



ECONOMY: FED RAISES RATES FOR FIRST TIME IN ALMOST TEN YEARS

Economic Data

U.S. economic data released in December, which largely capture economic activity in November, continued to suggest a moderate pace of economic growth for the U.S. economy. Taken as a whole, the data surprised modestly to the downside during the month, signaling something closer to the below-trend growth we have experienced during much of the current expansion rather than the return to trend growth some have expected. The basic themes for the year continued to hold true.

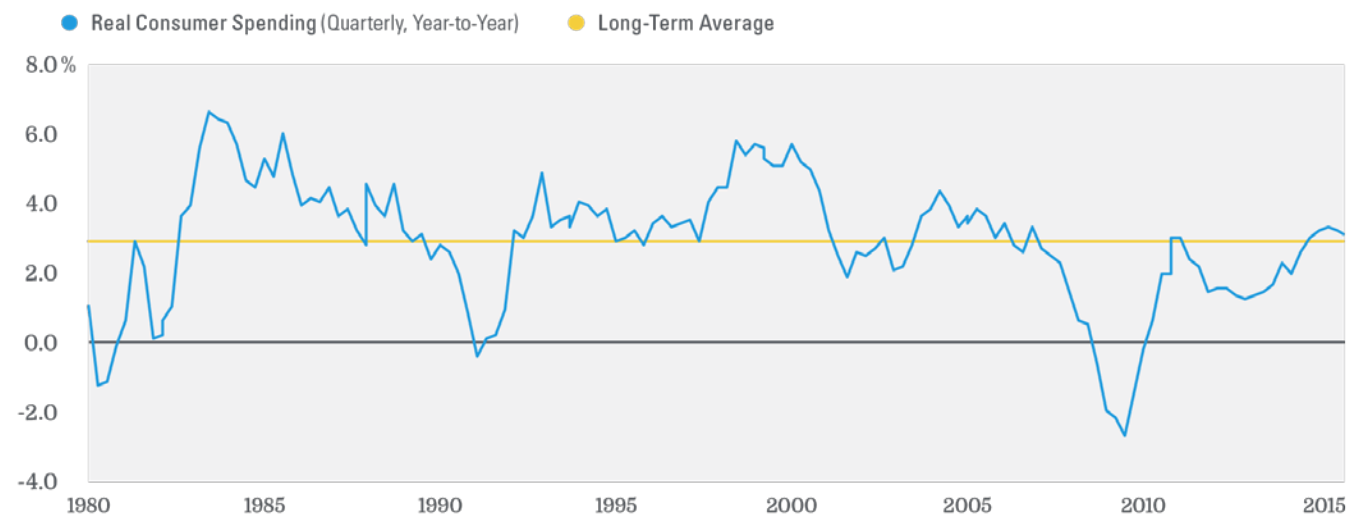
Manufacturing activity was sluggish as further declines in oil continued to weigh on capital expenditures in the oil patch and a strong dollar restricted demand for U.S. goods abroad; but U.S. consumers, who account for roughly two-thirds of gross domestic product (GDP), have

remained a bright spot, and the services sector continues to show steady expansion.

Labor markets continued to heal in November. The economy added 211,000 net new jobs, topping consensus expectations, with a strong upward revision of +27,000 to October's already robust number. The unemployment rate held steady at 5%, approximately the level of the long-term natural rate of unemployment according to the Congressional Budget Office (CBO). Stronger labor markets were reflected in several data points, including an upside surprise in personal income and consumer sentiment. Despite slower growth in the headline number for retail sales, underlying data showed meaningful areas of strength. Retail sales ex-auto and gas surprised to the upside, while some key discretionary spending categories such as restaurants, electronics and appliances, and clothing saw meaningful gains, suggesting a solid start to holiday shopping.

Manufacturing continued to weaken but has shown some resilience in the face of stiff headwinds from declining oil prices and falling export demand. The Institute for Supply Management's Manufacturing Purchasing Managers' Index (PMI) for November fell below 50, the level that indicates contraction, for the

REAL CONSUMER SPENDING GROWING NEAR LONG-TERM RATE



Source: LPL Research, Bureau of Economic Analysis 12/31/15

first time since 2012, but Markit's Manufacturing PMI for November topped expectations and remained in expansionary territory at 52.8. Markit's Services PMI for November showed steady growth in November, coming in at 56.1, similar to ISM's non-manufacturing composite (55.9).

