JJ BURNS

“Got nowhere to run, baby, nowhere to hide” Martha and the Vandellas

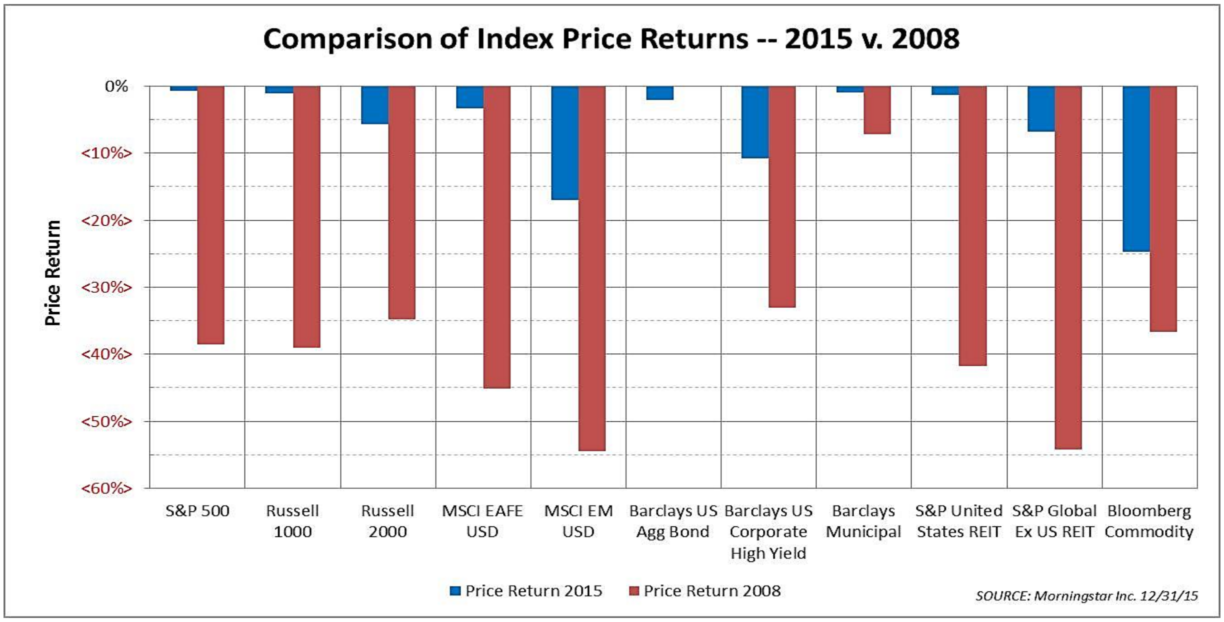
Martha and the Vandellas, the classic Motown group, had two big hits that perfectly capture investor sentiment: “Dancing in the Streets” is suitable for what we might term ‘better years’; “Nowhere to Run” was more appropriate for 2015 returns. What we expected for the year didn’t pan out, and, as usually happens with market uncertainty, investors turned pessimistic. As Martha sang, there was nowhere to hide. Here are a couple of ways to look at the markets:

Index	2015	2014	2013
Fixed Income			
Barclays US Aggregate Bond TR	0.55%	5.97%	<2.02%>
Barclays High Yield Corporate TR	<4.47%>	2.45%	7.44%
Citi WGBI [Global Bonds]	<3.57%>	<0.48%>	<4.00%>
U.S. Equities			
Russell 1000 TR [Large-cap Stocks]	0.92%	13.24%	33.11%
Russell 2500 TR [SMID-cap Stocks]	<2.90%>	7.07%	36.80%
S&P 500 TR	1.38%	13.69%	32.39%
International Equities			
MSCI ACWI Ex USA NR [All Stocks]	<5.66%>	<3.87%>	15.29%
MSCI EAFE NR [Developed Markets]	<0.81%>	<4.90%>	22.78%
MSCI EM NR [Emerging Markets]	<14.92%>	<2.19%>	<2.60%>
Real Assets			
Morningstar US Real Asset Index TR	<4.22%>	3.35%	0.11%
Bloomberg Commodity TR	<24.66%>	<17.01%>	<9.52%>
S&P Global Ex US REIT TR	2.54%	30.26%	2.40%
S&P United States REIT TR USD	<2.77%>	11.88%	3.31%

Source: Morningstar, Inc. All data are USD total returns with dividends and interest.

