CAPITAL MARKETS REVIEW
2nd Quarter 2015

June 30, 2015

OVERVIEW

Market activity in the second quarter of 2015 saw the reversal of several major trends. First, U.S. Dollar strength dissipated to a degree, as it sold off almost 3% relative to other developed currencies. Second, developed market interest rates, which had been trending lower and were negative in some markets, reversed sharply. And third, oil prices, in part helped by weakness in the U.S. Dollar, bounced off the Q1 lows and finished the second quarter higher. Relatively benign equity volatility in April and May gave way to heightened volatility in the second half of June, with investors fixated on Greece's debt situation and government intervention in China. Still, global equity markets generally finished the quarter with small gains.

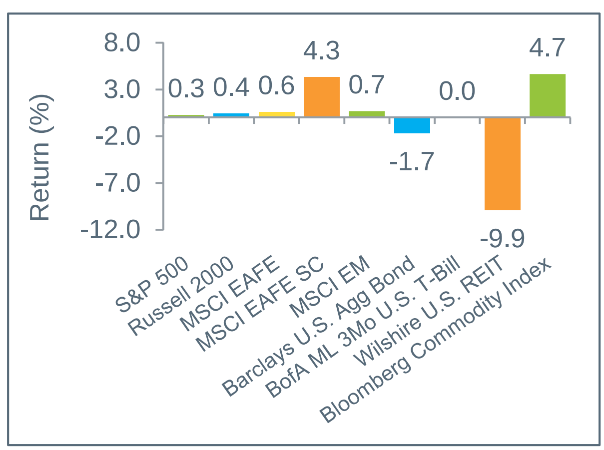
In the U.S., the much anticipated June Federal Open Market Committee came and went. Uninspiring first half economic data across a number of categories was enough to convince the Federal Reserve to maintain interest rates at 0%. The Board cited below target inflation, softer GDP growth, and lower labor productivity as reasons to be wary of increasing rates. Economic data released during the second quarter was largely consistent with that view. Though unemployment continued to trend downward, finishing the quarter at 5.3%, the pace of non-farm payroll job gains in 2015 has been considerably lower than the pace in 2014. Payroll growth in 2014 averaged 260,000 jobs per month compared to monthly gains of just 208,000 jobs thus far in 2015. Manufacturing growth seems to have moderated from its 2014 pace as well, with average PMI readings for the year at 52.6 compared to 55.7 in 2014. Investors have been viewing the current headline CPI numbers, which are below the Fed's target of 2%, cautiously as some expect they fail to fully account for underlying wage growth acceleration. If wage growth accelerates, many view a 2015 interest rate increase as probable.

Weak data domestically coincided with some notable developments in Europe and China during the final weeks of the quarter. In Europe, Greece's problems deteriorated significantly after bailout talks broke down. The Syriza-led government missed a $1.7 billion payment due to the IMF in June, and was forced to introduce capital controls in the form of shuttering their banks and limiting ATM withdrawals. As of this writing, the situation in Greece continues to unfold. In China, the government's desire to rotate investment from its real estate sector to the equity markets hit a snag, as the Shanghai Composite fell 20% in the final 10 trading days of the quarter. In response, the People's Bank of China cut its benchmark interest rate by 0.25% during the final week of June. Selling continued into July, though China's equity market is still up significantly year-over-year.

TRAILING PERIOD MARKET PERFORMANCE (%)

	QTD	CYTD	1 Year	5 Years	10 Years
S&P 500	0.3	1.2	7.4	17.3	7.9
Russell 2000	0.4	4.8	6.5	17.1	8.4
MSCI EAFE	0.6	5.5	-4.2	9.5	5.1
MSCI EAFE SC	4.3	10.1	-0.8	12.4	6.6
MSCI EM	0.7	2.9	-5.1	3.7	8.1
Barclays U.S. Agg Bond	-1.7	-0.1	1.9	3.3	4.4
BofA ML 3Mo U.S. T-Bill	0.0	0.0	0.0	0.1	1.4
Wilshire U.S. REIT	-9.9	-5.7	5.2	14.7	6.9
Bloomberg Commodity Index	4.7	-1.6	-23.7	-3.9	-2.6

