TIMONIER

Wealth Beyond Financial™

From the Engine Room

4th Quarter 2014

Quarterly Market Review

Fourth Quarter 2014

This report features world capital market performance and a timeline of events for the past quarter. It begins with a global overview, then features the returns of stock and bond asset classes in the US and international markets.

The report also illustrates the performance of globally diversified portfolios and features a quarterly topic.

"The best way to predict the future...is to create it!"

Overview:

Are You Trying to Sprint in a Marathon?

"Man has falsely identified himself with the pseudo-soul or ego. When he transfers his sense of identity to his true being, the immortal Soul, he discovers that all pain is unreal. He no longer can even imagine the state of suffering."
~Paramanhansa Yogananda (1893-1952)

2014 may go down in financial history as the year that a lot bad of things didn't happen to investors. For example, despite numerous nervous headlines that it might be best to prepare for the worst, there was no universal stock correction. And despite Federal Reserve announcements on ending quantitative easing in the U.S., there was no major slump in the bond markets. With the 10-year US Treasury Bond yielding a paltry 2.17% at year's end, *all* 46 economists that had predicted higher interest rates for the 2014 *Wall Street Journal* forecasting survey were, ut um, wrong!

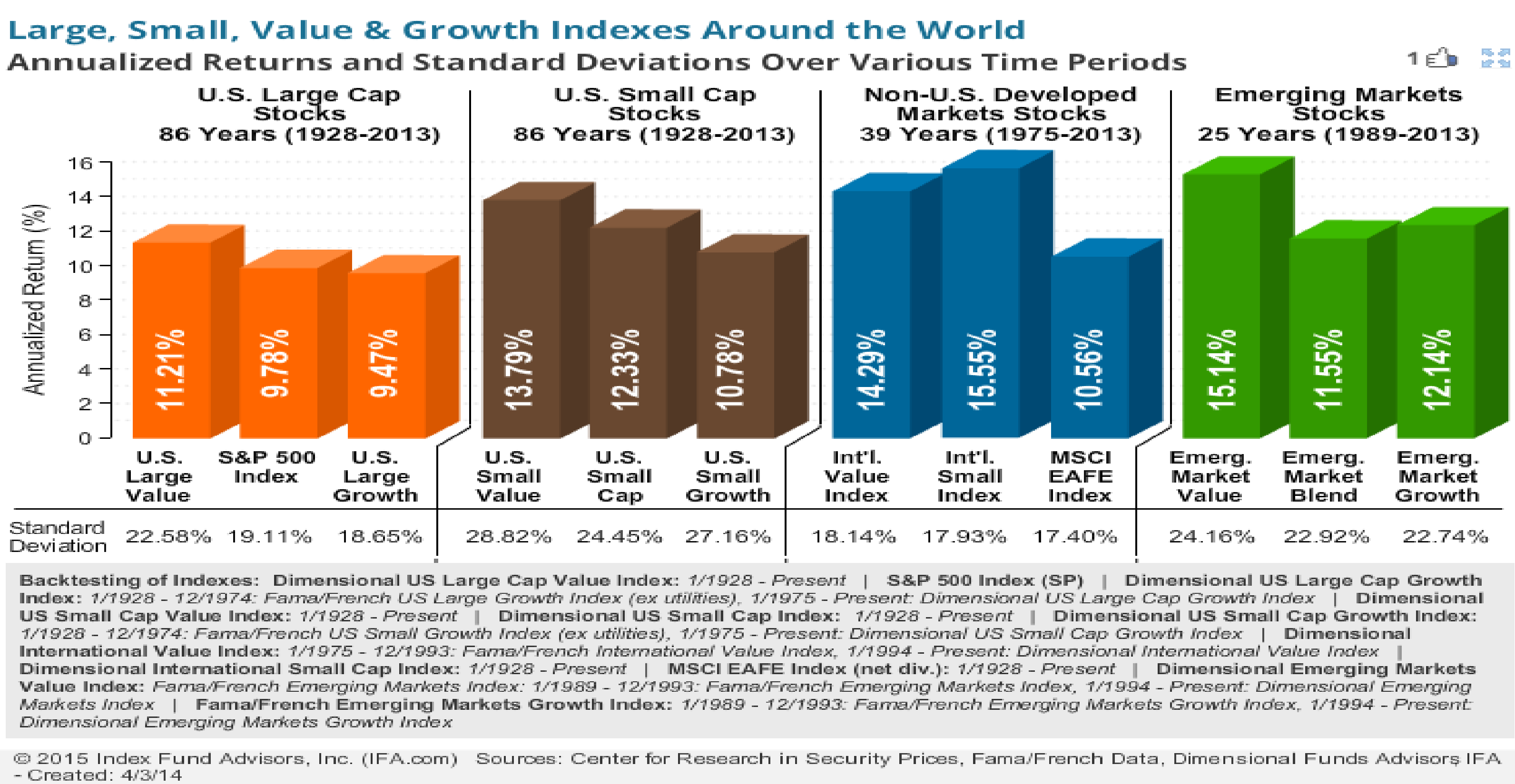
Another non-event for globally diversified investors was that we were not rewarded with higher annual returns relative to a concentrated, stay-at-home position. Large U.S. companies happened to enjoy a remarkable, double-digit year, even as other markets experienced negative to ho-hum results, especially for international, emerging market, and small-cap stocks. (You will see with complete detail, their respective performance in the pages that follow).

In late September, I got a few calls over concerns of a nominally high priced U.S. stock market as promoted by the media. U.S. stock prices had already started declining and over a 3 week period we had about a 10% retrenchment from intra day peak to intra day trough. Based on closing day prices it was promoted as a 7.5% decline. But I digress. Price alone, of a basket of stocks is utterly meaningless. Many other factors are evaluated in order to gain relative value perspectives. Factors such as level of corporate earnings and the price multiples applied to them, the state of the economy, the condition of the geopolitical atmosphere, and alternative investment options which vie for the investors savings program are just a few of the considerations in evaluating the pricey-ness of a stock market. U.S. stocks, in my opinion, were trading at a relative fair value at the start of the fourth quarter, and still are. I finished my last Quarterly Letter with the statement, "***There is simply no fundamental or global economic basis that suggests that stocks prices are primed for a sustainable decline."*** Quite fortuitously, the letter went out October 15th, the day that the US stock markets bottomed and I will always quite rightly claim this as LUCK! But after much discussion, and an abrupt rebound in the U.S. large company stock markets those same calls of concern turned into concerns that their other stock market categories weren't keeping up!

These observations were well founded. Because, at Timonier, we do not build portfolios to mimic the results of the U.S. large company stock market. We build customed globally diversified investment portfolios that will meet the LifePath goals of our clients Target Financial Plan. These portfolios are academically designed to efficiently provide the highest level of returns at various acceptable levels of volatility. The underlying asset classes within each portfolio are chosen knowing that they will not all move in sync in the near term, while providing similar benefits for long term growth. That means there will be times when some of the components of the engine will be booming in results while others may be dragging. **We are pleased that the U.S. large company stock component was one of the booming winners in 2014 with**

