Alternatives Update

1st Quarter 2017

"It was the best of times, it was the worst of times, it was the age of wisdom, it was the age of foolishness, it was the epoch of belief, it was the epoch of incredulity, it was the season of Light, it was the season of Darkness, it was the spring of hope, it was the winter of despair, we had everything before us, we had nothing before us, we were all going direct to Heaven, we were all going direct the other way – in short, the period was so far like the present period, that some of its noisiest authorities insisted on its being received, for good or for evil, in the superlative degree of comparison only."

The above quote from Dickens' masterpiece," A Tale of Two Cities", provides an eloquent summary for many aspects of today's society: the domestic economy, the global economy, the ever growing partisanship in Washington D.C., the accelerating prevarication by extremes in both political parties, the future of Great Britain, the integrity of the Euro bloc, the White House's relationship with the media, governmental regulation, healthcare, and even the relative performance within the capital markets. The closing words of "superlative degree of comparison only" seem especially apropos given that the capital markets have provided some superlative numbers to discuss.

In the 1st quarter, a quick rundown of traditional asset returns highlights the best of times for anyone long equities, especially emerging markets (see Figure 1). The 6.07% return in the 1st quarter of 2017 for the S&P 500 Index was a continuation of the excellent returns seen in 2016 and was in the top 30% of quarterly returns since 1988. The 11.45% return for emerging markets was in the top 25% of quarterly returns since 1999. As expected, Alternative Investment ("Alternatives") returns were more subdued as compared to traditional long only risk assets given that alternative strategies generally have lower volatility. For the quarter, 7 of the 11 alternative categories had positive returns. Given the strength of global equity markets, it should come as no surprise that hedged equity was the best performing category and short biased the worst (see Figure 2). As in the recent past, exposure to equity beta seems to have been a major driver of returns. As was the case for most of 2016, returns mostly aligned with the rank order correlation to the S&P 500 Index (see Figure 3). Real assets (commodities, real estate, gold), which had all done very well in 2016 began to see separation as gold prices accelerated and general commodities went negative for the quarter (see Figure 4).

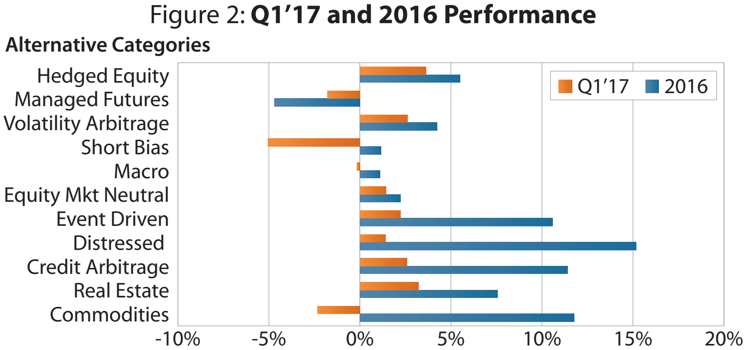
Managed futures, commodities, and macro strategies have historically shown low correlations to stocks and bonds, thus they serve as potentially strong portfolio diversifiers. Strategies such as credit, event driven, hedged equity, et al., which have higher correlations with equities and bonds, provide attractive risk/return profiles through lower volatility. These characteristics may allow investors to broaden their investment choices and create more efficient portfolios.

Figure 1: **Asset Class Returns**

	1Q17
S&P 500	6.07%
MSCI EAFE	7.25%
MSCI Emerging	11.45%
U.S. Treasury	1.42%
Real Estate	3.22%
Commodities	-2.33%
Bloomberg Barclays High Yield	2.44%
Bloomberg Barclays Aggregate	0.82%

Source: Bloomberg, 3/31/17. Past performance is no guarantee of future results. An investor cannot invest directly in an index.

Figure 2: **Q1'17 and 2016 Performance**



Source: Bloomberg, 3/31/17. Past performance is no guarantee of future results. An investor cannot invest directly in an index.

Figure 3: **Correlations (2-Year) & Returns**

	S&P 500	1Q17
Hedged Equity	0.86	3.62%
Event Driven	0.77	2.23%
Real Estate	0.70	3.22%
Distressed	0.60	1.42%
Credit Arbitrage	0.58	2.60%
Equity Market Neutral	0.54	1.44%
Volatility Arbitrage	0.48	2.61%
Macro	0.15	-0.15%
Commodities	0.12	-2.33%
Managed Futures	(0.10)	-1.79%
Short Bias	(0.69)	-5.05%

Source: Bloomberg, 3/31/17. Past performance is no guarantee of future results. An investor cannot invest directly in an index.

