GROVE STREET FIDUCIARY, LLC

WEALTH AND TRUST ADVISORS

AUGUST 2018

MARKET COMMENTARY & QUARTERLY MARKET REVIEW

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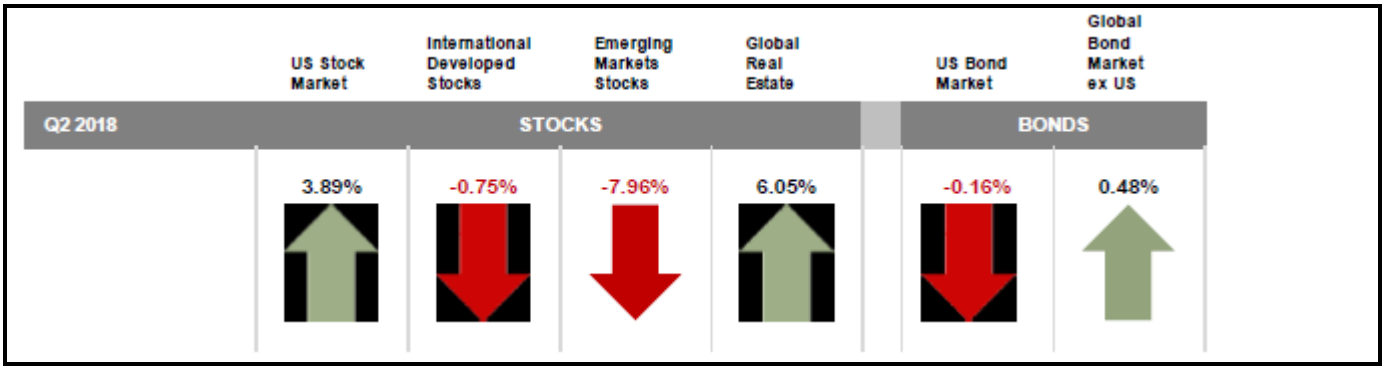
Market Commentary: August 2018

Where were you a decade ago? Ten years ago this summer, the Federal government seized California mortgage lender Indymac Bank, launching the start of the greatest recession in a generation. Many are wondering if any of the various events today, a brewing trade war, rising interest rates, a difficult Brexit, and bewildering political changes, will trigger another daunting downturn. From Europe to the Middle East to China, geopolitics is the number one risk to the world's economies and markets.

Be careful however. Like a funhouse mirror at a carnival, the geopolitical circumstances (as well as our own personal situations) can distort the reflection we see when looking at our investments. *It is tempting to see your entire portfolio in the reflection of today's state of affairs - but that would be a miscalculation.* On top of this cautionary note, we have some practical portfolio recommendations for you in the upcoming quarters resulting from two shifts in the investment environment. Before I expand on these ideas, let's review the returns for the quarter.



A quick glance at the arrows above (also found on page 2 of the Quarterly Market Review) and you will see that the markets had mixed results for the quarter, no longer moving in sync with one another. U.S. stocks and global real estate were strongly positive while emerging markets stocks were decidedly negative. International developed stocks and U.S. bonds were both down slightly while international bonds gained about one-half percent. Nonetheless, for the lagging year, stocks of all classes had solid gains while bonds were largely flat.

Returning to my caution above, why would it be a miscalculation to superimpose the reflection of the current state of affairs on your portfolio? *Because your portfolio is built for two different purposes and times, today's conditions do not equally apply to all of your investments.* Unquestionably, the short end of your investment portfolio (1-5 years) should reflect today's concerns as well as your current income needs. Therefore, although today's funhouse reflection may look frightening, it is corrected by the safe, steady, and true likeness of the cash and bonds in your portfolio allocated to ensure the next five years are not disturbed. The long end of your investment portfolio (beyond 5 years) requires an "investor's perspective" and calls for a

completely different calculus. These investments have longer reach purposes such as overcoming rising prices to ensure purchasing power in the future, insuring income a decade from now, or leaving a legacy. These investments will benefit from the shifts I describe below.

Integral to our fiduciary obligation is researching, understanding, and communicating investment realities to help shape our recommendations to you. Practical adjustments such as replacing an investment with a lower cost index to save you a few hundred dollars each year are common. Less frequent are the strategic changes. On this score, we have been analyzing two slow but significant shifts in investments. The first shift is largely unique to developed economies. As they mature and specialize, markets in the U.S., Japan, and Europe are declining in their share of the world's investment capital. However, over the last decade they have accelerated specialization in areas that have proven to reduce risk including a focus on sustainability or environmental, social, and governance (ESG). This is not the narrow application of socially responsible investing, but is more concentrated on stable growth and the importance of sound corporate governance to keep capital safe and yield a profit.

