MARKET COMMENTARY **October, 2015**

Q3 Market Overview

The third quarter 2015 ended with the S&P 500 index down 6.4%, the worst quarterly decline since 2011. The poor market returns for domestic equities unfolded against a backdrop of weak global economic growth. The global economy is in a soft patch, reflecting a significant slowdown in demand from one of the world's growth engines, China, and related concerns over weak emerging market debt and currencies. Concurrently, there remains high anxiety in financial markets over the Federal Reserve's widely anticipated decision on whether and when to raise interest rates.

There are two prongs to the debate over a Fed rate hike. First, there is a concern that the domestic economy has not yet normalized enough to sustain a rate hike. It is a widely held view that the Fed is on the brink of raising rates, having been held artificially low since 2009 to stimulate demand. Yet other influential policy makers and economists argue that rates are not inappropriately low. Monetary velocity remains anemic and money is not flowing out the fed discount window to banks and through banks to the rest of the economy. Despite historically low banking spreads (the difference between banks borrowing and asset earning rates), deposits are flowing into banks but not out of banks as loans to spur growth.

In reality, as Hoover Institute economist John Cochrane says, "The Fed isn't doing much of anything. Lots of deposits (saving) and a dearth of demand for investment (borrowing) drives (real) interest rates down and there is not a whole lot the Fed can do about that. Except to see the parade go by, grab a flag, jump in front and pretend to be in charge."

The second part of the debate is a heightened uncertainty over how the global economy and markets will react to Fed tightening. The Fed's decision to leave rates unchanged during the quarter did little to resolve investor concerns. As a result investors remain pessimistic and have pulled over $110 billion from equity mutual funds year to date 2015, while flows into bonds funds offering historically paltry rates have been strongly positive.

The New Normal: Lower for Longer

We believe that global growth will remain moderate and below historic norms. We do not anticipate a recession but rather slower growth, low inflation, low rates, a strong dollar, and lower oil and commodity prices over the extended horizon. Finally, we believe Fed bias will be for stimulative monetary policy for considerably longer, with global policy makers continuing to pull out all the stops to counter slow global growth and demand.

The end result for the third quarter, 2015, was an equity market correction in August/September that reached negative 12%. All in, by historical standards, the decline would be considered an average late summer correction, exacerbated as usual by hyperbole in the financial press pointing to a high level of perceived investor fear and specific sector volatility. Interestingly, it is noted that the market has already recovered about half of the third quarter losses.

Market and Sector Volatility

In the third quarter, 2015, commodity exposed sectors fared most poorly with energy and materials declining 18% and 17%, respectively. Underlying commodity prices were weak and oil fell most of all commodities, down 25%. Healthcare, an area that has enjoyed strong returns recently, declined with biotech particularly weak, down 14% in the quarter. Given the level of fear which accompanied the market swoon, it isn't surprising that higher quality and larger cap stocks performed better than the averages in what appears to be a flight to quality. Our investments, outside of energy, some healthcare and energy infrastructure generally participated in this flight to quality.

Dividends: The long term investment story often obscured by near term volatility

Some investors argue that there are only two important data points in the life of an investment: the purchase price and the selling price. We would add there is a third important data point over the life of an investment holding: the income stream. We thought this quarter, with the amount of money lost on paper in a very short period of time in energy related equities, a reminder on of the importance of the relative contribution of dividends in long term investments might be in order to put the near term price pressure in perspective.

Equity/MLP	Original Investment Value @ 12.31.06	Current Investment Value @ 10.9.15	Cumulative Dividend Income	Total Cumulative Wealth	% of Total Return Derived from Dividend
Coca Cola	$100,000	$174,173	$34,942	$209,115	32%
Enterprise Products	$100,000	$198,611	$73,004	$271,615	43%
Exxon	$100,000	$103,434	$23,046	$126,481	87%
Kimberly Clark	$100,000	$176,111	$36,237	$212,347	32%
Occidental Petroleum	$100,000	$157,062	$34,227	$191,290	37%
Pepsi	$100,000	$159,053	$28,342	$187,395	32%
Pfizer	$100,000	$128,340	$32,741	$161,081	54%
Plains All American	$100,000	$131,203	$70,581	$201,784	69%
United Technologies	$100,000	$152,497	$25,784	$178,281	33%

Notes: This chart is for education purposes only. It does not represent your specific portfolio. The chart represents a theoretical $100,000 investment in each of the securities listed above in January 2007. The $100,000 is then valued at market on October 9, 2015. The cumulative dividends from 2007-2014 are listed in the "dividend income" column. Finally, the column "total wealth" is the value of the equity position on October 9, 2015 plus the cumulative dividend income from January 2007 through December, 2014. Source: Dividends.com and Thomson Reuters and Advent. This is a select list of companies, does not reflect all holdings and portfolios. All information is pre-tax. Past results are not a predictor of the future.

The investment horizon for this table is January 2007 until the end of the October 9, 2015. This period includes the financial meltdown of 2008/2009 and the historically significant decline of MLP's and energy stocks in the third quarter of 2015. Despite the volatility in the sector during the holding period, MLPs kept pace or outperformed the consumer staples (usually seen as bell-weathers in volatile markets) on the strength of their outsized distributions.

Moreover, across the board, this table reflects the resiliency of long term investments in dividend paying stocks even when the principal investment is volatile (inevitable to all investments held for the long term). In each case the dividend accounted for over 30% of the wealth creation, and for over 50% in some cases. It is noted that this analysis only includes dividends from 2007-2014. Dividend income to date is actually materially higher. This is just a reminder of why we focus our investments on disciplined returners of shareholder capital.

Conclusion: Investors Who Stay the Course Should be Rewarded

Given the current environment, there are no good alternatives to investing in equities. Money market and treasury bonds are delivering next to nothing. There are a lot of high quality companies selling at attractive valuations, good dividend yields, and not particularly expensive in today's world. These are the companies that we own in our portfolios. If the consensus estimate for 2016 S&P 500 operating earnings is anything close to the mark, the S&P 500 is trading at only about 15.5 times next year's earnings.

The new normal is very positive for equities – modest growth, low rates, low inflation, and low commodity prices, all over a longer time frame. Yet investors, deeply scarred by the global financial crisis, remain frightened and mistrustful. It will take time for trust and risk tolerance to come back. It took a generation to return after the great depression of the 1930's.