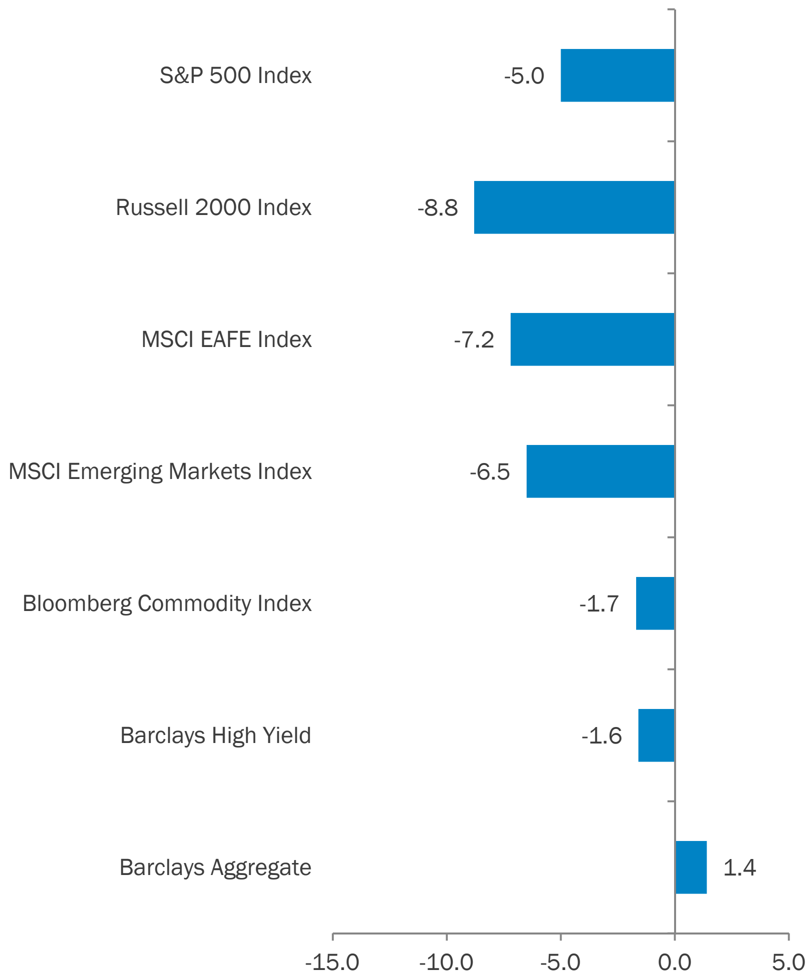
Market Update

As of January 31, 2016

Market Performance



Source: Morningstar Direct, MSCI, S&P, Bloomberg, Barclays

Observations

- **Stock Market:** U.S. equity markets experienced the worst opening two weeks in history, with the S&P 500 down 8%.
- **Macro News:** there have been a combination of negative macro headlines driving market sentiment:
  1. Slowing Chinese growth - potentially worse than expected
  2. Oil prices low and continuing to decline
  3. Monetary policy of major central banks have diverged, impacting fixed income and currencies
- **Oil:** prices have fallen 10% in 2016, recovering recently after hitting a 12-year low and prices below $30 per barrel.
- **China:** the local Shanghai stock market is down 23% 2016.
- **High yield:** spreads have widened from 6.6% to 7.3%. The energy sector has spreads above 15%, levels last experienced during the financial crisis in December 2008.
- **Equity valuations:** have decreased with U.S. Stocks trading at about 15.2x forward earning. U.S. Earnings are expected to grow at 15% for 2016.
- **U.S. Economic Data:** generally trended positive over the past year despite concerns surrounding global growth and impact of monetary policy.
- **Bear Markets:** of the last 15 bear markets since 1928, 10 have coincided with a recession.

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Drivers of the January 2016 Market Selloff

Concerns about China

- Economy is slowing during transition from an investment/ industrial to a consumer/services driven economy
    - Reduced demand for commodities
    - Manufacturing sector has slowed
- As demand has slowed, industrial companies have excess capacity and high debt levels
- Devaluation of the Yuan
    - Capital flight as citizens move capital offshore
- Questions regarding Chinese government's ability to achieve a soft landing

Falling Oil Prices

- Daily supply exceeding demand
- Surprise policy change in 2014 as Saudi Arabia no longer defending the price of oil
    - Predatory pricing by Saudis to protect market share from competitors (US Frackers)
- Excess oil in storage continues to grow dramatically
- Negative impact on energy companies and oil exporters who continue to pump oil at unprofitable levels to pay interest on debt used to expand production
- Given high issuance by energy companies and recent defaults, high yield bonds have sold off
- Outlook for global oil demand is in question, driven by slowdown in China

Monetary Policy

- Divergence of global monetary policies of major central banks (e.g., ECB, BOJ, China versus US, UK)
    - Outlook for the $ impacted by Fed communications regarding rate increases
- Stronger $ makes US exports more expensive, hurting US manufacturing
    - S&P 500 company revenues, half of which are from overseas, have been hurt by stronger $
    - Stronger $ lowers US inflation by making imports cheaper

