OUR FIRM

Boyd Watterson Asset Management, LLC is an SEC-registered investment advisory firm with $8.4 billion of assets under management. For nearly 90 years, we have successfully managed a broad range of fixed income, real estate, and equity strategies for institutions and individuals alike.

With a singular focus on the management of money and a dedication to the satisfaction of our clients' expectations, we offer the benefits of a boutique firm but with the resources usually attributable to a much larger asset management firm.

Please visit our website, ***www.boydwatterson.com***, for information about Boyd Watterson's investment strategies, insights, philosophy, and people.

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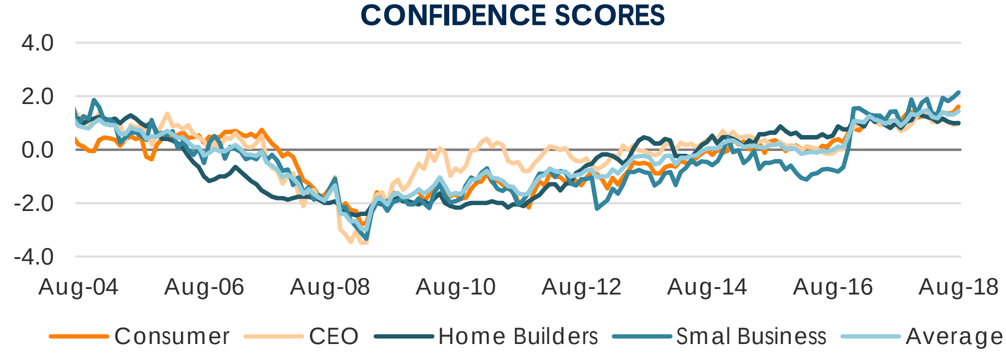
THE MACRO VIEW: THE BULL TRUDGES ON

The economic expansion is only nine months away from being the longest in U.S. history, and is being driven by a strong employment environment, high levels of both consumer and business confidence, and a monetary policy which remains slightly accommodative. Coming off second quarter real GDP growth of 4.2%, the Street expects growth to drop down to 3.0% in the third quarter, still a very respectable level. Corporations are generally enjoying strong earnings growth as well, and as a result, business investment has risen from the depressed levels that occurred after oil collapsed in 2015. This is all occurring while inflation remains tame, just recently reaching the Fed's target of 2.0% (Core PCE).

CONFIDENCE SCORES



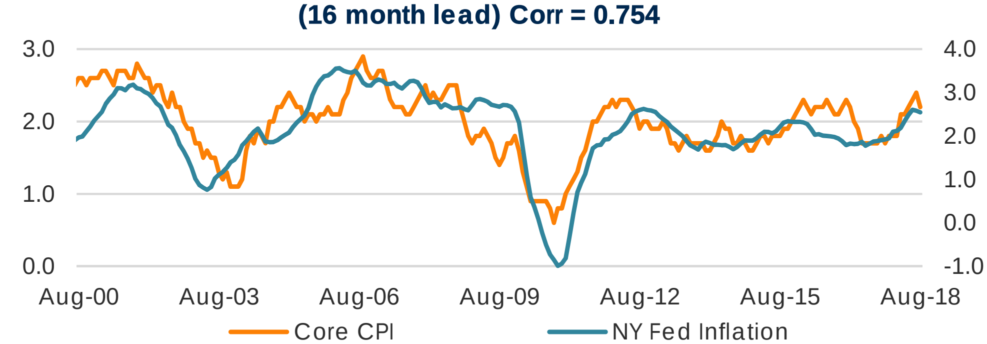
Source: Bloomberg. Data through August 31, 2018.

For the remainder of 2018, we see continued economic growth and expect the year to represent the highwater mark for the current expansion before moderating in 2019. We also do not expect a recession over the next 18 months. Our macro view is supported by:

- Economic growth that nears 3.0% for 2018, followed by growth of approximately 2.4% in 2019
- Moderate inflation hovering in the 2.0% area, but with the risk to the high side
- Low unemployment and solid payroll growth
- Corporate earnings growth rate near 20% for 2018 before declining to a more normal level of high single-digit growth rate

