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Second Quarter 2015 Market Summary

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While many of us enjoyed the 4th of July fireworks, Greece started another type of fireworks by decisively voting “no” on the austerity referendum and resoundingly rejecting the bailout terms. While we won’t know the ultimate consequences for weeks or months to come, there is a strong possibility that Greece will be forced to exit the Eurozone and thus will no longer use the Euro currency. While there may be economic chaos in Greece for a period of time and some short-term volatility in the markets, we believe ultimately the global financial impact will be minimal.

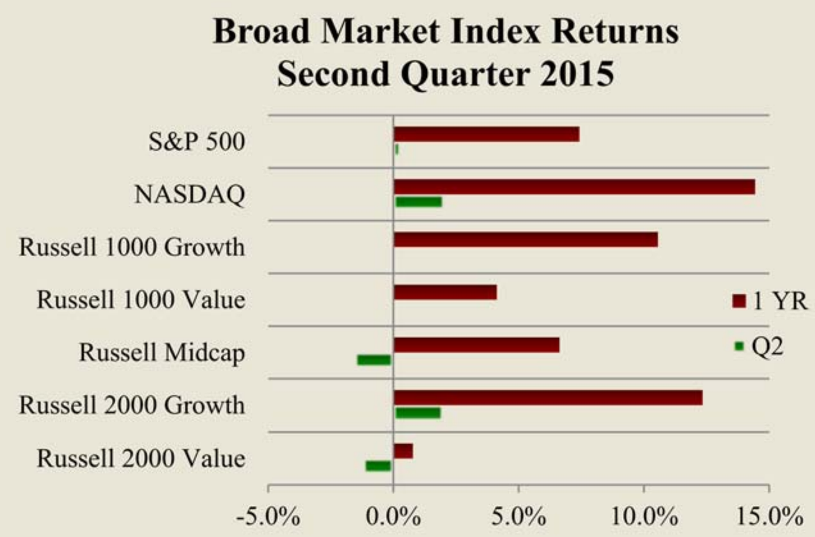
Despite the recent volatility, the S&P 500 has shifted into neutral during the last six months, and generated a very modest 1% year-to-date return. The market’s sluggishness is likely the result of investor focus on Greece and the anticipated increase in U.S. interest rates by the Federal Reserve Board. Investors appear to be ignoring the recent positive economic data and higher levels of M&A activity. The fact that the stock market is holding up as well as it has suggests that investors are relatively comfortable with current economic and market conditions.

While most equity categories are flattish thus far in 2015, interest sensitive categories were hit hard during the second quarter as a result of rising interest rates. Utilities declined roughly 10% year-to-date, while REITS dropped between 9 to 10%. In contrast, Healthcare remains a standout, while international and small cap stocks continue to out-perform US large cap stocks this year.

While stocks have shifted into neutral, bonds moved into reverse during the second quarter, snapping their positive trend over the previous five quarters. Bonds were negatively impacted by generally rising global interest rates during the quarter. The yield on the 10-year Treasury note rose to 2.34% from 1.93% at the end of the first quarter, while German 10-year bond yields rose to 0.74% from 0.18%.

Looking forward, investor perception of the U.S. economy and the more recent downturn in the Chinese markets will likely have much more impact on the global equity markets than the headlines regarding Greece. Though the U.S. economy has had a slow start to the year, recent economic data suggests that the U.S. economy is in the process of rebounding. While no “barn burner”, this improvement looks to be driven by the U.S. consumer. However, corporate earnings are definitely off their highs and the strong U.S. dollar will likely continue to provide a headwind for large US multinational companies.

As mentioned above, there has been a very sharp selloff in the Chinese markets. To date, the Chinese economy has withstood the selloff but there are concerns this continued activity could negatively impact the Chinese economy and have further spillover effects on European exports to China and ultimately on the US economy. Though it is too early to determine if these concerns are valid, we will continue to monitor this situation.



