



May 2015

## **Tucson Supplemental Retirement System**

1<sup>st</sup> Quarter 2015 Market Update

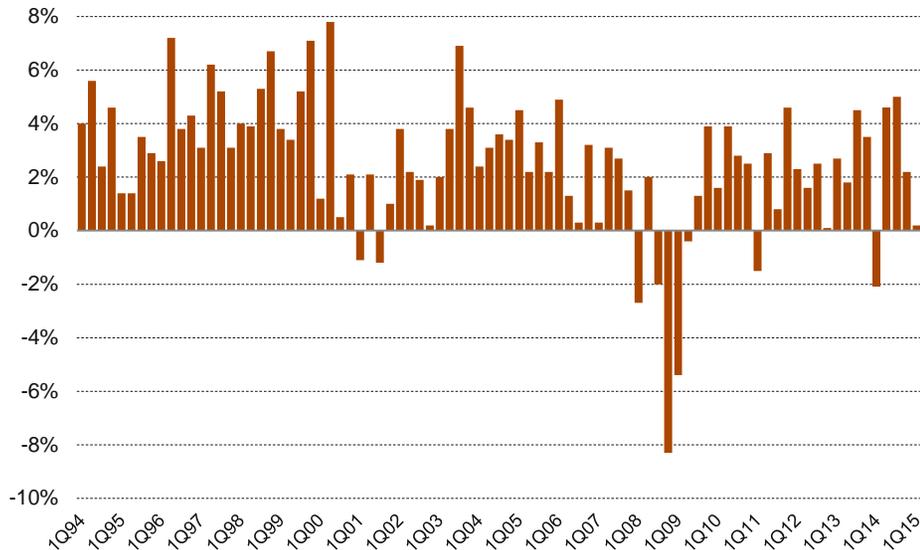
---

**Gordie Weightman, CFA**  
Vice President

# U.S. Economy

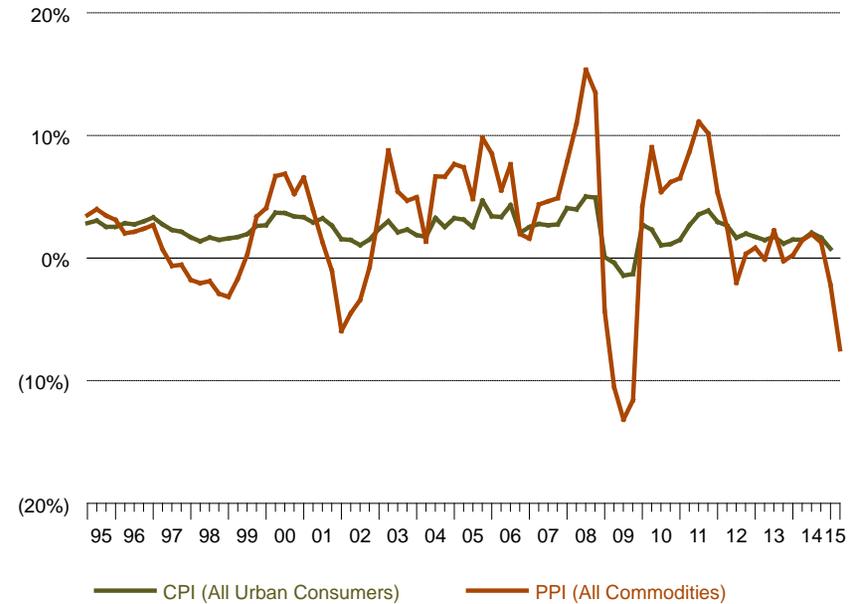
## Periods Ending March 31, 2015

Quarterly Real GDP Growth (20 Years)\*



Source: Bureau of Economic Analysis

Inflation Year-Over-Year



Source: Bureau of Labor Statistics

- Initial first quarter GDP came in at 0.2%, behind the 4<sup>th</sup> quarter's gain of 2.2%.
- March headline inflation fell 0.1% from a year earlier, core inflation was 1.8%.
- The unemployment rate was 5.5% at quarter end, down 0.1% from start of year.
- Payroll growth decelerated with an average addition of 185,000 jobs per month, down from 324,000 in 4Q14.
- U.S. crude oil prices are down 56% since June 2014

