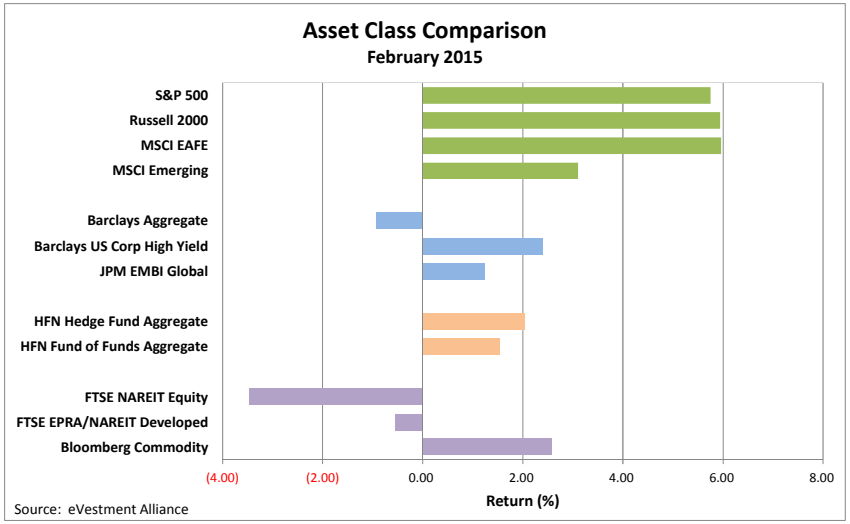
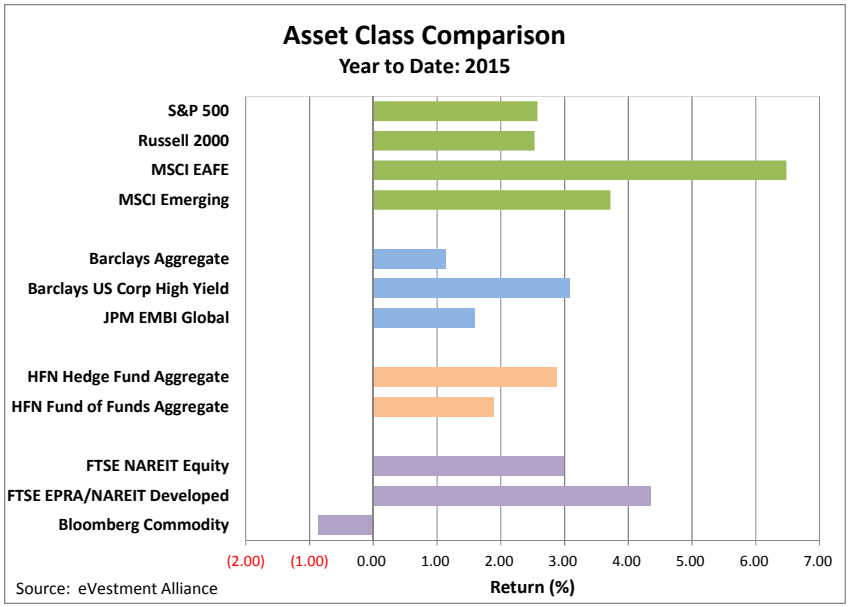
MESA: Monthly Market Flash

February 2015





Market Overview

- A month of real and perceived positive news flow helped investors globally to re-emphasize equities and lower grade credits, putting downward pressure predominantly on U.S. Treasury bonds. Global equity markets soared in February, with many markets posting their best monthly gains in years. Better than expected growth out of Europe and Japan helped fuel foreign market gains. While Greek debt concerns took the headlines early the period, a four-month extension on the debt relief agreement reached in the middle of the month further spurred investor buying in equities. European bonds fell slightly after dramatic increases last month following the announcement of the ECB's €1.1 trillion ECB bond buying program, which commenced in early March.

- While economic data was mixed In the U.S., as were corporate earnings released during the period, strong jobs data coupled with a view that interest rates would remain lower for longer helped keep demand for equities at high levels. A stabilization in energy prices also calmed investors. Comments made by Fed Chair Yellen to Congress in February were interpreted to be dovish given the reference to rate hikes potentially occurring during the 2nd half of the year rather than at the June meeting as had been speculated for some time. While unemployment has cooperated, moving steadily lower toward stated targets, low levels of inflation and moderating economic activity create some near term uncertainty regarding the sustainability of desired growth levels in the U.S. The revision of 4th quarter GDP to 2.2% from 2.6%, released late in the month, added to the perceived softness in recent data.