Figure 4: **Real Assets**

	1Q17	2016
Real Estate	3.22%	7.56%
Commodities	-2.33%	11.77%
Gold	8.43%	8.56%

Source: Bloomberg, 3/31/17. Past performance is no guarantee of future results. An investor cannot invest directly in an index.

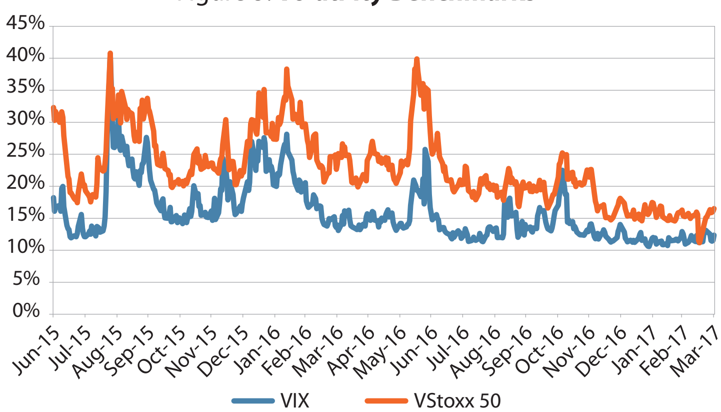
After the U.S. presidential election results in 2016, the markets rallied in response to two of the three branches likely to be pro-business and controlling the open appointee to the remaining branch of government (U.S. Supreme Court). Once inaugurated, President Trump wasted no time in seeking to implement his promised polices of immigration scrutiny and repeal of the Affordable Healthcare Act, informally known as "Obamacare". The speed of action seemed to be interpreted by the markets as significantly raising the odds that significant regulatory reform/reduction and tax reform would not only be forthcoming, but would pass quickly. Throw in positive signs of global growth, especially China, and you have the recipe for a rally in global equities. In January, U.S. equity volatility (as measured by the VIX Index) sank to a low (10.58) that had not been seen in over two years (see Figure 5). Failure to secure a vote on the proposed American Health Care Act of 2017 (H.R. 1628) temporarily jarred the markets and volatility rose slightly towards the end of the quarter but ended at very moderate levels. Even more remarkable, the average daily VIX level in the first quarter (11.69) was the second lowest reading since the creation of the VIX Index. The lowest reading was the 1st quarter of 2006 (11.03) and 3rd lowest reading was in the 1st quarter of 1995 (see Figure 6).

Credit spreads continued to ratchet downward and are near post financial crisis lows but have not yet approached lows achieved in the mid-1990s or mid 2000s prior to the financial crisis (see Figure 7 & 8).

Sentiment (the overall attitude of investors and their willingness to risk capital) in the 1st quarter was overall upbeat in tone. The ratio of New Highs to New Lows for the NYSE and for the NASDAQ moved slightly higher and continues to be in decidedly positive territory (see Figure 9).

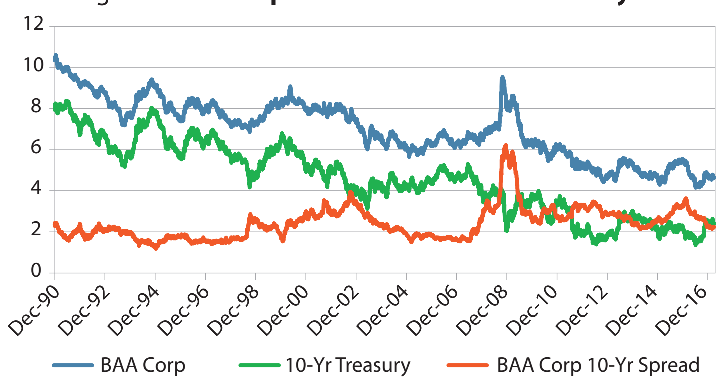
The Federal Open Market Committee (FOMC) raised rates 25 basis points (bps) and signaled that two more rate hikes are likely in 2017, not three. If there was any question as to the dovish leanings of the FOMC, it was once again put on display by the continued revision of milestones. Two central pillars of normalizing both rates and the Federal Reserve's (Fed) balance sheet have been acceptable unemployment rates and the achievement of a 2% inflation rate. 5% unemployment was breached in 2015 yet no action was taken. Now that a 2%+ Consumer Price Index (CPI) has been reached, talk of a revision in the target inflation rate has begun. Chair of the Federal Reserve, Dr. Janet Yellen, did not attempt to obfuscate the Fed's intentions.

