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Monthly Economic & Capital Market Update

May 2015

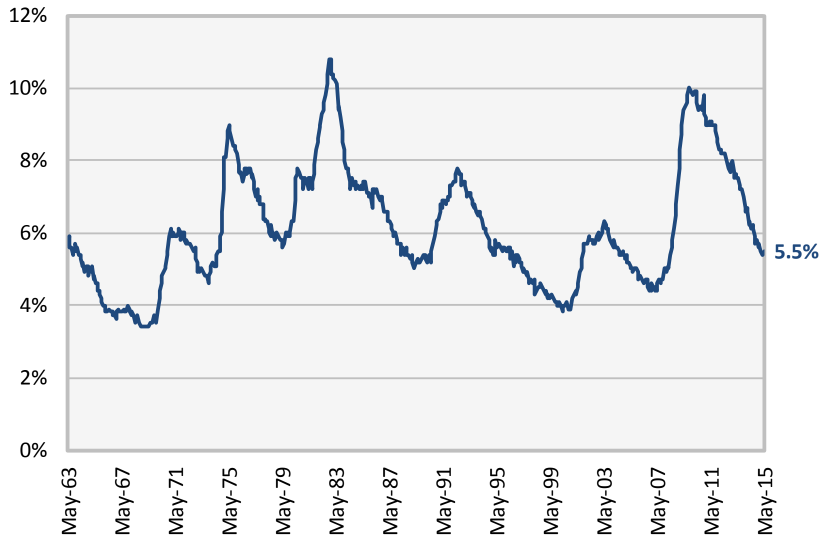
Economy

- The US economy showed a modest improvement in May over the slow start to 2015. Strong job gains, signs of increasing future demand, and continued recovery in the real estate market are signaling that the economy is likely to continue along its path of slow growth. The monetary policy of the US Federal Reserve remains very accommodative, as the Federal Funds rate has been near zero for more than six years. Central bank policy throughout the rest of the world has also eased, as policy makers lowered interest rates in an attempt to battle slowing growth and deflationary pressures.
- The labor market continues to be one of the few bright spots of the US recovery. Employers added 280,000 jobs in May, exceeding economist projections of 225,000 jobs added. The unemployment rate rose 10 basis points (bps) to 5.5% during the month, as more Americans joined the labor force in search of work. Previously published figures for March and April were revised higher by a combined 32,000 jobs. Wages rose 2.3% over the 12 months ending May.
- US consumer prices, as measured by the Consumer Price Index (CPI), rose 0.1% during April. CPI declined 0.2% for the 12 months ending April. Core prices, which exclude food and energy costs, rose 0.3% for the month and 1.8% for the 12 months ending April. The disparity between headline and core CPI has been mainly a result of falling energy prices.
- The Institute for Supply Management's Purchasing Managers' Index (PMI), a gauge of future demand and manufacturing activity in the US, came in at 52.8 versus expectations of 52.0 in May; a number over 50 implies economic expansion. After declining in each of the previous three months, the Index rose in May, a sign that growth may be picking up following a slow start to 2015. While the strong US dollar remains a concern to US manufacturers, it appears their outlook for the economy improved in May.
- Real GDP contracted 0.7% on an annualized basis during the first quarter of 2015 according to the second estimate from the Bureau of Economic Analysis; the initial estimate of Q1 GDP was for growth of 0.2%. Inventories and the trade deficit contributed less to GDP than previously expected, causing the second estimate to be revised lower.