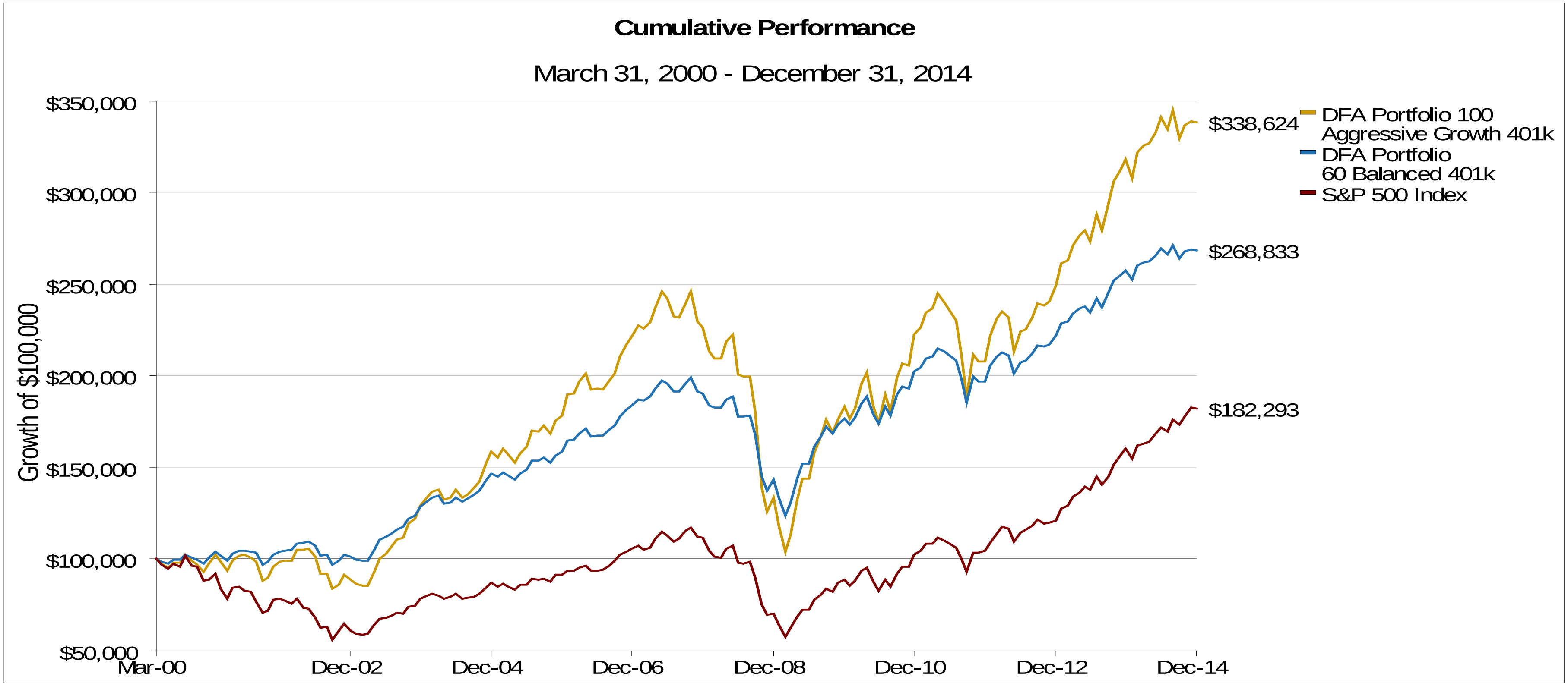
a 13.69% return! We are concerned however, if our clients believe that the S&P 500 index should be their portfolio now…or is their new barometer or benchmark in evaluating their own portfolio's performance. ***It will not be, and you don't want it to be!***

Our firm places the odds of you achieving success where there is clear evidence of historical performance with repeating patterns. We find these patterns (I like to refer to them as fractals) of behavior dating back to 1928, in that stocks outperform T-bills and bonds, value stocks outperform growth stocks, that small company stocks outperform large company stocks, and that these observations are consistent in every country in the world. We have consistently applied these strategies for the past 33 years in our work. And we are dedicated to continuing this process until overwhelming evidence reveals the benefits of an altering strategy. The chart below will help you see the weighty evidence that provides us confidence to build the portfolios we do and the staying power to see the long term results unfold.



"Many shall be restored that are now fallen and many shall fall that are now in honor!"
Horace, poet

I offer a simple graph for a longer perspective to the benefits of global diversification via two portfolios that we manage. It is not meant to be a complete analysis to the attributes of global investing. And there are many flaws to this type of single timeline analysis. But it does encompass a relative lengthy time period, one that most all of us have experienced as investors and in a portfolio in which many of us have had as an investment. The start date was established to match the youngest fund in the portfolios line up. The chart below, illustrates the investment performance of the Aggressive Growth Portfolio 100 and the Balanced Portfolio 60 that we use in our corporate 401k plans as compared to the S&P 500 index. We offer 10 such models based on varying weightings to stocks and bonds to offer up a wide range of return/risk based portfolios from ultra conservative to ultra aggressive. **Portfolio 100** as its name implies has no weighting to bonds or cash. It is 100% stocks. Roughly 60% of the holdings are in U.S. stocks and 30% are in international stocks, while 10% is allocated to global real estate stocks. As a side note, within this portfolio, is a 20% weighting to a U.S. "S&P 500 like" fund. **Portfolio 60** is our balanced portfolio and it's major weightings are 36% U.S. stocks, 18% international stocks, 6% real estate stocks, 39% bonds, and 1% cash equivalents. Obviously, the **S&P 500 Index** is a capitalization-weighted index of 500 stocks representing all major industries in the U.S. economy.



Past performance does not guarantee or indicate future results. Analytics are presented for informational purposes only and do not constitute an offer or recommendation to buy or sell securities or to engage an investment manager. Mutual fund results do not reflect the deduction of sales loads. Market Indices included are a general source of information and may not be the designated benchmark to evaluate an investment's performance.

"In the business world, the rearview mirror is always clearer than the windshield."
Warren Buffett

For Period Ending Dec 31, 2014	1 Year Total Return	3 Year Average Annual Return	5 Year Average Annual Return	10 Year Average Annual Return	Average Annual Return Since Mar 31, 2000	Volatility Score	Growth of $100,000 since March 31, 2000
Global Portfolio 100	6.34%	17.64%	13.08%	7.86%	8.62%	17.31	$338,624
Global Portfolio 60	4.35%	10.88%	8.72%	6.24%	6.24%	10.29	$268,833
S&P 500 Index	13.69%	20.41%	15.45%	7.67%	4.15%	15.12	$182,293

As you can see in the two charts above, there have been substantial financial rewards to **global diversification**. Many have quickly, forgotten the benefits broad diversification forged during the October 2000 to October 2002 Technology Dot Com Crash…and the Lost Decade for US Stocks that ended in March of 2009. During the Tech Dot Com Crash the S&P 500 Index declined a full 50% in value while the Global Portfolio 100 declined 25% cumulatively. During the period October 1, 2000 to February 27, 2009, the S&P 500 declined 40.3% while the Global Portfolio 100 had a slight gain of 4.5%. **These are substantial benefits in the preservation and creation of wealth over time.** But, many will be lulled into the recency of results to narrow their portfolio blends. And to chase what's hot. There are going to be periods where a U.S. only portfolio will win the performance game. The performance numbers above will show this in the last 1-year, 3-year, and 5-year time frames in the chart above. There are always exceptions to the prevailing laws of nature. To someone not in the profession of wealth management, it can be very frustrating to receive 4% and 6% returns when you hear everyday in the news the major indices of local markets are getting 13% and 14%. But that's where wisdom trumps the avalanche of information…and establishes the next trend line for prudent wealth accumulation.

In light of all that did not happen, there is one more thing we hope continues to not happen. We hope you do NOT *stress over* the current market by succumbing to two common behavioral biases: **Recency**, or giving recent events more weight than they deserve; and **Tracking-Error Regret**, or losing confidence in your personalized diversified portfolio to chase last year's Old Glory returns.

In his article, "There's a Perfect Storm Brewing," financial author, Larry Swedroe describes the risks associated with chasing past performance. While the U.S. S&P 500 Index has outperformed the MSCI EAFE (international stock) Index since 2010 by an annualized return of around 9 percent, the MSCI EAFE happened to deliver about the same outperformance in reverse from 2002-2007. Clearly, the tables can turn abruptly and destructively for an undiversified investor. As Swedroe says, "Diversification is like insurance. It's insurance against having all your eggs in the wrong basket."

