Strategy Newsletter
1st Quarter 2016

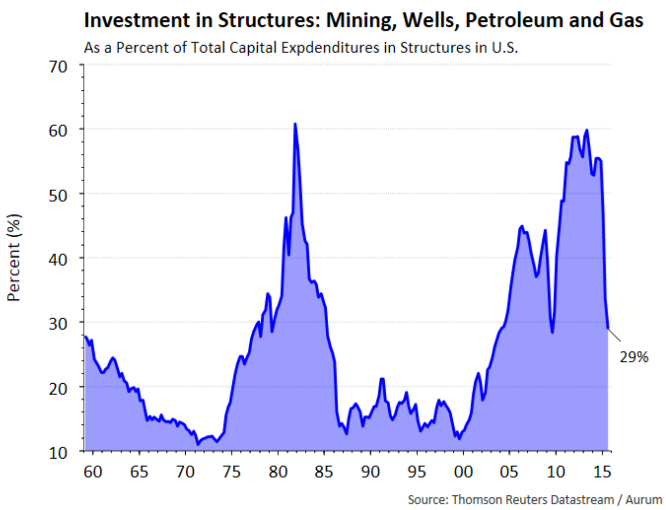
- Outside of the energy sector, the economy seems to be on solid footing for now.
- Equity markets look weaker below the surface.
- Spreads rise even for investment grade companies and yield curve moves up.
- Household net worth to GDP still near highs.

Economy

U.S. households received pay raises during the last quarter as average hourly earnings climbed to an 8-year high of 2.5%. In turn, spending remains strong for consumers, which makes up 70% of the U.S. Gross Domestic Product (GDP).

Contributing to consumers pockets is also the fall in oil prices. Rather than spend the new found dollars, the personal savings rate moved higher to 5.5% from 4.6% a year earlier.

Unfortunately, the decline in oil prices is having an adverse impact on the energy sector. Indeed, over the last decade, private investment in nonresidential structures reached a high of 60%, the same as the early 1980s.



Today it stands at 29% and could be in the doldrums as a percentage of capital expenditures for years if oil prices stay lower for longer. This seems likely given the lack of production cuts across the globe.

Oil producing nations from Brazil to Russia, to Saudi Arabia are all feeling the pinch of lower oil prices.
It is effectively a tax cut for importing nations like India and the European bloc.

News out of China continues to weigh on the global economy but we see little effect on U.S. growth for now. We shall see how the economy digests the first Fed rate hike in nearly 10 years.

Equity

Of all nine U.S. style boxes, (value, core, growth for each of large, mid, and small caps), only large core and large growth ended positive in 2015.

US Equity	4Q 2015	2015
Large Cap Stock		
Dow Jones Industrial Average	7.70%	0.21%
S&P 500	7.04%	1.38%
Small & Mid Cap Stock		
Russell Mid Cap	3.62%	-2.44%
Russell 2000	3.59%	-4.41%
Style Indices		
Russell 3000 Value	5.41%	-4.13%
Russell 3000 Growth	7.09%	5.09%
International Equity	**4Q 2015**	**2015**
MSCI EAFE	4.75%	-0.39%
MSCI EAFE Value	2.72%	-5.22%
MSCI EAFE Growth	6.70%	4.47%
MSCI Europe	2.53%	-2.34%
MSCI Japan	9.38%	9.90%
MSCI Emerging Markets	0.73%	-14.60%

