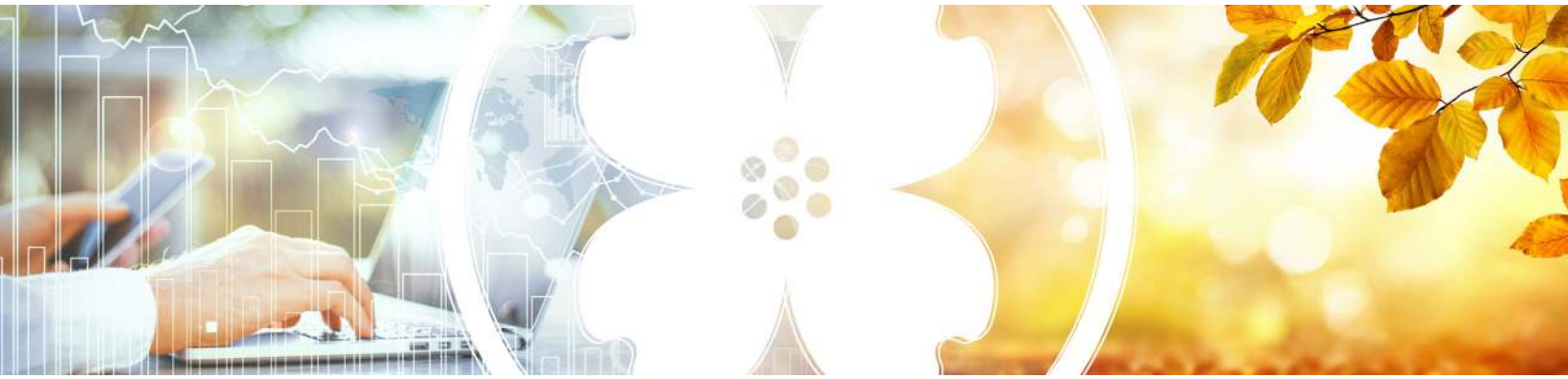


INVESTMENT UPDATE

FOURTH QUARTER **2017**

Global equity markets have continued to reach new record highs over the last year. The macro climate is very favorable for risk assets with the combination of a synchronized global expansion growing at a steady and moderate rate, low interest rates, stable inflation and only gradually declining monetary accommodation.

KEY TAKEAWAYS

1. The synchronized economic cycle is growing at a steady, moderate rate. With strong economic fundamentals, and low volatility across regions and financial markets, this trend can continue into 2018.
2. The U.S. economic cycle has entered its ninth year and the bull market in stocks remains intact. The typical signs of a recession are not evident and financial conditions remain loose.
3. Growth has broadened globally with the U.S. economy growing at 3% in two of last three quarters, Europe and Japan jumping to 2%, Emerging Markets at 5%, and China and India growing at 6-7% per year.
4. Global central banks have been highly accommodative by expanding their balance sheets, which has been a significant factor in the strong performance of financial assets and the real economy since 2009. Monetary accommodation is gradually diminishing in the U.S. and Europe. The Federal Reserve is raising interest rates and beginning to unwind its balance sheet and the European Central Bank is planning to taper its asset purchases. Overall, global monetary policy is still accommodative, but the removal of accommodation is a potential source of risk.
5. Inflation and interest rates remain low and stable.
6. Valuations are elevated, which is tempered by low inflation and rising earnings in the U.S. and across the globe.
7. Uncertainties include geopolitical risk, diminishing Central Bank balance sheet expansions, legislative uncertainty and the length of the U.S. expansion.
8. With a favorable macro backdrop, we remain moderately overweight stocks relative to bonds with a focus on quality, capital preservation, and diversification across asset classes and regions. We continue to be watchful for signs of deterioration in economic and market data.

