November Update | As of October 31, 2015

OCTOBER 2015 IN REVIEW

ECONOMY:
U.S. GROWTH REMAINS STABLE DESPITE HEADWINDS

Economic Data

October economic data, which mostly capture September economic activity, came in at levels that broadly indicated that the economy continued to expand, but at a rate below its long-term trend. Economic reports on the whole were modestly weaker than expected, with downside surprises from several key housing reports providing the largest misses following strong data over the summer. Outside of a disappointing headline jobs number, labor market data provided some of the strongest upside surprises, highlighted by weekly unemployment claims, whose four-week moving average fell to its lowest level in more than 40 years.

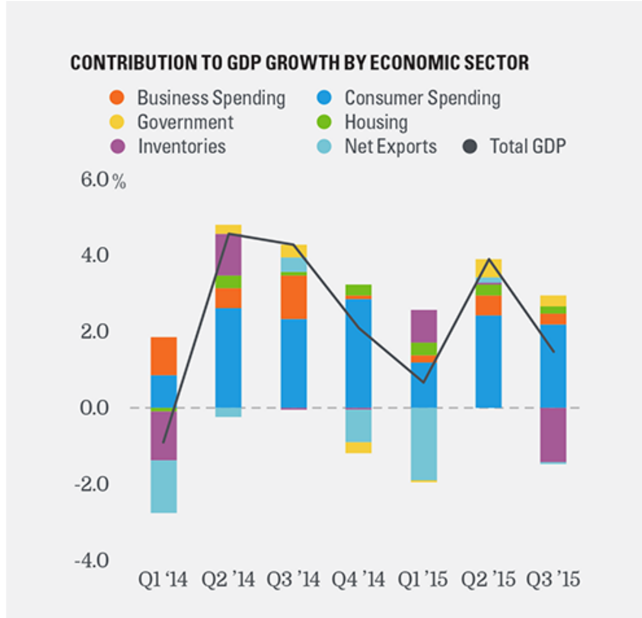
October saw the release of the advance estimate of third quarter gross domestic product (GDP). While GDP growth of 1.5% was largely in-line with expectations, it was the lowest rate of growth since the first quarter. Underlying data were stronger than the headline number would indicate. Much of the slowdown was due to falling inventories, the GDP component that has the strongest tendency to bounce back as low inventories drive restocking. Consumer spending, the largest element of GDP, grew a healthy 3.2%, the fifth time in the last eight quarters that it topped 3% after not reaching that level at all in the prior two years. The contribution of net exports to GDP growth was near neutral for the second quarter in a row, while fixed private investment had slowed but still posted a healthy 2.9% growth. Overall, the numbers indicate the resilience of the U.S. economy despite the slowdown in manufacturing and the impact of the strong dollar on the trade deficit.

Manufacturing continues to be closely watched, as a strong dollar, cuts in oil-related capital expenditures, and slower growth in China continue to create headwinds. Markit's manufacturing Purchasing Managers' Index (PMI) for September held steady at 53.1, but the Institute for Supply Management's (ISM) manufacturing PMI decelerated from 51.1 to 50.2. A level above 50 indicates expansion. U.S. manufacturing continues to hang tough despite headwinds, while the much larger services sector continues to power ahead, with both ISM's and Markit's

INITIAL CLAIMS FOR UNEMPLOYMENT, 4-WEEK AVERAGE

service sector PMIs remaining above 55.

Key leading indicators continue to imply a below historical chance of recession in the next 12 months. The Conference Board's Leading Economic Index (LEI), an aggregate of leading indicators, grew 3.4% year over year in September. The largest detractor for the month, S&P 500 stock prices, should be a strong positive contributor in October after the index posted its best one-month return since 2011. While economic surprises, as measured by the Citi Economic Surprise Index, continue to disappoint to the downside, the level has been improving and was approaching flat near the end of the month, indicating that economists' expectations right now are in-line with economic performance.



Central Banks

The Federal Reserve's (Fed) policy arm, the Federal Open Market Committee (FOMC), surprised markets by releasing a somewhat more hawkish than expected policy statement following its October 27–28 meeting. In the October statement, the FOMC removed language about the potential negative impact of international risks, although it retained language that it would continue to monitor international developments. It also pointedly discussed criteria for raising rates at its December meeting. Interest rates and fed fund futures markets, which had substantially pushed back rate hike expectations since a somewhat cautious statement following the FOMC's September meeting, quickly pulled expectations forward. The implied probability of a rate increase in December jumped from about 30% to 50% following the meeting, according to fed fund futures.

