FIRST QUADRANT

GLOBAL MARKET OUTLOOK

Max Darnell, Managing Partner,
Chief Investment Officer

GLOBAL MARKET OUTLOOK

Framework for thinking about state of financial markets

Key indicators

What this means today

What this framework misses

MARKET STATES VARY FROM FRAGILE TO RESILIENT

Fragile Markets

Markets are most fragile when investors are nervous and when the economy is weak. Asset prices are more vulnerable to negative news or events when fragile.

Resilient Markets

Markets are most resilient when investors are confident and when the economy can better withstand shocks. Asset prices will tend to bounce back more quickly after initial negative reactions to news or events when resilient.

MARKET STATES VARY FROM FRAGILE TO RESILIENT

Fragile
Markets

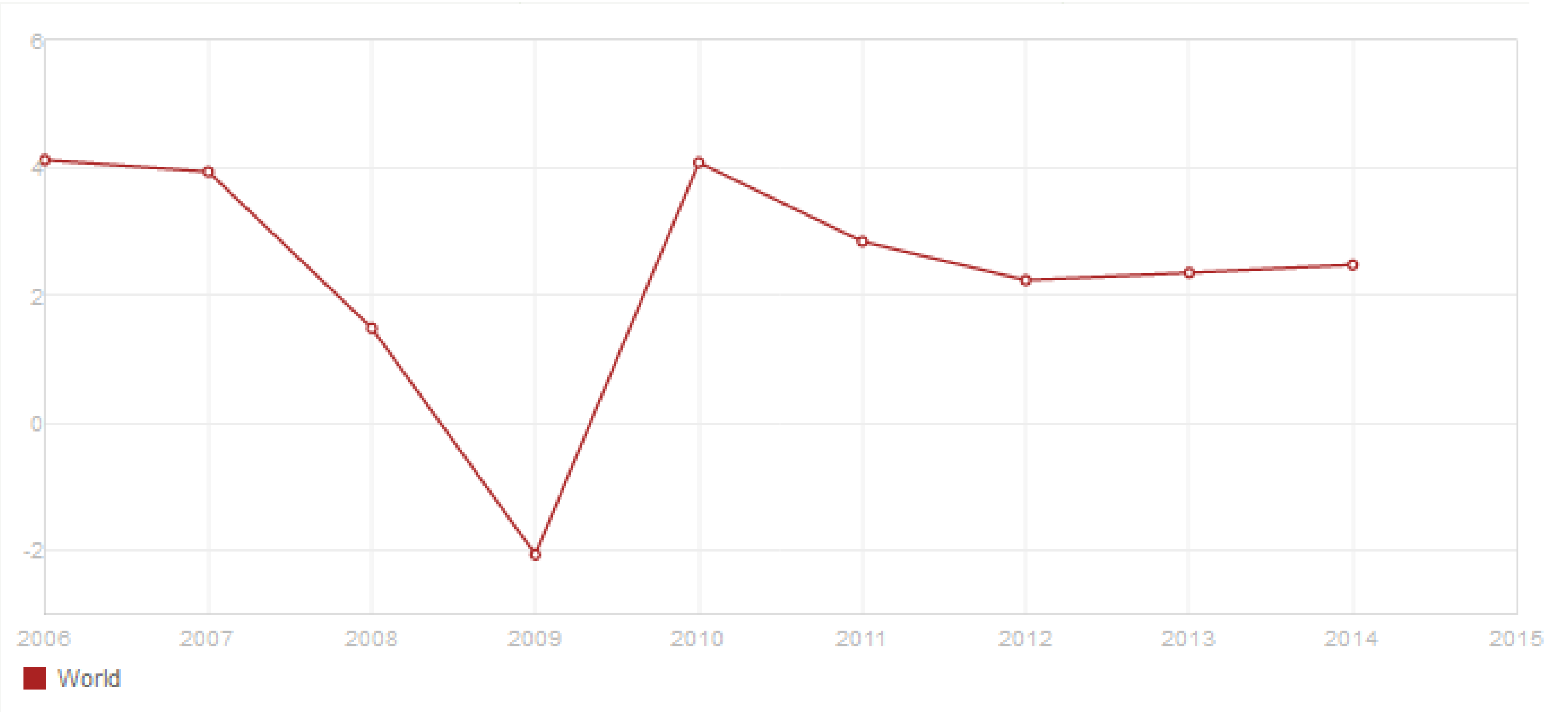
Resilient
Markets

This is not a forecast of returns

This is a measure of how markets would likely react in the face of bad news

SLOW GLOBAL GROWTH RELATIVE TO PRE-CRISIS

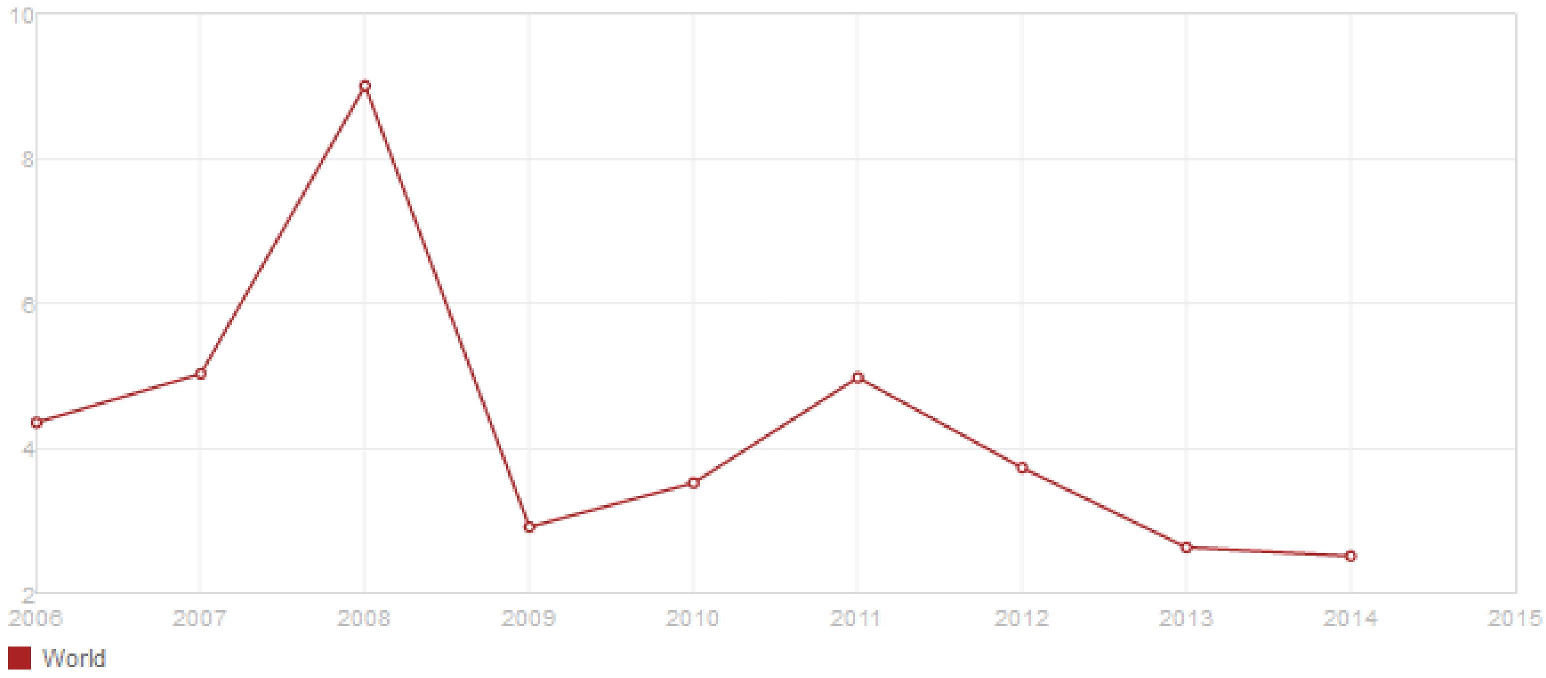
GPD Growth (annual %)



Source: The World Bank

STILL NO SIGNS OF WORRISOME INFLATION GLOBALLY

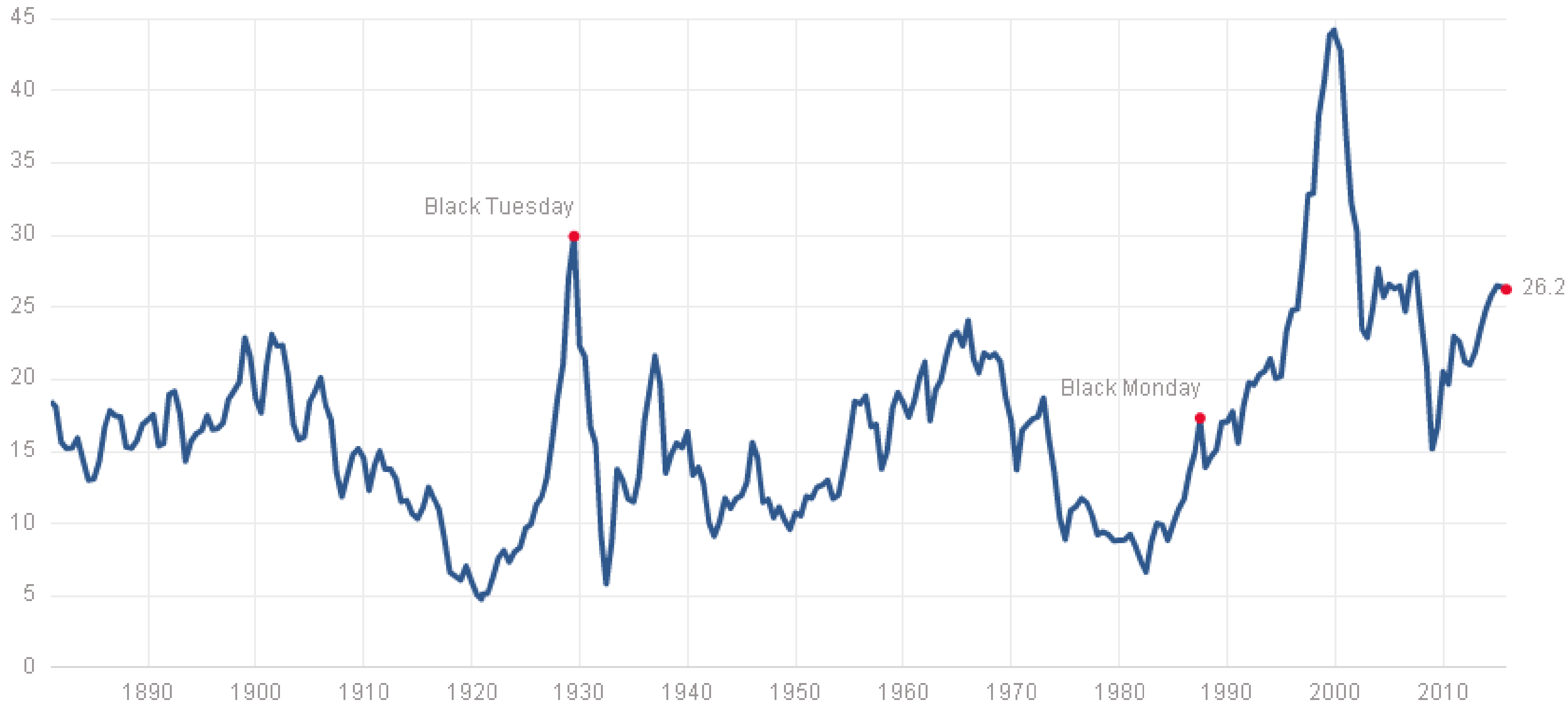
Consumer Price Inflation (annual %)



