NIS

EQUITY COMMENTARY

APRIL, 2016

During a quarter when talk of a nearing recession was as prevalent as its been in a long time, we also established a new low in unemployment claims and received early signs of a pick-up in the ailing manufacturing sector with the March ISM New Orders posting a 16 month high. This dichotomy showed up in the market too as the S&P 500 Index recorded its 9th worst January of all time, and then followed it up with a sharp snapback rally to finish the quarter up 1%.

To say that better earnings growth is needed would be obvious and repetitive, so more specifically we think it is hard to see the market move much higher without the participation of commodities and oil prices. In our January letter we pointed out that we seemed to have passed the point where lower oil prices were viewed as good for the economy. Fed President Yellen has since stressed how keenly aware she is of the Fed's actions as it relates to commodities and emerging market currencies, and is now emphasizing it in terms of a risk to the US. In her speech to the Economic Club of New York in late March, after mentioning the positives derived from lower commodities, Yellen stated:

> In the event oil prices were to fall again, either development could have adverse spillover effects to the rest of the global economy. If such downside risks to the outlook were to materialize, they would likely slow U.S. economic activity, at least to some extent, both directly and through financial market channels as investors respond by demanding higher returns to hold risky assets, causing financial conditions to tighten.

There is a natural positive correlation between oil prices and interest rates given the former's effect on inflation. Bank stocks are currently closely tracking longer term interest rates up and down, and when you also consider the credit concerns associated with the struggling energy sector, the current connection between oil prices and bank stocks becomes clear. After the January selloff, we added to both our bank and oil stocks. In our opinion, these decisions are supported by a clearer picture of the necessary supply response in the oil market, and a Fed who does not want to exacerbate the problem.

To provide another example of the current tie between oil and the market, as odd as this might sound, we believe that the airline stocks might actually perform better if oil prices rebound. Our Delta Airline's (DAL) free cash flow has skyrocketed from $1.7 billion in 2013 to nearly $5 billion last year. Steady volume growth and disciplined capital spending have played a part, but the lower fuel prices have provided a huge benefit. Despite these record profits, the market appears more concerned with the industry's current habit of passing along some of these savings to their customers with lower airfare. Price wars are one of those legacy worries that the industry is fighting hard to shed. If the outlook for oil prices changes, it might lead the airlines to ease up on the lower fares, thus alleviating the concern. Interestingly, Reuters recently published an article stating that airlines have stepped up their fuel cost hedging[1], which could be signaling a change in their view.

As always, we appreciate your continued trust in our service and we look forward to speaking with you soon.

