

4Q 2015

Market Overview

THE SEARCH FOR A MAXIMUM REGRET PORTFOLIO

Global economic growth has remained frustratingly lethargic after six years of unprecedented monetary stimulus by many of the world's central banks, while concern over slowing growth in China began to dominate markets as 2015 concluded (and became the catalyst for additional equity market downside as 2016 began). Persistent multi-year weakness in global commodity prices has been only one symptom of both this larger global growth malaise and the more recent slowdown in China's growth, given its previously voracious commodity demand. Crude oil prices in fact broke down again late in 2015, ending the year in the mid \$30s/barrel and lower than lows reached in August. The broader Bloomberg Commodity Index fell about 25% for the year.







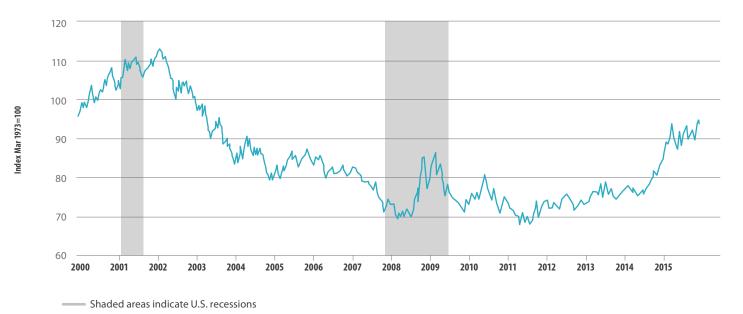
Market Summary

- In the U.S., short-term yields rose by 30 to 40 basis points with the Fed's December move to raise the Fed Funds rate target to a range of 0.25% to 0.50%.
- The Treasury curve is impacted at the short end by the Fed's plan to raise rates in 2016. Conversely, longer-term yields are restrained by disappointingly sluggish U.S. growth and low inflation.
- Global developed equity markets generally rebounded in Q4. Gains were built on the strong performance of a number of large-cap names; small-caps lagged.
- Growth once again outperformed value, mirroring the larger pattern for the year.
- Japan and Germany were the strongest major developed nation markets.
- Energy-intensive economies such as Norway and Canada lagged due to oil's continued weakness.
- EMs continue to suffer from commodity price weakness on export-dependent economies and declining currencies.

The U.S. continued to produce one of the developed world's strongest economic performances in 2015, although growth in gross domestic product remains frustratingly tepid by long-term historical standards. In the U.S., real GDP growth climbed from a weak 0.6% in Q1 to 3.9% in Q2, but fell back to 2.0% in Q3. With Q4 estimates grinding down under 2.0% as the year closed, full-year GDP is unlikely to be much higher than 2% to 2.5%. Eurozone growth has been even more sluggish, with real GDP growth of only 1.5% for the region as a whole in 2015. Japan emerged from recession during 2015 (although only after an initial government estimate of a 0.8% Q3 decline was revised up to a 1% gain in early December) but growth languishes with year-to-year gains at just over 1%. Along with the U.S., the United Kingdom remains one of the stronger global economies, but growth through Q3 2015 is barely above 2%.

The relative strength in U.S. economic growth along with its relatively higher yields (which only seem high compared to near-zero yields in Europe and Japan) has been a catalyst for another notable economic theme — the ongoing and broad strength in the U.S. dollar. On a trade-weighted basis against a broad basket of currencies, the U.S. dollar has climbed nearly 30% since mid-year 2011 and about 20% since mid-year 2014. A flip side of dollar strength is euro weakness; this has certainly benefitted European and other global exporters but has dampened U.S. corporate profits, as about 40% of S&P 500 revenues are generated outside the U.S. The relatively sluggish profit growth by U.S. corporations has played a key role in dampening equity returns. Revenue and earnings growth has generally been flat in 2015, driven especially by weak energy sector earnings. According to Zack's, total earnings for the S&P 500 index are expected to be down -7.3% in Q4 year on -4.6% lower revenues, the third straight quarter of earnings declines for the index.

TRADE WEIGHTED U.S. DOLLAR INDEX: MAJOR CURRENCIES



Source: Board of Governors of the Federal Reserve System (U.S.) via The Federal Reserve Bank of St. Louis as of December 11, 2015; myf.red/g/2WPA

even as the country skirted rec Europe, prospects of stronger along with continued, albeit m

reasonably upbeat about 2016, with consensus forecasts calling for 2.5% real U.S. GDP growth for this year and next. Corporate earnings outlooks were more upbeat, with FactSet's collection of analyst's estimates calling for +7% earnings growth in 2016 and above +10% in 2017, as the sharp negative hit from last year's very weak energy comparisons recedes and economic growth improves. The main threats to the U.S. earnings outlooks continues to be continued strengthening in the U.S. dollar, weaker than expected global growth (which only compounds the dollar's pressure on foreign earnings) and the possibility of disappointing domestic economic growth in the year ahead. The consensus growth outlook is positive, but more muted, for Europe, with the real GDP growth for the Eurozone block of nations expected to range around 1.5% for 2016. Japan's growth outlook is pegged at an even slower 1% for 2016 and 2017.

