Eagle Global Advisors

Market Review and Outlook

Q3 2018

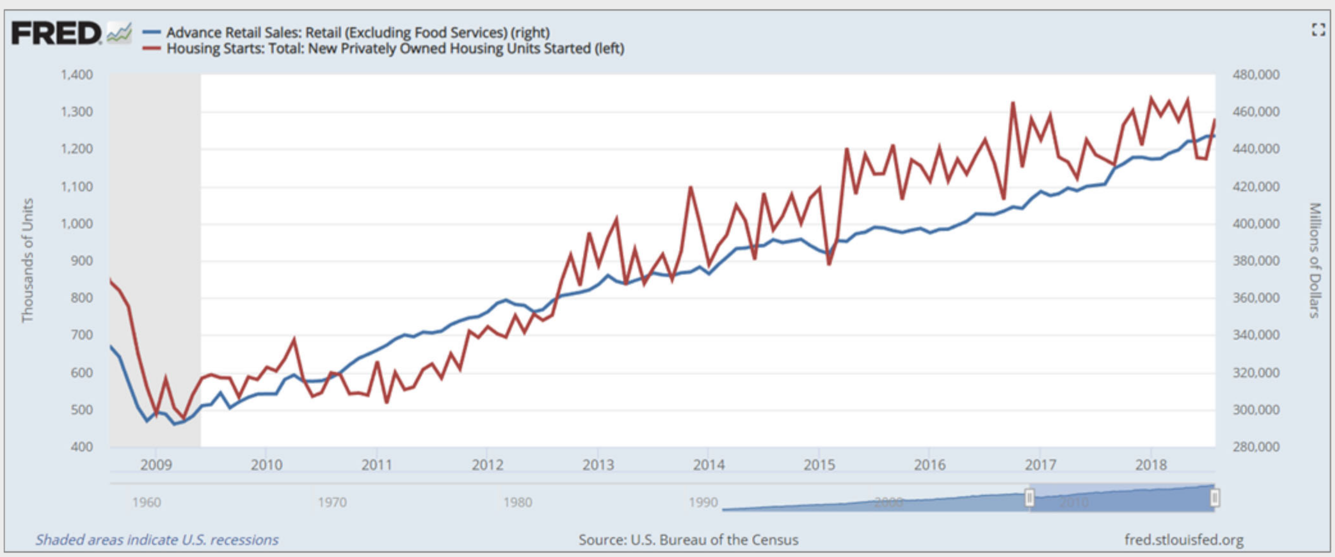
EGA U.S. Equity

From the EGA Portfolio Management Team

U.S. stocks soared during the third quarter with S&P 500 Index returning 7.7% for the quarter and 10.6% from the beginning of the year. International equities markets, as measured by the MSCI EAFE Index, rose 1.4% for the quarter bringing their return for the year to -1.4%. Interest rates rose along the yield curve leading generally to negative returns for fixed income securities. We continue to believe that current economic indicators in the U.S. are strong, but the trade tariffs create uncertainty for the global economy and markets.

Economy: *Economic Growth Continues*

Real Gross Domestic Product (GDP) increased at an annual rate of 4.2% in the second quarter, accelerating from 2% in Q1 2018. The acceleration in real GDP growth in the second quarter reflected accelerations in Personal Consumption Expenditures (PCE), exports, federal government spending, and state and local government spending, as well as a smaller decrease in residential fixed investment. These movements were partly offset by a downturn in private inventory investment and a deceleration in nonresidential fixed investment. Also, imports decreased after increasing in the first quarter.



U.S. retail sales rose by less than what was forecast in August following an upwardly revised July gain as purchases of automobiles and clothing fell, suggesting households took a breather from spending. The value of overall sales climbed 0.1 percent from the prior month after a 0.7 percent increase in July. So called retail control-group sales - which exclude food services, auto dealers, building materials stores and gasoline stations - advanced 0.1 percent after an upwardly revised 0.8 percent gain in July.

The housing market is giving mixed signals. New home construction rose more than forecasted to a three-month high in August, while permits unexpectedly declined. As a solid job market and lower taxes aid demand, rising property values and higher mortgage rates are hurdles for potential buyers. On the construction front, builders face higher costs, including costs for workers and for imported steel that's subject to tariffs. While new home sales rebounded in August after a three-month decline, contracts to buy previously owned U.S. homes declined in August by the most in seven months, indicating that the market is continuing to cool.

The ISM Manufacturing Index pulled back to 59.8 in September from a 14-year high reached in August as supply bottlenecks and price pressures eased. The ISM report indicates manufacturing is coming off the boil while still expanding at a solid pace amid steady demand and lower taxes, indicating the industry is poised to contribute to economic growth in the second half. Tariff wars with China remain a cloud over the outlook - with the ISM again citing respondents as "overwhelmingly concerned" about the levies - though an updated NAFTA agreement with Canada and Mexico should provide some relief.