Figure 5: **Volatility Benchmarks**



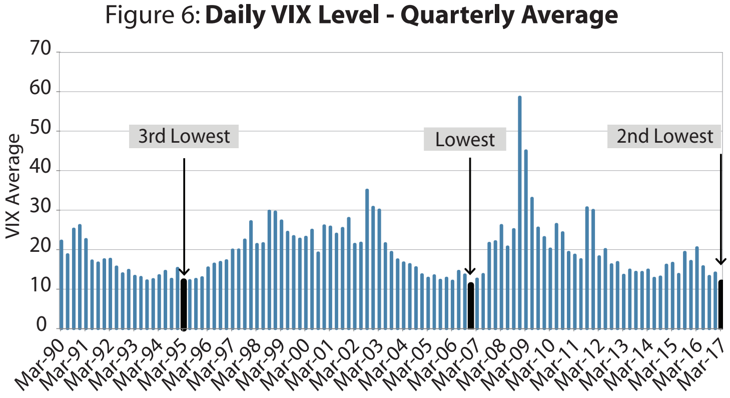
Source: Bloomberg, 3/31/17.

Figure 7: **Credit Spread vs. 10-Year U.S. Treasury**



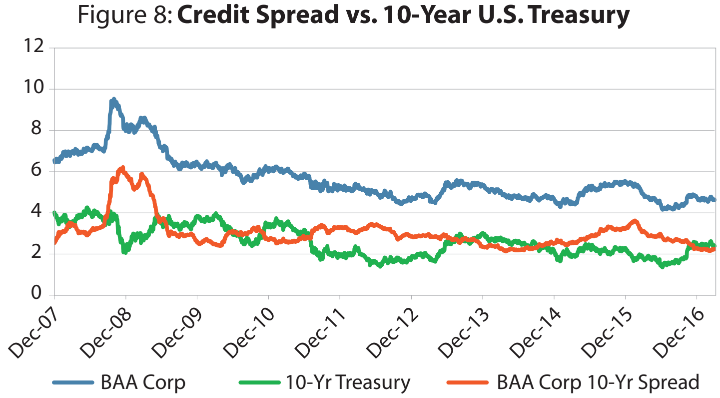
Source: Bloomberg, 3/31/17.

Figure 6: **Daily VIX Level - Quarterly Average**



Source: Bloomberg, 3/31/17.

Figure 8: **Credit Spread vs. 10-Year U.S. Treasury**



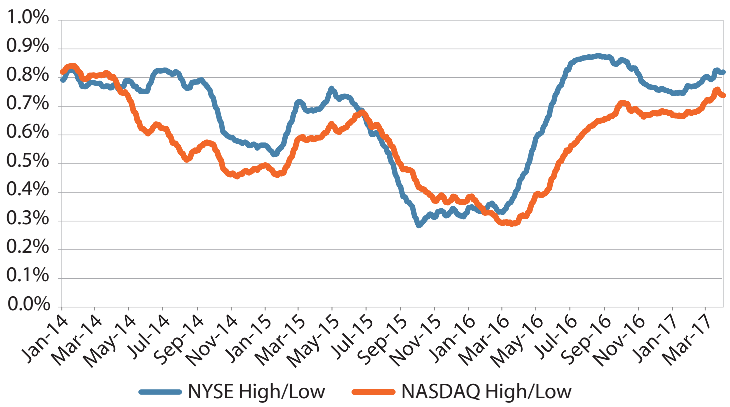
Source: Bloomberg, 3/31/17.

She provided a clear willingness to tolerate inflation beyond 2%, balance sheet shrinkage was far off and would be passive not active and the Fed's policy would be accommodative for some time. Risk asset holders had to like what they heard as some might interpret that as "the Fed Put" is alive and well, so "keep buying". It might also help explain the extraordinarily low volatility in the capital markets and the tremendous willingness of participants to continually "buy the dip."

