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CAPITAL ADVISORY SOLUTIONS

Advisory Solutions Monthly Update
February 2017

ASSET ALLOCATION UPDATE

- We recommend a mild underweight to Global Equities and overweight to Fixed Income across models.
- Within the equity allocation, we continue to recommend an overweight to non-U.S. developed equity, concentrated in the growth segment.
- Within the fixed income allocation, we recommend an overweight to U.S. TIPS.

EQUITY HIGHLIGHTS

- International and growth equities led the global equity markets higher in January, which represented a change in market leadership from the U.S. and value equity outperformance that occurred throughout much of 2016. Emerging markets equites were particularly strong during the quarter. U.S. large-cap and mid-cap indexes reached all-time highs in late January. After posting extraordinary gains after the U.S. elections, U.S. small-caps lagged large caps and mid-caps during the month.
- U.S. equity managers generally performed in line their benchmarks in January, with small cap managers generally producing outperformance. International actively-managed equity strategies also started the year strongly, with developed markets and emerging markets managers outperforming on average during the month.
- While international equities outpaced U.S. equites during the first month of the year, U.S. equity relative outperformance has been substantial since the financial crisis. The relative performance of U.S. versus international developed markets equites has tended to move in long cycles over time, with an average duration of 72 months. This current cycle of rolling three-year U.S. equity outperformance began 86 months ago, which suggests mean reversion could be on the horizon.

FIXED INCOME HIGHLIGHTS

- Fixed income markets were largely positive during the month of January. Within the opportunity set, high yield was once again the top performer, returning 1.45%, followed by emerging market debt, which returned 1.25%. Global Treasuries ex U.S. produced the lowest return of -1.06%. The Bloomberg Barclays U.S. Aggregate Bond Index, a proxy for the overall bond market, returned 0.20% during the month.
- Over the month, select international developed 10-year government bond yields increased, led by Italy and France. The 10-year U.S. Treasury yield was unchanged at 2.45%.
- Municipal/Treasury yield ratios moved lower for shorter-dated maturities and higher for longer-dated maturities. Ratios remain near historical averages across the curve.

Stock Indexes	YTD	Bond Indexes	YTD	Other Indexes	YTD	U.S. Treasury Yields		Rates/Commodities	
Russell Global	2.69%	Barclays US Aggregate	0.20%	60% LgShort-40% MktNeutral	1.38%	6-month	0.64%	Prime Rate	3.75%
Russell 3000	1.88%	Barclays Gbl Treas xUS Hdg	-1.06%	DJ Equity All REIT	0.14%	1-year	0.84%	LIBOR (3 Mo)	1.03%
S&P 500	1.90%	Barclays US TIPS	0.84%	Bloomberg Commodity	0.14%	3-year	1.46%	Oil Price ($/barrel)	$52.81
MSCI EAFE	2.90%	Barclays US High Yield	1.45%			5-year	1.90%	Gold ($/t oz)	$1,211.40
MSCI EM	5.47%	Barclays EM Aggregate	1.25%			10-year	2.45%		
						30-year	3.05%		

Data as of 01.31.2017; Source: Morningstar, FactSet, Russell Investments, Barclays, U.S. Department of Treasury

