

May 2018 Commentary and Strategy Review

About the Strategy

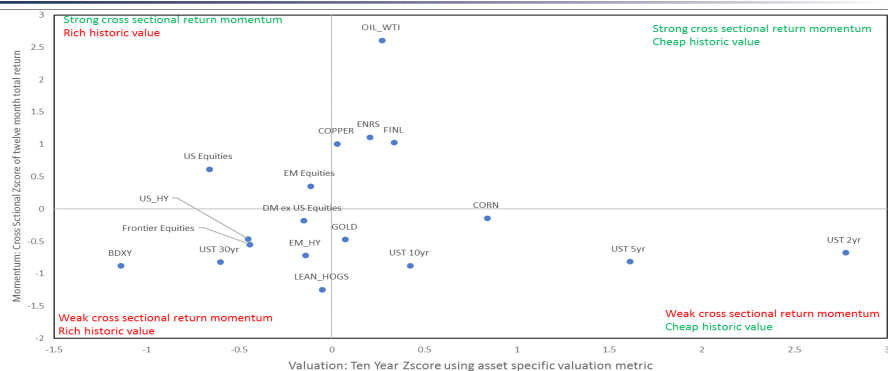
The Global All Asset Strategy (“GAA”) provides market exposure across the six major assets -equities, sovereign fixed income, commodities, currencies, credit fixed income, and real estate- via exchange-traded funds. The Innealta Capital investment team creates three different portfolios – Conservative, Moderate, and Growth – that have varying risk levels, based on the GAA framework. The investment team manages each portfolio relative to a unique, balanced benchmark. For example, Innealta’s Investment Team manages the Global All Asset Moderate strategy (“GAAM”) to a balanced benchmark of 40% Bloomberg Barclays Global Aggregate Bond Index, 24% MSCI All Country World ex U.S. Index, 21% Russell 3000 Index, 9% S&P GSCI Total Return Index, and 6% Dow Jones Global Select Real Estate Securities Index. The benchmark reflects the desired average weight of each asset class through a business cycle. Innealta Capital utilizes a proprietary quantitative framework that combines traditional corporate fundamental, macroeconomic and behavioral data to produce risk and return forecasts. The investment team then employs those forecasts along with trading optimization techniques and portfolio design research to create a unique portfolio, that, in our opinion, best suits a client’s risk-adjusted goals across all major asset classes.

Outlook

Momentum and valuation are two of the many core analytical techniques utilized in Innealta Capital’s investment framework to evaluate opportunities within financial markets. Empirical research has shown that return streams based on momentum and value strategies tend to provide positive alpha and have a low correlation with one another. Figure 1 applies a valuation metric, calculated as a z-score based on its unique history and a momentum metric, calculated a cross-sectional z-score using twelve-month total return, across the multiple assets classes. In calculating valuation z-scores, we used next twelve months’ price-to-earnings ratio for equities, yield-to-worst for fixed income, and price for commodities.

The figure has quite a few takeaways. First, equity investments in the Energy and Financials sectors appear attractive from both a momentum and valuation perspective. Both sectors have not recouped valuation levels previously obtained over the past 10 years. West Texas Intermediate Crude (“OIL_WTI”) has shown strong returns over the past twelve months, but is still well below the \$140 per barrel achieved in 2007. Investments in U.S. equities, Emerging Market equities, and Copper represent a trade-off between strong return momentum and above average valuations. We believe the momentum justifies the valuation, provided growth remains above average. Short-dated US Treasuries, particularly two-year Treasuries, appear attractive on a valuation basis. Yields on short-dated US Treasuries have increased for over two years, as the FED raises short-term policy rates. A large percentage of the 2018 and expected 2019 rate increases have already been priced into the market. We believe that this sector of fixed income offers relatively high return per unit of risk, especially when constructing a portfolio to manage volatility. Despite the strength in the past few months, we view the US Dollar as overvalued based on this framework.

