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3rd quarter summary

THE ECONOMIC CLIMATE

- The U.S. labor market continues to improve but at a slower pace. Real wage growth has risen but not as quickly as other periods of similar labor market tightness. Consumer expenditures remain the primary positive contributor to GDP growth. p. 8, 9
- U.S. inflation has risen steadily with Core CPI at 2.3%
 YoY as of August. Energy and gasoline prices continue
 to weigh on the Headline CPI figure of 1.1% YoY. p. 13
- The presidential election approaches. There has historically been a weak relationship between election outcomes and market performance. This election appears to have unique characteristics and may cause more unpredictable effects. p. 18

MARKET PORTFOLIO IMPACTS

Central bank discussions indicate we may be nearing fiscal expansion as a next form of policy accommodation. As fiscal policies are typically less analyzed and less understood by investors, markets may be more prone to surprise in this environment.
 p. 20

THE INVESTMENT CLIMATE

- U.S. corporate earnings are expected to decline by
 -2.1%, which would be the sixth consecutive
 quarter of YoY decline. Almost all of this decline is
 attributable to energy sector weakness. p. 30
- Low inflation and low bond yields may help to explain higher than usual equity valuations.
 However, this does not negate the fact that higher equity valuations historically have materially reduced subsequent returns. p. 35

ASSET ALLOCATION ISSUES

- We continue to remain underweight risk and believe that downside market potential outweighs upside market potential. p. 29
- Emerging market earnings per share growth turned positive in 2016, reversing a 5-year downward trend. Valuations remain below average on a relative basis and upside potential seems attractive. Investors may consider moving to an overweight in emerging market equities, though risks should be carefully considered. p. 33

We remain underweight to risk

Investors should be watchful of corporate earnings, and U.S. inflation trends



What drove the market in Q3?

"FED STANDS PAT, BUT SAYS CASE FOR RATE INCREASE HAS STRENGTHENED"

December Rate Hike Expectations

Apr 29th	May 31st	June 30th	July 29th	Aug 31st	Sep 30th
41%	42%	9%	31%	45%	51%

Source: WSJ, September 22nd 2016

"U.S. GOVERNMENT BONDS RALLY AS CENTRAL BANKS CALM INVESTORS"

10-Year Treasury Yield

Aug 26th	Sep 2nd	Sep 9th	Sep 16th	Sep 23rd	Sep 30 th
1.63%	1.60%	1.67%	1.69%	1.62%	1.59%

Source: WSJ, September 22nd 2016

"ELECTION UNCERTAINTY WEIGHS ON MARKETS"

U.S. Presidential Election Polls

March 31st		June 30th		Septemb	per 30th
Trump	Clinton	Trump	Clinton	Trump	Clinton
39.1%	49.7%	39.8%	44.6%	44.4%	47.5%

Source: CNBC, September 27th 2016

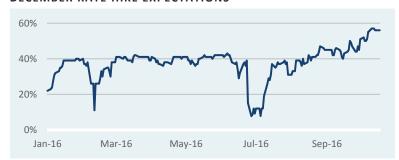
"POUND STERLING FALLS BELOW \$1.31 HITTING NEW 31-YEAR LOW"

GBP/USD

Apr 29th	May 31st	June 30th	July 29th	Aug 31st	Sep 30th
\$1.46	\$1.45	\$1.32	\$1.33	\$1.31	\$1.30

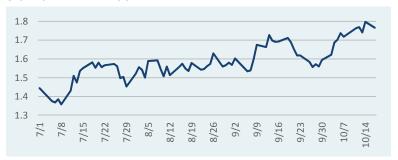
Source: The Independent, July 5th 2016

DECEMBER RATE HIKE EXPECTATIONS



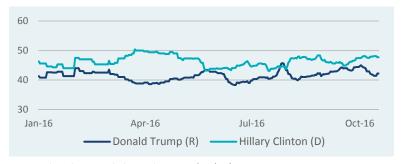
Source: Bloomberg, as of 10/17/16

U.S. 10-YEAR TREASURY YIELD



Source: Federal Reserve, as of 10/17/16

U.S. PRESIDENTIAL ELECTION POLLS



Source: Bloomberg, Real Clear Politics, as of 10/17/16



Economic environment



U.S. economics summary

- U.S. real GDP grew 1.4% YoY in Q2, up from 0.8% in Q1. This positive growth reflects contributions from greater consumer expenditures, exports, and non-residential fixed investments. These were partially offset by a decrease in private inventory investment.
- Headline inflation (CPI) rose 1.1% as of August YoY while core CPI rose 2.3%. Lower energy prices, and gasoline in particular (-17.8%), have weighed heavily on the headline inflation figure. Medical care services (+4.9%) and shelter (+3.4%) contributed to higher prices.
- If the U.S. economy continues to move closer to full employment and higher inflation, the market has expected the Fed to want to push harder for rate

- "normalization". However, the fear of disrupting financial markets and raising rates too early, too quickly, remains.
- Over the last few quarters we have continued to see the slow and steady return to the workforce of discouraged workers. This may help explain why productivity growth and wage inflation are lower than might be expected at this level of unemployment.
- Additions to nonfarm payrolls averaged slightly under 200,000 in the third quarter as the overall labor market continued to show strength. The unemployment rate increased slightly to 5.0% as more people entered the labor force.

Most Recent	12 Months Prior
1.4%	3.9%
6/30/16	6/30/15
1.1%	0.2%
8/31/16	8/31/15
1.8%	1.8%
9/30/16	9/30/15
0.25%	0.12%
9/30/16	9/30/15
1.6%	2.0%
9/30/16	9/30/15
5.0%	5.1%
9/30/16	9/30/15
9.7%	10.0%
9/30/16	9/30/15
	1.4% 6/30/16 1.1% 8/31/16 1.8% 9/30/16 0.25% 9/30/16 1.6% 9/30/16 5.0% 9/30/16



U.S. economics – GDP growth

U.S. real GDP grew 1.4% YoY in the second quarter, up from 0.8% in the first quarter. This positive growth reflects contributions from personal consumption expenditures, exports, and non-residential fixed investment. These were partially offset by a decrease in private inventory investment.

Domestic exports of goods and services grew 1.8% YoY in the second quarter while imports grew 0.2%. A stronger U.S. dollar and weaker demand from China have likely detracted somewhat from export growth.

The manufacturing sector continues to show weakness as durable goods orders have declined during three of the past four months. Additionally, shipments of manufactured durable goods also fell in August, down -0.4%.

The IMF cut U.S. growth expectations to 1.6% for 2016, down from 2.6% in 2015 and down 0.6% from three months prior. Lower business investment has been a primary headwind to growth, with investment decreasing for three consecutive quarters.

Consumer spending continues to drive growth

U.S. REAL GDP GROWTH



Source: FRED, as of 6/30/16

IMF U.S. GROWTH EXPECTATIONS



Source: IMF, as of 10/4/16

U.S. GDP COMPONENTS



Source: FRED



U.S. economics – Unemployment

U.S. unemployment has fluctuated between 4.7% and 5.0% over the past year, and currently sits at a rate of 5.0%. The back-and-forth pull between unemployment rate and participation rate continues as workers rejoin the workforce (higher participation) which then adds to the employment candidate pool (higher unemployment).

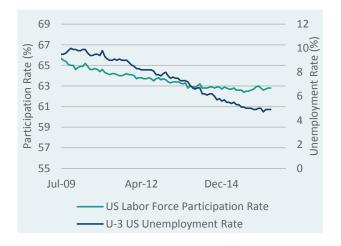
Average length of unemployment has trended downward to 27.6 weeks in August relative to 28.3

weeks one year prior. This is still substantially higher than the long-term median of 14 weeks (since 1948).