HIGHLIGHTS

GDP

- The Bureau of Economic Analysis released the third estimate of first quarter 2015 real GDP, an annual rate increase of -0.2% from the preceding quarter. This is the second year in a row in which GDP had negative growth in the first quarter.
- The University of Michigan Consumer Sentiment Index final reading for June was 96.1, which was an increase from May and the previous quarter. Consumer sentiment remains high as the labor market continues to improve.
- The ISM Manufacturing Index increased during the quarter from 51.5 in March to 53.5 in June. Similar to 2014, the ISM Index was weak at the start the year; however, it has rebounded throughout the year. Typically, when the ISM Index is above 55 it is bullish and when it is below 45 it is bearish.
- In June, the Conference Board Leading Economic Index increased 0.6% month-over-month to 123.6. The Index has been increasing gradually over the past year showing steady slow growth in the economy.
- The price of WTI Crude Oil was $59.48 at the end of June, which is 24.6% higher than $47.72 at the end of March. The price of Brent Crude Oil increased 12.3% in the quarter to $60.31. The price of oil rebounded the past quarter after declining over 50% from the middle of 2014 through March 2015.
- In June, the headline CPI was an increase of 0.1% year-over-year, up from a decrease of 0.2% in April. Core CPI, which does not include food and energy, had a 1.8% increase. Inflation levels have remained low over the past year and have been less than historical averages and the Fed's 2% inflation target.

HOUSING

- Preliminary existing home sales increased in June with an annualized rate of 5.49 million units from 5.21 million units in March. The June annualized rate is 9.6% above the 5.01 million units in June 2014. Home sales have picked up over the past few months after stalling in 2014.
- Median existing home sale prices increased during the quarter. The preliminary prices for June were 6.5% higher than the levels of one year ago and have been trending up since the beginning of 2012.
- New home sales were flat on the quarter with a seasonally adjusted annual rate of 482k homes sold in June versus 482k in March. Home sales have rebounded from the lows of May 2010, when 280k new homes were sold. The past few months' new home sales growth have accelerated on a year-over-year basis.
- S&P Case-Shiller 20-City Home Price Index (seasonally adjusted) showed home prices rose 4.9% year-over-year in April.

EMPLOYMENT

- The labor market slowed during June as nonfarm payrolls added 223,000 jobs in the month which was lower than expectations. In the second quarter, nonfarm payrolls averaged 221,000 jobs added per month which was more than first quarter's average of 195,000 jobs per month but was less than 284,000 recorded in 2Q 2014.
- The unemployment rate fell to 5.3% from 5.5% during the quarter.
- Initial Jobless Claims have been decreasing since 2009 and dipped to lows last seen in 1999.

DOMESTIC CORPORATIONS

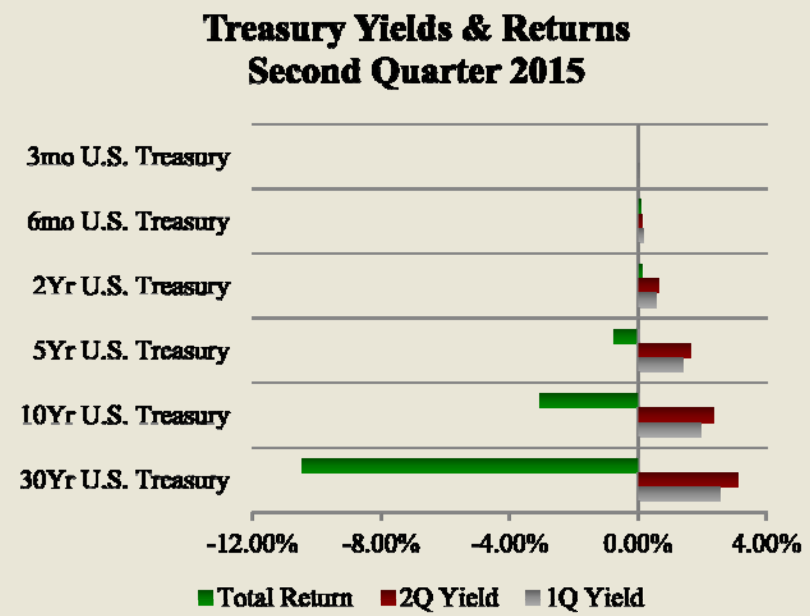
- Corporate operating earnings had a poor 1Q 2015 and are expected to be impacted by lower oil prices and weaker foreign currencies. Operating margins remain near all time highs.
- Forward and trailing P/E multiples have been expanding since 3Q 2011 and are now above historical averages.
- The U.S. dollar was relative flat versus the euro and yen in the quarter after appreciating considerably during the previous three quarters. If the dollar remains strong, multinationals could see their earnings pressured due to their international exposures.
- The price of oil has decline by fifty percent over the past year. This has significantly hurt energy companies but lower prices should help other sectors that use oil as an input such as the consumer industries.