The European Central Bank (ECB) did not introduce additional easing at its October meeting, but ECB President Mario Draghi signaled that the ECB may expand its quantitative easing (QE) program if needed, eliciting a positive market response. The Bank of Japan (BOJ) also left its policy unchanged at its October 30 meeting, disappointing rising expectations that it would expand easing measures. Unlike the ECB and BOJ, China's central bank, the People's Bank of China, did take action in October, cutting interest rates for the sixth time in a year as it continues to try to stimulate its slowing economy and fight deflation.

GLOBAL EQUITIES:

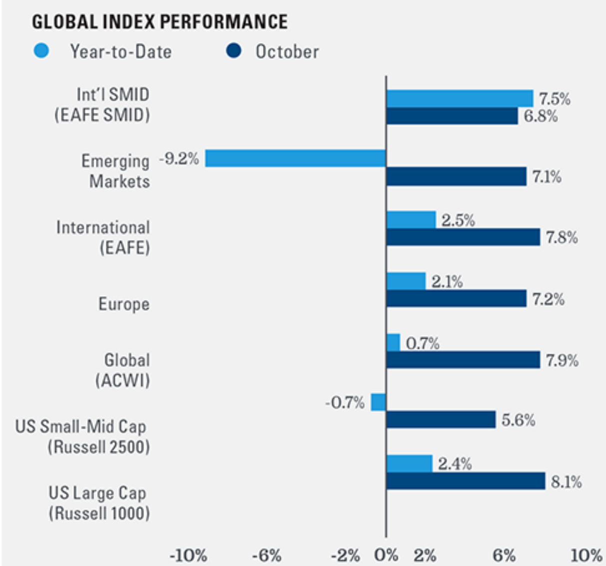
GROWTH CONCERNS DRIVE LOSSES, BUT DECLINES SLOW

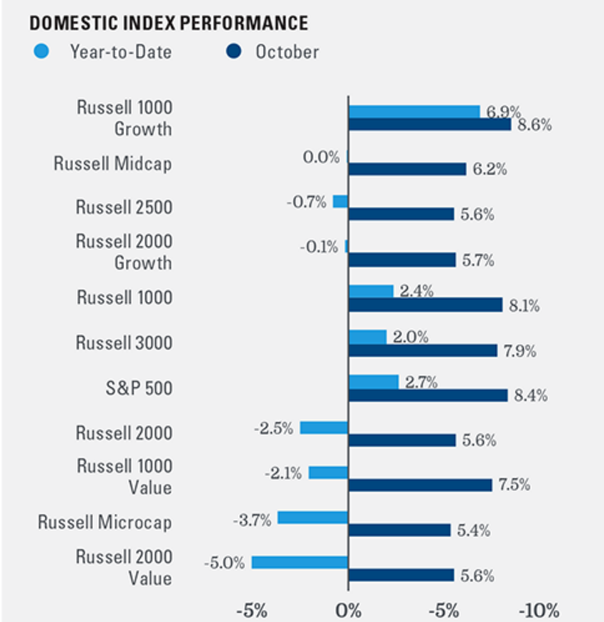
U.S.

October saw U.S. stocks, as measured by the S&P 500 Index, post their best monthly return since October 2011. The October run was supported by some bargain hunting in materials and energy (the two most beaten up sectors year to date), better than expected earnings, and improved sentiment on China. Investors' willingness to take on more risk was also supported by the resolution of potential political standoffs over the debt ceiling and funding for the federal government. Against the backdrop of Paul Ryan's ascension to Speaker of the House, the White House and congressional leaders reached a deal on a two-year budget plan and suspension of the debt limit into March 2017.

Small caps, and to a lesser extent mid caps, did not fully participate in the rally, underperforming large cap across styles, according to Russell Indexes. The drag was less about any deficiency in small caps and more likely about some high-profile large cap names posting strong earnings. Growth outperformed value across cap sizes, although the spread was not large, with value getting a small extra boost from significantly higher exposure to the energy sector. Utilities, despite posting a positive return, lagged all other sectors by more than 5% in October, weighed down by rising interest rates pushed higher by the market's response to the October FOMC meeting.