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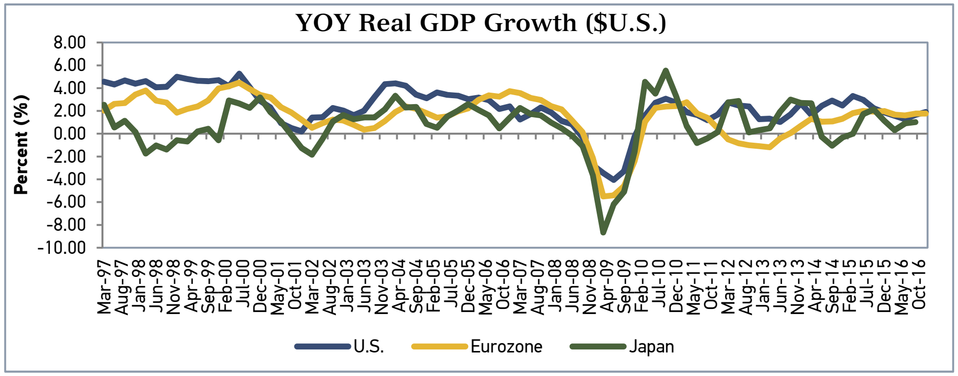
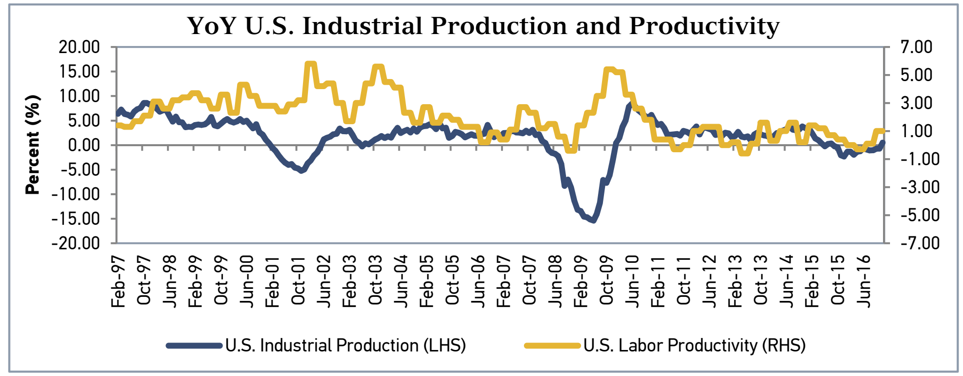
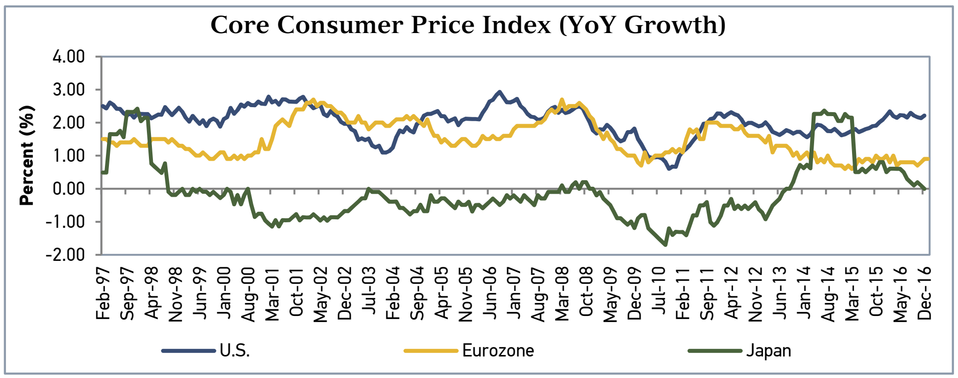
Global Economic Snapshot



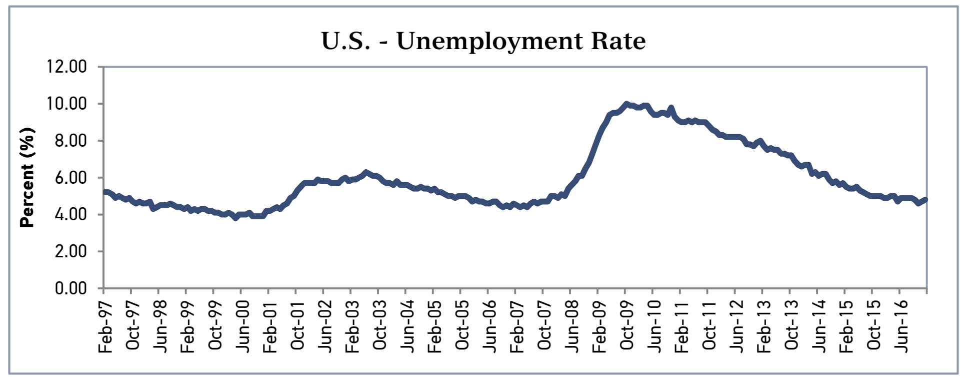
Japan data as of 09.30.2016. U.S. and Eurozone data as of 12.31.2016. Source: FactSet



Industrial Production as of 12.31.2016; U.S. Labor Productivity as of 12.31.2016; Source: FactSet



U.S. data as of 12.31.2016; Eurozone data as of 01.31.2017. Japan data as of 12.31.2016; Source: FactSet
The sudden increase in Japan CPI growth in 2014 coincided with an increase in national sales tax that impacted final price levels.



Data as of 01.31.2017; Source: FactSet

- U.S. GDP growth held steady in the fourth quarter of 2016 but remains tepid. The Eurozone has closed the growth gap to the U.S. and Japan growth has gradually improved.
- U.S. productivity showed further improvement in the fourth quarter but generally remains low. Continued productivity gains are essential to drive long-term real growth.
- Core inflation has slowly increased toward Fed target levels and Eurozone inflation is showing signs of picking up. Deflation remains a threat in Japan.
- Tightening U.S. labor markets suggest more inflation pressure that is likely to lead to further Fed rate hikes.

Note: Please see Appendix for important definitions.

