2016 REVIEW AND 2017 MARKET OUTLOOK

2016 MARKET EVENTS

- The year began with an equity downturn … and rally.
- The United Kingdom's Brexit vote blurred the European economic outlook.
- The U.S. Federal Reserve held steady its short-term interest rate for much of the year.
- The U.S. election results spurred a U.S. equity rally.

Significant events resonated in the capital markets in 2016, most notably the United Kingdom's vote in June to leave the European Union after more than 40 years and the results of the U.S. elections in November. Through it all, the year was marked by a tireless equity rally, with U.S. equity leading the way for Freedom portfolios.

SLOW START, STEADY RALLY

Equities began the year with a six-week downturn as concern over plummeting oil prices and an economic slowdown in China manifested in investor concern for a looming recession. On Jan. 20, oil sold for a 12-year low of less than $27 a barrel and the Standard & Poor's 500 index was down 9% from the first of the year. By mid-February, the S&P 500 was down a total of 10.5%, representing the stock market's worst start to a year and having a negative effect on Freedom portfolios with exposure. While equity markets struggled, most fixed income categories had a positive effect on Freedom portfolios with exposure, as the Bloomberg Barclays U.S. Aggregate index returned 3.03% for the quarter. Ultimately, investor sentiment shifted with an increase in the price of oil and the realization a recession was not imminent. By the end of March, the downturn in domestic large caps had been erased, with the S&P 500 eking out a 1.35% return.

BREXIT – WHAT'S IT MEAN?

The United Kingdom's referendum vote on June 23 to leave the European Union after more than 40 years – known as Brexit – stunned the world and, quite frankly, a good share of the United Kingdom. It marked the first significant manifestation of growing nationalist sentiment throughout Europe. It also sparked a two-day downturn in the equity market as investors pondered the decision's effect on the European and global economies. Calm was quickly restored. By the end of the quarter just seven days later, the equity market had rallied. The S&P 500 returned 2.5% for the quarter, while international developed equities were down 2.0%, as measured by the MSCI EAFE index.

In the third quarter, as investors came to understand the UK's withdrawal from the EU would be prolonged, international equity outperformed domestic equity for the first time since early 2015. Emerging markets led the way, creating a positive impact on portfolios with exposure to this asset class. Emerging markets returned 9.0%, as measured by the MSCI Emerging Markets index.

Commentary is generally written from a passive standpoint and there are limitations to this data as strategies include active management. Actively managed strategies and holdings may have reacted differently during the quarter than the markets segments discussed herein. Indices are not available for direct investment. Any investor who attempts to mimic the performance of an index would incur fees and expenses, which would reduce returns. All investments are subject to risk. There is no assurance that any investment strategy will be successful.

THE FED DILEMMA

At the beginning of the year, the U.S. Federal Reserve made clear its desire for a return to interest rate normalization. Three, maybe four increases were anticipated. Yet, despite positive economic data, the Fed's plans were repeatedly undone by timely events – the equity downturn to start the year, the Brexit vote in June and the looming U.S. election in the fall. Ultimately, each of those events caused only brief fluctuations in the capital markets, but the Fed's repeated decision not to raise the short-term interest rate likely allowed the markets to keep their footing. Finally, the Fed raised the rate 0.25% in December, and forecast two, maybe three increases in 2017. The rate increase, coupled with a year-end surge in U.S. equities, contributed to core fixed income posting its worst quarterly return in more than 36 years, a loss of -2.98% as measured by the Bloomberg Barclays U.S. Aggregate index. For the year, core fixed income returned 2.65%.

U.S. ELECTION BRINGS SURPRISING RETURNS

At first, the notion of a Donald Trump victory in the U.S. presidential election sparked concern for the stock market, as futures trading on election night forecast a post-election downturn. In the following days and weeks, however, stocks climbed. Amid expectations the new administration will encourage economic growth with fiscal stimulus initiatives and a reduced regulatory climate, investor confidence increased. The four major U.S. stock indices – the S&P 500, Dow Jones Industrial Average, Nasdaq and Russell 2000 – reached new highs. The S&P 500 returned 3.82% for the quarter, finishing the year with a gain of 11.96%. Underscoring the importance of diversification, Freedom investors with exposure to U.S. small caps saw a positive impact from a year-end surge as this asset class returned 8.83% for the quarter and 21.31% for the year. Conversely, non-U.S. assets were challenged, creating a negative impact on portfolios with exposure to international developed equity, which returned -0.71% as measured by the MSCI EAFE index; emerging markets, which returned -4.16% as measured by the MSCI Emerging Markets index; and global real estate, which returned -5.39% as measured by the FTSE EPRA/NAREIT Developed index.