"An economic forecaster is like a cross-eyed javelin thrower. They don't win many accuracy contests, but they keep the crowds attention!"
Unknown Author

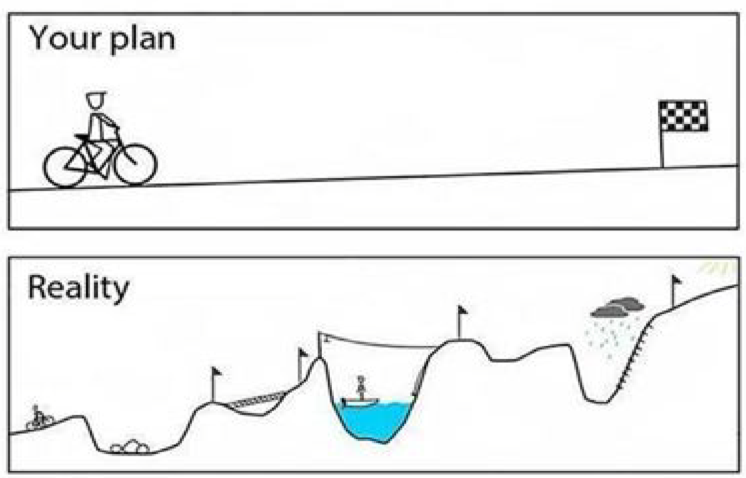
There remains decades of resounding evidence that one year or even several years does not a strategy make. That's why, come what may, we remain as convinced as ever that individualized diversification is the right policy every year. Maintaining a globally diversified portfolio according to your personal goals and risk tolerances does not guarantee that you will outperform other lucky scores you might have made instead. But it continues to offer the most rational approach to reaching your desired destination while managing the rocky paths along the way.

In the spirit of simplicity and length of this letter, I will reserve the discussion of world economic conditions for our phone calls, meetings, and those who have an interest. I have another 100 plus pages of charts and graphs that quietly show continued improvement in the world economy.

I am **in gratitude** each day of you allowing Timonier to be a part of this journey with you. Know that we are accountable as your fiduciaries. And our collaborative team of advisors look forward to another year of assisting you in making conscious choices for this one great life you deserve to live. Contact us any time, if we haven't contacted you first.

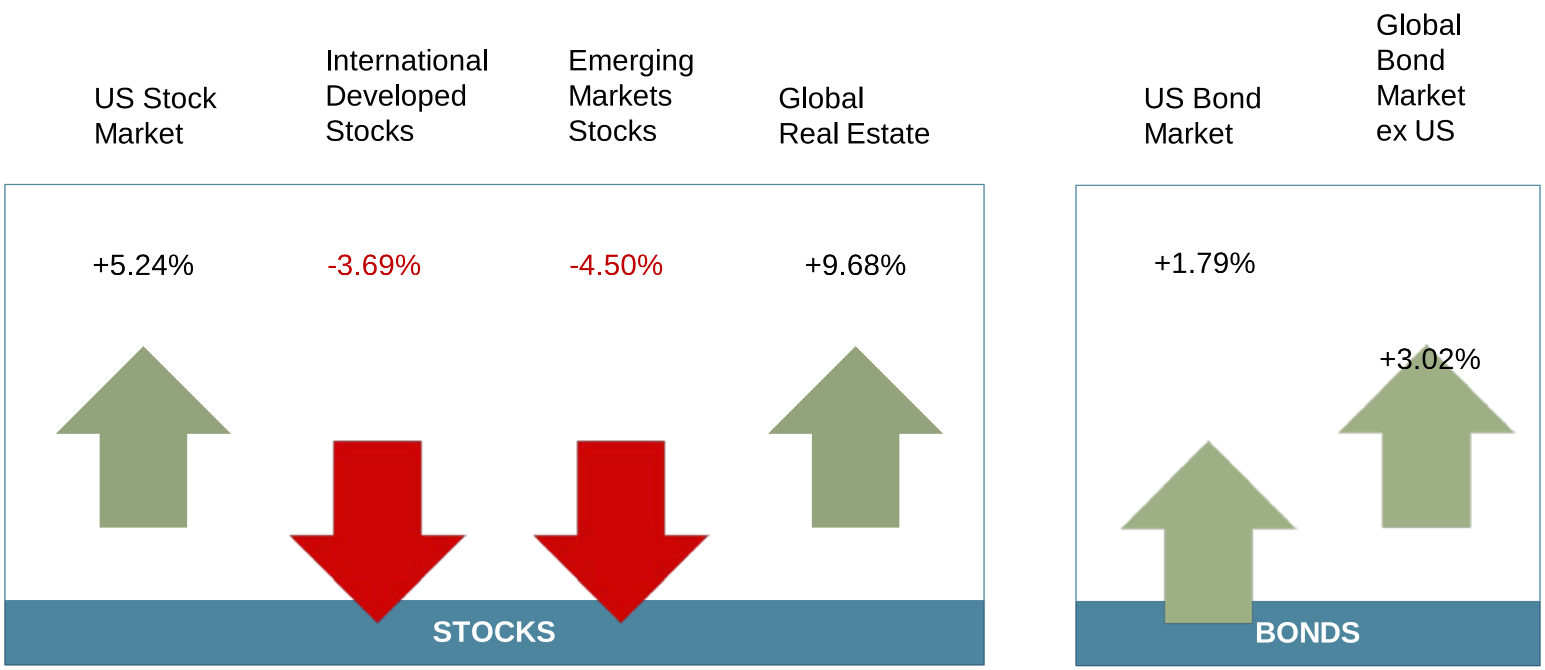
Namaste',

Tim L. Baker, CIMA, GFS



Market Summary

Fourth Quarter 2014 Index Returns



A number of prominent pension plans now consider 'Global Equity' as a single strategic asset class. Consultants too are more frequently recommending a global equity policy benchmark as the starting point for asset allocation. These developments - perhaps a natural consequence of globalization - reflect a possible evolution in the investment process for institutional investors looking to capture a global equity opportunity set and eliminate unintentional home-biases.

