **dividends and above average interest.** We believe this income stream, coupled with capital appreciation, is a vital aspect of total return.
- We dig deep for **value** often viewing crisis as an opportunity. We believe that fundamental research and patience are critical to long term success and that over time, the price of a company will rise to reflect the value of the underlying firm viewing each purchase as if were buying a piece of a business – not simply a stock certificate.
- We believe that **global revenue generation** is a key component to growth and sustainability and invest in companies with global growth opportunities. We are unafraid to take contrarian positions, but remain diligent about the risks of a global economy.

Performance Commentary

The Global Income strategy has posted a modest gain of 0.67% for the year versus a similar gain of 0.75% for the blended balanced benchmark. The annualized trailing returns for the strategy since our inception on January 1, 2003 are 7.15% versus 7.58% for the blended benchmark and 6.43% for Morningstar's US Fund Allocation – 50% to 70% Equity. The twelve month trailing yield for the Global Income strategy stands at 4.62% versus 1.71% for the Vanguard Balanced index fund (VBINX).

We remain underweight to a traditional 60% stock/40% bond portfolio due to the risks which remain and valuation metrics. That said, our portfolio maintains a reasonable 12.26 P/E (TTM) which is significantly lower than the broader market indices – most of which currently maintain multiples in excess of 20 times trailing earnings. Our focus continues to emphasize the importance of immediate income to our investors particularly in this volatile, low interest rate environment, which we believe will persist for longer than most economists. In the fixed income sector, our emphasis remains on high yield bonds, which we believe more adequately compensates our investors for credit risk, while providing better protection in a potentially rising interest rate environment. The following is an analysis of the independent strategies which comprise our flagship Global Income strategy in percentages indicated above.

Sector Allocation



Top Five Equity Holdings	Weight
Teva Pharmaceuticals	1.32%
Hanesbrands	1.16%
Phillips 66	1.13%
Mattel	1.12%
B&G Foods	1.11%

Top Five Fixed Income Holdings	Weight
Treehouse Foods	0.62%
AMC Entertainment	0.60%
Oppenheimer Holdings	0.59%
Lifepoint Health	0.58%
NCR Corporation	0.58%

Disciplined Alpha Dividend Strategy Commentary

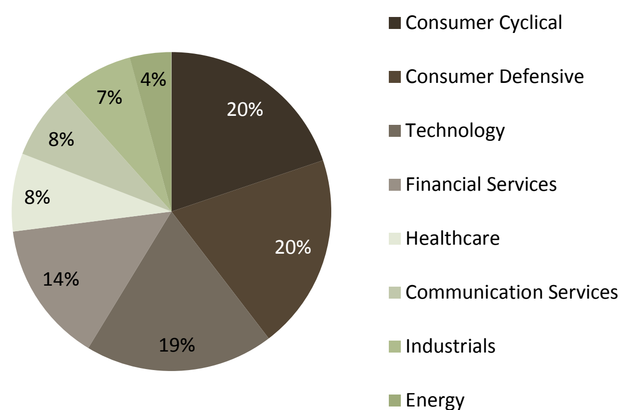
As value investors, we constantly focus on our duty to protect the principal of our investments even as we look for ways to grow them over time as well. As economists, we remain alert to trends taking place in the larger global economy. As analysts, we seek to invest in securities priced with a margin of safety in order to account for their near term volatility and our uncertainty about what the future holds. With this in mind, we look for opportunities in three specific categories: classic value, persistent earners, and distressed or contrarian.

Classic value stocks sell at attractive valuations and provide above-average dividend yields and growth. Persistent earners are companies which have steady and predictable earnings and that are selling below their historic valuation. The distressed/contrarian category refers to stocks that are out of favor due to what we perceive to be temporary factors and are likely to appreciate substantially as the temporarily distressing factor recedes. Typically the distressed category is the smallest in the portfolio.

Performance Commentary

The Disciplined Alpha Dividend strategy has returned 1.72% year-to-date while the Russell 3000 Value index has lost 1.16 this year. The strategy has produced outstanding ten-year risk adjusted returns soundly besting its index and large value peer group for the period earning a Morningstar 4-star overall and 10-year rating. The trailing annualized ten year returns were 10.21% for the strategy and 8.60% for the Russell 3000 Value index. Since inception on January 1, 2003, the strategy has returned 9.22% versus 9.23% for the Russell 3000 Value index and 9.81% for the Dow Jones US Select Dividend index.