In August 151,000 nonfarm jobs were added, below the trailing 12 month average of 204,000.

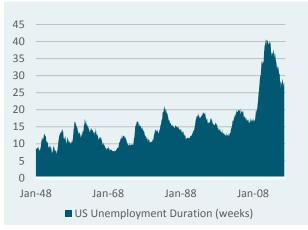
Over the past year, real average hourly earnings have risen by 1.3%. Positive upward pressure in average hourly earnings may help sustain economic growth and may also add to inflation pressures.

U.S. UNEMPLOYMENT & PARTICIPATION



Source: FRED, as of 8/31/16

UNEMPLOYMENT DURATION



Source: FRED, as of 8/31/16

REAL AVERAGE HOURLY EARNINGS



Source: FRED, as of 8/31/16



U.S. economics – The consumer

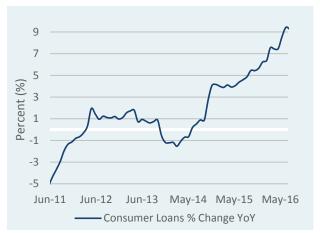
While corporates and governments seem to be at a later stage in terms of their credit cycles, consumer credit expansion has not been as pronounced. A healthy deleveraging has occurred across households since the global financial crisis, with credit expansion only picking up in recent years. It may make sense that the U.S. consumer has been a major contributor to economic growth.

Relatively strong gains in spending have been accompanied by modest increases in real wages and disposable income. Consumer lending growth accelerated

during the quarter, in part due to low borrowing costs and higher consumer confidence. Consumer loans at commercial banks rose 8.8% year-over-year in August. While this growth rate is higher than what we have seen during the current economic expansion, it is within a normal range with regard to historical experience.

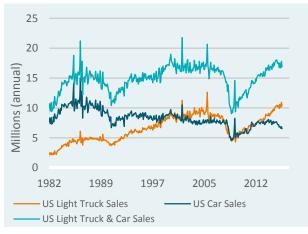
Auto sales have also been robust this year, a good indicator of consumer strength, though sales growth has flattened somewhat and automakers have increased pervehicle incentive spending to all time highs.

CONSUMER LOAN GROWTH



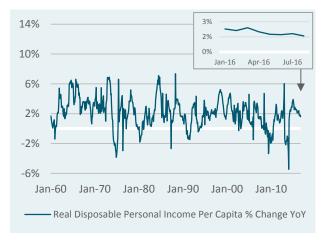
Source: FRED, as of 8/31/16

AUTO SALES



Source: FRED, as of 8/31/16

GROWTH OF DISPOSABLE INCOME



Source: FRED, as of 8/31/16



U.S. economics – The consumer

US REVOLVING OUTSTANDING CONSUMER CREDIT



US HOUSEHOLD DEBT AS % OF DISPOSABLE INCOME



Consumer credit expansion has not been as robust as previous recoveries

Debt service ratios remain low

HOUSEHOLD DEBT SERVICE RATIO %



HOUSING STARTS



Source: FRED, as of 8/31/16



U.S. economics – Sentiment

Consumer sentiment weakened slightly over the quarter. The University of Michigan Sentiment Index ended the quarter lower. Those surveyed indicated that current conditions worsened while expectations for future conditions brightened. The Bloomberg Consumer Comfort Index also declined, falling to its lowest level since mid-December.

zero for 18 consecutive months. However, following July the indicator slipped back into slightly negative territory.

The Citigroup Economic Surprise Index unexpectedly jumped into positive territory in July after staying below

CONSUMER COMFORT INDEX



Source: Bloomberg, as of 9/25/16 (see Appendix)

CONSUMER SENTIMENT



Source: University of Michigan, as of 9/30/16 (see Appendix)

ECONOMIC SURPRISE



Source: Bloomberg, as of 9/30/16 (see Appendix)



U.S. economics – Housing

U.S. housing inventories are near historic lows across single and multifamily markets. Limited supply may help to put upward pressure on new construction activity, which has been below average.

Vacancy rates are near all-time lows in the rental space while homeownership rates continue to fall. Demand for rental properties has increased and multifamily housing starts continue to ramp up; however, multifamily homes are thought to contribute

substantially less to economic growth than that of single-family homes. This may factor into future economic growth.

Lower mortgage rates and moderate wage growth have helped to suppress household debt burdens through greater discretionary income. These forces have contributed to a stronger consumer which may bolster future home purchase and ownership trends, especially as home affordability remains high.

HOME AFFORDABILITY



Source: National Association of Realtors, as of 6/30/16

HOMEOWNERSHIP RATE



Source: FRED, as of 7/1/2016

NEW & EXISTING HOME SALES



Source: Bloomberg, as of 8/31/16



U.S. economics – Inflation

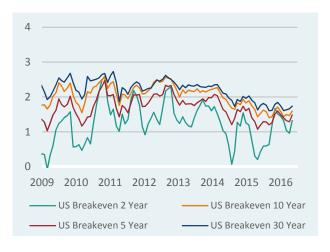
Inflation expectations were mixed during the quarter. The University of Michigan Inflation Expectations Survey reflected lower expected inflation, while the U.S. 10yr TIPS Breakeven indicated higher expectations.

Headline inflation rose 1.1% YoY while core inflation rose 2.3% YoY. Energy and gasoline continue to weigh on prices, while medical care services and shelter (housing costs) put upward pressure on overall prices.

Inflation surveys and inflation-sensitive instruments are inherently different and we might therefore expect discrepancies across these indicators.

Public fear of inflation remains very low, and the Federal Reserve is hesitant to raise rates. We believe investors should be watchful of inflation trends. An inflation overshoot remains a potential danger, given less worry over inflation and less ability and/or willingness of the Fed to raise rates.

U.S. TIPS BREAKEVEN INFLATION



U.S. CPI (YOY)



Source: FRED, as of 7/31/16

MARKET EXPECTATIONS OF INFLATION



Source: Bloomberg, as of 9/30/16



Source: FRED, as of 8/31/16

Where are we now?

RETAIL SALES, YOY (SINCE 1993)



U OF MICH. CONFIDENCE (SINCE 1978)



DURABLE GOODS ORDERS, YOY (SINCE 1992)



While these metrics clearly do not fall at the top end of their historical distribution, they are not outside normal ranges

PERSONAL INCOME, YOY (1948)



PERSONAL CONSUMPTION, YOY (SINCE 1947)



CITI SURPRISE INDEX (SINCE 2003)



Source: Bloomberg, as of 9/30/16



International economics summary

- Developed economies continued to experience slow growth and low inflation. While inflation ticked up slightly in the Eurozone to 0.4%, it remains materially under the ECB's target of "below, but close to, 2%".
- The ECB left monetary policy unchanged at its September meeting, and cut economic growth expectations for the next three years.
- The BOJ shook up its monetary policy after completing a "comprehensive assessment of its current easing programs". The central bank stated it will intentionally overshoot its inflation target of 2% and introduced a 0% target for the 10-year yield.