ECONOMY

SYNCHRONIZED GLOBAL EXPANSION

The global economy is in the midst of a synchronized expansion and is in the best period of growth in the last decade. Emerging markets have joined the developed economies and global growth is expected to expand from 3.2% last year to 3.8% this year. Global GDP is expected to continue its expansion in 2018 growing 3.9%. (Figures 1 and 2). Strong growth in the U.S. is being met with strengthening global growth. Europe likely will grow 2% this year surprising to the upside. Japan's reflationary policies are working and it will also likely grow close to 2% this year, its fastest growth in several years. Importantly, China's growth has stabilized and is growing nearly 7%. The U.S. is benefiting from global growth with U.S. multi-national corporations seeing accelerating foreign revenue.

FIGURE 1 – Synchronized Global Growth *Source: PIMCO, Haver*

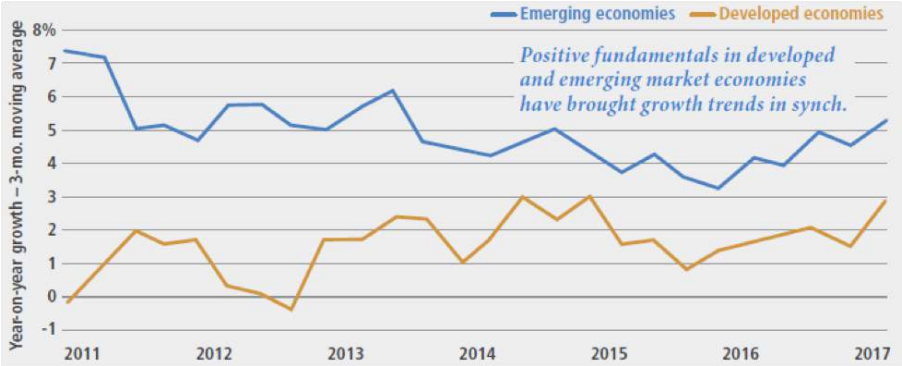


FIGURE 2 – GDP Forecast

GDP Growth Forecasts	2015 A	2016 A	2017 E	2018 E
World	3.3%	3.2%	3.8%	3.9%
EM	4.6%	4.6%	5.2%	5.5%
Advanced Economies	1.9%	1.7%	2.2%	2.1%
USA	2.4%	1.6%	2.3%	2.6%

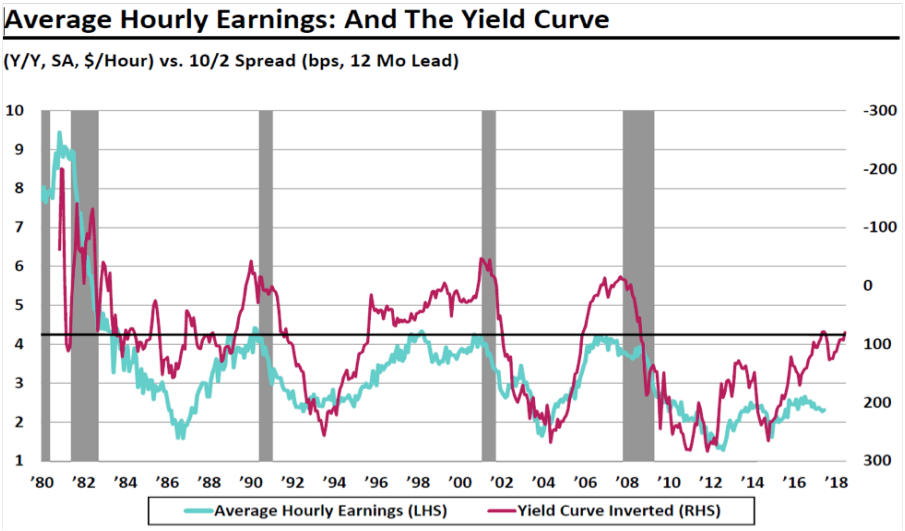
Forecasts—Source: Goldman Sachs *As of October 2017*

U.S. EXPANSION HAS ENTERED ITS NINTH YEAR

The current expansion in the U.S. has entered its ninth year and is 99 months old, the third longest on record. Stocks made a low in 2009 and have been in an uptrend since. Cycles, on average, last 47 months. The old truism is that expansions don't die of old age, but rather from excesses. With moderate, steady growth, the usual excesses are not present that lead to an overheating economy and a spike in inflation that causes the Fed to aggressively raise interest rates.

