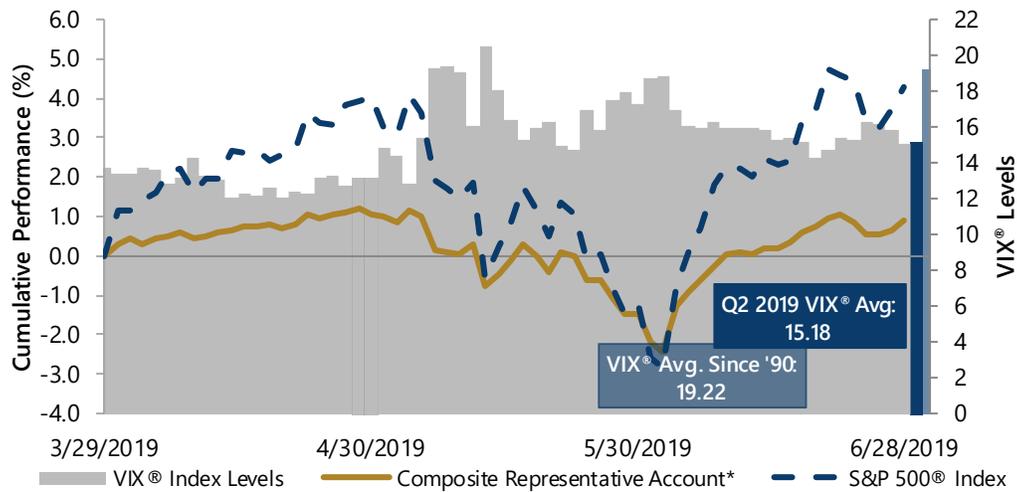


In Brief

- ◆ Gateway Index/RA Composite (the Composite) returned 0.94%, net of fees, in the second quarter of 2019 compared to the 4.30% return of the S&P 500® Index and the 3.08% return of the Bloomberg Barclays U.S. Aggregate Bond Index.
- ◆ During the quarter, the Composite provided 316 basis points (bps) of downside protection in May. The Composite underperformed the S&P 500 Index in April and June, as expected when the equity market advances at an above-average rate with below-average implied volatility.
- ◆ Trade policy and global growth concerns peaked in May when the equity market booked 2019's largest drawdown of 6.35%. The Federal Reserve (the Fed), however, helped allay investor concerns by shifting toward a dovish stance.
- ◆ Implied volatility exceeded realized volatility with the Chicago Board Options Exchange (Cboe®) Volatility Index (VIX®) averaging 15.18 for the quarter while the annualized standard deviation of the S&P 500® Index was 11.51%. The Composite* had an annualized standard deviation of 5.33%.
- ◆ Investors should contemplate the path forward and explore potential risks and rewards associated with uncertainty around global growth, monetary policy and trade policy. In particular, investors should consider the potential negative impact to both stock and bond markets if the Fed does not deliver the multiple rate cuts currently reflected in bond futures market prices.

Market Path & Implied Volatility



Source: Bloomberg, L.P. *The portfolio performance and annualized standard deviation reflected for the Composite are those measured by a representative account. This information represents supplemental information to the GIPS-compliant presentation. This representative account was selected as it is the largest account in the Composite.

Market Recap

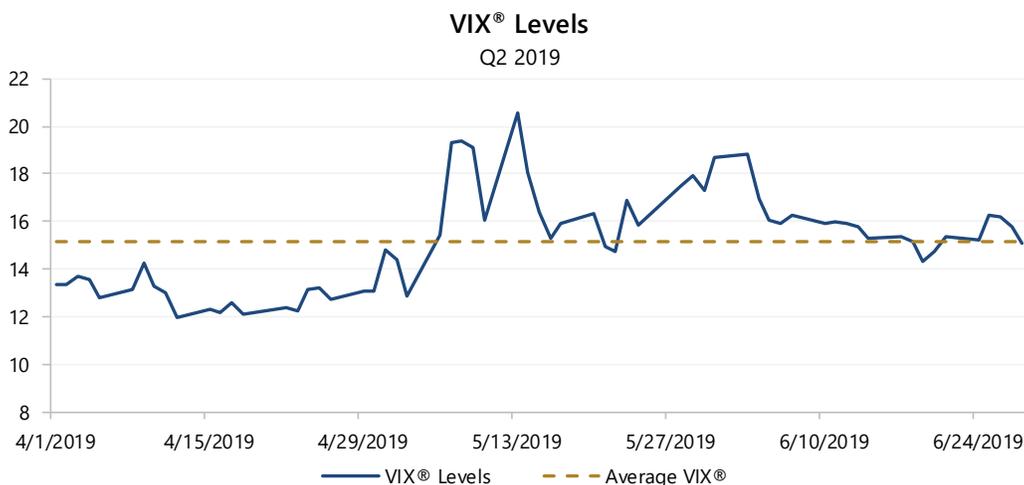
The S&P 500® Index weathered the storms in the second quarter of 2019 to return 4.30%, bringing its year-to-date return to an impressive 18.54%. The second quarter started strong with a 4.05% climb in April, digested 2019's largest monthly drawdown of 6.35% in May, then recovered by ending on a positive note with June's 7.05% return.