- Britain elected new prime
 minister Theresa May, who will
 be responsible for implementing
 Brexit. Increased uncertainty
 surrounding the timing and
 nature of the political change will
 continue. The potential impact of
 this uncertainty led to the first
 rate cut by the BOE since 2009.
- The IMF once again downgraded global growth forecasts for 2016 and 2017, this time to just above 3%. It now warns against economic stagnation and states that countries have found themselves in the position of relying on monetary and fiscal policy to lift growth prospects, and that this may be unsustainable.

	l		
Area	GDP (Real, YoY)	Inflation (CPI, YoY)	Unemployment
United States	1.4%	1.1%	5.0%
	6/30/16	8/31/16	9/30/16
Western	1.8%	0.4%	8.5%
Europe	6/30/16	9/30/16	6/30/16
Japan	0.8%	(0.5%)	3.2%
	6/30/16	8/31/16	6/30/16
BRIC Nations	5.1%	3.8%	5.5%
	6/30/16	6/30/16	6/30/16
Brazil	(3.8%)	9.0%	11.7%
	6/30/16	8/31/16	9/30/16
Russia	(0.6%)	6.9%	5.6%
	6/30/16	8/31/16	6/30/16
India	7.1%	5.1%	7.1%
	6/30/16	8/31/16	12/31/15
China	6.7%	1.3%	4.1%
	6/30/16	8/31/16	6/30/16



International economics

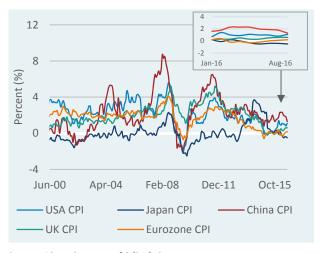
Further downward revisions and lackluster growth in Europe and Japan have encouraged central banks to maintain stimulus measures. Japan implemented a policy initiative which will target a 0% yield for the 10-year government bond. Japan continues to struggle with deflation as headline CPI fell to -0.5% YoY in August.

While economic data released in the U.K. post-Brexit has significantly beaten expectations, uncertainty remains regarding the specific details of the country's exit from the European Union. In its latest report, the BOE lowered the

2017 growth forecast to 0.8% from 2.3%. The central bank also expects inflation to hit 2.4% in 2018 and 2019, citing the fall of the pound sterling.

Emerging market economic growth picked up slightly at 4.6% YoY in the second quarter. After a drop off in growth following the global financial crisis, the outlook for emerging economies has improved. With slow growth expectations for developed markets, an opportunity may exist in both emerging market equities and fixed income.

INTERNATIONAL INFLATION



Source: Bloomberg, as of 8/31/16

REAL GDP GROWTH



Source: Bloomberg, as of 6/30/16

EM VS. DM REAL GDP GROWTH



Source: Bloomberg, as of 6/30/16



Post-Brexit

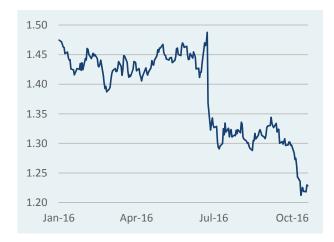
There have been significant changes in U.K. and European political behavior following the Brexit vote. Rear guard actions in both Parliament and the courts in the U.K. have begun to attempt to slow or stop the implementation of Brexit. The Prime Minister has said that Article 50 will be triggered in March 2017.

One of the key elements of the discussion has been debate over whether Brexit should be a 'hard' Brexit (full withdrawal from the Single Market) or a 'soft' Brexit (with continuing participation in the Single Market for a fee, and with continuing free movement of people). Pro-Brexit

campaigners point out that this issue was extensively discussed during the campaign, while Remainers claim that the U.K. population was ill-informed during the run-up to the vote, although their hand is weakened by the fact that their predictions of economic chaos were a Brexit vote to win have so far failed to materialize.

The remaining EU members remain unsure how to proceed, with hard-line negotiators appointed by the EU but strong financial interests in many countries in close ongoing trading links with the U.K.

GBP/USD



Source: FRED, as of 10/19/16

EUROPEAN EQUITY MOVEMENT



Source: Bloomberg, 6/23-9/30/16 – shown in local currency terms

U.K. BALANCE OF TRADE



Source: Bloomberg, as of 9/30/16



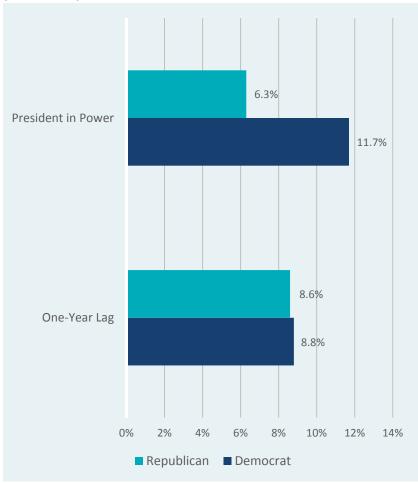
U.S. presidential election

Correlation between election results and long-term market performance has generally been weak, and the outcome depends on how the data is sliced. The S&P 500 has experienced greater price appreciation with a Democrat in power, but the results are less clear when a one-year policy lag is introduced; research results depend on how the relationship is defined.

It appears that a Clinton win would most likely result in little change from the current macroeconomic policy. However, strong congressional pressure would be likely on trade issues, and there would be continuing challenges to the long term sustainability of the Affordable Care Act. Both candidates have supported increased spending on infrastructure, which would provide support for the materials and construction sectors.

A Trump win might bring greater uncertainty because his economic policy plans are less known/understood. Trump's impact may also be felt more quickly through his use of executive orders to reshape the regulatory environment, and some policies enacted by Obama may be undone, through the same means.

AVERAGE CALENDAR YEAR S&P 500 PRICE RETURN (1951-2015)



The relationship between election results and market performance is weak

Note: Top chart = annualized return during time in office, Lower chart = annualized return during time in office but with 1-year lag



Fixed income rates & credit



Interest rate environment

- The U.S. Treasury curve continued to flatten, influenced by increased expectations of an interest rate hike by the end of the year.
- Global interest rates remain near all time lows, although volatility picked up. Continued easing by central banks in addition to low inflation and expectations for slowing growth contribute to an environment of secularly low yields.
- When thinking about bond yields today, it may be useful not only to consider nominal yields, which are at historic lows, but also real yields, which paint a much more reasonable picture. Current levels of inflation and future expectations may help put things into context. Furthermore, investors may see markets drive yields higher if inflation expectations were to rise.

- Negative yielding sovereign and corporate debt was \$11.6 trillion at quarter end, mostly from Japan and the Eurozone. We remain concerned about Japanese and European rates as negative yields and low liquidity detract from the attractiveness of these assets.
- Yields on Japanese Treasuries increased sharply in late July after the BOJ chose to keep stimulus measures on hold. The 10-year JGB yield briefly traded around 0% before falling back into negative territory at the end of September.
- European sovereign bonds sold off during the beginning of September over concerns that central banks may begin cutting back on monetary easing measures.