The near-term risks of a recession are low. A major concern would be an inverted yield curve that typically precedes recessions. A sign of the economy overheating is rapid wage growth, which is not currently present. Currently, the yield curve is a positive 80 basis points, which is close to the average yield curve spread of 90 basis points (Figure 3).

FIGURE 3 - The Yield Curve and Average Hourly Earnings
Source: Strategas, Blackstone



Another measure of economic health is the U.S. Leading Indicator, which has been climbing since late 2009. The index has recently paused in its upward trend. Typically, the index tops out one to two years before a downturn occurs (Figure 4).

Other risks include shocks from geopolitical events or a spike in oil prices. Oil prices have stabilized around the $50 per barrel level and are not likely to go substantially higher due to new supplies from shale that are keeping prices contained. North Korea continues to be a wildcard. Recent U. N. sanctions will be a major deterrent. China is the country with the most leverage over North Korea and it's encouraging that China joined the recent sanctions.

INTEREST RATES AND MONETARY POLICY: STILL ACCOMMODATIVE

Interest rates remain low, and even negative, in shorter maturities in many European countries. The Federal Reserve is on track to hike interest rates in December for the third time this year. The Fed is gradually beginning to reduce its balance sheet while slowly raising interest rates. The European Central Bank is planning to taper its asset purchases. In contrast, China and Japan's central banks continue to expand their balance sheets (Figure 5). Overall, even with tightening in the U.S. and Europe, global monetary policy is still loose.

FIGURE 4 – U.S Leading Indicator
Source: Evercore ISI, Blackstone

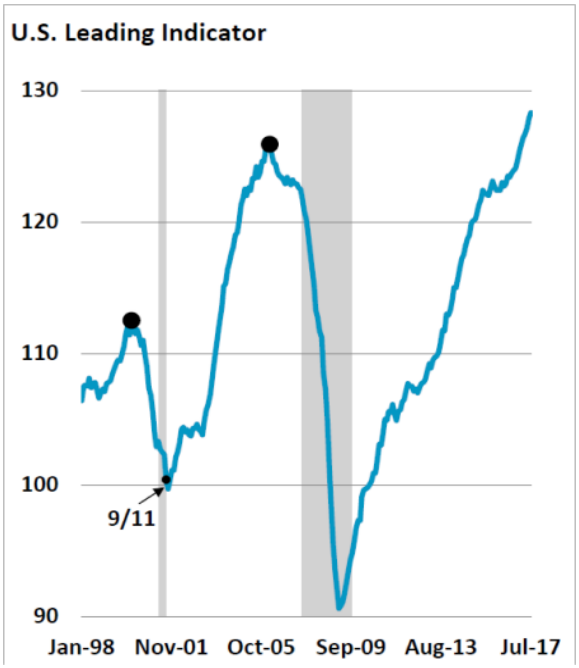


FIGURE 5 – **Global Central Bank Balance Sheets $18 Trillion in Assets**
Source: Blackstone

