Doug Sandler, CFA
GLOBAL STRATEGIST

Chris Konstantinos, CFA
CHIEF INVESTMENT STRATEGIST, DIRECTOR OF INTERNATIONAL EQUITY

Rod Smyth
DIRECTOR OF INVESTMENTS

Q1 '19: Strong Recovery from Tough Q4 '18

We Believe the Recovery Will Continue, but Expect Some Consolidation First

After living through the worst quarter since 2011, global investors were rewarded over the past three-months by the best quarter since 2012. In a nutshell, the first quarter of 2019 was almost a "mirror image" of the fourth quarter of 2018. For example, fears that the Fed would tighten too much shifted to expectations of a potential Fed cut, worries of imminent recession transitioned to the belief that any slowdown would be temporary, and, concerns over trade blossomed into hopes that a favorable resolution was close at hand. As macro-economic fears dissolved, and optimism began to grow, markets responded accordingly. The S&P 500 rose nearly 14%, developed international and emerging markets added 10%. Even the traditional "safe haven", the Bloomberg Barclay's US Aggregate index, returned an admirable +2.09% in the quarter. Perhaps, most encouraging of all was that global markets were able to rise despite a strained political atmosphere and the continuing saga of Brexit.

- Despite the strong performance of the first quarter we remain positive for 2019.
- Chinese fiscal and monetary stimulus appear to be having a positive impact.
- Valuations are cheap outside the US, in our view.
- US small business confidence remains robust.

OUTLOOK: REMAINING POSITIVE

After the strong quarter, stocks have achieved more in the first quarter than we had expected for the entire year under our base-case economic scenario in our 2019 Outlook. As 'worst-case fears' get replaced by 'best-case hopes' we are concerned over the short-term that expectations could get ahead of reality and the market will need to reset, as it usually does, to bring the two into alignment. Therefore, we would expect a period of consolidation to occur and continue to exercise prudence in our shorter-time horizon portfolios. Longer-horizon investors, in our view, can afford to be more patient given our positive long-term outlook and their higher tolerance for short-term volatility. We highlight below the reasons we remain long-term optimistic on global equities.

ACCORDING TO *PRICE MATTERS*®, VALUATIONS ARE NOT EXCESSIVE

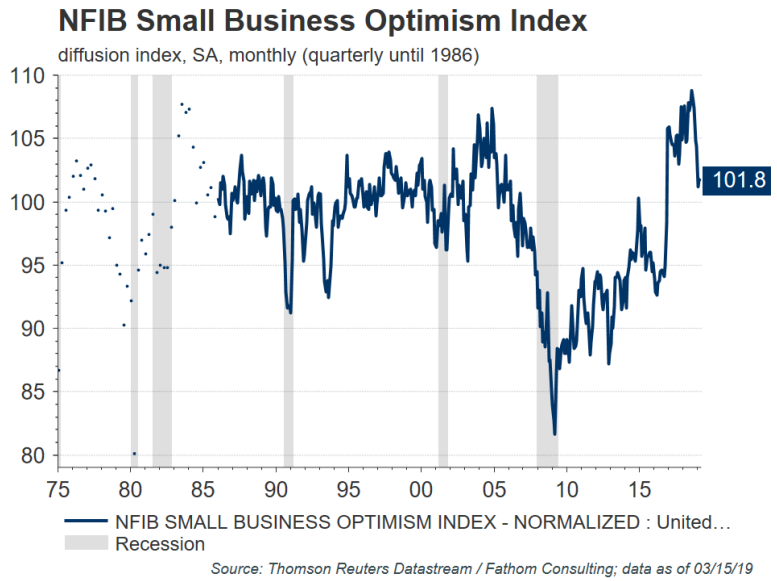
According to RiverFront's proprietary *Price Matters*® methodology, it does not appear to us that valuations are excessive on any of the four global equity classes (chart right). In fact, both developed international and

Asset Class	Index	Distance from Trend 2/28/19	Distance from Trend 2/28/18
US Large Cap	CRSP (1-2) Cap-Based Portfolio	13.1%	16.6%
Developed Intl	MSCI EAFE NR USD	-39.9%	-31.2%
US Small Cap	CRSP (6-10) Cap-Based Portfolio	11.7%	15.0%
Emerging Markets	MSCI EM NR USD	-14.3%	2.1%

Past performance is no guarantee of future results. Shown for illustrative purposes only, see the end of this publication for important disclosures and index definitions. You cannot invest directly in an index.

emerging markets remain valued below their long-term trend lines and all four asset classes are below their February 2018 *Price Matters*® levels.

We often say that valuation is a 'blunt instrument', when it comes to forecasting future returns, meaning that it tends to be most predictive when it is at extremes. Modest levels of overvaluation, which we believe we are experiencing in US large-caps and US small-caps, have historically not been enough of a catalyst to end a bull market.



