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Market Commentary
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Intro

Equity markets did not give investors any time to get comfortable in 2016. After only six weeks, the S&P 500 had corrected 13.3% from November highs and was down more than 10% for the year on February 11th. Markets suffered from a steady drumbeat of negative news related to China's demise, falling commodity prices, and the possibility of a U.S. recession. Additional toxic ingredients included uncertainty surrounding the Fed, speculation on the negative effects of energy defaults on banks, unusual currency volatility and large sell-offs in high-flying growth stocks that investors fell in love with in 2015. As history has shown over time, market volatility is the price of admission and often creates more opportunities than it takes away.

Domestic Equities

For the first time since the Great Depression the S&P 500 finished positive after falling more than 10% intra-quarter, ending the quarter up 1.4%**.** In the large cap space, last year's darlings like Amazon and Netflix each sold off roughly 25% as a huge disconnect emerged between the economy and the markets. While the U.S. economic backdrop continues to solidify, equity markets have not reflected that. The U.S. economy is growing faster than most of the developed world and the U.S. consumer is riding a wave of positive momentum. Notably, unemployment in the U.S. has declined to pre-recession levels, at 5%, and the early signs of wage growth are emerging. More discretionary income for U.S. consumers will equate to more customers for U.S. businesses.

Over time, improving economic growth, persistently low interest rates, modest inflation and a more stable U.S. dollar will be positives for corporate earnings, which have been poor for consecutive quarters. Eventually, these tailwinds should translate into an increase in stock prices, however patience is required as this process will take time to come to fruition. Looking ahead, stronger corporate earnings will need to materialize before investor apprehensions moderate enough to allow for a widespread reentry into equities. It is our expectation that markets will continue to be volatile for the remainder of 2016.

International Equities

With the expectation that the Federal Reserve would begin raising interest rates at regular intervals and other developed nations moving in the opposite direction by implementing more accommodative policies, the majority of people expected European and Japanese equity markets to outperform. Unfortunately for the majority, that narrative did not play out as the MSCI Europe Index was down -2.5% and the MSCI Japan Index was down -6.5%. Though developed international markets were negative on the quarter, valuations remain attractive relative to U.S. equities and continue to be an important part of a global equity allocation.

Conversely, emerging markets bounced back after three years of pain finishing the quarter up 5.7%. The strengthening dollar and falling commodity prices were significant impediments to emerging markets in 2015. This year, that story has reversed as the dollar has weakened, playing an important role in stabilizing commodity prices and other currencies. Most notably, prices for a barrel of WTI increased 58% from February 11th to March 22nd, which spurred a rally in some of the most beaten down areas of the market. Despite the rally, uncertainty still persists in the commodities and currencies space and it will take more than one quarter to know if this rally is sustainable.

Fixed Income
Bonds were the premiere asset class in the first quarter as the Barclays Intermediate Government/Credit Index finished up 2.5% and the Barclays High Yield Index was up 3.4%. The Fed indicated in December they were set on raising interest rates four times this year which led to a widespread belief that a rising rate environment was finally upon us. However, this was another lesson in humility as the yield on the 10 Year Treasury proceeded to fall from 2.27% to 1.76% in the quarter as fear drove investors into safe-haven government bonds. The market turbulence and global uncertainty sent the Fed a pronounced message that they needed to take their foot off the gas, which has since resulted in the Fed clarifying they will err on the side of caution, making two rate increases in 2016 the most likely result.

The Fed does not want to make a policy mistake that could derail the recent stabilization by tightening too quickly, which leads us to believe the next increase will most likely come in June. If the Fed raises rates gradually over a longer period of time, as expected, focusing portfolios on income can offset the decline in price. We continue to believe we are locked in a "lower for longer" rate environment and are positioning portfolios with intermediate term bonds, as well as less interest rate sensitive bonds represented through an allocation to high yield.

Alternatives
In a quarter characterized by elevated volatility in fixed income and equity markets, alternatives are an important defense mechanism and play a key role in diversification. Our alternative allocations have changed over time but we are currently allocated to three risk management strategies through Market Neutral, Equity Long/Short, and Multi-alternative products. When used appropriately, alternatives serve as invaluable diversifiers by acting in ways that are different than traditional equity and bond markets. We have always believed in the power of alternatives to add further diversification and protect against downside moves.
As an example, in the month of January when the S&P finished down -4.9%, the Credit Suisse Hedge Fund Index was only down -1.4%, providing the diversification benefits we would expect.

Real Estate
After a slowdown in home sales into year end, buying activity picked up modestly to start 2016. Home sales data is volatile from month to month, but the longer term trends are pointing in the right direction and there are a couple of reasons for optimism in a sustainable housing rally. First, it looks like employment gains and looser mortgage financing are starting to have a positive effect on prospective buyers. Second, wage growth is improving, making the prospect of purchasing a home more reasonable for people. As a result, further gains in home sales and home prices in 2016 should be expected.

Conclusion
As the calendar turned over to 2016, investors focused attentively on negative news stories which lead to a rise in investor anxieties and a very uncomfortable first six weeks of the year. From the February lows, the market proceeded to turn on a dime and a snapback equity rally tied to rising oil prices and improving sentiment followed. In our view, however, the negative headlines were overstated, as the U.S. has the ability to weather the perceived risks lingering in the marketplace and the consumer sector is the healthiest it has been in years. Undoubtedly, we anticipated that 2016 was not going to be without challenges, but the U.S. economy remains in a slow and steady state of improvement behind a strong labor market, improving wages, and a resilient U.S. consumer. All of these factors will continue to provide modest improvements for investors.