We at Sterling Capital Management are engaged in three key support areas: providing custom asset allocation frameworks, selecting high-quality investment managers and constructing well-diversified portfolios. Importantly, of course, we remain engaged every day in the ongoing monitoring and periodic rebalancing of those portfolios over time.

Today, we are pleased to provide a review of global financial markets during the second quarter of 2018, to reflect on changes we made to our portfolios during the quarter, and to update our current positioning and outlook.

EQUITY MARKET REVIEW

Beginning with equity markets, global equities gained ground in the second quarter, with the Russell Global Index increasing 0.66 percent despite a late-quarter pullback and broad-based weakness in emerging markets. Although the second quarter proved to be less volatile than the first quarter of 2018, rising trade war fears and falling emerging market currencies kept investors on their toes and contributed to a general lack of global equity market direction in the second quarter.

U.S. equities posted positive returns and outperformed international equities during the quarter. And while international developed markets experienced a modest decline in the second quarter, emerging market equities fell substantially. Global small-caps outperformed large-caps in the second quarter, and global growth equities continued to significantly outperform and have now outperformed global value equities in each of the last six quarters. Energy was the top-performing sector in the second quarter, followed by information technology and consumer discretionary. Financials, telecom services and industrials lagged the broader market and posted negative returns.

In the United States, the Russell 3000 broad equity market index rose 3.9 percent in the second quarter. Strong first-quarter earnings and generally favorable economic data, both of which were positively impacted by tax reform, helped overcome fears around monetary policy normalization, trade negotiation uncertainty, and peak earnings and economic growth. According to FactSet, first-quarter 2018 S&P 500 earnings rose approximately 25 percent year-over-year, coming in well ahead of consensus estimates of roughly 17 percent. Earnings guidance was also favorable during first-quarter earnings season, with second-quarter S&P 500 earnings growth estimates experiencing the largest intra-quarter increase in eight years. Merger and acquisition activity, accelerating stock repurchases and dividend increases, and rising capital expenditure expectations were also tailwinds for U.S. equities during the quarter. Rising wages, commodity prices and transportation costs, however, represent potential threats to future earnings growth.

On a sector, style and size basis, relatively narrow market leadership trends persisted in the second quarter. Growth continued to outperform value by a wide margin in the second quarter, although small-cap value stocks marginally outperformed small-cap growth stocks. Information technology and consumer discretionary were once again among the top-performing sectors during the quarter, led by continued relative strength in "FAANG" stocks. While value-oriented sectors such as energy and real estate produced strong returns during the quarter, other value-centric sectors, such as consumer staples, industrials and financials, failed to keep pace with the broader market. Small-cap stocks outperformed both large-caps and mid-caps. The Russell 2000 small-cap index increased 7.75 percent during the quarter and made several all-time highs in May and June.

Moving outside the United States, international equities fell 2.6 percent during the quarter. Emerging markets experienced the heaviest declines, losing more than 8 percent. International developed markets fared better but still declined by 0.77 percent. A surging U.S. dollar was a headwind for international equities during the quarter, as the U.S. Dollar Index rose approximately 5 percent to post its first quarterly gain since the fourth quarter of 2016. Slowing economic growth in Europe, a sluggish Brexit negotiation progress and political instability in Italy also weighed on international equity market returns during the quarter. Similar to the United States, growth produced material outperformance over value in international developed and emerging markets.

Australia, Canada and the United Kingdom were among the top-performing international equity markets during the quarter, while Brazil, South Korea and Italy were among the worst performers. China also experienced meaningful weakness during the quarter, driven by trade tensions with the United States, monetary policy tightening and concerns related to more stringent banking regulations. The energy and health care sectors were the only international sectors to post positive results during the quarter, while financials and telecom services fell significantly.

PORTFOLIO POSITIONING

In terms of portfolio positioning, we made multiple changes to the equity portion of portfolios during the early part of the second quarter. Most notably, we increased the portfolio's emerging market equity net-of-benchmark underweight as valuation metrics such as dividend yield and sales yield remained stretched when compared to developed markets. We also reduced international developed markets exposure during the quarter, though the portfolio maintained a small net-of-benchmark overweight to this segment. With the decreased exposure to international equities, the portfolio's overweight to U.S. equities was increased. While certain U.S. equity valuation factors remain elevated, U.S. dividend yields are reasonably attractive within the context of low interest rates and strong long run dividend growth.

BOND MARKETS

Now, turning to bond markets, the Bloomberg Barclays Aggregate Bond Index, a proxy for overall fixed income performance, posted a negative 0.16 percent return for the quarter.

Looking at different segments of fixed income markets, both investment grade and high yield corporate credit spreads widened for the second consecutive quarter. Investment grade corporate bonds declined by nearly 1 percent in the second quarter, bringing year-to-date returns to negative 3 percent. Despite widening spreads, high yield returns were positive for the quarter, however, and remain positive for the year as well.

Within the structured space, agency mortgage-backed securities outpaced duration-matched Treasuries for the quarter despite the Fed's continued exit putting pressure on the market.

Foreign developed bonds returned 0.37 percent for the quarter and 1.6 percent year-to-date.

At the Federal Open Market Committee meeting in June, the Federal Reserve continued its path of rate normalization by raising the target range for the fed funds rate by 25 basis points from 1.75 percent to 2 percent. This increase marked the seventh hike since rates were lowered to zero following the financial crisis nearly a decade ago. The Fed characterized U.S. economic growth as "solid." Chairman Jerome Powell acknowledged that while inflation has moved to the Fed's 2 percent target, it is "too early to declare victory" until inflation remains at the target for a sustained period.

In the Fed's forward guidance, the majority of Fed officials added an additional projected rate hike for 2018, which would bring the total number of increases from three to four.

For fixed income investors, the topic of the yield curve remains a focus. The curve continues to flatten as the front end of the curve moves higher, largely as a result of the Fed raising interest rates. However, the long end remains anchored as upward pressure on inflation remains muted. As of quarter end, the difference in yield between a 2-Year and a 10-Year Treasury fell to 33 basis points, the flattest the Treasury curve has been since before the financial crisis in 2007.

During the second quarter, no changes were made to our Core Fixed Income portfolio, and positioning remains similar to last quarter. Our taxable core fixed income portfolio remains short duration relative to its benchmark. It also maintains an overweight to credit, both corporate and structured, and an underweight to government-related securities, specifically Treasuries. Yield curve positioning remains a focus.

Our Municipal Bond portfolio also remains slightly short duration and maintains an overweight to essential service revenue bonds and an underweight to general obligation bonds.

SECOND-QUARTER REVIEW

For the second quarter overall, our balanced portfolio gained 0.7 percent. Manager selection decisions detracted slightly from benchmark relative returns in the second quarter, while asset allocation decisions contributed positively. The portfolio has delivered positive absolute returns and positive relative returns versus both benchmark and peers for the year-to-date, one-year, two-year and since inception periods as of June 30, 2018.

Leading contributors on the equity side for the second quarter included our underweight to emerging market equities, which trailed both U.S. and international developed markets by a wide margin. Also, our global unconstrained equity manager delivered strong performance once again, posting a positive 6.6 percent return in the second quarter, outperforming its benchmark by nearly 6 percent. On the fixed income side, the largest contributor came from our mortgage-related manager, which produced a positive absolute return for the quarter while the benchmark aggregate bond index declined.

Overall, we're pleased with second-quarter and longer-term results and the way our portfolios have weathered the increased volatility in both equity and fixed income markets thus far in 2018. We remain confident that we're well positioned for markets ahead.

Thank you very much as always for your interest, trust and support. We look forward to a continued strong and successful partnership.
