



Asset Strategy Consultants

MARKET ENVIRONMENT

First Quarter 2016

Market Environment: U.S. Economy

The first quarter of 2016 revealed a dramatic tale of two halves, split nearly evenly between "risk off" and "risk on" sentiment. Falling commodity prices and broad-based concerns over global economic growth contributed to poor performance in both the equity and corporate bond markets, as well as a sharp rally in US Treasuries through mid-February. February 11th marked the intra-quarter low in US stocks, oil prices, high yield bonds and risk appetite.

- Real GDP growth in the US for 4Q15 was +1.4% revised upward from initial estimate of 0.7%
 - The US remains a bright spot among global economies
 - Fed GDP forecasts, currently at 2.2% for 2016, have been declining given global headwinds and US dollar strength
- Inflation remained below the Fed's 2% target for the Personal Consumption Index ("PCE")
 - PCE Index +1.7% y-o-y as of February but has trended higher (was 1.3% y-o-y in November of 2015)
 - Core CPI has also been rising +2.3% (y-o-y) as of February
- Oil
 - Continued to drive market sentiment throughout the quarter
 - Hit low of \$26 on Feb 11 but closed quarter at \$37 (WTI)
- US Labor market continued to improve
 - Robust job gains
 - Unemployment at 5%
 - Even wages were up, albeit modestly (+2.3% y-o-y)
- Manufacturing
 - After significant weakness in 2015, begins to show signs of improvement at quarter-end
 - March's Institute for Supply Management Index expanded for the first time since last summer
- Car Sales & Housing
 - Car sales remain solid, helped by low rates and low unemployment
 - New-home construction in the U.S. rose more than economists forecast in February with strongest single-family building in more than 8 years
- Weakness outside of US
 - Bank of Japan shocked investors by cutting its benchmark rate to -0.1%
 - European Central Bank also surprised investors with handful of new measures aimed at battling deflation and bolstering the economy
 - Continued uncertainty over magnitude and path of China's slowdown



Market Environment: Fixed Income

US Treasuries posted their best first quarter return since 2008 as yields dropped nearly 50 bps from year-end. The Barclays US Treasury Index returned 3.2% for the quarter. The dollar weakened on dovish comments from the Fed rates fell across developed markets.

- Barclays U.S. Aggregate Index returned 3.0% for the quarter
 - Investment grade corporate bonds underperformed in January and early February before rebounding with oil and stocks through quarter-end
 - Financials underperformed Treasuries while Industrials benefited from a rebound in commodity prices
- High yield gyrated
 - Barclays High Yield Index was up 3.4% for the quarter but fell roughly 5% through Feb 11 before retracing losses
- Municipal bonds underperformed Treasuries but posted solid results
 - Barclays Municipal Bond Index returned 1.7% for the quarter with the Barclays 1-10 Year Blend up 1.2%
 - Longer maturity and lower quality performed the best
- Interest rates in developed markets fell and the dollar weakened
 - The yen gained 7% and the euro appreciated 5% vs. the dollar
 - Brexit worries put pressure on the pound, down 3% vs. the greenback
 - Yields dropped across the board on worries over pallid growth and deflation
 - Barclays Global Aggregate returned 5.9% (+3.3% hedged)
 - Unhedged returns approached 10% for many countries, including Japan which was up nearly 12% on the back of falling rates combined with yen strength
- Emerging markets produced strong returns
 - Dollar-denominated JPM EMBI Global Diversified Index up 5%
 - Local currency-denominated JPM GBI-EM Global Diversified Index up 11%



Market Environment: Global Equity

Equities commenced the quarter on very weak footing with many indices down more than 5%, and some as much as 10%, in the month of January. The weakness continued through mid-February at which point the S&P 500 staged a strong rally through quarter-end. Foreign equities followed a similar path as their domestic counterparts; however, most broad indices failed to fully recover and posted declines for the quarter.