The second shift in the investment environment is simply how capital (money and investments) is allocated across all stock markets in the world. Twenty years ago, emerging markets had a tiny portion of the world's public equity. Currently at 11%, it is five-fold greater today. China, India, and greater Asia combined will likely reach 30% in just the next ten years. In part due to fears of a trade war, emerging markets are a better value today given their expected increase in global growth.

These changes in the capital markets do not necessarily mean modifications to every client portfolio. Instead, we will discuss with you any adjustments needed to reflect these shifts – and profit from them. Economically speaking, we are in a far better place than we were a decade ago. In ten more years, I believe we will be able to say the same. Thank you for your continued trust. We are humbled and honored to serve you. Have a wonderful summer!

"Make use of time, let not advantage slip." – William Shakespeare

"If this were play'd upon a stage now, I could condemn it as an improbable fiction." – William Shakespeare

Best regards,

Carl Amos Johnson, MBA, CFP®, AIF®
August 2, 2018

Q2

Quarterly Market Review

Second Quarter 2018

Market Summary

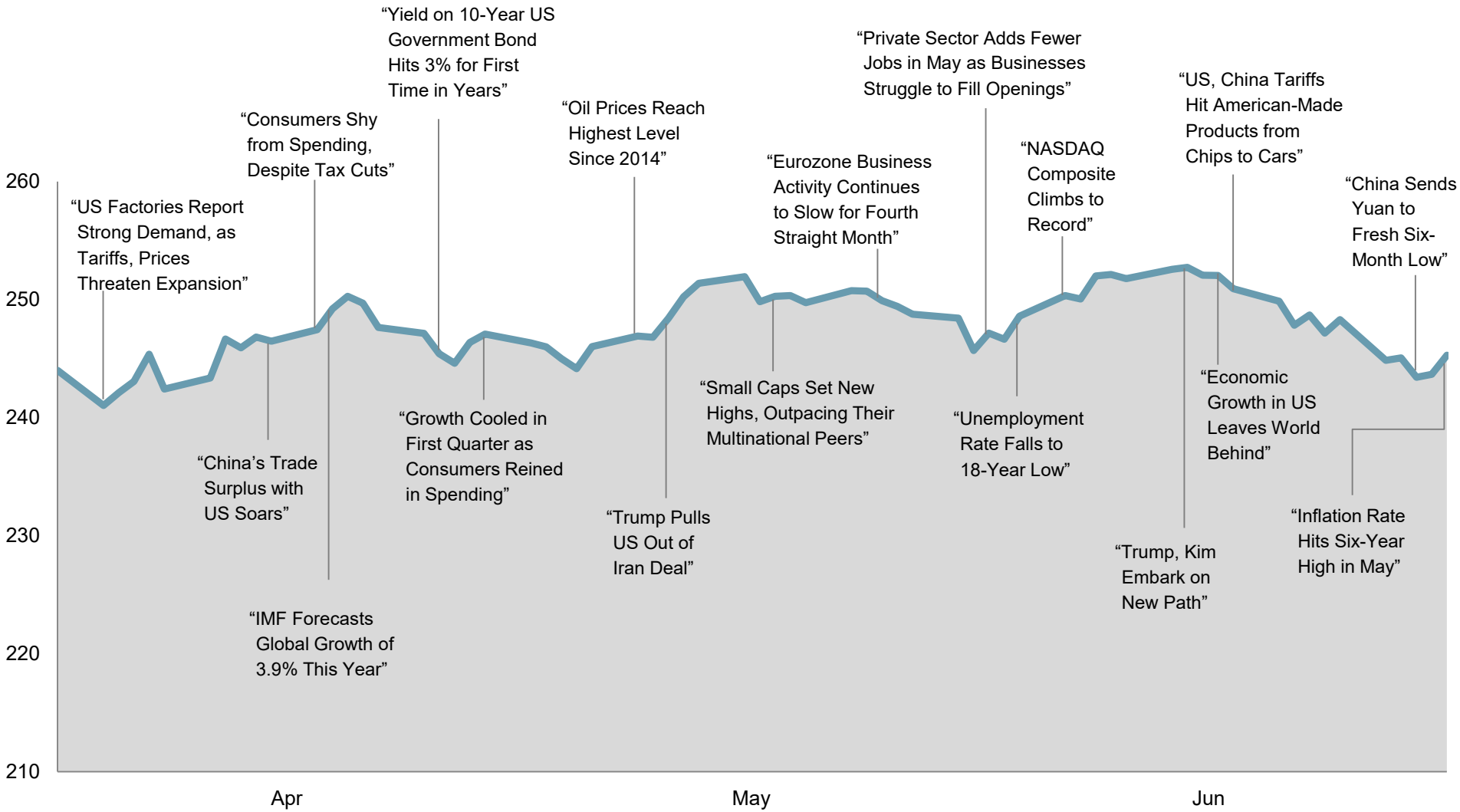
Index Returns

	US Stock Market	International Developed Stocks	Emerging Markets Stocks	Global Real Estate		US Bond Market	Global Bond Market ex US
Q2 2018	**STOCKS**					**BONDS**	
	3.89%	-0.75%	-7.96%	6.05%		-0.16%	0.48%
Since Jan. 2001							
Avg. Quarterly Return	2.0%	1.5%	3.0%	2.6%		1.1%	1.1%
Best Quarter	16.8%	25.9%	34.7%	32.3%		4.6%	4.6%
	Q2 2009	Q2 2009	Q2 2009	Q3 2009		Q3 2001	Q4 2008
Worst Quarter	-22.8%	-21.2%	-27.6%	-36.1%		-3.0%	-2.7%
	Q4 2008	Q4 2008	Q4 2008	Q4 2008		Q4 2016	Q2 2015

Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Market segment (index representation) as follows: US Stock Market (Russell 3000 Index), International Developed Stocks (MSCI World ex USA Index [net div.]), Emerging Markets (MSCI Emerging Markets Index [net div.]), Global Real Estate (S&P Global REIT Index [net div.]), US Bond Market (Bloomberg Barclays US Aggregate Bond Index), and Global Bond Market ex US (Bloomberg Barclays Global Aggregate ex-USD Bond Index [hedged to USD]).

World Stock Market Performance

MSCI All Country World Index with selected headlines from Q2 2018

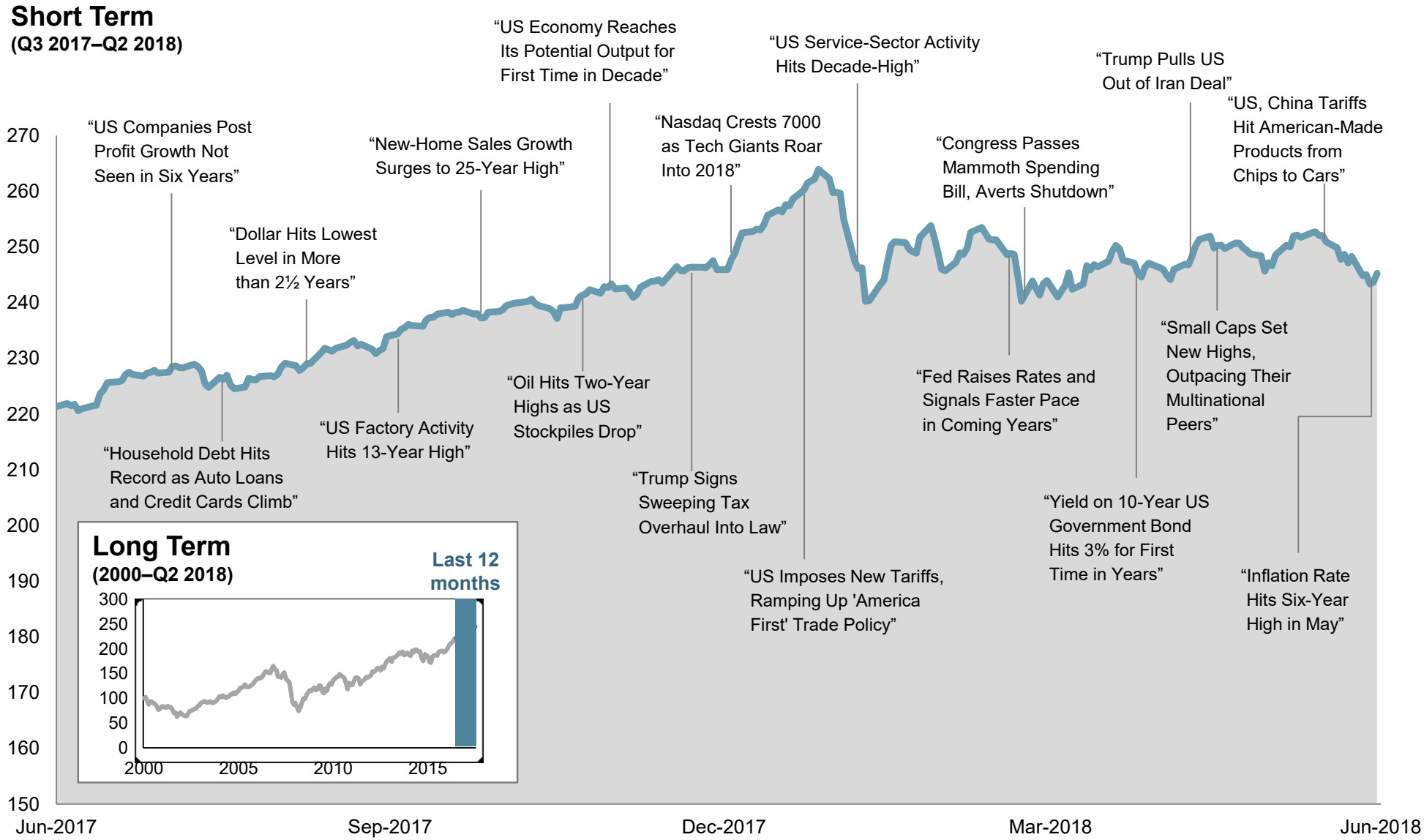


These headlines are not offered to explain market returns. Instead, they serve as a reminder that investors should view daily events from a long-term perspective and avoid making investment decisions based solely on the news.

