

Market & Portfolio Strategy Review

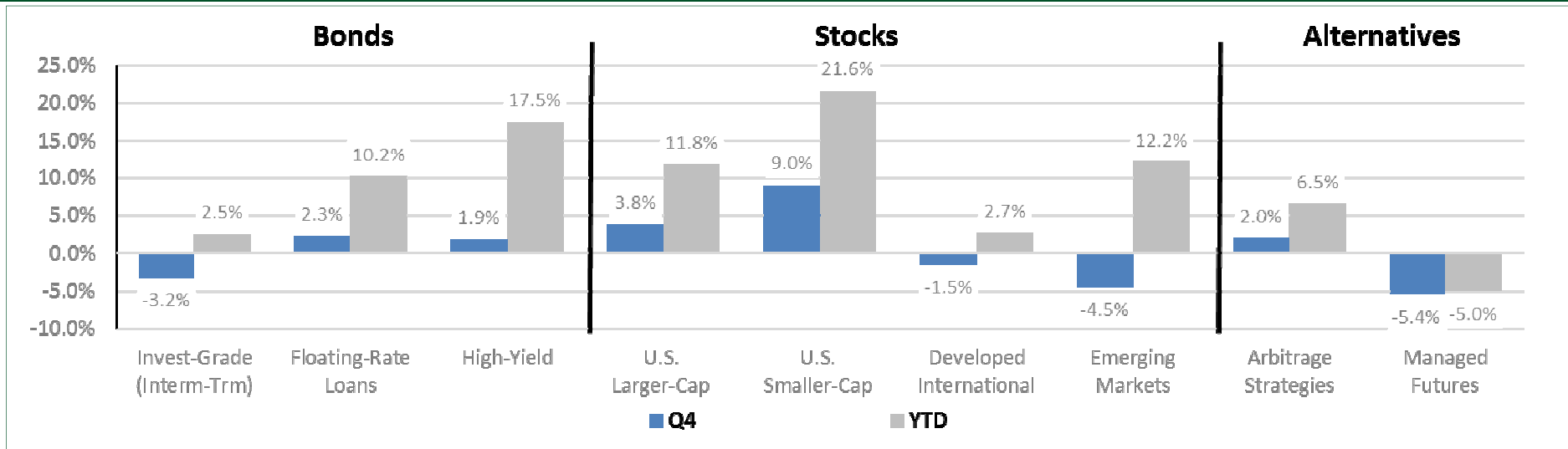
Fourth Quarter 2016





Market Review

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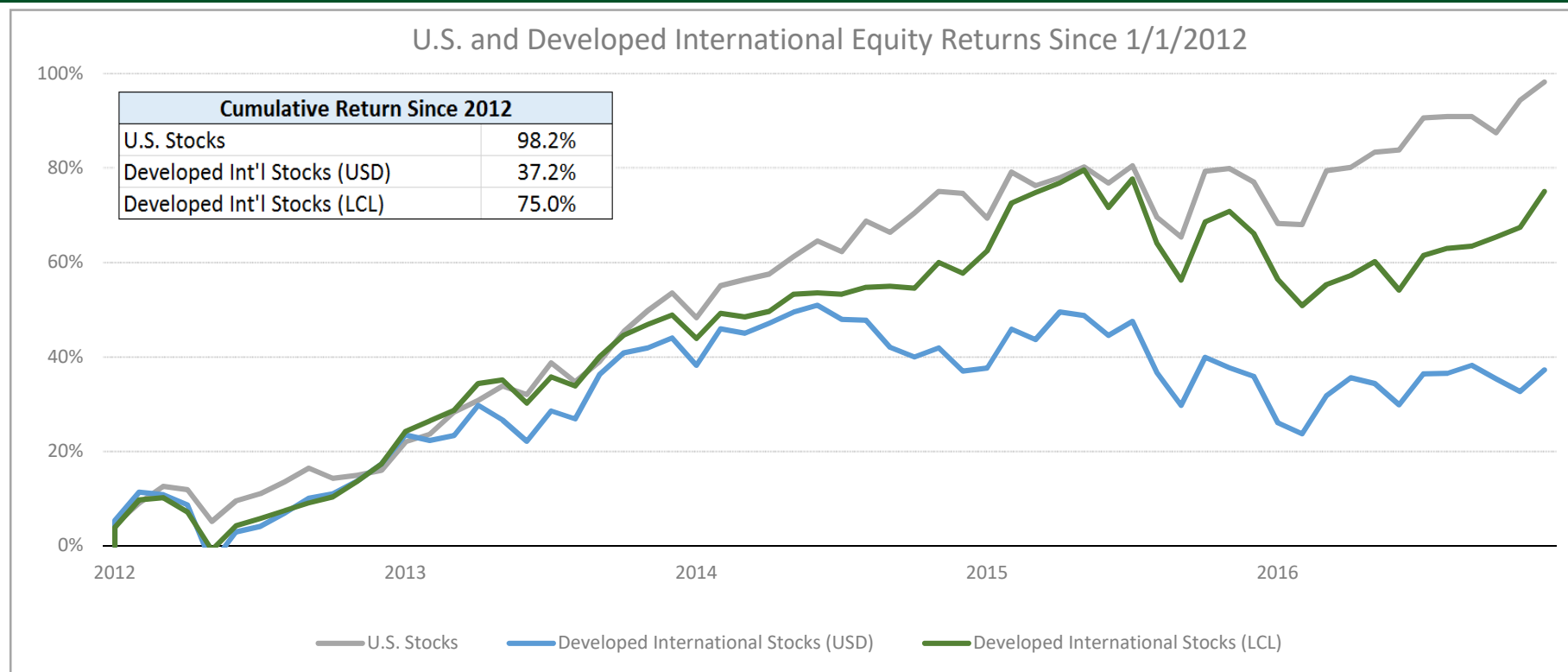
- Global equities performed well in absolute terms and relative to core bonds. U.S. stocks again took the lead, marking the eighth straight year the S&P 500 had a positive return. Emerging markets were also strong, though they did give back some gains in the fourth quarter.
- Developed International stocks were the big laggard on the year, returning just 2.7% in U.S. dollar terms. European stocks did worse, falling 0.4%. Currency exposure was again the main culprit as the British Pound and euro fell 16% and 3% relative to the U.S. dollar. This was the third straight year dollar appreciation was a drag on foreign stock returns.
- The core bond index fell 3.2% in the fourth quarter—its worst quarterly performance in 35 years. Fixed-income sectors with more credit risk (and less interest rate risk), such as high-yield and floating-rate loans, generated very strong returns both in the fourth quarter and year to date.