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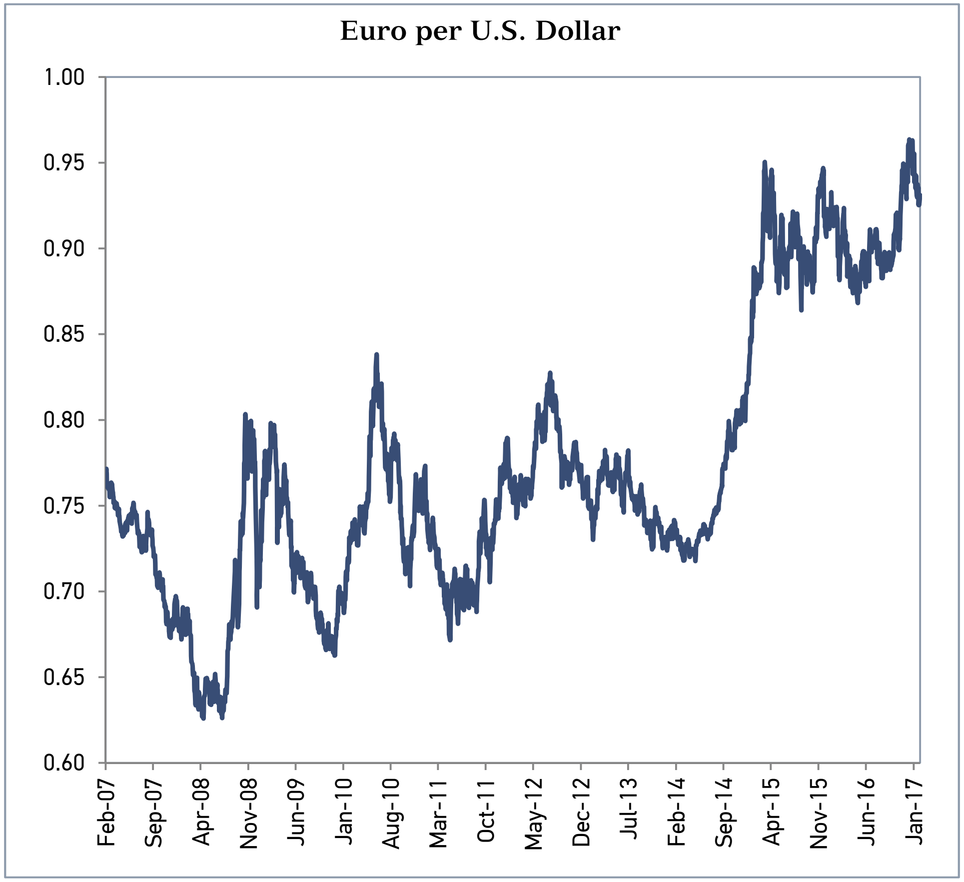
U.S. Economic Indicators

Leading — Coincident — Lagging

Initial Jobless Claims	• In the week ending February 4, the four-week moving average of Initial Jobless Claims was 244,250 – a decrease of 3,750 from the Initial Jobless Claims previous week's revised average.
Manufacturing	• ISM Manufacturing registered 56.0% in January, an increase of 1.5 percentage points from the prior month. A reading below 50.0% indicates contraction. • ISM Manufacturing New Orders registered 60.4% in January, 0.1 percentage points above the December reading. • ISM Non-Manufacturing registered 56.5% in January, 0.1 percentage points lower than the December reading.
Housing/Construction	• Building permits increased 1.3% in December and have increased 2.2% over the past year.
Consumer Confidence	• The Consumer Confidence Index decreased in January to 111.8 compared to 113.3 in December.
Nonfarm Payrolls	• Total nonfarm payroll employment increased by 227,000 in January. The unemployment rate was little changed at 4.8%.
Industrial Production	• Industrial Production rose 0.8 % in December and is up 0.5% over the past year.
Personal Income	• Real Disposable Personal Income increased 0.1% in December, and is up 2.1% over the past year.
Ratio of Consumer Installment Credit to Personal Income	• This ratio rose 0.09% in December, and is up 2.9% year-over-year. Consumer borrowing tends to lag improvements in personal income by many months because people remain hesitant to take on new debt until they are sure that their improved income level is sustainable.
Inflation	• CPI (All Items) rose 0.3% in December and is up 2.1% over the trailing one year period. CPI (Core) increased 0.2% in December, and is up 2.2% over the trailing one-year period.

Source: FactSet

Currency



- The Traded-Weighted U.S. Dollar Index (Major Currencies) fell 2.7% in January and the index is down 2.7% year-to-date. The dollar depreciated 2.4% versus the euro in January.