Our sector allocation weighting and active return have added to relative performance for the year against the Russell 3000 Value index. The consumer cyclical, consumer defensive, technology and healthcare sectors have been our largest attributors to active return, while the energy, financial services and communication services sectors were the largest detractors to relative performance. Though maintaining a focus on dividends and above average income generation, we believe the utility and real estate sectors remain overvalued and will perform poorly in a potentially rising interest rate environment. The top performers for the year were DineEquity (50.2%), AbbVie (18.4%), Cisco Systems (14.0%), Phillips 66 (12.6%) and Apple (10.2%). The bottom performers for the year have been Principal Financial (-23.7%), Pitney Bowes (-20.8%), AT&T (-15.0%), Metlife (-12.4%) and Qualcomm (-3.1%).



Top Ten Holdings	Weight
Hanesbrands	4.29%
Phillips 66	4.18%
Mattel	4.15%
B&G Foods	4.10%
Apple	4.02%
Norfolk Southern	4.01%
Merck & Co.	4.00%
Kimberly Clark	3.97%
Altria	3.88%
Cisco Systems	3.86%

Disciplined Alpha Dividend Strategy Commentary

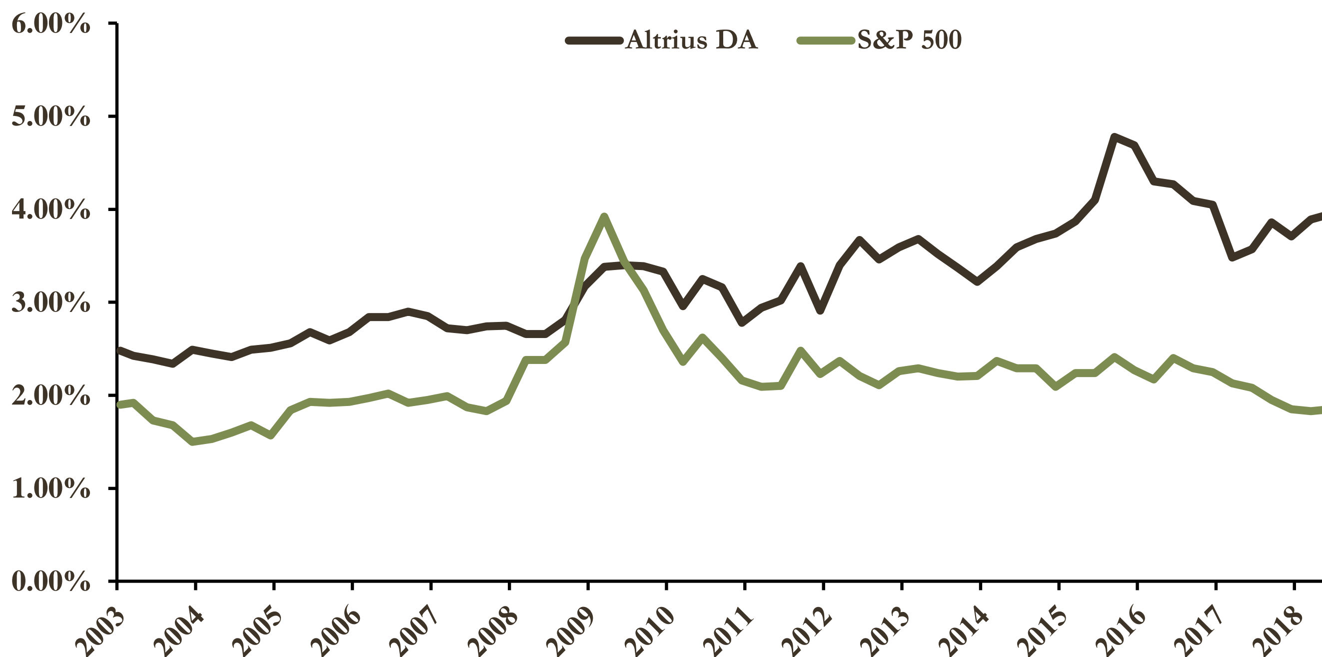
As one may recognize from the below chart, our firm has consistently provided a steady stream of income to our clients in the form of dividends. It is our assertion that this income stream has not only reduced the risk of our portfolio, but also provided a large part of the total return thereby leading to our performance success over this past tumultuous decade plus.