Source: The World Bank

US STOCKS CERTAINLY NOT CHEAP

Shiller PE Ratio



Source: http://www.multpl.com/shiller-pe/

MODEST CURRENT PRICES FOR "FINANCIAL INSURANCE"

S&P 500 options prices below median

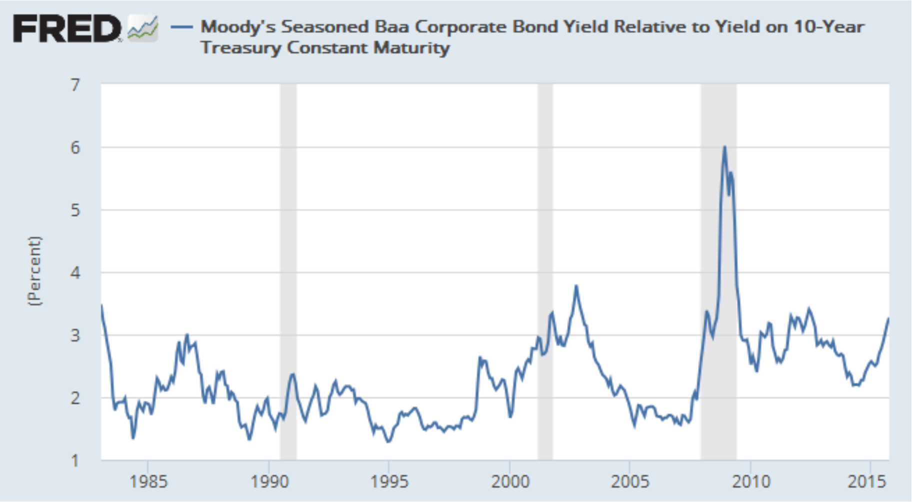
Gold options prices near median

Oil options prices above median

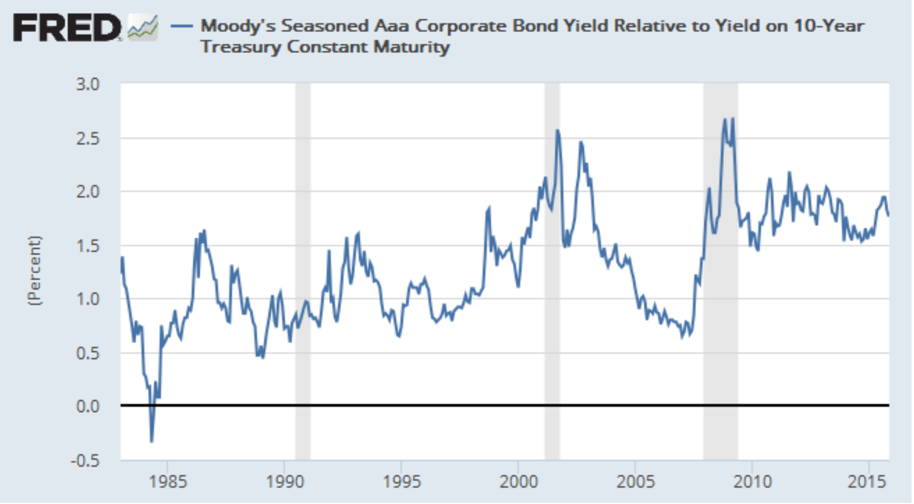
Source: Google Finance (VIX, GVX, OVX)

MODEST CURRENT PRICES FOR "FINANCIAL INSURANCE"