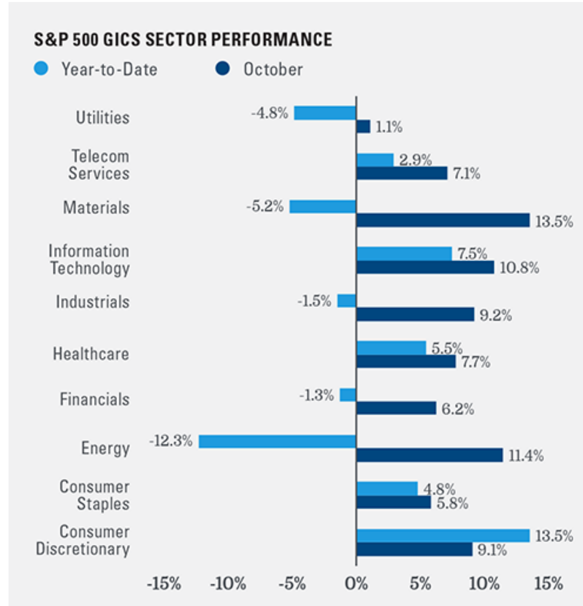
With nearly three-fourths of S&P 500 companies having reported as of October 30, earnings for the third quarter of 2015 are still projected to contract 1%, according to Thompson Reuters estimates, but a strong 72% beat rate has lifted expectations from -4.1% as of the start of the quarter. The current beat rate, if it holds, would be the highest since the third quarter of 2014. Every sector except financials has seen earnings expectations for the third quarter improve, with energy (off of very low expectations) and healthcare the standouts. In absolute terms, third quarter blended earnings growth expectations are highest for the consumer discretionary, financials, healthcare, and telecom sectors.





International

International shares also posted a strong October but lagged behind the U.S., with emerging markets trailing international developed by a small margin, according to MSCI Indexes. Even though international stocks lagged behind the U.S., the dampening of international growth concerns that helped support U.S. markets also lifted markets abroad, including supportive comments from the ECB and central bank action in China. Eurozone earnings expectations, while not robust, remain in positive territory year over year, ahead of the U.S., as the economy continues to show improvement. Emerging market performance was helped by China, which continues to recover from its dramatic midyear swoon as investors adjust to a lower growth trajectory, while investors continue to remain somewhat wary of emerging market commodity producers.



FIXED INCOME:

INTEREST RATES RISE AS GLOBAL GROWTH CONCERNS FADE

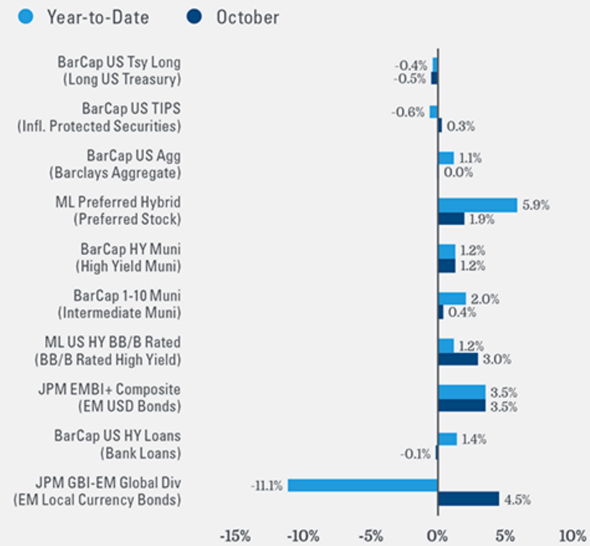
Interest rates rose modestly across the maturity spectrum during October, with the 10-year Treasury yield rising from 2.06% to 2.16% and the yield curve flattening slightly. Central bank action from China and indications of additional stimulus forthcoming from the ECB also helped boost growth expectations. The resultant rise in interest rates was a headwind for fixed income—the Barclays U.S. Aggregate was flat (+0.0%) on the month with interest income offset by price declines due to the slight rise in interest rates.

Fading concerns over China's economic slowdown led to gains for economically sensitive sectors such as high-yield bonds and emerging markets debt. Lower-rated bonds outperformed higher-quality issues as a result. High-yield returned 3.0% during the month, the index's largest gain since January 2012. Similarly, fears about an emerging markets slowdown also waned, leading to a tailwind for dollar-denominated emerging markets debt, which returned 3.5% during October.

Municipal bonds showed greater resilience than comparable maturity Treasuries amid the backdrop of rising interest rates. The Barclays Municipal 7-Year (6–8) Index returned 0.6% during October, while the Barclays Treasury Index returned -0.4%.