- Arbitrage strategies delivered solid absolute returns for the year and performed well as interest rates rose over the fourth quarter. Managed futures, which are volatile and have a wide range of potential returns, suffered from the many market reversals that occurred this year.

2016: A Year of Market Reversals

Performance Reversals in 2016

	Previous Two-Year Return	Return Since
Since Emerging-Markets Low in January		
Emerging-Markets Stocks	-25.5%	28.2%
Oil (WTI)	-68.7%	82.4%
Since U.S. Market Low in February		
U.S. Small Cap Stocks vs. U.S. Large Cap Stocks	-18.0%	19.5%
U.S. Value Stocks vs. U.S. Growth Stocks	-7.7%	10.8%
U.S. Value Stocks vs. U.S. Momentum Stocks	-11.2%	14.1%
Since 10-Year U.S. Treasury Yield Low in July		
U.S. Core Bonds	9.1%	-3.3%
U.S. Treasuries (7-10 Year Index)	14.8%	-7.0%
Since U.S. Presidential Election		
Consumer Staples Stocks vs. S&P 500	6.3%	-6.2%
Utilities Stocks vs. S&P 500	4.3%	-5.2%
Energy Stocks vs. S&P 500	-25.5%	4.0%
Financials Stocks vs. S&P 500	-3.4%	11.8%