SMALL BUSINESS OPTIMISM BODES WELL FOR US ECONOMY

Small businesses, which are defined as companies with fewer than 500 employees, have historically been a big contributor to the US economy. The Census Bureau, in their 2010 survey, noted that small businesses were responsible for:

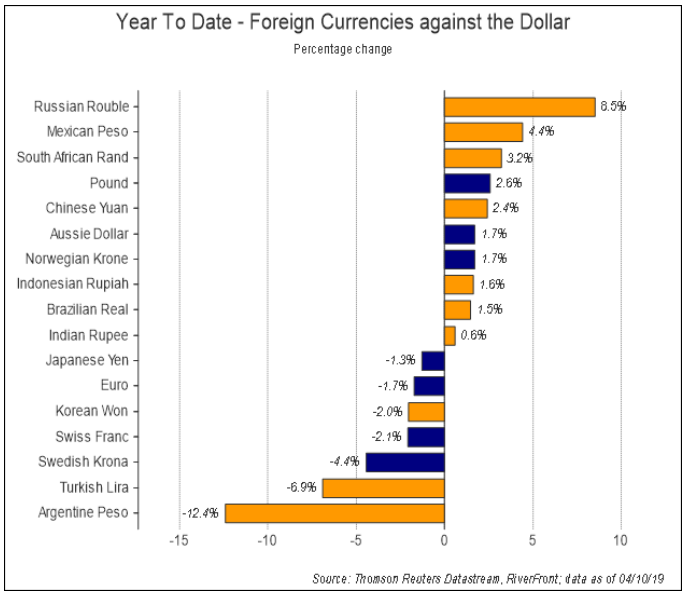
- 64% of net new private–sector jobs
- 49% of private-sector employment
- 42% of private-sector payrolls

The National Federation for Independent Business (NFIB) surveys its small business members to gauge their level of optimism. We believe that the dip in January 2019 was related to trade tensions and the government shutdown. We are encouraged to see the index stabilize above 100 over the last two-months (chart above) as the prospect of a US/China trade deal becomes more likely.

CHINA STIMULUS AND CURRENCY STRENGTH SHOULD BOOST INTERNATIONAL ECONOMIES

China is currently attempting to resuscitate its economy through fiscal and monetary stimulus. Recent Chinese economic data suggests that this simulative 'medicine' is beginning to take effect. Given that China represents more than 2.5x the weight of the second largest country (South Korea) in the emerging market index, their vitality is critical to both emerging market and developed international equity performance.

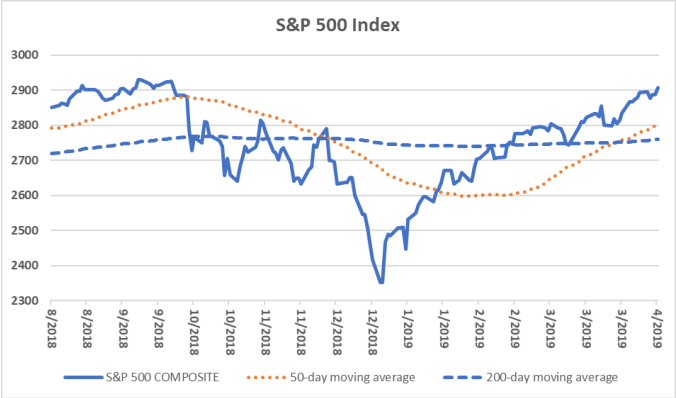
Many emerging currencies have also strengthened year-to-date (right chart), which we view positively given that many emerging market countries borrow in dollars or Euros. Strong emerging currencies make it easier for countries to pay back these obligations.

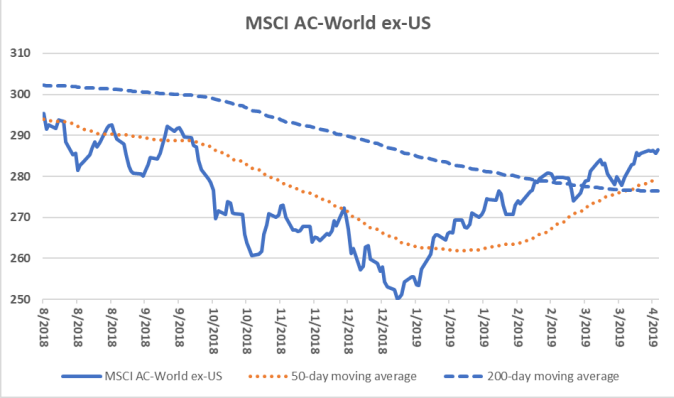


Source: Factset (8/1/18-4/12/19). Shown for illustrative purposes only. Past performance is no guarantee of future results.

GLOBAL EQUITY INVESTORS ARE NO LONGER 'FIGHTING THE TREND'

The US primary trend, which we define as the S&P 500's 200-day moving average (charts below, dashed-line), has flattened since the S&P 500's high of 2940 in September 2018, with the 50-day (dotted-line) rising. While the primary trend for international stocks [MSCI All Country World ex-US index] is still declining, the 50-day is rising, and the index is above both moving averages.