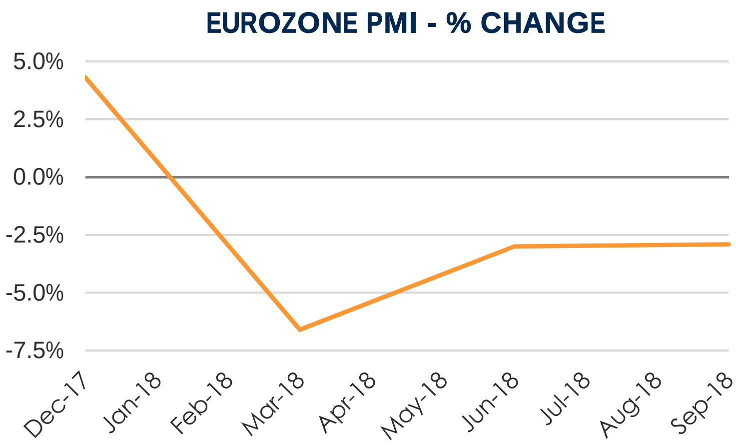
Timing the next recession is the real challenge. Although recessionary concerns remain low for 2018 and much of 2019, there is a growing concern that the economy will begin to slow and see more recessionary indicators as the benefits from tax cuts are behind us and the Fed continues on its path of raising interest rates. A Bloomberg survey given in late September shows two-thirds of business economists in the U.S. expect a recession by the end of 2020, while the NY Fed probability model is assessing only a 14.6% chance in the next 12 months.

CORE CPI AND NY FED INFLATION
(16 month lead) Corr = 0.754



Source: Bloomberg. Data through August 31, 2018.

On the international front, although the synchronized global growth story did not materialize as was expected, we have seen signs of stabilization (see graph below), even as trade tensions have taken center stage. Economic growth expectations in Europe have been dialed back, more in line with sub 2.0% growth. The wild card is China where trade tensions are high. The IMF is expecting growth in China to come in at the mid-to-low 6.0% range. We remain optimistic that the strength of the U.S. economy will not be overly impacted by trade wars and the modest growth of Europe.



Source: Bloomberg. Data through September 30, 2018.

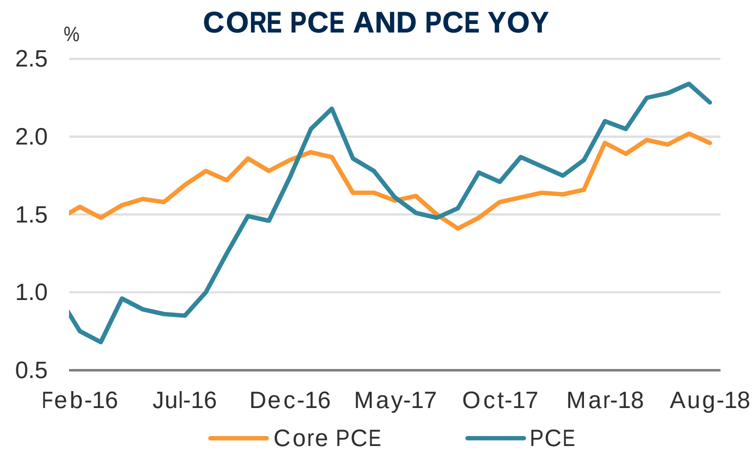
THE FED, INTEREST RATES AND INFLATION

In a continued, but more hawkish stance, the Fed raised rates another 25bps in September for the eighth time since December 2015, landing the fed funds rate at 2.00%-2.25%. Chairman Powell cited a modest increase in wages and inflation remaining around 2.0% as primary drivers supporting the decision to slowly continue to raise rates. Powell was clearly looking to quell investor anxiety that could cause market disruption - like the one felt in February earlier this year - explaining that despite borrowing costs rising for consumers, rates remain historically low, but such gradual increases are integral to Fed efforts to sustain the U.S. economy, maximize employment and stabilize prices by using “the right amount of support”.

Despite the growing geopolitical headwinds that have made for market jitters, the Fed appears convinced that the U.S. economy remains strong enough to support a policy of gradual interest rate hikes. In short, Chairman Powell noted specifically that tariffs, labor shortages and material costs could be positive catalysts that spur historically reluctant companies to finally raise prices. We think the Fed will raise rates in December, marking the fourth move in 2018.

In 2019, the Fed has projected three hikes over the course of the year. We are inclined to think that will get tempered down to two moves, rather than three, especially if interest rates remain historically low in Europe and Japan. Although we think the 10-year treasury will drift higher in 2019, the yield curve will likely remain fairly flat.

In terms of inflation, the story looks similar to last quarter with inflation remaining stable at the Fed’s target rate of 2.0%. The Fed has indicated that they are willing to let inflation exceed their projected level modestly without concern. As of the end of the third quarter, Core PCE YoY is averaging 2.0% while Core CPI is 2.2%. That said, we are closely watching indicators that may signal an increase in inflation, including a tightening labor market and a rise in average hourly earnings. We believe the risk to our outlook is for inflation to exceed our expectations.