Graph Source: MSCI ACWI Index [net div.].
It is not possible to invest directly in an index. Performance does not reflect the expenses associated with management of an actual portfolio. **Past performance is not a guarantee of future results**.

World Stock Market Performance

MSCI All Country World Index with selected headlines from past 12 months



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Graph Source: MSCI ACWI Index [net div.].
It is not possible to invest directly in an index. Performance does not reflect the expenses associated with management of an actual portfolio. **Past performance is not a guarantee of future results**.

US Stocks

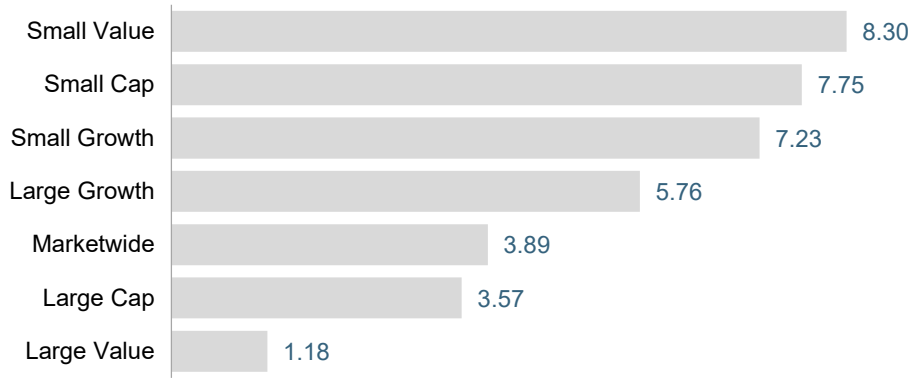
Second Quarter 2018 Index Returns

The US equity market posted a positive return, outperforming both non-US developed and emerging markets in the second quarter.

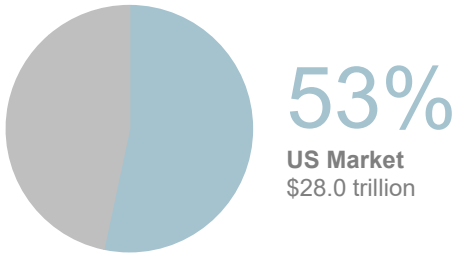
Large cap value stocks underperformed large cap growth stocks in the US; however, small cap value stocks outperformed small cap growth.

There was a positive size premium, as small cap stocks generally outperformed large cap stocks in the US.

Ranked Returns for the Quarter (%)



World Market Capitalization—US



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Small Growth	9.70	21.86	10.60	13.65	11.24
Small Cap	7.66	17.57	10.96	12.46	10.60
Large Growth	7.25	22.51	14.98	16.36	11.83
Small Value	5.44	13.10	11.22	11.18	9.88
Marketwide	3.22	14.78	11.58	13.29	10.23
Large Cap	2.85	14.54	11.64	13.37	10.20
Large Value	-1.69	6.77	8.26	10.34	8.49

Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Market segment (index representation) as follows: Marketwide (Russell 3000 Index), Large Cap (Russell 1000 Index), Large Cap Value (Russell 1000 Value Index), Large Cap Growth (Russell 1000 Growth Index), Small Cap (Russell 2000 Index), Small Cap Value (Russell 2000 Value Index), and Small Cap Growth (Russell 2000 Growth Index). World Market Cap represented by Russell 3000 Index, MSCI World ex USA IMI Index, and MSCI Emerging Markets IMI Index. Russell 3000 Index is used as the proxy for the US market. Frank Russell Company is the source and owner of the trademarks, service marks, and copyrights related to the Russell Indexes. MSCI data © MSCI 2018, all rights reserved.

International Developed Stocks

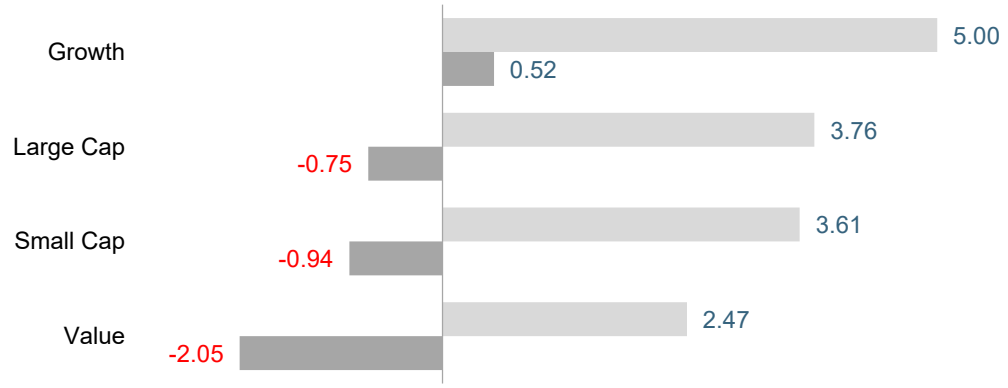
Second Quarter 2018 Index Returns

In US dollar terms, developed markets outside the US underperformed the US but outperformed emerging markets during the second quarter.