Currencies Were Again a Headwind for Foreign Stock Returns

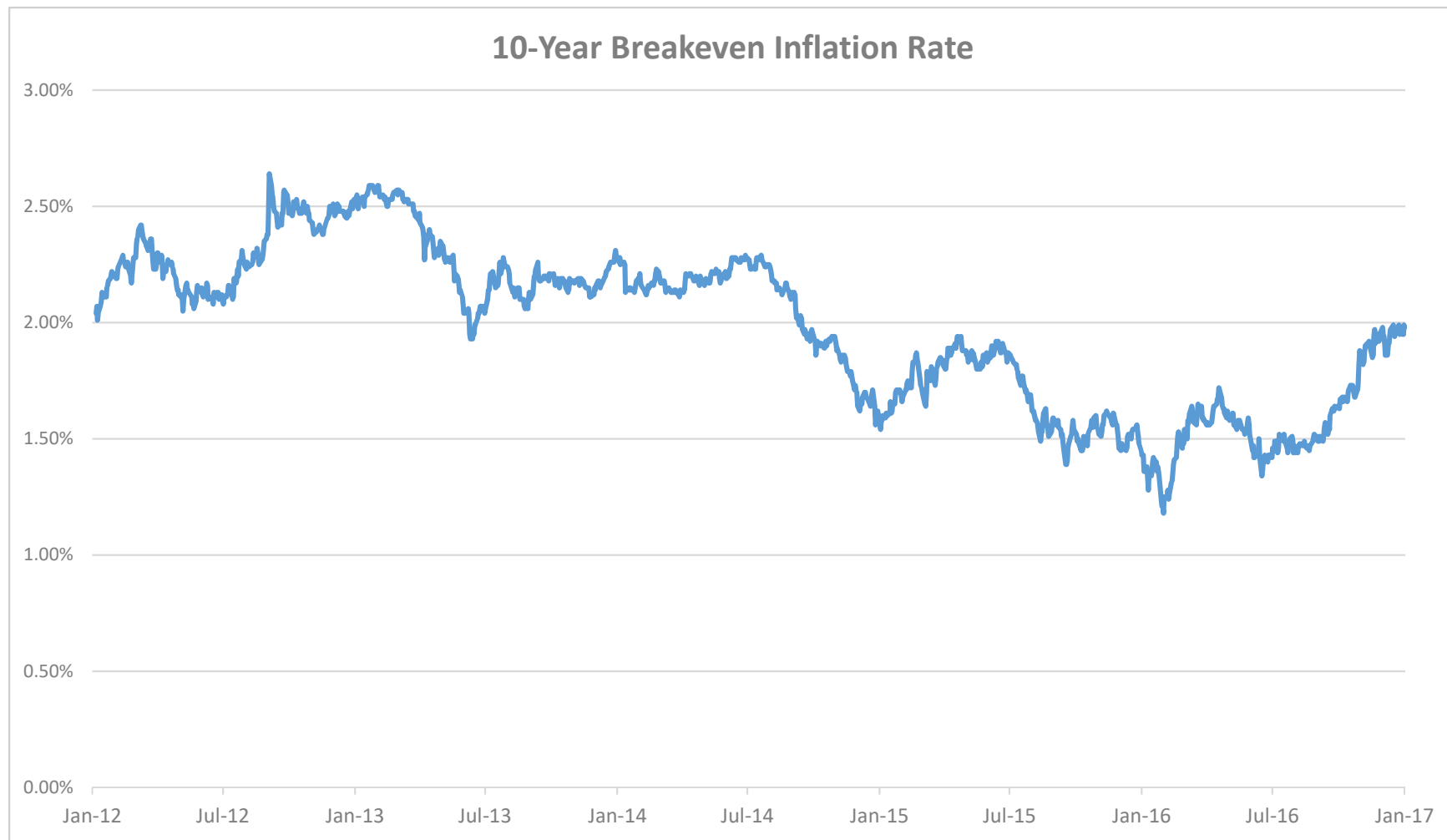


- For the third straight year, dollar appreciation was a drag on foreign stock returns. The major currency decliner was the British pound which fell 16% versus the U.S. dollar, triggered in June's Brexit vote.
- This marks the fourth straight calendar year and the sixth in the past seven that U.S. stocks have outperformed foreign stocks. Going back to 2008, this is one of the longest stretches of U.S. outperformance on record.

