

### January 2018 Commentary and Strategy Review

#### About the Strategy

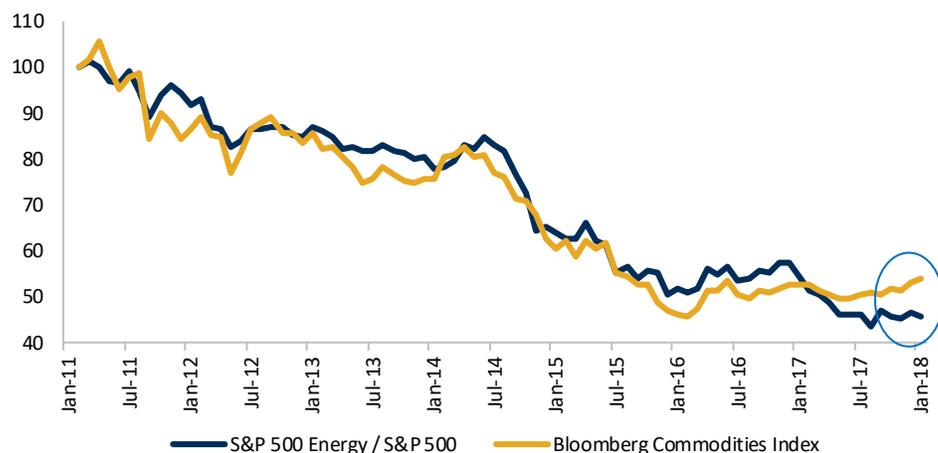
The Sector Rotation Portfolio (“SRP”) provides market exposure across U.S. equities and U.S. fixed income via exchange-traded funds. Innealta’s investment team manages the SRP strategy to a balanced benchmark of 70% S&P 500 index and 30% Bloomberg Barclays U.S. Aggregate Bond index. This benchmark reflects the average desired weight of equity and fixed income investments 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 utilizes 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 within U.S. equity and U.S. fixed income.

#### Outlook

Within the U.S. equity opportunity set, we remain cautiously optimistic and believe that certain sectors show increasing potential relative to others based on various behavioral, macroeconomic, and corporate fundamental drivers. At an aggregate level, the price-to-earnings ratio of the Russell 3000, a broad market index for U.S. equities, closed the month at 23.7x. The market has not seen this valuation level since the late 90’s, and profitability metrics in the U.S. have flatlined for last eight years. We do expect a small amount of multiple contraction during 2018 given both the elevated valuation levels and rising fixed income yields. We continue to expect earnings growth over the next few quarters. According to Factset, the blended S&P 500 Q4 2017 earnings is 13.4%, and all eleven sectors are reporting earnings growth, led by the Energy sector.

Within individual sectors, we see opportunities in Financials and Energy. As part of our overall global reflation theme and expectations of tightening U.S. monetary policy, we anticipate that U.S. Treasury yields will rise and ultimately the U.S. yield curve will steepen. In that environment, we anticipate that Financials will outperform the index. Additionally, we find the Energy sector attractive based on valuations, earnings growth and macroeconomic relationships. The “Chart of the Month,” shown below, displays the S&P 500 Energy sector relative to the S&P 500 against the Bloomberg Commodities index. Notice that the relationship has held over the past six years; however, over the past six months, it has broken down. We anticipate that the Energy sector’s performance relative to the S&P 500 will improve as earnings continue to improve. Finally, as the operating margin within the Energy sector has improved since 2015, the market has not rewarded the sector with a higher valuation multiple.

#### Chart of the Month



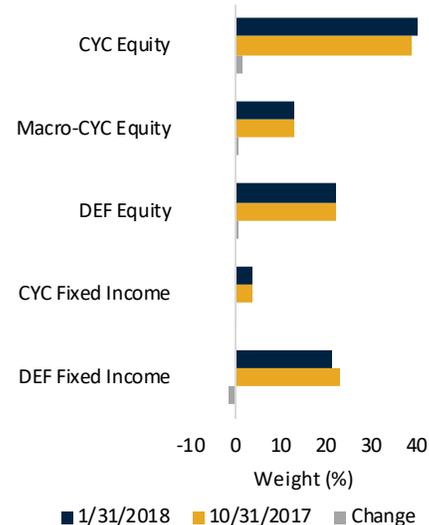
SOURCE: Innealta Capital using Bloomberg data from 01.31.2011 to 01.31.2018

#### Strategy Statistics

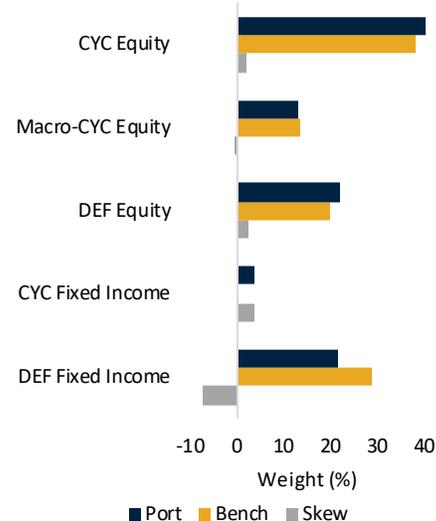
	Port	Benchmark
Alpha	0.97	0.00
Beta	0.38	1.00
R-Squared	0.44	1.00
Std. Dev.	4.71	8.19

Source: Innealta Capital using data as from Bloomberg. Data from 12.31.2009 to 01.31.2018. Benchmark represents a 70/30 blend of the S&P 500 TR Index and the Bloomberg Barclays Capital U.S. Aggregate Bond Index. Inception date for the portfolio is December 31, 2009.