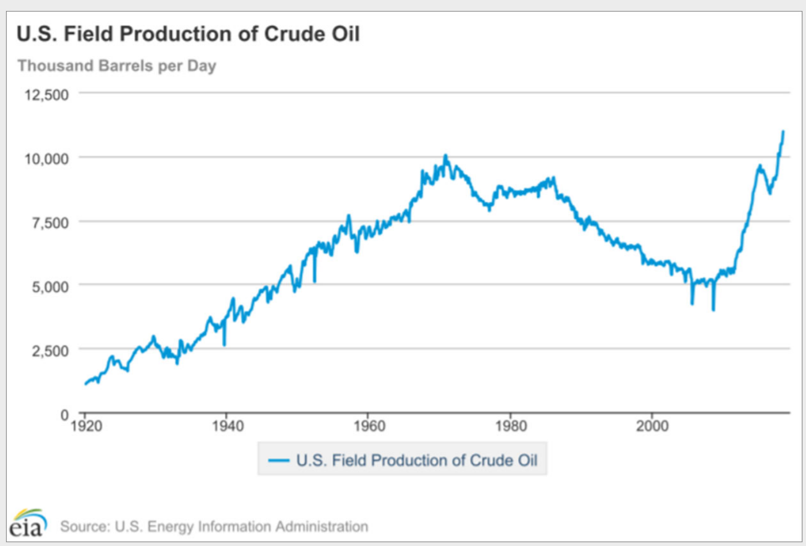
The conference board's Consumer Confidence Index soared to 138.4, the highest level in 18 years on brighter assessment of economic expectations. These historically high confidence levels should continue to support healthy consumer spending and should be welcome news for retailers as they begin gearing up for the holiday season.

The NFIB Small Business Optimism Index, a gauge of optimism among U.S. small business owners, rose to a record high as companies planned the most capital spending since 2007 and hiring intentions hit an all-time high.

The labor market continues to improve driven by wage growth, which unexpectedly climbed in August to 2.9%, the most since the last recession. The unemployment rate remained steady at 3.9% while the broad measure of unemployment rate, the U-6, which includes marginally attached workers and those working part time for economic reasons, fell from 7.5% in July to 7.4% in August.

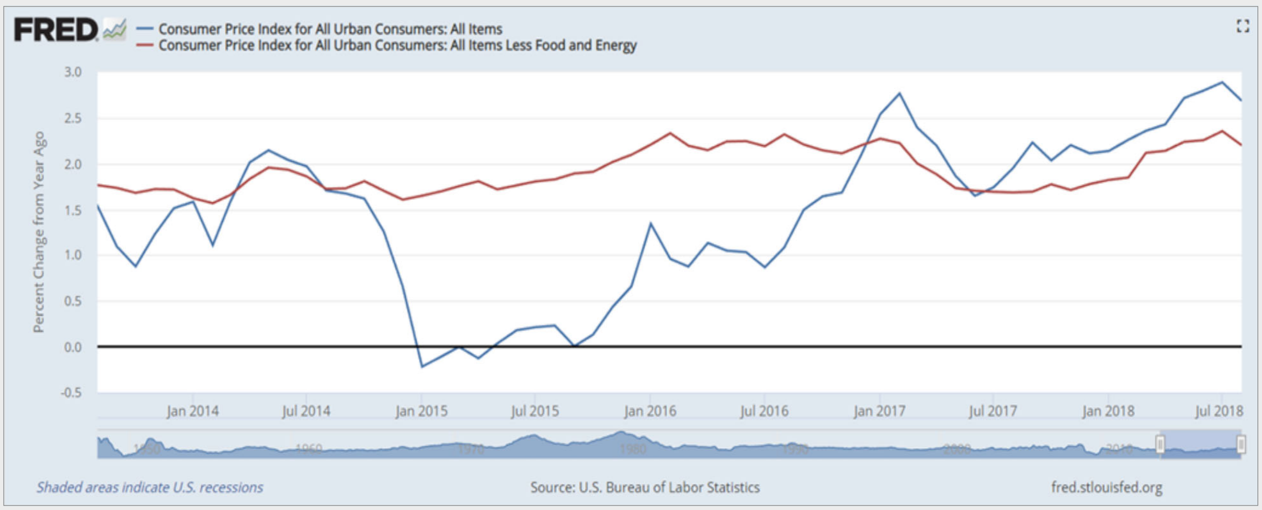
Oil: *WTI pauses while Brent continues to rally*

Global crude oil prices, as measured by ICE Brent Futures, rallied primarily on concerns that the sanctions on Iran and the collapse of Venezuelan production will lead to shortages in the coming year. West Texas Intermediate, the U.S. crude benchmark, was pressured by a steep decline in U.S. refinery capacity utilization, resulting in a decline of 1.2% during the quarter. Analysts expect a reduction of anywhere between 500,000 and 1.5 million b/d in Iranian supply due to the sanctions, with most expecting Saudi Arabia to take the lead in filling any supply gaps. During the September OPEC meeting, the Saudi energy minister stated that Saudi Arabia holds about 1.5 million barrels per day of spare capacity, which it can tap within weeks if needed. However, many are skeptical that the kingdom can produce that much oil on a sustained basis.



