# Sierra Update

**First Quarter 2014**

18 Years of Excellence
1996-2014

SIERRA INVESTMENT PARTNERS, INC.

## MARKET REVIEW

Depressed by abnormally severe winter weather in much of the nation, U.S. Gross Domestic Product (GDP) likely slowed in the first quarter. Some economists estimate that the above average snowfall and below average temperatures may have shaved 0.5% or more from real growth. Even the foreign trade sector was affected, as the ability to ship products was curtailed by adverse transportation conditions. We expect growth may have been a little less than 2.0%, after rising 4.1% in the final quarter of 2013.

Fortunately, the quarter ended on a much stronger note than it began in the U.S. Retail spending jumped in March, the labor markets are recovering from the inclement weather, nearly all jobs lost during the recession have been recouped, and inflation remains tame. We expect growth to rebound sharply next quarter before returning to more moderate growth in the second half of the year.

On the international front, Europe did not suffer from the same weather and their recovery continued. However, the Japanese market was among the weakest performers, China has the biggest market imbalances to correct, and the situation in Russia is a reminder why some emerging markets warrant high risk premia.

### Domestic Equity

Our **Large Cap Intrinsic Value Equity** product posted a gain of 3.4% (gross) in the quarter, stronger than the S&P 500 and Russell 1000 Value benchmark returns of 1.8% and 3.0%, respectively. Stock selection added most of our outperformance. Our selections in the Consumer Discretionary, Industrials and Technology sectors contributed the most. This strategy is staging a performance recovery as QE is tapered, which we believe is sustainable as correlations between stocks are declining and investors are now differentiating between fundamentally strong companies and all others.

After a strong finish to 2013, the first quarter of 2014 was a much more challenging period for equity investors. Our U.S. **Concentrated Growth** Composite had a difficult time compared to the Growth Index, as high valuation, high momentum stocks in the Index which we do not own performed very well. Mixed economic data releases in the U.S. along with concerns about economic growth in the emerging markets helped drive a sharp market sell-off in January, although equities gained some traction later in the quarter.

We are pleased to report our **Small Value Equity** representative account delivered an absolute return of 2.02% during the first quarter, outpacing the 1.78% performance of the benchmark Russell 2000 Value Index. Top sector contributors included Financials, Industrials, Consumer Staples and Energy. We continue to look for more opportunities to position the portfolio toward a recovering U.S. economy supportive of domestically oriented small cap companies.

### International Equity

Our **Global and Non-U.S. Equity** process has again proven its value through another challenging market cycle. The Global and Non-U.S. Equity composites posted absolute gains in excess of their respective benchmarks, the MSCI All Country World Index and MSCI All Country World ex-U.S. Index, extending recent outperformance across most major short-, medium- and long-term horizons. Our section allocations remained mostly unchanged as value recognition continued to unfold.

In **International and Global Growth Equity**, we saw the MSCI World Index return 1.4% for the quarter in U.S. dollar terms, while the MSCI EAFE Index returned only 0.8%. While European and U.S. equity market returns did not experience big swings, investors moved from favoring growth stocks to favoring value stocks in the United States. This move was reflected among industry and sector returns. We believe falling correlations may mean there is a higher probability that good stockpicks will be rewarded, but in the first quarter of 2014 it meant a wide range of returns between stocks that performed well and those that did not. We believe we are well positioned for the long-term, but may find in the meantime that news flow and investor sentiment will affect returns.

## Fixed Income

In the **Fixed Income** market arena, the Federal Reserve's ("Fed") QE should have benefited maturities longer than five years, and the tapering should have benefited shorter maturities, but this is not what occurred. Interest rates for longer dated maturities outperformed shorter maturities as the yield curve flattened. During the first quarter 2014, ten-year Treasury yields declined while two-year Treasury notes rose. Uncertainty leads to volatility, and the guidance from the Fed has been less than clear recently regarding economic policy.

The **High Yield** market continues to be supported by exceptional fundamentals with a moderately expanding economy and default rates that are approaching all-time lows. Access to capital remains abundant and economic policy remains accommodative, notwithstanding the current tapering program. High yield credit spreads have tightened and index yields are low, which makes credit selection critical since most opportunity for differentiation will be on the downside. Our portfolios modestly outperformed during the quarter due to good sector allocation but primarily from good security selection.

# SIERRA HEADLINES

## Thank You

We would like to extend our appreciation to the **Hawaii Electricians Pension Fund** and **Hawaii Electricians Annuity Fund** for allocating a portion of their assets to Sierra's Concentrated Growth Equity product, and to the **Southern States Savings & Retirement Plan Trust Fund** for allocation a portion of its assets to our Non-U.S. Equity commingled fund.

## DISCLOSURE

Sierra Investment Partners, Inc. (Sierra) is a manager of managers and uses exclusive sub-advisor relationships to manage plan assets. Sierra's sub-advisors are: Pioneer Institutional Asset Management, Inc. for Concentrated Growth Equity & Balanced; Todd Asset Management, LLC for Large Cap Intrinsic Value Equity & Balanced; Franklin Equity Group for Franklin Non-U.S. Equity & Global Growth Equity; Templeton for Non-U.S. Equity & Global Equity; PMG Advisors, LLC for Fixed Income; Robert W. Baird & Co. Incorporated for Small Value Equity; and Fort Washington Investment Advisors, Inc. for High Yield Fixed Income. Performance reflects that of our exclusive sub-advisor for each respective product. Returns are calculated and presented gross of fees. Gross of fees performance is calculated after the deduction of trading costs, but before the deduction of management fees, custodial fees or other fees. Fee schedules are described in Part II of Sierra's Form ADV. Sierra client returns would be reduced by investment management fees. For example, a five year gross annualized return of 20.10% would be reduced to 18.96% after the deduction of annualized fees of 1%. The information provided is historic in nature and should not be taken as any indication of future performance as future investments will be made under different economic conditions and may utilize different securities. The Large Cap Intrinsic Value Equity composite includes all fully discretionary, non-taxable portfolios invested in the equity strategy. The Russell 1000 Index is a market capitalization weighted index that consists of the 1,000 largest securities in the Russell 3000 Index. The S&P 500 Index is a market capitalization weighted index that contains approximately 500 industrial, transportation, utility and financial companies regarded as generally representative of the U.S. stock market. Investments are not limited to the companies in the Russell 1000 or the S&P 500. The Small Value Equity composite includes all fully discretionary, institutional portfolios over $5.0 million invested in the Small Value Equity strategy benchmarked against the Russell 2000. The Russell 2000 is a market capitalization weighted index which measures the performance of approximately 2000 companies that are between the 1000th and 3000th largest in the market. The Russell 2000 Value Index measures the performance of those Russell 2000 companies with lower price/book ratios and lower forecasted growth values. Investments are not limited to the companies in the Russell 2000 or Russell 2000 Value. The indexes chosen to compare performance are not identical in structure to the composites and are provided to represent the investment environment existing during the time periods shown. Indexes are unmanaged, fully invested and do not include deduction of fees or expenses. Information contained herein should be used for one-on-one presentations only and should be accompanied by this performance disclosure. This information is only an explanation of investment philosophy and historic performance and is not meant to be an investment recommendation. For a disclosure prepared in compliance with the Global Investment Performance Standards (GIPS®) and a list of composites and performance results, please call our corporate headquarters at (925) 941-6300. GIPS has not been involved with the preparation or review of this report. Past performance is no guarantee of future results.

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