The Lam Group

Investment Management

From a portfolio performance perspective 2Q 2015 was essentially a flat quarter, however this period was far from uneventful. With a solid 1Q 2015, 2Q started off strongly, but was interrupted by geopolitical problems in Greece, worries of rising US interest rates and the ramifications of a strong US dollar (up 5.84% YTD). These factors set the stage for a very volatile market environment.

While the majority of our equity exposures made marginal contributions in 2Q 2015, international small cap stocks led performance (up 4.34%) while domestic real estate struggled (down 10.00%). On a 2015 YTD basis, international small cap stock are up 10.15% and domestic real estate is down 5.75%. It is worth noting, but not surprising, that in 2014 these equity asset classes held exactly the opposite positions; domestic real estate (up 32.00%) was the leader while international small cap stocks struggled the most (down 4.95%).

These examples of 2014 vs 2015 (YTD) asset class performance data again remind us that asset class returns are unpredictable and when a given asset class does well (or poorly) in one year, it does not mean it will do well (or poorly) the next. This acknowledgement of unpredictability is a central tenet of our investment strategy.

No asset class goes up or down indefinitely and history has shown that the best way to identify opportunities to "buy low and sell high" is to maintain a disciplined rebalancing strategy within a globally-diversified and balanced portfolio with explicit asset allocation targets.

Table 1: Periodic Asset Class Returns as of 06/30/15

EQUITY ASSET CLASSES	**2Q 2015**	**YTD**	**12 Mos**	**3 Years***	**5 Years***	**10 Years***	**15 Years***
S&P 500 Index - *Domestic Large Cap Stocks*	0.28%	1.23%	7.42%	17.31%	17.34%	7.89%	4.36%
Russell 2000 Index - *Domestic Small Cap Stocks*	0.42%	4.75%	6.49%	17.81%	17.08%	8.40%	7.50%
MSCI EAFE Index - *International Large Cap Stocks*	0.62%	5.52%	-4.22%	11.97%	9.54%	5.12%	3.22%
MSCI EAFE SC Index - *International Small Cap Stocks*	4.34%	10.15%	-0.77%	15.69%	12.40%	6.59%	7.41%
MSCI EM Index -*Emerging Markets Stocks*	0.69%	2.95%	-5.12%	3.71%	3.68%	8.11%	7.86%
DJ US Select REIT Index - *Domestic Real Estate*	-10.00%	-5.75%	5.21%	8.67%	14.43%	6.78%	11.28%
S&P Global (ex-US) REIT Index - *International Real Estate*	-3.15%	-1.05%	-3.21%	9.24%	11.93%	4.01%	N/A
FIXED INCOME ASSET CLASSES	**2Q 2015**	**YTD**	**12 Mos**	**3 Years***	**5 Years***	**10 Years***	**15 Years***
BarCap Aggregate Bond Index - *US High-Grade Bonds*	-.1.68%	-0.10%	1.86%	1.83%	3.35%	4.44%	5.42%
BarCap High-Yield Bond Index - *US High-Grade Bonds*	0.00%	2.53%	-0.40%	6.81%	8.61%	7.89%	7.75%
BarCap TIPS Index - *US TIPS*	-1.06%	0.34%	-1.73%	-0.76%	3.29%	4.13%	6.05%
Bloomberg Commodities Index - *Commodities*	4.66%	-1.56%	-23.71%	-8.76%	-3.91%	-2.62%	1.56%
Citigroup Non-$ World Govt Bond Index - *Non-$ Bonds*	-1.54%	-5.83%	-13.49%	-3.88%	0.33%	2.63%	4.36%
JPM EMBI Global Diversified Bond Index - *Emerging Markets Debt*	-0.34%	1.67%	0.51%	4.30%	6.76%	7.45%	9.52%

Sources: Morningstar, JP Morgan & Dimensional. *annualized

Given all the recent concern about Greece it is important to know that our portfolio has minimal direct exposure to Greece (<0.1%), The Greek economy is small as are their stock and bond markets.

However, the risk posed by a Greek default is less about an explicit capital loss of a direct investment in Greece, but rather its potential to cause instability to the overall financial system. Recalling the global financial crisis in 2008, and the European debt crises in 2011-12, if a bank somewhere in the world has enough exposure to a large problem, this troubled bank can cause a systemic issue for the financial system as a whole. Fortunately, central bankers have learned a lot since 2008 and the major creditors and banks have had time to isolate their exposures to Greece.

At the same time, China, is showing signs of relative economic weakness and capital markets excess. While some are worried about the contagion effects of China and Greece to other markets/countries, it is likely that any geopolitical crisis will be met with accommodative monetary policies.

Geopolitical pressures notwithstanding, investors continue to be concerned about the prospect of rising US interest rates despite low (and lowering) foreign interest rate policies and little evidence of domestic inflation. While many believe a rise in US interest rates is a foregone conclusion, this Fed policy decision is not simple or obvious.

The Fed must be careful with the manner in which it executes its interest rate policy and has to be concerned with how it affects the overall strength of the US dollar. While counter-intuitive, a US dollar that is too strong may ***not*** be good for the US economy (or the domestic stock market). A strong and strengthening US dollar causes US goods and services to be less competitive on the global stage.

It is important to understand that the direction of currencies is driven by interest rate differentials between domestic and foreign markets. If this differential increases/widens too much (US rates rise while foreign rates decline), the US dollar could strengthen to a level that may negatively affect US equity markets. Because of the unintended consequences that a strong US dollar can bring, we are not concerned about the portfolio effects of a Fed-initiated increase in short-term interest rates in 2015. An imminent domestic rate increase has been incorrectly predicted by the media since 2013 (a broken clock is accurate twice a day). We expect any domestic Federal Reserve-initiated rate increases in 2015 (if any) will be marginal and well-telegraphed.

Nevertheless, we feel the portfolio is well-positioned despite all the uncertainties facing the markets. We continue to believe in our globally-diversified and balanced investment strategy and expect to rebalance the portfolio along investment policy guidelines as warranted.