Source: Thompson Reuters DataStream, RiverFront. Data as of 3/29/19. See Disclosures and Definitions pages 3-4. Past performance is no guarantee of future results.

THE TREND IS CURRENTLY AT A CROSSROAD

If the long-term trend turns positive, as the shorter term 50-day moving average is suggesting; the odds for a positive return over the next three months improve significantly. However, a decidedly negative turn would warrant continued caution. We rate the trend overall as 'neutral' and remain hopeful it will re-accelerate to become our 'friend' again.

Important Disclosure Information

The comments above refer generally to financial markets and not RiverFront portfolios or any related performance. Past results are no guarantee of future results and no representation is made that a client will or is likely to achieve positive returns, avoid losses, or experience returns similar to those shown or experienced in the past.

Information or data shown or used in this material is for illustrative purposes only and was received from sources believed to be reliable, but accuracy is not guaranteed.

In a rising interest rate environment, the value of fixed-income securities generally declines.

Small-, mid- and micro-cap companies may be hindered as a result of limited resources or less diverse products or services and have therefore historically been more volatile than the stocks of larger, more established companies.

Investing in foreign companies poses additional risks since political and economic events unique to a country or region may affect those markets and their issuers. In addition to such general international risks, the portfolio may also be exposed to currency fluctuation risks and emerging markets risks as described further below.

Changes in the value of foreign currencies compared to the U.S. dollar may affect (positively or negatively) the value of the portfolio's investments. Such currency movements may occur separately from, and/or in response to, events that do not otherwise affect the value of the security in the issuer's home country. Also, the value of the portfolio may be influenced by currency exchange control regulations. The currencies of emerging market countries may experience significant declines against the U.S. dollar, and devaluation may occur subsequent to investments in these currencies by the portfolio.

Foreign investments, especially investments in emerging markets, can be riskier and more volatile than investments in the U.S. and are considered speculative and subject to heightened risks in addition to the general risks of investing in non-U.S. securities. Also, inflation and rapid fluctuations in inflation rates have had, and may continue to have, negative effects on the economies and securities markets of certain emerging market countries.

RiverFront's Price Matters® discipline compares inflation-adjusted current prices relative to their long-term trend to help identify extremes in valuation.

RIVERFRONT INVESTMENT GROUP 1214 East Cary Street, Richmond, Virginia 23219 804) 549-4800 RIVERFRONTIG.com

Trend, according to Price Matters® is the slope of an exponential growth function that closely tracks a real (inflation-adjusted) long term Index for that Asset Class. Distance from Trend is the distance of the trend line relative to the current index level expressed as a percentage.

Stocks represent partial ownership of a corporation. If the corporation does well, its value increases, and investors share in the appreciation. However, if it goes bankrupt, or performs poorly, investors can lose their entire initial investment (i.e., the stock price can go to zero). Bonds represent a loan made by an investor to a corporation or government. As such, the investor gets a guaranteed interest rate for a specific period of time and expects to get their original investment back at the end of that time period, along with the interest earned. Investment risk is repayment of the principal (amount invested). In the event of a bankruptcy or other corporate disruption, bonds are senior to stocks. Investors should be aware of these differences prior to investing. It is not possible to invest directly in an index.

Standard & Poor's (S&P) 500 Index measures the performance of 500 large cap stocks, which together represent about 80% of the total US equities market.

Bloomberg Barclays US Aggregate Bond Index measures the performance of the US investment grade bond market. The index invests in a wide spectrum of public, investment-grade, taxable, fixed income securities in the United States – including government, corporate, and international dollar-denominated bonds, as well as mortgage-backed and asset-backed securities, all with maturities of more than one year.

The MSCI EAFE Index is designed to represent the performance of large and mid-cap securities across 21 developed markets, including countries in Europe, Australasia and the Far East, excluding the U.S. and Canada.

MSCI ACWI ex USA Index captures large and mid-cap representation across 22 of 23 developed markets (DM) countries (excluding the US) and 23 emerging markets (EM) countries.

MSCI Emerging Markets Index measures equity market performance of emerging markets. The index consists of 23 countries representing 10% of world market capitalization.

Market Cap index information calculated based on data from CRSP 1925 US Indices Database ©2016 Center for Research in Security Prices (CRSP®), Booth School of Business, The University of Chicago. Used as a source for cap-based portfolio research appearing in publications, and by practitioners for benchmarking, the CRSP Cap-Based Portfolio Indices Product data tracks micro, small, mid- and large-cap stocks on monthly and quarterly frequencies. This product is used to track and analyze performance differentials between size-relative portfolios. CRSP ranks all NYSE companies by market capitalization and divides them into ten equally populated portfolios.

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