The long end of the Treasury Yield Curve temporarily breached 3.20% before drifting lower in yield to 3.01%, leaving yields down 5bps for the quarter (see Figure 10). With the hike in the Fed Funds rate and a slight tick down in longer maturities, the yield curve flattened (see Figure 11). Flattening this early in a rate cycle is a bit unusual as yield curves are generally steepening in anticipation of growth and the long end tends to be more responsive than the short end, which is controlled by the FOMC. It is not clear whether the fixed income market is questioning growth prospects, Central Bank activity is suppressing the long end or market participants are clinging to long duration treasuries as a hedge on the political uncertainties in the U.S. and abroad.

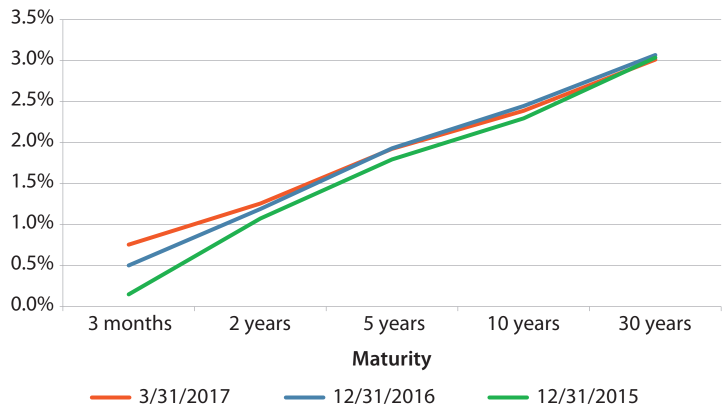
It was a strong 1st quarter for both "Risk On" (+4.32%) and "Risk Off" assets (+4.06%), (see Figure 12). It was not a rotation of assets or modification of risk preferences, but more a buy anything and everything trade mentality. Quarterly performance of every "Risk Off" asset class nearly matched or exceeded performance for all of 2016. Every category for "Risk On" assets was solidly positive with none less than 2% for the quarter. We continue to emphasize that Alternatives have historically provided significant diversification benefits when paired with a portfolio of traditional assets, in addition to both competitive absolute returns and attractive risk-adjusted returns.

Figure 9: **New Highs/New Lows** *(90-Day Rolling Average)*



Source: Bloomberg, 3/31/17.

Figure 11: **U.S. Treasury Yield Curve**

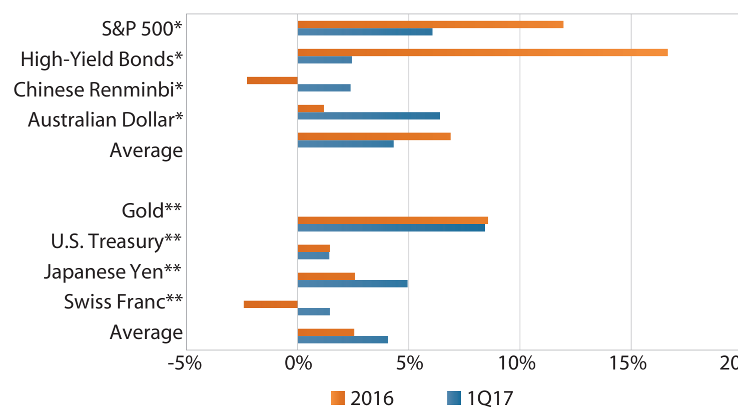


Source: Bloomberg, 3/31/17.

Figure 10: **U.S. 30-Yr. Treasury Yield**

Source: Bloomberg, 3/31/17.

Figure 12: **Risk Off vs. Risk On Asset Returns**



Source: Bloomberg, 3/31/17.
** Considered to be "Risk On" asset class. ** Considered to be "Risk Off" asset class.*

All charts shown herein are for illustrative purposes only and not indicative of any investment. The performance illustrations exclude the effects of taxes and brokerage commissions or other expenses incurred when investing. Past performance is not indicative of future results and there can be no assurance past trends will continue in the future. An investor cannot invest directly in an index.

Alternative investments may employ complex strategies, have unique investment and risk characteristics that may not be suitable for all investors.

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Definitions

Correlation: Pearson Product Moment Correlation is a linear statistical measure that quantifies the extent to which two or more data series fluctuate together. Values run from -1.0 to +1.0.

Bloomberg Barclays US Agg: The Bloomberg Barclays US Aggregate Bond Index is a broad-based benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market.