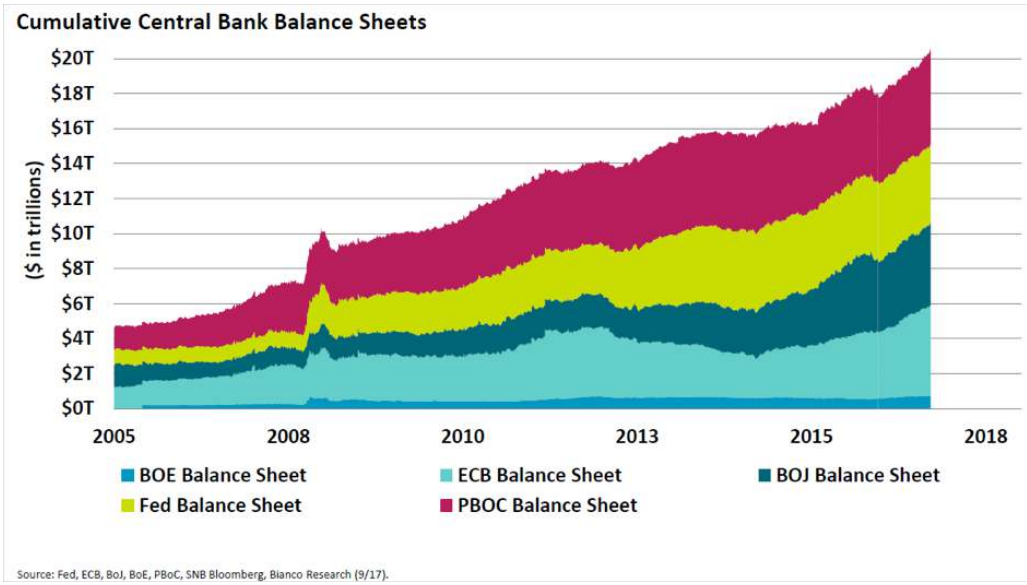
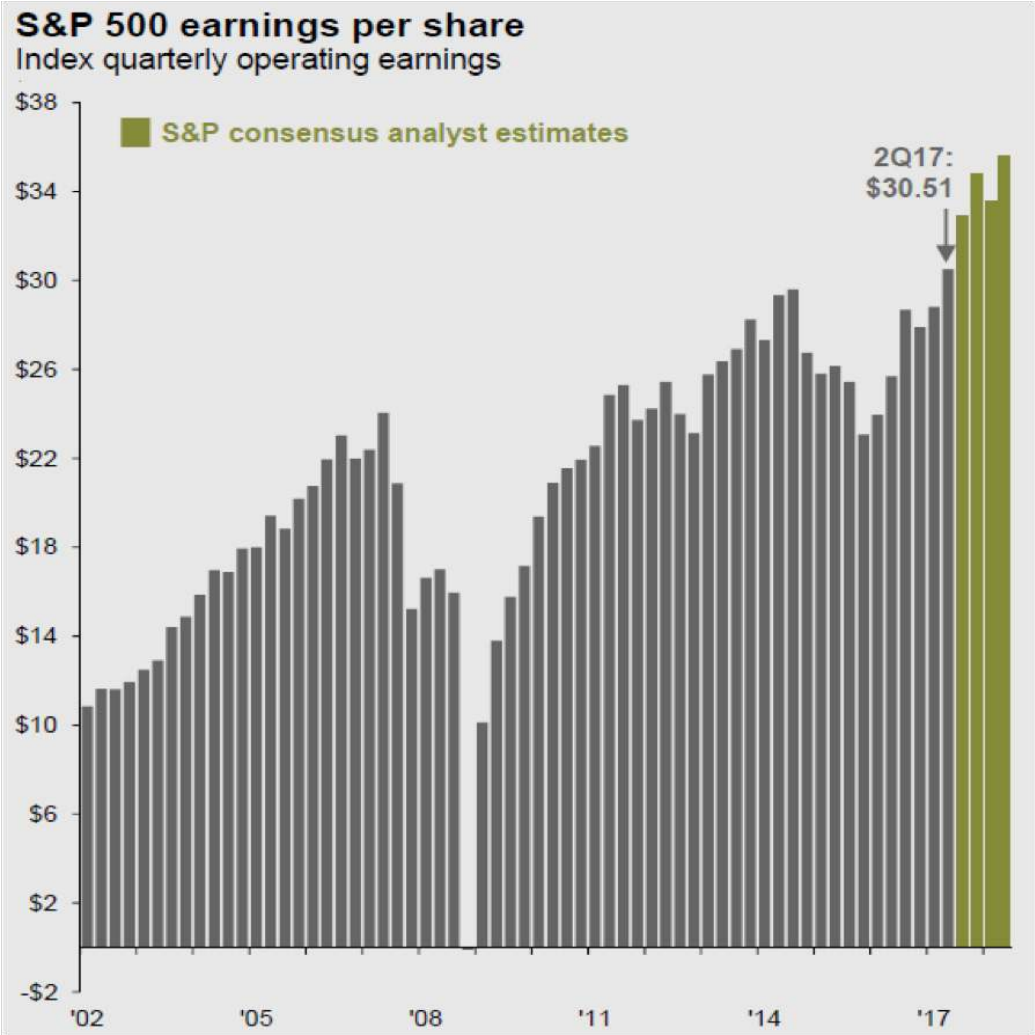