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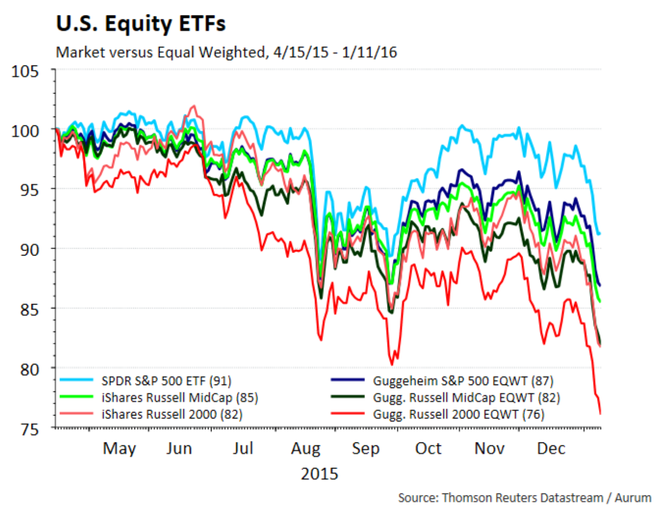
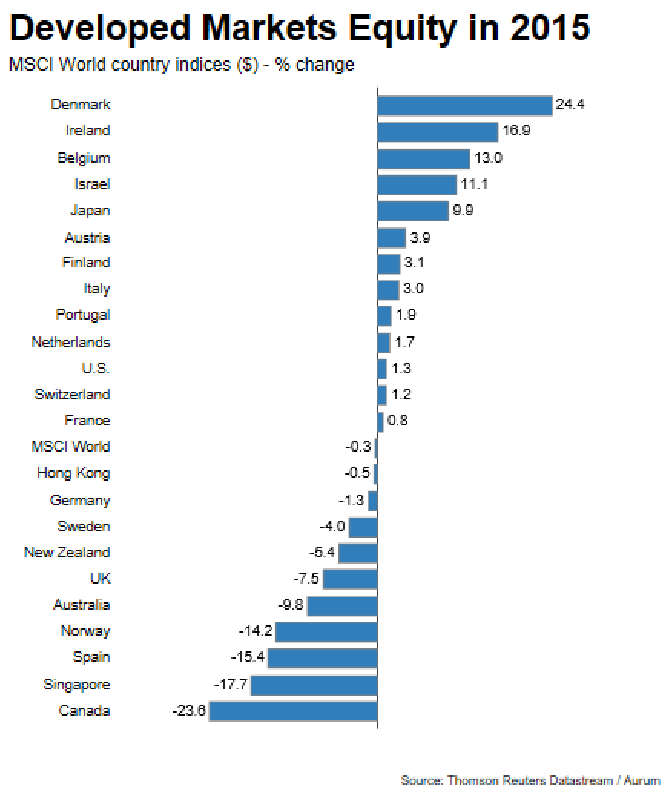
Upon first glance, it seems that large cap equity indices had an decent year. This masks the underlying performance of invidiual equities, however as it was a group of four stocks, affectionately known as “FANG” (Facebook, Amazon, Netflix, and Google – each of which had stand out performance in 2015) that actually contributed to the positive performance.

The graph below shows the market capitilzation weighted Exchange Traded Funds (ETFs) for large, mid, and small companies on the left side of the legend. On the right side are ETFs where companies are not weighted based on size, but are equally weighted. This is so that large companies do not drive the performance (such as the FANG stocks being up an average of 100% each, trouncing)

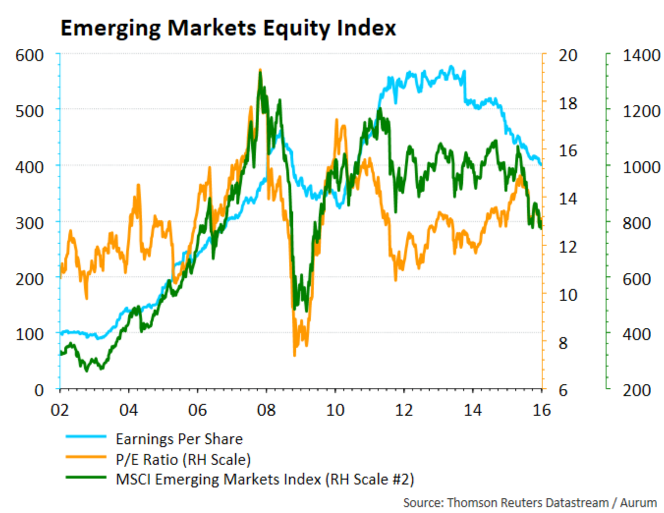


We find that since the broad equity market peaked on April 15, 2015, an equal weighted basket of the S&P 500 fell 13%, mid caps fell 18%, and small caps fell 24%. Suffice to say, mid and small cap stocks are in a downtrend and arguably a bear market. This despite the fact that few are calling it a bear market given the low single digit losses for the indices for the calendar year of 2015. The market cap weighted indices are still down 9%, 15%, and 18% for large, mid, and small respectively. Given the falling earnings and aleady above average multiples, we will need to see growth outpace expectations to turn the tides around

A few small developed countries posted outsized returns while Japan led the larger markets at nearly a 10% gain. Resource dependent countries like Australia and Canada found themselves towards the bottom.