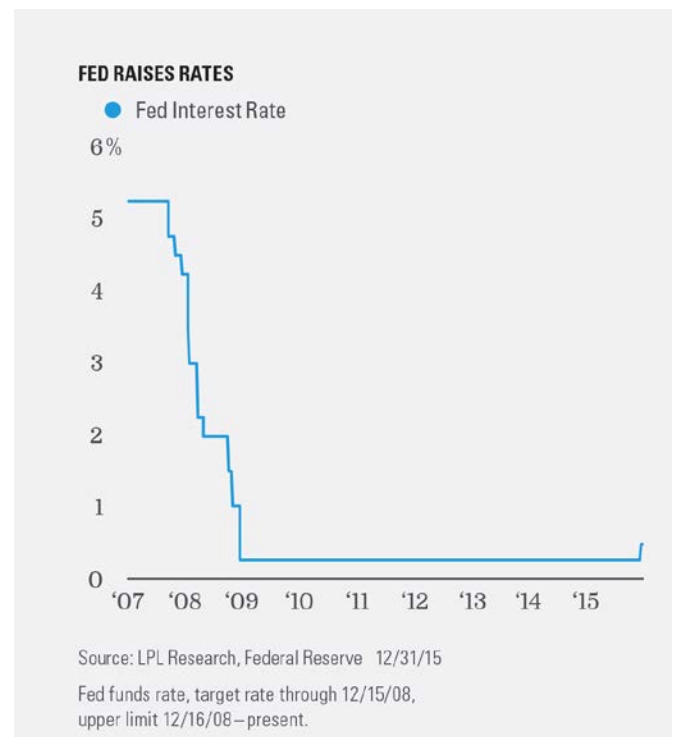
Leading indicators, as aggregated in the Conference Board's Leading Economic Index (LEI), continued to suggest a below-historical chance of recession in the next year. The LEI rose 0.4% in November, handily topping consensus expectations of a 0.1% increase. Building permits and interest spreads made the largest positive contributions, while new manufacturing orders and initial claims for unemployment were the largest detractors. However, Markit's preliminary PMIs for December called for tempered expectations. Manufacturing remained in expansionary territory, with the services sector number even more robust, but both missed consensus expectations and declined from the prior month. By contrast, the Federal Reserve's (Fed) decision to begin raising interest rates at its December meeting was an important vote of confidence in the underlying strength in the economy.

Central Banks

The Federal Open Market Committee (FOMC), the policy arm of the Fed, announced at the conclusion of its December 15 – 16 meeting that it would raise the target range for the federal funds rate from 0 – 0.25% to 0.25 – 0.50%. It had been almost 10 years since the last time the Fed raised rates and exactly 7 years since the Fed had brought the fed funds target range down to 0 – 0.25%. The FOMC policy statement noted that labor markets had exhibited "considerable improvement" and that factors weighing on inflation were likely transitory. Nevertheless, both the statement and Fed Chair Janet Yellen's comments in the post-meeting press conference suggest the Fed will continue to proceed cautiously.

Other major global central banks maintained broadly supportive monetary policies in December, but both the European Central Bank (ECB) and the Bank of Japan (BOJ) disappointed market expectations that they would do more. While the ECB announced it was lowering rates and extending its asset purchases following its December 3 meeting, many market participants expected an increase in the level of its asset purchases. Following its December 17–18 meeting, the BOJ also announced some structural changes in its quantitative easing program,

but, like the ECB, did not expand the size of its program as some market participants expected. Despite disappointing markets, the divergence between international central bank policy and Fed policy became even more pronounced after the Fed became the first major central bank to raise rates.



GLOBAL EQUITIES: DOMESTIC EQUITIES FALL IN DECEMBER; HOLD ON TO SLIM GAINS FOR YEAR

U.S.