The second quarter faced a quagmire of concerns around trade policy and global growth. These issues percolated throughout the quarter but peaked in May as tensions between the U.S., China and Mexico ratcheted higher. The Fed was quick in its attempt to appease investors with a more dovish stance than originally portrayed heading into the quarter. As the Fed acknowledged slowing global growth and potential negative impacts on domestic growth stemming from trade tensions, investors appeared sufficiently encouraged and helped the S&P 500® Index resume an impressive climb to record highs.

On the domestic front, the third estimate of Gross Domestic Product growth for the first quarter of 2019 came in at 3.1%, in line with consensus expectations. Corporate earnings also remained positive with more than 81% of companies reporting first quarter earnings that met or exceeded analyst estimates and aggregate operating earnings for S&P 500® Index companies grew nearly 16% year-over-year. The employment situation improved throughout the second quarter with the May unemployment rate declining to 3.6%

from 3.8% reported in March. The May Consumer Price Index, released on June 12, showed a 1.8% year-over-year increase, in line with expectations yet below the 2% level targeted by the Fed.

Implied volatility, as measured by VIX®, averaged 15.18 for the quarter. VIX® exceeded S&P 500® Index realized volatility, as measured by its annualized standard deviation of daily returns, of 11.51% for the quarter. VIX® started the second quarter at 13.40, before drifting to its intra-quarter low of 12.01 on April 12, then peaked at 20.55 on May 13 before closing the quarter at 15.08.



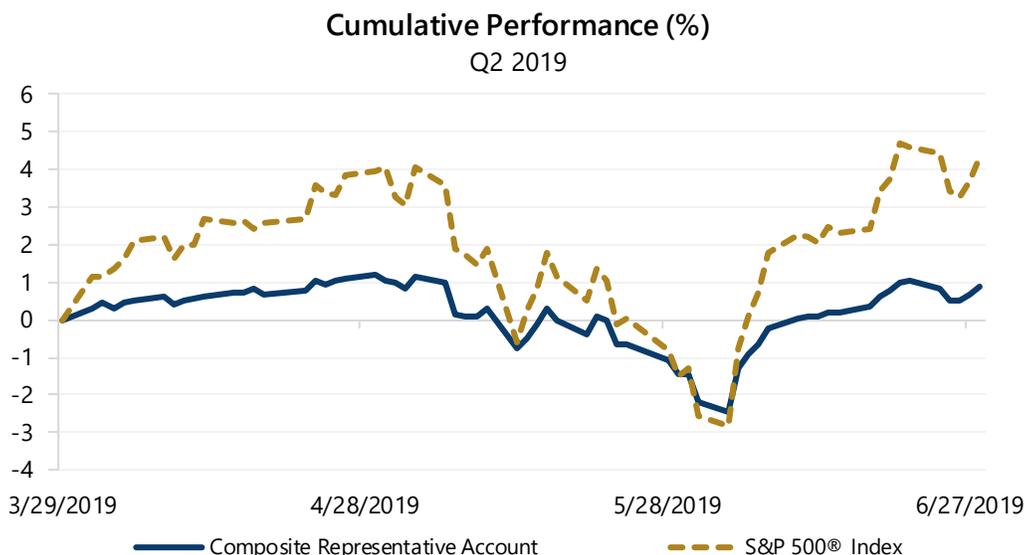
Source: Bloomberg, L.P.

The Bloomberg Barclays U.S. Aggregate Bond Index increased an impressive 3.08% in the second quarter. The yield on the 10-year U.S. Treasury Note started the quarter at 2.50%, reached a high in April of 2.59%, then drifted lower to end the quarter at 2.01%. The low point of the quarter came near the end of June with a yield of 1.99%.