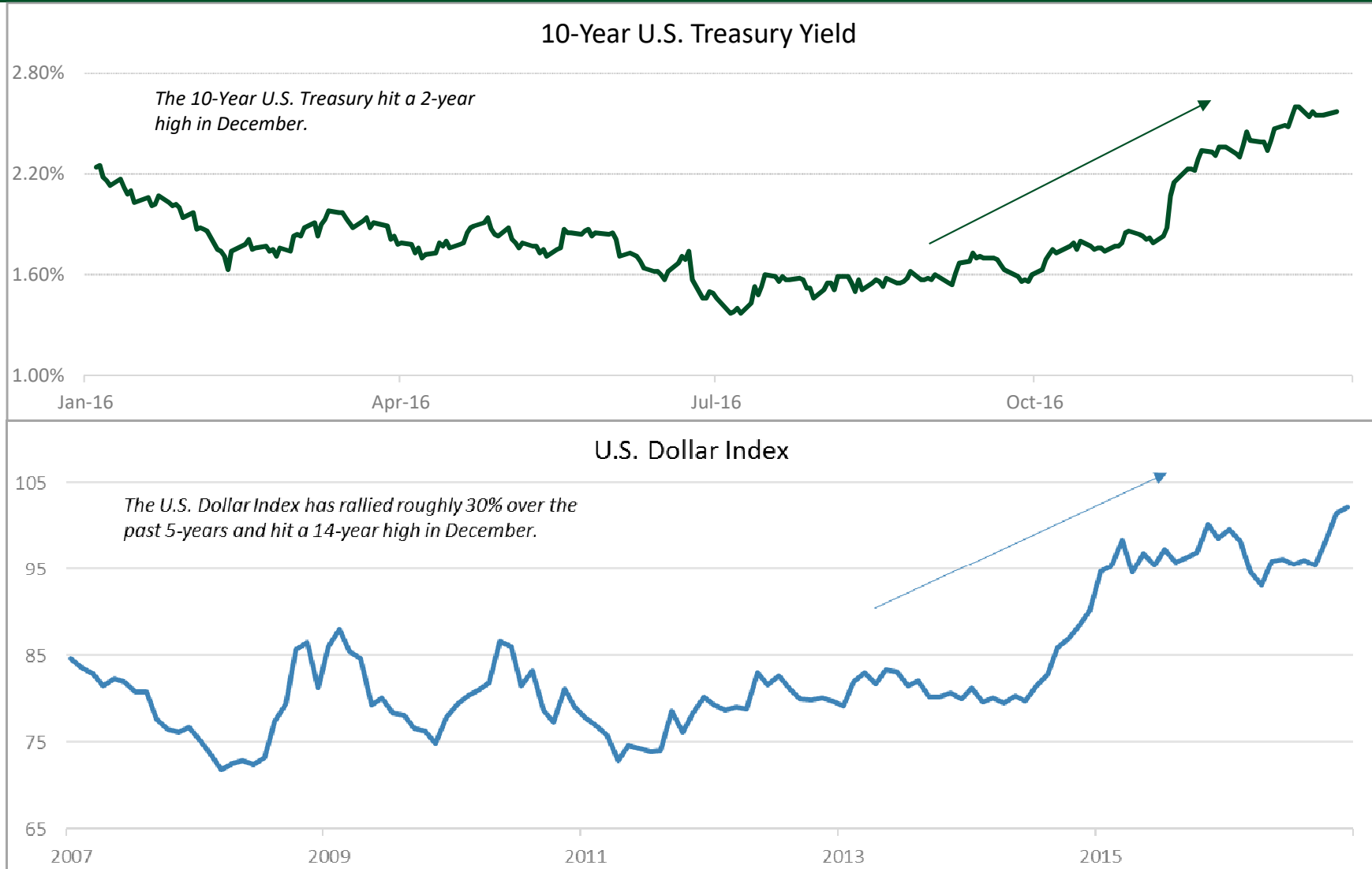


Investment Outlook & Positioning

Trump's Policy Agenda Suggests Further Inflationary Pressure is Likely



Interest Rates Rose and the Dollar Rallied Post-Election