U.S. EQUITY

- Results were mixed over the quarter
 - S&P 500 up 1.3%
 - Russell Midcap gained 2.2%
 - Small caps lost value (R2000: -1.5%)
 - Corporate profits down 8% in the 4th quarter
- Sector results were widely divergent
 - Defensive sectors performed best; Telecom (+16.6%) and Utilities (+15.6%)
 - Financials (-5.1%) and Health Care posted the worst returns (-5.5%)
 - High quality strongly outperformed low quality (+6.3% vs -0.0%)
- Value outperformed growth and large outperformed small
 - R1000 Growth: +0.7%
 - R1000 Value: +1.6%
 - R1000: +1.2%
 - R2000: -1.5%

INTERNATIONAL EQUITY

- Developed markets trailed US but dollar weakness helped to mitigate losses
 - MSCI EAFE Local: -6.4%
 - MSCI EAFE US\$: -3.0%
 - Japan was among the worst (local: -12.5%; US\$: -6.4%)
- Emerging markets fared better
 - MSCI EM US\$: +5.8%
 - After a 41% loss in 2015, Brazil was the quarter's top performer (+29%)
 - Russia was also strong (+16%)
 - India: -2.5%
 - China: -4.8%



Market Environment: Liquid Real Assets & Hedge Funds

Liquid real assets produced mixed results and hedge funds failed to keep pace with the broad stock and bond markets.

- Inflation remained benign but trended higher
 - Core CPI +2.3% (y-o-y) as of February
 - Ex-food and energy a more muted +1.0% y-o-y
- Oil prices bottomed
 - WTI hit \$26 but closed the quarter at \$37
- Gold was the star performer at +16%
 - Best quarterly performance since 1986
- MLPs continued to fall
 - Alerian MLP: -4.2%; -31.8% y-o-y
- REITs held up relatively well
 - NAREIT Equity: +6.0%
- TIPS outperformed nominal Treasuries
 - Barclays TIPS Index: +4.5% vs Barclays US Treasury +3.2%
 - Breakeven spread widened to 1.62% as of quarter-end
- Hedge funds underperformed stocks and bonds
 - HFRI Fund Weighted Composite (HFRI FWC: -0.8%)
 - Hedge Fund of Funds (HFRI FoF: -2.5%)
- Macro did the best
 - HFRI Macro: +1.2%



