CAPITAL MARKETS REVIEW
1st Quarter 2014

OVERVIEW

March 31, 2014

During the first quarter, capital markets delivered generally positive returns after an initial period of volatility in January. U.S. and developed non-U.S. equity markets moved higher and outpaced the negative returns of emerging market equities. After a difficult 2013, fixed income markets posted relatively strong returns, due in part to reduced anticipated growth stemming from worse than expected U.S. economic data. Finally, real assets responded positively to an uptick in short-term inflation expectations.

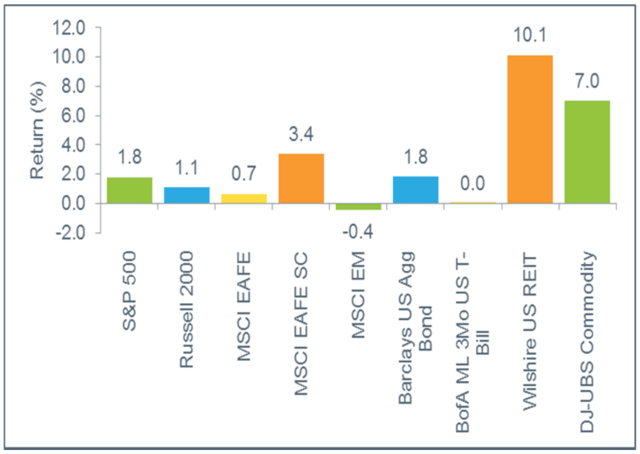
At quarter end, the IMF revised its global GDP growth estimate downward to 3.6% from an earlier estimate of 3.7%. Overall, investment managers and economists provided mixed long-term outlooks. Investors began the year fixated on the economic impact of severe weather conditions in the U.S. and escalation of the conflict in the Ukraine. While harsh winter weather likely played a role in relatively weak U.S. economic data, the effect of the disturbance on asset prices was subject to ongoing debate. The Russian annexation of Crimea contributed to sharp declines in Russian equity and currency markets. Outside of nearby emerging markets, global markets largely withstood the geopolitical turmoil. In the Asia-Pacific region, China's economic growth outlook slowed, while the results of Prime Minister Shinzo Abe's structural reforms in Japan appeared increasingly uncertain.

In the U.S., the Fed released the results of its bank stress tests, which indicated continued quality improvement in the U.S. banking industry. Private employment added 192,000 jobs in March with the retail, construction and healthcare sectors all contributing positively. The labor participation rate rose to 58.9%, a four-year high. U.S. GDP growth was revised upward for the last quarter of 2013 from 2.4% to 2.6%. In her first press conference as Fed chair, Janet Yellen focused on the persistently below target rate of inflation, distancing the Fed from its previously suggested unemployment rate threshold target of 6.5% as the actual rate held steady at 6.7%. The move gave Yellen more flexibility surrounding the asset purchase program. Additionally, Yellen indicated that the Fed would initiate rate increases, if consistent with economic data, approximately six months after the end of quantitative easing. This initial stance was more hawkish than markets assumed.

TRAILING PERIOD MARKET PERFORMANCE (%)

	QTD	CYTD	1 Year	5 Years	10 Years
S&P 500 (Cap Wtd)	1.8	1.8	21.9	21.2	7.4
Russell 2000 (Cap Wtd)	1.1	1.1	24.9	24.3	8.5
MSCI EAFE (Net)	0.7	0.7	17.6	16.0	6.5
MSCI EAFE SC (Net)	3.4	3.4	23.3	21.7	8.6
MSCI EM (Net)	-0.4	-0.4	-1.4	14.5	10.1
Barclays US Agg Bond	1.8	1.8	-0.1	4.8	4.5
BofA ML 3Mo US T-Bill	0.0	0.0	0.1	0.1	1.7
Wilshire US REIT	10.1	10.1	4.4	29.2	8.2
DJ-UBS Commodity (TR)	7.0	7.0	-2.1	4.2	0.4

QUARTER-TO-DATE PERFORMANCE (%)