FINAL THOUGHTS

The equity rally of 2016 brought with it positive returns across most asset classes represented in Freedom portfolios. Despite investor enthusiasm, the Asset Management Services (AMS) Investment Committee (IC) continues to have concern for the high price-to-earnings valuations of U.S. large-cap equity, and will watch for earnings to increase and more closely align with prices in the coming year.

2017 MARKET THEMES

- The U.S. economy ended 2016 on solid ground and should continue to improve, with increased earnings expected to help close the equity valuation gap.
- The U.S. Federal Reserve is expected to continue its march toward rate normalization.
- After several years below trend, inflation is picking up.
- Policies enacted by the new administration could have profound economic impact.

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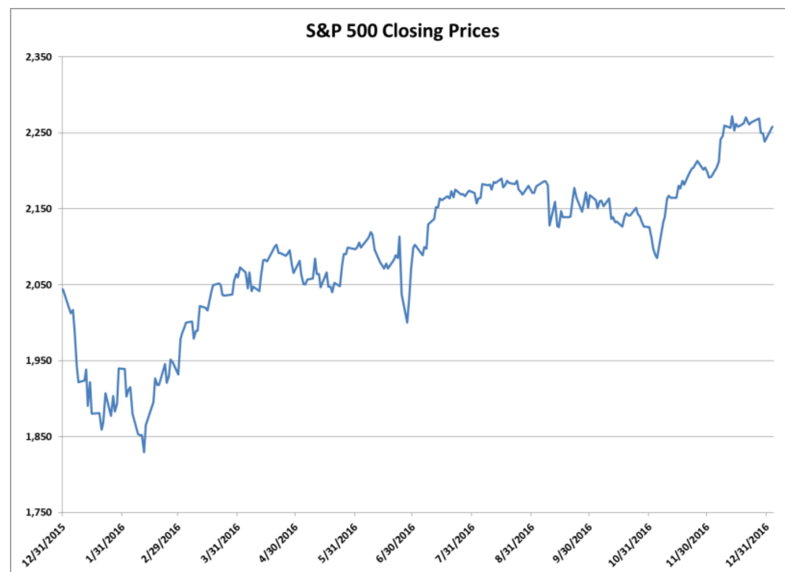
As we turn the page on 2016 – a year that saw positive returns across most asset classes in Freedom portfolios – it's time to turn our eyes toward the future. What will 2017 hold for the capital markets? In large part, the coming year will begin in earnest the journeys sparked by 2016's biggest political events: the United Kingdom's vote to leave the European Union after more than 40 years and the results of the U.S. election. The AMS IC is confident the U.S. economy will continue to improve, at least in the near term, while the outlook in Europe is less enthusiastic.

EQUITY

Domestic equity

The AMS IC believes U.S. economic growth should help produce earnings growth, which should cause the markets to continue to rally. Such growth, however, could depend upon new policies and laws enacted by the new administration, and so might take time.

Decreased regulation, lower taxes, increased fiscal spending and other proposed stimulus measures could promote U.S. economic and corporate earnings growth. Also, tax cuts appear likely, especially to U.S. corporate taxes, which are among the highest in the world. An accommodative repatriation tax could result in an influx of cash from U.S. companies with overseas venues.



Source: Morningstar as of 1/04/2017

Potential headwinds, however, exist. A tariff on imports from countries deemed to be currency manipulators likely would cause prices to rise on those imports and could lead to retaliatory tariffs on U.S. exports, possibly making them less competitive overseas. The potential exists for higher inflation in the United States than other global markets. Over time, stocks have tended to perform well in a steadily rising inflationary market, but not in a rapid one.

The U.S. Federal Reserve is expected to raise its federal funds rate two or three times in 2017, provided it sees proof of continued economic recovery and growth. Central banks around the world, however, are in no rush to raise interest rates, and likely will remain accommodative for some time. This could result in a continued strengthening of the dollar, which could negatively affect U.S. companies with multinational revenues.

U.S. small caps rallied after the presidential election and likely will continue to do so, in our opinion. The IC believes small caps benefitted from better starting valuations compared to larger companies and, going

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forward, likely will benefit from lack of exposure to a strong dollar and foreign revenue, as well as a potentially tightening trade market.

Domestic equity markets have reacted quickly to improving conditions, and the IC has some concern they might have overreacted, with small- and mid-cap stocks leading most markets since the election. The IC has generally recommended slightly reducing exposure to equities across the asset allocation strategies, especially domestic equities, based on increased valuations and declines in profitability and quality in earnings. There are some signs this has begun to improve.