FIGURE 6 – **S&P 500 Earnings – Quarterly** *Source: JP Morgan*



FISCAL POLICY

Fiscal policy across the globe is mildly supportive. In the U.S., markets have reacted favorably to the current Administration's pro-growth agenda and a more favorable pro-business approach in Washington. The lack of legislative achievements by the current Administration has been a disappointment, but markets have looked past the lack of progress due to the underlying strength of the economy, decreased regulation and stable inflation. Tax reform remains uncertain, but progress has been made and investors are beginning to anticipate tax cuts/reform by early 2018. The potential of infrastructure spending and rebuilding, as a result of the hurricanes, are also potential positives.

EARNINGS: EXPANDING GLOBALLY

Earnings are the primary driver of stock prices over the long-term. The U.S. had an 18-month profits recession that ended in the second half of 2016. Earnings grew 13% in the first quarter and 10% in the second quarter. For the third quarter, earnings (reported-to-date) are up a better-than-expected 4.7% held back by the effects of the hurricanes (Figure 6). For 2017, corporate earnings are expected to grow 9.3% with revenue growth of 6.0% (FactSet).

If tax reform is passed, it has the potential to add $10 to S&P earnings, which is an increase of approximately 8% from current levels. Tax reform could lift GDP growth by 0.5% to 1%, raising growth above 3% in the U.S., which would be a significant boost to the economy, revenues and wage growth.

ASSET ALLOCATION VIEWS AND PORTFOLIO POSITIONING

The following are our major asset class and asset allocation views. We build globally diversified portfolios by utilizing five major asset classes: equities, fixed income, real assets, alternatives and cash. The implications to your portfolio may vary depending on your particular individual situation. Please consult with your Central Trust financial advisor.

ASSET ALLOCATION

The global economy is experiencing synchronized global growth that is the best growth period over the last decade. Despite the length of the U.S. expansion and business cycle, recession risks are low at present. The combination of rising earnings, muted inflation and only gradually diminishing global monetary accommodation is supportive of stocks and other risk assets. Against this backdrop, global stock markets have reached record highs and valuations are elevated across most asset classes.

As the global expansion continues at a moderate and steady pace, with rising earnings and no recession in sight, we continue to have a favorable view on equities and other risk assets in our asset allocation. However, at his point in the economic cycle, we have begun to move to a less pro-growth tilt focused on up-in-quality exposures in select allocations. The combination of a maturing economic cycle, low but rising volatility and a shift away from monetary accommodation underscores the importance of a dynamic approach to asset allocation.

With a favorable macro backdrop, we remain moderately overweight stocks relative to bonds with a focus on quality, capital preservation, and diversification across asset classes and regions. We continue to be watchful for signs of deterioration in economic and market data.

FORWARD LOOKING INVESTMENT RETURNS

Due to the combination of slower than historical growth across developed countries, high levels of debt, low productivity and generally full valuations, the prospects for investment returns have moderated across almost all the major asset classes over the intermediate term.

Overall, our asset allocation shifts over the last 18 to 24 months have been additive to returns, while continuing the construction of diversified, high quality global portfolios.