QUARTER-TO-DATE PERFORMANCE (%)



KEY ECONOMIC INDICATORS

		As of	3/31/2015	12/31/2014	10 Year Average
Federal Funds Rate	0.08%	6/30/2015	0.06%	0.06%	1.49%
Treasury - 1 Year	0.26%	6/30/2015	0.23%	0.21%	0.33%
Treasury - 10 Year	2.35%	6/30/2015	1.92%	2.17%	3.22%
Treasury - 30 Year	3.11%	6/30/2015	2.54%	2.75%	3.96%
Breakeven Inflation - 1 Year	0.73%	6/30/2015	1.46%	-0.21%	1.08%
Breakeven Inflation - 10 Year	1.89%	6/30/2015	1.78%	1.68%	2.15%
Breakeven Inflation - 30 Year	2.03%	6/30/2015	1.87%	1.90%	2.37%
Barclays US Corp: Hi Yld Index - OAS	4.76%	6/30/2015	4.66%	4.83%	5.69%
Capacity Utilization	78.06%	5/31/2015	78.82%	79.58%	77.10%
Unemployment Rate	5.30%	6/30/2015	5.50%	5.60%	6.90%
ISM PMI - Manufacturing	53.50%	6/30/2015	51.50%	55.10%	52.40%
Baltic Dry Index - Shipping	800	6/30/2015	602	782	2,865
Consumer Confidence (Conf. Board)	101.40	6/30/2015	101.40	93.10	75.30
CPI YoY (Headline)	0.00%	5/31/2015	-0.10%	0.80%	2.20%
PPI YoY - Producer Prices	-3.00%	5/31/2015	-3.20%	0.60%	2.80%
US Dollar Total Weighted Index	$90	6/30/2015	$92	$85	$77
WTI Crude Oil per Barrel	$59	6/30/2015	$48	$53	$82
Gold Spot per Ounce	$1,172	6/30/2015	$1,184	$1,185	$1,106

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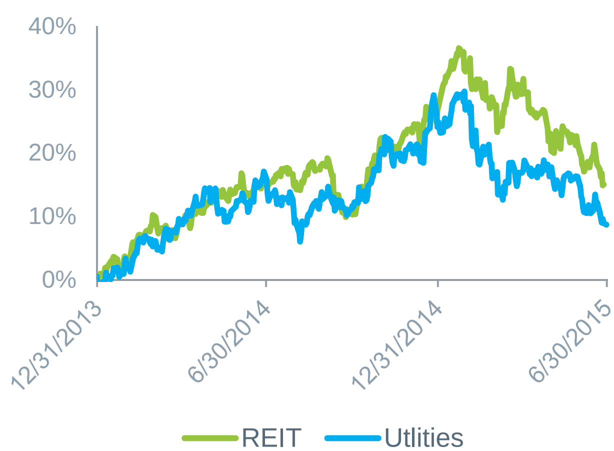
U.S. Equity

The U.S. equity markets ended the quarter relatively flat as market turmoil overseas impacted domestic markets in June and erased otherwise positive April and May performance. The Russell 3000 Index finished the quarter returning 0.14%, with growth moderately outperforming value. Large-cap stocks experienced mainly flat performance, while mid-cap stocks faced strong headwinds and ended in negative territory. Micro- and small-cap stocks were the top performers during the quarter. Within the micro- and small-cap segments, growth outperformed value by 414 and 318 basis points, respectively.

Continuing a trend from the first quarter of 2015, a strong U.S. dollar served as a hindrance to companies that derive significant earnings from non-U.S. regions. In addition, anticipated increases in consumer spending resulting from decreased oil prices proved lackluster. Investors with exposure to the consumer discretionary and health care sectors benefited from gains in those segments. The energy, industrials, REIT and utilities sectors posted notably negative performance.

