



Asset Strategy Consultants

MARKET ENVIRONMENT

Third Quarter 2016

Market Environment: Economy

Investor angst over the unexpected vote on Brexit was short-lived with a "risk-on" theme returning to the markets in July and leading to stock market highs for the Dow, NASDAQ and S&P 500 in August. Growth remained slow but steady both in the US and overseas, with continued accommodation from central banks and tepid inflation.

- Real GDP was revised modestly higher to +1.4% for the 2nd quarter
 - Consumer spending remained robust at a growth rate of 4.3% while residential investment slowed
 - Fed policymakers now expect growth for all of 2016 to be 1.8%, down from the June expectation of 2.0%
- Fed leaves Fed Funds rate unchanged
 - But sentiment shifts; three dissenting votes at September meeting
 - Market pricing in roughly 50% chance of Fed hike before year-end
- Inflation remained subdued
 - Core PCE Index +1.7% y-o-y as of August; below Fed's 2% target but highest in six months
 - Core CPI +2.3% as of August but Headline only +1.1%
- Unemployment hangs at 4.9%
 - Job creation remains steady
 - Wage growth increases to 2.4% y-o-y
- Consumer Confidence hits highest level since 2007
 - According to the Conference Board's Index
- House prices continue to climb
 - Average price of single family existing home (\$274,000) approaching high reached in October 2005 (\$275,000)
- Euro zone economies remain weak but positive
 - Euro zone unemployment remains elevated at 10%
 - Euro zone GDP +0.3% in 2nd quarter, down from 1st quarter's 0.5% print
 - Inflation has edged up and is no longer falling; core inflation +0.8% still well short of 2%
 - Talks surfaced late in the quarter of ECB tapering bond purchase program earlier than expected



Market Environment: Fixed Income

Yields in the US moved modestly higher during the 3rd quarter with the 10-year US Treasury yield rising 11 bps to close at 1.60%. However, the Treasury note did hit a record low of 1.37% on July 8th at the height of the Brexit-induced worries before trending higher through the remainder of the quarter. A risk-on theme propelled returns of riskier bonds higher.

- Bloomberg Barclays U.S. Aggregate Index returned +0.5% for the quarter; +5.8% y-t-d
 - Investment grade corporate bonds outperformed, lower quality performed the best
 - US Credit Index +1.2%; +8.9% y-t-d in spite of robust issuance
 - Bloomberg acquires Barclays indices and rebrands as Bloomberg Barclays
- High yield top performer
 - BB Barclays High Yield Index was up 5.6%; 15.1% y-t-d
 - Lower quality performed best
- Municipal bonds underperformed Treasuries
 - Record supply in August; much of it for new projects rather than refinancing
 - BB Barclays Municipal Bond Index returned -0.3%; +4.0% y-t-d
 - Shorter duration BB Barclays 1-10 Year Blend -0.1%; +2.6% y-t-d
- TIPS outperformed nominal Treasuries
 - BB Barclays TIPS Index +1.0% for the quarter
 - 10-year breakeven spreads widened to 1.60%
- Interest rates in developed markets fell, mostly
 - Mexico and Japan saw rising yields but yields fell elsewhere
 - Negative yielding government debt now exceeds \$12 trillion
 - BB Barclays Global Aggregate ex-US +1.0% (+13.1% y-t-d)
 - Yen and euro gained just over 1% versus the dollar, while pound weakened nearly 3%
 - Hedged indices modestly underperformed unhedged
- Emerging markets debt outperformed
 - Dollar-denominated JPM EMBI Global Diversified Index +4%; +15% y-t-d
 - Local currency-denominated JPM GBI-EM Global Diversified Index +3%; +17% y-t-d



Market Environment: Global Equity

Reduced fears of slowing global growth, particularly in China, optimism about the U.S. economy, and further delays in rate hikes contributed to a rebound in equity prices in the 3rd quarter. The S&P 500, Dow, and NASDAQ hit all-time highs in August. Non-US markets outperformed US and emerging markets' indices posted the best results.

