

Sherpa Investment View

2nd Quarter 2016

Presented by:

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Key Takeaways

- ▶ US equities remain expensive while the equities of emerging market countries and developed international countries have more attractive valuation levels albeit with commensurate levels of risk
- ▶ In the US, corporate profits must increase to justify inflated stock prices or else a correction is inevitable
- ▶ The fortunes of emerging market countries remain closely tied to energy prices
- ▶ A federal reserve rate hike is now likely off the table for 2016; central banks around the world are likely to continue to be accommodative while keeping an eye on contagion risk in the wake of BREXIT
- ▶ Oil prices rallied to over \$50 a barrel in the beginning of June before backing off on BREXIT news; we have a positive outlook for oil prices but heightened global inventories, high OPEC production levels and subdued Chinese oil demand remain near-term concerns for oil prices
- ▶ At this time the risk for global markets is contagion within the EU triggered by further departures by member countries; preventing this contagion will be a priority for member country leaders and a primary point of focus for us as we progress through 2016
- ▶ We continue to favor international stocks within equities and high yield municipal bonds within the fixed income markets due to the strong fundamentals of these asset classes

Second Quarter 2016

Commentary

US stocks finished the quarter ahead while international equities had mixed results. The big news this quarter was the UK's decision to exit the European Union; a decision that market participants were not expecting. In the immediate aftermath of the decision global investors fled to safety causing bond yields and stock prices to plummet across the world. Some \$2 trillion in asset values were erased and the pound fell to its lowest level against the dollar since 1985. As the quarter came to a close, however, markets across the world began to rebound.

For the quarter, US stocks gained 2.5% while international developed stocks lost approximately 1.5% and emerging market equities remained flat with a 0.7% increase. US bonds gained 2.2% while international bonds gained 3.4%. Commodities were up 13.48% for the quarter.

The US equity market continues to be defined by irrational bullishness driven by the Federal Reserve's accommodative stance. Corporate earnings in the US will need to catch up to the heightened valuations of stocks or a correction is inevitable. Across the pond, the EU is having its own woes. Apart from the UK's departure, the European banking sector is struggling due to the low interest rate environment in the region. Oil prices rallied to over \$50 a barrel in the beginning of June before backing off on BREXIT news; we have a positive outlook for oil prices but heightened global inventories, high OPEC production levels and subdued Chinese oil demand remain near-term concerns for oil prices.

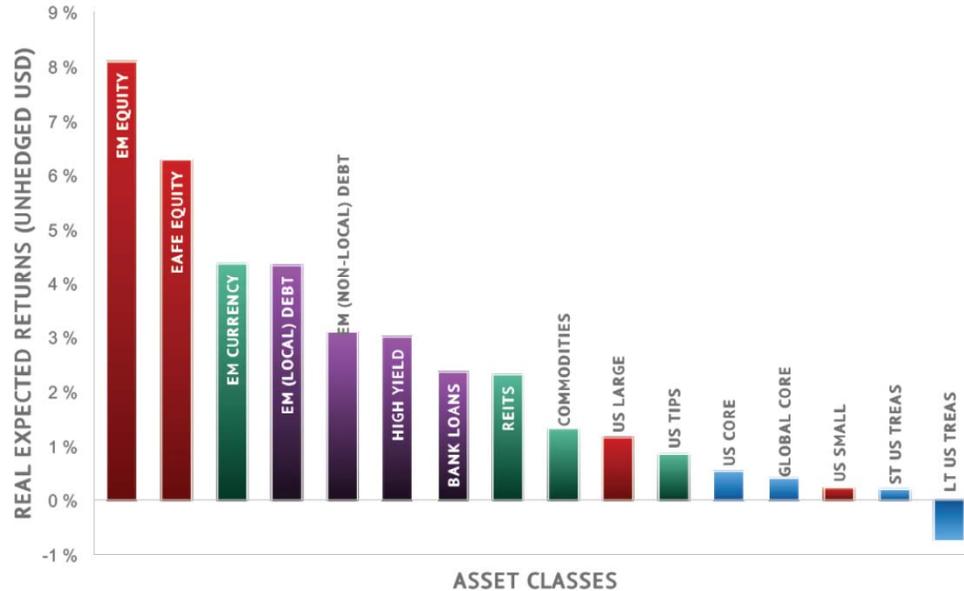
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Asset Classes

REAL 10-YEAR EXPECTED RISK & RETURN



Geometric expected returns for core asset classes show mainstream stocks and bonds suffering from low real yields and anemic growth. Opportunities for return do exist for investors willing to go beyond mainstream assets.