Emerging markets underperformed again driven by Latin American and Eastern European countries. Whlie the P/E multiple was attractive the last few years, the earnings drop of over 30% shows no signs of slowing (driven by resource-rich nations).



Our portfolios have a bias to emerging markets due to the relative value, attractive sentiment, and potential for reversion to the mean performance against developed nations. Our portfolios have a small underweight to developed international equities as managers raised cash as a result of the lack of bottom up opportunities available. Portfolios remain approximately equal weight equities against the strategic Aurum Asset Allocaiton Frameworks.

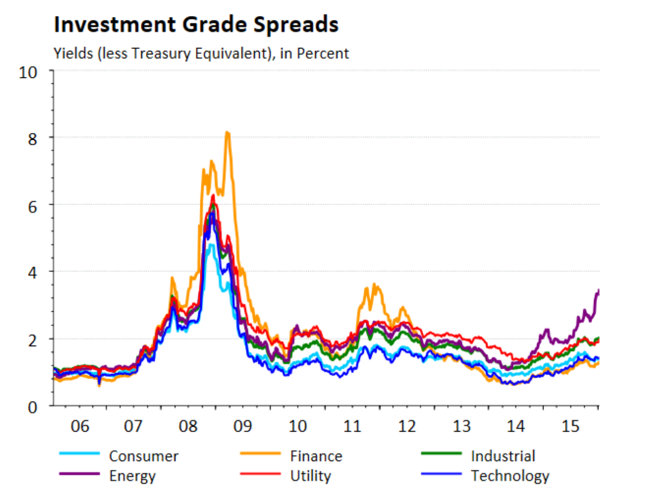
Fixed Income

Quality bonds rallied on the back of lower interest rates during the quarter and served as a safe-haven to the sell-off in global equities. Low quality credit related assets traded down.

Fixed Income	4Q 2015	2015
Barclays U.S. Aggregate Bond	-0.57%	0.55%
Barclays Corporate Inv. Grade	-0.58%	-0.68%
Barclays High Yield Bond	-2.07%	-4.47%
Barclays Global ex. U.S. Tres.	-1.08%	-4.84%
Barclays Municipal Bond	1.50%	3.30%

Grabbing headlines during the quarter was the failure of the Avenue Credit Strategies fund, which invested in high yield and distressed bonds of U.S. companies.

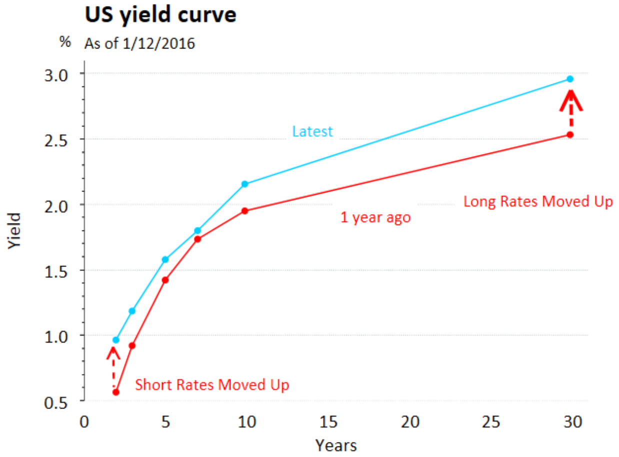
Junk, or high yield, rated companies are not the only ones seeing borrowing costs increase. The spreads on investment grade (BBB to AAA-rated) companies increased across all sectors, with energy the obvious outlier.



Source: Thomson Reuters Datastream / Aurum

Some of our managers see a tactical opportunity for corporate credit given the lower prices, however, we are not keen on committing new capital at this phase of the economic cycle. While we are not calling an end, even adding at today's level is difficult when we perceive lower risk from residential mortgage-backed securities and asset-backed securities. With similar yields and a higher likelihood to see a return of and on our capital, we have not made any changes.

The big news this quarter was the Federal Reserve finally raising the fed funds rate. This led to the front end (1 to 3-year portion) rising. The back-end (10 and 30-year bonds) actually fell during the quarter, but rose over the past year.



Source: Thomson Reuters Datastream / Aurum

It will be very interesting to monitor the Federal Reserve during 2016 as participants are split on whether we will see one more hike or a series of interest rate moves throughout the year. Inflation measures are showing some signs of life, and will likely be the key, along with overall financial stability on the pace of rate hikes. If inflation fails to materialize, there could be an opportunity to consider Treasury bonds over the next few quarters.