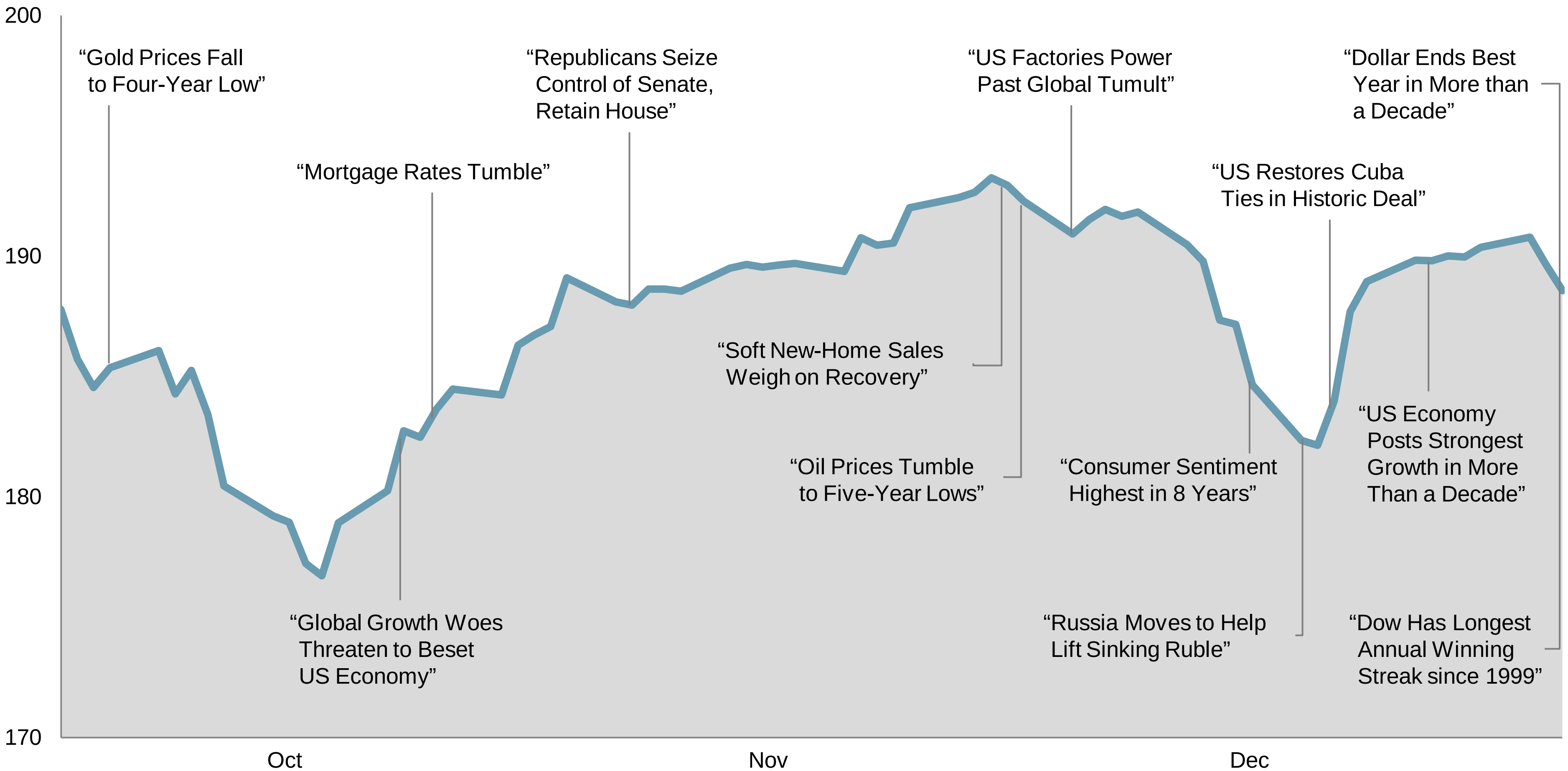
Investors seeking a comprehensive global equity benchmark may consider the MSCI ACWI All Cap Index. It covers approximately 14,000 securities and includes large, mid, small and micro cap size segments for all Developed Markets countries in the index together with large, mid and small cap size segments for the Emerging Markets countries.

~Morgan Stanley Country Index

Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Market segment (index representation) as follows: US Stock Market (Russell 3000 Index), International Developed Stocks (MSCI World ex USA Index [net div.]), Emerging Markets (MSCI Emerging Markets Index [net div.]), Global Real Estate (S&P Global REIT Index), US Bond Market (Barclays US Aggregate Bond Index), and Global Bond ex US Market (Citigroup WGBI ex USA 1−30 Years [Hedged to USD]). The S&P data are provided by Standard & Poor's Index Services Group. Barclays data provided by Barclays Bank PLC.

World Stock Market Performance

MSCI All Country World Index with selected headlines from Q4 2014



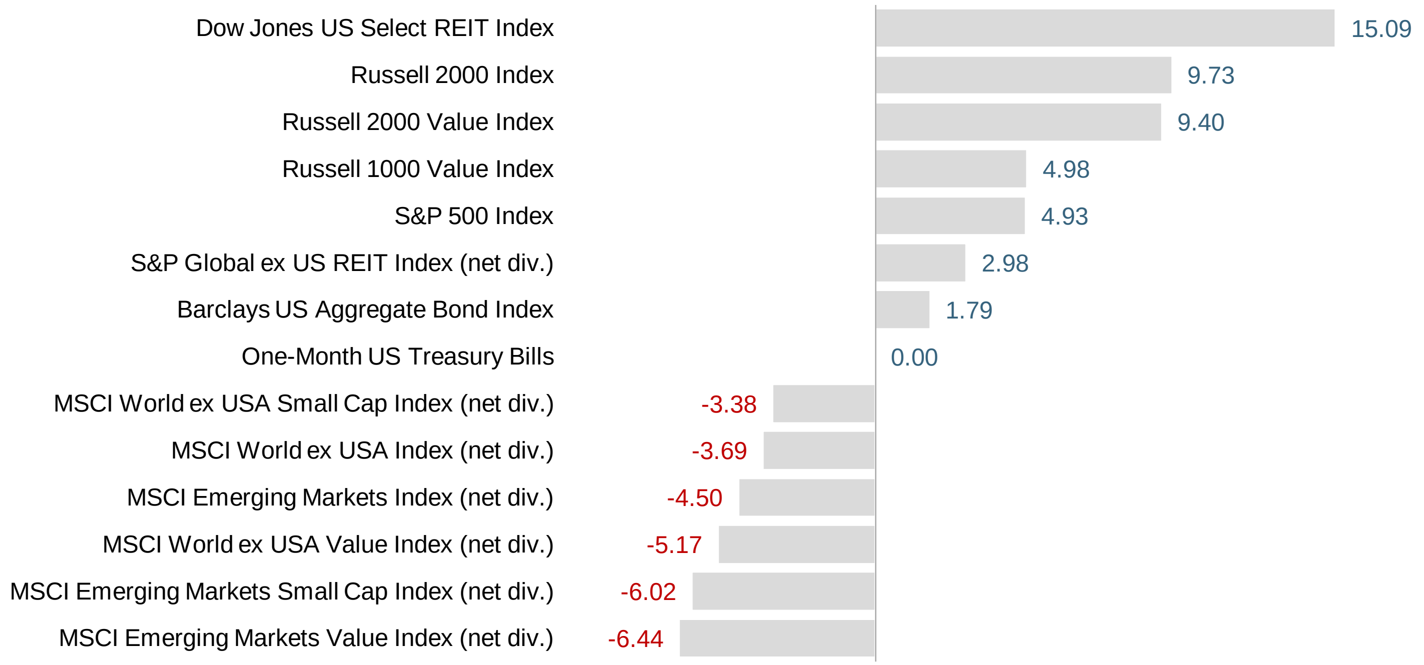
These headlines are not offered to explain market returns. Instead, they serve as a reminder that investors should view daily events from a long-term perspective and avoid making investment decisions based solely on the news.

It is not possible to invest directly in an index. Performance does not reflect the expenses associated with management of an actual portfolio. Past performance is not a guarantee of future results.

World Asset Classes

Fourth Quarter 2014 Index Returns

REITs, particularly in the US, had higher returns than most asset classes in the fourth quarter, outperforming equity indices. US equities performed better than non-US developed and emerging markets. Many equity markets outside the US declined in US dollar terms. Currency movements played a role; the dollar appreciated against most currencies. Small caps outperformed large caps in the US. In developed markets outside the US, small caps slightly outperformed large caps but underperformed in emerging markets. Broad market value indices outperformed growth indices in the US but underperformed in developed markets outside the US and in emerging markets. The results were mixed across size ranges in the various markets.



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US Stocks

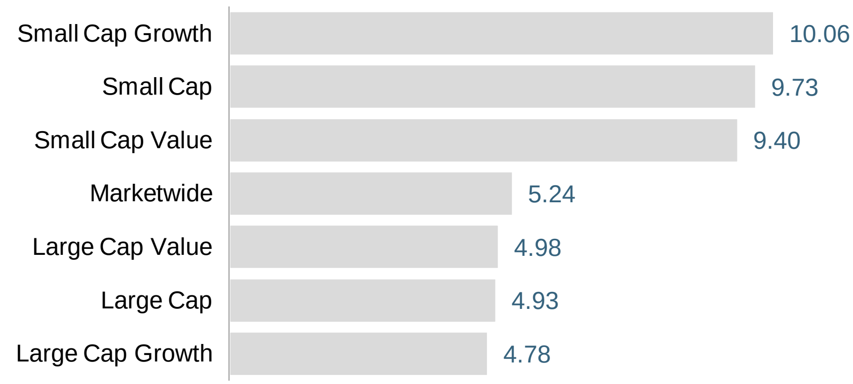
Fourth Quarter 2014 Index Returns

The US equity market performed better than most other markets for the quarter. Small cap indices outperformed large cap indices.