# Asset Class Performance

Periods Ending March 31, 2015

**Periodic Table of Investment Returns  
for Periods Ended March 31, 2015**

Last Quarter	Last Year	Last 3 Years	Last 5 Years	Last 10 Years
MSCI:EAFE US\$ 4.9%	S&P:500 12.7%	S&P:600 Small Cap 17.3%	S&P:600 Small Cap 16.3%	S&P:600 Small Cap 9.7%
S&P:600 Small Cap 4.0%	S&P:600 Small Cap 8.7%	S&P:500 16.1%	S&P:500 14.5%	MSCI:Emer Markets 8.8%
MSCI:Emer Markets 2.3%	Barclays:Aggregate Index 5.7%	MSCI:EAFE US\$ 9.0%	MSCI:EAFE US\$ 6.2%	S&P:500 8.0%
Barclays:Aggregate Index 1.6%	MSCI:Emer Markets 0.8%	Barclays:Aggregate Index 3.1%	Barclays:Aggregate Index 4.4%	MSCI:EAFE US\$ 4.9%
S&P:500 1.0%	3 Month T-Bill 0.0%	MSCI:Emer Markets 0.7%	MSCI:Emer Markets 2.1%	Barclays:Aggregate Index 4.9%
3 Month T-Bill 0.0%	MSCI:EAFE US\$ (0.9%)	3 Month T-Bill 0.1%	3 Month T-Bill 0.1%	3 Month T-Bill 1.5%

# Impact of Strong Dollar on S&P 500 Earnings

## Dinged by the Dollar

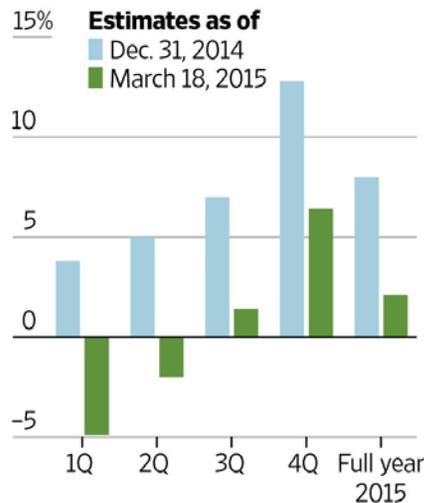
A strong U.S. dollar is taking a bite out of profit expectations.

### WSJ Dollar Index



Sources: WSJ Market Data Group (dollar index); FactSet (profit growth)

### Expected profit growth in 2015 from a year earlier, S&P 500 companies

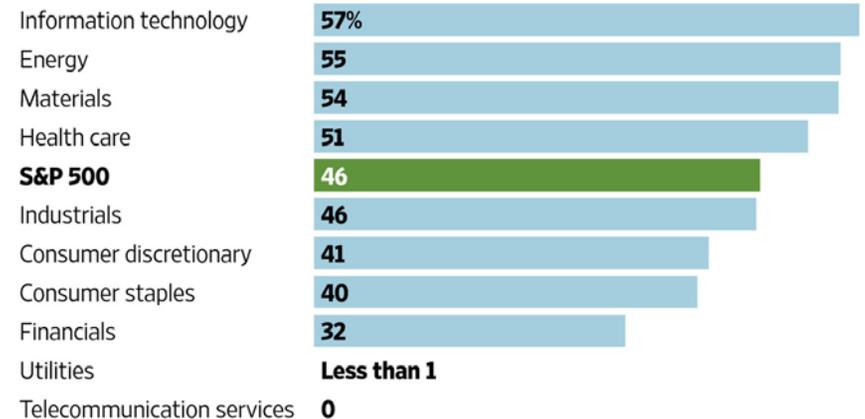


THE WALL STREET JOURNAL.

## Exposed

A surging U.S. currency is steering investors toward sectors that have the least foreign exposure.