Data as of 02.06.2017; Source: FactSet

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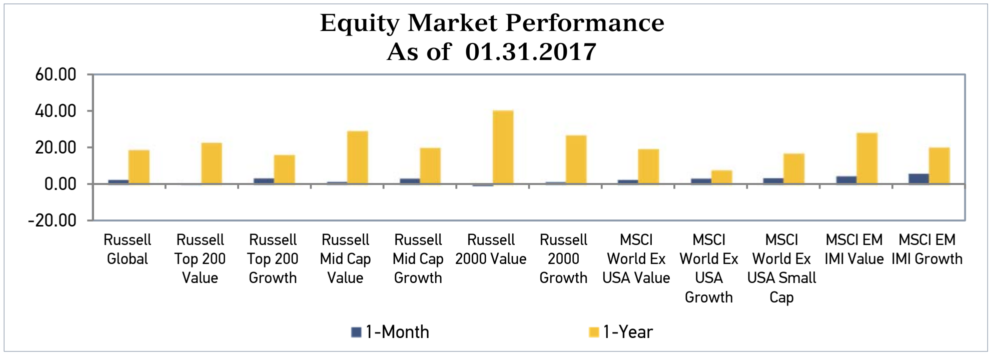
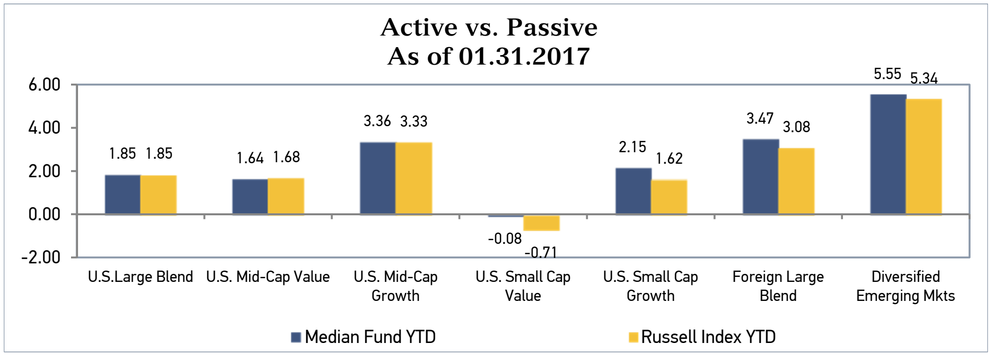
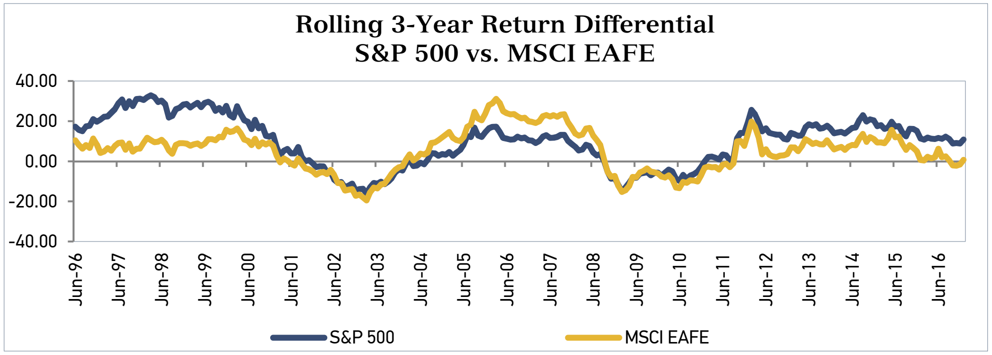
Global Equity Markets



Source: Morningstar, Russell Investments



Source: Morningstar, Russell Investments
Median return of Morningstar open-end fund category (institutional share class). Russell return of U.S. categories.



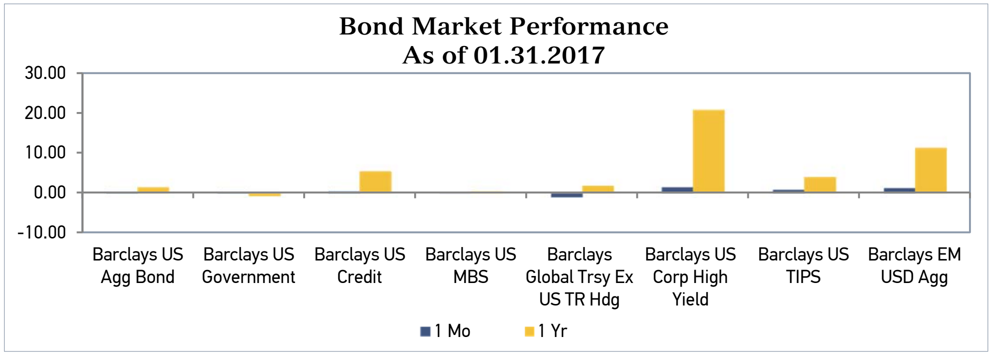
Data as of 01.31.2017; Source: Morningstar

- International and growth equities led the global equity markets higher in January, which represented a change in market leadership from the U.S. and value-led equity rally that occurred throughout much of 2016. Emerging markets equites were particularly strong during the quarter, as U.S. dollar weakness played a role in emerging markets relative strength during the month. After posting extraordinary gains after the U.S. elections, U.S. large-cap and mid-cap indexes reached all-time highs in late January, with the Dow Jones Industrial Average surpassing 20,000 for the first time. U.S. small-caps lagged large caps and mid-caps during the month. The information technology sector, which didn't fully patriciate in the post-election rally, was the top performing segment of the U.S. equity market during the month.

- U.S. equity managers generally performed in line their benchmarks in January, with small cap managers generally producing outperformance. International actively-managed equity strategies also started the year strongly, with developed markets and emerging markets managers outperforming on average during the month.