FIGURE 1: Cross-Sectional Value and Momentum Analysis



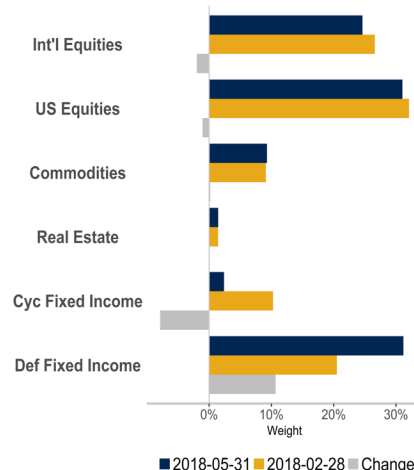
Source: Innealta Capital using Bloomberg data. Time frame 05/31/2008 to 05/31/2018, frequency weekly. “US Equities” refers to the S&P 500 index. “EM Equities” refers to the MSCI EM index. “DM ex US Equities” refers to the MSCI World ex USA index. “Frontier Equities” refers to the MSCI Frontier Emerging Market index. “UST 2yr” refers to the Bloomberg Barclays US Treasury Bellwethers 2 Year TR Index. “UST 5yr” refers to the Bloomberg Barclays US Treasury Bellwethers 5 Year TR Index. “UST 10yr” refers to the Bloomberg Barclays US Treasury Bellwethers 10 Year TR Index. “UST 30yr” refers to the Bloomberg Barclays US Treasury Bellwethers 30 Year TR Index. “US_HY” refers to the Bloomberg Barclays US Corporate High Yield Total Return Index. “EM_HY” refers to the Bloomberg Barclays Emerging Market High Yield Index. “OIL_WTI” refers to the generic front-month contract of West Texas Intermediate crude oil futures. “GOLD” refers to the generic front-month contract of gold, 100 ounce futures. “LEAN_HOGS” refers to the generic front-month contract of lean hog futures. “CORN” refers to the generic front-month contract of corn futures. “ENRS” refers to the S&P 500 Energy Select Sector index. “FINL” refers to the S&P 500 Financials Select Sector index. “BDX” refers to the Bloomberg Dollar Spot index. “COPPER” refers to the generic front-month contract of copper futures.

Strategy Statistics

	Port	Bench
Alpha (%)	0.94	0.0
Beta (%)	0.98	1.0
R-Squared (%)	91.69	100.0
Std.Dev (%)	8.83	8.64

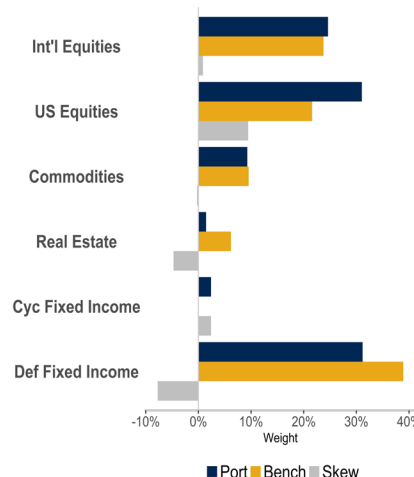
SOURCE: Innealta Capital using data from Bloomberg for the Global All Asset - Moderate Portfolio. Data from 12.31.2009 to 05.31.2018. The benchmark is 21% Russell 3000 Index / 24% MSCI ACWI ex US NR Index / 6% Dow Jones Global Select Real Estate Securities NR Index / 9% S&P GSCI Total Return CME / 40% Bloomberg Barclays Global Aggregate Bond NR Index. Inception date for the portfolio is December 31, 2009.

Portfolio Changes



SOURCE: Innealta Capital using data from Innealta Capital and Bloomberg as of 05.31.2018.

Portfolio Skews



SOURCE: Innealta Capital using data from Innealta Capital as of 05.31.2018.