We believe that dividends allow our investors to "get paid to wait" while patiently working through volatile business and market cycles. This strategy provides emotional support during difficult cycles and enables investors to weather turbulent periods by utilizing dividend income for personal needs or to reinvest cash at lower valuations. Our strategy is not only grounded in psychological and behavioral finance concepts, but is also supported by empirical evidence outperforming in both negative and full market cycles.

Dividends also act to align the interests of corporations and shareholders in helping to eliminate the agency effect. Corporate boards have recognized the value of dividends in stabilizing their stock prices and encouraging investment during both high and lower tax regimes. In supporting and increasing dividends over time, managers are compelled to maintain a reliable stream of cash flows to shareholders rather than waste capital on those expenses adding little to corporate revenue including executive perks, pet projects, and ill-timed, unwise acquisitions. It appears a paradox; however, our experience and academic studies have displayed that sufficient investment for a good business can still occur in conjunction with dividends as managers are forced to invest cash flow more prudently and only in those capital investments in which they have the highest conviction in adding to corporate revenue, particularly since stock buybacks are often ill-timed.

Altrius: A Story of Consistent Dividends Over the Years

The strategy has consistently delivered an above average dividend yield versus the S&P 500 since its inception.



Source: Morningstar

INTERNATIONAL ADR DIVIDEND INCOME STRATEGY COMMENTARY

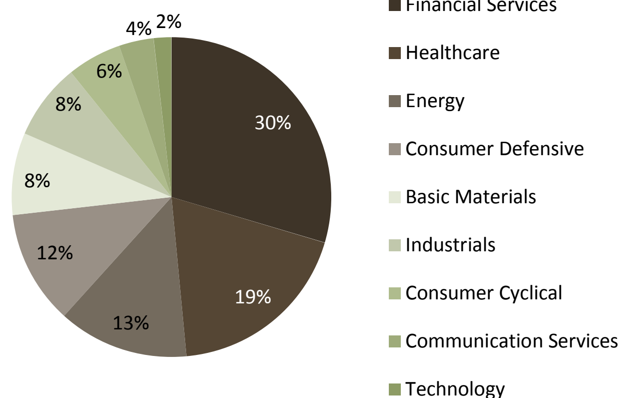
As value investors, we constantly focus on our duty to protect the principal of our investments even as we look for ways to grow them over time as well. As economists, we remain alert to trends taking place in the larger global economy. As analysts, we seek to invest in securities priced with a margin of safety in order to account for their near term volatility and our uncertainty about what the future holds. With this in mind, we look for opportunities in three specific categories: classic value, persistent earners, and distressed or contrarian.

Classic value stocks sell at attractive valuations and provide above-average dividend yields and growth. Persistent earners are companies which have steady and predictable earnings and that are selling below their historic valuation. The distressed/contrarian category refers to stocks that are out of favor due to what we perceive to be temporary factors and are likely to appreciate substantially as the temporarily distressing factor recedes. Typically the distressed category is the smallest in the portfolio.

PERFORMANCE COMMENTARY

The International ADR Dividend Income strategy has declined 2.71% outpacing its indices for the year. The MSCI EAFE Value index was lower by 4.61% while the S&P Int'l Dividend Opportunities index lost 4.04%. Since its inception on June 1, 2010, the strategy has produced annualized returns of 6.18% versus 4.50% for the S&P Int'l Dividend Opportunities and 6.44% for the MSCI EAFE Value indices respectively. Since its inception, the strategy has produced alpha against the MSCI EAFE Value index due to its lower beta.

Our sector allocations and stock selection have had a positive impact on active return versus the MSCI EAFE Value index during the quarter. The healthcare, energy, basic materials and technology sectors attributed the greatest portion to relative outperformance while consumer defensive, utilities and communication services were the largest detractors to active return. Going forward, we believe we will find more value amongst international issues than U.S. companies while expecting the energy and basic materials sectors to be continued benefactors of global economic stabilization. The top performers for the year have been Teva Pharmaceuticals (28.4%), Equinor (25.6%), GlaxoSmithKline (16.8%), ENI (13.9%) and BAE Systems (13.2%) while the bottom performers were British American Tobacco (-23.1%), Mitsubishi Financial Group (-22.4%), Vodafone (-22.3%), Daimler (20.8%) and ING Groep (-20.3%).