U.S. equities, as measured by the S&P 500 Index, fell -1.6% in December to finish the year with a 1.4% gain, inclusive of dividends. Investors hoping for a “Santa Claus rally” were largely disappointed, as markets were thin and many market participants seemed wary of stumbling at year-end with returns so close to flat on the year. With third quarter earnings in the books, the market action was dominated by the lead-up to the Fed’s December meeting and the aftermath of the decision to raise rates for the first time since June 2006. Pressure from the commodities complex and high-yield bond market also created headwinds for performance during the month.

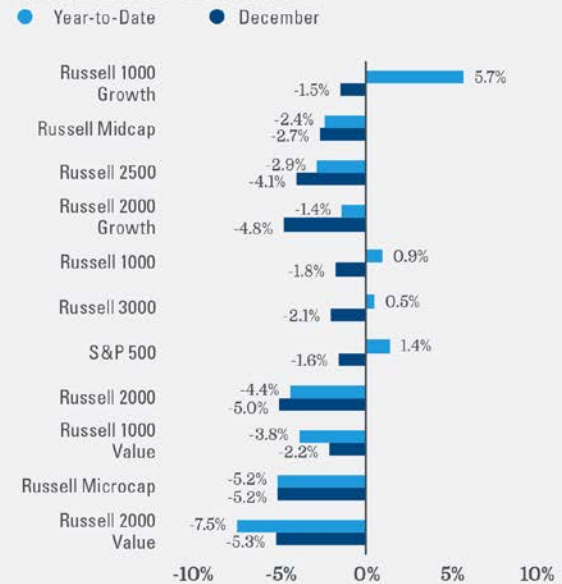
Small cap stocks, which have lagged behind large caps for most of the year, as measured by the Russell 2000 and 1000 indexes, respectively, underperformed significantly during December. Given weak performance year to date, December’s performance could reflect some year-end tax loss harvesting (selling stocks with capital losses to offset capital gains). Investors also expressed a preference for growth over value stocks across issuers of all sizes, as measured by Russell style indexes.

Performance dispersion among sectors, as measured by S&P GICS Sector Indexes, showed a strong divergence as the defensive sectors (consumer staples, utilities, telecom, and healthcare) were the only positive performers for the month. Defensives tend to be the most rate sensitive, so in a month where the Fed raised rates for the first time in nearly 10 years, traders “selling the news” might have been driving relative sector performance in addition to general risk aversion. Cyclical sectors, particularly the much maligned energy and materials sectors, underperformed during the month as investors continue to search for stabilization in the commodities complex and await fourth quarter earnings for signs of the continued health of the economy at large.

GLOBAL INDEX PERFORMANCE



DOMESTIC INDEX PERFORMANCE



Source: LPL Research, FactSet 12/31/15

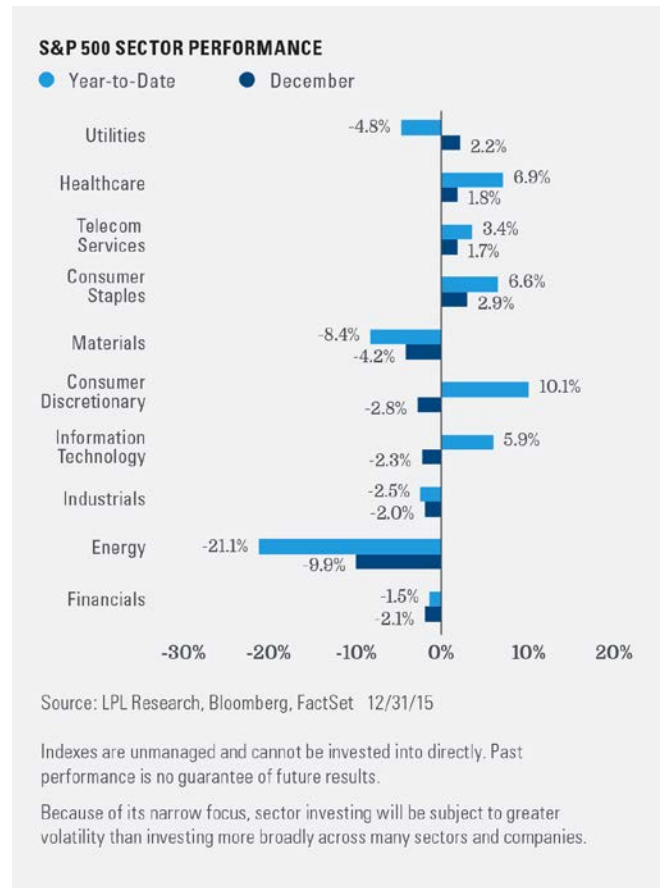
Indexes are unmanaged and cannot be invested into directly. Past performance is no guarantee of future results.