- U.S. non-investment grade bonds and emerging markets debt saw renewed interest during the period, as spreads came in. With yields rising in the U.S., yield sensitive areas such as REITs and utility stocks were weaker. Hedge fund strategies were all higher, helped by the stronger equity markets and strength in sub-investment grade credits. Commodities finally posted a positive month, thanks to a small recovery in oil prices. Volatility in commodities has been extremely high, driven by large daily fluctuations in oil and precious metals prices.

Equity Markets

- Investors showed renewed enthusiasm for global stocks in February, helped by the stabilization in oil prices, a four-month extension on Greek debt relief by the ECB and a relatively quiet period related to Russia/Ukraine turmoil punctuated by a peace agreement. Comments by Fed Chair Yellen to Congress were perceived as dovish, resulting in a bond to equity rotation for many investors. As a result, U.S. equity markets rebounded strongly from January's decline, with most style and capitalization segments posting their best monthly results since February last year. The S&P 500 index gained 5.75%, the best monthly gain for that index since December 2010. These gains came despite a very strong dollar that has begun to weigh on the results and forward guidance from multi-national corporations.

- All components of the traditional equity style box posted large gains with growth-oriented stocks leading value across the capitalization spectrum. Utilities were the only sector down for the month (-6.4%), pressured by the sharp rise in interest rates. All other sectors were up significantly, with the next lowest returning sector being energy (+4.1%), which posted only its 3rd gain in the last eight months. Cyclical sectors such as consumer discretionary, info technology and materials were all up over 8% for the month.

- Non-U.S. developed equity markets kept pace with the strong gains in the U.S., with the MSCI EAFE index up 5.98%. Europe and Japan were both strong performers, while developed Asia lagged (+4.5%). The Japanese economy emerged from technical recession with 2.2% GDP growth in the 4th quarter, helped by monetary easing, government spending and a trade balance that has swung in a more favorable direction thanks to a weak yen and lower energy prices. European shares responded positively to the ECB's commitment to keep interest rates low, and have been further supported by corporate earnings that have finally started to see meaningful positive revisions. Greece's debt issue got kicked four months down the road, easing the primary concern for European shares in the near term. Emerging markets gained 3.1% for the month, helped by Chinese central bank easing during the period and an end to fighting in the Ukraine. Russia soared 22.8% for the month on the news, but still has a ways to go to claw back the 46% decline suffered in 2014.

Russell U.S. Equity Index Style and Capitalization Returns (%)

February 2015

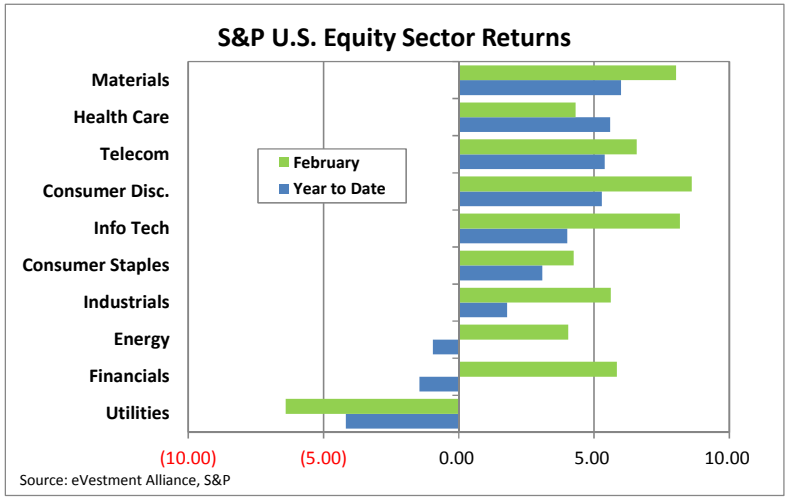
	Growth	Broad	Value
Large Cap	6.67	5.78	4.84
Mid Cap	6.88	5.54	4.10
Small Cap	7.20	5.94	4.64

Source: eVestment Alliance, Russell Indices

Year to Date

	Growth	Broad	Value
Large Cap	5.04	2.87	0.65
Mid Cap	5.08	3.89	2.61
Small Cap	4.76	2.53	0.29

Source: eVestment Alliance, Russell Indices



Non-U.S. Developed Market Returns (%)

	Month	Year to Date
MSCI EAFE ($)	5.98	6.50
MSCI Europe ($)	6.28	6.28
MSCI UK ($)	6.27	5.20
MSCI Japan ($)	6.07	8.55
MSCI Pacific ex Japan ($)	4.49	4.51

Source: eVestment Alliance, MSCI

Emerging Market Returns (%)

	Month	Year to Date
MSCI EM ($)	3.10	3.72
MSCI EM Asia ($)	2.42	4.88
MSCI EM EMEA ($)	4.84	5.02
MSCI EM Latin America ($)	4.21	(2.25)