Area	Short Term (3M)	10 Year
United States	0.27%	1.59%
Germany	(0.76%)	(0.12%)
France	(0.67%)	0.19%
Spain	(0.60%)	0.88%
Italy	(0.39%)	1.19%
Greece	3.34%	8.28%
U.K.	0.32%	0.75%
Japan	(0.33%)	(0.09%)
Australia	1.75%	1.91%
China	2.23%	2.74%
Brazil	13.73%	11.60%
Russia	9.80%	8.17%

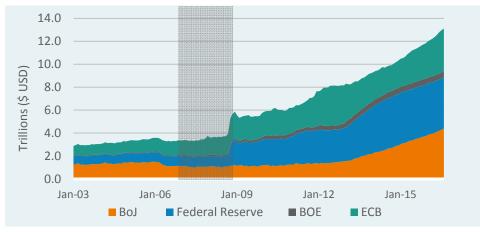
Source: Bloomberg, as of 9/30/16



Unwinding QE

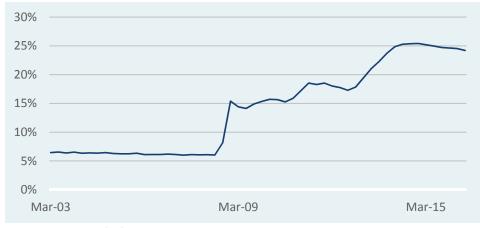
- It appears that we may be nearing the end stage of monetary policy expansion, with over \$7 trillion added to central bank balance sheets. The way in which central banks choose to unwind asset purchases, or how they manage them, could have a significant impact on financial markets.
- Balance sheets may be slowly trimmed through gradual asset sales, or by allowing existing bonds to mature. Shrinking the balance sheet in this manner naturally has a tightening effect, which places downward pressure on asset prices.
- Balance sheet sizes may also be maintained for some time or possibly indefinitely. Were the velocity of money to begin to pick up this balance sheet expansion might lead to inflationary pressure.
- Balance sheets might also be monetized by writing off assets, allowing governments to "walk away" from their debt. With few historical comparisons, forecasting the effects of such write offs is exceptionally difficult. In addition to inflation concerns, this strategy could undermine the independence of central banks and public confidence in them.

CENTRAL BANKS BALANCE SHEETS



Source: FRED, Federal Reserve, BOE, ECB, Verus, as of 8/1/16

FEDERAL RESERVE ASSETS TO GDP

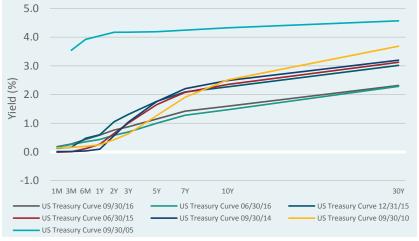


Source: FRED, as of 6/30/16

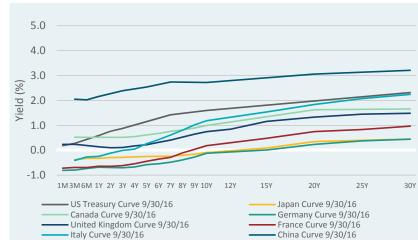


Yield environment

U.S. YIELD CURVE

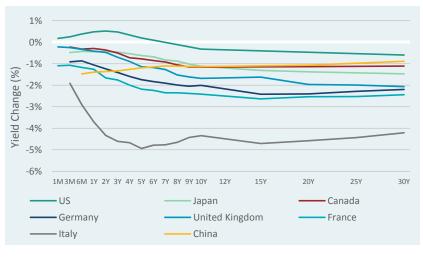


GLOBAL GOVERNMENT YIELD CURVES



Global
investors
continue to
prefer U.S.
Treasuries
due to higher
relative
yields

YIELD CURVE CHANGES OVER LAST FIVE YEARS



IMPLIED CHANGES OVER NEXT YEAR



Source: Bloomberg, as of 9/30/16



Yield environment



Negative <u>real</u> yields are not a new phenomenon

Yield levels should be viewed in context of the inflation environment

Source: Verus, as of 8/31/16



Credit environment

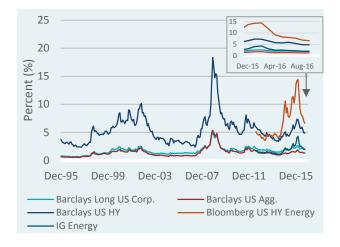
High yield returns across all sectors - energy and metals and mining in particular - have been strong since the trough in Q1. As evidence of this performance, high yield spreads have compressed to below 5.1% as of September from a high of 8.9% earlier in the year.

U.S. credit markets have broadly normalized following increased volatility in Q1. While below the long-term trend, U.S. GDP growth has remained positive, which has been a tailwind to credit markets in general. In addition, foreign demand for U.S. credit issuance has

remained positive as low developed market yields have been supportive of the "carry trade", where investors buy relatively higher yielding assets.

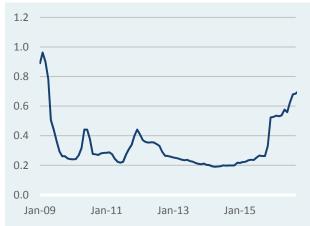
LIBOR rates have increased meaningfully as investors prepared for the pending regulatory changes to money market funds. Prime funds will now report a floating NAV. This change has prompted some investors to redeem their exposures, thereby reducing their demand for commercial paper and LIBOR-based loans causing the rate to increase.

CREDIT SPREADS



Source: Barclays Capital Indices, Bloomberg, as of 9/30/16

3 MONTH LIBOR



Source: Bloomberg, as of 9/30/16

SPREADS

Market	Credit Spread (9/30/16)	Credit Spread (1 Year Ago)
Long US Corporate	1.8%	2.1%
US Aggregate	0.9%	1.2%
US High Yield	5.1%	6.8%
US High Yield Energy	6.6%	11.4%
US Bank Loans	3.9%	3.9%

Source: Barclays, Credit Suisse, Bloomberg, as of 9/30/16



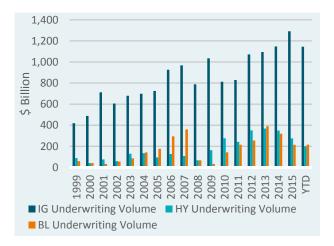
Issuance and default

Defaults have trended higher in recent months, particularly in the high yield debt space. Default rates have risen well above the trailing 20-year average and are at the highest levels since the global financial crisis; however, much of this activity has been driven specifically by energy issuers. Overall issuance is on track for a year-over-year decline.

New bond issuance in emerging markets, especially corporates, has continued at a relatively strong pace. Many of these issuers can only borrow in U.S. dollars. As such, eventual rises in U.S. interest rates would increase borrowing costs. Investors' appetites for emerging market debt remains strong based on relative value compared to developed market bonds.

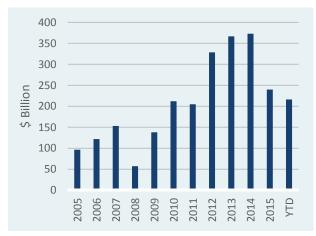
The recent increase in LIBOR rates has been a headwind for bank loan borrowers, as reflected in flattening issuance.