Stock investing involves risk, including loss of principal.

International and emerging markets investing involves special risks, such as currency fluctuation and political instability, and may not be suitable for all investors.

International

International stocks, as represented by the MSCI EAFE Index (foreign developed) and MSCI Emerging Markets Index, both posted losses in December and continued to underperform the S&P 500 on a year-to-date basis. European stocks were impacted by an ECB policy decision early in the month that fell short of market expectations. Further, Japanese equities were flat on the month as authorities were also hesitant to aggressively change their policy for monetary stimulus and announced no significant changes to existing policy. Emerging market declines were broad based, with weak commodity prices continuing to provide a significant headwind and the impact of the Fed move potentially also raising concerns.



FIXED INCOME:

RISK AVERSION LEADS TO DIFFICULT MONTH FOR ECONOMICALLY SENSITIVE SECTORS

Interest rates rose only modestly across the maturity spectrum in December, as fixed income markets had already priced in most of the Fed rate hike that took place on December 16, 2015. Yields on the 10- and 30-year Treasuries increased 0.06% and 0.03%, respectively. Shorter-term yields rose slightly more, with the 2- and 5-year yields increasing 0.12% and 0.11%, respectively, leading to a slight flattening of the yield curve. Rising interest rates were a challenging backdrop for fixed income generally, with the Barclays U.S. Aggregate returning -0.3%.

Relative to modestly rising interest rates, risk aversion was a greater contributor to fixed income performance during the month. Risk aversion to lower-quality fixed income, especially lower-rated high-yield bonds, overwhelmed fundamental factors and led to a -2.2% return for high-yield during December. This sentiment crept into emerging markets debt and bank loans, which returned -1.3% and -1.1%, respectively.

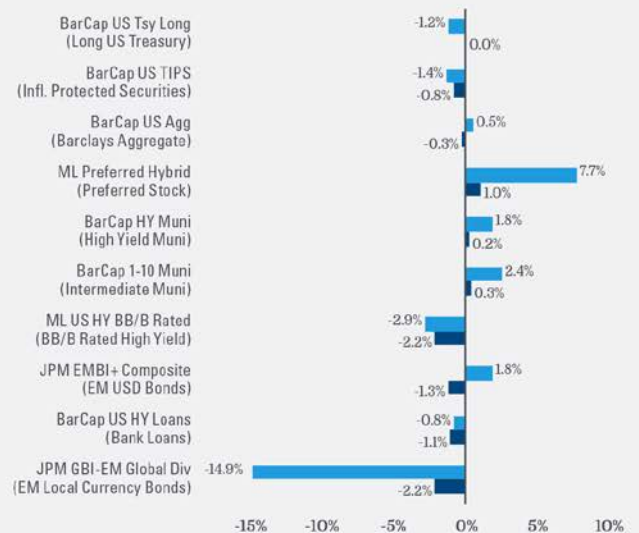
One beneficiary of outflows from high-yield bonds and bank loans was preferred securities, which returned 1.0%. Despite preferreds' elevated interest rate sensitivity (preferreds either have no maturity or are very long term, with maturities of 30 to 50 years) and the backdrop of rising interest rates, the pressure from high demand led to standout performance for the sector.

Spreads on investment-grade corporate bonds increased over the month due to the year-end conservative posturing, contributing to a -0.8% return, underperforming the overall bond market, as represented by the Barclays U.S. Aggregate.

Municipals enjoyed another strong month of performance, again holding up better than Treasuries in the backdrop of rising interest rates. The Barclays Municipal 7 Year (6–8) Index returned 0.5%, while the Barclays Treasury Index returned -0.2%. Unhedged foreign bonds enjoyed noteworthy performance as well, returning 1.5% in December, primarily driven by the 1.5% decline in the U.S. Dollar Index over the month.