This table sums up 2015 to: commodities down; real assets off, real estate (REITs) off, international stocks down, and a big reversal in high-yield and global government bonds.

This data doesn’t quite tell the whole picture, however. When Martha sang about nowhere to run, it reminded us to be thankful for dividends and interest payments, as price returns on major indices were disappointing last year. To find another market year when all prices were negative, we went back to 2008. Here’s how the comparative data looked:



Since the crisis, no year had fewer positive price returns than 2015. Since 2008, only the years 2011 and 2013 had more indexes with negative prices than positive; neither had more negative returns than 2015. So, does this bad news mean we're in for a better year in 2016?

"You've got your troubles / I've got mine" The Fortunes

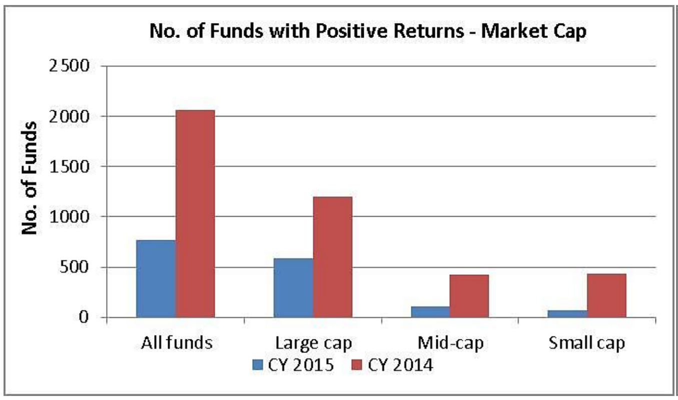
We think we are, though it won't be a spectacular year. Here's a look at what's happened to major markets (based on cumulative returns) since the S&P 500 price index reached its post-crash high on September 7, 2012:

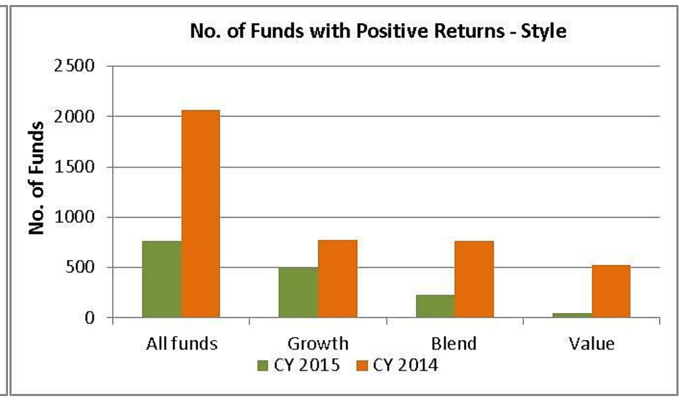
Index	Recovery to YE 2015	Recovery to 2014 High	2014 Dip to YE 2015	Current Market
U.S. Stocks				
S&P 500 TR	53.10%	46.70%	4.37%	BULL
Russell 2500 TR	46.31%	47.33%	<0.69%>	FLAT
International Stocks				
MSCI EAFE NR	25.94%	35.54%	<7.08%>	DECLINE
MSCI EM NR	<9.64%>	16.81%	<22.64%>	BEAR
U.S. Bonds				
Barclays US Agg Bond TR	5.12%	2.23%	2.83%	BULL
Barclays Municipal TR	11.27%	5.77%	5.21%	BULL
Barclays US HY 2% Issuer Cap TR	9.71%	17.31%	<6.48%>	DECLINE
Real Assets				
Bloomberg Commodity TR	<46.09%>	<17.38%>	<34.76%>	BEAR
S&P United States REIT TR	35.73%	17.44%	15.57%	BULL
S&P Global Ex US REIT TR	21.05%	23.32%	<1.84%>	FLAT

SOURCE: JJ Burns and Morningstar, Inc. Data through 12/31/15. Index returns in USD and include dividends and interest.

As the data show, aside from commodities and broad emerging markets, most major indexes are positive. Most of the return was earned prior to the brief pullback in the fall of 2014. Since then, markets are decidedly lackluster, with two—broad emerging markets and commodities—entering bear territory and two others approaching corrections. This leaves only the U.S. markets in positive territory, and those returns were hard-earned with a lot of volatility.

