

Quarterly Commentary

We are passionate educators and we believe this commentary is helpful in providing a high level summary of the stock and bond markets on a quarterly basis. However, it is important that investors refrain from market timing as this can have a potentially negative impact on one's long-term wealth accumulation. Instead, investors should continue to make allocation decisions based on their unique time horizon and risk tolerances. All charts referenced herein are provided on page 3 of the commentary.

U.S. Economy

- The U.S. economy expanded at a healthy pace and gathered momentum in 2017. In fact, when compared to 2016, economic growth in each quarter of the year was slightly higher than the year before (*see Chart 1*).
- Key structural improvements have been the drivers behind the advance in economic growth, and these areas have shown further signs of strength since midyear. These include unemployment at 4.1%, above average auto sales, rising consumer confidence, and manufacturing (which hit a 6-year high at the end of 2017).
- Inflation was below the Federal Reserve's target at midyear 2017. However, it was on an upward trajectory in the 2nd half due to the rebound in energy. U.S. inflation stood at 1.6% at midyear, but rose to 2.2% as of the end of November.
- The U.S. dollar weakened meaningfully throughout the course of the year. While there was a slight rebound in September and October, the dollar continued to fall through yearend, finishing well below where it started in 2017 (*see Chart 2*).
- Oil prices declined in the first six months of 2017, but they have since rebounded due to 1) a weaker U.S. dollar, 2) a pickup in economic growth, and 3) lower inventories. The oil price index stood at 52.3 at the beginning of 2017, 46.0 at midyear, and 60.2 at yearend (*see Chart 3*).

U.S. Stocks

- A strong year in the U.S. equity market further expanded valuations. However, while stocks as a whole are more fully valued, higher prices are at least partially justified if corporate earnings remain strong. In addition, the corporate tax rate was cut to 21% from 35%, which may lead to increased dividend and share buybacks and further justification for higher stock prices. With this said, tighter valuations always increase risk for stock investors.
- The performance gap between growth and value widened since midyear. The Russell 3000 Growth Index outperformed its value counterpart by 16.4% for the year, which was up from the 9.4% gap at midyear.
- As was the case in the 1st half, small cap stocks continued to underperform large cap stocks in the last 6 months of the year. The difference between large and small was 4.3% at midyear but jumped to a 7.0% difference as of yearend 2017.
- There was a wide deviation among sector returns. The difference between the best (Technology) and worst (Energy) sector in 2017 was 39.0%. Technology, Consumer Cyclical, Basic Materials, and Healthcare were among the best performers, while Energy, Communication Services, Real Estate, and Utilities stocks have been the weakest performers.

(Continued on page 2)

Benchmark Performance	Sector	Quarter	YTD	1-Year Average	3-Year Average	5-Year Average	10-Year Average
Index : Russell 3000 TR USD	Total US Stock	6.34	21.13	21.13	11.12	15.58	8.60
Index: S&P 500 TR USD	Large Blend	6.64	21.83	21.83	11.41	15.79	8.50
Index: Russell 2000 TR USD	Small Cap Stock	3.34	14.65	14.65	9.96	14.12	8.71
Index: MSCI ACWI Ex-US IMI NR USD	Total Foreign Stock	5.23	27.81	27.81	8.38	7.22	2.20
Index: Barclays Aggregate Bond TR USD	Bond	0.39	3.54	3.54	2.24	2.10	4.01
Index: US Treasury Bill 3-Month	Stable Value	0.32	0.97	0.97	0.45	0.29	0.34

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U.S. Bonds

- In their latest December meeting, the Fed voted to increase interest rates by a quarter percentage point to a target range of 1.25% to 1.50%, marking the third time the Fed took action in 2017. With regard to future increases, the expectation is relatively the same next year with 3 increases anticipated. However, Federal Reserve Chairwoman, Janet Yellen, will be replaced in 2018, which provides a degree of uncertainty with regard to Fed action.
- Though the Fed raised rate targets, there was actually a market driven decrease in rates during 2017. The 10-year U.S. Treasury rate stood at 2.45% at the beginning of the year, fell to 2.05% in September, and finished at 2.40% at yearend. From a return standpoint, the Bloomberg Barclays U.S. Aggregate bond index gained 3.5% in 2017.
- Amid a persistent low interest rate environment, the demand for riskier sectors in fixed income remains high, which has contributed to strong performance within Corporate bonds (specifically High-Yield). On the other hand, high-quality Treasury Inflation Protected Securities (TIPS) and U.S. Treasuries have been negatively impacted as inflation has been muted and investors have sought more higher-yielding fare. This has been the case in recent years (see Chart 4).