Top Ten Holdings	Weight
Teva Pharmaceuticals	5.19%
Astrazeneca	4.09%
HSBC Holdings	3.72%
Lloyds Banking Group	3.72%
Barclays	3.62%
Equinor	2.33%
BP PLC	2.21%
BHP Billiton	2.17%
Sasol	2.17%
Royal Dutch Shell	2.10%

International ADR Dividend Income Strategy Commentary

As one may recognize from the below chart, our firm has consistently provided a steady stream of income to our clients in the form of dividends. It is our assertion that this income stream has not only reduced the risk of our portfolio, but also provided a large part of the total return thereby leading to our performance success over this past tumultuous decade plus.

We believe that dividends allow our investors to "get paid to wait" while patiently working through volatile business and market cycles. This strategy provides emotional support during difficult cycles and enables investors to weather turbulent periods by utilizing dividend income for personal needs or to reinvest cash at lower valuations. Our strategy is not only grounded in psychological and behavioral finance concepts, but is also supported by empirical evidence outperforming in both negative and full market cycles.

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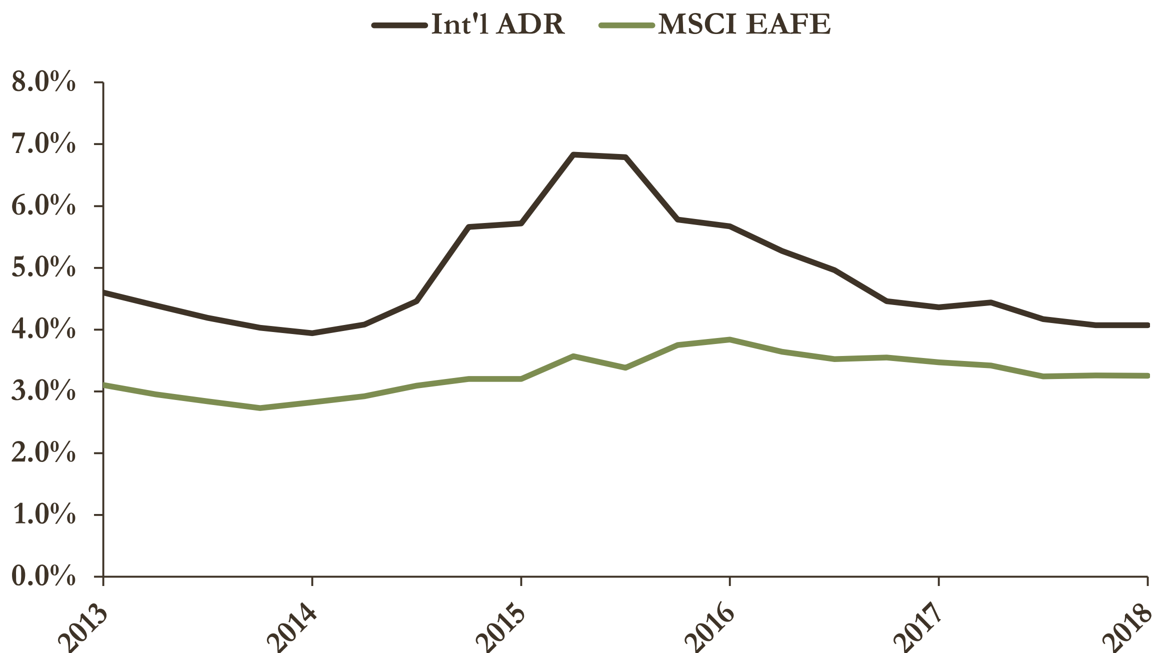
Altrius: A Story of Consistent Dividends Over the Years

The strategy has consistently delivered a higher dividend yield than the MSCI EAFE index since its inception.



Source: Morningstar

ALTRIUS
CAPITAL MANAGEMENT

Unconstrained Fixed Income Strategy Commentary

Based on our macroeconomic outlook over a three to five year period and our cyclical views from quarter to quarter, we employ top-down strategies that focus on yield curve positioning, volatility, and sector rotation. We then utilize bottom-up analysis to drive our security selection process and facilitate the identification of undervalued securities with the potential for above average income. We invest in securities that operate across diversified sectors in the fixed income markets of the United States, primarily those in U.S. dollar denominated high yield and investment grade bonds, including government securities, corporate bonds, and mortgage- and asset-backed. Sources of added value:

Credit Analysis - We emphasize independent analysis and do not rely on credit agencies.

Duration Risk - We avoid long, extreme duration shifts generally operating within a moderate duration range typically between two and four years.

