SLOW GLOBAL GROWTH IMPLYING CONTINUED POLICY ACCOMODATION

After a choppy September, equity market volatility moderated in October as tepid GDP numbers stoked expectations of extended policy accommodation by the world's central banks.

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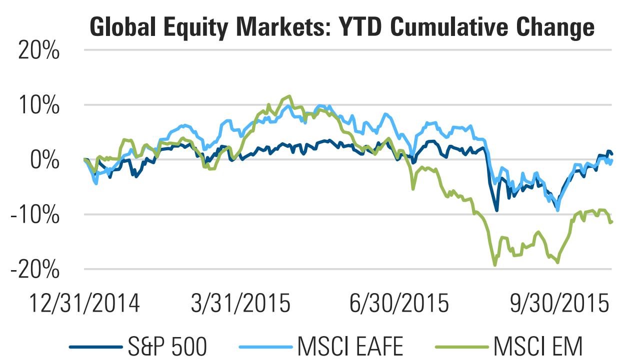
OCTOBER RECOVERY PUSHES US EQUITIES BACK INTO POSITIVE TERRITORY YEAR TO DATE

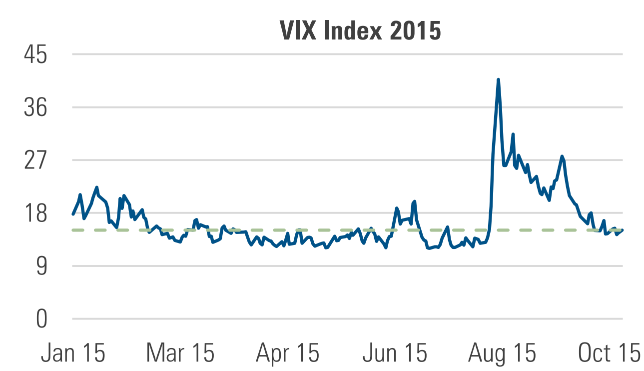
October 2015 marked the S&P 500 Index's fifth best October on record dating back to 1950. After falling nearly 7% in Q3, the index rose 8.3% in October, bringing it back into the black year-to-date:

Figure 1



Volatility subsided in October, reverting back near to the levels seen prior to the late-August spike:

Figure 2

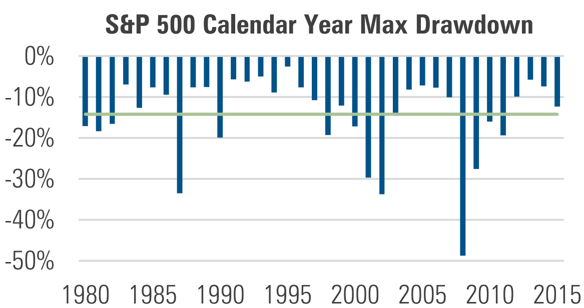


MANAGED VOLATILITY PORTFOLIOS

During October, we estimate that a typical managed volatility growth portfolio saw its net equity exposure gradually increase, doubling from approximately one-third at the end of September to approximately two-thirds by the end of October. As volatility moderated off a multi-year high, the reduction in portfolio hedges provided increasing exposure to the market's steady upward climb.

In the US, 2015's max drawdown of -12.4% on the S&P 500 marks the largest in a calendar year since 2011. Its place in recent memory may make it seem large, but it's actually smaller than the historical average. Looking back to 1980, the average calendar-year max drawdown of the S&P 500 is -14.2%. Equally noteworthy is that over the same timeframe, the index finished each calendar year an average of 10% higher than it started the year, and 21% higher than its intra-year low.

Figure 3



Drawdowns like these offer useful reminders that while equity markets carry the potential to generate attractive returns, they also carry risk of significant downturns along the way. For investors in or nearing retirement, significant and extended drawdowns can have a devastating effect on portfolios, reducing either their lifespan or the potential rate of withdrawal. In these situations, risk-managed equities offer a way to maintain exposure to the growth potential of equities while seeking to mitigate participation in down markets.

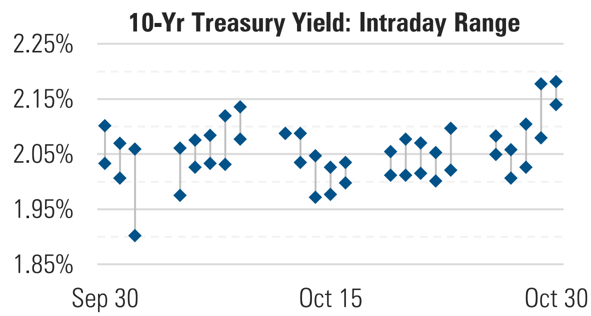
MARKET COMMENTARY

After one of the poorer quarterly performances in recent memory, global markets rallied in October, recovering much of the ground they had lost year-to-date, but still finishing the month below their 2015 highs:

Index %Δ	S&P 500	MSCI EAFE	MSCI EM
Q3 2015	-6.9%	-10.7%	-18.5%
October 2015	8.8%	7.0%	6.8%
YTD	1.5%	-0.9%	-11.5%

Interest rates were largely unchanged for most of the month, with the yield on the 10-yr Treasury trading in a narrow range below 2.10%:

Figure 4



It wasn't until after the FOMC meeting at the end of the month that rates began to breakout to the upside. Data from Morningstar show October 2015 to be the fourth largest month over the last 10 years for inflows into taxable bond ETFs. Much of the flow was into intermediate and longer-term bond ETFs, suggesting investors aren't currently overly concerned about rising rates.