KEY ECONOMIC INDICATORS

		As of	12/31/2013	9/30/2013	10 Year Average
Federal Funds Rate	0.06%	3/31/2014	0.07%	0.06%	2.08%
Treasury - 1 Year	0.11%	3/31/2014	0.11%	0.09%	0.63%
Treasury - 10 Year	2.72%	3/31/2014	3.03%	2.61%	4.05%
Treasury - 30 Year	3.56%	3/31/2014	3.97%	3.68%	4.69%
Breakeven Inflation - 1 Year	1.79%	3/31/2014	1.50%	0.41%	1.09%
Breakeven Inflation - 10 Year	2.14%	3/31/2014	2.23%	2.19%	2.11%
Breakeven Inflation - 30 Year	2.28%	3/31/2014	2.36%	2.35%	2.45%
Barclays US Corp: Hi Yld Index - OAS	3.58%	3/31/2014	3.82%	4.61%	6.00%
Capacity Utilization	78.40%	2/28/2014	78.40%	78.30%	76.50%
Unemployment Rate	6.70%	3/31/2014	6.70%	7.20%	6.40%
ISM PMI - Manufacturing	53.70%	3/31/2014	56.50%	56.00%	52.10%
Baltic Dry Index - Shipping	1,362	3/31/2014	2,277	2,003	3,487
Consumer Confidence (Conf. Board)	82.30	3/31/2014	77.50	80.20	81.93
CPI YoY (Headline)	1.10%	2/28/2014	1.50%	1.20%	2.40%
CPI YoY (Core)	1.60%	2/28/2014	1.70%	1.70%	1.90%
US Dollar Total Weighted Index	76.97	3/28/2014	76.44	75.37	84.31
WTI Crude Oil per Barrel	$102	3/31/2014	$98	$102	$60
Gold Spot per Ounce	$1,284	3/31/2014	$1,206	$1,329	$687

ASSET CLASS COMMENTARY

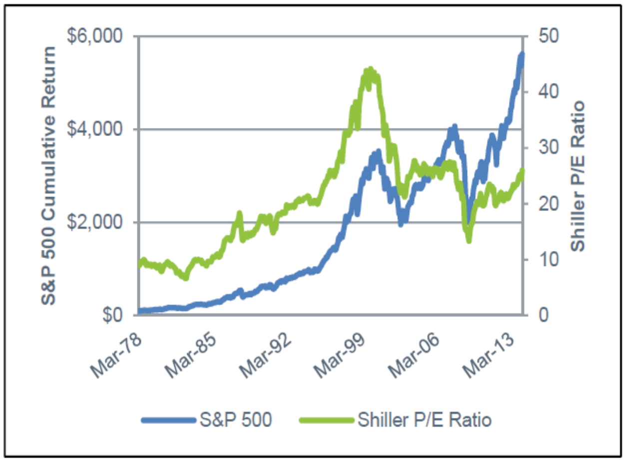
U.S. Equity

U.S. stock returns faltered at the start of the quarter following a robust year in 2013, but finished in positive territory. Mid-cap stocks posted the most attractive returns, followed by large- and small-cap respectively. Growth stocks outperformed Value stocks in January and February. Market preferences shifted in March with Value stocks ending the quarter ahead due to rising appreciation. High-dividend paying stocks outperformed as interest rates fell from the highs achieved in 2013. This market theme hurt active managers who generally expressed a bias toward stocks with high-dividend growth potential rather than those with high current payouts in preparation for rising rates. A weak performing Consumer Discretionary sector was also detrimental to active managers, as this space had been an area of emphasis for the past few quarters. Overall, less than a third of active managers outperformed their preferred benchmarks. Portfolios with above average concentrations of high-dividend and Healthcare stocks fared better than most.

Switching focus to longer-term performance, **Figure 1** illustrates the current market rally relative to a cyclically-adjusted valuation indicator. The S&P 500 has appreciated far above its 2007 level; yet, despite moving upward the Shiller Price-to-Earnings ratio has not yet breached the levels associated with the past two market peaks.