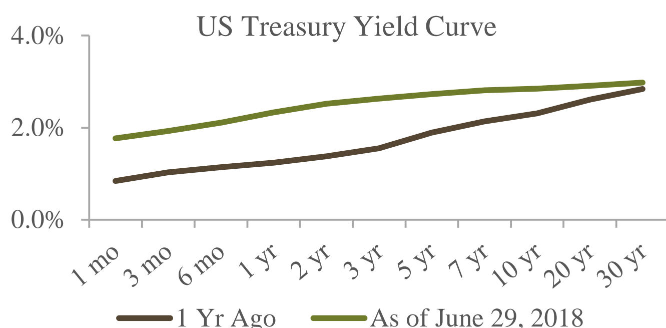
High Income - Our research attempts to identify issues paying above average income.

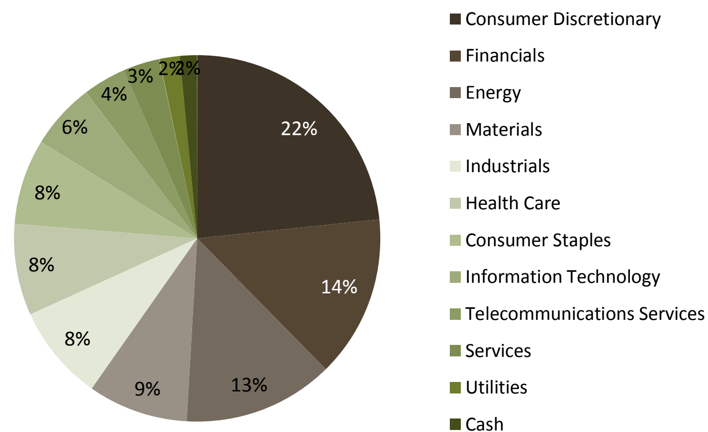
Risk Premium Management - We seek to attain an attractive yield/spread in relation to a five-year treasury within acceptable levels of portfolio risk.

Performance Commentary

Market Overview

Following a rough opening quarter to the year, most all major subsectors of the broad based taxable US fixed income market generated positive returns in the second quarter of 2018, with the exception of investment grade corporate bonds, which declined approximately -1.0% as a result of rising rates. After falling -1.46% in the first quarter of the year, the Barclays US Aggregate Bond index continued to decline by -0.16% in Q2, and is now down -1.62% YTD. In its June meeting, the Fed raised rates by 0.25% for the second time this year to bring the federal funds target rate to 1.75%-2.00%. With the Fed's dual mandate of 'price stability' (low and contained inflation of around 2.0% per annum) and 'maximum employment' (US unemployment at or below 4.0%; currently approximately 3.8%) appearing stable, market consensus and Fed posturing is signaling an additional two rate hikes will likely occur before year's end.



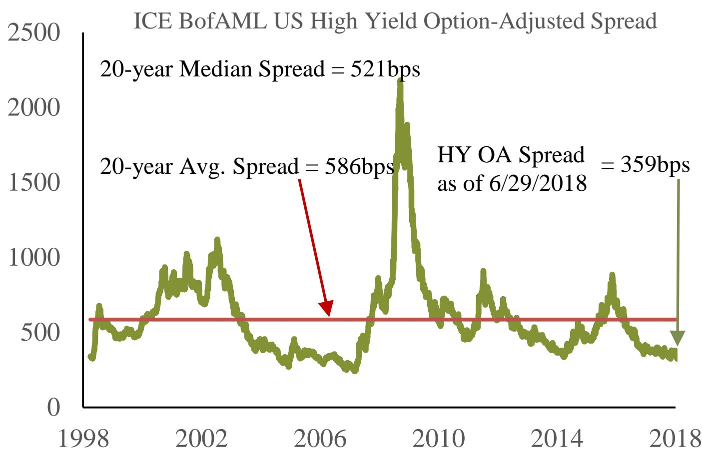


Top Ten Holdings	Weight
Treehouse Foods	1.28%
AMC Entertainment	1.27%
Oppenheimer	1.25%
Tempur Sealy	1.24%
Lifepoint Health	1.23%
Quad/Graphics	1.22%
Centurylink	1.20%
NCR Corporation	1.20%
Infor	1.20%
Coeur Mining	1.19%

UNCONSTRAINED FIXED INCOME STRATEGY COMMENTARY

The US Treasury curve continued to flatten during the quarter as a result of the aforementioned rate hikes, with yields rising across all maturities and the spread between the 2-year and 10-year compressing 14bps from Q1's ending level to a differential of 33bps by quarter end.