### Foreign sales as a percentage of total, by S&P 500 sector\*



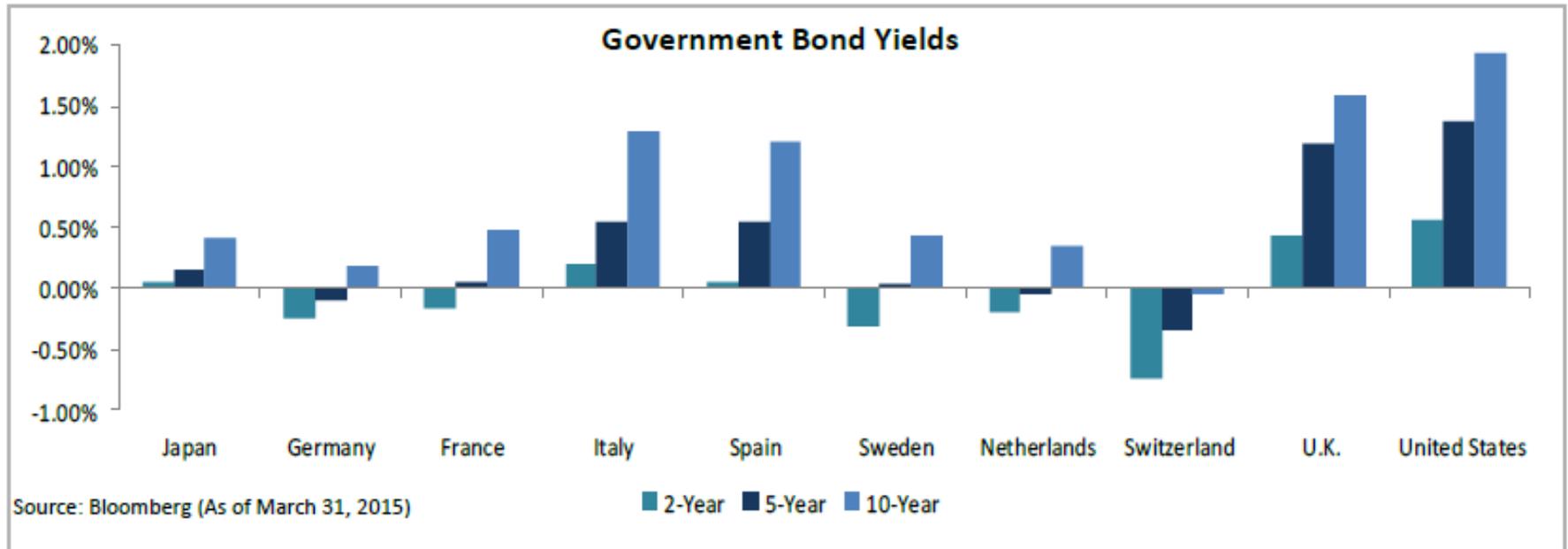
\*Latest data, from 2013  
Source: S&P Capital IQ

THE WALL STREET JOURNAL.

- Approximately 45% of S&P 500 sales are outside the U.S.; 19% for the Russell 2000
- Biggest dollar headwinds are felt in technology, industrials, health care and materials

Source: Wall Street Journal

# Global Sovereign Yields Reaching Historic Lows



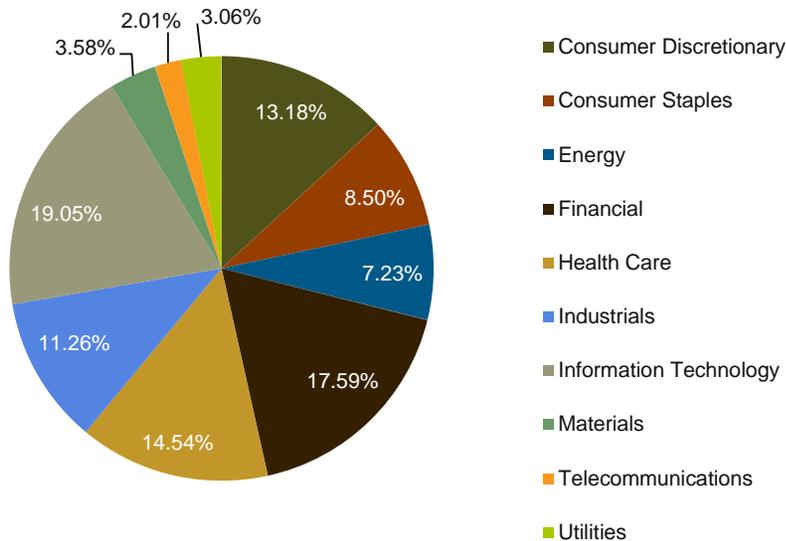
Source: Dupont Capital, "Fixed Income Market Review and Outlook," 3/31/15.