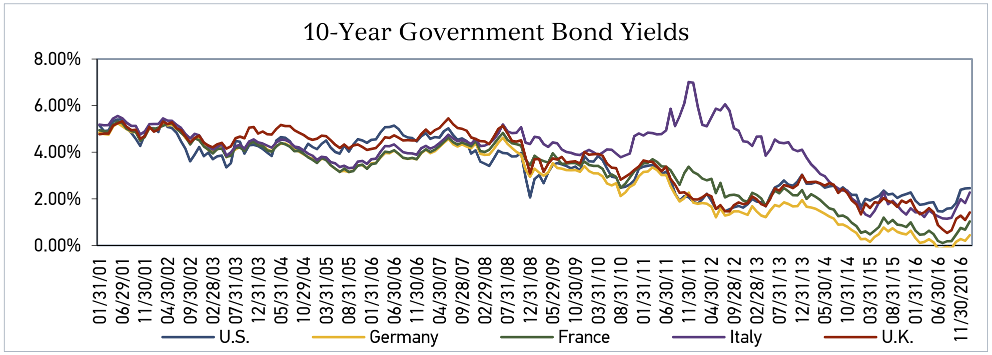
- While international equities outpaced U.S. equites during the first month of the year, U.S. equity relative outperformance has been substantial since the financial crisis. The relative performance of U.S. versus international developed markets equites has tended to move in long cycles over time, with an average duration of 72 months. This current cycle of rolling three-year U.S. equity outperformance began 86 months ago, which suggests mean reversion could be on the horizon.

Fixed Income Markets



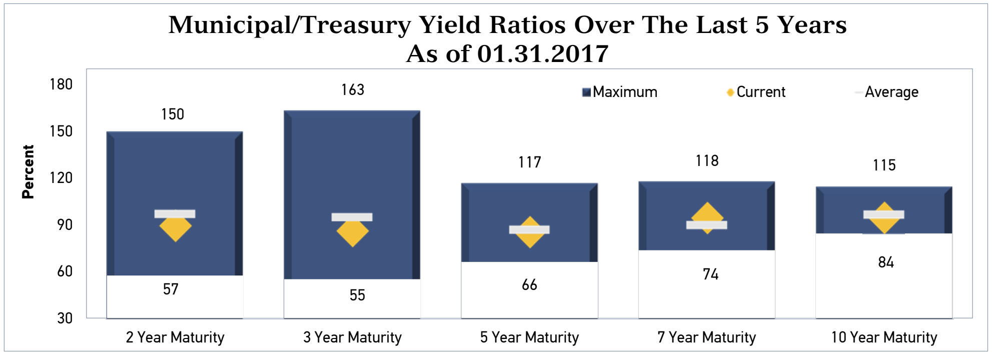
Source: Morningstar, Barclays

- Fixed income markets were largely positive during the month of January. Within the opportunity set, high yield was once again the top performer, returning 1.45%, followed by emerging market debt, which returned 1.25%. Global Treasuries ex U.S. produced the lowest return of -1.06%. The Bloomberg Barclays U.S. Aggregate Bond Index, a proxy for the overall bond market, returned 0.20% during the month.



Data as of 01.31.2017; Source: FactSet, U.S. Department of Treasury

- Over the month, select international developed 10-year government bond yields increased, led by Italy and France. The 10-year U.S. Treasury yield was unchanged at 2.45%.



Source: Thompson Reuters; Sterling Capital Management Analytics.

- Municipal/Treasury yield ratios moved lower for shorter-dated maturities and higher for longer-dated maturities. Ratios remain near historical averages across the curve.

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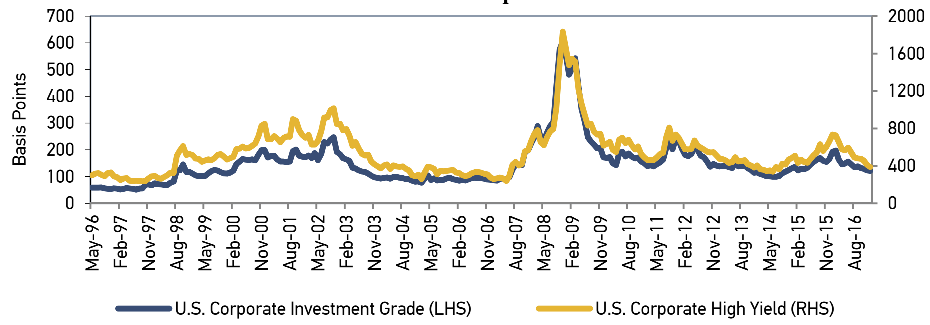
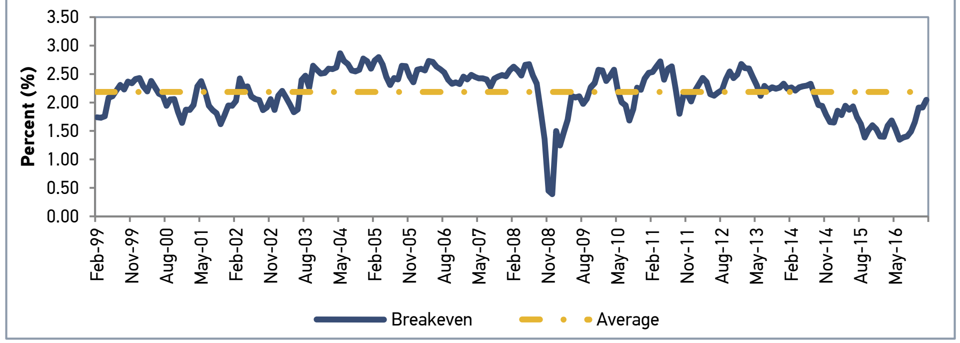
Fixed Income Spreads and TIPS Breakeven