Foreign Economies

- Foreign economies continue to show signs of improvement on several fronts. Coupled with improving fundamentals in the U.S., it appears as though the global economy is collectively moving in a positive direction in a way not seen in years - a key driver of global equity performance.
- According to the Global Purchasing Managers' Index (PMI), manufacturing around the globe is quite strong (96% of countries scored a reading above 50). *A reading above 50 indicates expansion, while a reading below 50 indicates a contraction.*
- The Eurozone showed its fastest pace of expansion since the region's economies slipped back into a recession in 2011 during the European Debt Crisis. Unemployment fell to 8.8% at yearend from its peak of 12.1%, and loan demand, consumer spending, and wage growth are rising.
- Japan has also maintained a healthy footing as its unemployment has been steadily declining since 2010 and is now at 2.7%. A rebound in economic growth has been a key driver behind these results and Japanese GDP continues to land above its 20-year average.
- Broadly speaking, a rebound in commodity prices and a falling U.S. dollar provided support for a strong period in Emerging Market economic and market performance.
- As China has continued to transition from an economy that was driven primarily by government investment to more of an emphasis on the consumer, it seems as though there have been no material impacts. Thus far, their economy has continued to expand at a healthy pace.

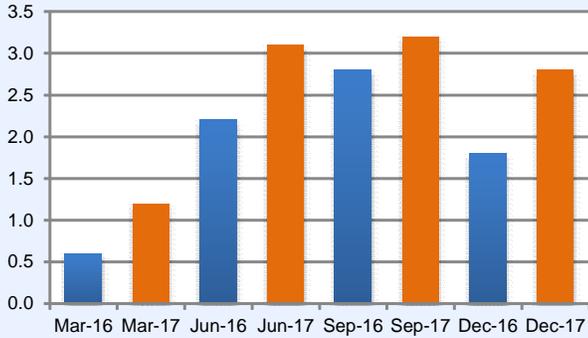
Foreign Stocks

- U.S. and Japanese corporate earnings are at all-time highs. However, European and Emerging Markets earnings are still well below their peak, which may indicate there is further room to run in the equity markets of these regions relative to the U.S. and Japan. Of course, many of these countries are still in a fragile state and economic improvements will need to persist to support further advances.
- Foreign stocks outperformed by a wide margin in the 1st half of 2017. However, while foreign stocks continued to outperform domestic in the 2nd half, the degree to which this occurred was much more modest. All told, foreign stocks outpaced their domestic counterparts by 6.7% in 2017, which has helped to narrow the gap between domestic and foreign stock performance since 2010 (see Chart 5).
- Within foreign markets, growth outperformed value by a wide margin, as was the case in the U.S. However, opposite of what occurred on the domestic front, smaller cap stocks outperformed large cap stocks by 5.0% in 2017.
- As macroeconomic concerns have abated, global stock market correlations have fallen to a multi-year low (see Chart 6) amid an improving economic picture and investors' refocusing on fundamentals. However, NAFTA re-negotiations, geopolitical tension in North Korea and the Middle East, and certain elections that are set to occur in 2018 could cause spouts of volatility.
- Emerging Markets (EM) equities advanced strongly in 2017 with a 36.8% gain through yearend. The year-to-date performance gap between EM and Developed Market stocks was 10.7%, up from 3.9% midyear.

Foreign Bonds

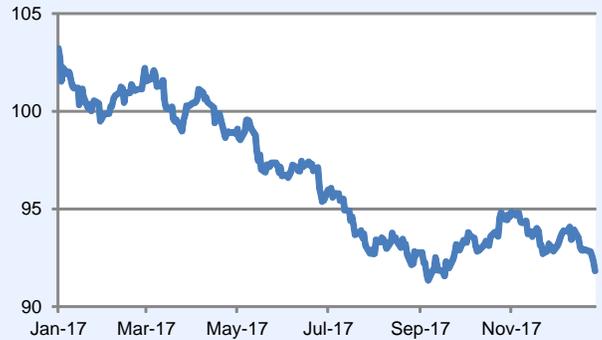
- As economic data continue to gradually improve, there has been an increasing level of discussion that foreign central banks will start to normalize monetary policy and taper their stimulative efforts. This was evident in 2017 as all of the top 10 developed market central banks implemented interest rate hikes during the year without any cuts. This is the first time this has occurred in a decade. However, given the continued fragility (even after improvement) of many foreign economies, there is a high likelihood that current and future measures will continue to be taken cautiously.
- Foreign bonds continued to outpace domestic bonds in the 2nd half. The Bloomberg Barclays Global Aggregate ex-U.S. Index finished 7.0% ahead of the domestic Bloomberg Barclays U.S. Aggregate Bond Index in 2017.
- Within the global fixed income universe, Emerging Markets bonds continue to be the top-performing sector as the demand for risk assets continues to remain strong. This has generally been the case since the Financial Crisis.