That being stated, the IC could very easily reverse this in favor of more exposure, once it sees confirmation that an even greater acceleration in earnings and economic growth is gaining a foothold to validate current enthusiasm. The IC would like to see earnings grow into equity prices, as they appear positioned to do.

International equity

In Europe, the political divide between nationalism and globalism could continue to hamper economic growth. The emergence of protectionism was exemplified by the United Kingdom's vote to leave the European Union, and the repercussions from that decision are yet to be known. The quickly rising dollar has also contributed to the poor performance of international investments, both stocks and bonds, the past several years. With the dollar expected to strengthen further, exchange rates likely will continue to be unfavorable for U.S. investors in international assets.

It has been the viewpoint of the IC that, relative to the United States, international developed markets were attractive from a valuation standpoint. Yet, if earnings growth fails to materialize and political winds continue to shift toward nationalism, the IC is likely to decrease exposure to developed equity in favor of opportunities for improved valuations and earnings.

Emerging markets

The world's emerging markets, which tend to be dominated by China, have been affected by fluctuating commodity prices, slowing global demand and a strong dollar. Growth rates in emerging markets have slowed from 8% to around 6.5% from 2012 to 2016 according to the National Bureau of Statistics of China, yet still are more than double those of the United States and other developed countries. Despite inherent volatility, emerging markets can offer long-term growth for patient investors with diversified portfolios. The IC has a neutral opinion on emerging market exposure within the pertinent Freedom portfolios at this time.

FIXED INCOME

The tailwinds for economic growth likely will lead to higher interest rates and slightly elevated inflation. The Federal Reserve is expected to raise the federal funds rate two or three times in 2017, which should cause bond yields to rise and prices to fall. Investment grade bonds are not likely to return more than their yield as they face the headwind of rising rates.

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This does not make them a bad investment, if used appropriately. The IC currently uses investment grade fixed income as a way to help mitigate equity volatility in asset allocation strategies. While the IC has reduced exposure to bonds for most of the growth strategies, it holds a slightly larger position for the most conservative strategies, where there is a lessened exposure to equity and mitigating downside risk is paramount.

ALTERNATIVES

If the equity markets continue to rally around new U.S. policies, alternative investments would be possibly challenged. If, however, stock prices have gotten ahead of earnings and interest rates continue to rise, alternative strategies may help investors mitigate some of the downside risk in their portfolios.

FINAL THOUGHTS

The AMS IC is encouraged by what 2017 could potentially have to offer investors, yet is cautious as equity valuations remain elevated compared to historical norms. The IC is watching many factors for signs of continued improvement in valuations, including corporate earnings and economic growth. Consequently, the IC is concerned about the potential impact rising interest rates could have on bond investors, as well as how the stock market might react to actual policy changes compared to its anticipation of such changes. While the enthusiasm for U.S. stocks has risen over most investments, the IC continues to recommend a slightly below normal weight until such time as earnings can grow into these elevated expectations.

Further information on the funds selected for the Freedom portfolios is available by prospectus, which can be obtained through your financial advisor. Investors should carefully consider the investment objectives, risks, charges and expenses of mutual funds and exchange-traded funds before investing. All investments are subject to risk. The prospectus contains this and other information about the funds and should be read carefully before investing.

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There is no assurance that any investment strategy will be successful. All investments carry a certain degree of risk and you may incur a profit or a loss.

RISK: It is important to review the investment objectives, risk tolerance, tax objectives and liquidity needs before choosing an investment style or manager. All investments carry a certain degree of risk and no one particular investment style or manager is suitable for all types of investors, you may incur a profit or a loss.

- High-yield (below investment grade) bonds are not suitable for all investors and may present greater credit risk than other bonds.
- There is an inverse relationship between interest rate movements and fixed income prices. Generally, when interest rates rise, fixed income prices fall and when interest rates fall, fixed income prices generally rise. Bond and bond fund investors should carefully consider risks such as: interest rate risk, credit risk, liquidity risk and inflation risk.
- International investing involves special risks, including currency fluctuations, different financial accounting standards, and possible political and economic instability.
- Investing in emerging markets can be riskier than investing in well-established foreign markets. Emerging and developing markets may be less liquid and more volatile because they tend to reflect economic structures that are generally less diverse and mature and political systems that may be less stable than those in more developed countries.
- Investing in small-cap stocks generally involves greater risks, and therefore, may not be appropriate for every investor. Stocks of smaller or newer or mid-sized companies may be more likely to realize more substantial growth as well as suffer more significant losses than larger or more established issuers.
- Commodities trading is generally considered speculative because of the significant potential for investment loss. Among the factors that could affect the value of the fund's investments in commodities are cyclical economic conditions, sudden political events, changes in sectors affecting a particular industry or commodity, and adverse international monetary policies. Markets for precious metals and other commodities are likely to be volatile and there may be sharp price fluctuations even during periods when prices overall are rising.
- Specific sector investing such as real estate can be subject to different and greater risks than more diversified investments. Declines in the value of real estate, economic conditions, property taxes, tax laws and interest rates all present potential risks to real estate investments.
- Some accounts may invest in Master Limited Partnership ("MLP") units, which may result in unique tax treatment. MLPs may not be appropriate for ERISA or IRA accounts, and cause K-1 tax treatment. Please consult your tax adviser for additional

information regarding the tax implications associated with MLP investments.