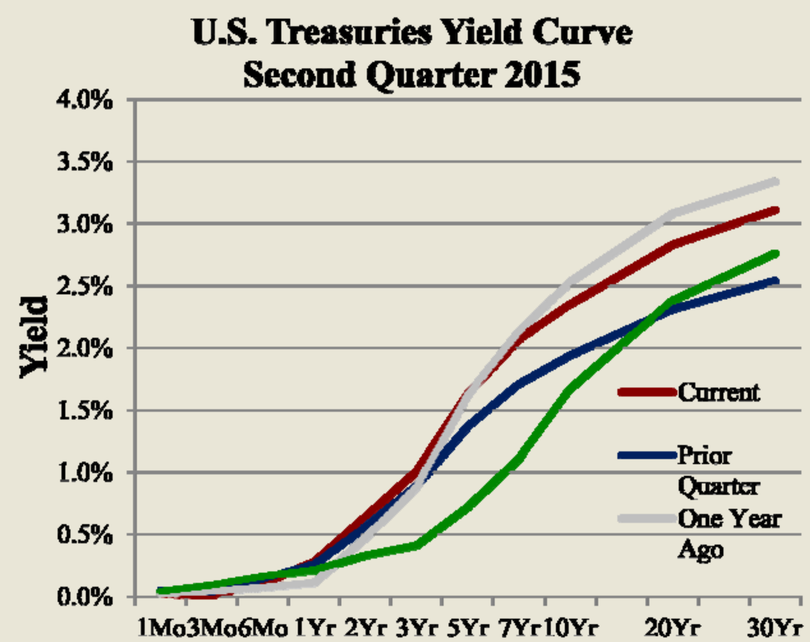
FED POLICY

- In June, the Federal Open Market Committee (FOMC) announced they will leave the federal funds rate at 0% to 0.25% percent. In their statement, the Fed noted the economy is expanding moderately and expressed they have seen progress towards their goals of maximum employment and inflation at 2%.
- The consensus view is the Fed will raise rates slightly before year end as economic data points towards a relatively stable and growing economy. However, with troubles in Greece, Puerto Rico and China some investors believe the rate hike may not occur until 2016.

FIXED INCOME

- The yields on longer-term Treasury securities increased quarter-over-quarter, while yields on very shorter-term Treasury securities were about flat causing the yield curve to steepen. On a historical basis, the yield curve is relatively steep due to the Fed holding down short term rates. A steep curve indicates market participants are not concerned about a recession over the next year.