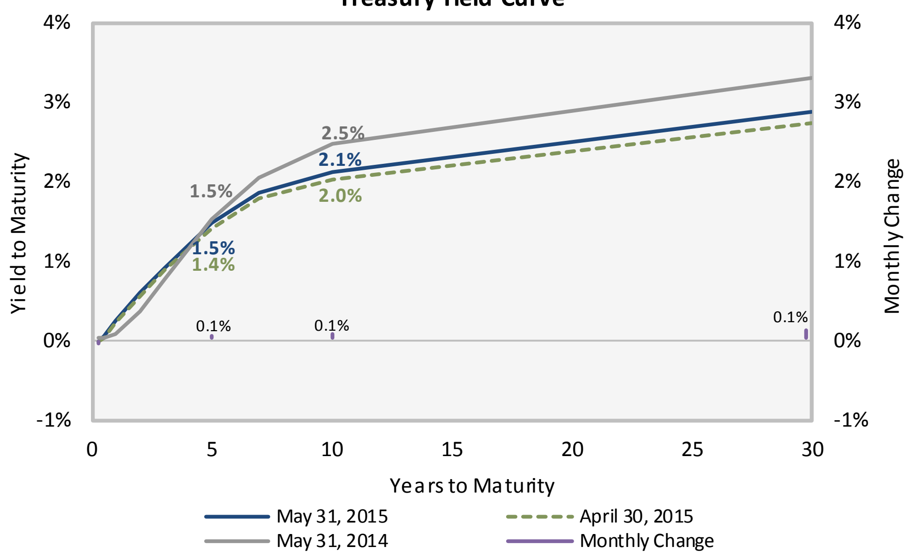
Yield Curve

- The spread between 2-year and 30-year Treasuries increased 10 bps to 230 bps at the end of May. Rates rose across the curve during the month.

Unemployment Rate



Treasury Yield Curve



Growth Assets

May 31, 2015

Public Equities

- Equity market performance was varied throughout the world during May, resulting in muted gains for the global index (MSCI ACW IMI, 0.1%). US stocks (S&P 500, 1.3%) outperformed international (MSCI EAFE, -0.5%) by 180 bps, and within the US small caps (Russell 2000, 2.3%) outperformed large caps (Russell 1000, 1.3%). The S&P 500 reached an all-time high during the month, moving higher despite mixed economic data which included disappointing first quarter economic growth. Emerging markets were the worst equity performers, with the volatile Chinese market ending the month nearly 4% lower.
- Upstream MLPs declined -13.5% during the month. Consolidation of upstream MLPs is occurring and is expected to continue as this sub-sector is the most challenged of the energy MLP universe. Notable trends include two very successful MLP IPOs in May of general partner interests, both of which priced at low yields and at the high ranges of their target IPO price. Investor demand for publicly traded GP MLP interests remains strong.

Public Debt

- High yield bonds saw small gains in May, with the Barclays US High Yield Index returning 0.3%. Spreads tightened 5 bps to 435 bps and remain below their 20-year average of 530 bps.

Private Equity

- Purchase price multiples, as measured by S&P Leveraged Commentary and Data (LCD), were 9.5x at the end of the first quarter; this multiple is higher than any annual average on record. Pricing is being driven by managers competing with each other and a renewed vigor from corporate buyers, who have a lower cost of capital and significant cost synergies that support higher prices. Despite this market dynamic, fundraising has not dropped significantly from the robust pace of 2014. Fundraising continues to be fueled by record distributions across the industry as well as investors increasing allocations in a search for higher returning assets.