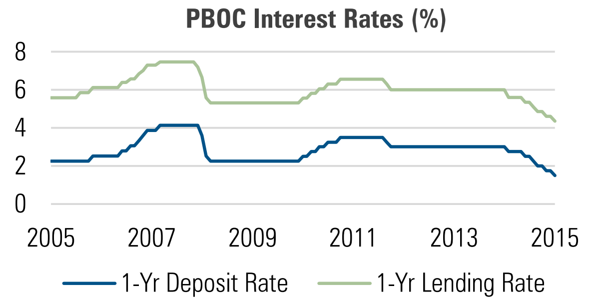
CHINA'S POLICY ADJUSTMENTS OFFER A WINDOW INTO ECONOMIC REALITY

The Chinese government reported that its economy grew at an annualized rate of 6.9% during Q3, substantially lower than the 10% rate it reported just five years ago.

In Q3, in response to slowing growth, the Chinese government devalued the yuan by 3% and intervened in its declining stock market. In October, those measures were followed up with an easing of monetary policy and a remarkable change in China's one-child policy to now allow couples to have two children.

In addition to the October reduction of the reserve requirement ratio for banks, the People's Bank of China (PBOC) reduced the one year deposit and lending rates for the fifth time in 2015, pushing the rates below their levels during the financial crisis:

Figure 5

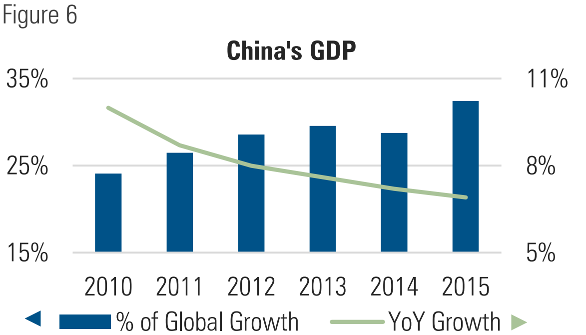


Notwithstanding the reliability of the economic data coming out of China, these significant policy changes seem to, at the very least, validate the slower growth being reported; they likely also leave at least some observers wondering if the growth isn't perhaps even slower than the numbers indicate.

As the world's second largest and fastest growing economy, China has long been a driver of the world's economy. In spite of its slowing growth, China's contribution to global growth has climbed over the last decade.

Now accounting for nearly 20% of the world's population and one-third of global GDP growth, China's slowing economy along with its policy responses have disproportionate implications on the world economy.

Figure 6



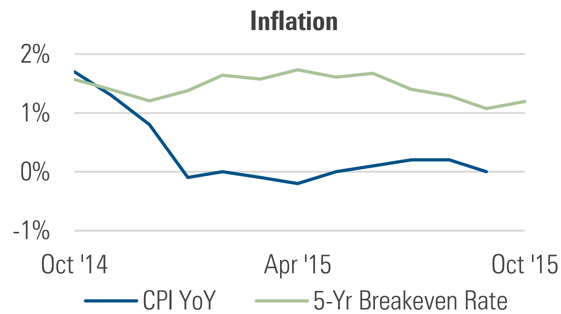
On a nominal basis since 2000, imports into the US from China have increased more than 500%, and more than 260% relative to US GDP. Notably, the reduction of short-term interest rates and devaluation of the yuan in China will make Chinese imports cheaper and generate downward pressure on prices in the US.

For a Federal Reserve in search of any hint of rising inflation and eager to pounce on any opportunity to raise the fed funds rate, the policy adjustments coming out of China offer little help.

MARKETS CONTINUE TO TREAT NEWS OF WEAKNESS AS GOOD NEWS

GDP data released in October showed that the US economy grew by 0.4% in Q3, or 1.6% on an annualized basis. The rate of unemployment remains at 5.1%, but the labor participation rate continues to inch downward. The latest reading of CPI shows it was unchanged in September and remains at the same level it was at a year ago. Inflation expectations remain low:

Figure 7



Much of October's market rally may be attributable to investors' expectation that the Fed would stand pat at its October meeting. Having done just that, the Fed's next meeting in December will be its last chance in 2015 to increase the fed funds rate. At the end of October the Fed press release noted:

*In determining whether it will be appropriate to raise the target range at its **next meeting**, the Committee will assess progress…toward its objectives of maximum employment and 2 percent inflation. This assessment will take into account a wide range of information, including measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on **financial and international developments**.*

By attaching such a narrow time frame ("next meeting") to its discussion of raising the target range, and by linking it to "financial developments," the Fed diminishes its credibility. In the absence of any inflation, a hike in December would be reason for market participants to question the Fed's independence and commitment to its mandate. This would contribute to market uncertainty and a diminished appetite for risk.

Against that backdrop and the prospect for higher volatility, we expect risk management will remain a critical component to portfolio management in the weeks and months ahead.

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