Chart 1 - U.S. Real GDP



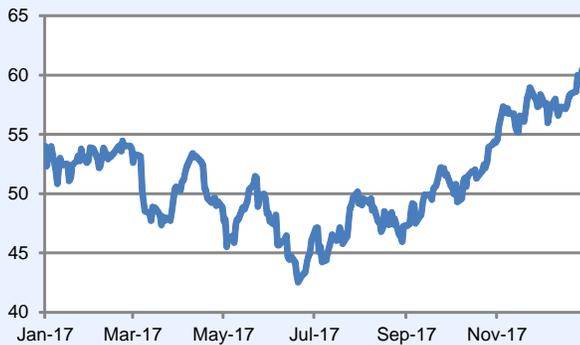
Source: U.S. Bureau of Economic Analysis. Represents seasonally adjusted annual rates. 4th quarter 2017 GDP is a projection from the Federal Reserve Bank of Atlanta, but this may change as accurate and official data are received.

Chart 2 - U.S. Dollar



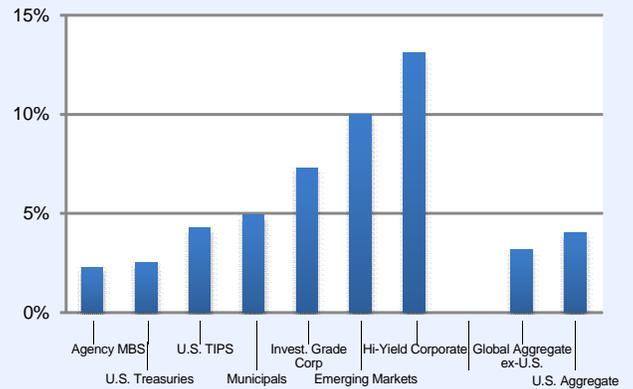
Source: CNBC. Represents the data from the DXY U.S. Dollar Currency Index.

Chart 3 - Oil Prices



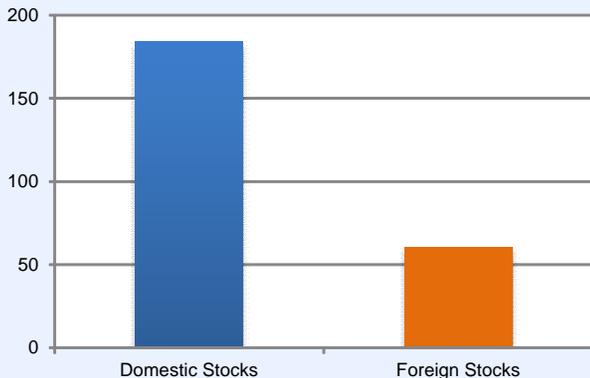
Source: CNBC. Represents West Texas Intermediate (WTI) oil price data.

Chart 4 - 2017 Fixed Income Returns



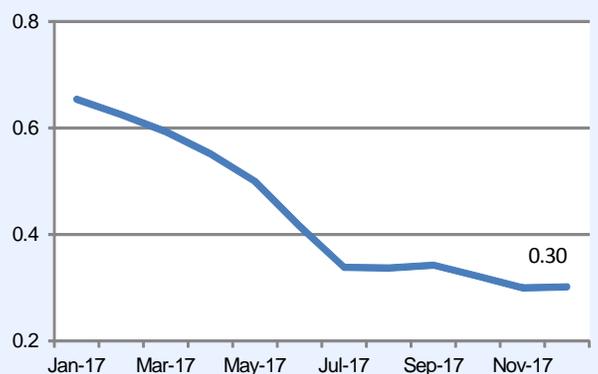
Source: Morningstar Direct. Represents annualized fixed income returns by sector, as well as the broad domestic and foreign bond markets, since the market bottom on March 9, 2009.

Chart 5 - Domestic vs. Foreign



Source: Morningstar Direct. Represents the cumulative returns for the broad domestic and foreign stock markets since January 1, 2010.

Chart 6 - Global Correlations



Source: Morningstar Direct. Global equity market correlations were calculated based on rolling 1-year correlations of 30 countries, including the major international economies and the U.S., ending 12/31/17.