- It's a strange world for bonds....
  - For the first time ever, a country sold 10-year debt with a negative yield. Switzerland auctioned 10-year bonds yielding -0.055% on April 8. Mexico sold a 100 year bond in Euros with a yield of 4.2%
- 2- and 5-Year yields for many European sovereigns tipped into negative territory as the European Central Bank implemented its quantitative easing program
- 10-year yield for Germany approaching zero with UK and US the only developed markets 10-year note yielding above 1.5%

# U.S. Equity Returns

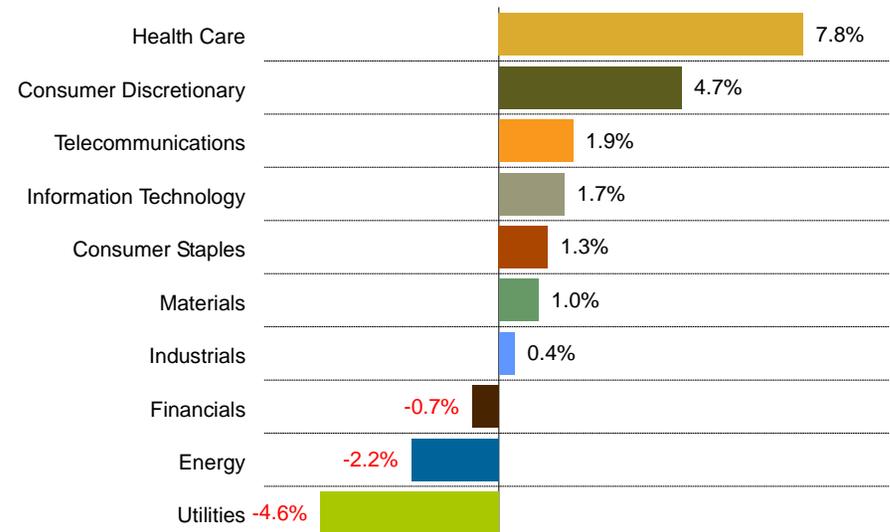
Periods Ending March 31, 2015

Economic Sector Exposure (Russell 3000)



Pie chart may not sum to 100% due to rounding  
Source: Russell Investment Group

Quarterly Returns (Russell 3000)

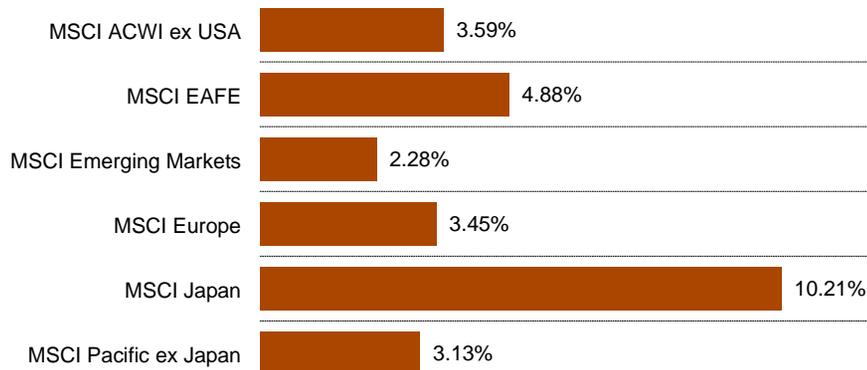


- Volatile first quarter for U.S. equities (down in Jan, up in Feb, mixed in Mar)
- Large caps lagged small caps as strong dollar detracted from large multinational's earnings
- Style generated largest differential in 6 years (RU1V: -0.7%; RU1G: +3.8%)
- Oil prices will likely remain suppressed with U.S. inventories near 80 year highs