FIXED INCOME PERFORMANCE

● Year-to-Date ● December



US TREASURY YIELDS

Security	11/30/15	12/31/15	Change in Yield
3 Month	0.22	0.16	-0.06
2 Year	0.94	1.06	0.12
5 Year	1.65	1.76	0.11
10 Year	2.21	2.27	0.06
30 Year	2.98	3.01	0.03

AAA MUNICIPAL YIELDS

Security	11/30/15	12/31/15	Change in Yield
2 Year	0.70	0.75	0.05
5 Year	1.39	1.41	0.02
10 Year	2.32	2.30	-0.02
20 Year	3.79	3.75	-0.04
30 Year	4.46	4.42	-0.04

Source: LPL Research, Bloomberg, FactSet 12/31/15

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Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values and yields will decline as interest rates rise, and bonds are subject to availability and change in price.

Bank loans are loans issued by below investment-grade companies for short-term funding purposes with higher yield than short-term debt and involve risk.

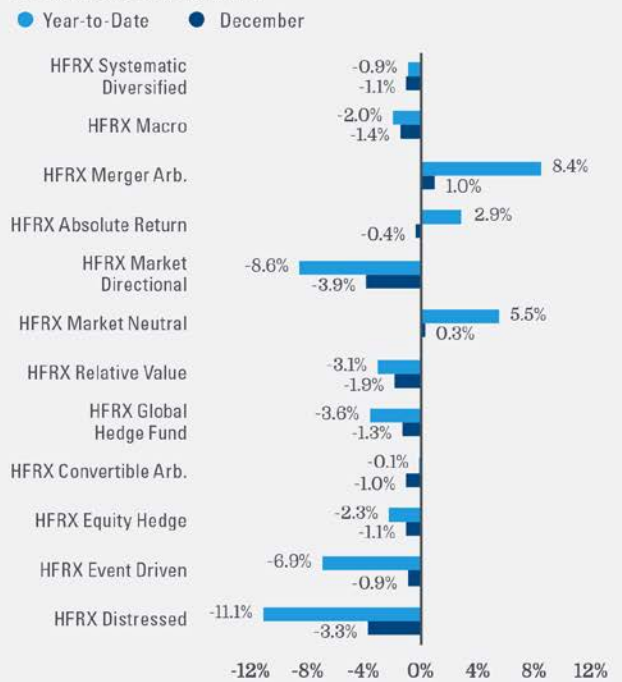
ALTERNATIVES: END YEAR ON SOFT NOTE

Alternative investment strategies finished the year on a weak note, as December, and more broadly, fourth quarter performance was rather lackluster for a majority of the underlying strategies. The fourth quarter contrasts with what had been an extremely promising year for alternative investment strategies through the first nine months. Unfortunately, many of the more net long equity strategies failed to participate in the October rally and subsequently delivered sideways returns during the final two months of the year.

The HFRX Equity Market Neutral category continued to lead gains, with a monthly return of 0.3% and a 5.5% return for the year. Profits from short positions continue to drive performance, specifically in the materials and energy sectors. With a year-end beta of 0.34, long/short equity managers failed to properly protect portfolios on a risk-adjusted basis. The HFRX Equity Hedge fell -1.1% during the month and -2.3% for the year, versus the -1.6% and 1.4% total returns of the S&P 500.

In the macro space, many systematic managers were negatively impacted by their long-duration exposure; however, strategies with more reactive, short-term models were able to protect from the upward move in rates. We continue to believe that a diversified mix of short-, intermediate-, and long-term trend following works best in participating in sustained trends, also providing a degree of protection in the event of a sharp reversal. The struggle for distressed and high-yield related managers continued (HFRX Distressed down -3.3% for December and -11.1% for 2015), as spread widening across the industry persisted. Positions in the energy sector continued to be marked lower. Certain distressed managers have also been impacted by heavy redemption requests, which can often lead to selling at discounted levels to raise the required cash amounts.

HFRX INDEX PERFORMANCE



MORNINGSTAR INDEX PERFORMANCE



Source: LPL Research, FactSet 12/31/15

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Alternative strategies may not be suitable for all investors and should be considered as an investment for the risk capital portion of the investor's portfolio. The strategies employed in the management of alternative investments may accelerate the velocity of potential losses.