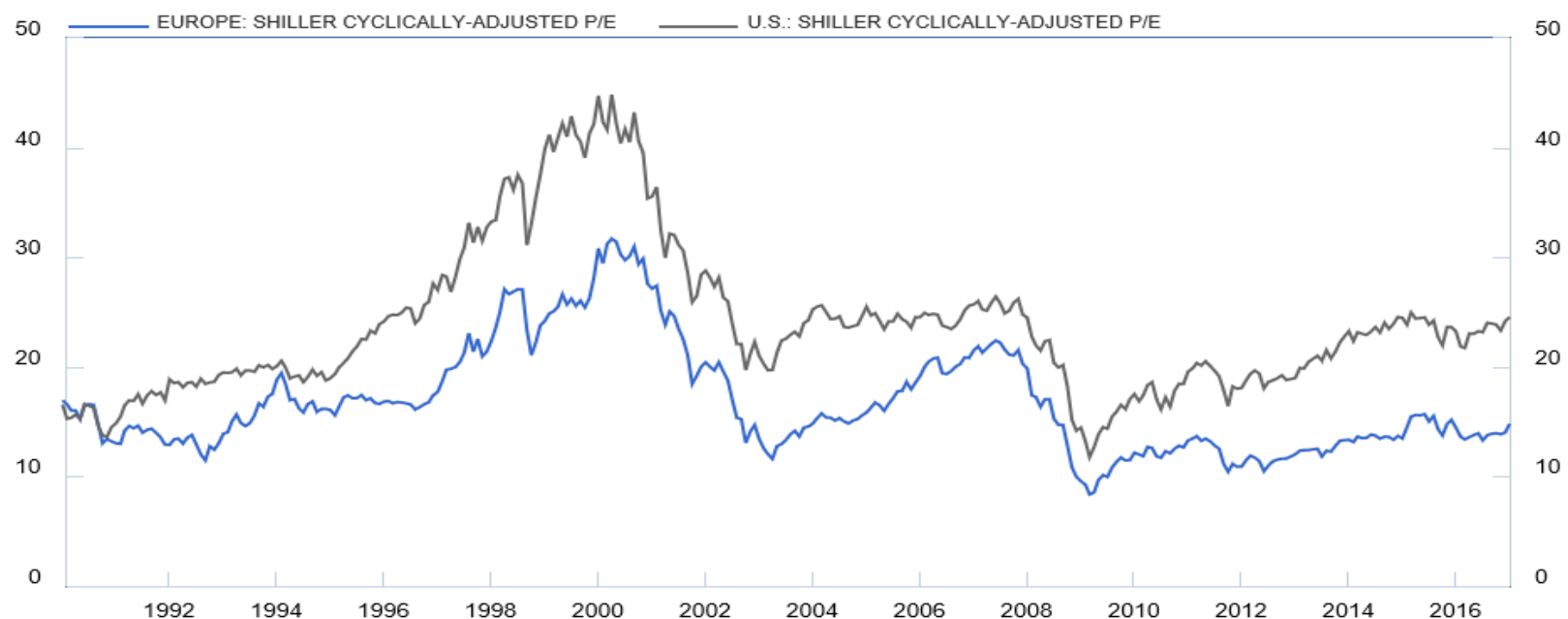
U.S. Stocks Appear Overvalued With a Lot of Optimism Baked into Current Prices

U.S. Stock Market Valuations



European Stocks are Trading at a Valuation Discount in Absolute Terms and Relative to U.S. Stocks