# International Equity Returns

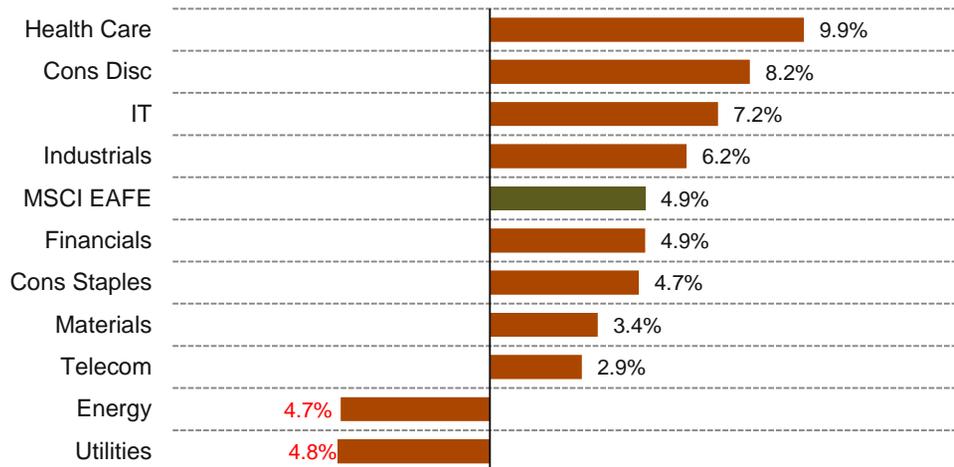
Periods Ending March 31, 2015

## Regional Quarterly Performance (U.S. Dollar)



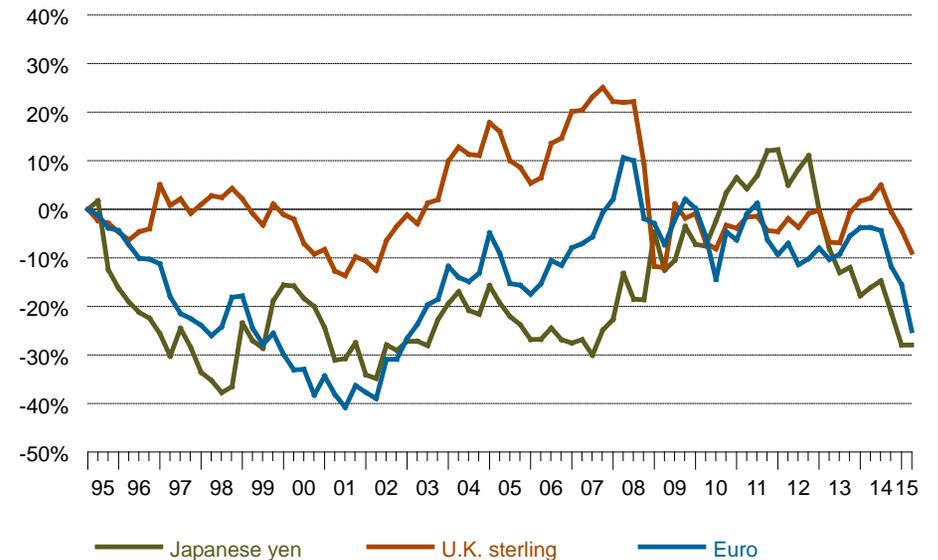
Source: MSCI

## MSCI EAFE Sector Returns



Source: Barrow Hanley Quarterly Benchmark Review

## Major Currencies' Cumulative Return (vs. U.S. Dollar)



\*Euro returns from 1Q99. German mark prior to 1Q99.