High yield corporate bonds, specifically the lowest rated issues within the segment (B to CCC), continued to be the best performing area in the US fixed income markets producing a return of approximately +1.0% during the quarter. While the aggregate option-adjusted spread for high yield bonds contracted modestly from 372bps to 359bps by quarter end, aggregate spreads for investment grade corporate bonds expanded by roughly the same margin increasing from 117bps at the end of the first quarter to 130bps by the close of Q2.



PERFORMANCE SUMMARY

After generating a strong +0.68% gross return for Q1 while most all other fixed income market segments and indices finished the first three months of the year in negative territory, the Unconstrained Fixed Income strategy continued to produce exceptional results posting a +1.29% gross return during the second quarter of 2018 and is up +1.97% YTD. While the Barclays US Aggregate Bond index continued to decline during the second quarter falling -0.16% and is now down -1.62% YTD, the ICE Bank of America Merrill Lynch High Yield Total Return index generated a positive return of +1.00% for Q2, essentially drawing back to even for the year with a YTD return of +0.08%.

During the second quarter, a number of the strategy's holdings in the previously distressed sectors of telecommunication services, health care, and energy experienced strong price recovery/appreciation and contributed significantly to the strategy's exceptional performance for the quarter. Telecommunication services was the strategy's best performing sector during the quarter generating a return of over +4.0% with health care, energy, and consumer discretionary each returning approximately +2.0%. Given their substantial weight of strategy assets comprising 23.2% and 13.2% respectively, the consumer discretionary and energy sectors were the most notable contributors to the strategy's Q2 results. The information technology sector was the only negatively performing sector within the strategy for the quarter declining roughly -1.7%. The tables below outline the strategy's five best and worst performing issues for the second quarter of 2018.

Top 5 Contributors	Avg Wgt	Return	Contrib
Rent A Center 6.625% 2020	1.07	11.63	0.12
Denbury Res. 6.375% 2021	0.49	15.37	0.07
Supervalu 7.750% 2022	0.75	8.65	0.06
CenturyLink 6.750% 2023	1.22	4.98	0.06
Ensco PLC 8.000% 2024	0.96	6.13	0.06

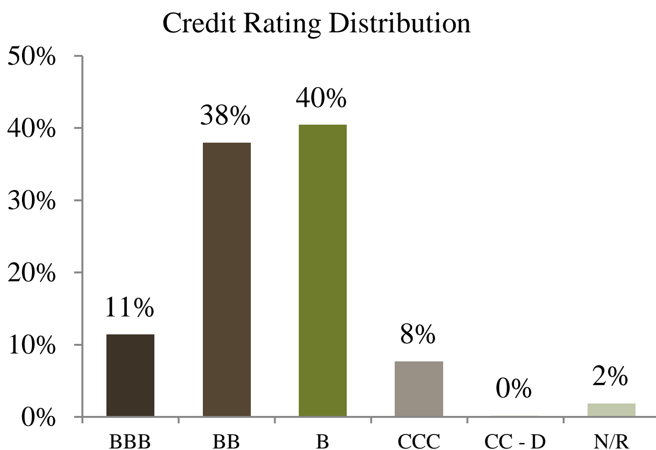
Bottom 5 Detractors	Avg Wgt	Return	Contrib
Diebold 8.500% 2024	1.09	(7.02)	(0.08)
Pitney Bowes 4.700% 2023	1.06	(2.76)	(0.03)
R. Venezuela 7.000% 2018	0.09	(26.39)	(0.03)
Coeur Mining 5.875% 2024	1.23	(1.57)	(0.02)
Ferrellgas 6.750% 2022	0.65	(2.68)	(0.02)

UNCONSTRAINED FIXED INCOME STRATEGY COMMENTARY

STRATEGY CHARACTERISTICS

The strategy is heavily invested in the consumer discretionary, financial services, and energy sectors, with each accounting for approximately 23.2%, 14.2%, and 13.2% respectively of total strategy assets as measured by aggregate market value as of 06/29/2018. Exposure to the materials, industrials, and health care sectors is also robust with each accounting for approximately 8.8%, 8.4%, and 8.0% respectively. Despite the seemingly high degree of investment exposure to the aforementioned sectors, the strategy is always invested in an array of unaffiliated companies within each sector in order to provide broad diversification and help mitigate against issue specific credit risk.