As of 06/30/2016. Source: These expected returns are calculated by Research Affiliates LLC using data provided by MSCI Inc., Bloomberg, and Barclays. Volatility is measured as standard deviation. These forecasts are forward-looking statements based upon the reasonable beliefs of RA and are not a guarantee of future performance. This content is not investment or tax advice or an offer, sale or any solicitation of any offer to buy any security, derivative or any other financial instrument. Any use of the above content is subject to and conditioned upon the user's agreement with all important disclosures, disclaimers and provisions found at www.researchaffiliates.com/Pages/Legal.aspx. In the event the above content is provided or modified by a third-party, Research Affiliates LLC fully disclaims any responsibility or liability for such content. ©2016 Research Affiliates, LLC. All rights reserved.

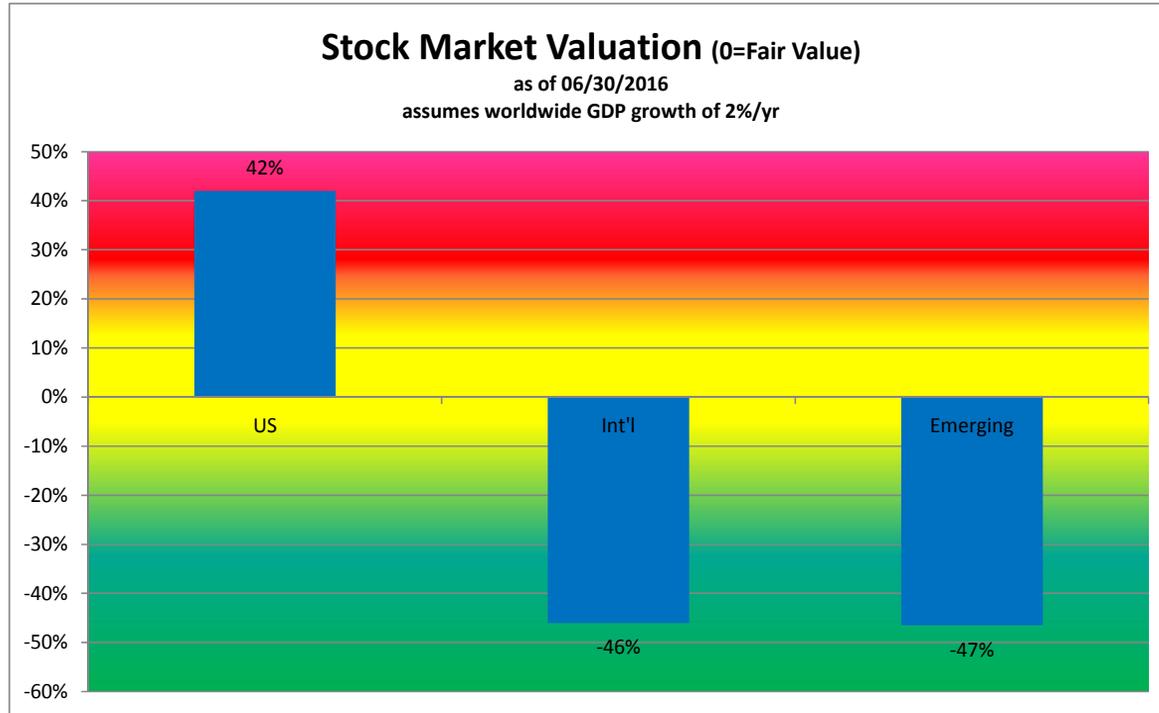
Stocks outside the US are expected to have the highest return, with emerging market equities leading the charge.