- Alternative investments are generally considered speculative in nature and may involve a high degree of risk, particularly if concentrating investments in one or few alternative investments. These risks are potentially greater and substantially different than those associated with traditional equity or fixed income investments. The investment strategies used by certain Funds may require a substantial use of leverage. The investment strategies employed and associated risks are more fully disclosed in each Fund's prospectus, which is available from your financial advisor.
- Changes in the value of a hedging instrument may not match those of the investment being hedged.
- These portfolios may be subject to international, small-cap and sector-focus exposures as well. Accounts may have over weighted sector and issuer positions, and may result in greater volatility and risk.
- Companies in the technology industry are subject to fierce competition, and their products and services may be subject to rapid obsolescence.

INDEX DESCRIPTIONS:
These indices are not available for direct investment. Any product which attempts to mimic the performance an index will incur expenses such as management fees and transaction costs that reduce returns.

Bloomberg Barclays U.S. Aggregate Bond Index (U.S. Fixed Income): This index includes investment grade U.S. Government bonds, corporate bonds, mortgage pass-through securities and asset-backed securities that are publicly offered for sale in the United States. The securities in the index must have at least one year remaining to maturity.

Dow Jones Industrial Average: The Dow Jones Industrial Average (DJIA) is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange (NYSE) and the NASDAQ. The DJIA was invented by Charles Dow back in 1896. Often referred to as "the Dow," the DJIA is one of the oldest, single most-watched indices in the world. When the TV networks say "the market is up today," they are generally referring to the Dow.

FTSE EPRA/NAREIT Developed Index: This index is designed to represent general trends in eligible real estate equities worldwide. Relevant activities are defined as the ownership, disposal and development of income-producing real estate. The index series now covers Global, Developed and Emerging indices, as well the UK's AIM market.

MSCI EAFE Index (International Large Cap): A free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the U.S & Canada. It consists of the following 22 developed market country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Greece, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom.

MSCI EM Index: An index created by Morgan Stanley Capital International (MSCI) designed to measure equity market performance in global emerging markets. It is a float-adjusted market capitalization index that consists of indices in 23 emerging economies: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Greece, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Peru, Philippines, Poland, Qatar, Russia, South Africa, Taiwan, Thailand, Turkey and the United Arab Emirates.

Russell 2000 (U.S. Small Cap): Measures the performance of the 2,000 smallest companies in the Russell 3000 Index, which represent approximately 8% of the total market capitalization of the Russell 3000 Index.

Russell 3000: A market capitalization weighted equity index maintained by the Russell Investment Group that seeks to be a benchmark of the entire U.S. stock market. More specifically, this index encompasses the 3,000 largest U.S.-traded stocks, in which the underlying companies are all incorporated in the U.S.

S&P 500 Index (U.S. Large Cap): The index consists of 500 of the largest stocks in the U.S. stock market. A market value weighted index (stock price times number of shares outstanding after float adjustment), with each stock's weight in the index proportionate to its market value.
-momentum strategies. Other strategies included in this category are systematic mean-reversion, discretionary global macro strategies, commodity index tracking, and other futures strategies.

Nasdaq: A global electronic marketplace for buying and selling securities, as well as the benchmark index for U.S. technology stocks. Nasdaq was created by the National Association of Securities Dealers (NASD) to enable investors to trade securities on a computerized, speedy and transparent system, and commenced operations on February 8, 1971. The term "Nasdaq" is also used to refer to the Nasdaq Composite, an index of more than 3,000 stocks listed on the Nasdaq exchange that includes the world's foremost technology and biotech giants.

TERMS & DEFINITIONS:
Commodity: A commodity is a basic good used in commerce that is interchangeable with other commodities of the same type. Commodities are most often used as inputs in the production of other goods or services. The quality of a given commodity may differ slightly, but it is essentially uniform across producers. When they are traded on an exchange, commodities must also meet specified minimum standards, also known as a basis grade.

National Bureau of Statistics of China: This is an agency within the State Council of the People's Republic of China charged within the collection and publication of statistics related to the economy, population, and society at national and local levels.

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