Private Debt

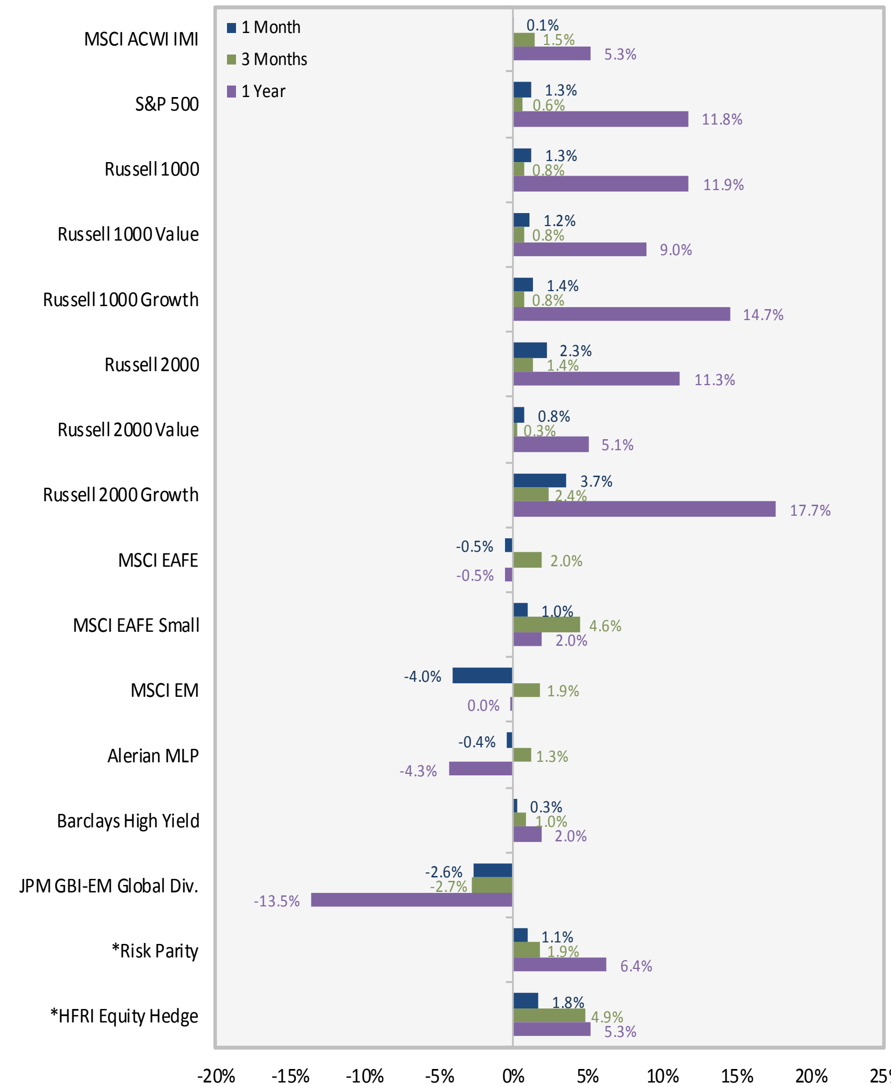
- There was an uptick in covenant relief amendments in the first quarter. While it is only one quarter of data, we will be monitoring for more reliefs in coming quarters as oil prices test the capital structures of several sponsor-backed deals in the oil patch. Debt/EBITDA ratios remain near all-time highs, but capital structures appear to be on firm footing; CapEx and interest coverage remain significantly higher than the low coverage rates seen in 2006 and 2007.

Risk Parity

- Risk parity strategies were generally positive in April. Global nominal bonds detracted while equities and commodities were positive.

Growth Hedge Funds

- Gains in equity and emerging market-oriented funds drove performance in April, while long/short equity and event-driven strategies were also positive.



* Data was not available at time of publication – returns are previous month's.
Note: Risk Parity returns are based on an internally comprised benchmark.
All returns are USD.

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Public Debt

- Interest rates generally rose across the world in May. Bond market volatility remains elevated compared to levels in recent years, as investors have reacted to global economic data, commentary from Federal Reserve officials regarding the timing of the first interest rate increases, and ongoing central bank intervention outside the US. European rates have been among the most volatile; interest rates moved to very low (and in some cases, negative) levels following the announcement of the ECB's stimulus program. Subsequently, bonds have sold off and rates have increased dramatically. For example, the German 10-year reached a low of 7 bps in late April before rising to 72 bps in May.
- Core fixed income (Barclays Aggregate) performed in line with core plus (Barclays US Universal) during the month, with both indices declining on falling rates and modest spread widening.
- US Government bond prices fell in May, returning -0.2%.
- Corporate bonds also declined in May, with spreads widening 5 bps to 135. Corporate bond spreads have averaged 145 bps over the past 20 years.
- Mortgage-backed securities were unchanged as agency MBS spreads remained at their lowest level since August 2010.
- International bonds once again declined as foreign interest rates rose and the US dollar strengthened, with the Barclays Global Aggregate ex-US Index returning -3.0%. Over the last 12 months, international bonds have returned -12.2% in USD terms, mostly due to dollar appreciation.