U.S. And Europe Shiller PE

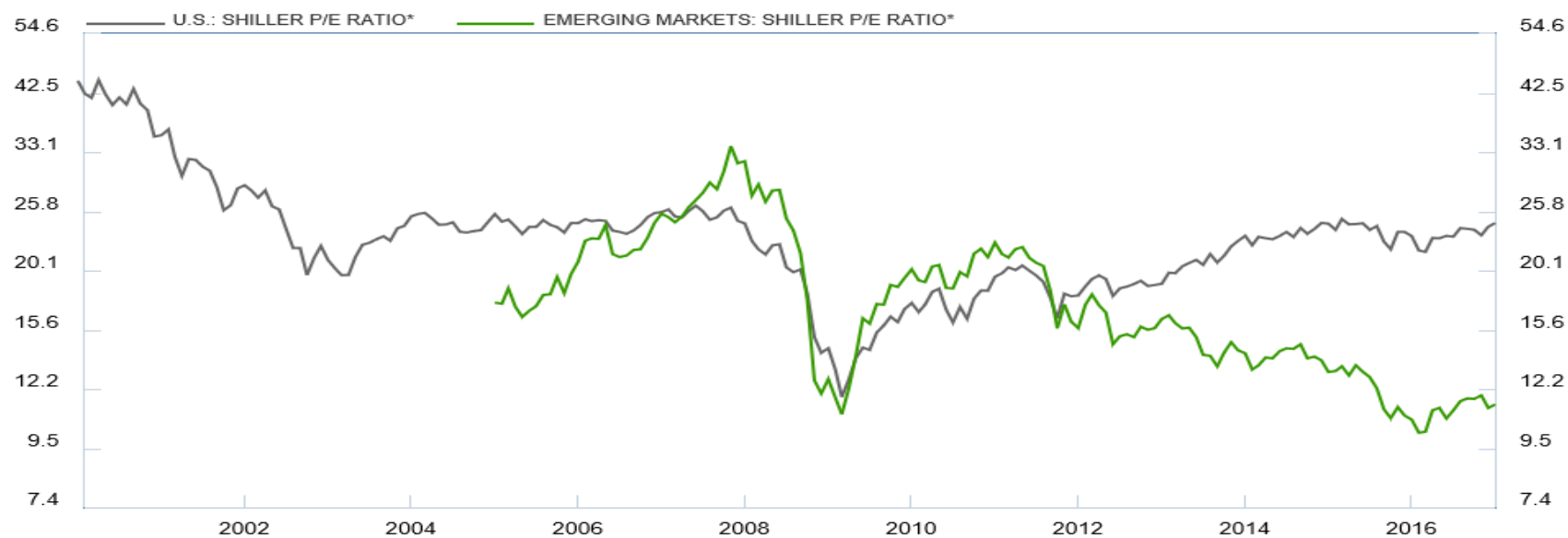


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Region	Current Shiller P/E	Historical Median	Premium/Discount
U.S. Stocks	24.9	19.8	26%
European Stocks	12.5	17.5	-29%

Valuations and Expected Returns for Emerging-Market Stocks are Still Very Attractive