Asset Classes - Equities

| Index Name▲ | HISTORICAL REAL TOTAL RETURN | | | | | | FORECAST REAL RETURN | | |
|-----------------------|------------------------------|--------|-------------------|-------------------|--------------------|---|----------------------|---|-----------------|
| | YTD | 1-Year | 3-Year Annualized | 5-Year Annualized | 10-Year Annualized | 10-Year Relative Rank | 10-Year Annualized | 10-Year Relative Rank | Growth of \$10K |
| EQUITY | | | | | | | | | |
| MSCI EAFE | -6.0% | -10.8% | 1.4% | 0.8% | 0.3% |  | 6.3% |  | \$18,388 |
| MSCI EMERGING MARKETS | 4.6% | -12.8% | -2.3% | -4.8% | 2.1% |  | 8.1% |  | \$21,773 |
| RUSSELL 2000 | 0.2% | -7.8% | 6.0% | 7.0% | 4.5% |  | 0.2% |  | \$10,235 |
| S&P 500 | 1.9% | 2.9% | 10.6% | 10.8% | 5.7% |  | 1.2% |  | \$11,215 |

Source: Research Affiliates as of 6/30/2016

Global Equities - Outlook

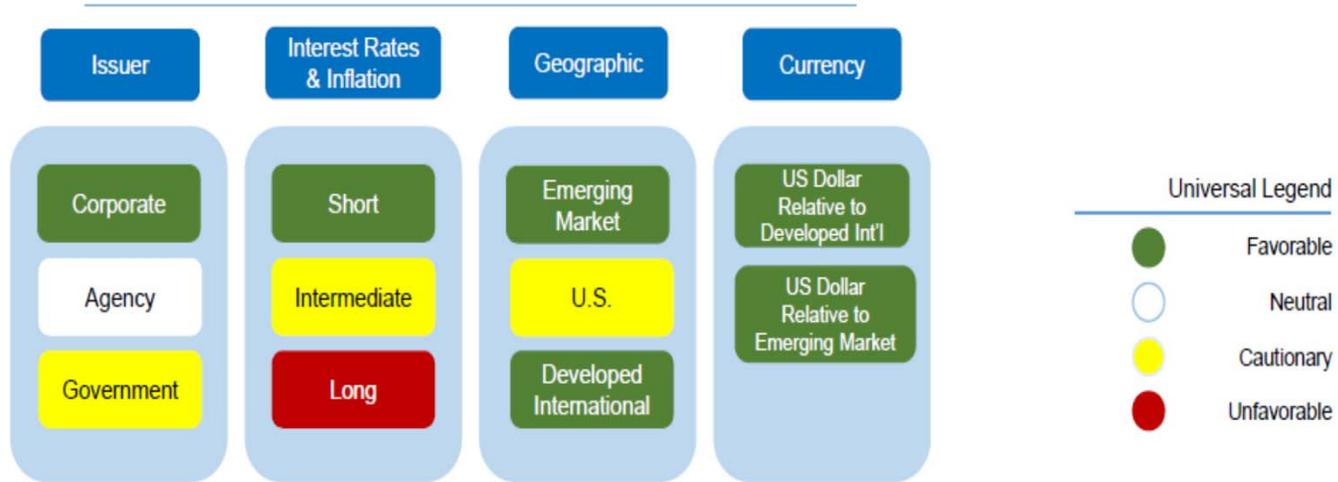


Created by Sherpa Investment Management and data obtained from <http://www.econ.yale.edu/~shiller/data.htm> & Research Affiliates

Based on the Cyclically Adjusted Price Earnings (CAPE) ratio The US equity market is approximately 42% overvalued while developed international countries' equities are 46% undervalued, and emerging market countries' equities are 47% undervalued. As a result, we have tilted out of US stocks as we view them as overpriced and unfavorable and tilted into the stock markets of developed international and emerging market countries.