Private Debt

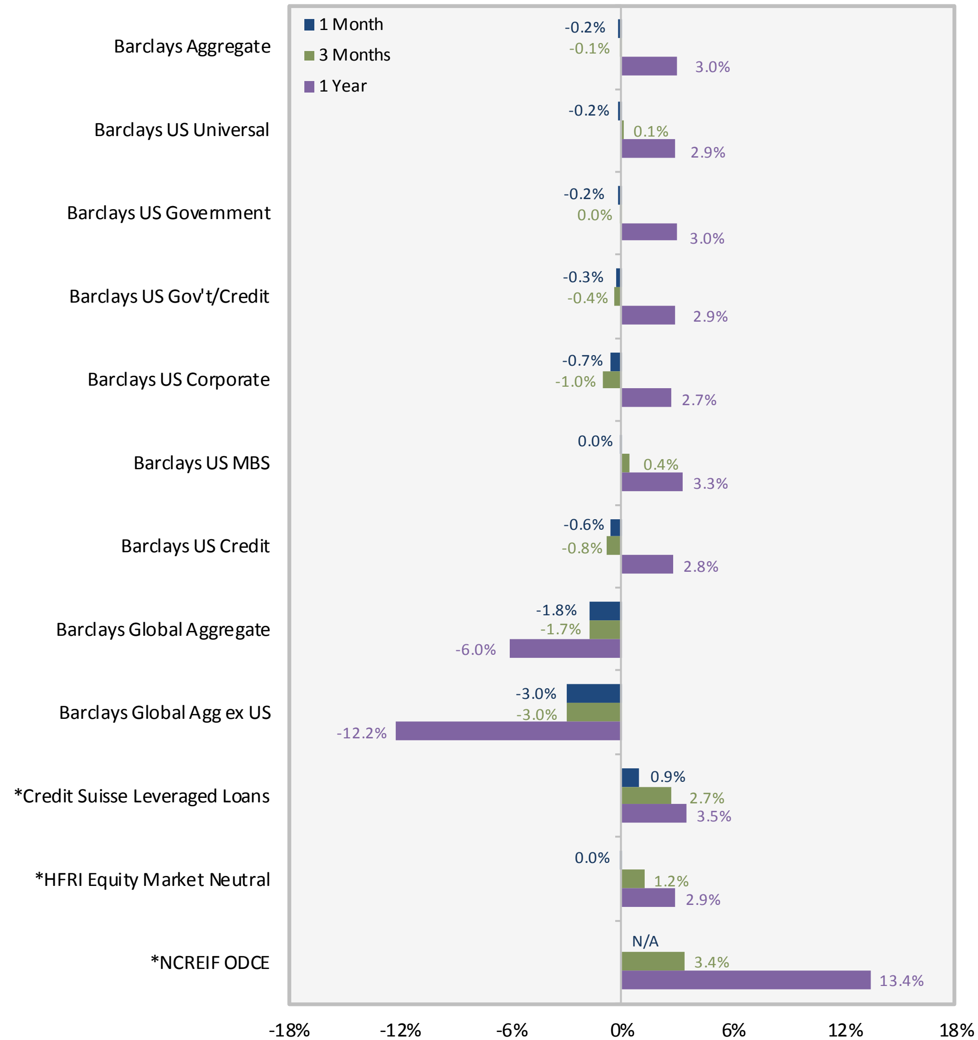
- Leveraged loans gained in April, bringing the one-year return for the Credit Suisse Leveraged Loan Index to 3.5%.

Relative Value Hedge Funds

- Credit and convertible arbitrage strategies led performance in April, while equity market neutral strategies were flat in aggregate.

Core Real Estate

- The first quarter gross return for core real estate is 3.4%, as measured by the NCREIF ODCE Index. Economic growth throughout the US has fueled favorable returns in the commercial real estate sector. Another contributing factor to the appreciating returns by the NCREIF ODCE Index has been financing, as funds with maturing debt continue to benefit from historically low Treasuries.



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Diversification Assets

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Inflation

- TIPS declined in May as real yields rose, returning -0.8%. The 12-month performance for the Barclays US TIPS Index was -0.5% as of May 31.