Figure 1 uses the MSCI U.S. REIT and MSCI USA Utilities indexes to showcase the negative cumulative returns from rate sensitive sectors in 2015. This represents a reversal of a multi-year trend where each sector had benefited from the market's preference for yield-generating securities.

Figure 1: Rate Sensitive Sector Returns



Non-U.S. Equity

The developed international markets outperformed domestic for the second quarter in a row, with growth stocks continuing to outperform value. The strongest contributor to performance for the quarter, as measured by the MSCI EAFE Index, was Japan. Japan reported 2.4% GDP growth for the previous quarter, giving some confidence that Abenomics has started to work.

The emerging markets slightly outperformed their developed counterparts. Within EM, value stocks outperformed; reversing the strong outperformance of growth stocks within emerging

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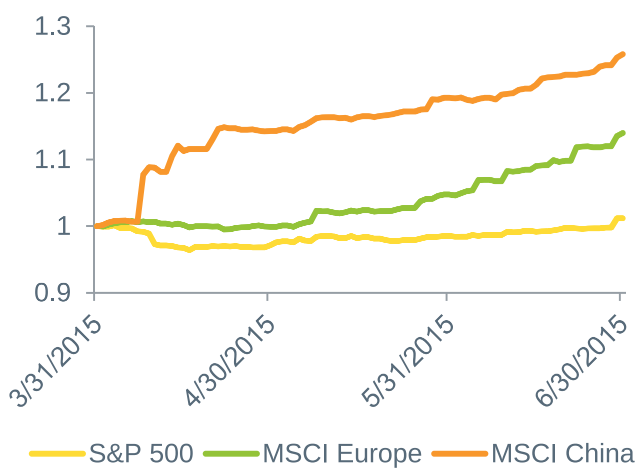
markets over the past few years. Greece's debt crisis dominated the headlines yet its equity markets actually saw positive performance for the quarter. However, performance from Greek stocks over the past 5 years has been negative; many active managers have little to no exposure to the country as the situation has become too unpredictable. China had a strong positive quarter, but volatility was elevated. Over the past year, the Shanghai composite has risen over 150%, partially fueled by government intervention. The increased use of margin debt in China has garnered attention recently and contributed to sharp downturns in the local Chinese markets. **Figure 2** tracks the cumulative rate of change in 12-month volatility for equity indexes in the U.S., Europe and China. The chart displays the significant increase in volatility in China early in the quarter. Volatility in Europe picked up in June as the markets reacted to the ongoing concerns in Greece.

Figure 2: Changes in Regional Volatility



Fixed Income

Fixed income markets were down as rates rose and credit spreads widened. The Barclays U.S. Aggregate Bond Index was down 1.68% posting negative returns for all three months of Q2 – the first 3-month negative run since 2008. Reduced liquidity in fixed income markets has led to higher market price volatility and increased trading costs.

The 10- and 30-year Treasury yields rose by 40 and 57 basis points, respectively, in anticipation of a Fed funds rate hike. Long duration bonds suffered accordingly. The Barclays Long U.S. Government/Credit Index lost 7.57%.

Investment grade credit spreads widened and the Barclays U.S. Credit Index was down 2.88%. High yield bonds, however, ended the quarter flat as energy prices partially rebounded after reaching a trough in the previous quarter.

Government bond yields for many of the larger European countries bottomed out in April and climbed through the month of May and June as questions arose about whether Greece would be able to service its debt. The German Bund reached a year-to-date high of 1.05% in June. Hard currency emerging market debt outperformed local currency for the ninth consecutive quarter.