Hedged Equity: Hedge Fund Research HFRI Equity Hedge Total Index. Investment Managers who maintain positions both long (positions that are owned) and short (positions that are owed) in primarily equity and equity derivative securities. Hedged Equity managers would typically maintain at least 50%, and may in some cases be substantially entirely invested in equities, both long and short.

Managed Futures: BarclayHedge US Managed Futures Industry Top 50 (BTop 50) Index. The Index seeks to replicate the overall composition of the managed futures industry with regard to trading style and overall market exposure.

Volatility Arbitrage: Hedge Fund Research HFRI Relative Value Volatility Index. Volatility strategies trade volatility as an asset class, employing arbitrage, directional, market neutral or a mix of types of strategies, and include exposures which can be long, short, neutral or variable to the direction of implied volatility, and can include both listed and unlisted instruments. Directional volatility strategies maintain exposure to the direction of implied volatility of a particular asset or, more generally, to the trend of implied volatility in broader asset classes. Arbitrage strategies employ an investment process designed to isolate opportunities between the price of multiple options or instruments. Volatility arbitrage positions typically maintain characteristic sensitivities to levels of implied and realized volatility, levels of interest rates and the valuation of the issuer's equity, among other more general market and idiosyncratic sensitivities.

Short Bias: Hedge Fund Research HFRI EH Short Bias Index. Short-Biased strategies employ analytical techniques in which the investment thesis is predicated on assessment of the valuation characteristics on the underlying companies with the goal of identifying overvalued companies.

Macro: Hedge Fund Research HFRI Macro Total Index. Investment Managers which trade a broad range of strategies in which the investment process is predicated on movements in underlying economic variables and the impact these have on equity, fixed-income, hard currency and commodity markets.

Equity Market Neutral: Hedge Fund Research HFRI EH Equity Market Neutral Index. Equity Market Neutral strategies employ sophisticated quantitative techniques of analyzing price data to ascertain information about future price movement and relationships between securities, select securities for purchase and sale. Equity Market Neutral Strategies typically maintain characteristic net equity market exposure no greater than 10% long or short.

Event Driven: Hedge Fund Research HFRI Event-Driven Total Index. Investment Managers who maintain positions in companies currently or prospectively involved in corporate transactions of a wide variety including but not limited to mergers, restructurings, financial distress, tender offers, shareholder buybacks, debt exchanges, security issuance or other capital structure adjustments.

Distressed: Hedge Fund Research HFRI ED Distressed/Restructuring Total Index. Distressed/Restructuring strategies employ an investment process focused on corporate fixed-income instruments, primarily on corporate credit instruments of companies trading at significant discounts to their value at issuance or obliged (par value) at maturity as a result of either formal bankruptcy proceeding or financial market perception of near term proceedings.

Credit Arbitrage: Hedge Fund Research HFRI ED Credit Arbitrage Index. Credit Arbitrage strategies employ an investment process designed to isolate attractive opportunities in corporate fixed-income securities; these include both senior and subordinated claims as well as bank debt and other outstanding obligations, structuring positions with little of no broad credit market exposure. These may also contain a limited exposure to government, sovereign, equity, convertible or other obligations but the focus of the strategy is primarily on fixed corporate obligations and other securities are held as component of positions within these structures.

Real Estate: Dow Jones US Real Estate Total Return Index. The DJ US Real Estate Index represents REITs & other companies that invest directly or indirectly in real estate through development, management or ownership, including property agencies.

Commodities: Bloomberg Commodity Total Return Index. The Bloomberg Commodity Total Return index is composed of futures contracts and reflects the returns on a fully collateralized investment in the Bloomberg Commodity Index. This combines the returns of the Bloomberg Commodity Index with the returns on cash collateral invested in 13 week (3 Month) U.S. Treasury Bills.

Investment Grade CDX Spread: Markit CDX North America Investment Grade Index. The Markit CDX North America Investment Grade Index is composed of 125 equally weighted credit default swaps on investment grade entities. A credit default swap is an agreement in which the buyer makes payments to the swap seller until maturity of the contract. In return the seller agrees that, in the event that the debt issuer has a credit event (missed payment or a default) the seller will pay the security's premium as well as interest.

Credit Spread: The difference in yield between two fixed-income instruments with differing credit profiles.