20-Year U.S. Corporate OAS



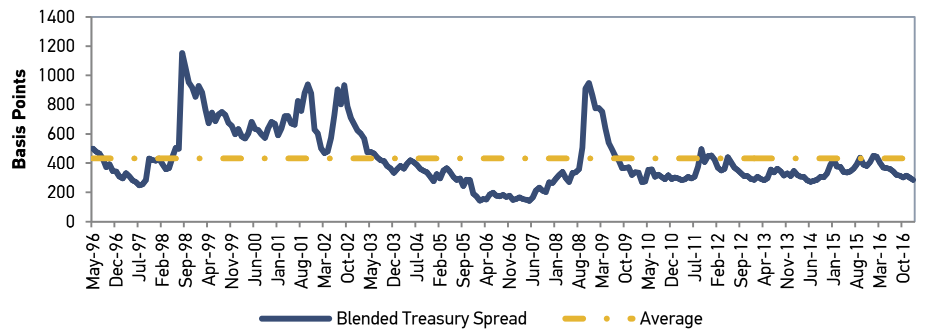
Data as of 01.31.2017; Source: FactSet

10-Year TIPS Breakeven



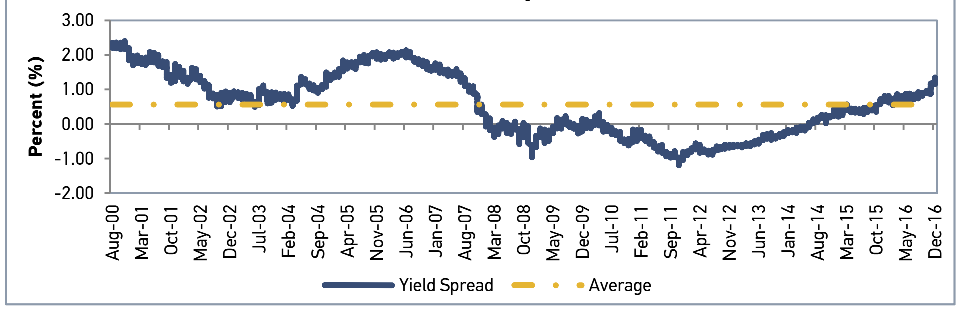
Data as of 01.31.2017; Source: Federal Reserve Board of Governors