EQUITIES

Based on a favorable macro backdrop, we maintain a positive tilt on equities relative to other risk assets. After the strong advance this year, we expect more moderate returns over the balance of the year supported by rising earnings and continued global growth. In the U.S., potential changes in tax reform, infrastructure spending and reduced regulation may provide additional support to domestic companies. The weaker dollar is beneficial for large U.S. export-oriented companies like technology and industrial companies. We have increased allocations over the last year to developed

international markets benefiting from the broadening global expansion. Europe, Japan and China have all had upside surprises in growth in 2017. We have a positive view on emerging markets that have less expensive valuations and are benefiting from stability in China and rising global growth.

We have increased our allocation to the hedged equity sub-class within the equities allocation to lessen tail risks and be a bit more defensive. Historically, markets experience a 10% correction about once a year on average. As markets have not had a correction since early 2016, we would not be surprised by a pullback after the strong advance, which would be healthy and normal in a bull market.

FIXED INCOME

With the economy near full employment and global growth expanding, we continue to be cautious on longer-dated fixed income due to the potential of rising bond yields in the future. With the Fed in a gradual tightening mode,

interest rates will have an upward bias. On a global basis, U.S. yield levels are significantly higher than in the Eurozone and Japan, which make the U.S. market attractive to foreign investors. Eurozone bonds are at risk given their low and even negative yields at a time when the European Central Bank is preparing to taper asset purchases.

U.S. Treasury and investment grade bonds are attractive defensive assets for economic slowdown scenarios. Investment grade bonds diversify the riskier growth oriented investments in portfolios like stocks. In periods when stocks have negative returns due to economic downturns or shocks, bonds historically have positive returns.

Traditional core fixed income is important as the current U.S. expansion is 99 months old. We have an allocation to TIPS (Treasury Inflation Protected Securities) that provide a hedge against rising inflation.

For diversification, we utilize the Credit sector of fixed income that has less interest rate sensitively. We are neutral on Credit as credit spreads are currently tight, and they historically start to widen in the late stages of an economic cycle. Floating rate bonds have yields that increase when interest rates rise offering protection in a rising rate environment. High yield bonds spreads are tight and remain near full value. International developed market fixed income is avoided due to the low levels of interest rates relative to the U.S.

REAL ASSETS

Real assets provide inflation protection and are an important portfolio diversifier. We have an allocation to gold as a portfolio diversifier that acts as insurance during periods of financial uncertainty.

ALTERNATIVES

The alternative strategies we utilize in building portfolios are designed to lower portfolio volatility and improve portfolio efficiency due to low correlations with other asset classes. Alternatives act as a hedge in volatile markets and provide better performance in a rising interest rate environment than bonds.

CASH

Portfolios will typically have a small amount of cash due to interest income and dividends being generated. At times, higher allocations of cash are beneficial to decrease portfolio volatility and provide a source of funds for purchase of attractive opportunities.

THE **NEW LOOK** OF CENTRAL TRUST COMPANY

We are excited to announce that Central Trust Company will be unveiling its new website, client dashboard, and mobile app in January 2018. This update will bring technology to our clients like never before. Our interactive website will be filled with insights about what's going on in the markets as well as issues that matter to you when it comes to your financial planning and wealth management needs. With the launch of the Central Trust Company mobile app on both iPhone and Android, your accounts and investment information will now be readily available at your fingertips. **Look for more information on the launch of these exciting new features in the coming weeks.**

LAUNCHING IN JANUARY

MARKET RECAP FOR 2017: YEAR-TO-DATE

EQUITIES

Global equities continue to make record highs, driven by moderate synchronized global growth, rising corporate earnings, low inflation and low interest rates. Stocks have significantly outperformed bonds year-to-date. The U.S. Dollar has weakened by 8% this year benefiting international assets due to the currency effect. All the major asset classes have registered gains year-to-date.

Global equity markets reached new record highs in 2017. Year-to-date (10/31/17), the S&P 500 has gained 16.9% and the MSCI All Country World Index has advanced 19.6%. International developed equity markets have increased 20.8%, while emerging markets have led equity markets with a gain of 32.3%, aided by a weak dollar. The U.S. market has enjoyed an eight-year advance and is over triple the level of the lows reached in 2009.