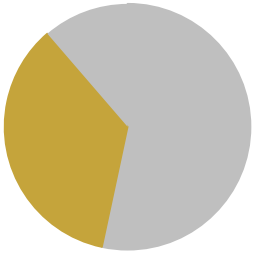
Value underperformed growth in non-US developed markets across large and small cap stocks.

Small caps underperformed large caps in non-US developed markets.

Ranked Returns (%)



World Market Capitalization—International Developed



35%

International Developed Market
$18.5 trillion

Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Growth	-1.05	9.26	5.95	7.11	2.92
Small Cap	-1.44	11.87	9.45	10.28	6.09
Large Cap	-2.77	7.04	4.87	6.23	2.63
Value	-4.53	4.80	3.70	5.27	2.29

Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Market segment (index representation) as follows: Large Cap (MSCI World ex USA Index), Small Cap (MSCI World ex USA Small Cap Index), Value (MSCI World ex USA Value Index), and Growth (MSCI World ex USA Growth Index). All index returns are net of withholding tax on dividends. World Market Cap represented by Russell 3000 Index, MSCI World ex USA IMI Index, and MSCI Emerging Markets IMI Index. MSCI World ex USA IMI Index is used as the proxy for the International Developed market.

Emerging Markets Stocks

Second Quarter 2018 Index Returns

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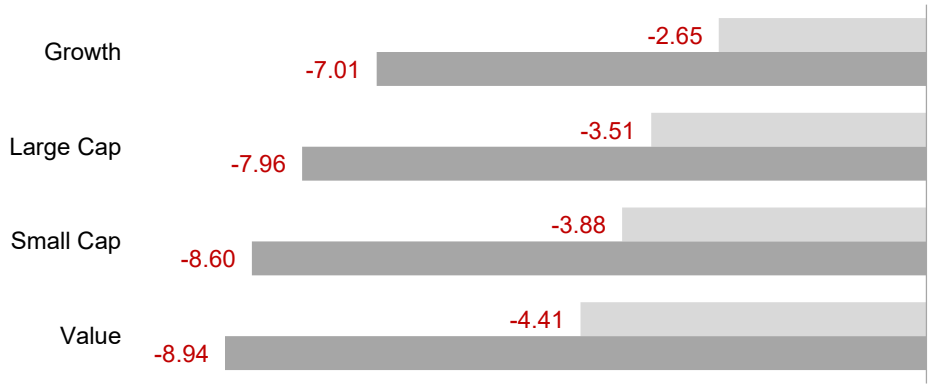
In US dollar terms, emerging markets posted negative returns in the second quarter, underperforming developed markets including the US.

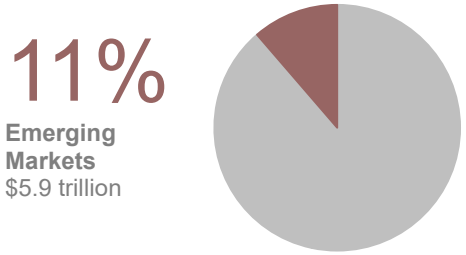
The value effect was negative in large caps; however, value and growth stocks had similar performance among small cap stocks within emerging markets.

Small caps underperformed large caps in emerging markets.

Ranked Returns (%)



World Market Capitalization—Emerging Markets



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Growth	-5.88	11.92	8.34	7.16	3.28
Large Cap	-6.66	8.20	5.60	5.01	2.26
Value	-7.47	4.28	2.76	2.77	1.14
Small Cap	-8.45	5.64	2.55	4.32	4.44

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Real Estate Investment Trusts (REITs)