EM Debt OAS



Data as of 01.31.2017; Source: Barclays

Yield Spread of Barclays U.S. Treasury Index to Global Ex-U.S. Treasury Index

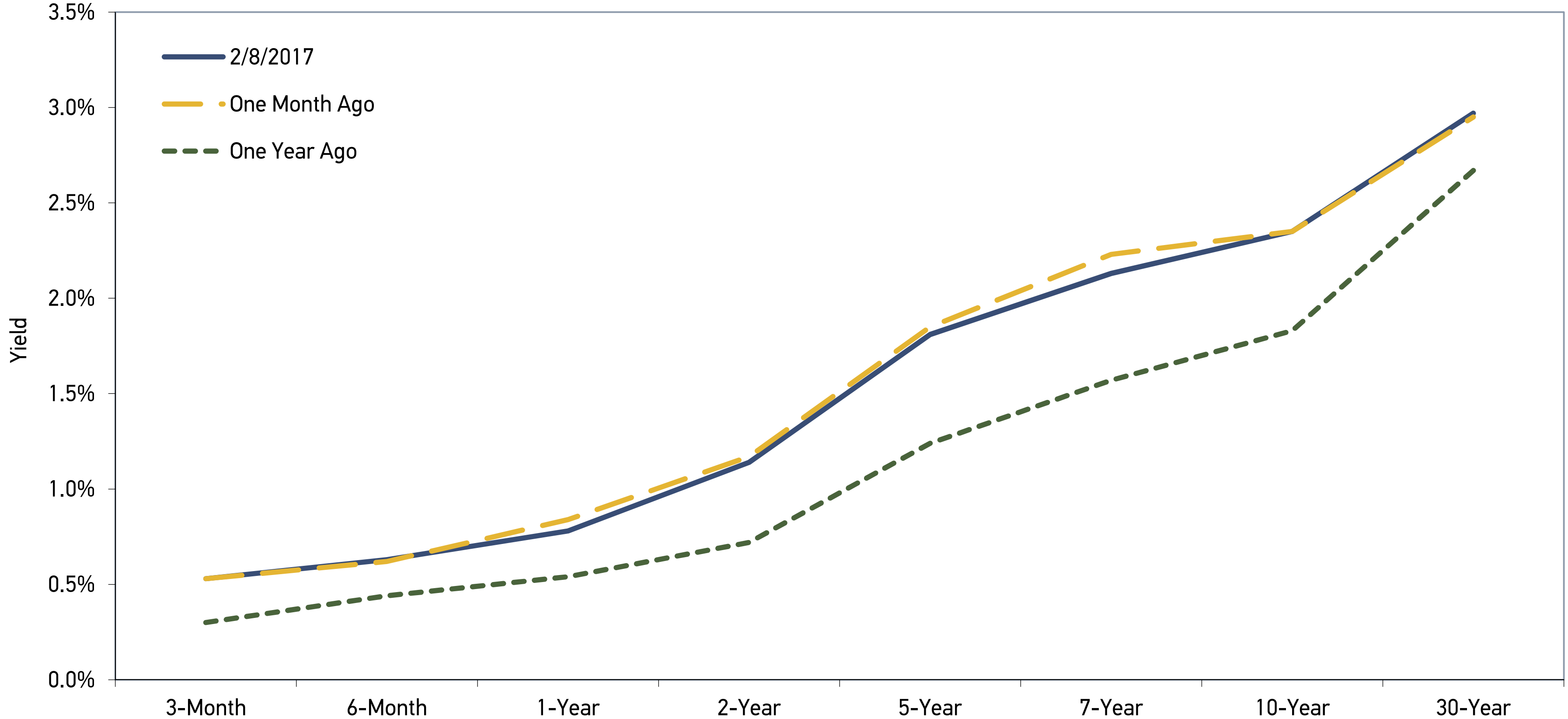


Data as of 01.31.2017; Source: Barclays

- Corporate credit spreads have continued to decline from the wide levels of early 2016 and are below historical averages.
- Market inflation expectations as measured by TIPS breakeven rates have increased significantly in recent months and are approaching long run averages.
- Emerging market spreads have moved below their historical average, while the yield spread of U.S. to Global Treasuries has moved slightly above the historical average.

Note: Please see Appendix for important definitions.

U.S. Treasury Yield Curve



- Month-over-month, yields were mostly higher across the curve with the front-end seeing the largest increase.

Data as of 02.08.2017; Source: FactSet

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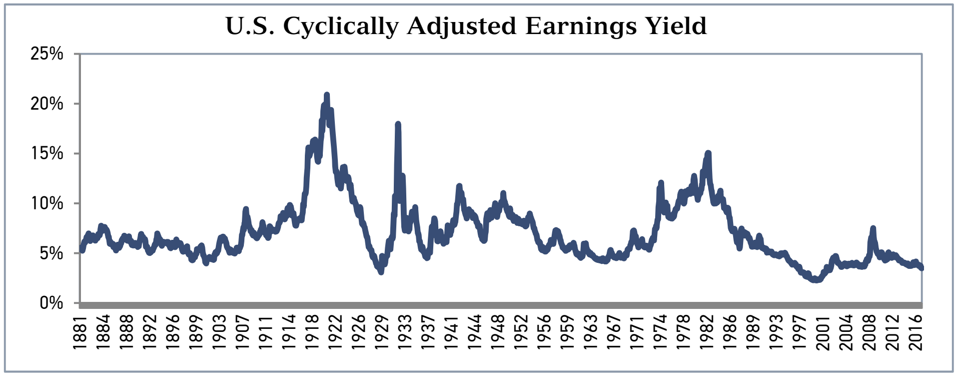
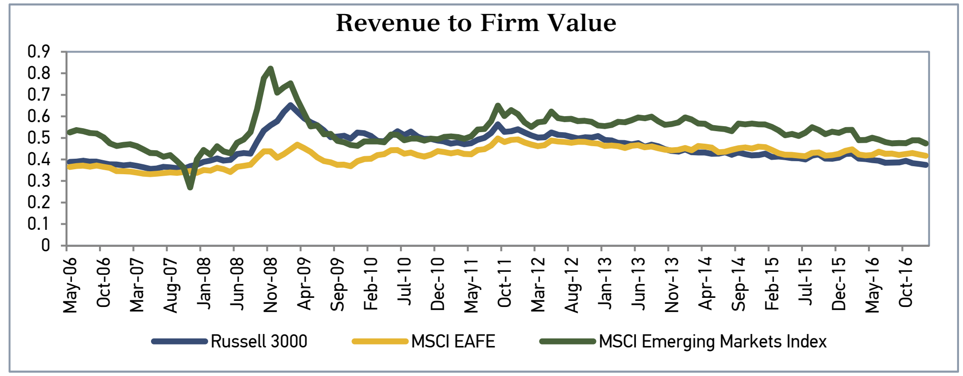
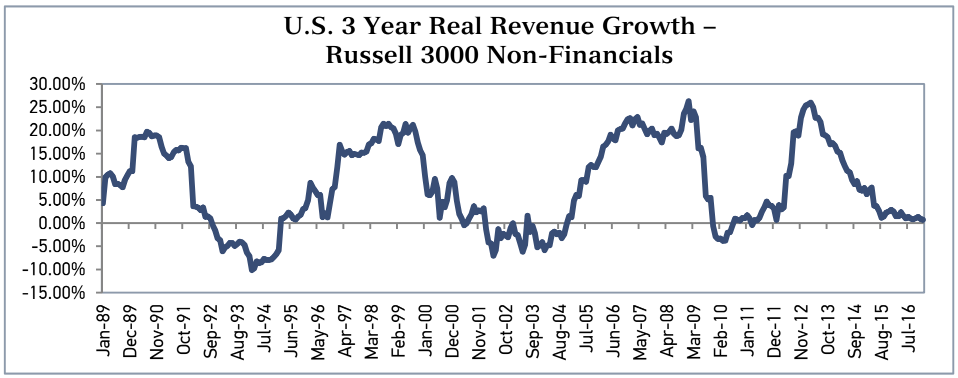
Global Equity Market Fundamentals