Here's another way to look at how the U.S. market has turned. These two graphs demonstrate a dramatic decline in performance for domestic stock-fund managers, according to Morningstar data. It was clearly a more difficult environment in 2015 versus 2014, as far fewer managers had positive returns this past year:





SOURCE: JJ Burns and Morningstar, Inc. Data through 12/31/15. Survey is for the oldest class of funds in each U.S. category listed.

Presently, markets are favoring large-cap-growth stocks and managers. This is what a late-stage bull market looks like, but given the unusual circumstances of this recovery, we don't believe that we can make any firm predictions about the future strength of this bull.

"I went down to the crossroads / Tried to flag a ride" Cream

What are the issues the markets are seeking clarity for? Here are three major ones we see:

- **China** – the Chinese growth miracle has played out, and what was long suspect has been revealed to be fact: a command economy (one based on central planning) doesn't have the solutions to smoothing the capitalist boom-bust cycle. Developed economies haven't solved them over the centuries, and the Chinese haven't in their 25 years of economic change. Years of building roads to nowhere and empty megalopolises, buying huge quantities of raw materials, expanding manufacturing, indiscriminate lending, currency pegging and stock-market manipulation have left the government with no firm policy. As these facts became evident last year and China and other nations that rely heavily on China for growth stumbled, the story unraveled.

This doesn't mean China's growth is fully played out; it does mean that investors and the Chinese government need to rethink what the best course of action is, and how to profit from these changes. One certainty is that one year is not enough time for these issues to be resolved.

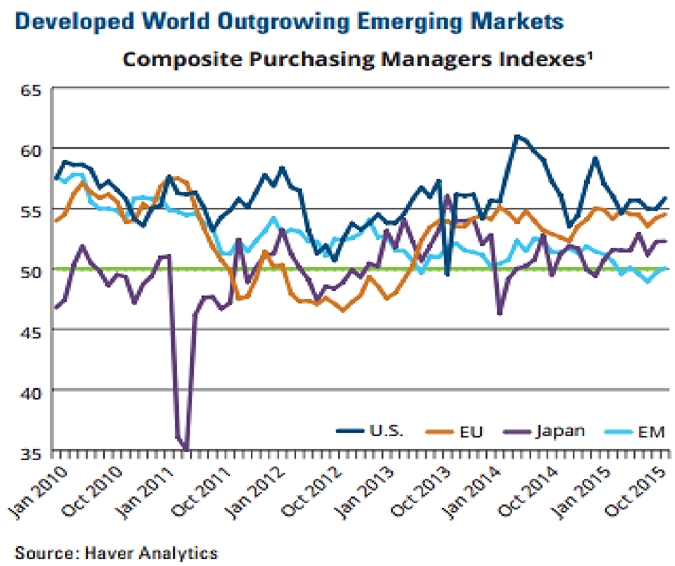
- **Oil** – this issue extends to other commodities, too, but what is clear is that the commodities growth super-cycle is in reversal. U.S. energy-production gains of the past few years have been denuded by the stubbornness of OPEC, particularly the House of Saud. Expectations last year were that oil's price collapse in 2014 would begin a slow ascent to normalization in the $60-$70 per barrel range by sometime in 2016. That cycle hasn't yet begun despite declines in energy-production investment such as new rigs. Worries have turned to geopolitical issues (e.g. the Middle East conflagrations); the fears of deflation from lower oil prices; and the conflict of profit extractors (e.g. the U.S.) versus fiscal extractors (e.g. Saudi Arabia, Russia, Brazil), or really any state that drills oil for its government coffers. This standoff is a difficult game to manage, and the normal benefits of low oil prices—global expansion—have not yet been felt. Of further concern is the deterioration in a number of markets that are related to energy, including U.S. MLPs and high-yield bonds that finance the energy sector. What is also surprising is the resilience of low prices despite the Middle East's armed conflicts. Investors would normally expect this to push prices higher, not lower. Waiting is the only policy for the moment.