Low-end investment grade bonds reflecting concern

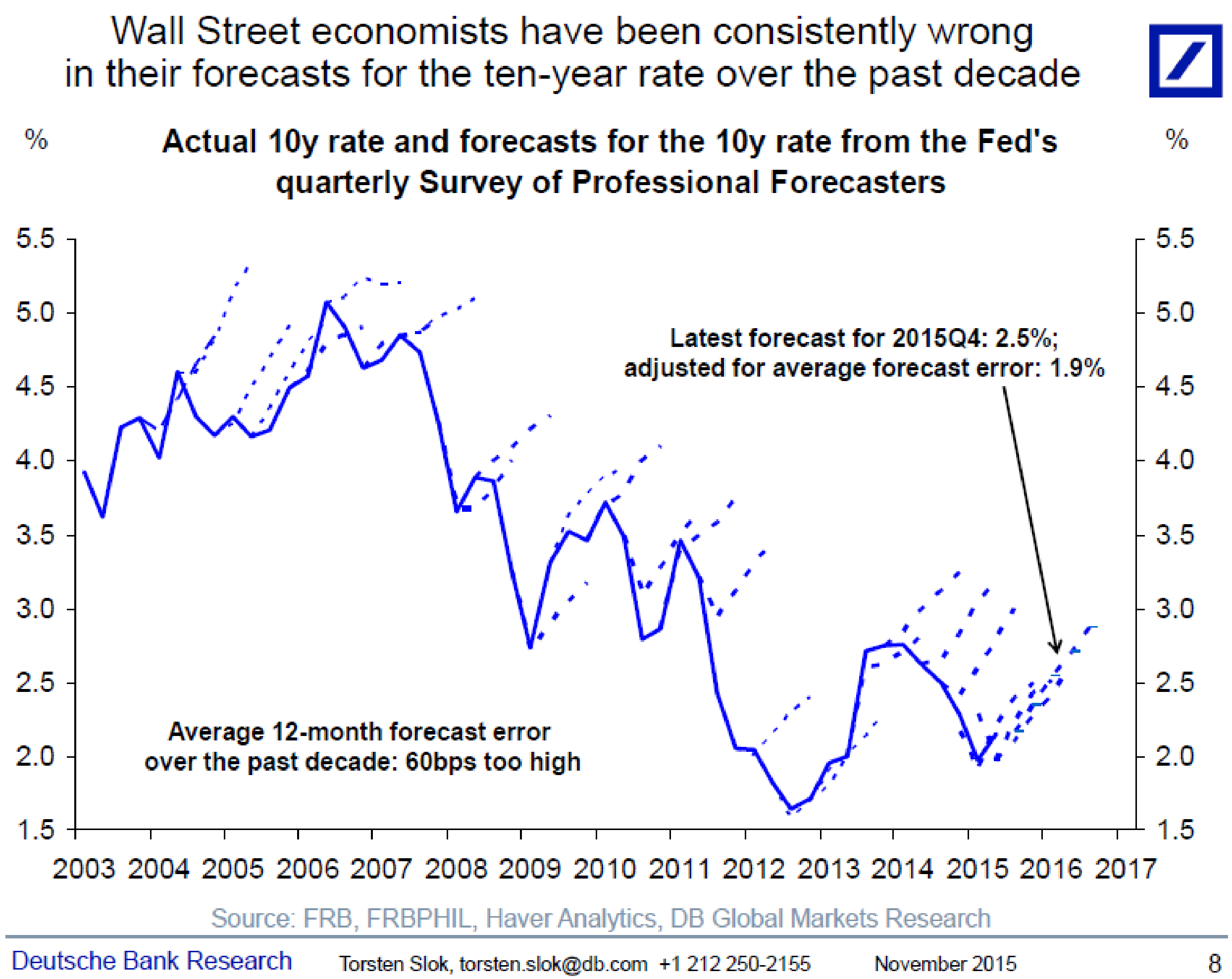


High-end investment grade bonds also reflecting concern



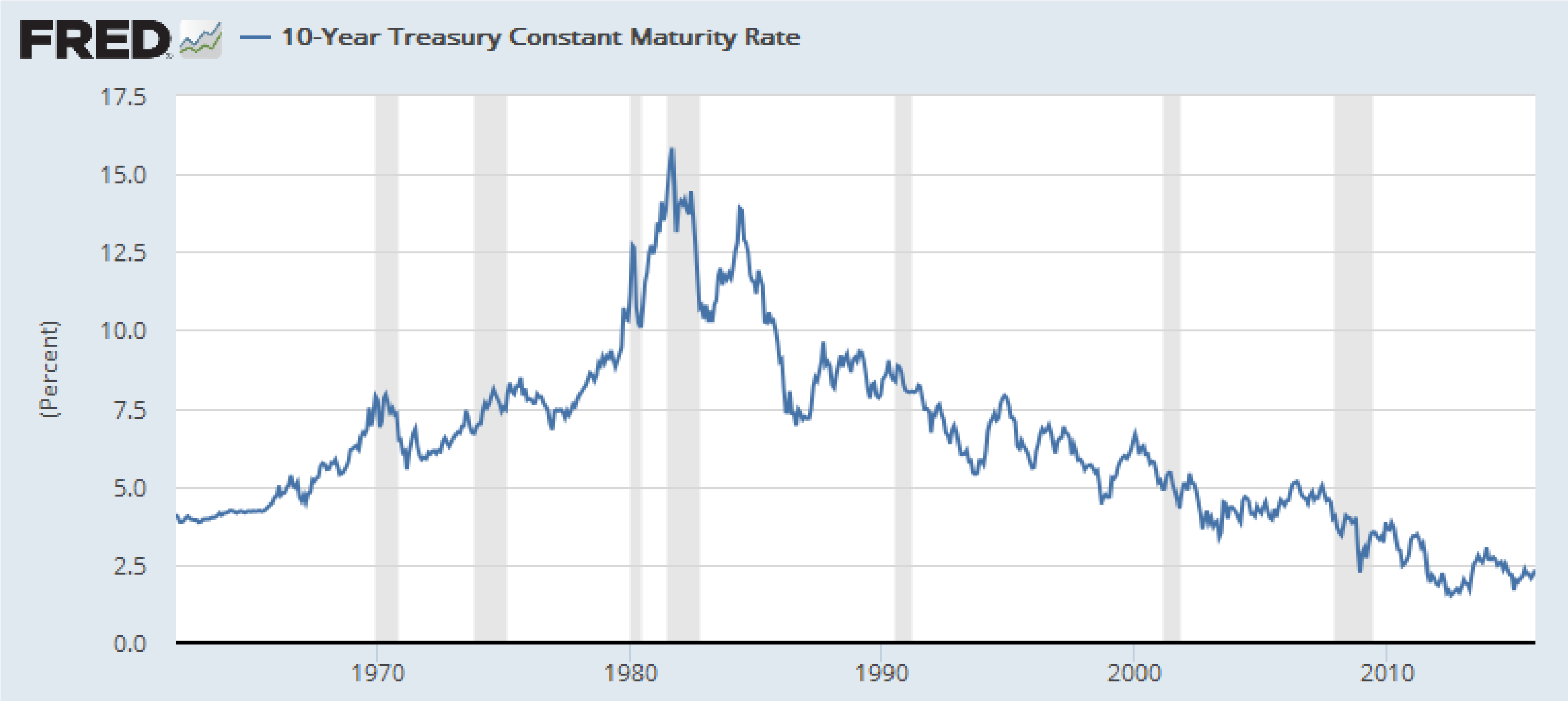
Source: Federal Reserve Bank of St. Louis