Source: Bloomberg. Data through August 31, 2018.

CONCLUSION

We remain optimistic about economic growth for the remainder of 2018 and into 2019. We assign a very low probability of a recession, even though the Fed will continue to raise interest rates. In our view, current conditions do not call for a defensive posture and we continue to favor risk assets over the risk-free rate.

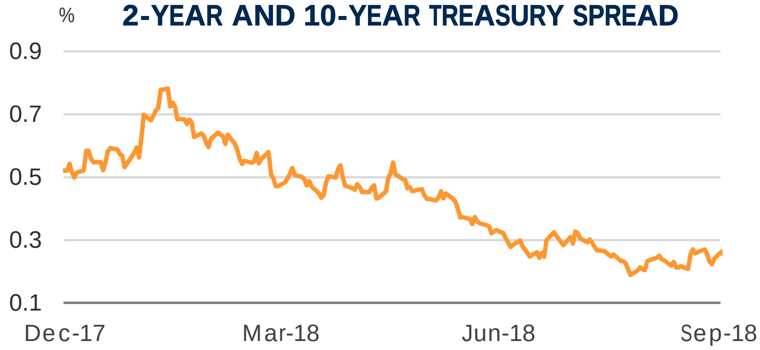
There are, however, no shortage of risks to the outlook and catalysts that could affect the timing of the next recession. Although we believe the U.S. economy can continue its positive growth through the risks and ensuing volatility that we see on the horizon, below are some of the near-term catalysts we are monitoring that could impact our forecast:

- A major delay to the European Central Bank (ECB) ending its QE policy
- Continued slowdown in China, partially due to trade tariffs
- Rising nationalism, trade negotiations and tariffs and their impact to prices and supply/demand

THE OVERVIEW BY MARKET
FIXED INCOME

Interest rates rose during the third quarter as the Fed continued to increase the federal funds rate. The recent pressure on interest rates has driven the 10-year Treasury note 66bps higher year-to-date. The short-end of the yield curve, which has experienced additional pressure from the Fed rate hikes, has risen 94bps on the year. This has resulted in a continual flattening of the yield curve as the spread differential between the 2- and 10-year Treasury ended the quarter at 24bps.

2-YEAR AND 10-YEAR TREASURY SPREAD



Source: Bloomberg. Data through September 30, 2018.

The credit sectors performed much better for the quarter, overcoming the rise in Treasury yields to produce positive total returns. From a quality perspective, lower quality generally outperformed higher quality and longer duration credit outperformed shorter duration credit. The securitized sectors also remained durable against underperformance over the quarter, with agency mortgage-backed, commercial mortgage-backed and asset-backed securities all generating positive excess returns over Treasuries.

PERFORMANCE FOR PERIODS ENDING SEPTEMBER 30, 2018

	QTD	YTD	1-YR	3-YR	5-YR
2-Year Treasury	0.13	0.17	-0.17	0.19	0.45
10-Year Treasury	-1.11	-3.76	-4.03	-1.13	1.34
Bloomberg Barclays Aggregate	0.02	-1.60	-1.22	1.31	2.16
Corporate Investment Grade	0.94	-2.21	-1.12	3.14	3.55
Corporate High Yield	2.40	2.46	2.85	8.16	5.51
Leveraged Loans	1.93	4.36	5.58	5.43	4.35
Mortgage Backed Securities	-0.14	-1.04	-0.90	0.99	2.00
S&P 500	7.71	10.56	17.91	17.31	13.95
MSCI EAFE	1.35	-1.43	2.74	9.23	4.42

Source: Interactive Data, Credit Suisse, Bank of America/Merrill Lynch/Bloomberg. Data through September 30, 2018.

As we approach the final quarter of 2018, we continue to be positioned for rising interest rates and flat-to-tighter spreads. We are defensive in our duration positioning while also remaining favorable toward the credit sectors. Credit valuations are fair by most measures, and remain supported by strong fundamentals, but spread tightening potential may be somewhat limited. Therefore, we continue to focus on income generation and maintaining a yield advantage relative to the benchmark, by overweighting both credit and securitized sectors that are offering beneficial yields over Treasuries.