NEGATIVE ENDING TO THE YEAR FOR LIQUID REAL ASSETS

Liquid real assets experienced yet another negative month to end a particularly tough year for the asset class. The Bloomberg Commodity Index fell -3.1% in December against the backdrop of a weaker dollar and a modestly higher 10-year Treasury rate. Commodities rounded out 2015 with their ninth negative month of the year. Bearish inventory data were one impetus for WTI crude oil prices falling -11.1% in December.

MLPs & Global Listed Infrastructure

Master limited partnerships (MLP) benefited from a bounce starting in mid-December but ultimately ended the month with a return of -3.6%, as measured by the Alerian MLP Index. The market was shocked early in the month by news of a bellwether in the pipeline space announcing a distribution cut. The cut was viewed positively, as many saw it as an example of a management team cutting a distribution in favor of reducing leverage and increasing cash on hand, as opposed to a cut out of necessity. As the second worst year ever for MLPs has ended, we see one technical headwind — that of tax loss selling and its corollary of retail fund outflows — as having abated, which could provide footing to the group.

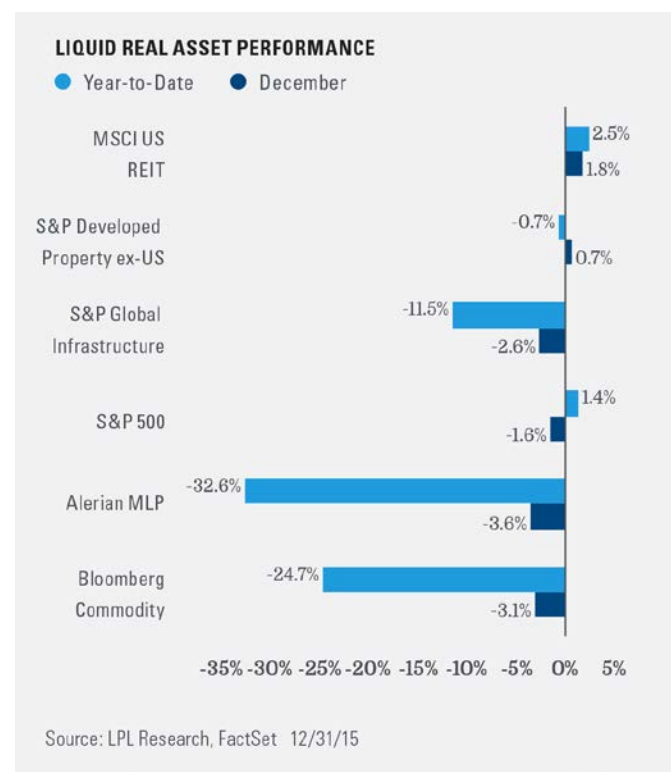
Global listed infrastructure, as measured by the S&P Global Infrastructure Index, returned -2.6% for the month. The energy component of the index dragged down performance as oil was sharply lower for the month.

REITs

The Fed raised the fed funds rate and actual rates ticked up for most parts of the yield curve but real estate investment trusts (REIT) were unfazed. The MSCI U.S. REIT Index returned 1.8% for the month, outperforming the S&P 500 by 3.4%. Significantly outperforming were healthcare REITs, and significantly underperforming were hotel and diversified REITs. It remains to be seen how the market will react as the Fed continues its rate hiking campaign.

Commodities

Commodities were lower again in December as the Bloomberg Commodity Index returned -3.1%. As was the case last month, oil dragged on the index's returns, with WTI crude prices falling -11.1% and Brent falling -16.4%. The lifting of the U.S. oil export ban did little to help prices, but did contribute to the price of WTI crude briefly surpassing that of Brent. A bright spot for energy was natural gas, which saw a price increase of 4.6%. Copper managed a positive return for the month, while gold and silver both fell. Agricultural commodities broadly, as measured by the Bloomberg Agriculture Subindex, returned -1.0%, as grains continued their slide. This all came against the backdrop of a weaker dollar as the U.S. Dollar Index returned -1.5% in December.



Commodity-linked investments may be more volatile and less liquid than the underlying instruments or measures, and their value may be affected by the performance of the overall commodities baskets as well as weather, geopolitical events, and regulatory developments.

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