



Q1 2015 Brought Selective Opportunities

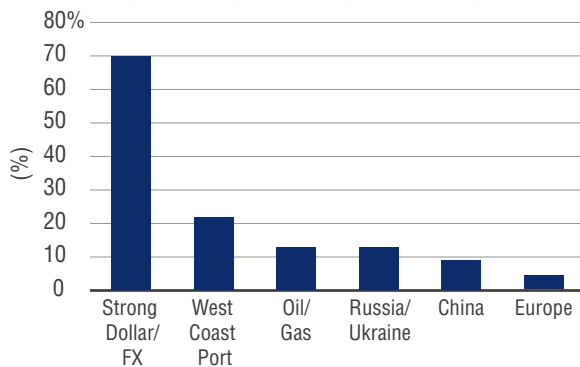
Principals Nicholas Chermayeff, Robert Greenhill Jr. and David Bechtel provide their perspective on the first quarter and their thoughts on the economy and markets as we move forward in 2015.

Strengthening Dollar Crimps Foreign Profits

The first quarter exhibited, yet again, another shift in the investment landscape. Investors tried to figure out how a strengthening dollar would affect U.S. companies' profits and when Chairwoman Yellen would move off of the zero bound (the zero bound is when the short-term nominal interest rate is at or near zero which causes a liquidity trap and limits the ability of the central bank to stimulate economic growth).

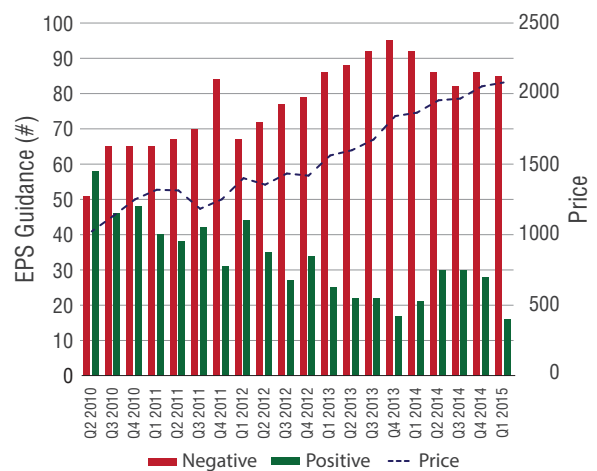
The uptrend in the dollar has weighed on the top line of many S&P 500 companies that receive a large portion of their revenue from overseas. During earnings calls, many S&P 500 companies cited the dollar trend as their greatest headwind. Furthermore, according to FactSet, the first quarter had the lowest number of S&P 500 companies issuing positive guidance since 2006.

Percentage of S&P 500 Companies Citing Negative Impact During Q1 Earnings Calls



Source: Business Insider, FactSet

S&P 500 Negative and Positive Preannouncements: 5-Year



Source: FactSet

Smaller Capitalizations Outperform Larger Brethren

The dollar impact was also apparent in performance results during the first quarter as small- and mid-cap companies, which tend to have less exposure to foreign revenues, significantly outperformed large-cap companies. **(Click here to see our Consequences of a Strengthening Dollar paper for additional context.)**



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Index	Q1 2014	Q2 2014	Q3 2014	Q4 2014	Q1 2015 Sorted
S&P 400 TR	3.04%	4.33%	-3.98%	6.35%	5.31%
Russell 2000 TR	1.12%	2.05%	-7.36%	9.73%	4.32%
S&P 600 TR	1.13%	2.07%	-6.73%	9.85%	3.96%
S&P 500 TR	1.81%	5.23%	1.13%	4.93%	0.95%

Source: Bloomberg

While investors witnessed outperformance by smaller capitalizations, there was also a shift amongst style as investors tended to favor growth over value.

Index	Q1 2014	Q2 2014	Q3 2014	Q4 2014	Q1 2015
S&P 600 Growth	-1.14%	3.52%	-6.96%	6.83%	9.85%
S&P 400 Growth	2.14%	2.90%	-3.29%	5.84%	7.55%
S&P 400 Value	3.99%	5.82%	-4.69%	6.88%	2.83%
S&P 500 Growth	1.39%	5.82%	1.92%	5.06%	2.47%
S&P 600 Value	1.49%	1.52%	-7.99%	8.75%	1.13%
S&P 500 Value	2.26%	4.60%	0.25%	4.78%	-0.69%

Source: Bloomberg

Looking Ahead

Another looming issue that has dominated headlines lately is the Fed's interest rate policy. While the Fed hasn't raised rates in almost 10 years, historically tightening has had little effect on the total return of the S&P 500.

