Quant Coalescence

November '2015: "Fool us Once….."

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Our October newsletter was titled, Fed Surprises by Holding Off on Rate Increase, Dollar Weakens, Commodities Rise.

The sentiment that the Fed will hold off until well into 2016 to raise rates lasted for about a month and now with the surprisingly strong November jobs report released last week, Fed Fund futures are once again indicating that Janet Yellen, et al are more likely than not to raise rates before the end of 2015.

Since the middle of August, the Fed has failed miserably at trying to keep the markets stable with transparency and telegraphing their intentions of the timing of a rate hike. Since then, the equity markets have been down 10%, back up 5.3%, back down 5.8%, back up 12% and as of today back down almost 4% from the recent highs. One week the market is sure that the Fed is moving and the next week the market is certain they will wait and so on. In the words of Yogi Berra, who I see just passed away in September, "It's like déjà vu all over again". The Fed's "transparent guidance" attempt is about as helpful as another "Berra-ism"…"When you come to a fork in the road, take it." In Janet's defense, it is not uncommon for markets to experience these types of swings after an extended bull market like we have had. With P/E's again getting very rich and negative overall earnings being reported last quarter for the first time since 2009, the market is very nervous about not only the first rate hike, but what the Fed will do after the first hike.

We have said for quite some time that with equities close to all-time highs and bonds in a 30 plus year Bull Run, how can portfolios be truly diversified with a traditional 60% equities/40% bonds mix? It will be difficult for bonds to make up for the losses in equities when the market does have a pullback. I read an article this week titled, "60/40 Portfolios are Hopelessly Broken" by Jeff Benjamin. In it he states that Yale University's endowment currently has only a 6% allocation to stocks and a 5% allocation to bonds. The rest is invested amongst strategies like ours that are highly non-correlated to stocks or bonds and/or have the ability to make positive returns in falling markets. It is nice to see validation of our philosophy from one of the most successfully managed endowments in the world.

Many of our models were positioned to make positive returns in the 10% correction that we saw in August and performed much better than their benchmarks for the 3rd quarter. The models also did a good job of rotating out of the inverse positions and avoiding a "whipsaw" as the markets rebounded in October

The November allocations theme is equities with a bias towards dividend payers, commodity exporting countries, technology, materials and emerging market bonds. Many of these are a result of "following the money" after the Fed surprised by not raising rates in late September. As mentioned above, the rate hike is now back on the table for December.

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PCM Strategies: 11.01.2015 Allocations*

*(Please note that performance numbers on the website for indexes do not include dividends and are appropriately calculated sequentially.)

1. PCM US Bond Total Return Index sm : Investment grade corporates cash equivalent.
2. PCM Absolute Bond Index sm : 1-3 month U.S. Treasury bills and emerging market bonds.
3. PCM Absolute U.S. Sector Index sm : Technology, materials and consumer discretionary.
4. PCM U.S. Industries Total Return Index sm : Added technology and REITs, and remained in consumer staples and the insurance industry.
5. PCM Absolute Equity Income Index sm: REITs and dividend paying equities.
6. PCM Emerging Market Total Return Equity Index sm : BRIC's, emerging Asia and cash equivalent.
7. PCM Total Return Portfolio Index sm and PCM Stable Growth Plus+ Portfolio Index sm : Technology, materials and dividend payers is also a common theme, both Indexes also hold the Japanese yen and emerging market bonds.
8. PCM Global Tactical Index sm : Equities in New Zealand, technology, consumer discretionary, and dividend payers in the U.S. and broad based U.S. equities.
9. Global Macro Index sm : Exposure to the U.S. dollar, broad based U.S. equities, emerging market bonds and cash equivalent.
10. PCM Alpha 1 Index sm : Dividend payers.
11. PCM Absolute Commodities Index sm : Gold and sugar.

We have enhanced our website at http://www.pcminvestment.com. One of the main enhancements is that we now include performance for both our indexes and our composites, as applicable. Also new; you will be asked to enter your email address to get into the website. There will be no password required, so you won't have to worry about forgetting it. This is partly due to helping us stay in compliance with requirements in our industry that we know who has reviewed our website content. Also, links in this newsletter to individual indexes have been removed temporarily. Please use the website link above to see all of our indexes and composites.

PCM Index Strategy composites have been recognized for performance by Informa Investment Solutions; most recently for the PCM Absolute Bond Composite sm for the three year performance ending the 4th quarter of 2014, as well as previous awards for 1-year trailing performance and 3-year trailing performance. As of 2nd quarter 2014, the PCM Absolute Bond Composite sm and the PCM Absolute Commodities Composite sm both won a "Top Gun" award for performance in their respective category for the 1-year trailing performance period, with the PCM Absolute Bond Composite sm also winning the "Top Gun" award for 3-year trailing performance. The PCM Alpha 1 Composite sm was awarded the "Top Gun" performance award for the 1st quarter of 2014. We are very pleased to see these particular multi directional strategies being recognized, as the PCM Absolute Bond Strategy sm and PCM Alpha 1 Strategy sm are particularly timely for where we are in the current market cycle.

To view Morningstar Fact sheets of all of our index models, please visit our website at ww.pcminvestment.com under the "PCM mult- directional Strategies" tab.

The views and strategies described herein are for illustrative purposes only and may not be suitable for all investors. The information is not

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About "PCM Quant Coalescence"

Welcome to Provident's "Quant Coalescence" communication. We suspect that many of you are no different than us. That is to say that when our quantitative models rebalance every 2 weeks for some indexes or once a month for other indexes, you sometimes find yourselves asking "What is behind a rotation into that ETF?" This communication is our opportunity to "unite for a common end" with our clients and partners; keeping you updated on our thoughts and perspectives. As you know, our indexes are based on an absolute approach: we strive to make money in up markets or down markets, while trying to greatly minimize loss in any market environment.

Our indexes are also quantitative, reflective of our systematic, unbiased and technical approach. Since our indexes are unbiased, the quantitative models would obviously at times rotate into positions that cause us to scratch our heads. Nevertheless, being so close to the analysis as it unfolds, allows us to quickly begin to validate the fundamental reasons behind the quantitative "following of the money." At other times, the trades are not validated right away; the story unfolds as the days pass. We have been very excited about many of these "validations" and "ah ha" moments. We had another "ah ha" moment when we decided that these insights would also be interesting to those who have entrusted us with their financial peace of mind. Our goal is to be short and to the point, specific to what is happening in our indexes rather than a lengthy macroeconomic perspective.

For further disclaimers and disclosures, see our website for index disclosures and composite disclosures.