U.S. Equity

- Small capitalization stocks outperformed
 - S&P 500 +3.9%; +7.8% y-t-d
 - Russell Mid Cap gained 4.5%; +10.3% y-t-d
 - Russell 2000 rose 9.1%; +11.5% y-t-d
 - Growth exceeded Value modestly across market capitalizations, helped by Tech and less exposure to Utilities and Telecom
- Investors preferred income so far in 2016
 - High Dividend Yield (+13.2% y-t-d) was the strongest among MSCI's factor-based indices
 - Quality (+6% y-t-d) was the weakest
- Real Estate became the 11th top-line sector in GICS
 - Representing 3.1% of the S&P 500

International Equity

- Developed markets outperformed US
 - MSCI EAFE: +6.4%; +1.7% y-t-d
 - Best performers were Germany (+10.0%) and Austria (+16.7%)
 - Worst was Denmark (-6.3%)
- Emerging markets surged for the quarter
 - MSCI EM: +9.0%; +16% y-t-d
 - Brazil continued to rebound: +11.3% for the quarter; +62.9% y-t-d
 - Russia and China were also strong; +8.4% and +13.9% respectively
 - Turkey lagged at -5.3%; +6.1% y-t-d
 - India: +5.9%; +7.1% y-t-d



Market Environment: Liquid Real Assets

Prices for liquid real assets were relatively flat with commodities pulling back and TIPS posting modest positive returns.

- Oil prices fell but are flat year-to-date
 - WTI fell 5% during the quarter; -0.1% y-t-d
- Gold declined modestly
 - Down 1% for the quarter but up 23% y-t-d
- Bloomberg Commodity Index -3.9% for the quarter; +8.9% y-t-d
- MLPs up modestly
 - Alerian MLP: +1.1%; +15.9% y-t-d
- REITs down slightly
 - NAREIT Equity: -1.4%; +11.8% y-t-d
- Inflation remained benign
 - Core CPI +2.3% (y-o-y) as of August
 - Headline CPI a more muted +1.1%
- TIPS outperformed nominal Treasuries
 - Barclays US Treasury Index -0.3%; Barclays US TIPS Index +1.0%
 - 10-year breakeven spreads widened to 1.60% from 1.40% over the quarter