REAL ESTATE

Real estate fundamentals remain strong at the end of the third quarter, despite the rising interest rate environment, with an abundance of available equity and debt capital, balanced supply growth and continued investor demand. Transaction volume growth has been negative year-over-year for several quarters due to a decrease from record levels in 2015. However, absolute volume levels remain above average and the commercial lending environment remains upbeat for borrowers, with ample debt capital available to potential borrowers and those looking to refinance. In the current rising rate environment with tight spreads, financing options have become increasingly competitive and new alternative financing options with substantially looser standards are beginning to gain market share on conventional lower-risk, but higher-priced lenders. We are closely tracking lending activity and debt capital flows as a measure of any increased risk to the market. Specifically, we are beginning to track more closely unregulated residential lending for signs of over-development that could have a larger impact on overall real estate credit markets.

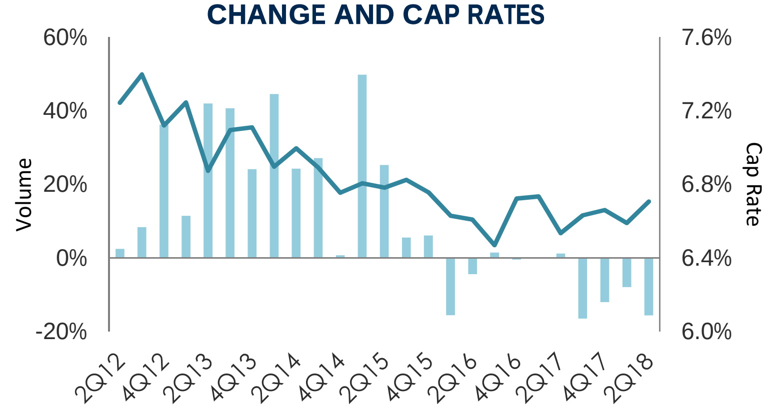
INVESTMENT PERFORMANCE BY PROPERTY SECTOR

	QTD	YTD	1-YR
Industrial	1.61%	7.36%	9.27%
Office	-2.45%	-2.98%	0.26%
Retail	0.87%	-1.33%	5.37%
Residential – Apartments	4.48%	5.42%	3.87%

Source: Bloomberg. Data through September 30, 2018.

Property sector performance has started to display some divergence in the last twelve months as Industrial properties have clearly outperformed all other major sectors. Multi-family (residential apartments) had a strong quarter, benefiting from increased rent growth despite some concerns about over-supply in certain markets. Although we see plenty of stamina remaining, even as we sit at the later stage of the cycle, the commercial real estate sector has started showing some signs of choppiness. Construction and labor costs have been increasing, which is beneficial for existing asset values but makes development more difficult and concentrated in higher-end products.

COMMERCIAL REAL ESTATE QUARTERLY TRANSACTION VOLUME YEAR-OVER-YEAR CHANGE AND CAP RATES



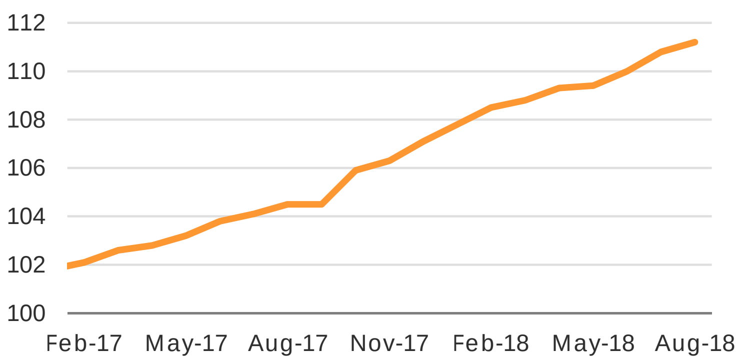
Source: Real Capital Analytics. Data through June 30, 2018.

Barring any unforeseen catalysts, we see healthy fundamentals coupled with strong liquidity as positive signs for the remainder of 2018, with no sign of a rapid downturn.

EQUITIES

A strong performing U.S. economy continues to drive solid equity performance, but the current rich valuations are mostly justified by the low-interest rate, low-inflation environment. Solid U.S. corporate earnings continue to catapult consumer confidence in U.S. equities, while the projections of the Fed continuing on the path of additional interest rate hikes is leaving investors more concerned for 2019. Although rising interest rates add to the prospect of inflation rising too rapidly, it appears inflation remains tepid for now for U.S. equities. Finally, the rising geopolitical tensions and tariff discussions have not had substantive financial outcomes to date. In fact, the equity market has largely ignored the trade tensions to this point, as the S&P 500 returned 7.71% on the quarter.

COMPOSITE INDEX OF 10 LEADING INDICATORS



Source: The Conference Board. Data through August 31, 2018.