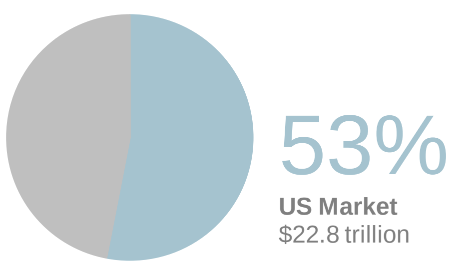
Marketwide value indices outperformed growth indices, and large and mid-cap value indices outperformed their growth counterparts. However, value underperformed growth among both small and micro cap stocks.

REITs, which are included to varying degrees in many benchmarks, boosted index returns.

Ranked Returns for the Quarter (%)



World Market Capitalization—US



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Marketwide	12.56	12.56	20.51	15.63	7.94
Large Cap	13.69	13.69	20.41	15.45	7.67
Large Cap Value	13.45	13.45	20.89	15.42	7.30
Large Cap Growth	13.05	13.05	20.26	15.81	8.49
Small Cap	4.89	4.89	19.21	15.55	7.77
Small Cap Value	4.22	4.22	18.29	14.26	6.89
Small Cap Growth	5.60	5.60	20.14	16.80	8.54

Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Market segment (index representation) as follows: Marketwide (Russell 3000 Index), Large Cap (S&P 500 Index), Large Cap Value (Russell 1000 Value Index), Large Cap Growth (Russell 1000 Growth Index), Small Cap (Russell 2000 Index), Small Cap Value (Russell 2000 Value Index), and Small Cap Growth (Russell 2000 Growth Index). World Market Cap represented by Russell 3000 Index, MSCI World ex USA IMI Index, and MSCI Emerging Markets IMI Index. Russell 3000 Index is used as the proxy for the US market. The S&P data are provided by Standard & Poor's Index Services Group.

International Developed Stocks

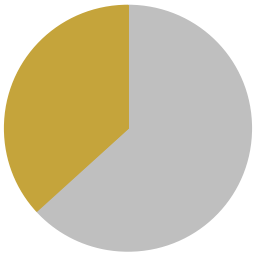
Fourth Quarter 2014 Index Returns

International developed broad market indices measured in US dollars underperformed the US indices but outperformed emerging markets as a group. Small caps slightly outperformed large caps.

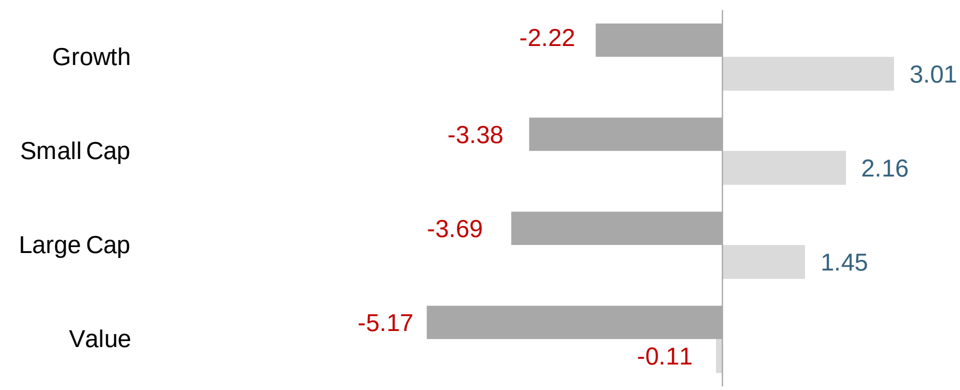
Value underperformed growth across all size segments.

The US dollar strengthened against most currencies during the quarter.

World Market Capitalization—International Developed



Ranked Returns (%)



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Large Cap	-4.32	-4.32	10.47	5.21	4.64
Small Cap	-5.35	-5.35	11.77	7.91	5.87
Value	-5.41	-5.41	10.46	4.52	4.18
Growth	-3.26	-3.26	10.43	5.85	5.04

Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Market segment (index representation) as follows: Large Cap (MSCI World ex USA Index), Small Cap (MSCI World ex USA Small Cap Index), Value (MSCI World ex USA Value Index), and Growth (MSCI World ex USA Growth). All index returns are net of withholding tax on dividends. World Market Cap represented by Russell 3000 Index, MSCI World ex USA IMI Index, and MSCI Emerging Markets IMI Index. MSCI World ex USA IMI Index used as the proxy for the International Developed market.

Emerging Markets Stocks

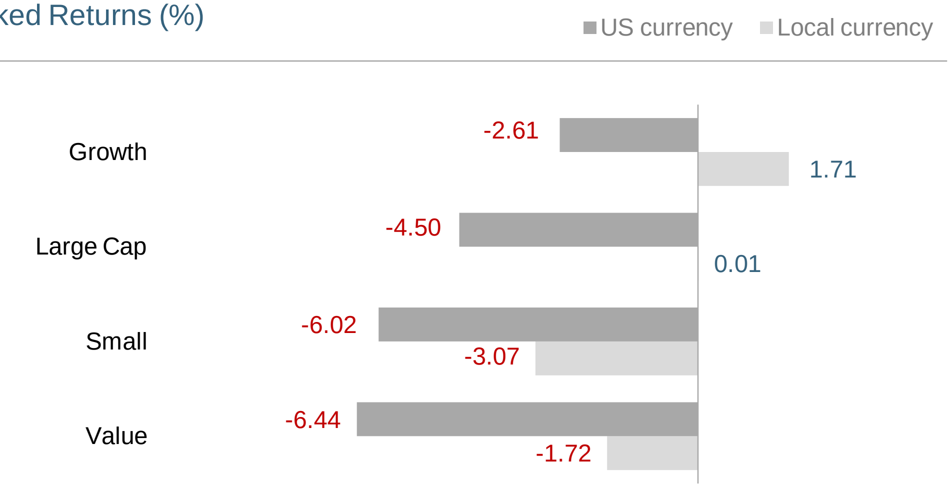
Fourth Quarter 2014 Index Returns

Broad market emerging markets indices underperformed developed markets, including the US.

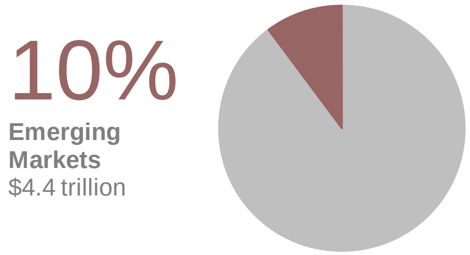
Small cap indices underperformed large cap indices for the quarter. Value indices underperformed growth indices in large caps and mid-caps but outperformed in small caps.

The US dollar strengthened against most currencies during the quarter.