Chart 1: US (black) and OPEC (purple) Oil Production **Source: Bloomberg**

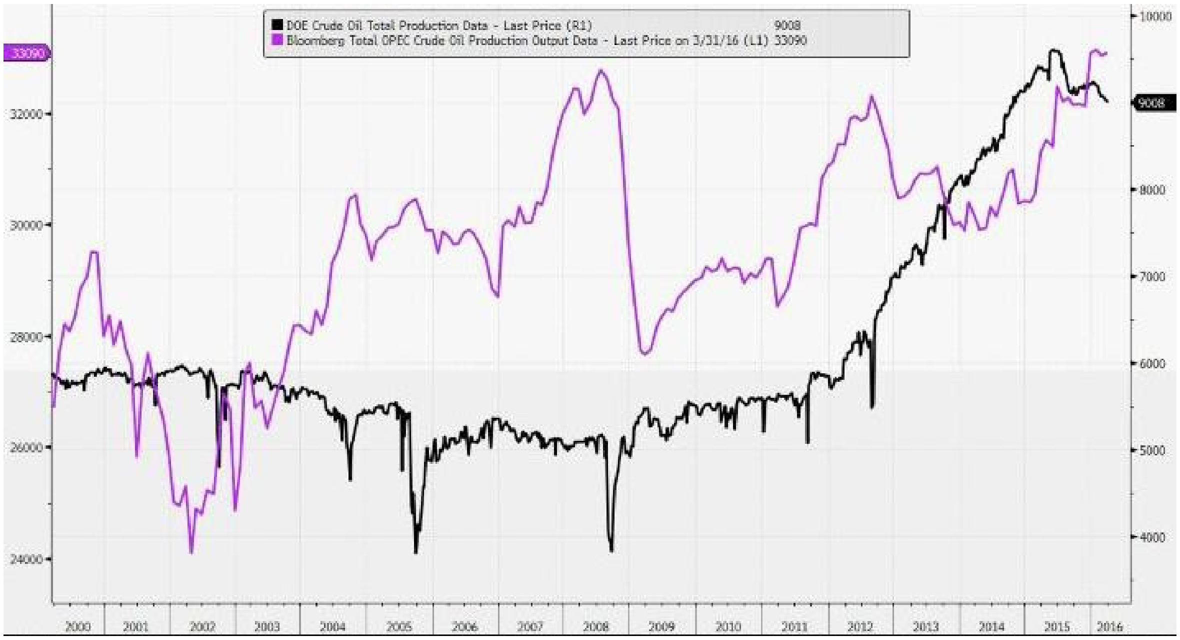
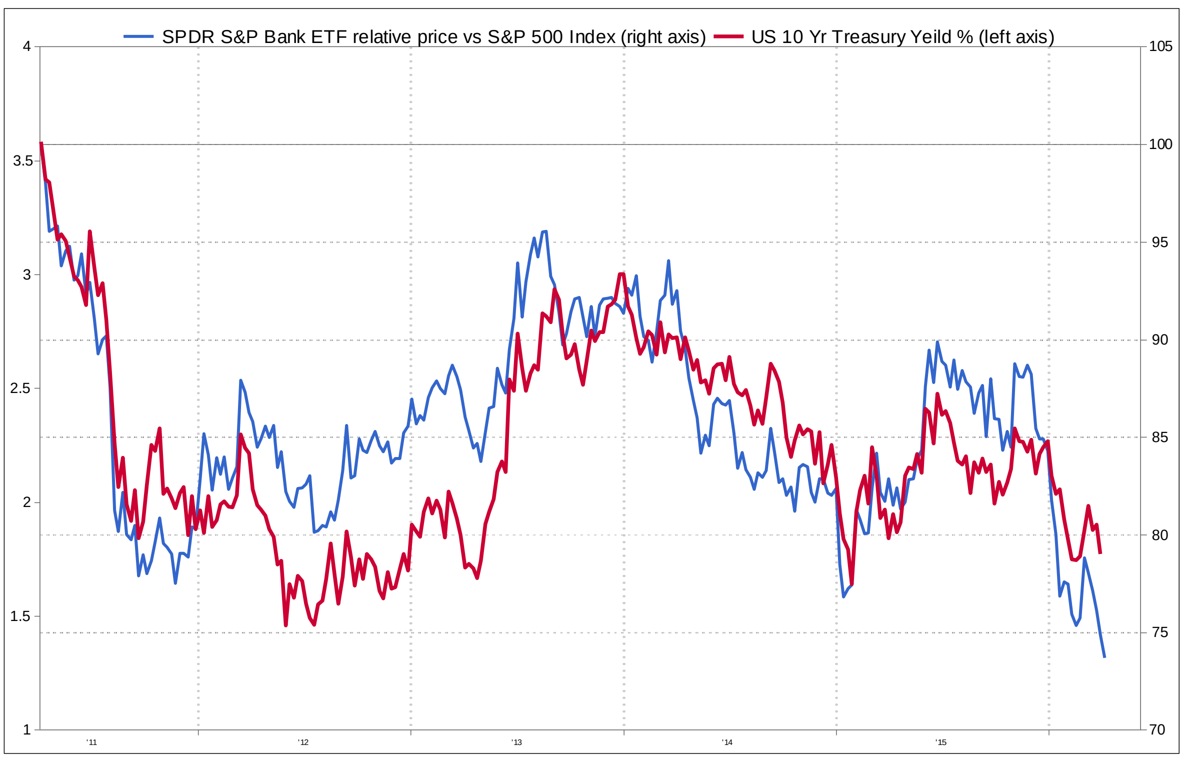


Chart 2: S&P Bank stocks' relative performance and Interest Rates **Source: FactSet**



Tyler Pullen, CFA

Portfolio Manager

Past performance does not guarantee future results. Market conditions can vary widely over time and can result in a loss of portfolio value. In accordance with the rules of the Securities and Exchange Commission, we notify you that a copy of our ADV, Part II filing with the SEC is available to you upon request.

[1] Reuters, *Airline hedges fuel rally in later dated oil prices*, 4/6/16 http://www.reuters.com/article/usa-airlines-oil-idUSL2N1731M8