

Q2 2018 Tactical Update

May 1, 2018

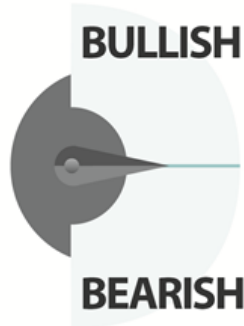
Please refer to Appendix – Important Disclosures.

In this piece, we provide a series of near-term tactical calls within the context of the current message from the weight of the evidence and our other tactical indicators. Operating from this premise, we offer a series of tactical allocation calls, beginning with a macro call on stocks versus bonds versus cash. On the next page, these calls are further distilled. For example, we make distinctions from a size, style and sector perspective for domestic equities, and suggest tilts toward or away from the various satellite asset classes. These calls are made in light of the long-term outlook and summarize our expectations for the coming quarter.

Weight of the Evidence Summary:

MACRO FACTORS (WHAT COULD HAPPEN):

FED POLICY



ECONOMIC FUNDAMENTALS



VALUATIONS



MARKET FACTORS (WHAT IS HAPPENING):

SENTIMENT



SEASONAL PATTERNS AND TRENDS



BREADTH



Tactical Investment Decision	Baird's Call ¹	Date of First Call ²	Level of Conviction ³	Rationale
Stocks vs. Bonds vs. Cash?	Cash over Stocks & Bonds	Q2 18	High	<ul style="list-style-type: none"> Weight of the evidence has turned neutral, arguing for a more cautious outlook on stocks. With bond yields rising, investors might want to endure heightened volatility by holding elevated levels of cash.

¹ Tactical over- or under-weight relative to Baird's strategic asset allocation models. Please ask your Baird advisor for more information on the strategic model most applicable to you.

² Date when Baird first made this call.

³ Level of conviction in the tactical investment call: low, medium, high.

Tactical Investment Decision	Baird's Call ¹	Date of First Call ²	Level of Conviction ³	Notes
Domestic Stocks: Size	Mid-Caps Over Large-Caps & Small-Caps	Q2 18	Medium	<ul style="list-style-type: none"> Industry group relative strength trends show move away from large-cap leadership. Small-caps face seasonal headwinds heading into mid-term elections.
Domestic Stocks: Style	Value Over Growth	Q2 18	Low	<ul style="list-style-type: none"> Sector-level leadership rotation favors value focus. Price and momentum trends across capitalization levels show value gaining strength.
Domestic Stocks: Sector	Energy Utilities Health Care	Q1 18 Q2 18 Q2 18	Medium	<ul style="list-style-type: none"> Energy has moved to the top of our relative strength rankings. With recent leaders starting to lag, interest in defensive areas could increase.
Global Stocks: Region	Asia ex Japan United Kingdom	Q2 18 Q2 18	Medium	<ul style="list-style-type: none"> United Kingdom is breaking out of a four-year down-trend versus the rest of the world. Asia ex Japan benefits from global growth and commodity demand.
Global Stocks: Developed vs. Emerging Markets	Developed Markets	Q2 18	Medium	<ul style="list-style-type: none"> Emerging Markets are a crowded trade and are seeing some price and momentum weakness relative to Developed Markets.
Global Developed Stocks: Domestic vs. International	International	Q3 17	Low	<ul style="list-style-type: none"> Multi-year trend favoring domestic leadership is being tested after a lengthy period of consolidation. Short-term momentum trend shifting in favor of international.
Bonds: Treasury vs. Spread Product	Spread Product	Q3 16	Low	<ul style="list-style-type: none"> Trends continue to favor high-grade corporate bonds versus treasuries.
Bonds: Intermediate vs. Short-Term	Short-Term	Q4 17	Medium	<ul style="list-style-type: none"> Bond yields are breaking to the upside with a momentum tailwind. With yield curve having flattened, yield benefits of moving out on the curve are diminished.
Bonds: High-Grade vs. High-Yield	High-Grade	Q4 17	Low	<ul style="list-style-type: none"> Longer-term trend shows bias toward high-yield, but within this trend, high grade could see period of relative leadership. Relative lack of liquidity in high yield market could be a negative if volatility picks up in second quarter.
International Real Estate	Bullish	Q2 17	Medium	<ul style="list-style-type: none"> Real Estate stumbled in early 2018, but price and momentum trends are now improving.

Commodities	Bullish on Commodities	Q1 17	High	<ul style="list-style-type: none"> Commodities benefitting from strong global demand. Stock market volatility and rising bond yields making commodity exposure more attractive.
Currencies	Neutral on Dollar	Q2 18	Medium	<ul style="list-style-type: none"> Rally off of early 2018 lows has carried dollar through resistance at the down-trend off of late 2016 peak. Need to see further evidence of improvement to suggest uptrend is emerging.
Gold	Overweight	Q4 17	Medium	<ul style="list-style-type: none"> Gold has been making a series of higher lows, but has been unable to break out to a new high.
Hedges	NASDAQ 100	Q2 18	High	<ul style="list-style-type: none"> Recent high-fliers have cooled, with recent rally attempts failing to improve the deteriorating momentum backdrop. Lack of short-interest reflects still-elevated complacency among investors.

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Model Portfolio	Mix: Stocks / (Bonds + Cash)	Risk Tolerance	Strategic Asset Allocation Model Summary
All Growth	100 / 0	Well above average	Emphasis on providing aggressive growth of capital with high fluctuations in the annual returns and overall market value of the portfolio.
Capital Growth	80 / 20	Above average	Emphasis on providing growth of capital with moderately high fluctuations in the annual returns and overall market value of the portfolio.
Growth with Income	60 / 40	Average	Emphasis on providing moderate growth of capital and some current income with moderate fluctuations in annual returns and overall market value of the portfolio.
Income with Growth	40 / 60	Below average	Emphasis on providing high current income and some growth of capital with moderate fluctuations in the annual returns and overall market value of the portfolio.
Conservative Income	20 / 80	Well below average	Emphasis on providing high current income with relatively small fluctuations in the annual returns and overall market value of the portfolio.
Capital Preservation	0 / 100	Well below average	Emphasis on preserving capital while generating current income with relatively small fluctuations in the annual returns and overall market value of the portfolio.

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