In 2017, markets have had a changing leadership in market cap sizes and styles. Large Cap growth stocks have led the market higher. Growth has outperformed Value on a style basis, and Large Cap has outperformed Small Cap stocks on a size basis.

As of July 31, 2017		Trailing Performance (annualized for periods > 1 year)						
Asset Class	**Index**	**MTD**	**QTD**	**YTD**	**1Y**	**3Y**	**5Y**	**10Y**
EQUITIES								
Benchmark	MSCI All Country World IMI	2.0%	2.0%	19.6%	23.5%	8.2%	11.0%	4.0%
Large Cap	S&P 500	2.3%	2.3%	16.9%	23.6%	10.8%	15.2%	7.5%
Styles	Russell 1000	2.3%	2.3%	16.8%	23.7%	10.6%	15.2%	7.6%
	R1000 Growth	3.9%	3.9%	25.4%	29.7%	13.1%	16.8%	9.1%
	R1000 Value	0.7%	0.7%	8.7%	17.8%	8.0%	13.5%	6.0%
Sectors	Real Estate	0.8%	0.8%	8.2%	9.4%	4.7%	7.1%	2.2%
Long-Short	S&P 500 / LIBOR plus 3	1.4%	1.4%	10.2%	13.9%	7.2%	9.4%	5.7%
Small/Mid Cap	Russell 2500	1.5%	1.5%	12.7%	24.7%	9.6%	14.5%	8.1%
Mid Cap	Russell Mid Cap	1.7%	1.7%	13.6%	21.1%	9.0%	14.9%	8.1%
Small Cap	Russell Small Cap	0.9%	0.9%	11.9%	27.8%	10.1%	14.5%	7.6%
International	MSCI World Ex US (net)	1.4%	1.4%	20.8%	22.7%	5.6%	7.9%	1.0%
Emerging Markets	MSCI Emerging Markets (net)	3.5%	3.5%	32.3%	26.5%	5.7%	4.8%	0.6%

FIXED INCOME

Yields have fallen 6 bps (0.06%) year-to-date on the U.S. 10-year Treasury bond helping the Barclays Aggregate Index advance 3.1%. Interest rates have spiked from a low of 1.32% in July 2016 to 2.37% on the U.S. 10-year Treasury currently. TIPs (Treasury Inflation Protected Securities) have gained 2.1% year-to-date. Inflation expectations have moderated since the first quarter.

The Credit sector continues to outpace investment grade bonds as economic growth strengthens and spreads remain tight. High-yield has gained 7.5%, floating rate debt rose 3.6%, and emerging market debt gained 8.9% year-to-date.

As of July 31, 2017		Trailing Performance (annualized for periods > 1 year)						
Asset Class	**Index**	**MTD**	**QTD**	**YTD**	**1Y**	**3Y**	**5Y**	**10Y**
FIXED INCOME								
Benchmark	Citi World Broad Investment Grade	-0.4%	-0.4%	5.9%	1.6%	1.2%	0.6%	3.2%
U.S. Aggregate	Barclays US Aggregate	0.1%	0.1%	3.2%	0.9%	2.4%	2.0%	4.2%
Money Market	BofA Merrill Lynch 0-3 Month T-Bill	0.1%	0.1%	0.6%	0.7%	0.3%	0.2%	0.4%
U.S. Government	Bloomberg Bond Index US Govt (ST)	-0.1%	-0.1%	0.6%	0.2%	0.7%	0.6%	1.7%
	Bloomberg Bond Index US Govt (IT)	-0.2%	-0.2%	2.2%	-0.9%	2.0%	1.4%	4.3%
	Bloomberg Bond Index US Govt (LT)	-0.1%	-0.1%	6.0%	-2.4%	3.9%	2.9%	6.7%
U.S. TIPS	Citi U.S. Inflation Linked Securities	0.2%	0.2%	2.1%	-0.1%	1.4%	-0.1%	3.9%
Tax Exempt	BOFA Merrill Lynch US Municipal	0.2%	0.2%	4.8%	2.1%	3.2%	3.1%	4.6%
U.S. Corporate	Barclays iShares Intermediate Corp	0.0%	0.0%	3.5%	1.8%	2.5%	2.2%	4.4%
U.S. Corp High Yield	Barclays US Corporate High Yield	0.4%	0.4%	7.5%	8.9%	5.6%	6.3%	7.8%
U.S. Floating Rate	S&P/LSTA Leveraged Loan	0.6%	0.6%	3.6%	5.1%	4.0%	4.2%	4.7%
International	Citi Non USD WGBI	-0.8%	-0.8%	7.8%	0.7%	0.5%	-1.1%	2.4%
Emerging Markets	JPM Emerging Markets	0.2%	0.2%	8.9%	5.9%	5.5%	4.2%	7.0%