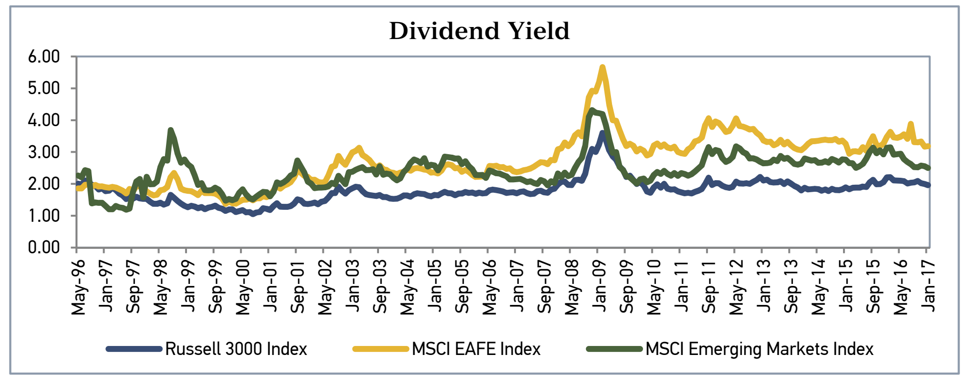
Data as of 01.31.2017; Source: Online Data Robert Shiller "US Stock Markets 1871-Present and CAPE Ratio"



Data as of 01.31.2017; Source: Russell, MSCI



Data as of 01.31.2017; Source: FactSet, Russell, Bureau of Labor Statistics, Sterling Capital Analytics



Data as of 01.31.2017; Source: Russell, MSCI

- The U.S. cyclically adjusted earnings yield continues to slowly decline and is well below longer-term averages, while real U.S. sales growth continues to be weak.
- Revenue to firm value in the U.S. has moved below international developed markets. The emerging markets' ratio is only slightly higher than developed markets.
- International developed equities provide a significant dividend yield advantage over emerging market and U.S. equities.

Note: Please see Appendix for important definitions.

Appendix

Definitions

Core Consumer Price Index: Core inflation is a measure of inflation that excludes certain items, usually food and energy, that face volatile price movements.

Option Adjusted Spread (OAS): A bond's yield spread over comparable maturity government bonds, adjusted for any embedded options.

Real GDP: Real gross domestic product (GDP) is an inflation-adjusted measure that reflects the value of all goods and services produced by an economy in a given year, expressed in base-year prices.

Revenue to Firm Value: Total Index Revenues of the past 12 months divided by the sum of equity market value and the value of total debt. This is a measure of total sales generated on the total value (debt plus equity) of firms in the index.

TIPS Breakeven: The inflation rate implied by the spread in yield between U.S. TIPS (Treasury Inflation Protected Securities) and nominal U.S. Government Bonds of equal maturity.

U.S. 3 yr. Real Revenue Growth, Russell 3000 Non-Financials: For the Russell 3000 excluding financial firms, the percentage change in trailing 12-month inflation adjusted revenue over 12-month inflation adjusted revenue three years prior.

U.S. Cyclically Adjusted Earnings Yield: The 10-year average of annual, inflation adjusted earnings divided by the current inflation adjusted price of the S&P 500 index. This measure is the inverse of the Shiller CAPE Ratio.

YOY US Productivity Growth: The year-over-year growth in real U.S. output produced per hour worked for non-farm workers.

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