Ranked Returns (%)



World Market Capitalization—Emerging Markets



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Large Cap	-2.19	-2.19	4.04	1.78	8.43
Small Cap	1.01	1.01	7.65	2.93	9.63
Value	-4.08	-4.08	1.79	0.51	8.59
Growth	-0.35	-0.35	6.24	3.00	8.22

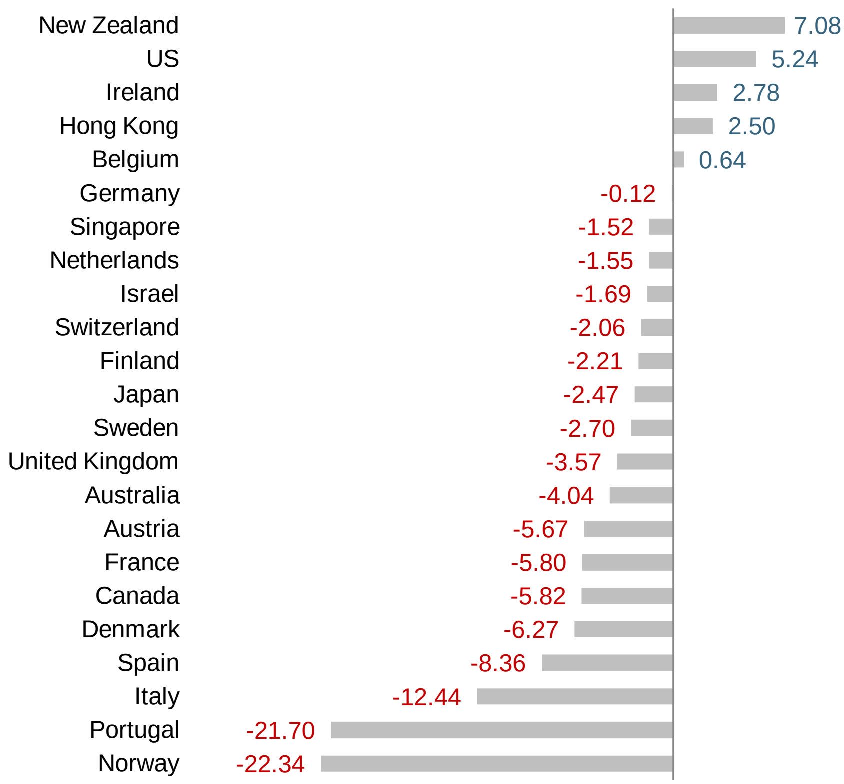
Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Market segment (index representation) as follows: Large Cap (MSCI Emerging Markets Index), Small Cap (MSCI Emerging Markets Small Cap Index), Value (MSCI Emerging Markets Value Index), and Growth (MSCI Emerging Markets Growth Index). All index returns are net of withholding tax on dividends. World Market Cap represented by Russell 3000 Index, MSCI World ex USA IMI Index, and MSCI Emerging Markets IMI Index. MSCI Emerging Markets IMI Index used as the proxy for the emerging market portion of the market.

Select Country Performance

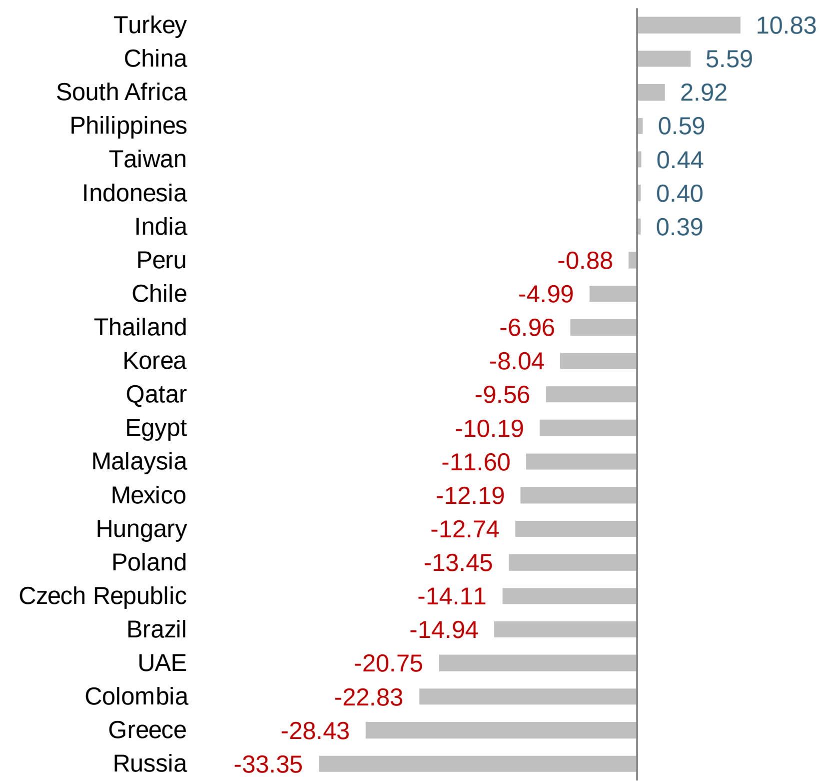
Fourth Quarter 2014 Index Returns

In US dollar terms, New Zealand was the best performer in developed markets during the fourth quarter. The fall in commodity prices, in particular the decline in the price of oil, contributed to the lower performance of commodity-dominated countries such as Norway and Russia. Turkey and China recorded the highest performance among emerging markets.

Ranked Developed Markets Returns (%)



Ranked Emerging Markets Returns (%)



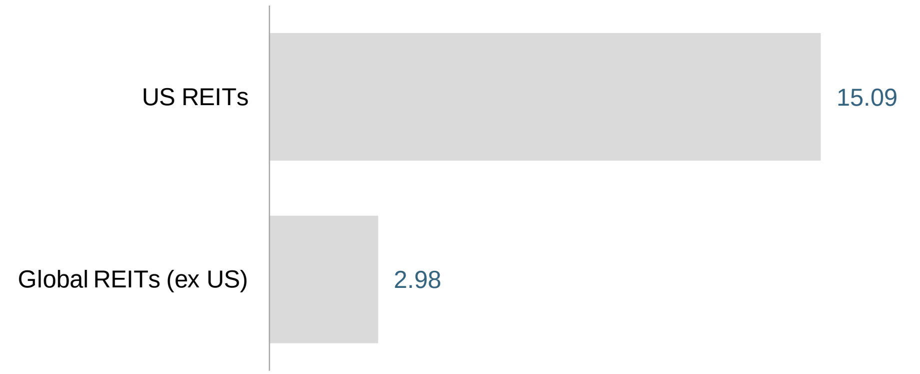
Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Country performance based on respective indices in the MSCI World ex US IMI Index (for developed markets), Russell 3000 Index (for US), and MSCI Emerging Markets IMI Index. All returns in USD and net of withholding tax on dividends. UAE and Qatar have been reclassified as emerging markets by MSCI, effective May 2014.

Real Estate Investment Trusts (REITs)

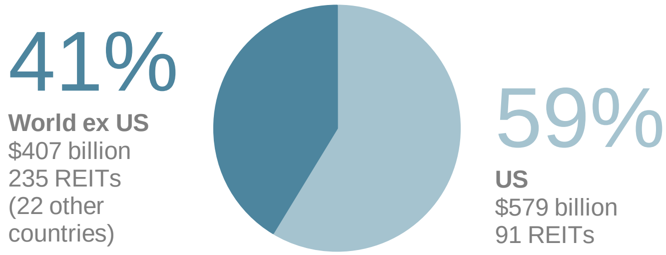
Fourth Quarter 2014 Index Returns

US REITs outperformed the broad equity market for the quarter. REIT indices in developed markets outside the US outperformed broad market equity indices.

Ranked Returns (%)



Total Value of REIT Stocks



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
US REITs	32.00	32.00	16.10	16.99	8.13
Global REITs (ex US)	10.94	10.94	14.42	9.86	4.29

Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio.
Number of REIT stocks and total value based on the two indices. All index returns are net of withholding tax on dividends. Total value of REIT stocks represented by Dow Jones US Select REIT Index and the S&P Global ex US REIT Index. Dow Jones US Select REIT Index used as proxy for the US market and S&P Global ex US REIT Index used as proxy for the World ex US market. Dow Jones US Select REIT Index data provided by Dow Jones ©. S&P Global ex US REIT Index data provided by Standard and Poor's Index Services Group © 2014.