As 2015 came to a close, economists and analysts remained

ECONOMIC OVERVIEW

Global developed equity markets generally rebounded in Q4 after a weak Q3. In the United States, the S&P 500 returned 7.04%, slightly outperforming the broader Russell 1000 Index's 6.5% return. However market gains were built mostly on the strong performance of a number of large-cap names, particularly for the year as whole. Small-caps lagged with the Russell 2000 returning 3.6% for the quarter. And growth once again outperformed value, with the Russell 1000 Growth Index returning 7.3% for the quarter versus the Russell 1000 Value's 5.6%. The pattern of returns for the quarter mirrored the larger pattern for the year. The S&P 500 returned 1.38% for 2015, while the growth sector outperformed the value sector 5.67% versus -3.83%, as measured by the Russell Indices.

Outside of the U.S., the developed markets, measured by MSCI EAFE Index, returned 6.4% for the quarter in local currency returns. For the year, equity performance for developed markets was 5.76% in local currency returns. Continued strengthening of the U.S. dollar eroded these returns by a few percentage points for U.S. dollar-based investors, in both the quarter and year. Japan and Germany were the strongest developed nation markets. Japanese stocks gained about 10% even as the country skirted recession later in the year. In Europe, prospects of stronger exports due to a weakening euro along with continued, albeit modest, improving economic sentiment lifted European markets. MSCI Europe was up +5.6% in euros in Q4, led by the 10.7% return in Germany.

The emerging markets continued to lag the developed markets for the quarter and year. The MSCI Emerging Markets Index returned 1.56% and -5.38% in local currency returns for the quarter and year, respectively. As with the developed markets, U.S. dollar strength versus foreign currencies eroded returns fairly significantly for U.S. based investors. Brazil (-3.2% for the quarter and -41% for the year) was by far the weakest emerging market, as the country was beset by recession and political scandal. However, many emerging markets were exposed to the negative impact on their export-driven economies of weak commodity prices. While China's domestic market rout and awkward political response (including the arrest of financial industry executives, evidently because stocks went down) was the subject of considerable financial media attention, the MSCI China Index (a separate market open to global investors) was off only -7.6% in U.S. dollar terms for the year, on par with India's -6.1% decline. Russia returned -4% for Q4 and +5.0% in U.S. dollar terms for the full year.

Activity in the fixed income markets was dominated by two major themes: The US Federal Reserve's interest rate hike, and the credit weakness in the metals, mining and oil and gas sectors. In the U.S., short-term yields rose by 30 to 40 basis points with the Fed's December move to raise the Fed Funds rate target to a range of 0.25% to 0.50%. The yield curve flattened as long term yields increased by about 15 basis points during the quarter. The increase in yields produced a -0.57% return for the Barclays Capital Aggregate Index, though the Index had a positive 0.55% return for the year as coupon income offset price declines. The Mortgage and Asset Backed sectors were the best performing sectors. The High Yield corporate sector, reflecting the weakness in the energy, mining, and oil and gas sectors, was the worst performing sector, returning -2.07% and -4.45%, for the quarter and year, respectively.

In Europe, the German bund curve rose slightly at lower maturities but yields remained below zero out to the five year point. Indeed, European government yields in general remained deeply depressed during both Q4 and 2015. At year end, the region showed generally negative government yields to the five-year maturity, rising above 1% only beyond the 15-year maturity.

CAPITAL MARKETS REVIEW

Equities			
CAPITALIZATION AND STYLE			
INDEX	3 Mo.	12 Mo.	
S&P 500	7.04	1.38	
Russelll 1000 Value	5.64	-3.81	
Russelll 1000 Growth	7.32	5.64	
Russelll 2000 Value	2.88	-7.44	
Russelll 2000 Growth	4.32	-1.38	
MSCI EAFE (USD/Local Currency)	4.75/6.38	-0.39/5.76	
MSCI Emerging Markets (USD/Local Currency	0.73/1.56	-14.55/-5.38	

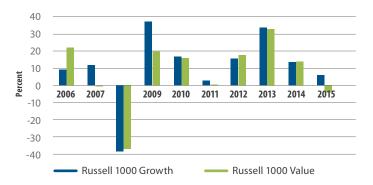
Fixed Income			
U.S. SECTOR RETURNS – ABSOLUTE			
SECTOR	3 Mo.	12 Mo	
Barclays US Aggregate	-0.57	0.55	
Treasury Index	-0.94	0.84	
MBS Index	-0.10	1.50	
ABS Index	-0.57	1.24	
CMBS Index	-1.32	0.94	
Inv. Grade Corporate Index	-0.58	-0.68	
High Yield Index	-2.07	-4.45	

THE VALUE/GROWTH DIVERGENCE

As we noted last quarter, one of the prominent equity market trends over the past few years is the dominance of growth-style returns over those of value. CBIS' quantitative sub-advisers have noted the strong performance of their growth-related factors, such as strong trailing and forecast earnings growth and price momentum. Investors' search for earnings in a low global growth environment may be the equity market equivalent of investors' stretch for yield in a low global interest rate environment. The Russell 1000 Growth Index gained +5.7% in 2015 versus the Russell 1000 Value Index's -3.8% decline. Growth's outperformance even persists, although to a much lesser degree, in the trailing five-year period (at +13.5% versus +11.3%). Much of the performance divergence relates to the industry/ company compositions of the style indices. The very weak energy sector (down -21% in the S&P 500 in 2015) is considerably overweighted in the Value index while the strong consumer discretionary sector (up about +10% in the S&P 500) is far more dominant in the Growth index. Strong information technology company gains also accrue disproportionately to the growth index.