Both the aggregate maturity and overall duration of the strategy contracted slightly relative to Q1 2018 levels, ending the quarter at 3.53 years and 3.04 respectively. The strategy's overall credit quality remained unchanged over the prior the quarter, and currently stands at 'B+'. The strategy's overall credit rating distribution is displayed in the following exhibit:



STRATEGY OUTLOOK

The carnage that investment grade corporate bonds have been experiencing thus far this year, especially those with higher durations in excess of 6.0, exhibits the importance of managing interest rate risk within a fixed income strategy. Over the prior five plus years we made the strategic decision to focus on allocating strategy assets on shorter duration high yield bonds, focusing more attentively on mitigating 'default risk' within the strategy. While in the period between 2010 and 2016 it was 'safe' to extend on longer duration bonds due to the fact that the Fed left rates unchanged at 0.00%-0.25%. We are now however in a rising rate investment environment given the two rate hikes that have already been instituted and another two which will likely occur during the latter six months of this year.

With default rates of high yield bond issuers currently at approximately 2.0% (roughly half of the 30 year average of 3.8%), and given the aforementioned rising rates, investor demand for high yield bonds is exceptionally robust right now. We anticipate that high yield bond spreads will remain largely unchanged from current levels and returns for the remainder of the year will come primarily from coupon payments alone.

Despite the strong performance of the strategy's telecommunication services positions this past quarter, issuers in the sector remain highly levered leaving us cautious of increasing the strategy's allocation to the sector. With oil prices recovering and stabilizing at and above $70/bbl, there are a number potential opportunities that are present in the energy sector, specifically in regard to 'lower duration' issues.

With the US and global economy expected to grow at approximately 2.5%-3.0% and 3.5%-4.0% respectively in 2018, the fundamentals supporting the high yield bond market appear favorable for the remainder of this year. Despite lofty valuations, we maintain that high yield remains both the most compelling and stable segment of the fixed income markets in which to be invested, especially in the face of rising interest rates.

DISCLOSURES

This report includes candid statements and observations regarding investment strategies, individual securities, and economic and market conditions; however, there is no guarantee that these statements, opinions or forecasts will prove to be correct. These comments may also include the expression of opinions that are speculative in nature and should not be relied on as statements of fact. Altrius is committed to communicating with our investment partners as candidly as possible because we believe our investors benefit from understanding our investment philosophy and approach. Our views and opinions include "forward-looking statements" which may or may not be accurate over the long term. Forward-looking statements can be identified by words like "believe," "expect," "anticipate," or similar expressions. You should not place undue reliance on forward-looking statements, which are current as of the date of this report. We disclaim any obligation to update or alter any forward-looking statements, whether as a result of new information, future events or otherwise. While we believe we have a reasonable basis for our appraisals and we have confidence in our opinions, actual results may differ materially from those we anticipate.

The information provided in this material should not be considered a recommendation to buy, sell or hold any particular security. The S&P 500® Index is an unmanaged index of 500 selected common stocks, most of which are listed on the New York Stock Exchange. The Index is adjusted for dividends, weighted towards stocks with large market capitalizations and represents approximately two-thirds of the total market value of all domestic common stocks. The Russell 3000 Value Index is an unmanaged index commonly used as a benchmark to measure value manager performance and characteristics. The Dow Jones U.S. Select Dividend Index is an unmanaged index commonly used as a benchmark to measure dividend manager performance and characteristics. The Russell 2000 Index, the Russell 2000 Growth Index, and the Russell 2000 Value Index are unmanaged indices commonly used as benchmarks to measure small cap manager performance and characteristics. The MSCI EAFE® Index is a free float-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the U.S. & Canada. The Bloomberg Barclays U.S. Aggregate Bond Index and Bank of America Merrill Lynch US High Yield Master II Total Return Index are unmanaged indices that are commonly used as benchmarks to measure fixed income performance and characteristics. Index performance returns do not reflect any management fees, transaction costs or expenses. Investments cannot be made directly in an index. **Investments made with Altrius Capital Management, Inc. are not deposits or obligations of any bank, are not guaranteed by any bank, are not insured by the FDIC or any other agency, and involve investment risks, including possible loss of the principal amount invested. Past performance is not a guarantee of future returns.**

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