- **The Fed** – the U.S. central bank is really a proxy for rising rates. Normally, rising rates are a good thing, as it implies a higher level of economic growth and some inflation. Because the Fed has delayed the liftoff for so long, they've put themselves in a difficult position with respect to the size and duration of the hike cycle. U.S. economic data don't seem to reflect the need to hike, and the strong U.S. dollar is now a concern as well. In fact, the dollar may be a bigger factor than investors expect, despite the seeming pause in the dollar's rise. Certainly a slow rate-hike cycle and a pause or retrenchment in the dollar will be a stimulus for U.S. and foreign growth.

"'cause I can't give the best / Unless I got room to move" John Mayall and the Bluesbreakers

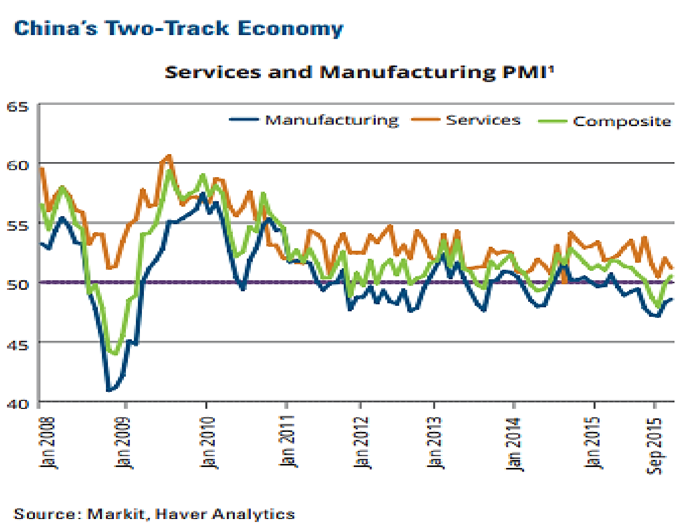
These are major issues that will take time to play out. We also see some bright spots to focus on, and we think investors will benefit by considering those:

- **Growth** — first and most important is growth. As we have noted, different countries and regions are in different stages of expansion and contraction. The U.S., despite indications of interest-rate hikes, is still in expansion. A review of some broad regional PMI (Purchasing Managers Index) data indicate that the growth picture isn't as gloomy as believed:

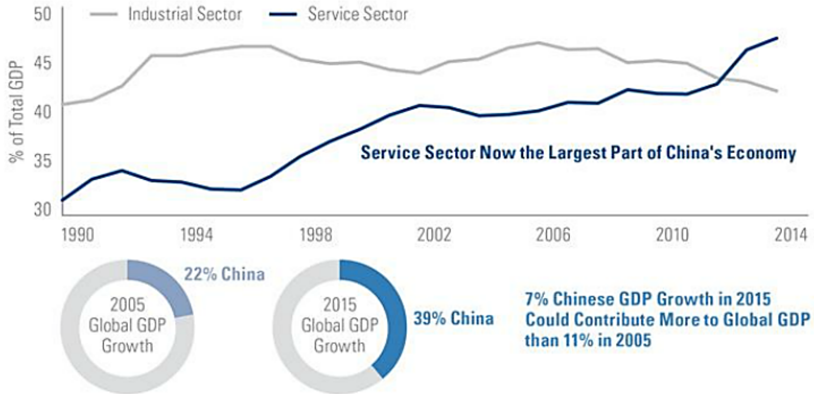


As the title indicates, developed markets are in better shape than emerging markets, but all of these indices are at or above a reading of 50, which suggests expansion. With still-accommodative monetary and fiscal policies in place, there are some tailwinds for growth. It's important to note that 'emerging markets' is a catch-all term for 23 different countries; broad generalizations may lead to overlooked opportunities.

- **China** — yes, we noted above that China has major issues. This does not mean, however, that China is a lost cause. In fact, there are some encouraging signs that more balance is helping the growth story there, and it's focused on the Chinese consumer and service sectors:



This graph implies that China is still growing despite the fact that its manufacturing sector is probably in recession. These are still positive data, and China observers that we follow indicate that a lot is happening there that is not easily reflected in data. Also, a smaller increase on a large number (China's GDP growth as a share of the world's GDP) still translates into significant global growth. [See the next graph.]



Top Chart Source: Bloomberg, National Bureau of Statistics of China, and GSAM. Bottom Chart Source: International Monetary Fund World Economic Outlook Database and GSAM.

Regardless of recent slowdown fears, China is increasingly the largest contributor to global real GDP growth.