Returns for Various Periods

	Month Ending			Last Quarter	Last 2 Quarters	Last 3 Quarters	Last Year	Last 3 Years	Last 5 Years	Last 10 Years	Last 15 Years
	Jan-31	Feb-29	Mar-31								
MSCI:ACWI	-6.01	-0.63	7.48	0.38	5.55	-4.30	-3.81	6.10	5.80	4.63	5.63
Russell:3000 Index	-5.64	-0.03	7.04	0.97	7.30	-0.48	-0.34	11.14	11.01	6.90	6.38
Russell:3000 Growth	-5.97	-0.09	6.81	0.34	7.45	1.08	1.35	13.16	12.00	8.09	6.09
Russell:3000 Value	-5.29	0.03	7.29	1.65	7.15	-2.05	-2.05	9.09	9.95	5.60	6.54
<u>MegaCap</u>											
Russell:Top 50	-4.13	-0.95	6.36	1.00	10.43	4.34	5.87	11.80	11.83	6.83	--
Russell:Top 200	-4.90	-0.51	6.46	0.73	8.52	1.66	2.55	11.98	11.80	6.92	5.29
Russell:Top 200 Growth	-4.80	-0.66	6.59	0.81	9.51	4.99	5.74	14.74	13.44	8.71	5.59
Russell:Top 200 Value	-5.01	-0.34	6.32	0.65	7.45	-1.74	-0.72	9.19	10.12	5.11	5.03
<u>Large Cap</u>											
S&P:500	-4.96	-0.13	6.78	1.34	8.48	1.50	1.78	11.82	11.58	7.01	5.98
S&P:500 HQ	-2.04	2.24	6.14	6.30	12.53	8.43	7.06	14.49	14.34	7.98	8.03
S&P:500 LQ	-9.69	0.53	10.11	-0.03	5.76	-4.77	-5.89	11.00	10.05	7.80	8.82
Russell:1000 Index	-5.38	-0.03	6.97	1.18	7.75	0.39	0.51	11.52	11.35	7.06	6.28
Russell:1000 Growth	-5.58	-0.04	6.74	0.74	8.11	2.39	2.51	13.61	12.38	8.28	6.03
Russell:1000 Value	-5.17	-0.03	7.20	1.64	7.36	-1.65	-1.54	9.38	10.25	5.72	6.40
<u>MidCap</u>											
S&P:400 Mid Cap	-5.69	1.41	8.52	3.79	6.49	-2.56	-3.59	9.46	9.52	7.78	9.42
Russell:Midcap	-6.55	1.13	8.19	2.24	5.94	-2.54	-4.04	10.45	10.30	7.45	9.11
Russell:Midcap Growth	-7.57	1.57	7.14	0.58	4.72	-3.64	-4.74	10.99	10.00	7.43	7.95
Russell:Midcap Value	-5.53	0.70	9.23	3.92	7.16	-1.45	-3.39	9.88	10.52	7.23	9.66
<u>Small Cap</u>											
S&P:600 Small Cap	-6.17	1.12	8.20	2.66	6.48	-3.39	-3.20	10.39	10.41	6.99	9.60
Russell:2000 Index	-8.79	0.00	7.98	-1.52	2.02	-10.14	-9.76	6.84	7.20	5.26	7.65
Russell:2000 Growth	-10.83	-0.71	7.66	-4.68	-0.57	-13.55	-11.84	7.91	7.70	6.00	6.86
Russell:2000 Value	-6.72	0.68	8.29	1.70	4.63	-6.60	-7.72	5.73	6.67	4.42	8.22
Russell:Microcap	-10.35	-1.51	7.09	-5.43	-1.90	-15.41	-13.05	6.34	6.61	3.18	7.60
<u>Non-US Equity</u>											
MSCI:ACWI ex US	-6.79	-1.11	8.21	-0.26	3.03	-9.43	-8.78	0.77	0.76	2.40	5.43
MSCI:EAFE US\$	-7.23	-1.83	6.51	-3.00	1.57	-8.83	-8.27	2.23	2.30	1.80	4.35
MSCI:EAFE Gr w/ net div	-6.36	-1.74	6.42	-2.08	4.45	-4.66	-3.70	3.80	3.70	2.92	4.43
MSCI:EAFE Val w/net div	-8.13	-1.93	6.60	-3.96	-1.39	-13.00	-12.81	0.59	0.82	0.60	4.16
MSCI:EAFE Small Cap	-7.86	-0.12	8.02	-0.59	6.16	-1.10	3.20	7.29	5.58	3.45	8.86
MSCI:Emer Markets	-6.48	-0.15	13.26	5.76	6.53	-12.41	-11.70	-4.15	-3.80	3.34	9.69
<u>Fixed Income</u>											
Barclays:Aggregate Index	1.38	0.71	0.92	3.03	2.45	3.71	1.96	2.50	3.78	4.90	4.97
Barclays:US TIPS Index	1.48	1.11	1.80	4.46	3.79	2.61	1.51	-0.71	3.02	4.62	5.49
Barclays:Gov/Credit Long	2.10	2.19	2.84	7.30	6.29	8.61	0.39	4.81	8.51	7.57	7.38
Barclays:Credit A Long	1.01	1.78	3.64	6.56	6.37	9.08	0.86	5.05	8.24	6.94	7.03
Barclays:High Yield CP	-1.61	0.57	4.44	3.35	1.21	-3.71	-3.71	1.84	4.95	7.01	7.48
Barclays:Muni 1-10 Blend	1.08	0.24	-0.07	1.24	2.05	3.39	2.87	2.50	3.68	4.21	4.17
Barclays:Gl Agg xUS UH	0.50	3.49	4.09	8.26	6.90	7.58	6.68	-0.32	0.39	3.89	5.50
Barclays:Gl Agg xUS DH	1.58	1.18	0.71	3.51	4.13	5.67	2.85	4.55	5.16	4.67	4.61
JPM:EMBI+	0.65	1.97	3.22	5.93	7.81	6.81	5.88	2.78	6.08	7.12	8.96
<u>Other Assets</u>											
Bloomberg Commodity	-1.68	-1.63	3.82	0.42	-10.14	-23.14	-19.56	-16.87	-14.15	-6.16	-0.53
S&P GSCI	-5.17	-2.01	4.93	-2.50	-18.71	-34.40	-28.67	-24.49	-17.43	-10.66	-3.69
Gold (S&P Spot Price Index)	5.30	10.57	0.10	16.55	10.80	5.45	4.43	-8.17	-3.01	7.73	10.97
NAREIT Equity Index	-3.35	-0.42	10.14	6.00	13.69	15.97	4.43	10.47	11.89	6.56	11.57
Alerian MLP Index	-11.10	-0.48	8.32	-4.17	-6.82	-27.41	-31.84	-10.32	-0.56	7.67	10.99