U.S. DEBT ISSUANCE



Source: Bloomberg, BofA Merrill Lynch, as of 9/30/16

EM DEBT ISSUANCE



Source: JP Morgan, as of 9/30/16

HY DEFAULT TRENDS (ROLLING 1 YEAR)



Source: Credit Suisse, BofA, as of 9/30/16



Fixed income – rising yields



During rising
yield
environments
(6 months of
consecutive
rising yields)
BC Agg and
S&P 500
returns have
shown very
different
correlation

We are currently in a negative correlation environment

Date	Months	Yield increase	Average return correlation*	
Jan 1994-Jun 1994	6	1.68	0.70	
Dec 1995-May 1996	6	1.28	0.30	
Mar 1999-Aug 1999	6	0.73	0.11	
Dec 2005-June 2006	7	0.75	-0.18	
Sep 2010-Mar 2011	7	0.96	-0.44	

^{*}Rolling 12 Month correlation between Barclays US Aggregate and S&P 500. "Rising yield environment" is defined as 6 months of consecutive yield increases Source: Bloomberg, MPI, as of 8/31/16



Fixed income – decreasing yields



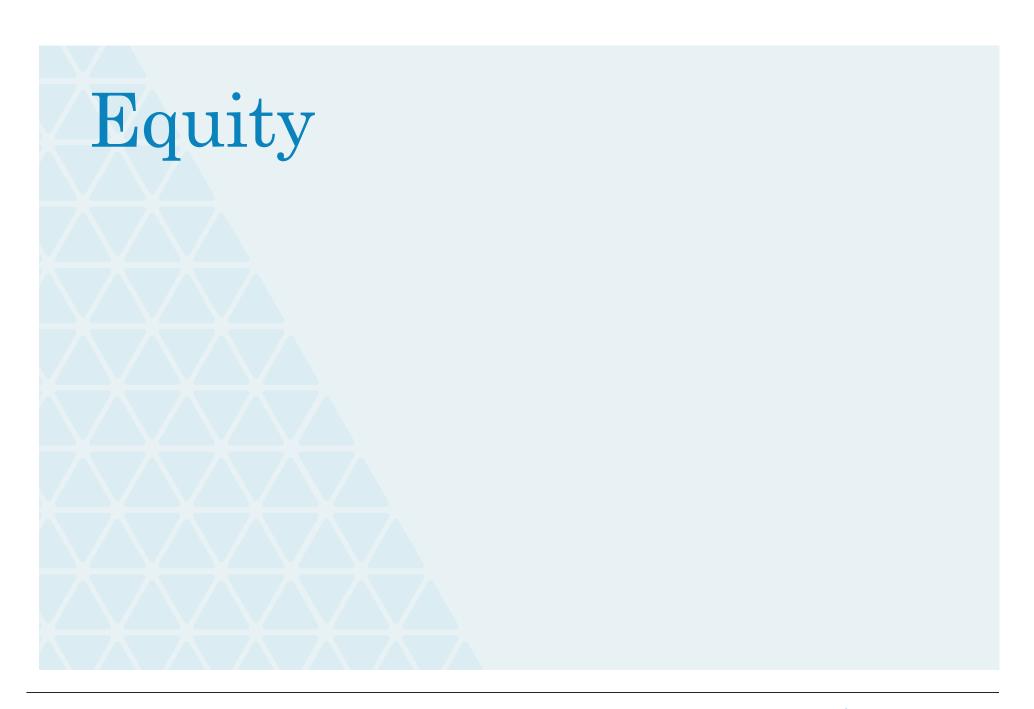
Correlations
have varied
during
decreasing
yield
environments
(6 months of
falling yields),
from -0.66 to
0.71

Diversification benefits have not been clearly linked to the rate environment

Date	Months	Yield decrease	Average return correlation*
Nov 1994-June 1995	8	1.70	0.71
Mar 2002-Sep 2002	7	1.80	-0.66
Mar 2010-Aug 2010	6	1.36	-0.07

^{*}Rolling 12 Month correlation between Barclays US Aggregate and S&P 500. "Decreasing yield environment" is defined as 6 months of consecutive yield decreases. Source: Bloomberg, MPI, as of 8/31/16





Equity environment

- Equity market risks continue to appear asymmetrical to the downside - the U.S. equity market in particular.
- U.S. equities rallied to start the quarter as central banks communicated to the markets that further monetary easing would be available if necessary, in response to the Brexit vote. In the final two months of the quarter, the U.S. equity markets stayed relatively flat and volatility was below average.
- A sixth consecutive quarter of year-over-year earnings decline is expected for the S&P. FactSet has forecast a -2.1% earnings decline for Q3.
- Information technology (12.9%)
 was the best performing sector
 in the S&P 500 by a large margin
 on the back of higher earnings

- expectations. Utilities (-5.9%) and telecom services (-5.6%) were the worst performing sectors in the index.
- The FTSE 100 (hedged) returned
 7.1% over the third quarter after
 concerns over the impact of
 Brexit somewhat subsided.
- The U.S. dollar fell 0.7% in Q3 on a trade-weighted basis.
 Recent dollar stabilization may be disrupted if the Fed goes ahead with further rate hikes. As most developed economies remain in easing mode, further U.S. hikes would likely add to dollar strength.

	QTD TOTAL	. RETURN	YTD TOTA	L RETURN	1 YEAR TOTAL RETURN		
	(unhedged)	(hedged)	(unhedged)	(hedged)	(unhedged)	(hedged)	
US Large Cap (Russell 1000)	4.0	%	7.9	9%	14.9%		
US Small Cap (Russell 2000)	9.0	%	11.	5%	15.5%		
US Large Value (Russell 1000 Value)	3.5	%	10.	0%	16.2%		
US Large Growth (Russell 1000 Growth)	4.6	%	6.0)%	13.8%		
International Large (MSCI EAFE)	6.4%	6.3%	1.7%	(1.0%)	6.5%	5.3%	
Eurozone (Euro Stoxx 50)	6.3%	4.8%	(2.4%)	(4.1%)	0.4%	0.5%	
U.K. (FTSE 100)	4.0%	7.1%	0.6%	14.1%	1.5%	18.4%	
Japan (NIKKEI 225)	8.2%	5.9%	4.4%	(14.3%)	13.6%	(6.2%)	
Emerging Markets (MSCI Emerging Markets)	9.0%	6.3%	16.0%	9.7%	16.8%	10.7%	

Source: Russell Investments, MSCI, STOXX, FTSE, Nikkei, as of 9/30/16



Domestic equity

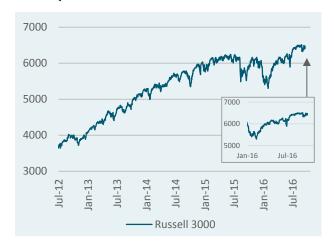
After minimal reaction to Brexit, domestic equities continued higher in July, then delivered two quiet months to finish the quarter. The S&P 500 returned 3.9% in Q3. The market appears to be taking a wait-and-see approach with important oncoming events such as elections and Federal Reserve meetings.

With higher equity prices and lower overall earnings, valuations have expanded. The forward earnings multiple for the S&P 500 was 18.5 at quarter end,

relative to its 25-year average of 16.6 (in the 81st percentile). Year-over-year earnings growth is expected to be negative for the sixth consecutive quarter, heavily influenced by the energy sector and lower oil prices. As the effects of monetary stimulus on U.S. financial markets wanes, earnings will play an important role for future equity returns.

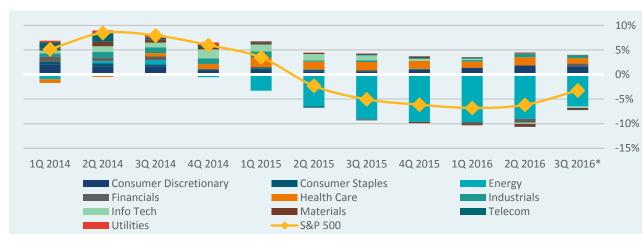
U.S.
earnings
results will
likely dictate
the path of
equities

U.S. EQUITIES



Source: Russell Investments, as of 9/26/16

SECTOR IMPACT ON S&P 500 EARNINGS GROWTH



Source: Bloomberg, as of 9/30/16



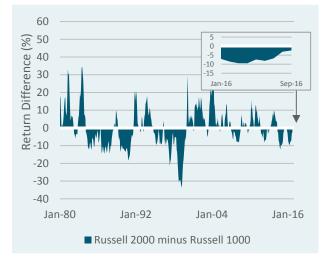
Domestic equity size and style

Growth stocks outperformed value during the third quarter as the Russell 1000 Growth Index and Russell 1000 Value Index returned 4.6% and 3.5%, respectively. However, value has outperformed growth by 4.0% year-to-date.