Inflation: *Eases Slightly*

Consumer price pressures began to moderate in August after a buildup in inflation through much of the year, a positive signal for workers who have seen bigger paychecks largely eaten up by price increases. The August Consumer Price Index (CPI) increased 2.7%, down from 2.9% in the previous month. Core CPI, which excludes food and energy prices, rose 2.2% from a year earlier, also slightly slower than July's annual gain. Shelter prices rose 3.5% and medical costs increased 2.4%. A decline in the cost of apparel and medical care helped keep overall price growth modest in August. Another factor helping keep prices in check is a stronger dollar, which makes imported goods relatively more affordable. Shelter and rent costs, which account for about a third of overall consumer spending, rose 3.4% from a year earlier. Additionally, energy prices were up 10.2%, led by a 20.3% increase in gasoline prices. Recently announced trade tariffs have yet to start showing up in the CPI report.



Corporate Profits: *Profits Growth Expected To Be Strong*

According to Factset, Q3 earnings for the S&P 500 Index are estimated to grow 19% versus last year. All sectors are expected to report year-over-year earnings growth, led by Energy, Financials and Materials. With the S&P 500 Index currently near 2924, the Price-to-Earnings Ratio of the market is around 16.4 times the 2019 mean earnings estimate, slightly above its long-term average. While valuations are just a bit above average levels, stocks do not appear expensive relative to bonds and inflation. Also supporting valuations is robust expected earnings growth. According to Factset, S&P 500 earnings are expected to grow 21% in 2018 and 10% in 2019.

Interest Rates: *A Steeper Path Of Rate Hikes*

As expected, the FOMC raised interest rates for the eighth time this cycle, moving the target range for the Federal funds rate up by 25 bp to 2.0%-2.25%. The Federal Reserve is now projecting a stronger GDP growth in 2018 and 2019 compared to its June projections. The projections for the Fed funds rate were left unchanged.

Fixed Income: *Rates Rise*

Short-term and long-term interest rates increased throughout the quarter which was capped by the Federal Reserve increasing its target for Fed funds by 25 basis points. Credit spreads were generally flat, which led corporate bonds to slightly outperform Treasuries. The Federal Reserve removed its reference to monetary policy being accommodative in its September statement and signaled that it plans to raise rates again in December and from two to three times in 2019. At Eagle, our portfolios generally outperformed with our emphasis on shorter maturities and a higher exposure to bonds with credit spreads. As we expect rates to continue rising, we are maintaining our preference for shorter maturities and high-quality corporates.

Stock and Portfolio Highlights

Outperformers: Industrials, Utilities and Energy were the top performing sectors relative to the benchmark. On an absolute level, Health Care stocks performed best, followed by Industrials stocks.

Disappointments: Stocks in the Information Technology and Consumer Discretionary sectors lagged in performance relative to the benchmark.

Purchases / Additions In The Quarter

Amazon.com Inc.: Several years ago, Amazon was viewed with skepticism on the sustainability of its loss making online retail business. Then came Amazon Web Services (AWS), which filled the profitability gap and allowed the company to expand while gaining scale in it retail operations. Along with it, came Amazon Prime, a program designed to increase utilization of Amazon's capacity and further promote scale. More recently, Amazon has layered another high profit margin business – advertising – on top of its core retail, AWS and subscription businesses. With these developments Amazon's story is changing from a top line growth story to a margin expansion story.

Carnival Corp.: Carnival shares have de-rated due to a softer Caribbean cruise market (one-third of CCL's total capacity) following the adverse impact of the 2017 hurricane season, concerns over 2019 industry supply impacting net yields, and higher crude prices. However, contrary to these fears, industry data suggests an environment of continued strong demand benefitting bookings and prices. We expect this data to reflect in company outlook in the next few quarters.

Concho Resources Inc.: Concho is a premier operator in the Permian basin, one of the most attractive oil basins in the world. The recent temporary infrastructure bottleneck in the Permian has created an opportunity to build a position in CXO's low-cost, high-growth assets at an attractive valuation. Additional upside is possible from synergies created through the RSP acquisition.

Raytheon: Raytheon is a play on increased U.S. and global defense spending. A recent sell-off which began with the 2018 Inter-Korean Summit provided an opportunity to add to our position.

Wells Fargo: Wells Fargo is a U.S. centric bank, with historically high ROA and ROE, characterized by lower funding costs due to its sticky deposit franchise. The addition to our Wells Fargo position is premised on expectations of cost reduction and capital return. The bank is reducing cost by closing branches, removing FDIC surcharge and reducing third party compliance costs. Management has indicated that capital requirements for the industry would likely be lower under the currently proposed capital framework. It is committed to returning excess capital to shareholders over next 2-3 years.

Sells / Trims In The Quarter

SunTrust Banks Inc.: We trimmed our position in SunTrust to harvest gains from its sizeable outperformance over the last 12 months. Net interest margin (NIM) expansion is likely to be more limited going forward as the rate hike cycle matures and because SunTrust has indicated that it expects additional hikes to have a close to neutral impact on NIMs.