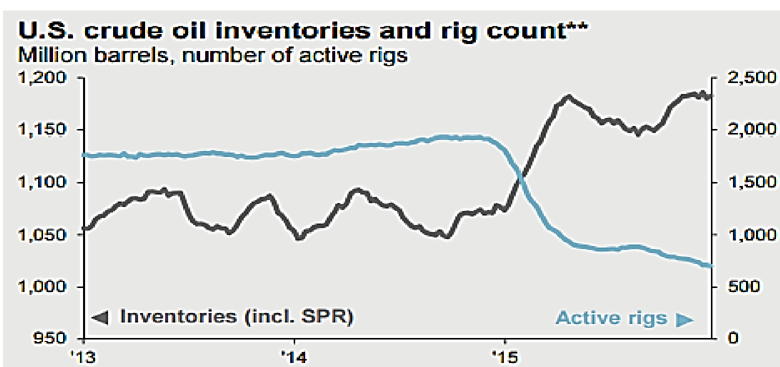
While China's industrial economy continues to slow, services continues to grow, becoming the largest contributor to the Chinese economy. Typically, as consumer wealth increases, spending rises. But, productivity falls, and therefore GDP growth may decelerate during this economic transition.

- **Oil** — this is one of the most difficult areas to forecast, and the markets have been wrong for almost two years now. Here are two data summaries that indicate there is some light at the end of the tunnel:

Change in production and consumption of oil
Production, consumption and inventories, millions of barrels per day

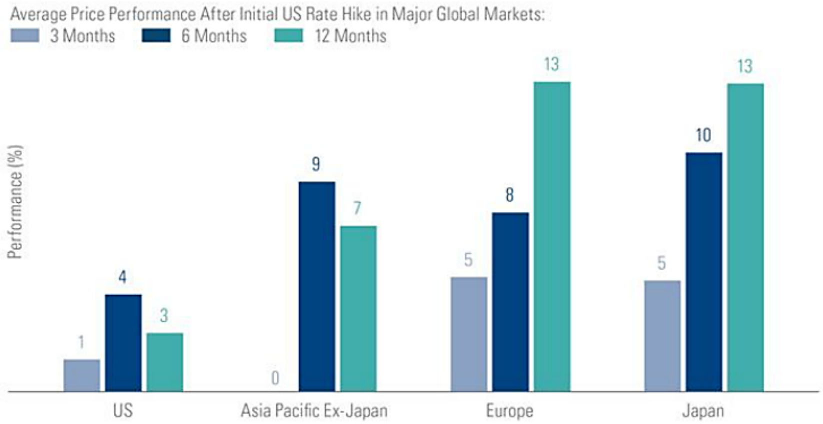
Production	2013	2014	2015*	2016*	Growth since 2013
U.S.	12.4	14.1	14.9	14.7	19.0%
OPEC	36.4	36.4	37.4	38.1	4.5%
Global	**90.9**	**93.3**	**95.5**	**95.8**	**5.4%**
Consumption					
U.S.	19.0	19.1	19.4	19.6	3.2%
China	10.5	10.9	11.2	11.5	9.7%
Global	**91.3**	**92.5**	**93.8**	**95.2**	**4.3%**
Inventory Change	-0.4	0.8	1.7	0.6	

This table implies that the supply/demand gap should begin to narrow as production begins to taper and demand increases. While not a price-favorable equilibrium, it presages some stabilization or (ideally) upward movement in process, both of which are preferred to declines.



U.S. energy-industry capital investment and rig count are on a steep decline, as the rig count data above are a proxy for the oil industry's production and expansion plans. This has implications for prices and activity in the capital markets, and may indicate an easing of some of the pressures energy-company stocks and bonds are facing.

- **U.S. interest rates** — we've been discussing this for a number of months now, and believe that, based on historical evidence, rate-increase fears are overrated. Here are two data summaries that offer some perspective:



Source: Bloomberg and GSAM.

International equities have shown resilience following US rate hikes.

Economic recoveries in the Euro Area and Japan have trailed the US expansion. But today, we believe these regions offer an attractive combination of earnings growth and relative valuations. Major global equity markets in Europe and Asia have the potential to outperform US equities in this hiking cycle.

In the past, rate hikes have correlated well with stock price increases, both in the U.S. and abroad.