Second Quarter 2018 Index Returns

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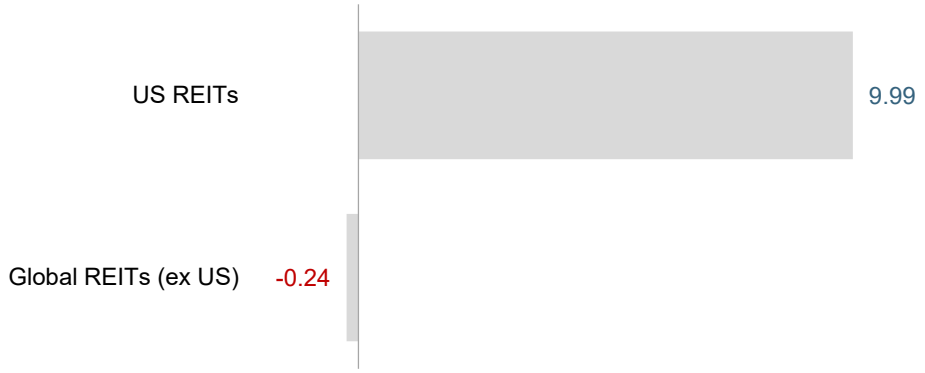
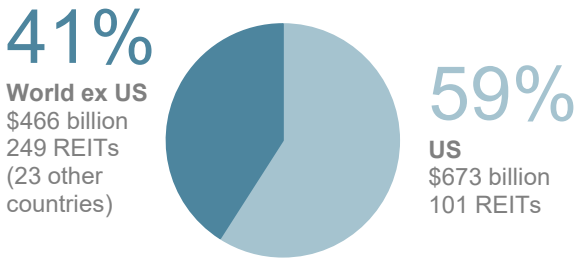
US real estate investment trusts outperformed non-US REITs in US dollar terms.

Ranked Returns (%)



Total Value of REIT Stocks



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Dow Jones US Select REIT Index	1.82	4.23	7.71	8.29	7.63
S&P Global ex US REIT Index (net div.)	-1.49	7.17	4.62	5.49	3.83

Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Number of REIT stocks and total value based on the two indices. All index returns are net of withholding tax on dividends. Total value of REIT stocks represented by Dow Jones US Select REIT Index and the S&P Global ex US REIT Index. Dow Jones US Select REIT Index used as proxy for the US market, and S&P Global ex US REIT Index used as proxy for the World ex US market.

Commodities

Second Quarter 2018 Index Returns

The Bloomberg Commodity Index Total Return gained 0.40% during the second quarter.

The energy complex led performance with Brent oil returning 16.18% and WTI crude oil 12.70%.

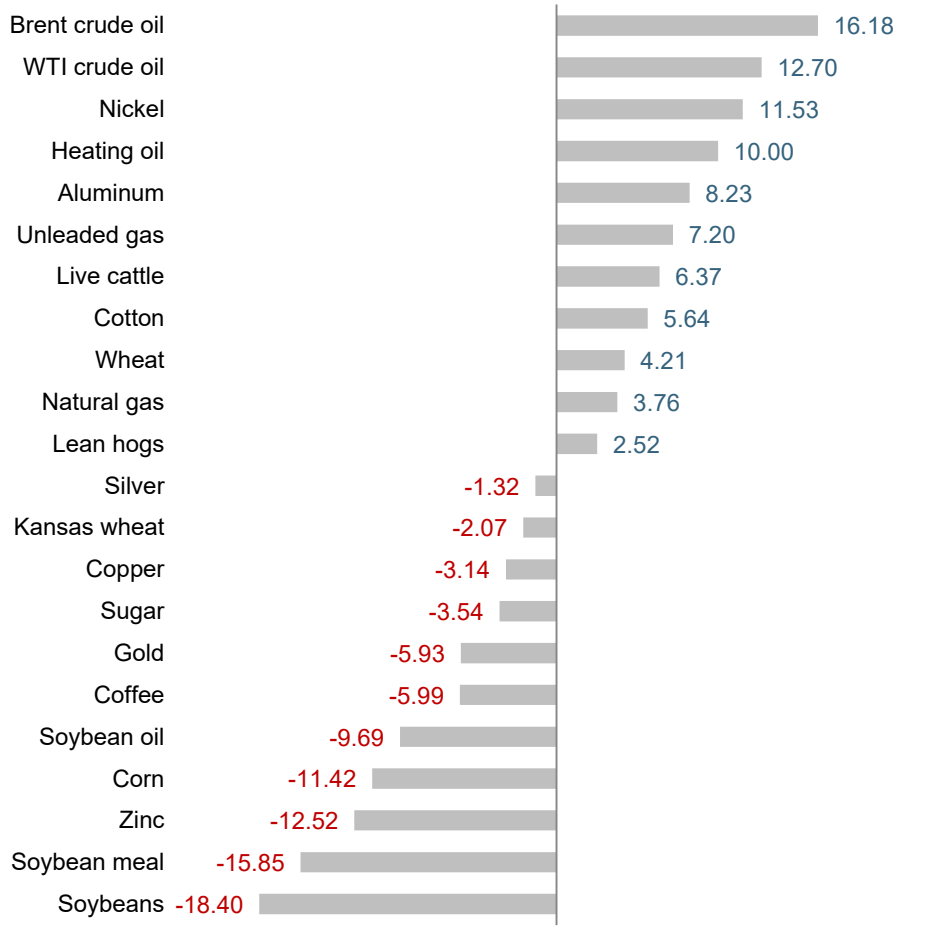
Grains was the worst-performing complex; soybeans declined 18.40%, and soybean meal lost 15.85%.