ABC Company 401(k) Retirement Plan

Category	Fund Name	Manager	Mngr Tenure	Ticker	Exp Ratio	Web site	Quarter	YTD	1-Yr Avg	3-Yr Avg	5-Yr Avg	10-Yr Avg
Large Growth	Large Growth Fund	XXXXXX X. XXXXXXXXX	27.3	XXXXX	0.68	www.xxxxxxx.com	6.75	32.26	32.26	13.33	16.43	8.96
Large Blend	Large Blend Index Fund	XXXXXX X. XXXXXXXXX	Index	XXXXX	0.04	www.xxxxxxx.com	6.64	21.79	21.79	11.38	15.75	8.49
Large Blend	Large Blend Fund 1	XXXXXX X. XXXXXXXXX	24.8	XXXXX	0.31	www.xxxxxxx.com	6.71	23.72	23.72	13.14	15.86	8.33
Large Blend	Large Blend Fund 2	XXXXXX X. XXXXXXXXX	17.8	XXXXX	0.89	www.xxxxxxx.com	5.98	21.14	21.14	11.26	16.09	11.01
Large Value	Large Value Fund	XXXXXX X. XXXXXXXXX	26.0	XXXXX	0.52	www.xxxxxxx.com	5.75	18.33	18.33	11.08	16.29	7.71
Mid Growth	Mid Growth Fund	XXXXXX X. XXXXXXXXX	16.9	XXXXX	1.04	www.xxxxxxx.com	7.22	27.31	27.31	8.45	12.42	9.40
Mid Value	Mid Value Fund	XXXXXX X. XXXXXXXXX	16.2	XXXXX	1.16	www.xxxxxxx.com	4.72	12.36	12.36	7.44	11.32	8.86
Small Growth	Small Growth Fund	XXXXXX X. XXXXXXXXX	Index	XXXXX	0.07	www.xxxxxxx.com	5.75	21.92	21.92	9.59	13.60	9.32
Small Value	Small Value Fund	XXXXXX X. XXXXXXXXX	24.1	XXXXX	1.21	www.xxxxxxx.com	4.41	13.65	13.65	9.90	12.30	7.98
Foreign Large Growth	Foreign Large Growth Fund	XXXXXX X. XXXXXXXXX	26.1	XXXXX	0.50	www.xxxxxxx.com	4.23	31.17	31.17	9.66	9.21	3.90
Foreign Large Value	Foreign Large Value Fund	XXXXXX X. XXXXXXXXX	15.0	XXXXX	0.95	www.xxxxxxx.com	3.86	23.16	23.16	0.10	0.99	-0.01
Foreign S/M Blend	Foreign Small Blend Fund	XXXXXX X. XXXXXXXXX	18.0	XXXXX	0.41	www.xxxxxxx.com	5.50	38.77	38.77	13.97	13.37	5.49
Moderate Allocation	Moderate Allocation Fund	XXXXXX X. XXXXXXXXX	Index	XXXXX	0.07	www.xxxxxxx.com	3.96	13.89	13.89	7.58	10.09	7.14
Interm-Term Bond	Intermediate Term Bond Fund 1	XXXXXX X. XXXXXXXXX	3.3	XXXXX	0.46	www.xxxxxxx.com	0.11	5.13	5.13	2.80	2.21	5.23
Interm-Term Bond	Intermediate Term Bond Fund 2	XXXXXX X. XXXXXXXXX	29.0	XXXXX	0.43	www.xxxxxxx.com	0.48	4.36	4.36	3.09	3.07	5.01
Stable Value	Stable Value Fund	XXXXXX X. XXXXXXXXX	NA	XXXXX	NA	www.xxxxxxx.com	0.74	3.00	3.00	3.00	3.00	3.22
Index Funds												
Large Blend	Large Blend Index Fund	XXXXXX X. XXXXXXXXX	Index	XXXXX	0.04	www.xxxxxxx.com	6.34	21.17	21.17	11.08	15.55	8.72
Foreign Large Blend	Foreign Large Blend Index Fund	XXXXXX X. XXXXXXXXX	Index	XXXXX	0.11	www.xxxxxxx.com	4.88	27.55	27.55	8.53	7.12	1.92
Interm-Term Bond	Intermediate Term Bond Index Fund	XXXXXX X. XXXXXXXXX	Index	XXXXX	0.05	www.xxxxxxx.com	0.41	3.57	3.57	2.18	2.02	3.95

Data Source: Morningstar, December 31, 2017; www.Morningstar.com; fund family Web sites; direct communication with fund families. Note: Past performance does not guarantee future returns. Investment returns and principal values vary and investors may realize a gain or loss when shares are sold. Mutual fund performance shown is after the deduction of all applicable fund operational expenses and fees (net). Mutual fund returns and index returns are provided by Morningstar. The total return is calculated assuming a purchase of the fund shares at Net Asset Value (NAV). More information on funds may be obtained by visiting fund Web sites or by requesting fund prospectuses from your Plan contact.

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