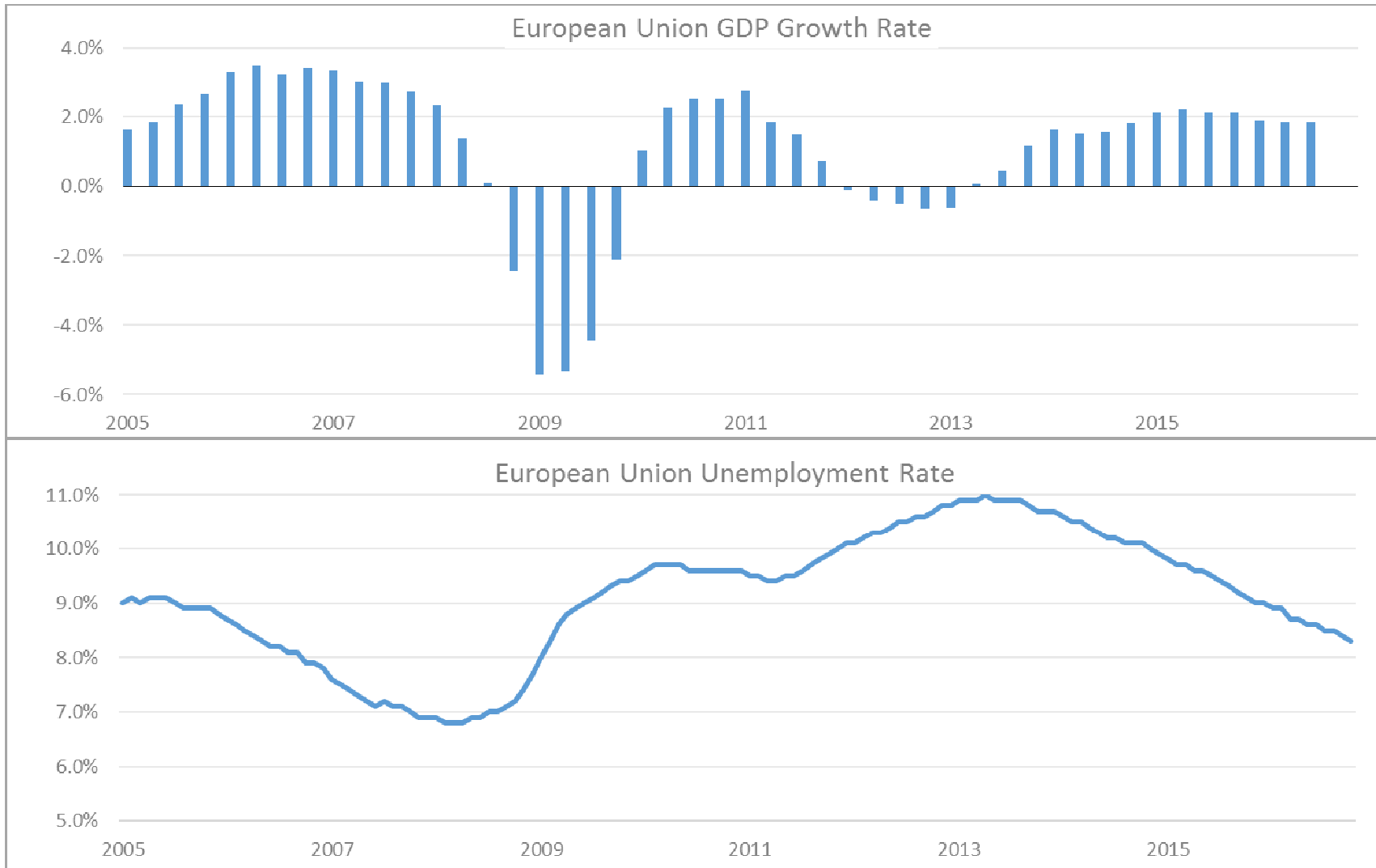
U.S. and EM Shiller P/E Ratios



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* SOURCE: THOMSON REUTERS, OECD MAIN INDICATORS.

Region	Current Shiller P/E	Historical Median	Premium/Discount
U.S. Stocks	24.9	19.8	26%
Emerging-Markets Stocks	11	17.2	-36%

Mild Economic Recovery Continues in Europe



Tactical Investment Outlook

- U.S. Equities: Risk
 - Profit margins are elevated and unsustainable
 - Stocks are pricey and historical outcomes from current valuation levels are not encouraging
 - Rising interest rates: Risk
 - Very low returns expected for core bonds over the next five years
 - Active absolute-return-oriented fixed income managers manage yield and duration
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- International Equities: Opportunity
 - Attractive stock valuations despite recent elevated macro uncertainty
 - Probability is high that market earnings growth will be higher than current depressed levels indicate
 - Alternative strategies: Opportunity
 - Risk-adjusted return potential in up and down equity and bond markets
 - Diversification and a source of return independent from traditional stock and bond markets

Disclosures

Asset Class Descriptions:

Domestic Investment-Grade Bonds (Barclays Capital U.S. Aggregate Bond Index): We are currently using the Vanguard Total Bond Market Index Fund to represent the Barclays Capital U.S. Aggregate Bond Index, an index of domestic investment grade bonds.

Floating Rate Loans (S&P/LSTA Leveraged Loan Index): We are currently using the S&P/LSTA Leveraged Loan Index to represent an index of floating rate loans.

High Yield Bonds (Merrill Lynch U.S. High Yield Master Cash Pay Index): We are currently using the Merrill Lynch U.S. High Yield Master Cash Pay Index to represent an index of domestic high yield bonds.

Domestic Larger-Cap Stocks (S&P 500 Index): We are currently using the Vanguard 500 Index Fund to represent the S&P 500, an index of primarily domestic larger-cap stocks.

Domestic Smaller-Cap Stocks (Russell 2000 Index): We are currently using the Russell 2000 Index iShares Exchange Traded Fund (ETF) to represent the Russell 2000, an index of primarily domestic smaller-cap stocks.

International Developed-Market Stocks (FTSE Developed ex North America Index): We are currently using the Vanguard FTSE Developed Markets Exchange Trade Fund (ETF) to represent an index of international developed-market stocks. Prior to May 2013, this Vanguard Exchange Traded Fund followed MSCI-EAFE. Prior to the July 2007 inception of Vanguard MSCI EAFE ETF, we use iShares MSCI EAFE Index from September 2001 to July 2007, and the MSCI EAFE Index adjusted for 0.35% expenses annually prior to September 2001.

International Emerging-Market Stocks (FTSE Emerging Markets Index): We are currently using the Vanguard FTSE Emerging Markets Index Exchange Traded Fund (ETF) to represent an index of emerging market stocks. Prior to January 2013, this Vanguard Exchange Traded Fund followed the MSCI Emerging Markets Index. Prior to the March 2005 inception of Vanguard MSCI Emerging Markets ETF, we use iShares MSCI Emerging Markets Index from May 2003 to March 2005, and the MSCI Emerging Markets Index adjusted for 0.67% expenses annually prior to May 2003.

Managed Futures: We are currently using an average of the AQR Managed Futures Strategy HV, Natixis ASG Managed Futures Strategy Y and PIMCO TRENDS Managed Futures Strategy.

Arbitrage Strategies: We are currently using an average of the AQR Diversified Arbitrage Strategy (ADAIX) and the Arbitrage Event Driven Strategy (AEDNX).

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