It's an old saying in the investment business that the stock market is "a market of stocks", meaning that broad topdown themes are sometimes simply the summation of many individual and separate underlying stories. These individual company stories are another way to frame the divergence between growth and value. The Russell 1000 Growth Index contains some heavyweights that posted very strong results in 2015, such as Amazon (+117%), Alphabet (formerly Google and up +44%), Facebook (+34%), Home Depot (+28%), Starbucks (+48%) and Netflix (+134%). All are absent from the Russell 1000 Value Index, and the Russell 1000 Growth has no exposure to some of the weakest names in the energy sector.

RUSSELL GROWTH VS. VALUE



AVERAGE ANNUAL TOTAL RETURNS

RUSSELL 1000 GROWTH	RUSSELL 1000 VALUE
5.67%	-3.83%
16.83%	13.08%
13.53%	11.27%
17.11%	13.04%
8.53%	6.16%
	5.67% 16.83% 13.53% 17.11%

CENTRAL BANK DIVERGENCE

With the U.S. Federal Reserve now intending to implement additional short-term rate boosts in 2016 (with the oft-stated qualification that policy will be data dependent) the Fed has definitively entered a tightening policy stance, at least in relation to the European Central Bank (ECB) and the Bank of Japan (BOJ). Both of these major developed market central banks continue to aggressively support markets with quantitative easing programs and resultant balance sheet expansions. Central bank easy money has lifted markets in recent years, but the tension between lack of tangible earnings growth and central bank support eventually has to be reconciled - and it will be in favor of hard evidence of earnings since earnings drive long-term stock returns. This policy divergence by the world's leading central banks is the first significant one since the 2008/2009 financial crisis. Whether this divergence will have a meaningful impact on markets is unclear, but it's likely to be a catalyst for considerable volatility in the markets.

THE MAXIMUM REGRET PORTFOLIO

In our Q2 quarterly letter we urged participants to brace for a return of volatility, although we did not expect the onset to be so immediate. In the Q3 letter we encouraged participants to embrace volatility, knowing full well how difficult this is to do. Downside volatility allows our sub-advisers to commit new capital at better entry prices for stronger long-term returns. For the investor seeking long-term capital gains, volatility can be a gift not a curse. In the near term, however, embracing volatility comes with self-doubt and regret. At any given moment in time, a fully and intelligently diversified portfolio will contain exposures to asset classes and styles that are underperforming, possibly declining and maybe even declining sharply. Many investors will chastise themselves for these exposures, "If only I'd not been in that!" These emotional impulses are entirely human, but they are an investor's worst enemy. Given the unpredictable nature of markets and the inevitable volatility that buffets all portfolio exposures, successful investing comes with a constant dose of regret. The successful investor checks this regret and reminds himself or herself that hindsight is 20/20 while foresight is shrouded in fog and uncertainty. This is ever and always true, and it is the reason why a well-planned investment policy, thoughtful diversification and a disciplined rebalancing policy, is the best way to manage the regrets that arise in the minds of all investors. Growth's dominance today will give way to value's dominance at some point but we don't know when. The momentum factor's outperformance will reverse, probably sharply, but it is difficult to predict this in advance. Successful energy company stocks will ultimately rebound and achieve strong gains, but the timing is difficult to predict. Emerging markets, which contain the majority of the globe's growing youthful populations seeking a better, happier and more prosperous life, will ultimately rebound reflecting the strong demographic tailwind. All market trends come to an end and new ones begin. These turning points are difficult to predict in advance but, to the extent that financial market history is any guide, we can know with virtual certainty that they will occur.

A thoughtful and effective diversified portfolio is always a portfolio that contains exposure to regret. If one did not have some short term regret, we would argue the portfolio is not adequately diversified. But for the true long-term investor, the sub-optimal portfolio strategy is the one where investors caved in to this regret by impetuously selling losers and jumping on the presumed bandwagon of the winners of the moment. Such a portfolio is almost guaranteed to be constructed with a "buy high/sell low" strategy. This portfolio will be emotionally satisfying in the very short term, but over the long term it will produce a punishing degree of underperformance. The longterm can seem so far away at times, but it always arrives. It's better to think carefully about that now and maximize your odds of success by constructing a portfolio of maximum regret.

Important Information

This is for informational purposes only and does not constitute an offer to sell any investment. The funds are not available for sale in all jurisdictions. Where available for sale, an offer will only be made through the prospectus for the funds, and the funds may only be sold in compliance with all applicable country and local laws and regulations.