The Aurum Asset Allocation Frameworks continue to hold an equal weight to fixed income with a bias to structured credit.

Alternative Investments

REITs led the way for a second straight quarter while hedge funds and TIPS posted mixed results.

Alternative Assets	4Q 2015	2015
HFRI Hedge Fund of Funds	0.63%	-0.36%
Dow Global Select REIT	7.54%	2.65%
Barclays TIPS	-0.64%	-1.44%

Long/short equity managers struggled as the slightly long bias combined with a bear market for mid and small cap stocks which led to mixed results.

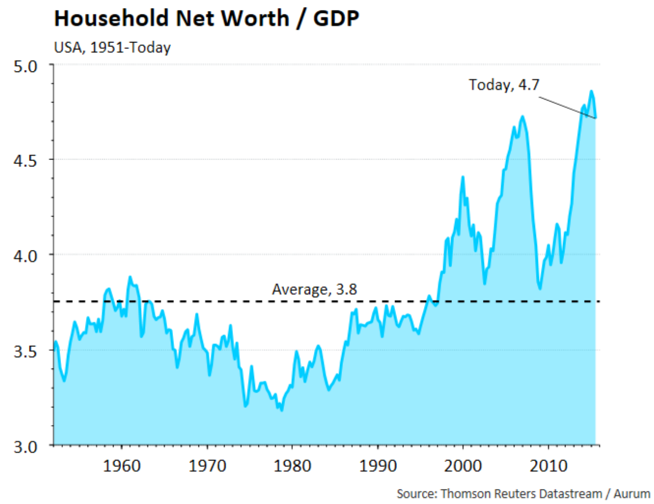
At the end of the quarter, we added to a managed futures fund along with a relative value manager. We see opportunity in strategies with low correlation to broad markets.

Diversified alternative strategies maintain the bulk of our alternative allocation with multiple hedge fund strategies actively managing risk and seeking asymmetric opportunities.

Conclusion

Generally we avoid repeat charts, yet this is so important we will show it once again (updated now, originally shown in the 3Q15 Strategy Newsletter).

It is a ratio of Household Net Worth (Assets minus Debt) divided by Gross Domestic Product.



It reached its highest levels ever in 2015, and still stands at 4.7. With stocks, bonds, and real estate each near all-time high prices, America's net worth relative to its production is near the highs. If it were to get back to the *20-year average*, net worth would need to drop 11%. If it were to fall to the *long-term 63-year average*, net worth would drop 21%. We mention this to manage expectations as loose monetary policy suppressing yields and awakening investing spirits, has made forward looking returns look lean. We do see pockets of opportunity and will be wary of risk as we enter 2016.

Aurum Asset Allocation Frameworks

	Income		Conservative		Moderate		Growth		Aggressive	
	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical	Strategic	Tactical
Equity	0%	0%	20%	20%	35%	35%	50%	50%	70%	72%
U.S. Equity	0%	0%	12%	8%	20%	14%	30%	22%	42%	35%
Int'l - Develop. Markets	0%	0%	6%	6%	12%	12%	16%	16%	21%	21%
Int'l - Emerg. Markets	0%	0%	2%	6%	3%	9%	4%	12%	7%	16%
Fixed Income	65%	60%	45%	42%	30%	30%	17%	18%	10%	10%
U.S. Fixed Income	56%	57%	39%	39%	26%	27%	15%	15%	7%	8%
Global Fixed Income	9%	1%	6%	1%	4%	1%	2%	1%	3%	1%
Alternative Invest.	25%	28%	28%	28%	30%	28%	30%	28%	19%	18%
Diversified Strategies	19%	28%	22%	28%	24%	28%	24%	28%	15%	18%
Real Estate & REITs	2%	0%	2%	0%	3%	0%	3%	0%	4%	0%
Inflation-Indexed Sec.	4%	0%	4%	0%	3%	0%	3%	0%	0%	0%
Cash/Equivalents	10%	12%	7%	10%	5%	7%	3%	4%	1%	1%
U.S. Dollar	10%	12%	7%	10%	5%	7%	3%	4%	1%	1%

The risk designations are relative only to the five Strategic Allocation targets and do not represent comparisons with any other investment or risk of the overall strategies.

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