Market reaction during previous rate hiking cycles

	May 1983 – July 1984	March 1988 – February 1989	February 1994 – February 1995	June 1999 – May 2000	June 2004 – June 2006	Average
Change in interest rates						
Federal funds rate	3.13%	3.25%	3.00%	1.75%	4.25%	**3.08%**
2-year Treasury	3.11%	2.27%	3.05%	1.21%	2.38%	**2.40%**
10-year Treasury	2.74%	0.85%	1.89%	0.49%	0.51%	**1.30%**
S&P 500 return	-9.6%	6.8%	-2.1%	8.5%	12.0%	**3.1%**
U.S. dollar	10.4%	1.7%	-4.8%	3.4%	-5.8%	**1.0%**

Source: FactSet, Federal Reserve, Standard & Poor's, J.P. Morgan Asset Management.

As we can see above, 10-year U.S. Treasury rates rose slightly during the previous two Fed rate increases, the U.S. dollar was mixed and U.S. stocks were positive. Some dollar weakness and stock appreciation would be welcome now.

"And the beat goes on / The beat goes on" Sonny & Cher

Diversification's basic principle is letting time work for us. We still see positive signs for stocks over bonds, credit in the intermediate-maturity range, municipal bonds and some non-U.S. stocks and markets. We don't expect a gangbuster year, as the global economy and markets need time to recalibrate. This does offer an opportunity for our active managers and thematic investments to work, and we think our clients have time for the transition to take hold.

As always, we welcome your comments, questions and feedback. We wish you and all you hold dear a healthy, happy and prosperous new year.

-Your Wealth Management Team at JJ Burns & Company

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Investing risks include loss of principal and fluctuating value. Small cap securities are subject to greater volatility than those in other asset categories. International investing involves special risks such as currency fluctuation and political instability. Investing in emerging markets may accentuate these risks. Sector-specific investments can also increase these risks.

Fixed income securities are subject to increased loss of principal during periods of rising interest rates. Fixed-income investments are subject to various other risks, including changes in credit quality, liquidity, prepayments, and other factors. REIT risks include changes in real estate values and property taxes, interest rates, cash flow of underlying real estate assets, supply and demand, and the management skill and creditworthiness of the issuer.

The Russell 1000 Index measures the performance of the large-cap segment of the U.S. equity universe. It includes approximately 1000 of the largest securities based on a combination of their market cap and current index membership. The Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership.

The Barclays U.S. Corporate High-Yield Index covers the USD-denominated, non-investment grade, fixed-rate, taxable corporate bond market. The Barclays U.S. Aggregate Index covers the USD-denominated, investment-grade, fixed-rate, taxable bond market of SEC-registered securities.

The Citi World Government Bond Index (WGBI) provides a broad benchmark for the global sovereign fixed income market. It measures the performance of fixed-rate, local currency, investment grade sovereign bonds, currently includes sovereign debt from over 20 countries denominated in a variety of currencies.

The Morningstar® US Real Asset Index is a diversified portfolio of four different asset classes that have historically displayed high sensitivity to inflation. Real assets are defined as TIPS, commodity futures-based strategies, real estate investment trusts, and inflation-sensitive equities such as upstream commodity stocks and master limited partnerships

The S&P U.S. REIT Index defines and measures the investable universe of publicly traded real estate investment trusts domiciled in the United States. The S&P Global REITis a comprehensive benchmark of publicly traded equity REITs listed in both developed and emerging markets. The S&P 500® index includes 500 leading companies and captures approximately 80% coverage of available market capitalization.

The MSCI ACWI index captures large and mid-cap representation across 23 Developed Markets (DM) and 23 Emerging Markets (EM) countries. The MSCI EAFE Index is an equity index which captures large and mid-cap representation across Developed Markets countries around the world, excluding the US and Canada. The MSCI Emerging Markets Index captures large and mid-cap representation across 23 Emerging Markets (EM) countries.

The Bloomberg Commodity Total Return index is composed of futures contracts and reflects the returns on a fully collateralized investment in the BCOM. The index currently represents 20 commodities, which are weighted to account for economic significance and market liquidity.

Charts and graphs from Wellington Management (p. 5), Goldman Sachs Asset Management (pp. 6-7), and J.P. Morgan Asset Management (pp. 6-7).