3.5% year-to-date, reversing a recent trend of large cap outperformance. The relative P/E ratio of small to large cap equities at the end of September was 2.07 - well above its long-term average of 1.39 - suggesting that small cap stocks may be relatively overvalued.

In the third quarter, the Russell 2000 Index returned 9.0% and the Russell 1000 Index returned 4.0%. Small cap equities have also beaten large cap equities by

SMALL CAP VS LARGE CAP (YOY)



Source: Russell Investments, as of 9/30/16

VALUE VS GROWTH (YOY)



Source: Russell Investments, as of 9/30/16

RELATIVE P/E RATIO (SMALL VS LARGE)



Source: Russell, Bloomberg, as of 9/30/16



International equity

Central banks remained accommodative in Q3, helping to generate a rally in international equities. Low and negative yields in Japan and the Eurozone helped maintain the relative attractiveness of equities in these markets.

On a hedged basis, international developed equities outperformed domestic equities with the MSCI EAFE returning 6.3%, and the S&P 500 returning only 3.9% during the quarter.

Financial stocks continue to lag, though the third quarter saw more healthy returns. Banks in Japan and the Eurozone were given a boost when the BOJ and ECB chose not to increase stimulus measures. Significant headwinds remain, however, as negative interest rates continue to hurt bank profitability.

GLOBAL EQUITY PERFORMANCE



Source: Bloomberg, as of 9/30/16

12-MONTH ROLLING RELATIVE FINANCIAL SECTOR RETURNS



Source: MPI, as of 9/30/16, in local currency terms

INTERNATIONAL FORWARD P/E RATIOS



Source: MSCI, as of 9/30/16



Emerging market equity

Emerging market equities experienced a rebound during Q3, returning 6.3% on a hedged basis and 9% unhedged. Emerging market earnings per share growth turned positive in 2016, reversing a 5-year downward trend. Valuations remain below average and materially more attractive than those of developed markets.

Moderating commodity prices, continued developed central bank accommodation, less U.S. dollar strengthening, and stability in China, have helped to bolster investor risk appetites and the emerging market

outlook, fueling fund flows into these markets.

Many emerging market economies experienced a rough readjustment period following the commodity supercycle reversal and saw severe currency depreciation. However, many economies such as Russia have allowed currency devaluation to work as an effective economic shock absorber to mitigate current account problems which these economies often experience during commodity (export) price choppiness.

ECONOMIC GROWTH (REAL GDP YOY)



Source: Bloomberg, as of 6/30/16

EM VS. DM REAL GDP GROWTH



Source: Bloomberg, as of 6/30/16

FORWARD P/E



Source: MSCI, as of 9/30/16



Equity valuations

Domestic large cap equity valuations remain above average. The forward earnings multiple for the S&P 500 was 18.5 at quarter end, relative to its 25-year average of 16.6. This places the forward P/E in the 81st percentile of the past 25 years.

Large cap equity valuations are also slightly above average based on the Shiller P/E ratio.

Small cap equity valuations are above long-term

averages, suggesting that small caps are currently overvalued. The forward P/E ratio for the Russell 2000 as of September 30th was 28.1, compared to the long-term average of 25.3.

Historically, low interest rate and low inflationary environments have coincided with above-average valuations (see slide 35). This makes it difficult to tell whether equities are truly overvalued or if current valuations simply reflect the economic environment.

MSCI VALUATION METRICS (3 MONTH AVERAGE)



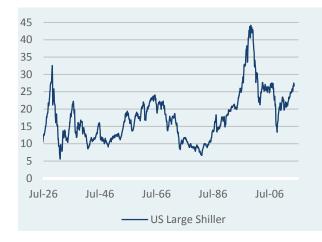
Source: MSCI, as of 9/30/16

FORWARD P/E



Source: Yale/Shiller, Verus as of 9/30/16

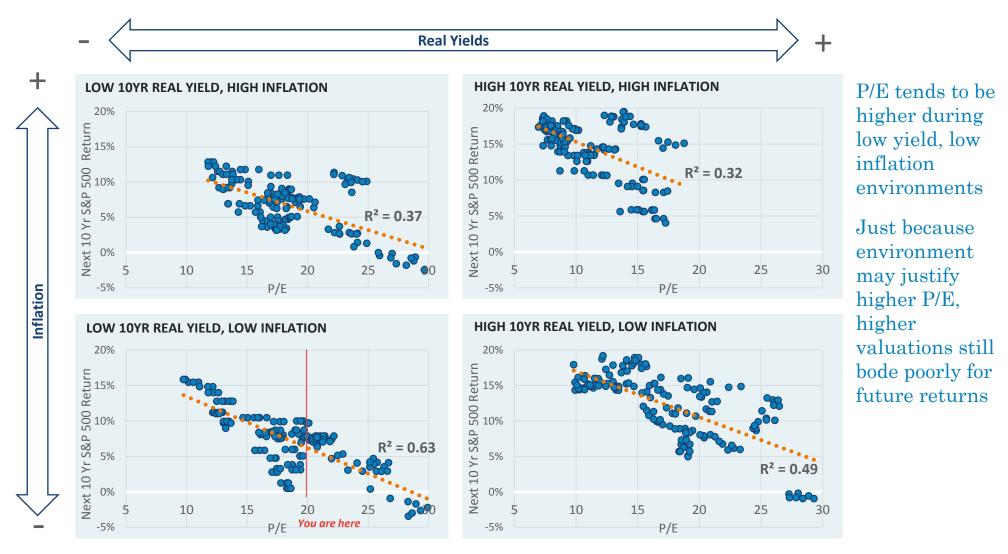
S&P 500 SHILLER P/E RATIO



Source: Yale/Shiller, as of 9/30/16



Putting valuations into context



Using data since 1954, sorted the economic environment into the above 4 market environments: low 10yr Treasury real yield & high inflation, high 10yr Treasury real yield & low inflation, and high 10yr real yield & low inflation. Within each quadrant, plotted each point-in-time P/E level for the S&P 500 (the x-axis) and the subsequent 10 year equity return (y-axis).



Equity volatility

Following a substantial spike in volatility during the Brexit vote announcement, equity volatility fell and remained subdued. The VIX index has averaged around a level of 20 during the past 25 years. More recently investors have seen VIX levels below this average which is typical during equity bull markets.

Volatility expectations, as indicated by VIX, continue to be low, though we might expect rising levels given political uncertainty leading up to the U.S. presidential election.

International equity market volatility has remained in a normal range, following choppiness during news surrounding and following the Brexit referendum. Unhedged currency exposure has also added to variation in investors' experienced equity returns — and much more so in recent years.

U.S. EQUITY VOLATILITY



Source: CBOE, as of 9/22/16

INTERNATIONAL EQUITY VOLATILITY

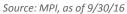


Source: MSCI, as of 9/30/16



Long-term equity performance







Other assets

Commodities

Commodity prices, and oil in particular, continue to fill the news headlines. Though short-term price movements are not particularly relevant to portfolio decision-making, effects of the commodity supercycle reversal are important.