Asset Classes – Fixed Income

Bond Risk Factors



Created by Sherpa Investment Management

Fixed Income - Outlook

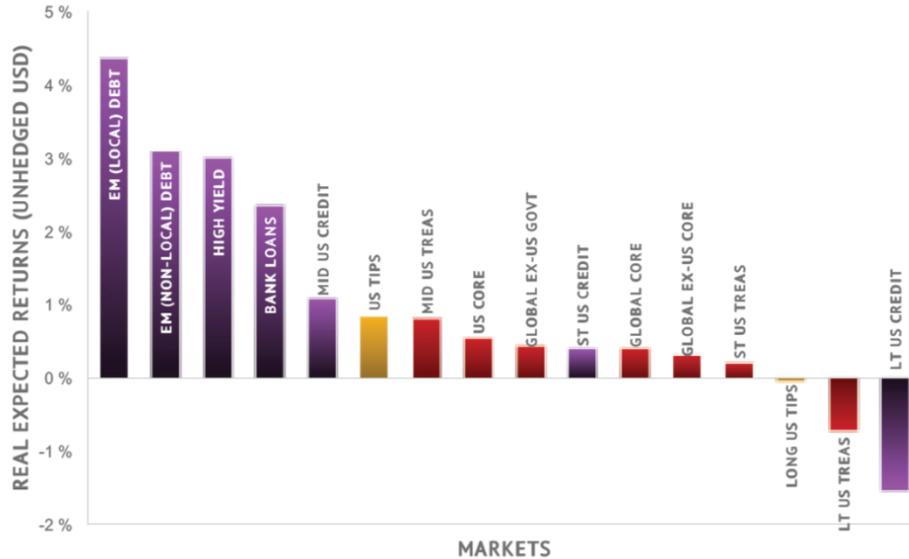
- High demand for government bonds around the world have pushed these bonds into overvalued territory warranting caution in this asset class
- When interest rates inevitably rise, longer-term bonds will be negatively impacted more than shorter-term bonds; as a result, we prefer shorter maturity bonds
- We favor international and emerging market bonds due to more favorable monetary policy overseas
- We forecast that the US dollar will continue to strengthen against most foreign currencies. This means that when interest is paid in foreign currencies these currencies will buy fewer dollars upon conversion. Monetary easing in most countries is causing capital to flow out of these countries, resulting in lower currency values. As a result, we have hedged (removed) our client's exposure to foreign currencies.

Fixed Income - Outlook

REAL 10-YEAR EXPECTED RISK & RETURN



Low yields indicate low future real returns for most government and credit assets. Inflation-linked securities could benefit if inflation rates are higher than market-priced break even inflation rates. Local emerging-markets debt benefits from higher credit ratings for these countries as well as higher yields.



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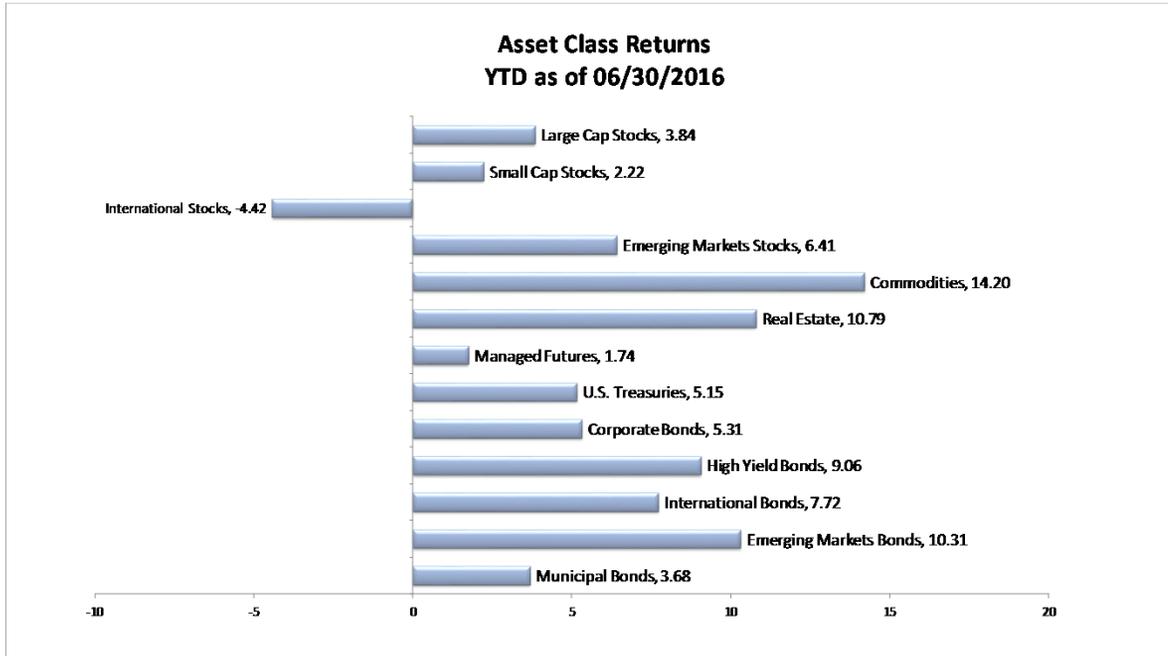
In the bond space, emerging market bonds denominated in local (emerging market) currencies are expected to have the highest return with commensurate risk.