Inflation expectations also rose over October, partially driven by the Fed's hawkish October FOMC meeting statement. The Fed's preferred inflation indicator, the five-year, five-year forward inflation expectation rate, rose from 1.75% to 1.86% during October, leading to a 0.3% return for the Treasury Inflation-Protected Securities (TIPS) Index, outperforming the broader bond market, as represented by the Barclays U.S. Aggregate Index.

FIXED INCOME PERFORMANCE



US TREASURY YIELDS

Security	9/30/15	10/31/15	Change in Yield
3 Month	0.00	0.08	0.08
2 Year	0.64	0.75	0.11
5 Year	1.37	1.52	0.15
10 Year	2.06	2.16	0.10
30 Year	2.87	2.93	0.06

AAA MUNICIPAL YIELDS

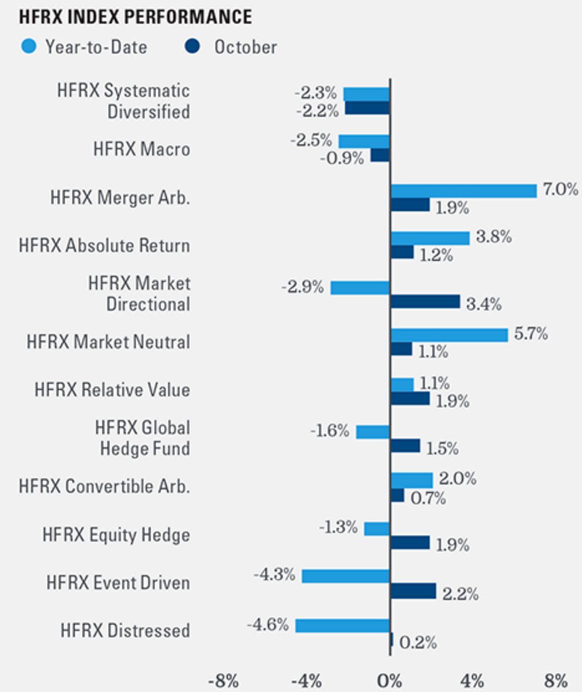
Security	9/30/15	10/31/15	Change in Yield
2 Year	0.65	0.65	0.00
5 Year	1.37	1.33	-0.04
10 Year	2.31	2.28	-0.03
20 Year	3.77	3.76	-0.01
30 Year	4.45	4.43	-0.02

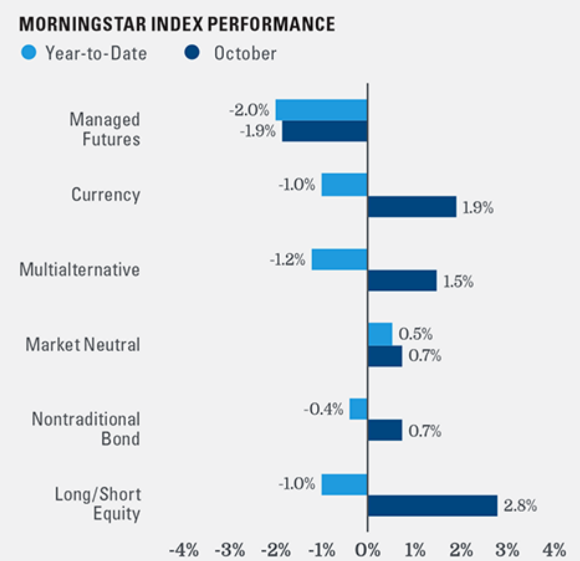
ALTERNATIVES:

EQUITY RALLY SUPPORTS BROAD AI GAINS

With the S&P 500 delivering an impressive 8.4% rebound in October, all equity-centric alternative investments provided gains, albeit with differing levels of success. On a risk-adjusted basis, equity market neutral managers continued to outperform their more directional long/short peers, as the HFRX Equity Market Neutral Index returned 1.1% (5.7% year to date), with a negative 0.02 beta, an indication of strong stock selection and alpha generation, a difficult task to accomplish during a broad market rally. At 1.9%, performance from long/short managers in the HFRX Equity Hedge Index was relatively lackluster, as the group only captured 22% of the S&P 500's monthly gains. Overall, many strategies retained a more conservative stance during October, as managers were cognizant of the recent losses suffered during an extremely volatile September. This reduction in exposure can be seen in the index's beta profile, which declined from an average of 0.43 during the third quarter to only 0.30 in October. Event driven strategies recovered from an extremely difficult September, during which overweight exposure to biotech and healthcare-related events weighed heavily on returns. The broad-based HFRX Event Driven Index returned 2.2%, while the best performance was seen in the Special Situations sub-category, with a rebound of 3.1%. Much of these gains were driven by positions in the energy sector, which rallied 11.4% during the month.