Declining profits in the energy sector have pushed U.S. equity earnings into negative territory for the past 1.5 years. Many commodity exporting nations have

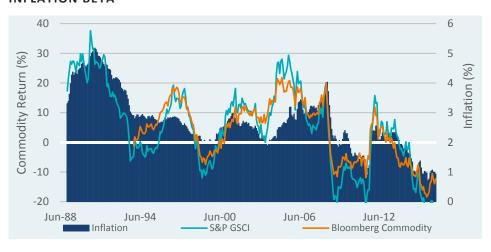
realized extreme currency devaluation which has harshly impacted the unhedged returns of foreign investors. Here at home energy-related debt defaults are accelerating and fueling worries that a prolonged energy slump could have a serious fallout effects for the U.S. energy sector. OPEC members and nonmembers alike continue discussions regarding production cut strategies and agreements, though it is debatable whether these agreements will be upheld.

COMMODITY PERFORMANCE



Source: Bloomberg, as of 9/30/16

INFLATION BETA



Source: Standard & Poor's, Bloomberg, as of 9/30/16



Currency

The U.S. dollar, weighted by major trading partners, fell 0.7% in the third quarter, benefitting investors with unhedged equity exposure. The pound sterling has had the opposite effect for U.S. investors, as new multidecade lows were reached during the quarter, following a significant market flash crash (but recovery).

After a recent period of appreciation, the dollar has stabilized so far this year. Moderation of the USD would have a positive impact on earnings of U.S. companies with significant international exposure.

However, with the Fed expected to continue increasing interest rates while other central banks are still in easing mode, there may be upward pressure on the dollar as interest rate differentials increase.

The pound sterling fell to a 31-year low against the U.S. dollar, influenced by uncertainty surrounding the details of the U.K.'s exit from the European Union. Theresa May announced that she would invoke Article 50 by March 2017.

LONG-TERM TRADE WEIGHTED USD



EFFECT OF CURRENCY (1YR ROLLING)



Source: MSCI, as of 9/30/16

GBP/USD



Source: FRED, as of 10/19/16

Source: FRED, as of 9/30/16

Appendix

Periodic table of returns – September 2016

BEST																											
<u></u>		1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	YTD	5-Year	10-Year
	Small Cap Value	74.8	16.6	38.4	23.2	35.2	38.7	66.4	31.8	14.0	25.9	56.3	26.0	34.5	32.6	39.8	5.2	79.0	29.1	14.3	18.6	43.3	13.5	10.1	16.0	16.6	8.8
	Emerging Markets Equity	32.9	8.1	37.8	23.1	32.9	27.0	43.1	22.8	8.4	10.3	48.5	22.2	21.4	26.9	16.2	1.4	37.2	26.9	7.8	18.1	38.8	13.2	5.7	15.5	16.4	8.3
	Small Cap Equity	26.3	6.4	37.2	22.4	31.8	20.3	33.2	12.2	7.3	6.7	47.3	20.7	20.1	23.5	15.8	-6.5	34.5	24.5	2.6	17.9	34.5	13.0	0.9	11.5	16.2	7.4
	Large Cap Value	23.8	4.4	31.0	21.6	30.5	19.3	27.3	11.6	3.3	1.6	46.0	18.3	14.0	22.2	11.8	-21.4	32.5	19.2	1.5	17.5	33.5	11.8	0.6	10.0	16.1	7.4
	Large Cap Equity	19.3	3.2	28.5	21.4	22.4	16.2	26.5	7.0	2.8	1.0	39.2	16.5	7.5	18.4	11.6	-25.9	28.4	16.8	0.4	16.4	33.1	6.0	0.0	8.9	15.8	7.1
	60/40 Global Portfolio	18.9	2.6	25.7	16.5	16.2	15.6	24.3	6.0	2.5	-5.9	30.0	14.5	7.1	16.6	10.9	-28.9	27.2	16.7	0.1	16.3	32.5	5.6	-0.4	8.0	15.4	5.9
	Small Cap Growth	18.1	0.4	19.6	14.4	13.9	8.7	21.3	4.1	-2.4	-6.0	29.9	14.3	6.3	15.5	10.3	-33.8	23.3	16.1	-2.1	15.3	23.3	4.9	-0.8	7.9	11.5	5.8
	US Bonds	13.4	-1.5	18.5	11.3	12.9	4.9	20.9	-3.0	-5.6	-11.4	29.7	12.9	5.3	15.1	7.0	-35.6	20.6	15.5	-2.9	14.6	12.1	4.2	-1.4	7.5	7.4	4.8
	Large Cap Growth	10.2	-1.8	15.2	10.3	10.6	1.2	13.2	-7.3	-9.1	-15.5	25.2	11.4	4.7	13.3	7.0	-36.8	19.7	13.1	-4.2	11.5	11.0	3.4	-2.5	6.0	7.2	4.6
	Commodities	9.7	-2.0	11.6	9.9	9.7	-2.5	11.4	-7.8	-9.2	-15.7	23.9	9.1	4.6	10.4	5.8	-37.6	18.9	10.2	-5.5	10.5	9.0	2.8	-3.8	5.8	3.2	3.9
	Real Estate	3.1	-2.4	11.1	6.4	5.2	-5.1	7.3	-14.0	-12.4	-20.5	11.6	6.9	4.6	9.1	4.4	-38.4	11.5	8.2	-5.7	4.8	0.1	0.0	-4.4	4.3	3.1	1.8
	International Equity	2.9	-2.9	7.5	6.0	2.1	-6.5	4.8	-22.4	-19.5	-21.7	9.0	6.3	4.2	4.8	-0.2	-38.5	5.9	6.5	-11.7	4.2	-2.0	-1.8	-7.5	1.7	3.0	1.8
	Cash	1.4	-3.5	5.7	5.1	-3.4	-25.3	-0.8	-22.4	-20.4	-27.9	4.1	4.3	3.2	4.3	-1.6	-43.1	0.2	5.7	-13.3	0.1	-2.3	-4.5	-14.9	0.2	0.1	0.8
\downarrow	Hedge Funds of Funds	-1.1	-7.3	-5.2	3.6	-11.6	-27.0	-1.5	-30.6	-21.2	-30.3	1.0	1.4	2.4	2.1	-9.8	-53.2	-16.9	0.1	-18.2	-1.1	-9.5	-17.0	-24.7	-0.1	-9.4	-5.3
WORST				Large	e Cap E	quity					Small (Cap Gr	owth			ı	Co	ommo	dities								
>				Large	Cap V	/alue					Interna	ationa	l Equit	У			Re	eal Est	ate								
				Large	Cap	Growth					Emergi	ng Ma	rkets I	Equity			Не	edge F	unds o	of Fund	S						
				Smal	l Cap E	quity					US Bon	ds					60)% MS	CI ACW	/1/40%	BC Glo	obal B	ond				
				Smal	l Cap V	/alue					Cash																

Source Data: Morningstar, Inc., Hedge Fund Research, Inc. (HFR), National Council of Real Estate Investment Fiduciaries (NCREIF). Indices used: Russell 1000, Russell 1000 Value, Russell 1000 Growth, MSCI EAFE, MSCI EM, BC Agg, T-Bill 90 Day, Bloomberg Commodity, NCREIF Property, HFRI FOF, MSCI ACWI, BC Global Bond. NCREIF Property performance data as of 6/30/16.



