APRIL 14, 2016

"There is no other shelter hereabout: misery acquaints a man with strange bed-fellows."
– William Shakespeare, *The Tempest*

Since the end of 2014, if one checked the level of the S&P 500 only at the end of each calendar quarter, it would appear as if nothing had happened. However, even a casual observer knows that not to be the case, especially, in periods like the last three months. Much like each quarter of 2015, the popular benchmark began and ended the first quarter of 2016 at roughly the same level, yet fluctuated significantly during the period.

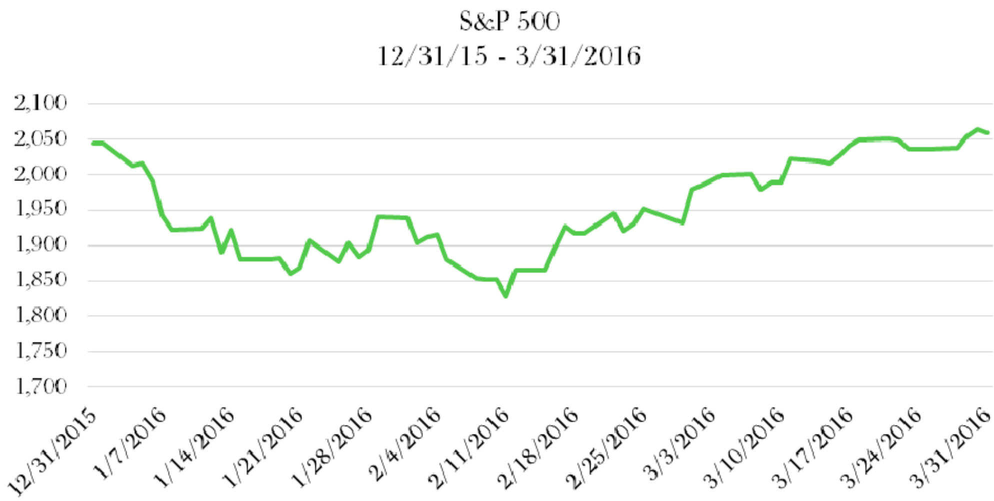
Date	12/31/2014	3/31/2015	6/30/2015	9/30/2015	12/31/2015	3/31/2016
S&P Closing Price	2058.90	2067.89	2063.11	1920.03	2043.94	2059.74

Source: FactSet

Right from the opening bell on the first day of trading on January 4, stocks dropped precipitously, declining more than 11% by early February. The reasons cited by market observers and the financial press were mostly a rehash of concerns that we too have pointed out in previous commentaries: slowing growth in China and potentially the U.S.; continued recession in Europe and Japan; the ongoing slide in the price of oil and other commodities; uncertainty about U.S. interest rate policy; etc. Investors also took notice of the two warning signs that we mentioned in our last letter: widening credit spreads (higher yields for junk bonds relative to U.S. Treasury securities) and narrowing stock market leadership (a disproportionate contribution to index average performance from a small number of companies).

A new worry was added to the list during the first quarter of 2016. While negative short-term interest rates have been used by the European Central Bank and other European banks over the last few years, this was largely considered a temporary anomaly. In January, the Bank of Japan surprised the markets by announcing its own negative interest rate policy. Investors have been understandably troubled by the potential implications of a policy that is both untested and counterintuitive. It is hard to imagine why anyone would willingly place money in a bank or buy a bond, knowing that they would receive back an amount less than their original deposit or investment. It is one thing to pay for storage of unused furniture and last year's wardrobe; entirely different when the subject is money. The practice seems irrational, which gives the impression that central bankers are overreaching and possibly concerned about even deeper challenges in the future.

On February 11, for no apparent reason, financial markets reversed course. Over the subsequent six weeks, market benchmarks around the world almost perfectly retraced their steps. Even oil got into the action. West Texas Intermediate crude hit a 12-year low of $26 barrel, only to bounce 50% by the first day of spring. Fears did not simply recede; they disappeared, calling to question whether today's complacency is any more rational than January's concerns.



Source: FactSet

In our year-end commentary we stated "*we are not predicting a downdraft, but should one occur we believe it will create more opportunity than risk*". On the face of it, that assessment appears to have been correct. Though the "opportunity" was fleeting, we did take advantage of depressed prices to establish a new position in Whirlpool in mid-February. However, despite the fact that the S&P 500 stands at virtually the same spot it did three months ago, we think it is prudent to adopt a bit more cautious stance. Asset prices are similar, but the investment climate has noticeably changed.

Though the S&P 500 **average** is at virtually the same level it was both at year end 2015 (2043.94) and 2014 (2058.90), the behavior of underlying stocks and sectors has dramatically changed. Last year's losers have been this year's winners, so far. But this is not just a case of laggards catching up. Markets are sending decidedly mixed messages. Risky global assets like emerging market stocks and commodities, which performed badly last year, had solidly positive returns in the first quarter. When risky assets start to outperform, it is usually a sign that it is safe to speculate. However, the two strongest sectors in the U.S market have been utilities and telecoms, generally among the most conservative. The inconsistency of these unlikely companions is difficult to explain and gives us pause.

	2015 Return	2016 YTD Return
Emerging Market Stocks	-17.97%	6.49%
GS Commodity Index	-22.49%	3.57%
US Utilities	0.22%	14.82%
US Telecoms	-0.47%	11.12%

Source: FactSet

Past performance does not guarantee future results. The performance data quoted represent past performance and current returns may be lower or higher. Share price and investment return fluctuate and an investor's shares may be worth more or less than original cost upon redemption. For periods less than one year, performance is not annualized. For performance data current to the most recent month-end please call 866-684-4915. Securities in the Funds do not match those in the indexes and performance of the Funds will differ. It is not possible to invest directly in an index.

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What seems to be troubling U.S. investors most is uncertainty. The future path of short-term interest rates is no clearer today than it was before Chairperson Yellen announced the first rate hike in December 2015. The uniquely unorthodox nature of the 2016 Presidential campaign has created a level of unpredictability that is unusual in the United States.

The financial and healthcare sectors were the two worst-performing sectors of the market this quarter, declining 4.86% and 5.82%, respectively. This has impacted your portfolio as these represent two of our largest sector concentrations.

Though we were able to do a little bargain hunting mid-quarter, on balance we have taken a somewhat more conservative stance. Where appropriate, we have raised cash modestly in portfolios. Companies will begin to report their first quarter earnings by April 11. With the market close to its all-time high, there is room for disappointment. While it is likely that asset prices will continue to be volatile, it is important to maintain proper perspective. As we have said in previous commentaries, the fundamental backdrop is not nearly as risky today as it was before the financial crisis. In due course, we may again have the opportunity to use the extra cash to invest in cheap assets.

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