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
	Sep-30	Aug-31	Jul-31								
MSCI:ACWI	0.61	0.34	4.31	5.30	6.34	6.60	11.96	5.17	10.63	4.34	6.47
Russell:3000 Index	0.16	0.26	3.97	4.40	7.14	8.18	14.96	10.44	16.36	7.37	7.61
Russell:3000 Growth Index	0.45	-0.38	4.86	4.92	5.76	6.12	13.64	11.40	16.56	8.80	7.46
Russell:3000 Value Index	-0.13	0.90	3.09	3.87	8.62	10.40	16.38	9.46	16.09	5.84	7.59
MEGA CAP											
Russell:Top 50	-0.10	0.15	3.33	3.38	5.70	6.75	16.72	11.51	15.68	6.69	--
Russell:Top 200	0.03	0.29	3.51	3.84	6.19	6.96	15.23	11.25	16.29	7.05	6.45
Russell:Top 200 Growth	0.52	-0.57	4.64	4.58	4.83	5.67	14.80	13.12	16.94	9.06	6.82
Russell:Top 200 Value	-0.49	1.22	2.31	3.05	7.69	8.39	15.71	9.36	15.61	5.03	6.08
LARGE CAP											
S&P:500	0.02	0.14	3.69	3.85	6.40	7.84	15.43	11.16	16.37	7.24	7.15
S&P:500 HQ	-1.19	-0.08	2.50	1.20	3.68	10.20	16.66	12.68	17.46	8.00	8.59
Russell:1000 Index	0.08	0.13	3.81	4.03	6.67	7.92	14.93	10.78	16.41	7.40	7.48
Russell:1000 Growth	0.37	-0.50	4.72	4.58	5.22	6.00	13.76	11.83	16.60	8.85	7.35
Russell:1000 Value	-0.21	0.77	2.90	3.48	8.22	10.00	16.20	9.70	16.15	5.85	7.46
MID CAP											
S&P:400 Mid Cap	-0.64	0.50	4.29	4.14	8.30	12.40	15.33	9.35	16.50	9.11	10.42
Russell:Midcap Index	0.20	-0.25	4.57	4.52	7.84	10.26	14.25	9.70	16.67	8.32	10.44
Russell:Midcap Growth	-0.05	-0.29	4.95	4.59	6.23	6.84	11.24	8.90	15.85	8.51	9.66
Russell:Midcap Value	0.42	-0.21	4.24	4.45	9.43	13.72	17.26	10.49	17.38	7.89	10.72
SMALL CAP											
S&P:600 Small Cap	0.64	1.36	5.09	7.20	10.93	13.88	18.12	9.04	17.86	8.71	10.78
Russell:2000 Index	1.11	1.77	5.97	9.05	13.18	11.46	15.47	6.71	15.82	7.07	9.26
Russell:2000 Growth	1.44	1.06	6.54	9.22	12.76	7.48	12.12	6.58	16.15	8.29	8.90
Russell:2000 Value	0.79	2.49	5.40	8.87	13.55	15.49	18.81	6.77	15.45	5.78	9.38
Russell:Microcap	2.94	2.70	5.23	11.25	15.66	9.38	13.47	5.84	16.37	5.50	8.85
NON-US EQUITY											
MSCI:ACWI ex US	1.23	0.63	4.95	6.91	6.22	5.82	9.26	0.18	6.04	2.16	6.56
MSCI:EAFE	1.23	0.07	5.07	6.43	4.88	1.73	6.52	0.48	7.39	1.82	5.81
MSCI:EAFE Growth	1.49	-1.41	4.89	4.96	4.80	2.63	9.47	2.39	8.73	3.14	6.13
MSCI:EAFE Value	0.97	1.62	5.26	7.99	4.98	0.82	3.52	-1.49	5.99	0.44	5.41
MSCI:EAFE Small Cap	2.97	-0.59	6.13	8.64	5.82	5.19	12.33	5.08	11.07	4.39	10.20
MSCI:EM	1.29	2.49	5.03	9.03	9.75	16.02	16.78	-0.56	3.03	3.94	11.55
FIXED INCOME											
BB Barclays:Aggregate Idx	-0.06	-0.11	0.63	0.46	2.68	5.79	5.19	4.03	3.08	4.79	4.80
BB Barclays:US TIPS Index	0.55	-0.45	0.87	0.97	2.69	7.27	6.58	2.40	1.93	4.48	5.39
BB Barclays:Long Gov/Cr	-1.26	-0.03	2.55	1.24	7.87	15.74	14.65	10.08	6.32	7.84	7.61
BB Barclays:Long Credit A	-1.21	0.13	2.89	1.78	7.92	15.00	14.79	9.90	7.09	7.19	7.27
BB Barclays:High Yield CP	0.67	2.09	2.71	5.56	11.39	15.12	12.73	5.28	8.33	7.71	8.62
BB Barclays:Mn 1-10(1-12)	-0.30	-0.02	0.22	-0.11	1.33	2.59	3.40	3.34	2.95	4.04	4.02
BB Barclays:Gl Agg ex US	1.02	-0.81	0.82	1.03	4.47	13.10	11.67	0.75	0.70	3.82	5.41
BB Barclays:Gl Agg x US H	0.02	-0.04	0.55	0.53	3.26	6.89	7.53	5.78	5.04	4.68	4.65
JPM:Emer Mkt Bond +	0.46	1.76	0.86	3.11	9.29	15.78	17.82	7.99	7.35	7.62	9.75
OTHER ASSETS											
BLMBRG:TR Idx	3.13	-1.76	-5.11	-3.86	8.42	8.87	-2.58	-12.34	-9.37	-5.33	0.57
GS Commodity Index	4.14	1.77	-9.57	-4.15	7.99	5.30	-12.21	-22.16	-12.61	-9.04	-2.19
S&P:Gold Spot Price Ix	0.43	-3.40	2.79	-0.27	6.60	24.23	18.10	-0.25	-4.08	8.10	10.51
FTSE:NAREIT Equity Index	-1.76	-3.67	4.15	-1.43	5.42	11.75	19.86	14.22	15.91	6.35	11.38
Alerian:MLP Index	1.85	-1.31	0.56	1.07	20.98	15.94	12.74	-4.82	4.96	9.01	11.16