Period Returns (%)

** Annualized*

Asset Class	QTR	YTD	1 Year	3 Years*	5 Years*	10 Years*
Commodities	0.40	0.00	7.35	-4.54	-6.40	-9.04

Ranked Returns for Individual Commodities (%)



Past performance is not a guarantee of future results. Index is not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio.
Commodities returns represent the return of the Bloomberg Commodity Total Return Index. Individual commodities are sub-index values of the Bloomberg Commodity Total Return Index. Data provided by Bloomberg.

Fixed Income

Second Quarter 2018 Index Returns

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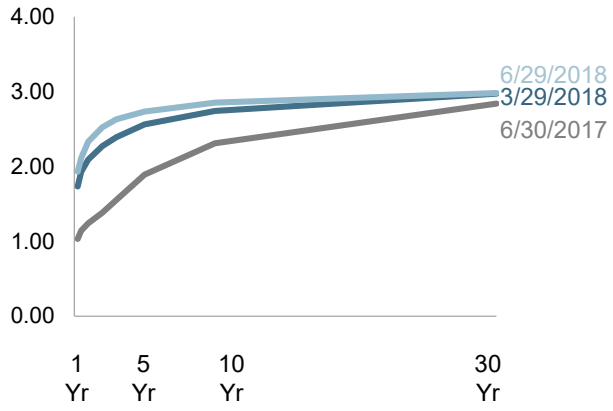
Interest rates increased in the US during the second quarter. The yield on the 5-year Treasury note rose 17 basis points (bps), ending at 2.73%. The yield on the 10-year T-note rose 11 bps to 2.85%. The 30-year Treasury bond yield climbed 1 bps to 2.98%.

The 1-month Treasury bill yield rose 14 bps to 1.77%, while the 1-year Treasury bill yield increased 24 bps to 2.33%. The 2-year Treasury note yield finished at 2.52% after increasing 25 bps.

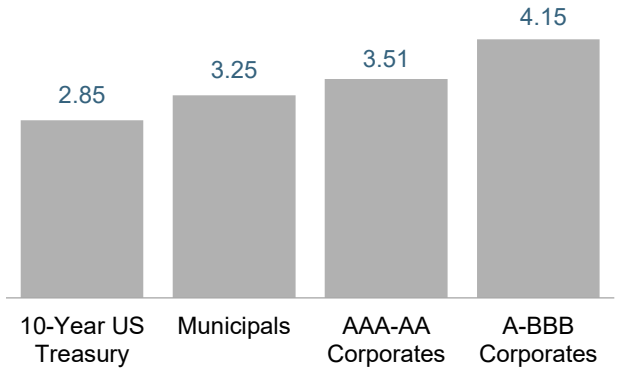
In terms of total return, short-term corporate bonds gained 0.29%, while intermediate-term corporate bonds declined 0.10%.

Short-term municipal bonds added 0.66%, while intermediate-term munis returned 0.81%. Revenue bonds performed in-line with general obligation bonds, returning 0.90% and 0.87%, respectively.

US Treasury Yield Curve (%)



Bond Yields across Issuers (%)



Period Returns (%)

* Annualize

Asset Class	QTR	YTD	1 Year	3 Years*	5 Years*	10 Years*
Bloomberg Barclays US High Yield Corporate Bond Index	1.03	0.16	2.62	5.53	5.51	8.19
Bloomberg Barclays Municipal Bond Index	0.87	-0.25	1.56	2.85	3.53	4.43
Bloomberg Barclays US TIPS Index	0.77	-0.02	2.11	1.93	1.68	3.03
ICE BofAML 3-Month US Treasury Bill Index	0.45	0.81	1.36	0.68	0.42	0.35
ICE BofAML 1-Year US Treasury Note Index	0.40	0.65	0.92	0.64	0.49	0.77
Bloomberg Barclays US Government Bond Index Long	0.26	-2.97	-0.13	3.40	4.56	6.02
FTSE World Government Bond Index 1-5 Years (hedged to USD)	0.24	0.41	0.89	1.18	1.33	2.08
Bloomberg Barclays US Aggregate Bond Index	-0.16	-1.62	-0.40	1.72	2.27	3.72
FTSE World Government Bond Index 1-5 Years	-2.66	-1.06	0.73	1.19	-0.58	0.63

One basis point equals 0.01%. **Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio.** Yield curve data from Federal Reserve. State and local bonds are from the S&P National AMT-Free Municipal Bond Index. AAA-AA Corporates represent the Bank of America Merrill Lynch US Corporates, AA-AAA rated. A-BBB Corporates represent the Bank of America Merrill Lynch US Corporates, BBB-A rated. Bloomberg Barclays data provided by Bloomberg. US long-term bonds, bills, inflation, and fixed income factor data © Stocks, Bonds, Bills, and Inflation (SBBI) Yearbook™, Ibbotson Associates, Chicago (annually updated work by Roger G. Ibbotson and Rex A. Sinquefield). FTSE fixed income indices © 2018 FTSE Fixed Income LLC, all rights reserved. ICE BofAML index data © 2018 ICE Data Indices, LLC.