Deflation

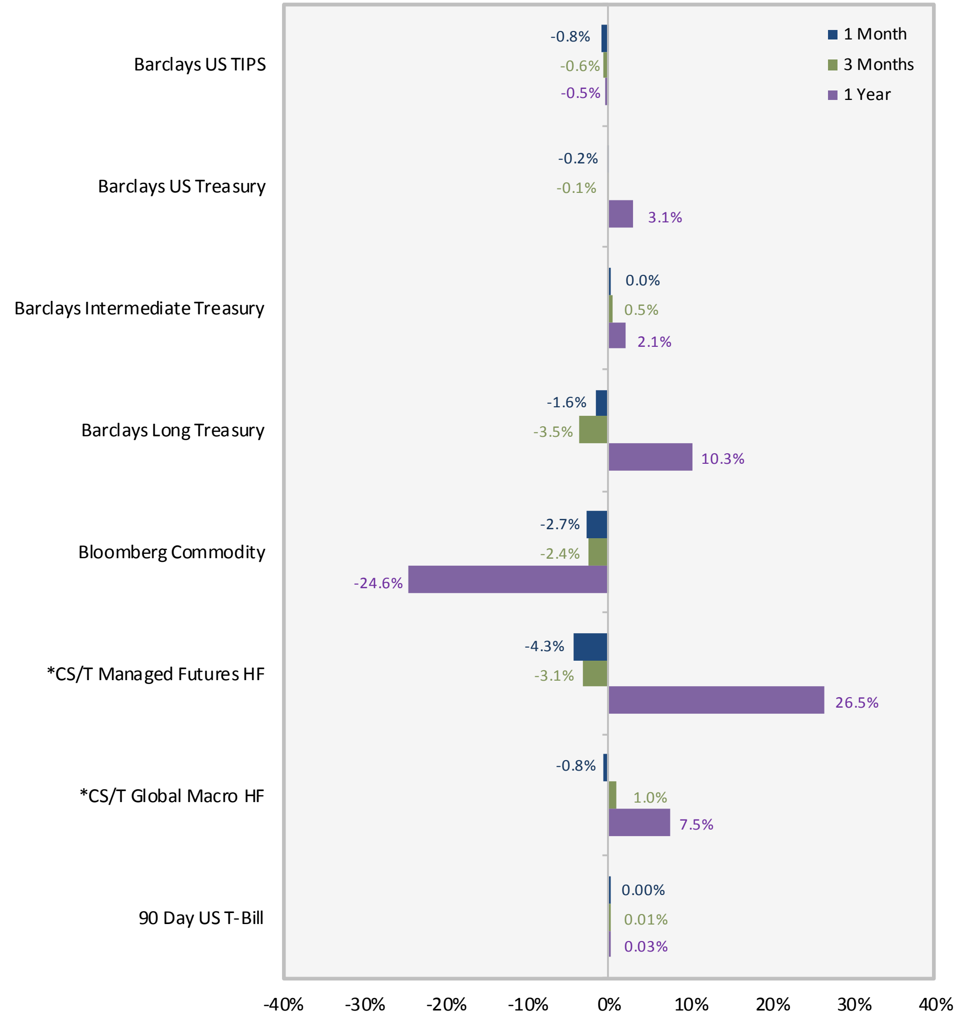
- Treasury prices fell during May, with the Barclays US Treasury Index returning -0.2%.
- Intermediate Treasuries were unchanged and long duration Treasuries returned -1.6% for the month. Intermediate and long Treasuries have earned 2.1% and 10.3%, respectively, over the past year. After declining to all-time lows in January, long-term interest rates have risen in recent months. As of January 31, the 30-year Treasury yield was 2.2%; at the end of April, this yield had risen to 2.9%.
- Cash continues to offer virtually no return, as 90-Day T-Bills have gained just 3 bps over the past year.

Commodities

- Agriculture and livestock commodities were generally mixed during May, although dispersion of returns was not wide. In energy, WTI crude oil (+1.1%) outperformed Brent crude oil (-1.8%) as non-North American producing regions continued to produce at high output levels. This was further influenced by an expectation that OPEC would maintain its current production level. Global oil prices have leveled out around $60 in the short term, with long term futures price expectations around $70 per barrel. Both gold and silver were modestly up during the month, while industrial metals all fell due to the combination of weak demand and elevated inventory levels and expectations.

Tactical Trading

- Discretionary managers posted varying performance, while CTAs detracted despite strong performance year-to-date.



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