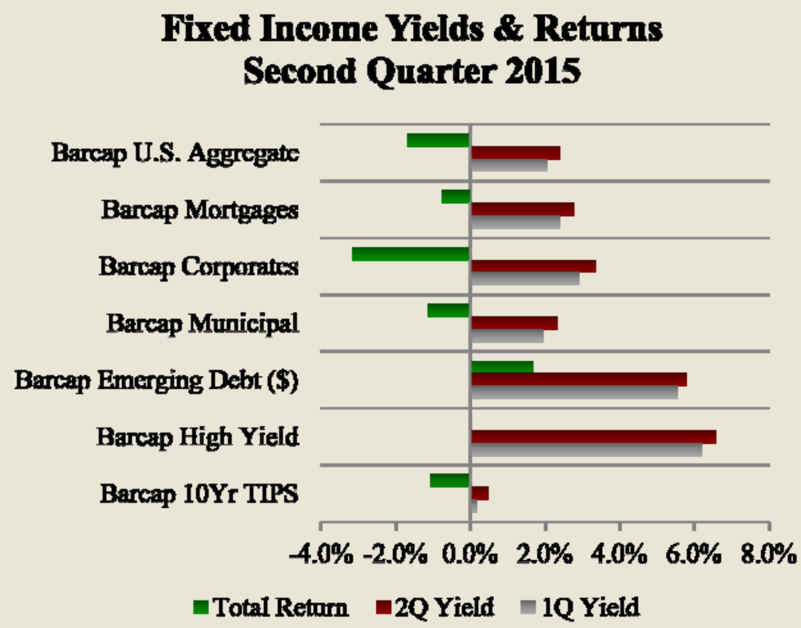


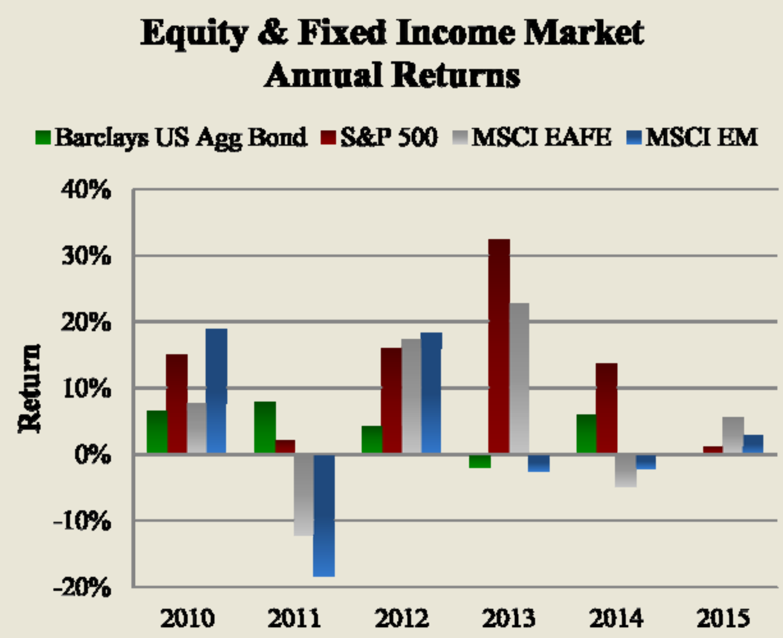
FIXED INCOME (continued)

- Yields in all fixed income sectors increased during the quarter. Fixed income yields remain low due to low interest rates and tight spreads. Returns were mostly negative across sectors, due to rising rates. The Barclays U.S. Aggregate was down almost two percent. Corporates were the worst performing sector while emerging market U.S. denominated debt had positive returns and was the best performing sector.
- Fixed income returns, going forward, are expected to be lower than historical averages as interest rates are starting at a very low level. Historically, future ten year fixed income annualized returns have been about the 10 year Treasury yield at the start of the period.

EQUITIES

- For the past two quarters, international and emerging market equity returns were stronger than U.S. large capitalization stocks, which is a reversal from last year. In the U.S., small capitalization stocks performed better than U.S. large capitalization stocks. Growth continued to strongly outperformed value stocks across market capitalizations during the quarter.
- After multiple very strong years for the equity markets, returns are expected to be lower as earnings growth remains sluggish and valuations are slightly higher than average.