E+R=O, a Formula for Success[1]

Second Quarter 2018

Grove Street Fiduciary, LLC
Wealth and Trust Advisors

Combining an enduring investment philosophy with a simple formula that helps maintain investment discipline can increase the odds of having a positive financial experience.

"The important thing about an investment philosophy is that you have one you can stick with."

David Booth
Founder and Executive Chairman
Dimensional Fund Advisors

AN ENDURING INVESTMENT PHILOSOPHY

Investing is a long-term endeavor. Indeed, people will spend decades pursuing their financial goals. But being an investor can be complicated, challenging, frustrating, and sometimes frightening. This is exactly why, as David Booth says, it is important to have an investment philosophy you can stick with, one that can help you stay the course.

This simple idea highlights an important question: How can investors, maintain discipline through bull markets, bear markets, political strife, economic instability, or whatever crisis du jour threatens progress towards their investment goals?

Over their lifetimes, investors face many decisions, prompted by events that are both within and outside their control. Without an enduring philosophy to inform their choices, they can potentially suffer unnecessary anxiety, leading to poor decisions and outcomes that are damaging to their long-term financial well-being.

When they don't get the results they want, many investors blame things outside their control. They might point the finger at the government, central banks, markets, or the economy. Unfortunately, the majority will not do the things that might be more beneficial—evaluating and reflecting on their own responses to events and taking responsibility for their decisions.

e+r=o

Some people suggest that among the characteristics that separate highly successful people from the rest of us is a focus on influencing outcomes by controlling one's reactions to events, rather than the events themselves. This relationship can be described in the following formula:

e+r=o (Event + Response = Outcome)

Simply put, this means an outcome—either positive or negative—is the result of how you respond to an event, not just the result of the event itself. Of course, events are important and influence outcomes, but not exclusively. If this were the case, everyone would have the same outcome regardless of their response.

Let's think about this concept in a hypothetical investment context. Say a major political surprise, such as Brexit, causes a market to fall (event). In a panicked response, potentially fueled by gloomy media speculation of the resulting uncertainty, an investor sells some or all of his or her investment (response). Lacking a long-term perspective and reacting to the short-term news, our investor misses out on the subsequent market recovery and suffers anxiety about when, or if, to get back in, leading to suboptimal investment returns (outcome).

To see the same hypothetical example from a different perspective, a surprise event causes markets to fall suddenly (e). Based on his or her understanding of the long-term nature of returns and the short-term nature of volatility spikes around news events, an investor is able to control his or her emotions (r) and maintain investment discipline, leading to a higher chance of a successful long-term outcome (o).

1. Jack Canfield, The Success Principles: How to Get from Where You Are to Where You Want to Be (New York: HarperCollins Publishers, 2004).

E+R=O, a Formula for Success[1]

(continued from page 16)

This example reveals why having an investment philosophy is so important. By understanding how markets work and maintaining a long-term perspective on past events, investors can focus on ensuring that their responses to events are consistent with their long-term plan.

THE FOUNDATION OF AN ENDURING PHILOSOPHY

An enduring investment philosophy is built on solid principles backed by decades of empirical academic evidence. Examples of such principles might be: trusting that prices are set to provide a fair expected return; recognizing the difference between investing and speculating; relying on the power of diversification to manage risk and increase the reliability of outcomes; and benchmarking your progress against your own realistic long-term investment goals.

Combined, these principles might help us react better to market events, even when those events are globally significant or when, as some might suggest, a paradigm shift has occurred, leading to claims that “it’s different this time.” Adhering to these principles can also help investors resist the siren calls of new investment fads or worse, outright scams.

THE GUIDING HAND OF A TRUSTED ADVISOR

Without education and training—sometimes gained from bitter experience—it is hard for non-investment professionals to develop a cogent investment philosophy. And even the most self-aware find it hard to manage their own responses to events. This is why a financial advisor can be so valuable—by providing the foundation of an investment philosophy and acting as an experienced counselor when responding to events.

Investing will always be both alluring and scary at times, but a view of how to approach investing combined with the guidance of a professional advisor can help people stay the course through challenging times. Advisors can provide an objective view and help investors separate emotions from investment decisions. Moreover, great advisors can educate, communicate, set realistic financial goals, and help their clients deal with their responses even to the most extreme market events.

In the spirit of the e+r=o formula, good advice, driven by a sound philosophy, can help increase the probability of having a successful financial outcome.

Adapted from “E+R=O, a Formula for Success,” The Front Foot Adviser, by David Jones, Vice President and Head of Financial Adviser Services, EMEA.