Due to the longevity of the equity bull market and relatively high cyclically-adjusted valuations, many managers are positioning their portfolios for a flatter forward-looking return trajectory, and are also looking to multinationals to hedge against potential valuation contraction in the U.S.

Figure 1: Market Appreciation and Valuation



Non-U.S. Equity

Non-U.S. developed markets continued to lag the U.S. markets; however, returns of major indices were still positive across the board. The Asia-Pacific region was the worst performing sector, dragged down by Japanese equities and a reversal of the short Yen trade. Developed non-U.S. large- and mid-cap stocks underperformed

ASSET CLASS COMMENTARY

small-cap stocks. Returns were bolstered by improving valuations in Europe, as well as near-zero inflation rates and improving growth rates in the Eurozone.

Disappointing performance persisted in the emerging markets which started the year with another negative quarter. A selloff occurred in January due to slowing growth and economic concerns. The main drivers were a surprise contraction in China's manufacturing activity along with eased controls on dollar purchases in Argentina following a devaluation of the currency. The volatility eased in February with bargain hunters stepping in to prevent emerging economies from depreciating further.

Figure 2 shows the performance drawdowns, in gross returns, of the MSCI Emerging Markets Index over the past 20 years. The performance after a correction is mixed, with some negative cycles lasting multiple years. Even so, long-term investors have ultimately been rewarded for patience following extended periods of negative returns.

Figure 2: MSCI Emerging Market Performance

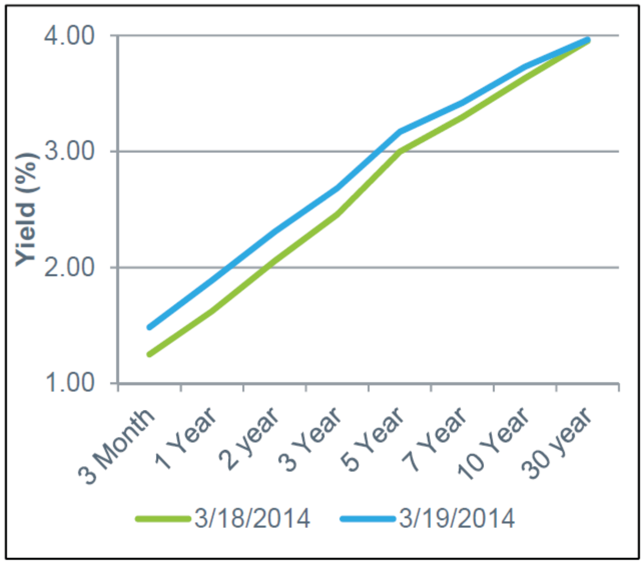
Year	Drawdown	Following Year
2013	-2.3%	TBD
2011	-18.2%	18.6%
2008	-53.2%	79.0%
2002	-6.0%	56.3%
2001	-2.4%	-6.0%
2000	-30.6%	-2.4%
1998	-25.3%	66.4%
1997	-11.6%	-25.3%
1995	-5.2%	6.0%

Fixed Income

During the quarter, the Fed's comments on the end of quantitative easing pushed the 2-year yield up to 0.44%, a 6 basis point increase, while concerns over the global economic environment weighed on longer maturities. The yield on the 30-year Treasury declined over 40 basis points for the quarter, resulting in a significant flattening of the yield curve.

Figure 3 illustrates the immediate impact of Yellen's comment by showing a before and after snapshot of the implied treasury yield curve.

Figure 3: 2-Year Forward Treasury Yield Curve



Near-term inflation expectations increased, which helped TIPS make up some of the losses spurred by the rise in real yields in 2013. Investment-grade corporate markets posted a 2.9% gain for the first quarter, led by the Utility sector, as issuance remained strong. Within below investment grade credit, CCC-rated issues continued to outperform higher quality high yield, and bank loan inflows remained healthy as investors pushed further out the risk spectrum in search of yield. Ongoing tapering of the Fed's asset purchase program caused Agency MBS to underperform the broad fixed income markets. Turning abroad, hard currency emerging market debt (EMD) outperformed local currency EMD following heightened currency volatility early in the quarter.

