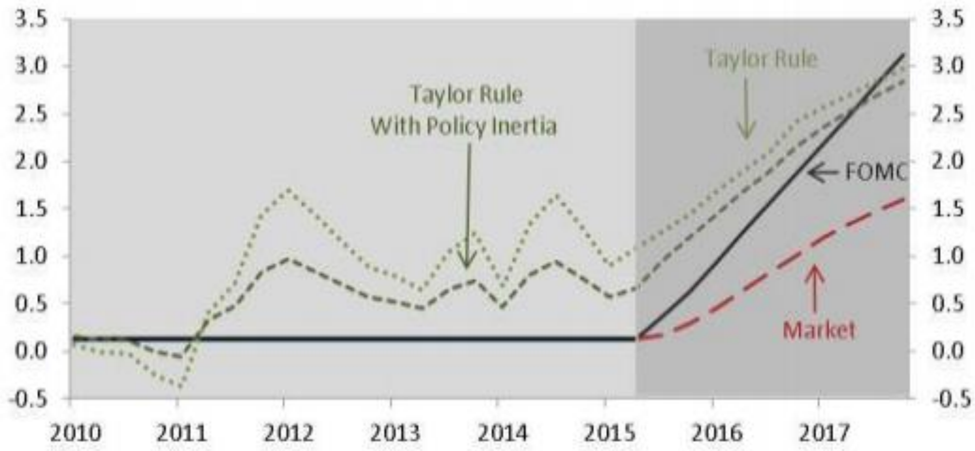
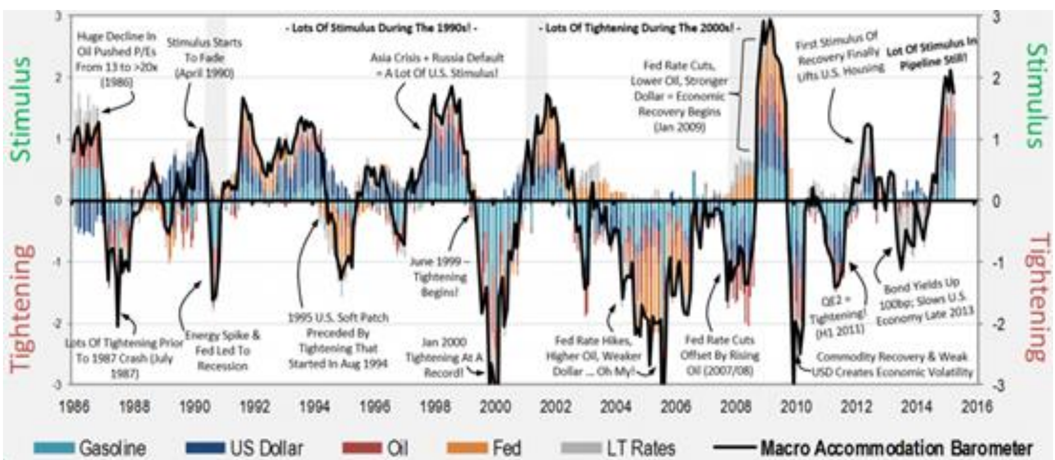
Market Recap

Anticipated Federal Funds Rate Movements



Source: Cornerstone Macro

Macro Effects of Stimulus and Tightening



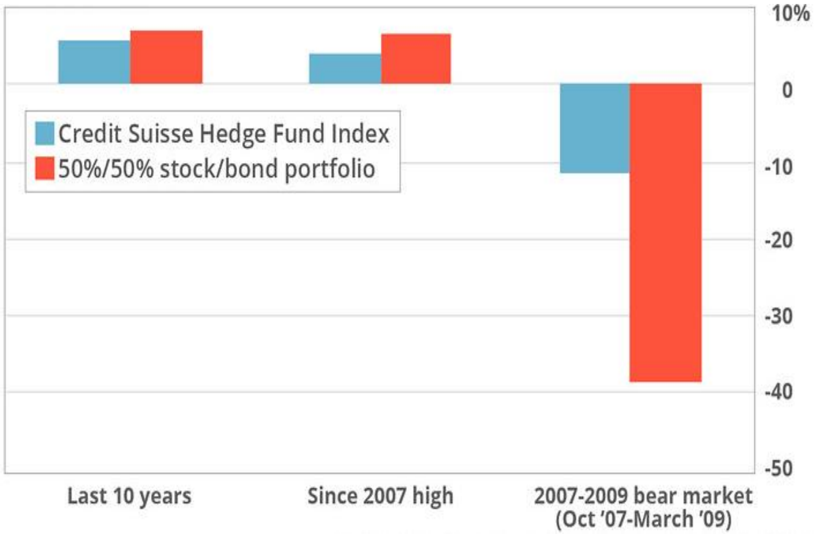
Source: Cornerstone Macro, Global Wellness Institute