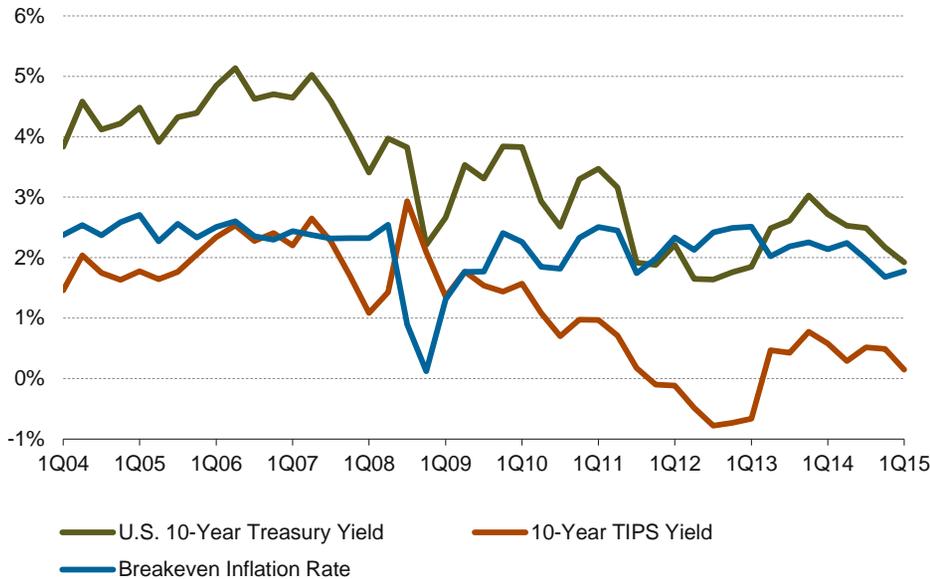
Source: MSCI

- The euro (-11.2%) was hit hard by the ECB quantitative easing program. The pound (-4.8%) also depreciated versus the dollar while the yen was flat.
- Emerging markets lagged their developed counterparts for the quarter.