REAL ASSETS

Gold has advanced 9.6% in 2017. Gold benefits from financial uncertainty and is a portfolio diversifier. Commodities have moved higher since the lows in early 2016 on prospects of higher global growth, but have given back gains in 2017. Real assets benefit from the reflation trend of higher growth and inflation.

As of July 31, 2017		Trailing Performance (annualized for periods > 1 year)						
Asset Class	**Index**	**MTD**	**QTD**	**YTD**	**1Y**	**3Y**	**5Y**	**10Y**
REAL ASSETS								
Benchmark	Gold	-1.0%	-1.0%	9.6%	-1.1%	2.1%	-6.4%	4.0%
Inflation	Consumer Price Index (CPI)	0.5%	0.5%	1.7%	1.9%	1.2%	1.2%	1.6%
Commodities	Bloomberg Commodities	2.1%	2.1%	-0.8%	2.3%	-9.5%	-9.4%	-6.9%
Silver	LBMA Silver Price	-0.2%	-0.2%	3.6%	-5.3%	1.3%	-12.2%	1.6%

ALTERNATIVES

Alternatives provide additional stability to portfolios by enhancing diversification and reducing volatility due to low correlations with stocks and bonds. Low volatility alternatives are an attractive alternative to traditional fixed income in a rising interest rate environment.

As of July 31, 2017		Trailing Performance (annualized for periods > 1 year)						
Asset Class	**Index**	**MTD**	**QTD**	**YTD**	**1Y**	**3Y**	**5Y**	**10Y**
ALTERNATIVES								
Benchmark	LIBOR + 3	0.4%	0.4%	3.5%	4.2%	3.7%	3.5%	3.8%
Conservative	Hedge Fund Research HFRI FOF C	0.3%	0.3%	3.7%	4.2%	2.1%	3.4%	0.7%
Multi-Strategy	Hedge Fund Research HFRI RV Mu	-0.5%	-0.5%	3.9%	4.2%	3.3%	4.6%	3.7%
Global Macro	Credit Suisse Global Macro Ind	0.1%	0.1%	1.3%	3.3%	1.8%	2.7%	4.3%
Managed Futures	Credit Suisse Managed Futures	-2.7%	-2.7%	-2.9%	-4.6%	-0.8%	1.0%	1.7%

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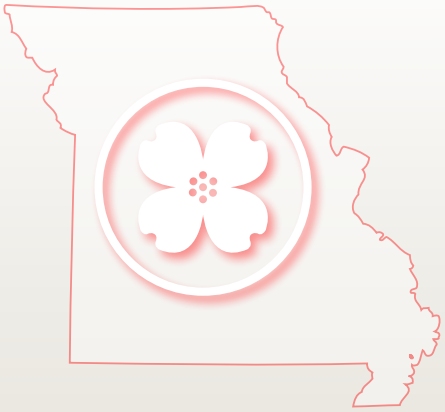

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THE CENTRAL VIEW

A publication produced by Central Trust Company providing you with up-to-date market commentary.

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Please consult with your Central Trust Company advisor for more guidance on how Central Trust can tailor solutions for your particular needs based on these evolving economic and market conditions.

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