Major asset class returns

ONE YEAR ENDING SEPTEMBER



TEN YEARS ENDING SEPTEMBER



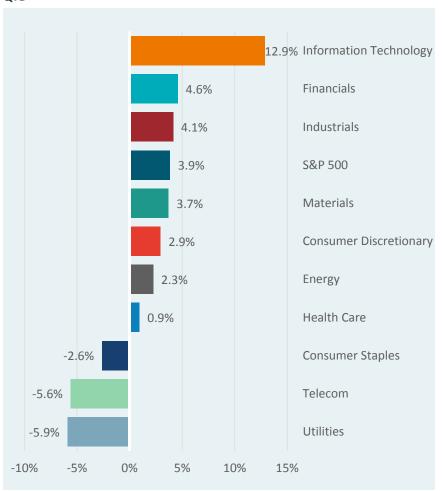
Source: Morningstar, as of 9/30/16

Source: Morningstar, as of 9/30/16

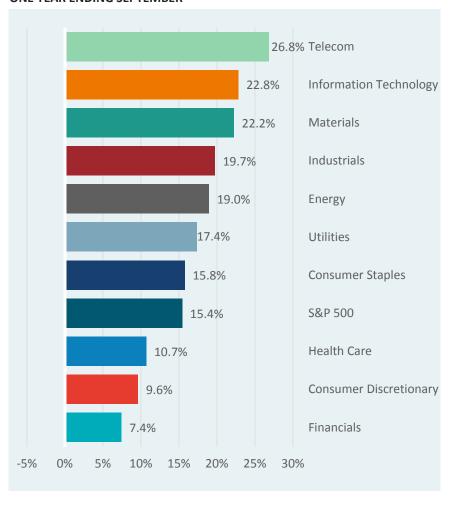


S&P 500 and S&P 500 sector returns

QTD



ONE YEAR ENDING SEPTEMBER



Source: Morningstar, as of 6/30/16

Source: Morningstar, as of 6/30/16



Detailed index returns

ЛFST		

	Month	QTD	YTD	1 Year	3 Year	5 Year	10 Year
Core Index							
S&P 500	0.0	3.9	7.8	15.4	11.2	16.4	7.2
S&P 500 Equal Weighted	0.1	4.5	10.6	16.1	10.8	17.4	8.8
DJ Industrial Average	(0.4)	2.8	7.2	15.5	9.2	13.8	7.4
Russell Top 200	0.0	3.8	7.0	15.2	11.3	16.3	7.0
Russell 1000	0.1	4.0	7.9	14.9	10.8	16.4	7.4
Russell 2000	1.1	9.0	11.5	15.5	6.7	15.8	7.1
Russell 3000	0.2	4.4	8.2	15.0	10.4	16.4	7.4
Russell Mid Cap	0.2	4.5	10.3	14.2	9.7	16.7	8.3
Style Index							
Russell 1000 Growth	0.4	4.6	6.0	13.8	11.8	16.6	8.8
Russell 1000 Value	(0.2)	3.5	10.0	16.2	9.7	16.2	5.9
Russell 2000 Growth	1.4	9.2	7.5	12.1	6.6	16.1	8.3
Russell 2000 Value	0.8	8.9	15.5	18.8	6.8	15.4	5.8

FIXED INCOME

	Month	QTD	YTD	1 Year	3 Year	5 Year	10 Year
Broad Index							
BC US Treasury US TIPS	0.5	1.0	7.3	6.6	2.4	1.9	4.5
BC US Treasury Bills	0.0	0.1	0.3	0.3	0.2	0.1	1.0
BC US Agg Bond	(0.1)	0.5	5.8	5.2	4.0	3.1	4.8
Duration							
BC US Treasury 1-3 Yr	0.1	(0.1)	1.3	0.9	0.9	0.7	2.3
BC US Treasury Long	(1.6)	(0.4)	14.7	13.1	11.2	5.5	8.1
BC US Treasury	(0.1)	(0.3)	5.1	4.1	3.4	2.2	4.5
Issuer							
BC US MBS	0.3	0.6	3.7	3.6	3.6	2.6	4.7
BC US Corp. High Yield	0.7	5.6	15.1	12.7	5.3	8.3	7.7
BC US Agency Interm	0.2	(0.0)	2.3	1.7	1.8	1.4	3.4
BC US Credit	(0.3)	1.2	8.9	8.3	5.4	4.8	5.8

INTERNATIONAL EQUITY

Broad Index							
MSCI ACWI	0.6	5.3	6.6	12.0	5.2	10.6	4.3
MSCI ACWI ex US	1.2	6.9	5.8	9.3	0.2	6.0	2.2
MSCI EAFE	1.2	6.4	1.7	6.5	0.5	7.4	1.8
MSCI EM	1.3	9.0	16.0	16.8	(0.6)	3.0	3.9
MSCI EAFE Small Cap	3.0	8.6	5.2	12.3	5.1	11.1	4.4
Style Index							
MSCI EAFE Growth	1.5	5.0	2.6	9.5	2.4	8.7	3.1
MSCI EAFE Value	1.0	8.0	0.8	3.5	(1.5)	6.0	0.4
Regional Index							
MSCI UK	1.0	4.0	0.8	1.5	(1.8)	6.0	1.4
MSCI Japan	1.6	8.6	2.5	12.1	3.3	7.4	1.0
MSCI Euro	0.7	7.3	(0.6)	2.8	(0.9)	7.3	0.2
MSCI EM Asia	1.3	10.5	13.0	16.9	3.5	6.3	5.6
MSCI EM Latin American	(0.8)	5.4	32.2	28.6	(7.9)	(3.9)	2.4

OTHER

Index							
Bloomberg Commodity	3.1	(3.9)	8.9	(2.6)	(12.3)	(9.4)	(5.3)
Wilshire US REIT	(2.1)	(1.2)	9.7	17.9	14.3	15.8	5.9
Regional Index							
JPM EMBI Global Div	0.4	4.0	14.8	16.2	8.2	7.8	7.7
JPM GBI-EM Global Div	2.0	2.7	17.1	17.1	(2.6)	0.1	5.5
Currency (Spot)							
Euro	0.9	1.2	3.5	0.7	(6.0)	(3.5)	(1.2)
Pound	(0.8)	(2.8)	(11.9)	(14.2)	(7.1)	(3.6)	(3.6)
Yen	2.1	1.3	18.8	18.3	(1.0)	(5.3)	1.5

Source: Morningstar, as of 9/30/16



Definitions

Bloomberg US Weekly Consumer Comfort Index - tracks the public's economic attitudes each week, providing a high-frequency read on consumer sentiment. The index, based on cell and landline telephone interviews with a random, representative national sample of U.S. adults, tracks Americans' ratings of the national economy, their personal finances and the buying climate on a weekly basis, with views of the economy's direction measured separately each month. (www.langerresearch.com)

University of Michigan Consumer Sentiment Index - A survey of consumer attitudes concerning both the present situation as well as expectations regarding economic conditions conducted by the University of Michigan. For the preliminary release approximately three hundred consumers are surveyed while five hundred are interviewed for the final figure. The level of consumer sentiment is related to the strength of consumer spending. (www.Bloomberg.com)

Citi Economic Surprise Index - objective and quantitative measures of economic news. Defined as weighted historical standard deviations of data surprises (actual releases vs Bloomberg survey median). A positive reading of the Economic Surprise Index suggests that economic releases have on balance been beating consensus. The indices are calculated daily in a rolling three-month window. The weights of economic indicators are derived from relative high-frequency spot FX impacts of 1 standard deviation data surprises. The indices also employ a time decay function to replicate the limited memory of markets. (www.Bloomberg.com)

Merrill Lynch Option Volatility Estimate (MOVE) Index – a yield curve weighted index comprised of a weighted set of 1-month Treasury options, including 2.5.10 and 30 year tenor contracts. This index is an indicator of the expected (implied) future volatility in the rate markets.

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