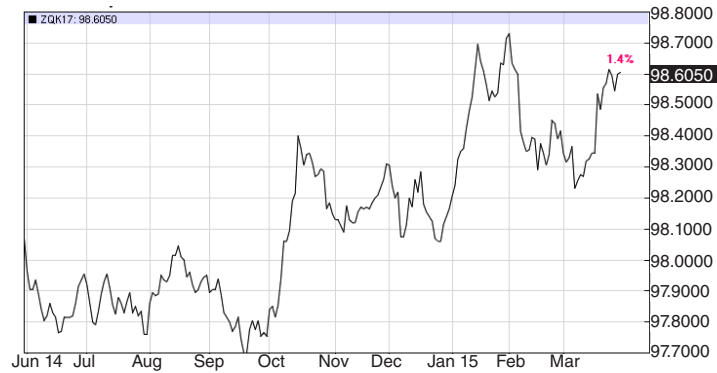
S&P 500 Performance Before and After First Fed Rate Hike

Date of First Raise	6 Months Prior	3 Months Prior	3 Months After	6 Months After	12 Months After
March 1983	27.0%	8.8%	9.9%	8.6%	4.1%
January 1987	0.2%	7.9%	19.1%	21.1%	2.6%
March 1988	-19.8%	4.1%	6.0%	5.4%	13.3%
February 1994	4.7%	2.7%	-3.9%	-2.4%	1.9%
June 1999	11.7%	6.7%	-6.6%	7.0%	6.0%
June 2004	2.6%	1.3%	-2.3%	6.2%	4.4%
Average	4.4%	5.2%	3.7%	7.7%	5.4%

Source: Strategas Research

We also expect the Fed's tightening to occur at a very slow pace, allowing the U.S. economy and markets abroad to digest the changes and adjust. At the end of the first quarter, the May 2017 Fed Funds Futures Contracts were pricing the overnight rate at just 1.4% two years from now.

May 2017 Fed Funds Futures Contract



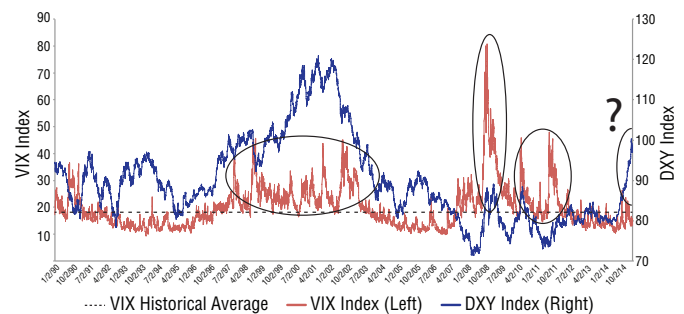
Source: Barchart

Food For Thought

Circling back to our earlier discussion on the strengthening dollar and our outlook for future volatility, the implications of the following historical chart gives us food for thought.

During periods of a strengthening dollar, markets tend to experience above average volatility. With the dollar up significantly in 2015, we still have not seen much activity from the VIX Index. To the extent that volatility returns to the market, we as stock pickers, look forward to the investment opportunities that are likely to present themselves.

Volatility Typically Accompanies Strengthening Dollar



Source: Bloomberg

As we move forward in 2015, we will continue to be methodical and dispassionate about finding opportunities. At Barrow, we focus on spotting attractive entry levels for stocks that have the potential to provide outstanding performance within our portfolios over time. ■



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Important Information

The **S&P 400 Index** is an unmanaged index commonly used to measure the performance of 400 medium-capitalization U.S. stocks. The **Russell 2000 Index** is an unmanaged index commonly used to measure the performance of 2000 U.S. small-capitalization stocks. The **S&P 600 Index** is an unmanaged index commonly used to measure the performance of 600 small-capitalization U.S. stocks that exhibit the strongest growth characteristics. The **S&P 600 Growth Index** is an unmanaged style-concentrated index designed to track the performance of 600 small-capitalization U.S. stocks that exhibit the strongest growth characteristics. The **S&P 400 Growth Index** is an unmanaged style-concentrated index designed to track the performance of 400 medium-capitalization stocks that exhibit the strongest growth characteristics. The **S&P 400 Value Index** is an unmanaged style-concentrated index designed to track the performance of 400 medium-capitalization U.S. stocks that exhibit the strongest value characteristics. The **S&P 500 Growth Index** is an unmanaged style-concentrated index designed to track the performance of 500 large-capitalization U.S. stocks that exhibit the strongest growth characteristics. The **S&P 600 Value Index** is an unmanaged style-concentrated index designed to track the performance of 600 small-capitalization U.S. stocks that exhibit the strongest value characteristics. The **S&P 500 Value Index** is an unmanaged style-concentrated index designed to track the performance of 500 large-capitalization U.S. stocks that exhibit the strongest value characteristics. The **Volatility Index (VIX)** shows the market's expectation of 30-day volatility. It is constructed using the implied volatilities of a wide range of S&P 500 index options. The **DXY Index** (U.S. Dollar Index) is an unmanaged index used to measure the value of the United States dollar relative to a basket of U.S. trade partners' currencies and is a weighted geometric mean of the dollar's value relative to other select currencies. It is not possible to invest directly in indexes which are unmanaged and do not incur fees and charges.

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