Gateway IndexRA Composite Performance

The Composite returned 0.94%, net of fees, in the second quarter, underperforming the S&P 500® Index by 336 bps, and bringing its year-to-date net return to 6.05%. With monthly returns of 1.04%, -3.19% and 3.19% for April, May and June, respectively, the Composite's downside protection in May did not make up for its lagging performance as compared to the S&P 500 Index in April and June. The Composite's underperformance in April and June was expected due to above-average rates of advance for the equity market combined with below-average implied volatility levels.

The portfolio performance contributions, annualized standard deviation and portfolio statistics quoted for the Composite in the following paragraphs are those measured by a representative account¹.



Source: Bloomberg, L.P.

¹: Represents supplemental information to the GIPS-compliant presentation. This representative account was selected as it is the largest account in the Composite.

The Composite's underlying equity portfolio returned 3.76% for the quarter, trailing the performance of the S&P 500® Index by 54 bps. The Composite's written index call option positions detracted from returns for the quarter. However, index call option writing generated risk-reducing cash flow throughout the quarter and gains on written index call option positions contributed to downside protection during May's equity market decline. Similarly, gains from index put option positions provided downside protection in May, but losses on index put options during the equity market advances of April and June resulted in a net loss from index put options for the quarter. The Composite's annualized standard deviation of daily returns for the quarter was 5.33% as compared to 11.51% for the S&P 500® Index. The Composite exhibited a beta to the S&P 500® Index of 0.43 for the quarter.

Gateway's investment team was active in their response to changes in market conditions and direction throughout the quarter. In periods when the equity market advanced, the team focused on exchanging index call options well in advance of their expiration dates for ones with later expiration dates and higher strike prices. This was in an effort to maintain a typical amount of equity market exposure and protect the Composite from the potentially adverse impact of a sharp reversal in market direction. As markets turned south during the middle of the quarter, the investment team took advantage of the relatively elevated volatility levels by making several index call option trades that increased potential cash flow while maintaining a typical risk profile.

The Composite maintained full put coverage throughout the second quarter. In managing the Composite's index put option portfolio, during periods when the equity market advanced, the investment team focused on managing the cost of downside protection by trading select contracts well in advance of their expiration while extending weighted-average time to expiration. During the intra-quarter drawdown, as market volatility increased, the team realized profits in select index put option contracts and purchased new contracts with lower strike prices and later expiration dates.

At the end of the quarter, index call options were sold against over 95% of the equity portfolio's value and had a weighted average strike price between 1.5% in-the-money and 1.5% out-of-the-money, 40 days to expiration and annualized premium to earn between 10.0% and 15.0%. Index put options covered more than 95% of the portfolio and had a weighted average strike price between 10.0% and 12.5% out-of-the-money, 67 days to expiration and an annualized cost of less than 2.5%. Relative to the beginning of the quarter, this positioning represented slightly higher potential net cash flow and similar market exposure.

Market Perspective

The first half of 2019 unfolded in a way few predicted coming into the year. The equity market not only recovered to new all-time highs in the second quarter, but it approached and even surpassed levels that many prognosticators had predicted for the full year. Meanwhile, in the bond market, falling interest rates and expectations of future rate cuts helped the Bloomberg Barclays U.S. Aggregate Bond Index deliver its best total return over the first half of a year since 1995.

Given the surprises thus far in 2019, what should investors expect going forward? There are few, if any, scenarios in which both stocks and bonds continue to deliver the very high returns of the last six months. In other words, what is good for stocks in the short-term is likely to be bad for bonds and vice versa. Furthermore, since strength in both markets has coincided with increasing expectations that the Federal Reserve will cut short-term rates in the second half of the year, downside risk in both markets may have increased.

As surprising as the first half returns of the stock and bond markets have been, the environment in which the returns have transpired makes them even more surprising. The strong returns of the equity market came despite a significant slow-down in the growth rate of corporate earnings. After growing at a rate of more than 6% in each of the first three quarters of 2018, S&P 500® Index operating earnings expanded at a rate of less than 1% in both Q4 2018 and Q1 2019 and are currently expected to grow less than 1% in Q2 2019. Slowing growth appears to be primarily a corporate phenomenon rather than a sign of broader domestic economic deterioration.

The bond market environment has changed dramatically over the last six months. After their December 2018 meeting, the Fed had prepared the market to expect two rate hikes in 2019. Market seers who had forecast low to negative returns from bonds based on the Fed's outlook are, to this point, off by more than a country mile. The yield on the 10-year U.S. Treasury Note has defied both the Fed and market prophets by briefly falling below 2% during the second quarter, a mark that put it within spitting distance of all-time lows. Moreover, at the end of Q2 2019, futures market prices for the Fed funds rate reflected a 100% probability of at least one rate cut this year, with the first likely to come as soon as July. Futures pricing also reflected rising probabilities of additional cuts by year-end. Falling rates and strong bond market returns occurred despite robust Q1 2019 GDP growth, strong employment figures and an elevated Conference Board Leading Economic Index.