# Yield Curve Changes

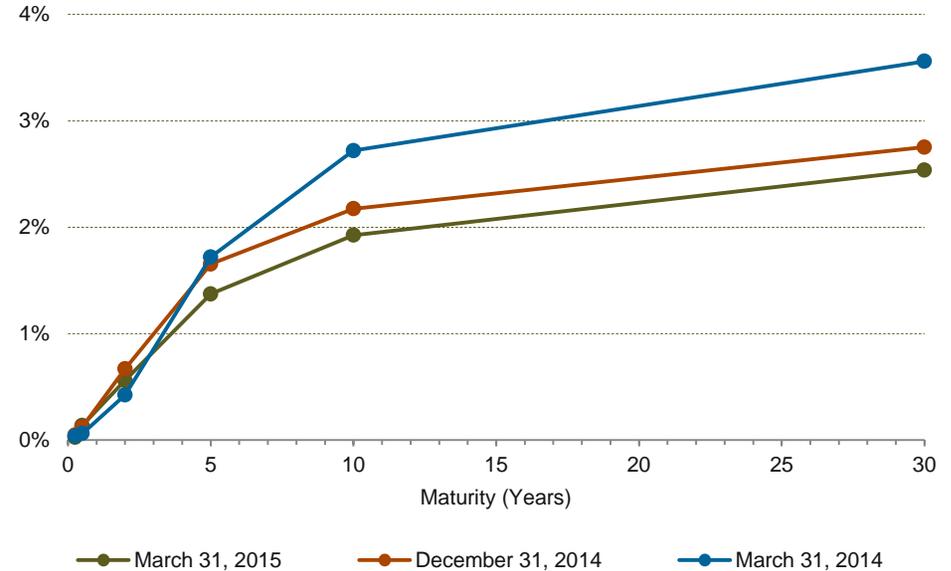
## Periods Ending March 31, 2015

Historical 10-Year Yields



Source: Bloomberg

U.S. Treasury Yield Curves



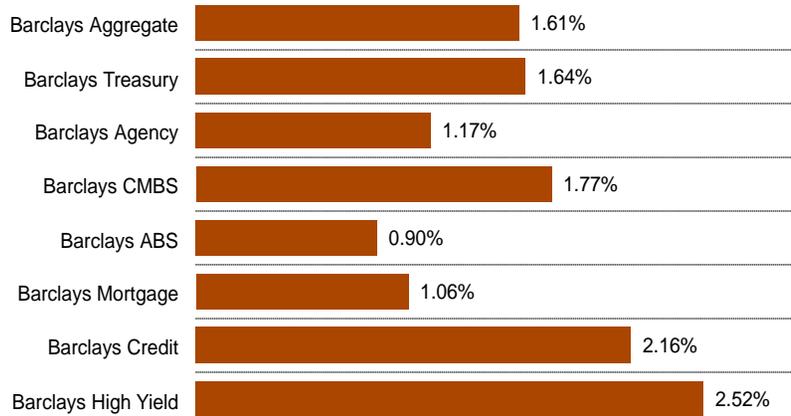
Source: Bloomberg

- The yield curve shifted downward, boosting fixed income returns
- The 10-year Treasury yield fell to 1.94%, a decline of 23 basis points from the end of 2014
- Real yield on 10-year Treasury fell to 0.18%, a drop of 28 basis points since the start of the year
- The breakeven inflation rate rose to 1.77% on a sharp decline in real yields

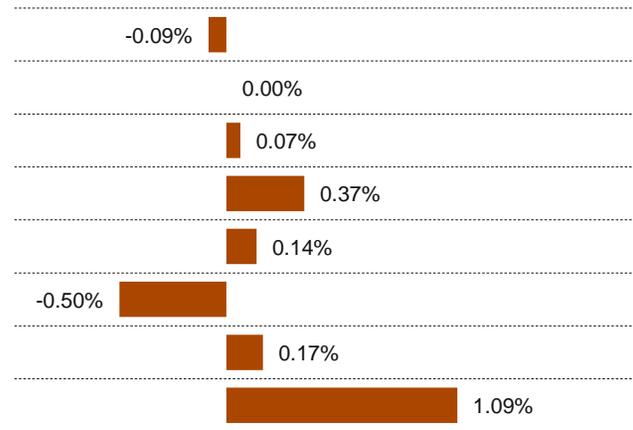
# Total Rates of Return by Bond Sector

Periods Ending March 31, 2015

Absolute Returns for Quarter ended March 31, 2015

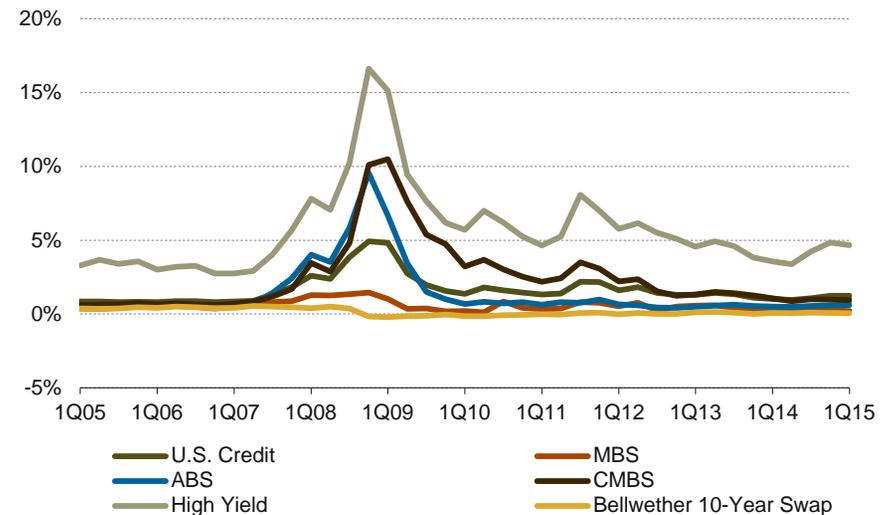


Excess Return versus Like-Duration Treasuries



- BC Aggregate gained 1.6% as yields fell
- BC Credit Index returned 2.2% as market absorbed record 1Q issuance
- High yield spreads narrowed during the quarter and the BC High Yield Index led all other segments of the bond market

Effective Yield Over Treasuries



Source: Barclays