FORECASTING BOND YIELDS IS EASY. *HA!*



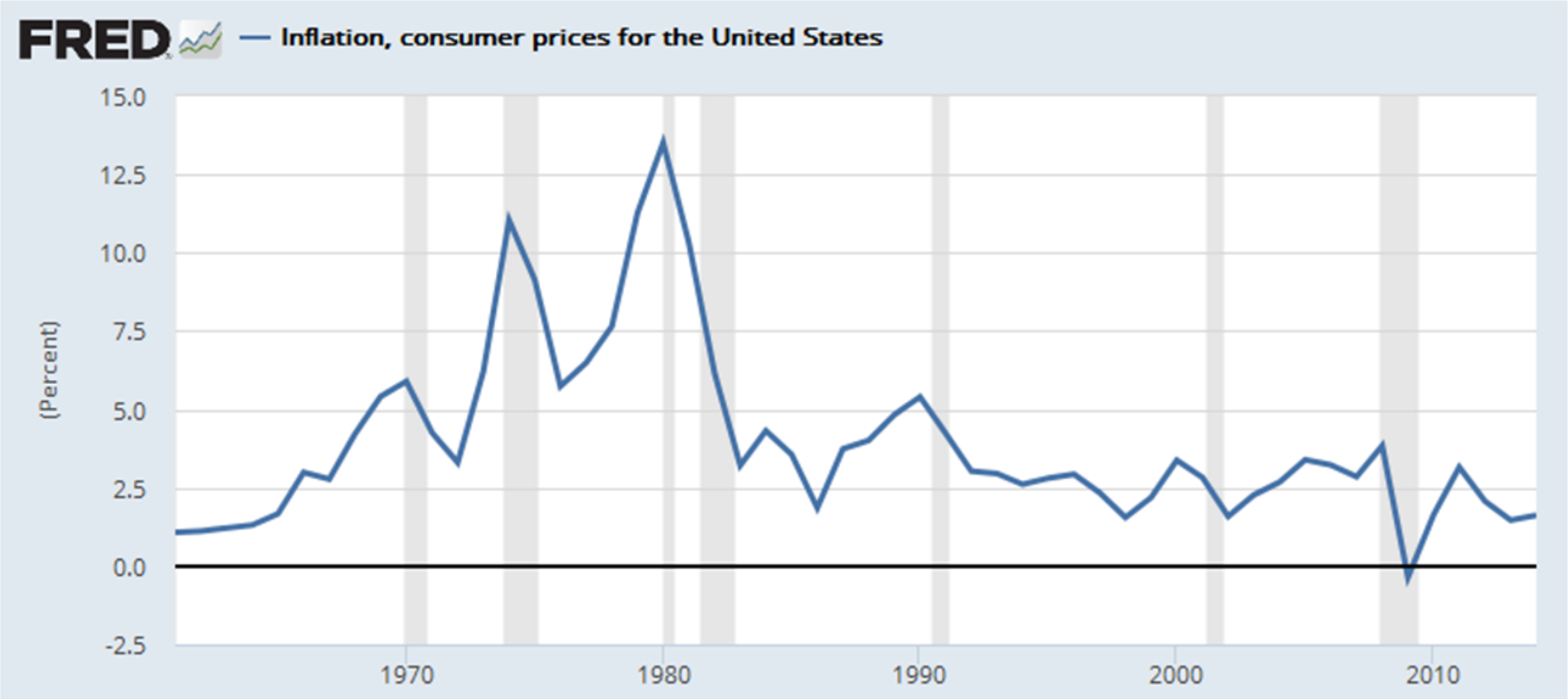
Source: Deutsche Bank Research - FRB, FRBPHIL, Haver Analytics, DB Global Markets Research

HARD TO ADJUST TO NEW REALITY?