Commodities

Fourth Quarter 2014 Index Returns

Commodities were broadly negative during the fourth quarter. The Bloomberg Commodity Index fell 12.10%. Energy led the decline with WTI crude oil and natural gas returning -40.65% and -32.49%, respectively.

Wheat was the best performer with a gain of 21.82%.

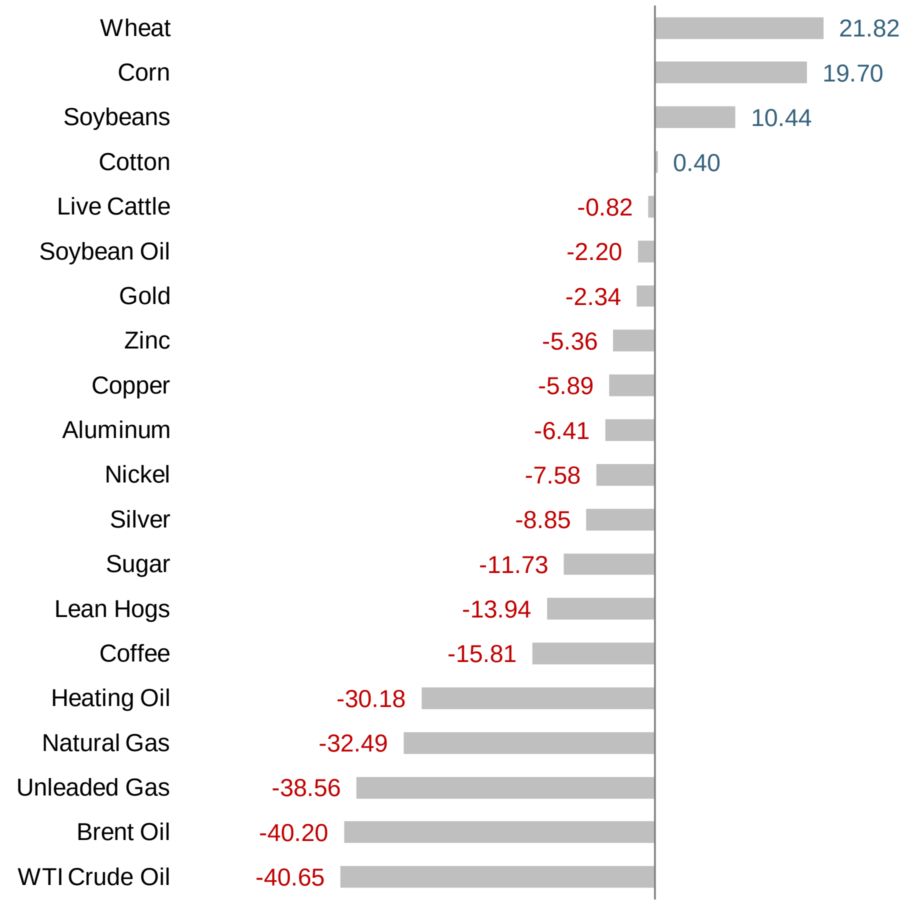
After experiencing negative returns in the third quarter, corn and soybeans gained a respective 19.70% and 10.44% in the fourth quarter.

Period Returns (%)

** Annualized*

Asset Class	YTD	Q4	1 Year	3 Years*	5 Years*	10 Years*
Commodities	-17.01	-12.10	-17.01	-9.43	-5.53	-1.86

Ranked Returns for Individual Commodities (%)



Past performance is not a guarantee of future results. Index is not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. All index returns are net of withholding tax on dividends. Securities and commodities data provided by Bloomberg.

Fixed Income

Fourth Quarter 2014 Index Returns

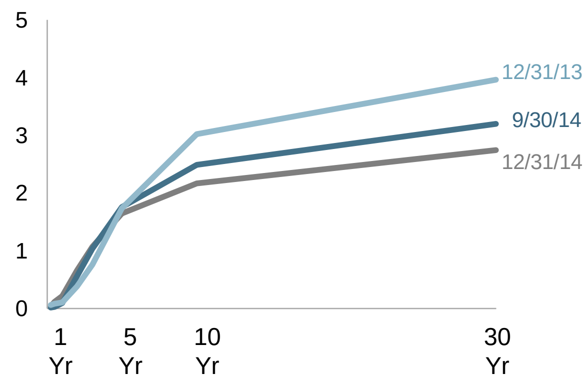
Interest rates across US fixed income markets generally declined during the quarter. The yield on the 10-year Treasury note ended at 2.17%, a dip of 34 basis points over the period. (One basis point equals one-hundredth of a percentage point.) Long-term US Treasury bonds gained 27% in 2014.

While intermediate- and long-term rates declined, short-term rates increased. The two-year Treasury note was up 10 bps to 0.68%.

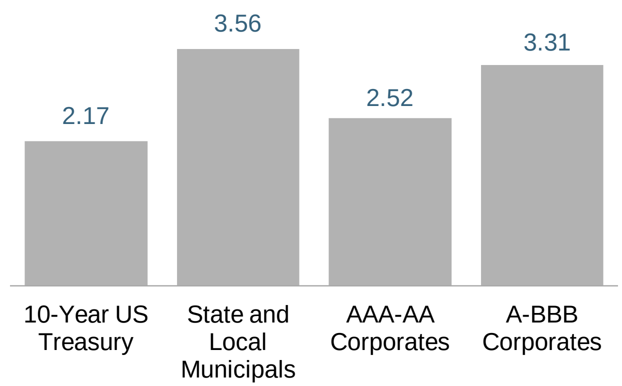
Long-term corporate bonds returned 3.98% for the quarter and 15.73% for the year. Intermediate-term corporates gained 85 bps for the quarter and 4.35% for the year.

Municipal revenue bonds (+1.54%) again slightly outpaced municipal general obligation bonds (+1.11%) for the quarter. Long-term munis continued to outperform all other areas of the curve.

US Treasury Yield Curve



Bond Yields across Issuers



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
BofA Merrill Lynch Three-Month US Treasury Bill Index	0.04	0.04	0.07	0.09	1.54
BofA Merrill Lynch 1-Year US Treasury Note Index	0.18	0.18	0.23	0.41	2.00
Citigroup WGBI 1−5 Years (hedged to USD)	1.90	1.90	1.54	1.78	3.11
Long-Term Government Bonds	23.87	23.87	4.29	9.88	7.48
Barclays US Aggregate Bond Index	5.97	5.97	2.66	4.45	4.71
Barclays US Corporate High Yield Index	2.45	2.45	8.43	9.03	7.74
Barclays Municipal Bond Index	9.05	9.05	4.30	5.16	4.74
Barclays US TIPS Index	3.64	3.64	0.44	4.11	4.38

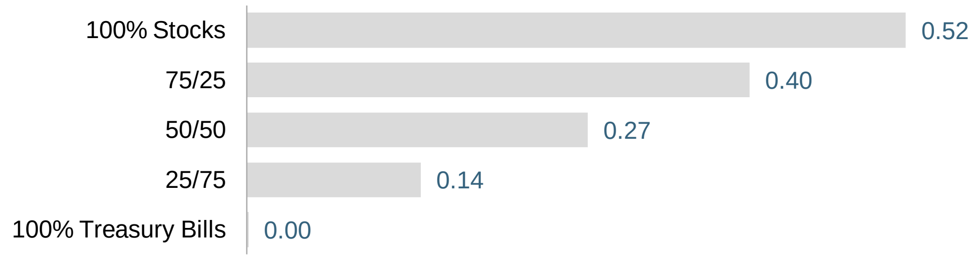
Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Yield curve data from Federal Reserve. State and local bonds are from the Bond Buyer Index, general obligation, 20 years to maturity, mixed quality. AAA-AA Corporates represent the Bank of America Merrill Lynch US Corporates, AA-AAA rated. A-BBB Corporates represent the Bank of America Merrill Lynch US Corporates, BBB-A rated. Barclays data provided by Barclays Bank PLC. US long-term bonds, bills, inflation, and fixed income factor data Merrill Lynch, Pierce, Fenner & Smith Incorporated is a wholly owned subsidiary of Bank of America Corporation.