Diversified Hedge Funds (DHF)

Most hedge fund strategies generated positive returns in the second quarter, adding to gains realized in Q1. Long/Short equity funds in particular are having a strong 2015. Top tier managers have added alpha on both their long and short positions as they were able to capture the majority of equity market upside during the months of April and May, and protected capital well toward the end of June as markets sold off. The environment for Event Driven strategies remains favorable as well, aided in part by heavy involvement from the Activist investor community. Corporate management teams are increasingly looking to maximize shareholder wealth through M&A activity, share buybacks, and spinoffs. Event Driven and Merger Arbitrage strategies were up on the quarter as a result. Fixed Income oriented hedge funds also generated gains during the second quarter, as most managers were well positioned for a reversal in developed market interest rate trends. By contrast, Global Macro managers, and Systematic Trend Followers in particular, were positioned incorrectly for the interest rate moves. Macro strategies were the strongest performing strategy in 2014 and into Q1-2015, as managers were able to ride trends in developed market rates, the U.S. Dollar, and energy. However, April and May brought sharp reversals in a number of these trends; consequently many Macro funds were hit with heavy losses during the second quarter.

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Global Tactical Asset Allocation (GTAA)

In April and May, most GTAA managers posted gains and outperformed a relatively-undiversified, U.S.-centric 60/40 allocation; however, the majority posted losses for the quarter due to the volatility that occurred in June. In a break from performance characteristics of the past two quarters, valuation-driven managers outperformed growth-oriented equity strategies. Thematic and/or secular focuses on yield-oriented holdings, however, were a key determinant in the underperformance of several managers as yield-sensitive equities, especially REITs, lagged. Managers with modest overweight exposure to traditional global equity and short-duration fixed income exposure fared best as foreign and emerging allocations marginally added to performance, while cash outperformed moderate duration fixed income, which finished the quarter negative. Risk parity managers in general faced an especially difficult quarter as bond yields increased globally while equities provided only moderate returns.

Diversified Inflation Strategies (Real Return)

DIS managers again provided a wide range of performance outcomes as market expectations for short-term inflation decreased while longer-term expectations increased as measured by a steepening of the TIPS breakeven curve. The market's 10 year view for future inflation was modestly higher at 1.9% as of the quarter's end compared to 1.8% last quarter, while the 1 year view decreased from 1.5% to 0.7%. Measured inflation was again disparate as Core CPI decreased to 1.7% from 1.8%. The more-volatile Headline CPI increased from -0.10% to -0.04%. CPI measures reflect year-over-year changes as of May since data is released with a one month lag. Inflation sensitive assets also diverged widely for the quarter, including various subsets of the commodities complex.

Even with low short-term inflation expectations, disparate measures of inflation, a difficult quarter for equities and rising real yields, most diversified inflation strategies outperformed a moderate duration TIPS allocation. Managers with larger energy and agricultural commodities exposures saw a key reversal of their underperformance from earlier in the year. Managers with larger U.S. REIT equity allocations underperformed with the partial exception of managers focused on the full capital structure within REITs, which participated in less of the downside. Managers with larger TIPS exposures, especially those in longer duration securities, underperformed the broader group.

Real Estate

While real estate securities returns were hampered by rising long-term interest rates in Q2, as evidenced by a -8.93% return in the FTSE NAREIT All REITS Index, private real estate continued its run of strong, positive returns. Preliminary reports from the NCREIF-ODCE Index show that U.S. Core Real Estate returned 3.82% for the quarter and 14.84% for the trailing year, marking the 21st consecutive quarter of positive returns in this sector.

Improving economic conditions in the U.S. have led to positive momentum in the fundamentals of major property types, including vacancy decreases in the office, industrial, retail, and apartment sectors. Additionally, the hotel sector has experienced the most active recent gains, showing a 97% year-over-year gain in transaction volume. These continued improvements have been reflected in market cap rates, as commercial real estate yields have compressed to near or below pre-recession levels across all major property types.

While real estate deal activity remained strong in the U.S., transaction volumes were down 8% and 7% in the Asia-Pacific and Euro regions, respectively. On a global level, transaction volume for Q2 totaled $161 billion, resulting in nearly the same level of activity on a year-over-year basis.

Investor appetite in real estate remains strong as closed-end private real estate funds closed on $26 billion of capital during Q2 across 47 funds, and hold $23 billion in dry power available for investment.

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