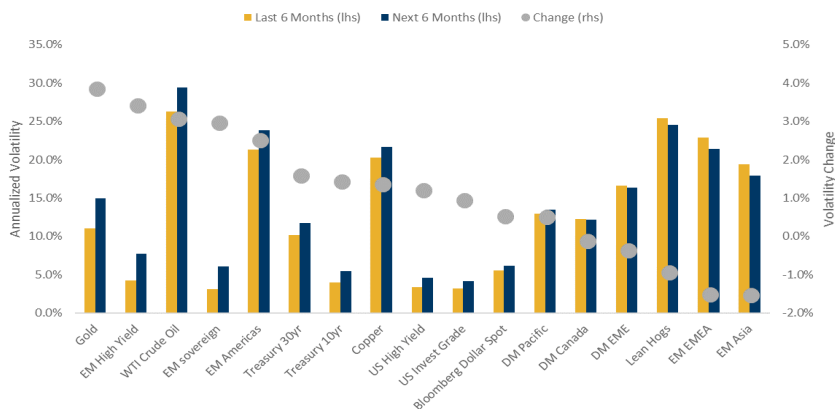
Performance

Broad asset classed performance during May showed diverging trends as U.S. equities outperformed, while Emerging Market equities underperformed. Although trade war tensions declined, and the Bloomberg Dollar Spot index declined, country-specific concerns erupted in Emerging Market countries. In Brazil, transportation strikes due to rising gasoline prices and calls for a new government triggered equity weakness as the MSCI Brazil USD index fell 16.53%, the largest decline since September 2014. In Turkey, rising inflation rates and the president's desire to keep interest rates low handcuffed the Turkish Central Bank from reacting quickly, in our opinion. Simultaneously the country's deteriorating current account situation and weakening consumer confidence contributed to its depreciating currency and declining equity market. In May, the MSCI Turkey index declined 3.56% after declining over 9% in April. Despite the weakness in Emerging Market equities, we still find them attractive relative to the opportunity set. With global inflation below 2% and long-term yields on average around 3% for developed markets, the macroeconomic and earnings growth in emerging markets appears attractive.

During May, the Innealta Capital Global All-Asset Moderate portfolio returned 0.66%, while its blended benchmark returned -0.05%. The portfolio benefitted from overweight allocations, relative to its benchmark, in U.S. equities, and an underweight allocation, relative to its benchmark, in defensive fixed income. The top two contributors to portfolio performance during the month were investments in small capitalization U.S. equities and broad market U.S. equities, while the top two detractors to the portfolio performance were European equities and Frontier Market equities. The Innealta Capital investment committee did not rebalance the portfolio during May.

Looking forward to the next six months, we are anticipating modest changes in market volatility. We see a pickup in market volatility across Emerging Market Americas equities, Gold, Emerging Market High-Yield debt, Emerging Market Sovereign USD denominated debt, and crude oil. We anticipate small declines in market volatility for Emerging Market Europe, Middle East, and Africa ("EM EMEA") equities, Emerging Market Asia ("EM Asia") equities, and Developed Market Europe and Middle East ("DM EME") equities. Finally, the expected increase in U.S. Treasury volatility, combined with the flattening of the U.S. Treasury yield curve, further reinforces our view that short-dated Treasuries offer attractive returns per unit risk.

FIGURE 2: Benchmark Performance, Trailing 3-Month



Source: Source: Innealta Capital using Bloomberg data. Time frame 05/25/2008 to 05/25/2018, frequency weekly. "GOLD" refers to the generic front-month contract of gold, 100 ounce futures. "EM_HY" refers to the Bloomberg Barclays Emerging Market High Yield Index. "OIL_WTI" refers to the generic front-month contract of West Texas Intermediate crude oil futures. "EM Sovereign" refers to the Bloomberg Barclays EM USD Aggregate Total Return Index. "EM Americas" refers to the MSCI EM Americas index. "EM Asia" refers to the MSCI EM Asia Index. "EM EMEA" refers to the MSCI EM Europe, Middle East and Africa index. "DM Canada" refers to the MSCI Canada index. "DM EME" refers to the MSCI Europe and Middle East index. "DM Pacific" refers to the MSCI Pacific index. "Treasury_10yr" refers to the Bloomberg Barclays US Treasury Bellwethers 10 Year TR Index. "Treasury_30yr" refers to the Bloomberg Barclays US Treasury Bellwethers 30 Year TR Index. "US_High Yield" refers to the Bloomberg Barclays US Corporate High Yield Total Return Index. "LEAN_HOGS" refers to the generic front-month contract of lean hog futures. "Copper" refers to the generic front-month contract of copper futures. "ENRS" refers to the S&P 500 Energy Select Sector index.

Top Contributors

1. iShares S&P SmallCap 600 Index ETF (IJR)
2. Vanguard Total Stock Market ETF (VTI)

Bottom Contributors

1. Vanguard FTSE Europe ETF (VGK)
2. iShares MSCI Frontier 100 ETF (FM)

SOURCE: Innealta Capital using Innealta Capital data from 02.28.2018 to 05.31.2018.

Strategy Performance

	Gross (%)	Net (%)	Benchmark(%)
1-Month	0.66	0.66	-0.04
3-Month	1.05	0.84	0.27
YTD	0.71	0.17	0.36
1-Year	10.44	9.31	8.57
3-Year	5.8	4.61	4.42
5-Year	5.38	4.25	4.16
Inception	7.15	6.08	5.23

SOURCE: Innealta Capital using data as of 05.31.2018. The benchmark is 21% Russell 3000 Index / 24% MSCI ACWI ex US NR Index / 6% Dow Jones Global Select Real Estate Securities NR Index / 9% S&P GSCI Total Return CME / 40% Bloomberg Barclays Global Aggregate Bond NR Index. Inception date for the portfolio is December 31, 2009.