#### Portfolio Changes



#### Portfolio Skews



SOURCE: Innealta Capital using data from Innealta Capital as of 01.31.2018

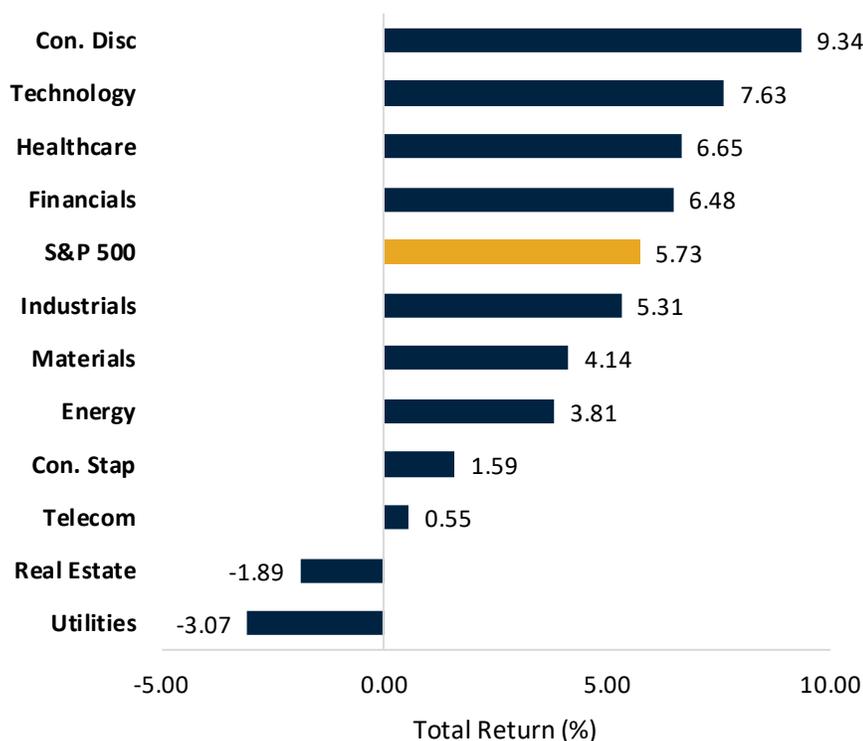
### Performance

The S&P 500 posted a record-breaking month, returning 5.73%, the largest monthly January return since 1997. In our opinion, the market's focus was on an improving earnings story, and the results from Q4 earnings helped support that view. The "Benchmark Performance" bar chart below shows the monthly return across all 11 GICS sectors and the S&P 500 index. The major theme during January was the performance in consumer cyclical oriented sectors as the Consumer Discretionary sector and Technology sector returned 9.3% and 7.6% respectively.

Despite the strong return in domestic equity markets, domestic fixed income markets struggled. The Bloomberg Barclays U.S. Aggregate Bond index returned -1.15% as the market sentiment continues to shift toward inflation concerns. We are also concerned about not only an increase in inflation but also an increase in the term premium.

The Innealta Capital Sector Rotation Portfolio exhibited strong performance during January, returning 3.6% gross of fees while a blended benchmark of 70% S&P 500 and 30% Bloomberg Barclays U.S. Aggregate Bond index returned 3.7%. Allocations to the Technology sector and the Consumer Discretionary sector were the top two contributors to the portfolio's performance. Allocations to the Utility sector, a bond-like proxy, and broad-based U.S. fixed income were the top two detractors to the portfolio's performance. The portfolio concluded the month with overweight allocations, relative to the benchmark, in Cyclical fixed income, Defensive equities, and Cyclical equities, while underweight allocations in Macro-Cyclical equities and Defensive fixed income. There were no significant changes to the portfolio during January.

**FIGURE 1: Benchmark Performance, Trailing 1-Month**



SOURCE: Innealta Capital using Bloomberg data from 12.31.2017 to 01.31.2018

### Top Contributors

1. Technology Select Sector SPDR (XLK)
2. Consumer Discretionary Select Sector SPDR (XLY)

### Bottom Contributors

1. Utilities Select Sector SPDR (XLU)
2. Vanguard Total Bond Market ETF (BND)

SOURCE: Innealta Capital using Innealta Capital data from 12.31.2017 to 01.31.2018.

### Strategy Performance

	Gross	Net	Benchmark
1-Month	3.57	3.29	3.62
3-Month	6.82	6.46	6.78
YTD	3.57	3.29	3.62
1-Year	16.48	14.89	18.67
3-Year	9.31	7.81	10.63
5-Year	5.94	4.40	11.75
Inception	6.73	5.30	11.40

SOURCE: Innealta Capital using data as of 01.31.2018. Benchmark represents a 70/30 blend of the S&P 500 TR Index and the Bloomberg Barclays Capital U.S. Aggregate Bond 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.

For comparison purposes, the composite is measured against a blended benchmark: 70% S&P 500 Index / 30% Bloomberg Barclays U.S. Aggregate Bond Index. **The S&P 500 Index** is a broad market sample based on the market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ. **The Bloomberg Barclays US Aggregate Bond Index** is representative of the entire universe of taxable fixed-income investments. It includes issues of the US Government and any agency thereof, corporate issues of investment grade quality (Baa/BBB or better), and mortgage-backed securities.

The "Benchmark Performance, Trailing 1-Month" chart contains return data for the individual S&P 500 sector indices as defined by GICS. Additional information can be found at <http://us.spindices.com/index-finder/?currentSearchCriteriaName=&AssetFamily=equity&query=energy&resultsPerPage=25>.

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 funds. 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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