Hedge Funds

Despite a fluctuating market environment, most hedge funds delivered positive returns in the first quarter. Initial estimates show multi-strategy funds of hedge funds with gains ranging from 1.5% to 3.0% in the first quarter. In January many funds demonstrated impressive downside protection relative to equity markets with a February rally in most risk assets providing a tailwind.

ASSET CLASS COMMENTARY

Estimates for March suggest neutral to slightly negative returns, with credit strategies outperforming. Extending a trend from 2013, fundamental stock picking generated positive risk-adjusted alpha on the long and short side. Encouraging returns in long and short positions in February were followed by sobering reports of losses on long positions in March. Still, most long/short equity funds ended in positive territory and delivered results roughly in line with equity markets. Macro strategies posted weak results, with declines in January and March offsetting gains in February. Discretionary and systematic strategies posted losses for the quarter, and managed futures strategies struggled with trend reversals. Long/short credit performance moved higher, with early reports indicating strength in long-biased credit and distressed strategies. First quarter results for diversified hedge funds are in line with or slightly better than expected given market conditions.

Global Tactical Asset Allocation (GTAA)

GTAA strategies performed well in the first quarter as most asset classes provided positive returns after shrugging off a difficult equity environment in January. Dispersion between U.S. and international equity markets continued to be a meaningful predictor of manager success. Continuing on a theme from 2013, U.S. equities outperformed their developed international and emerging counterparts, leaving managers with less U.S. equity exposure at a disadvantage. In a reversal of trends that played out in 2013, managers that deviate significantly from a traditional 60/40 mix in favor of holding more spread-sensitive, foreign or longer maturity fixed income experienced strong returns. In particular, emerging market debt, which was one of the worst performing asset classes in 2013, posted attractive returns in the first quarter, rewarding managers that maintained exposure in the face of ongoing balance of payments issues. Duration sensitive assets rebounded and provided positive results as nominal yields in the U.S. fell even as the Fed announced continued tapering. Viewed over a 1-year horizon, U.S. and other developed equity exposure has been the main driver of returns.

Diversified Inflation Strategies (Real Return)

During the first quarter, Diversified Inflation Strategies moved broadly higher as most real assets experienced gains. Despite continuing monetary stimulus, the inflationary environment remained largely subdued with expectations of future inflation remaining well anchored to the Fed's long-term goal of 2%. In the recent past, and notably calendar year 2013, these conditions have proven difficult for strategies specifically designed to have meaningful betas to persistently high or unexpected inflation. Nevertheless, managers with heavier allocations to REITs and commodities performed relatively well in the first quarter. REITs posted attractive returns while commodities, especially those related to agricultural goods, experienced significant gains given weather-related issues over the quarter. Managers with larger strategic allocations to natural resource equities faced relative headwinds, as resource equities trailed other inflation hedging asset classes. On the fixed income side of the ledger, TIPS appreciated slightly ahead of U.S. nominal government bonds, and bank loans modestly lagged.

Real Estate

Core U.S. Real Estate started out 2014 with modest, positive performance. Preliminary returns show ODCE index component funds gained between 1.5% and 3.0% during the quarter, and were up between 12.0% and 17.0% for the trailing one-year period. Publicly-traded real estate experienced strong growth during the first quarter with an 8.5% return in the FTSE NAREIT All Equity REITs Index. Although improving economic conditions are expected to increase commercial real estate transaction volumes, there was muted growth across all major property sectors. However, preliminary data shows that lending amounts for commercial real estate property in secondary markets and for non-core property have increased significantly. Institutional investors continue to show an appetite for riskier private real estate strategies. Capital raised by opportunistic funds increased to $36 billion compared to $20 billion two years earlier. Core real estate fundraising decreased to $2.3 billion from $6.5 billion from the prior year.

Data Sources: Bloomberg, Morningstar, http://www.econ.yale.edu/~shiller/data.htm, www.ncreif.org.