Source: Federal Reserve Bank of St. Louis

BASIS FOR LOW YIELDS



Source: Federal Reserve Bank of St. Louis

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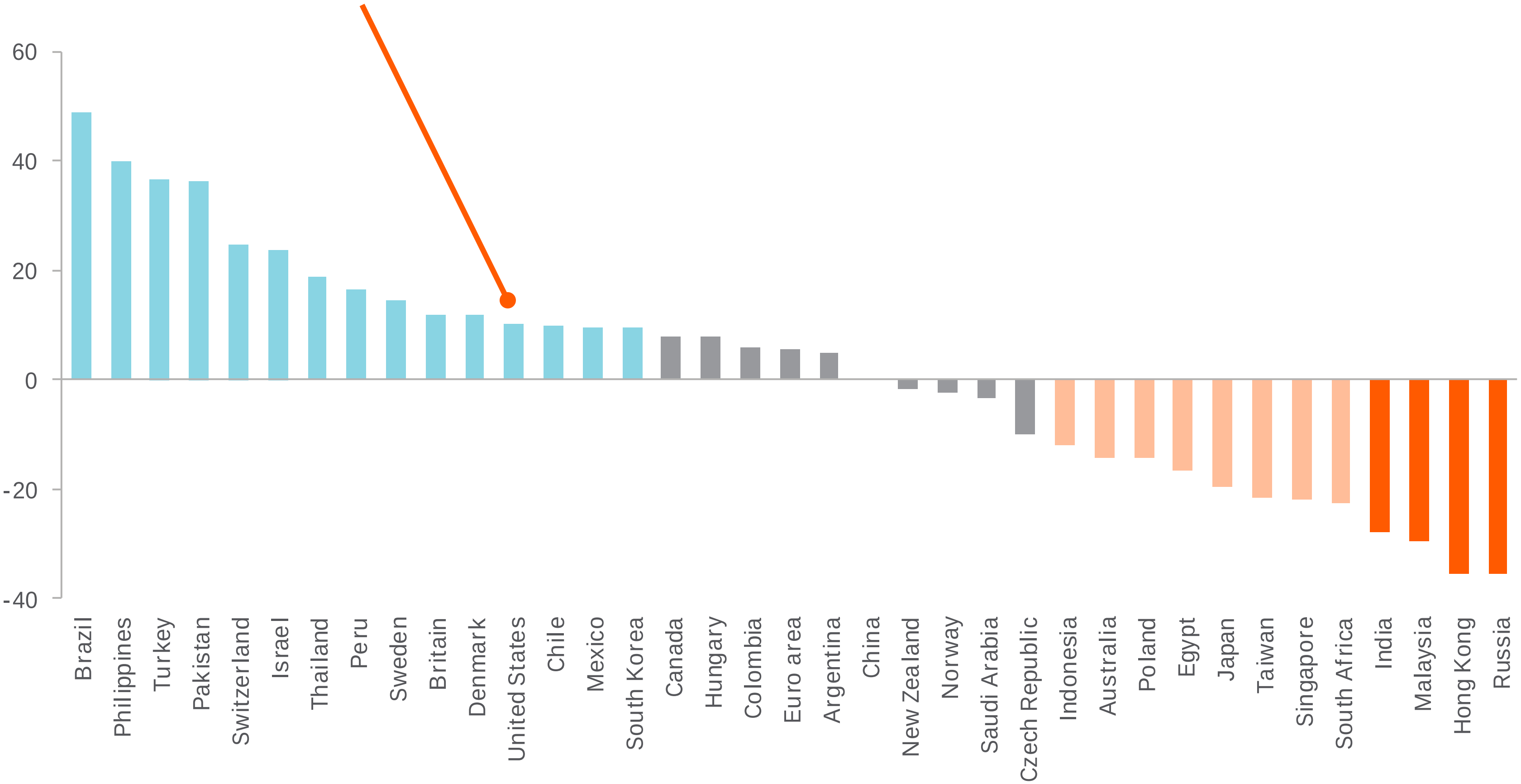
STRONG DOLLAR?