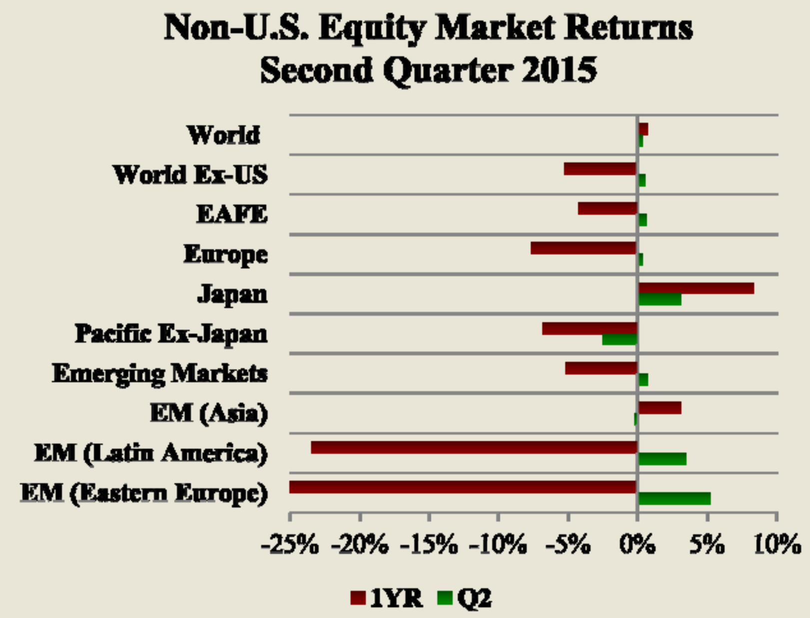


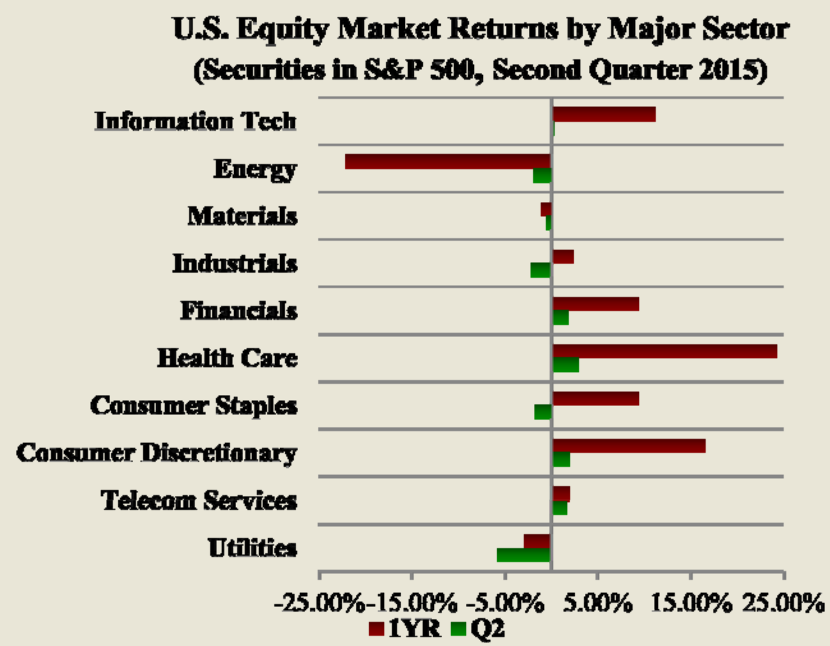
INTERNATIONAL EQUITIES (continued)

- Developed international stocks performed better than U.S. domestic equities. The MSCI EAFE index of international markets stocks increased 0.62% during the quarter. On a year-over-year basis, the EAFE is down 4.22%. Germany and Australia were the worst performing regions of the international developed markets during the quarter and Japan performed the best.
- During the quarter, emerging market stocks performed better than developed markets but emerging markets performed worse on a one year basis. The MSCI Emerging Markets Index increased 0.69% in the quarter and has a negative 5.12% return over the past year. Returns were stronger in Latin America and Eastern Europe than Asia as they recovered some of the large losses over the past year.
- Valuations are lower in developed international and emerging market equities; however, many regions are trying to recover from economic slowdowns or are going through structural changes.

DOMESTIC EQUITIES (continued)

- The Russell 1000 Index of large capitalization stocks posted a total return of 0.11% during the quarter. On a year-over-year basis, the Russell 1000 Index has advanced 7.37%.
- Small capitalization stocks, as represented by the Russell 2000 Index, posted a total return of 0.42% during the quarter. On a year-over-year basis, the index has increased 6.49%.
- Energy, utilities and industrials were the worst performing sectors in the quarter while health care and consumer discretionary were the best performers. Energy companies have underperformed significantly as the price of oil decreased by 50% over the past year. The market leadership has been narrow with strong performances from certain industries within health care and technology.





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