Fixed Income - Outlook

| Index Name▲ | HISTORICAL REAL TOTAL RETURN | | | | | | FORECAST REAL RETURN | | |
|-----------------------------|------------------------------|--------|-------------------|-------------------|--------------------|-----------------------|----------------------|-----------------------|-----------------|
| | YTD | 1-Year | 3-Year Annualized | 5-Year Annualized | 10-Year Annualized | 10-Year Relative Rank | 10-Year Annualized | 10-Year Relative Rank | Growth of \$10K |
| CORE BONDS | | | | | | | | | |
| BARCLAYS GLOBAL AGGREGATE | 7.0% | 7.8% | 1.7% | 0.4% | 2.7% | | 0.4% | ■ | \$10,408 |
| BARCLAYS US AGGREGATE | 3.3% | 4.9% | 3.0% | 2.4% | 3.4% | ■ | 0.5% | ■ | \$10,550 |
| BARCLAYS US TREASURY 1-3 YR | -0.5% | 0.2% | -0.1% | -0.5% | 0.7% | ■ | 0.2% | ■ | \$10,204 |
| BARCLAYS US TREASURY LONG | 13.1% | 18.2% | 9.4% | 9.0% | 7.0% | ■ | -0.7% | ■ | \$9,297 |

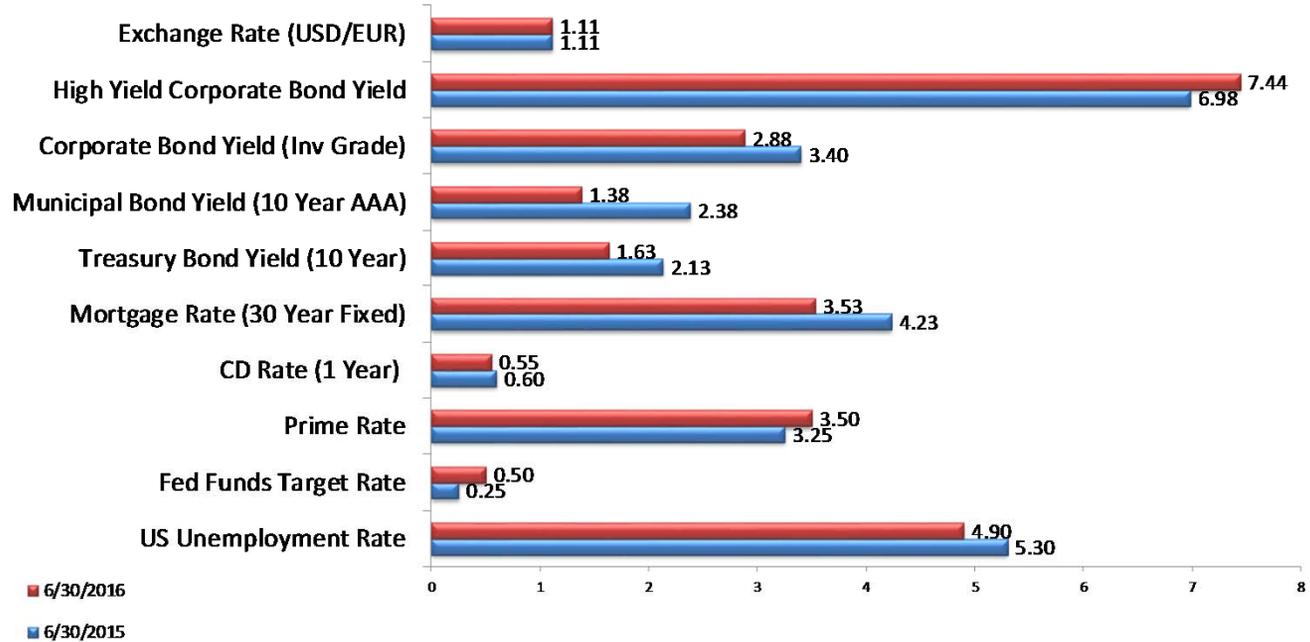
Source: Research Affiliates as of 6/30/2016

Market & Economic Review



Data obtained from Morningstar

Key U.S. Rates



Data obtained from Morningstar