JULY 2015

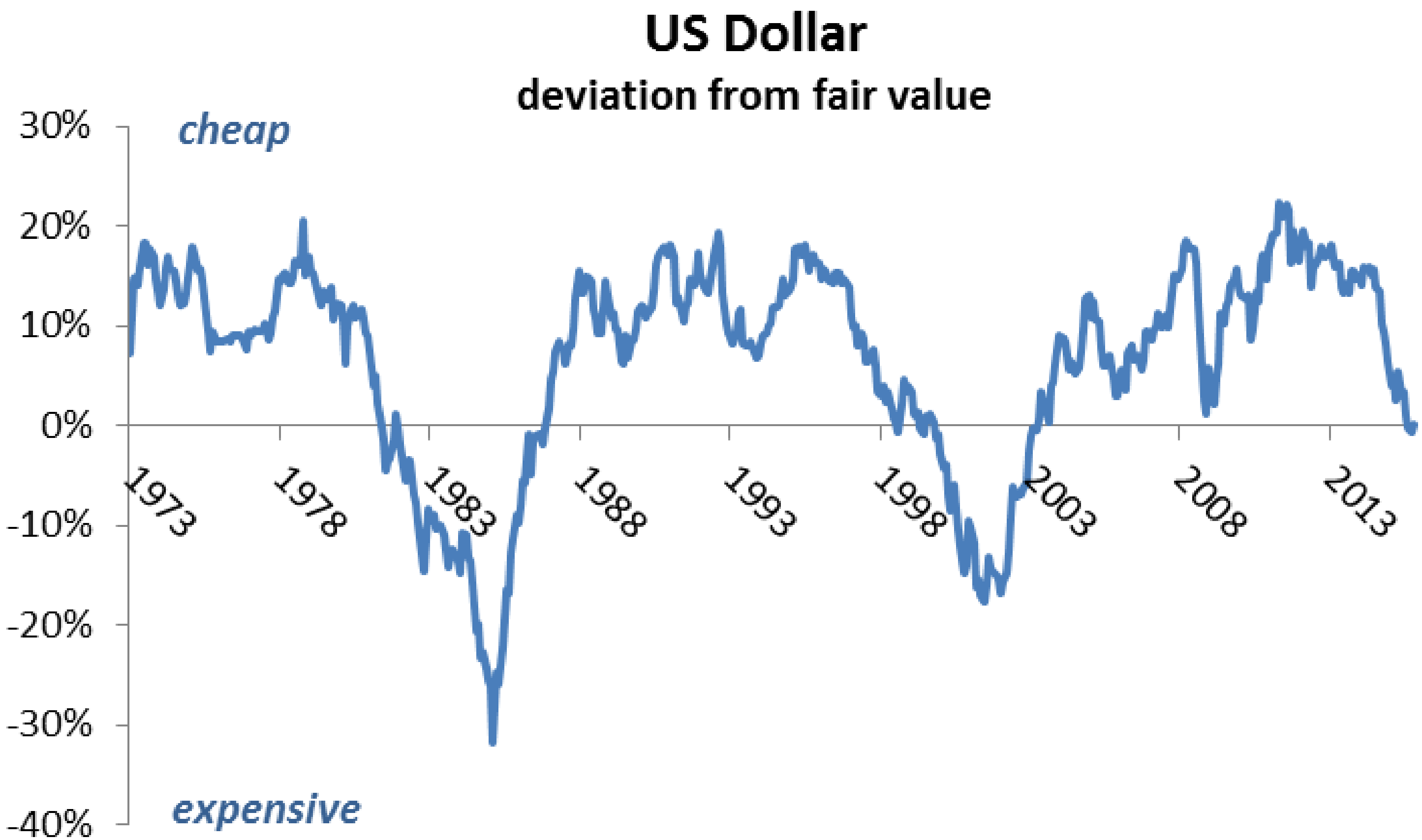
US Dollar has plenty of room to rise from here



At market exchange rate

Source: The Economist, Big Mac Index adjusted for GDP per person (July 2015)

BIG DOLLAR RALLY HAS LEFT DOLLAR FAIRLY VALUED



Source: First Quadrant, proprietary PPP model comparing US dollar valuation against developed world currency basket