Systematic macro strategies declined 2.2%, as long U.S. government debt and short commodity exposure detracted from returns. The profitable long-term trend in Treasury debt was interrupted by a back-up in rates after the October FOMC meeting. Many market participants believed language from the statement left open the possibility for a rate hike at their next meeting in mid-December. For those managers employing counter-trend or short-term models, equity contract gains helped offset these losses to a moderate extent.





LIQUID REAL ASSETS SHINE IN OCTOBER

In a stark reversal of recent months' activity, liquid real assets (LRA) performed admirably in October with most individual assets boasting positive returns. This occurred even with a modestly higher U.S. dollar. Risk assets in general did well, with the U.S. stock market showing strong returns and Treasury yields backing up.

MLPs & Global Listed Infrastructure

Master limited partnerships (MLPs), as measured by the Alerian MLP Index, bounced back from five straight monthly declines, returning 9.7% for the month of October and outpacing the S&P 500 Index for only the second time in the past six months. The index seemed to benefit from a recovery from what may have been a short-term oversold level that was reached in late September; in addition, it was helped by quarterly distribution announcements, which were positive. Of the quarterly distribution announcements released as of month-end, the majority were up from the prior quarter. A decent amount of distributions were flat, with a few decreases. Among midstream MLPs, there were no distribution cuts. Investors have been concerned about the viability of distribution growth for the asset class and, for the most part, may have been reassured by the announcements.

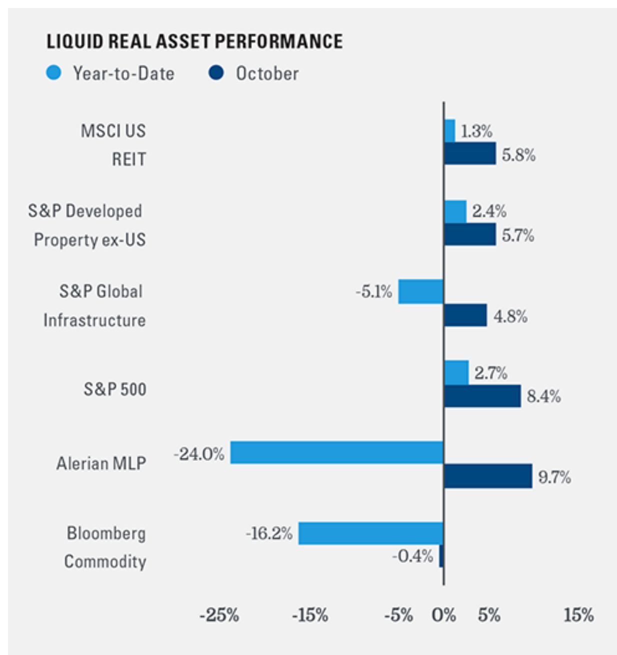
Global infrastructure, as measured by the S&P Global Infrastructure Index, returned 4.8% for the month. The year has been an up and down one for the asset class, as five months have ended in positive returns and five months have ended in negative territory. The index benefited from strong energy infrastructure returns.

REITs

Real estate investment trusts (REIT) continued their positive trend, now having gained ground in three of the last four months. Against a headwind of modestly rising rates, the MSCI US REIT Index was up 5.8% for the month. This performance did, however, lag that of the S&P 500. It remains to be seen how the asset class will react once certainty around Fed rate hikes arrives in the market.

Commodities

Commodities, broadly, were slightly negative for the month, returning -0.4%. Industrial metals (aluminum and copper) and natural gas weighed on the index's returns, while other large constituents—namely crude oil, gold, silver—were positive. Natural gas returned -8.0% in October after one particularly rough day of performance triggered by a bearish inventory report. WTI crude oil finished up 3.3%, a potentially encouraging sign for those looking for the attainment of market balance and a bottoming of the oil market. The Bloomberg Agriculture Subindex ended the month with an unremarkable 1.6% return, the smallest absolute monthly return for the subindex since April. Precious metals were up disparately in October with silver outperforming gold by 4.9%.



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