Outlook

- China has over $3 trillion in reserves to defend its currency and support its economy
    - The Chinese Central Bank continues to take accommodative steps to support economy
    - China's GDP is still relatively high
- Cheap oil and gasoline help consumers, net importers and industries using them in production
    - Depletion of existing wells and reduced rig counts combined with reduced investment in new oil wells may lead to a future supply shortages
- The Fed may pause on plans to hike interest rates
    - Factors pushing $ higher may already be priced in
    - The strong $ helps countries that export to the US

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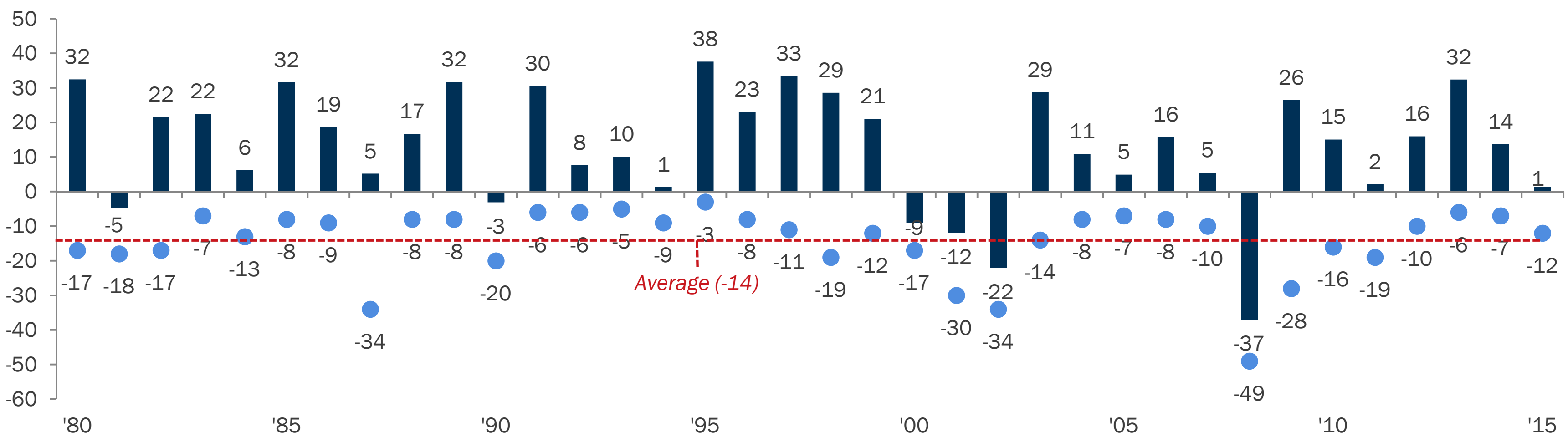
U.S. Stock Market: Bull & Bear Markets

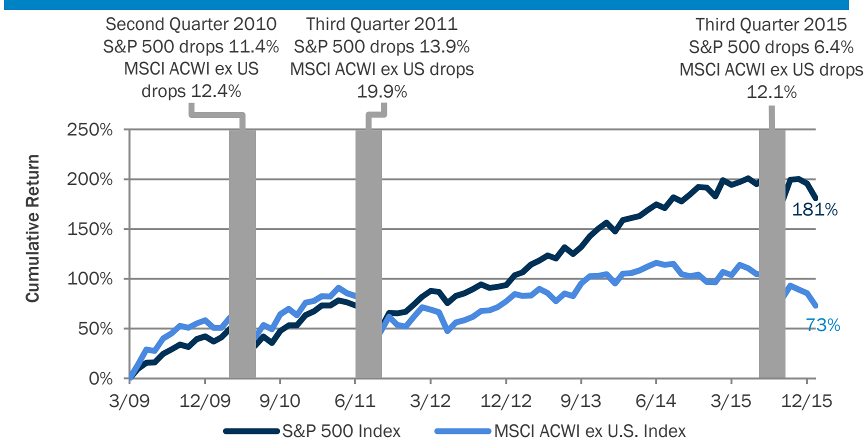
As of January 31, 2016

S&P 500 Index: Intra-Year Declines vs. Calendar Year Returns



Source: Morningstar Direct, S&P

Market Volatility



Source: Morningstar Direct, S&P, MSCI

Characteristics of Bull and Bear Markets

	Bull Markets			Bear Markets		
Market Corrections	Bull Begin Date	Bull Return	Duration (months)	Market Peak	Bear Return*	Duration (months)
Crash of 1929	Jul-26	152%	38	Sep-29	-86%	33
1937 Fed Tightening	Mar-35	129%	24	Mar-37	-60%	63
Post WWII Crash	Apr-42	158%	50	May-46	-30%	37
Flash Crash of 1962	Oct-60	39%	14	Dec-61	-28%	7
Tech Crash of 1970	Oct-65	103%	74	Nov-68	-36%	18
Stagflation	May-70	74%	32	Jan-73	-48%	21
Volcker Tightening	Mar-78	62%	33	Nov-80	-27%	3
1987 Crash	Aug-82	229%	61	Aug-87	-34%	31
Tech Bubble	Oct-90	417%	115	Mar-00	-49%	31
Global Financial Crisis	Oct-02	101%	61	Oct-07	-57%	17
Current Cycle	Mar-09	181%	83			

Source: JP Morgan

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Endnotes

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