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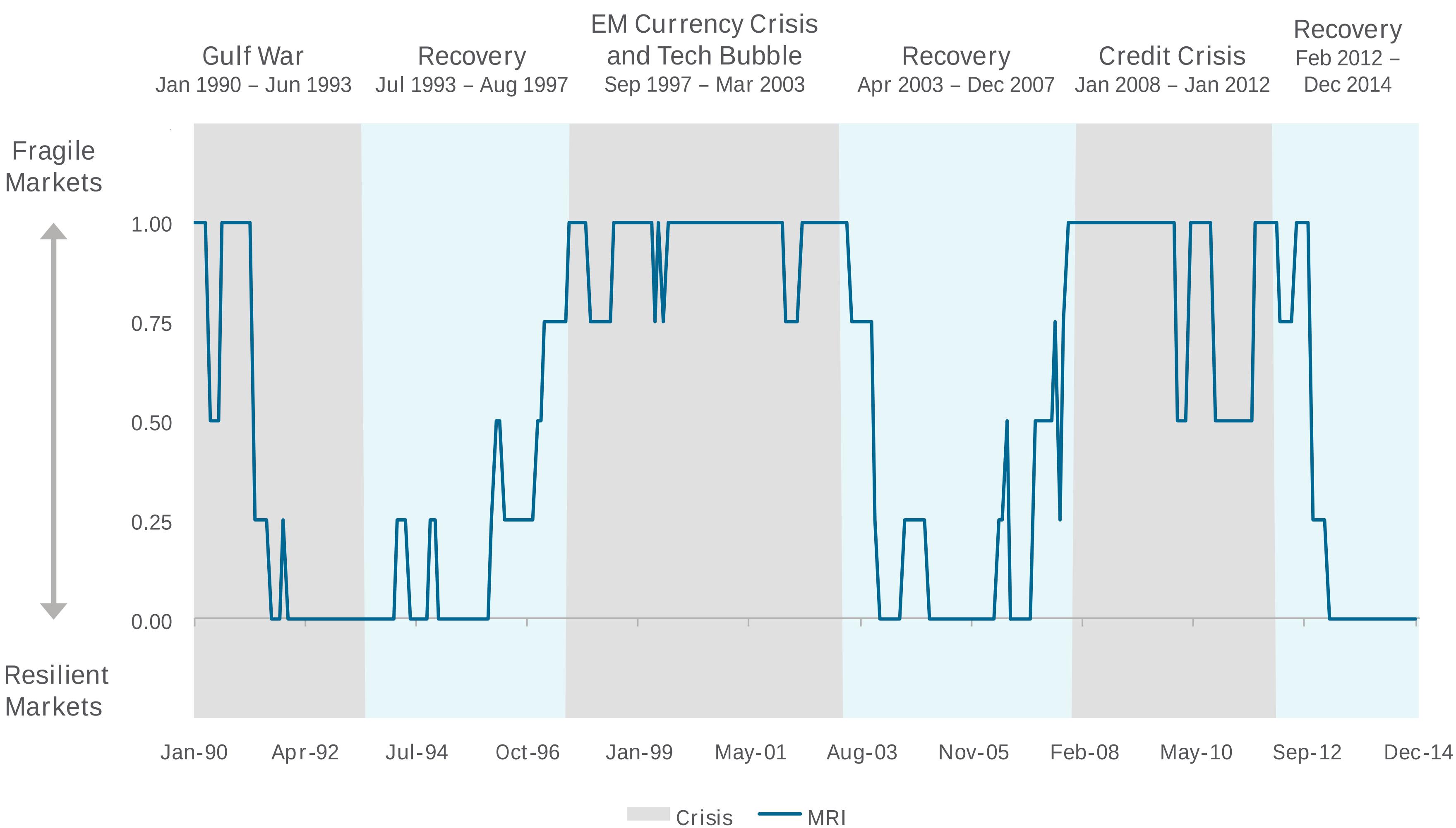
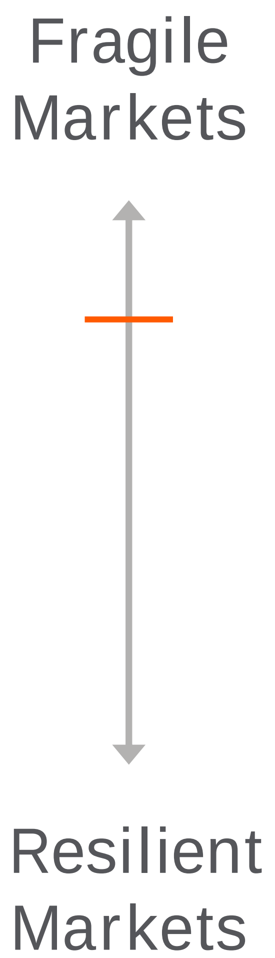
MARKET STATES VARY FROM FRAGILE TO RESILIENT



Sources: First Quadrant, L.P., Bloomberg LP

MODEST FRAGILITY TODAY



We view the markets as having moved into a modestly fragile state in 2015. The **“price of insurance” in the options** markets (US, Europe, commodities) is modestly high on average; credit spreads are modestly wide signaling growing investor concern, and the global economy has weakened somewhat.

There are extenuating circumstances, **and we don’t view the markets as being** in a most fragile state.

THINK ON THESE THREE THINGS…

1. There is no Yellen or Draghi "put"
2. **Geopolitical risk is at it's post Cold**-War high
3. QE is not going to work in Europe the way it did in the US

YOU THINK YOU'RE DIVERSIFIED. *ARE YOU?*

- Global Stocks
- Small Cap Stocks
- Emerging Markets
- Real Estate
- Commodities
- High Yield Bonds
- Sovereign Bonds
- TIPS
- Long-Duration Sovereign Bonds
- Long Duration TIPS

CAPITAL ALLOCATION

RISK ALLOCATION

92% of the risk is in equities in a typical asset allocation approach (as measured by the correlation of the total portfolio to equities).

IN AN INCREASINGLY FRAGILE MARKET ENVIRONMENT, THIS IS A CONCERN.

Sources: First Quadrant, L.P., StyleAdvisor, Bloomberg LP, Global Financial Data (GFD)

CONTACT INFORMATION

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Max Darnell has served as First Quadrant's Managing Partner since 2012, and Chief Investment Officer since 2002. Max is responsible for setting the strategic direction of the firm, and for overseeing the firm's investment products with emphasis on strategic research and development initiatives. Max began his career at First Quadrant in 1991, managing derivatives research throughout the decade. In 2000 he was named Director of Research. Max earned a Master's degree in Economics from the University of California, Los Angeles, in 1991.