Looking forward, continued economic expansion may be necessary to support a reacceleration of earnings growth that would justify current market valuations and support a continuation of the robust equity market advance. However, this would likely put upward pressure on interest rates and lower the likelihood that the Fed could justify the multiple future rate cuts currently priced into futures markets. Similarly, significant progress on trade policy, specifically between the U.S. and China, may benefit stocks but would also likely alleviate some of the concerns about a global economic growth slowdown that may have contributed to expectations of future rate cuts by the Fed. Conversely, if economic data begin to conclusively show that the domestic economy is deteriorating due to tariffs, slowing global growth or some other phenomena, the bond market may continue to rally. However, any or all of these developments would be negative for the stock market.

While it is difficult to envision scenarios that would allow both the stock and bond markets to simultaneously continue their high returns, there is a scenario with the potential to trigger a simultaneous retrenchment in both markets. If the Fed is unable to deliver on the rate cut expectations currently reflected in bond futures market prices, both stock and bond markets could potentially give back a substantial portion of their recent gains.

Investors may be compelled to attempt shifting money to the winning horse that has gotten out to a stronger than expected start. Gateway believes investors are best served by maintaining exposures that are consistent with their risk tolerance. Shifting portfolio allocation toward the asset class that is expected to do the best over the short term could result in exceeding risk tolerance, or unnecessarily lowering risk below tolerance. Gateway strategies, which combine equity exposure and index option-based cash flow to lower risk, are a potentially attractive middle ground for investors who see long-term opportunity in equities but shorter-term risks in both stock and bond markets.

VIX[®] ended the second quarter at 15.08. While this is below its historical average, it is notable because the S&P 500[®] Index was above 2900 and near its all-time high. VIX[®] ended the second quarter significantly higher than its reading the previous times the S&P 500[®] Index made new highs above 2900. Specifically, VIX[®] was 28% higher than it was at the market peak on September 20, 2018 and 17% higher than the peak on May 3, 2019. The implied volatility represented by VIX[®] is the vital component of strategies that write index options to lower the risk of equity market exposure. Higher VIX[®] levels result in higher cash flow from index option writing. Higher cash flow has the potential to translate into greater returns if the equity market advance continues. Increased cash flow can also provide improved protection if downside risk materializes in the equity market.

Gateway strategies have a long history of utilizing cash flow from option writing to achieve a lower risk profile than the broader equity market. Investors seeking to maintain their historical risk profile while reducing direct exposure to the potential risks of stock and bond markets may find a useful role for Gateway strategies in their diversified portfolios.

Important Information

All data as of 06.30.2019, unless noted otherwise.

For more information and access to additional insights from Gateway Investment Advisers, LLC, please visit www.gia.com/insights.

Gateway Investment Advisers, LLC (Gateway) is an independent registered adviser and a successor in interest to Gateway Investment Advisers, L.P. as of February 15, 2008. Performance information for the Gateway Index/RA Composite shown in this illustration is an asset-weighted composite of discretionary accounts under Gateway's management which share the same investment objectives and hedging strategies.

The Composite was created in January 1993. Prior to January 1, 1993, not all fully discretionary portfolios were represented in composites. Results shown for 1988 through 1992 are those of one representative account.

The Gateway Index/RA Composite net of fee performance results reflect the reinvestment of dividends and other earnings, and reflect the deduction of investment advisory and fees.

The effectiveness of Gateway's strategy might be reduced if the portfolio doesn't correlate to the performance of the index underlying its option positions. Rebalancing of a portfolio may involve tax consequences.

Selling index call options can reduce the risk of owning stocks, but limits the opportunity to profit from an increase in the market value of stocks in exchange for up-front cash at the time of selling the call option. Unusual market conditions or the lack of a ready market for any particular option at a specific time may reduce the effectiveness of the Composite's option strategy, and for these and other reasons the Composite's option strategy may not reduce the volatility to the extent desired.

Performance data shown represents past performance and is no guarantee of, and not necessarily indicative of, future results. A more detailed description of Gateway's standardized fees is included in Form ADV, Part 2.

The Annual Disclosure Presentation for the Gateway Index/RA Composite is included with this document. Additional copies are available upon request by calling 513.719.1100.

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Data Source: Gateway Investment Advisers, LLC and Morningstar DirectSM

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