Source: eVestment Alliance, MSCI

U.S. Fixed Income Returns (%)

	Month	Year to Date
Barclays Aggregate	(0.94)	1.14
Barclays Government	(1.48)	0.98
Barclays U.S. TIPS	(1.20)	1.91
Barclays U.S. Inv. Grade Corp.	(1.01)	1.99
Barclays U.S. Mortgaged Backed	(0.16)	0.69
Barclays U.S. High Yield	2.41	3.09
Credit Suisse Leveraged Loan	1.41	1.67

Source: eVestment Alliance, Barclays, Credit Suisse

Non-U.S. Fixed Income Returns (%)

	Month	2014
Citigroup Non-U.S. WGBI Hedged	(0.38)	1.41
Citigroup Non-U.S. WGBI Unhedged	(0.95)	(2.50)
JP Morgan EMBI Global	1.25	1.59

Source: eVestment Alliance, Citigroup, JP Morgan

Fixed Income Market

- During the month, interest rates increased sharply and the yield curve steepened slightly as global growth appeared to be improving and the flow of capital moved strongly toward equity markets. The yield on the 2-year Treasury rose by 15 bps to 0.63% while the 10-year and 30-year Treasury yields increased by 32 and 35 bps, respectively, to end at 2.00% and 2.60%, respectively. Long Treasuries and credit were the worst performing sectors on the month, with the Barclays Long Gov't/Credit index down 3.38%. Treasury Inflation Protected Securities (TIPS) also experienced considerable weakness, with the index falling 1.2%.

- Investment grade corporate bonds were unable to provide protection during February's rise in rates, with the index falling just over 1%. Speculative grade corporate issues, however, moved sharply higher helped by a rebound in energy prices and the equity market. In February, spreads narrowed from 509 bps to 431 basis points during the month as Treasuries sold off and high yield shares saw buying interest. Similarly, the leveraged loan index gained 1.41% during the period, the largest monthly gain since January 2012. This move offset the 1.10% loss suffered in December last year, which was the largest monthly loss since August 2011. As oil price volatility has increased, and uncertainty over Fed tapering timing increases, volatility of non-investment grade issues has gone up.

- Interest rates increased slightly in Europe after having moved demonstrably lower last month in the wake of the announced ECB buying plans. The U.S. dollar moved higher versus most key currencies in February, resulting in a 57 bps return advantage for the hedged version of the Non-U.S. bond index. Issuance has been increasing in Europe, as U.S. companies look to take advantage of extremely low rates to refinance higher dollar-denominated debt. The emerging bond index was higher despite concerns in Brazil following a meaningful downgrade of Petrobras bonds, raising concerns about the broader market in general. The JPM EMBI index closed the period with a 6.2% yield.

Liquid Alternative Strategies

- Strong equity market returns and spread compression for speculative grade credit proved beneficial for most hedge fund strategies in February. The HFN Hedge Fund Aggregate index delivered its best gain since January 2013, climbing 2.05% for the month, with all major strategies posting gains. Year to date, many hedge fund strategies have already surpassed the returns achieved in all of 2014.

- The biggest beneficiaries of strong global equity markets was the equity long short managers, which as a group were up over 3%. Also performing well were event driven and distressed, gaining 2.9% and 2.6%, respectively. Distressed had been under steady pressure given the backdrop of persistent spread widening in higher yielding issues the prior two quarters. The gain in February represented the strategy's first positive return since June 2014. Last year's best performing category, CTA/managed futures, was up for the month, but was the worst performing strategy (other than dedicated short-selling) with its 0.36% rise, as longer-term trend following struggled with sudden reversals in equity, bond and commodity prices. Equity market neutral was the other lagging strategy, although the 0.53% gain in February was slightly higher than the average monthly gain of 0.46% achieved by the strategy over the past two years.

- Global REITS bucked the positive return trend in February, with U.S. REITs falling nearly 3.5% while non-U.S. REITs fell 0.56%. REITs were a victim to the rise in rates during the period, as historically low yields were deemed less attractive than they had been. REITs were last year's big winner, posting 30% gains in the U.S., a trend that had continued with solid results in January. The yield for the FTSE NAREIT All Equity Index was 3.4% as of the end February.

- After falling each of the prior seven months, the Bloomberg Commodity index finally registered a gain in February, climbing 2.57% thanks in part to increases in oil and related energy prices. The increase only partially offsets last month's loss of 3.3%. Oil recovered as companies slashed capital budgets and idle rigs in response to excess supply, helping the energy segment of the index to gain over 8%. Weakness was primarily seen in precious metals, down nearly 5% for the month.