VIX: Chicago Board Options Exchange SPX Volatility Index. The Chicago Board Options Exchange Volatility Index reflects a market estimate of future volatility, based on the weighted average of the implied volatilities for a wide range of strike prices.

VStoxx 50: Euro Stoxx 50 Volatility Index VSTOXX. VSTOXX Index is based on a methodology jointly developed by Deutsche Borse and Goldman Sachs to measure volatility in the Eurozone. VSTOXX is based on the EURO STOXX 50 Index options traded on Eurex. It measures implied volatility on options with a rolling 30 day expiry.

BAA Corp: Moody's Bond Indices Corporate BAA. Moody's Long-Term Corporate Bond Yield Averages are derived from pricing data on a regularly replenished population of corporate bonds in the U.S. market, each with current outstandings over $100 million. The bonds have maturities as close as possible to 30 years; they are dropped from the list if their remaining life falls below 20 years, if they are susceptible to redemption, or if their ratings change. All yields are yield-to- maturity calculated on a semi-annual basis.

10-Yr Treasury: Yield of U.S. Treasury securities maturing in approximately 10 years.

S&P 500 Implied Volatility: 30 day implied volatility of S&P 500 options at 100.0% moneyness from Bloomberg volatility model. Moneyness is the relationship between the strike price of an option and the current price of its underlying security. 100% moneyness means the strike price and underlying security price are equal.

S&P 500 Realized Volatility: A measure of the risk of price moves for a security calculated from the standard deviation of day to day logarithmic historical price changes. The 30-day price volatility equals the annualized standard deviation of the relative price change for the 30 most recent trading days closing price, expressed as a percentage.

NYSE High/Low: Bloomberg New Highs and New Lows Sentiment Index NYSE. The New Highs and New Lows indices represent the 52-week highs/lows for the securities on a specific exchange (NYSE) on a given day. New Highs divided by the sum of the new highs plus the new lows.

NASDAQ High/Low: Bloomberg New Highs and New Lows Sentiment Index NASDAQ Composite. The New Highs and New Lows indices represent the 52-week highs/lows for the securities on a specific exchange (NASDAQ Composite) on a given day. New Highs divided by the sum of the new highs plus the new lows.0

U.S. 30-Yr Treasury Yield: Yield of U.S. Treasury securities maturing in approximately 30 years.

S&P 500: An unmanaged index of 500 stocks used to measure large-cap U.S. stock market performance.

Bloomberg Barclays High Yield Bonds: A component of the Bloomberg Barclays US Corp High Yield Index that is designed to track a more liquid component of the USD-denominated, high yield, fixed-rate corporate bond market. The US High Yield VLI uses the same eligibility criteria as the US Corp High Yield Index, but includes only the three largest bonds from each issuer that have a min amount outstanding of USD500mn and less than five years from issue date.

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Chinese Renminbi: The S&P Chinese Renminbi Index is designed as a tradable index that replicates the performance of the Chinese Renminbi versus the U.S. Dollar.

Australian Dollar: The return from selling the short currency (USD) to buy the long currency (AUD) and earning interest. The return is calculated by adding the spot return to the interest earned from the long currency position. It is designed to measure the performance of the Australian dollar vs. the U.S. dollar.

Gold: The return of the gold spot price as quoted as U.S. dollars per Troy Ounce.

U.S. Treasury: The ICE U.S. Treasury 20+ Years Bond Index is part of a series of indices intended to assess U.S. Treasury issued debt. Only U.S. dollar denominated, fixed-rate securities with minimum term to maturity greater than twenty years are included.

Japanese Yen: The return from selling the short currency (USD) to buy the long currency (JPY) and earning interest. The return is calculated by adding the spot return to the interest earned from the long currency position. It is designed to measure the performance of the Japanese yen vs. the U.S. dollar.

Swiss Franc: The return from selling the short currency (USD) to buy the long currency (CHF) and earning interest. The return is calculated by adding the spot return to the interest earned from the long currency position. It is designed to measure the performance of the Swiss franc vs. the U.S. dollar.

MSCI EAFE: The MSCI EAFE Index covers Developed Market countries in Europe, Australasia, Israel, and the Far East. The index is a free-float weighted equity index.

MSCI Emerging: The MSCI Emerging Markets Index captures large and mid cap representation across Emerging Markets (EM) countries. The index is a free-float weighted equity index and captures 85% of the free float-adjusted market capitalization in each country.