Global Diversification

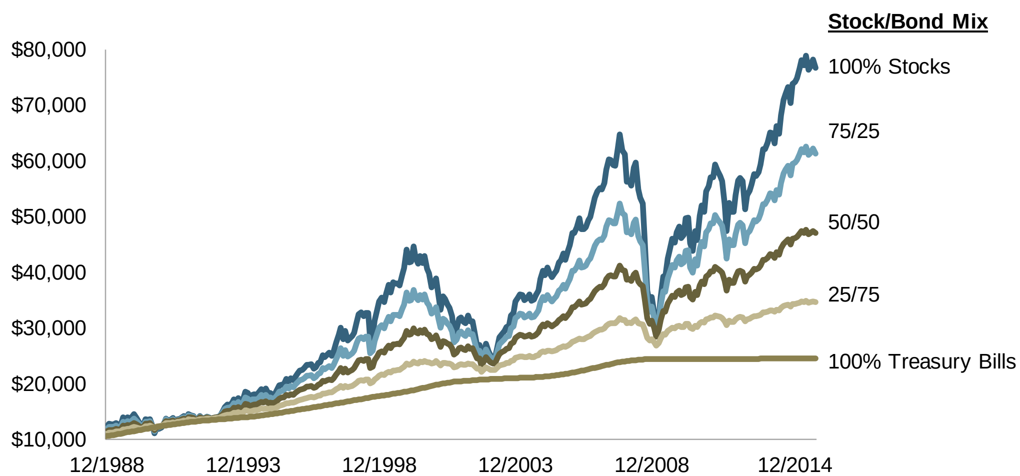
Fourth Quarter 2014 Index Returns

These portfolios illustrate the performance of different global stock/bond mixes and highlight the benefits of diversification. Mixes with larger allocations to stocks are considered riskier but have higher expected returns over time.

Ranked Returns (%)



Growth of Wealth: The Relationship between Risk and Return



Period Returns (%)

** Annualized*

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
100% Stocks	4.71	4.71	14.72	9.74	6.65
75/25	3.58	3.58	10.99	7.45	5.60
50/50	2.43	2.43	7.29	5.07	4.37
25/75	1.24	1.24	3.64	2.60	2.98
100% Treasury Bills	0.02	0.02	0.03	0.05	1.42

Diversification does not eliminate the risk of market loss. Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect expenses associated with the management an actual portfolio. Asset allocations and the hypothetical index portfolio returns are for illustrative purposes only and do not represent actual performance. Global Stocks represented by MSCI All Country World Index (gross div.) and Treasury Bills represented by US One-Month Treasury Bills. Globally diversified allocations rebalanced monthly, no withdrawals. Data © MSCI 2015, all rights reserved. Treasury bills © Stocks, Bonds, Bills, and Inflation Yearbook™, Ibbotson Associates, Chicago (annually updated work by Roger G. Ibbotson and Rex A. Sinquefield).

So…Are We Keeping Pace with the Indices?

Our financial forecasts developed in our ***MasterPlan*** reports are predicated on achieving investment returns as illustrated by globally diversified indices. Below are the primary equity asset class structures that we use to design our investment portfolios. Their returns are compared to the benchmark of stocks that they have a high degree of correlation with (as noted by R^2). In order for our forecasts to have validity we need to at least match the indices returns ***in aggregate***. **So far so good!** The results are illustrated for the past 5 and 10 years and since inception. By example, the US Micro Cap Portfolio has outperformed the Russell Microcap and Russell 2000 Index by 169 basis points per year since 1982. 169 basis points is equal to 1.69% of outperformance on average per year.

Performance against Conventional Benchmarks

As of December 31, 2014

Annualized difference (100 bps equals 1.0%)

Dimensional Structured Stock Portfolio	Inception	Conventional Benchmark Indices	Last 5 Years	Last 10 Years	Since Inception	R^2
US Micro Cap Portfolio	1982	Russell Microcap and 2000 Index	138	182	169	0.93
US Small Cap Portfolio	1992	Russell 2000 Index	181	106	143	0.98
US Small Cap Value Portfolio	1993	Russell 2000 Value Index	251	104	198	0.94
US Targeted Value Portfolio	2000	Russell 2000 Value Index	198	143	222	0.95
US Large Cap Value Portfolio	1993	Russell 1000 Value Index	160	80	45	0.93
International Small Company Portfolio	1996	MSCI World ex USA Small Cap Index	37	80	302	0.97
International Small Cap Value Portfolio	1995	MSCI World ex USA Small Cap Index	52	123	393	0.93
International Value Portfolio	1994	MSCI World ex USA Index	-102	-5	142	0.92
Emerging Markets Small Cap Portfolio	1998	MSCI Emerging Markets Index	317	224	449	0.89
Emerging Markets Value Portfolio	1998	MSCI Emerging Markets Index	-185	35	371	0.92
Emerging Markets Portfolio	1994	MSCI Emerging Markets Index	90	13	125	0.93

* Long-term outperformance of popular benchmarks with reasonable tracking (as noted by R^2)

Living with Volatility, Again

Fourth Quarter 2014

Volatility is back. Just as many people were starting to think markets only ever move in one direction, the pendulum has swung the other way. Anxiety is a completely natural response to these events. Acting on those emotions, though, can end up doing us more harm than good.

There are a number of tidy-sounding theories about why markets have become more volatile. Among the issues frequently splashed across newspaper front pages: global growth fears, policy uncertainty, geopolitical risk, and even the Ebola virus.

In many cases, these issues are not new. The US Federal Reserve gave notice it was contemplating its exit from quantitative easing (an unconventional monetary policy used by central banks to stimulate the economy when standard monetary policy has become ineffective). Much of Europe has been struggling with sluggish growth or recession for years, and there are always geopolitical tensions somewhere.

In some ways, the increase in volatility could be just as much a reflection of the fact that volatility has been very low for some time.

Markets do not move in one direction. If they did, there would be no return from investing in stocks and bonds. And if volatility remained low forever, there would probably be more reason to worry.

For those still anxious, here are six simple truths to help you live with volatility:

1.Don't make presumptions.
Remember that markets are unpredictable and do not always react the way the experts predict they will. When central banks relaxed monetary policy during the crisis of 2008-09, many analysts warned of an inflation breakout. If anything, the reverse has been the case with central banks fretting about deflation.

2. Someone is buying.
Quitting the equity market when prices are falling is like running away from a sale. While prices have been discounted to reflect higher risk, that's another way of saying expected returns are higher. And while the media headlines proclaim that "investors are dumping stocks," remember someone is buying them. Those people are often the long-term investors.

3. Market timing is hard.
Recoveries can come just as quickly and just as violently as the prior correction. For instance, in March 2009—when market sentiment was at its worst—the S&P 500 turned and put in seven consecutive months of gains totalling almost 80%. This is a reminder of the dangers for long-term investors of turning paper losses into real ones and paying for the risk without waiting around for the recovery.

4. Never forget the power of diversification.
While equity markets have turned rocky again, highly rated government bonds have flourished. This helps limit the damage to balanced fund investors. So diversification spreads risk and can lessen the bumps in the road.

5. Nothing lasts forever.
Just as loading up on risk when prices are high can leave you exposed to a correction, dumping risk altogether when prices are low means you can miss the turn when it comes. As always in life, moderation is a good policy.

6. Discipline is rewarded.
The market volatility is worrisome, no doubt. But through discipline, diversification, and understanding how markets work, the ride can be made bearable. At some point, value re-emerges, risk appetites reawaken, and for those who acknowledged their emotions without acting on them, relief replaces anxiety.