Disclosures & Important Information

The U.S. Dollar is the currency used to express performance. The strategy includes portfolios charged bundled or wrap fees and portfolios charged transaction fees or trading costs. Bundled fee portfolios pay a fee based on a percentage of assets under management in place of a transaction fee. They include the advisor's fee and, in most cases, also include a fee for investment management and portfolio monitoring. Live returns are presented net of management fees, gross of withholding taxes on any dividends, interest or capital gains, and include the effects of trading costs and reinvestment of all income. Net of fee performance was calculated using actual management fees charged to the client. Gross returns are shown as supplemental information, include the effects of the reinvestment of all income, and are stated gross of all fees except for transaction fees, when charged.

Past performance is no guarantee of future results.

Investing involves risk, principal loss is possible, and there can be no assurance that investment objectives will be achieved. Past performance is not indicative of future results. Exchange traded funds (ETFs) are subject to risks similar to those of stocks, such as market risk, and investors who have their funds invested in accordance with the portfolios may experience losses. Additionally, fixed income (bond) ETFs are subject to interest rate risk, which is the risk that debt securities in a portfolio will decline in value because of increases in market interest rates. Investments in foreign investments may incur greater risks than domestic investments. For more information on the risks associated with investment in ETFs, please refer to AFAM Capital's Form ADV Part 2A.

Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request. Actual investment management fees will vary, beginning at 1.5% per annum. Our full management fee schedule is described in more detail in AFAM's Form ADV Part 2A.

Alpha is a measure of the difference between a portfolio's actual returns and its expected performance, given its level of risk as measured by beta. **Beta** is a measure of volatility, or systematic risk, of a portfolio in comparison to a benchmark. A beta greater than one indicates more volatility, while a beta less than one indicates less volatility than the relevant benchmark. **Annualized Standard Deviation** is a measure of the dispersion of investment returns from the mean. A higher standard deviation indicates higher volatility. **R Squared** is a measure of how close the relationship is between a portfolio and its benchmark.

DEF Fixed Income: Defensive Fixed Income refers to any debt type contained within the Bloomberg Barclays U.S. Aggregate Bond or the Bloomberg Barclays Global Aggregate Bond index as well as inflation protected debt and municipal debt. **CYC Fixed Income:** Cyclical Fixed Income refers to Emerging market debt, both USD and locally denominated, and U.S High Yield.

For comparison purposes, the strategy is measured against a blended benchmark: 21% Russell 3000 Index, 24% MSCI ACWI ex US NR Index, 6% Dow Jones Global Select Real Estate Securities NR Index, 9% S&P GSCI CME Index, 40% Bloomberg Barclays Global Aggregate Bond NR Index. **The Russell 3000 Index** measures the performance of the largest 3,000 U.S. companies. **The MSCI All Country World Index ex US NR** captures large- and mid-cap representation across 22 of 23 developed markets countries-excluding the United States. **The Dow Jones Global Select Real Estate Securities NR Index** represents equity real estate investment trusts (REITs) and real estate operating companies (REOCs) traded globally. **The S&P GSCI CME Index** is a measure of general commodity price movements and inflation in the world economy. Index is calculated primarily on a world-production-weighted basis comprised of the principal physical commodities futures contracts. **The Bloomberg Barclays Global Aggregate Bond NR Index** is a measure of global investment grade debt from twenty-four different local currency markets. This multi-currency benchmark includes fixed-rate treasury, government-related, corporate and securitized bonds from both developed and emerging markets issuers. Net total return ("NR") indexes reinvest dividends after the deduction of withholding taxes, using a tax rate applicable to non-resident institutional investors who do not benefit from double taxation treaties. **The MSCI World ex USA Index** is a free-float weighted equity index that captures large and mid cap representation across 22 of 23 Developed Markets (DM) countries - excluding the United States. **The MSCI Emerging Markets Index** captures large and mid cap representation across 23 Emerging Markets (EM) countries. With 846 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

Net total return ("NR") indexes reinvest dividends after the deduction of withholding taxes, using a tax rate applicable to non-resident institutional investors who do not benefit from double taxation treaties.

It is not possible to invest directly in an index. Blended benchmarks are calculated daily and rebalanced quarterly.

Innealta Capital is a division of AFAM Capital, Inc., a Registered Investment Advisor to individually managed client accounts and certain mutual fund. The firm only transacts business in states where it is properly registered or exempt from registration. Registration of an investment adviser does not imply any certain level of skill or training.

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