Varying opinions exist as to the timing and pace of future interest rate hikes in the United States. At present, the stock market anticipates that the Fed's actions will be much more measured than the Fed, itself, projects. The Taylor rule, one of the more popular methods of determining the proper Fed Funds rate (taking into consideration a myriad of economic data), would suggest that the Fed would have been justified in raising rates back in 2011. Additionally, this formula hints that rates should rise significantly higher than the expectations of the market, reaching 3% at the end of 2017. In contrast, the market is pricing in a modest increase in Fed Funds to 1% by the end of 2016 and to 1.6% by the end of 2017. This slow and modest change implies equally slow growth in GDP and inflation over the next several years.

Economic growth and, ultimately, company earnings and stock performance, are driven by the macro effects of stimulus and tightening. Typically, the two forces are simultaneously moving in the same direction. For example, between 2004 and 2006, the Federal Reserve was tightening (raising rates) at the same time as oil prices were moving higher, proving to be a recipe for an economic slowdown and an eventual stock market correction. In reverse, lower interest rates, combined with falling energy prices, lead to positive economic growth and stock market performance. Today is one of the rare occasions in which inflation and monetary policy are working in opposite directions, making the second half of 2015 that much more difficult to predict. The balance of 2015 stock performance may hinge on which opposing force – Federal Reserve rate hikes (tightening), or a stronger US dollar coupled with falling oil prices (stimulus) – has a greater impact on the economy and stocks.

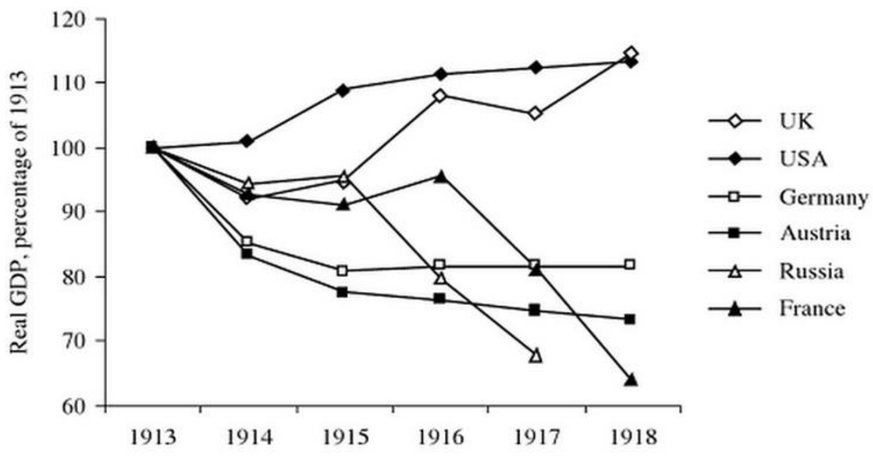
Market Recap

Performance of Hedge Funds



Source: Marketwatch

Impact of WWI on Global Economies



Source: Vox.com

Investors are second-guessing their investments in hedge funds, with redemptions over the last two quarters ending March 31, 2015 reaching $34.6 billion. This represents the largest consecutive quarterly outflow since March 2009, and has led to closure of a number of hedge funds. In fulfilling their role, hedge funds are structured to lag behind the markets during bull markets, yet outperform the (unhedged) markets during bear markets. As we enter the sixth year of the current bull market which has seen record highs in all the major indices, investors have largely forgotten about the benefits of hedge funds in a portfolio. They see that, over the last decade, an investor would have outperformed hedge fund performance by simply using a conservative 50/50 portfolio of stocks and bonds. Conveniently, they overlook the period between 2007-2009 during which hedge funds performed appropriately, protecting the downside and substantially beating the broader equity markets.

The rise of the United States as a global economic, military, and geo-political superpower was, in part, due to the decline of other former world leaders. World War I ranks high among the events that spurred America towards worldwide dominance. For centuries prior, world leadership had been divided among several competing global powers. World War I spelled the beginning of the end for the established order. The toll of the war devastated the economies and output of all global powers except the United States and Great Britain. Two effects were at play: the physical carnage caused by the war was limited almost exclusively to continental Europe; while the boon in industrial production necessary to meet wartime demand for weapons and equipment actually increased American output and GDP throughout that period of time.

Contact: If you have any questions or comments, please do not hesitate to contact us at 703.992.6164. For more information about Harbour Capital Advisors, please visit our website at www.harbourcapitaladvisors.com.

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