



2015 MARKET OUTLOOK

 WEALTHMANAGEMENT



Each New Year brings a new set of challenges on how to position a portfolio. There are literally thousands of data points to examine and evaluate in order to properly allocate an investment.

At WT Wealth Management we constantly ask ourselves how the financial markets will perform, what sectors will outperform, what rates will be higher or lower, if this will be the year the international markets finally stage a comeback, and if oil will rebound or potentially drop even further.

Furthermore, we strive to calculate how all of these issues affect investments in our clients' portfolios; and while we are not in the prediction making business, we do examine the plethora of empirical data made available by central banks around the world and develop a "game plan" to hopefully best position portfolios for the coming 12 months.

OVERVIEW

CENTRAL BANK DIVERGENCE

As the Federal Reserve (Fed) ends monetary easing and is set to raise rates sometime in mid to late-2015, the European Central Bank (ECB) and Bank of Japan (BoJ) are moving toward additional easing programs to help their stagnant economies. Short-term bonds should feel the impact of rate increases more than long-term bonds, as lower rates in Europe and Japan increase demand for long-term U.S. bonds with relatively more attractive yields. That, as well as several secular trends, will likely keep long-term U.S. bond yields low relative to history.

EXPECT A STRONGER DOLLAR

Divergent central bank policies support a stronger dollar, with a number of implications, including lower oil prices, which benefits oil-importing countries like China, India, and Japan. A stronger dollar is likely to hold down inflation and long-term interest rates as well. With the U.S. economy likely to outperform the economies of other developed countries, especially Europe and Japan, we're expecting the dollar to continue to advance higher. The dollar is up about 8% since last summer and the diverging trends in growth and monetary policy between the United States and other major countries should mean the dollar gets stronger.

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OVERVIEW CONTINUED

U.S. ECONOMY LEADS THE PACK

We believe the U.S. economy will show gross domestic product (GDP) growth in the area of 2.75% to 3.25% in 2015 and potentially higher if oil stays low. While the U.S. economy is not without its challenges (as an example, labor participation is still low), it's in a better position than other developed markets around the world. Perhaps the biggest challenge facing the U.S. economy is weaker growth overseas and the associated decrease in demand for U.S. products and services from multi-nationals. The rapid drop in oil prices will likely bolster global economic growth in the short term to medium term.

THE BOTTOM LINE

We continue to prefer stocks over bonds, even with volatility expected to rise. This secular bull market is likely in a more mature phase. We expect a moderate rate hike by midyear and increased volatility as a result. We intend to focus on opportunities in certain international markets and typically "safe" sectors like HealthCare, Utilities and Consumer Staples. We feel as though this will be a bounce back year for international equity market, with catalysts for further stock gains on the horizon around the world.

BE PREPARED FOR HIGHER VOLATILITY

Volatility, as measured by the VIX Index, is still below its historical average. This was the case for most of 2014 (with a few notable exceptions, such as this past fall). With the Fed ready to change directions, the economy struggling in Europe and geopolitical tensions in places like Ukraine, we expect higher volatility in 2015. Fed tightening cycles tend to usher in volatility and pullbacks but don't typically upend bull markets. One catalyst for volatility in 2015 could be interest-rate uncertainty as the Fed moves toward an initial rate increase. The onset of Fed tightening cycles has not upended bull markets historically—quite the contrary—but it does often usher in bouts of volatility and pullbacks. Actually, equities markets tend to perform well in the 12 months after the first Fed rate increase.

THE DETAILS

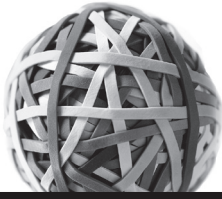
UNITED STATES

We remain positive on U.S. stocks. Within the United States, we favor sectors that tend to outperform in later stages of economic recoveries. We also have a bias toward large-caps and dividend paying securities rather than high multiple growth stocks and smaller capitalized equities.

Our view is that the current bull market is secular, not cyclical. Secular bull markets—like from 1949 to 1968 and 1982 to 2000—are extended bull markets characterized by above-average annualized returns and generally less-dramatic downside risk. Plus, lower energy prices put downward pressure on overall inflation, a plus for the U.S. economy and stock market.

This does not mean this market is immune to corrections, but it shares characteristics of past secular bull markets. For one, the Standard & Poor's 500-stock index has posted an annualized return of 22% in the first four years of this bull market. This closely mirrors the first four years of prior secular bull markets, which had similar annualized S&P 500 returns. Economic characteristics of past secular bull markets at their outset

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THE DETAILS CONTINUED

include secular valuation lows, secular unemployment rate highs and negative real interest rates. All three characteristics also were in place at the beginning of the current bull market.

An accelerating U.S. economy is a notable exception in a world where growth is expected to be below the long-term trend for most countries. The U.S. has just experienced 2 of the fastest growing quarters on record as measured by GDP. We anticipate growth in the area of 2.75% to 3.25% in 2015.

The good is outweighing the bad in the U.S. economy. Lower energy prices and reduced debt levels alongside higher equity and recovered home values compensate for low and slowly rising wages while the consumer continues to spend liberally on iPhones and lattes. Businesses are back to investing and we continue to believe in capex (Capital Expenditure) strategies, and although companies are cautious about hiring, some “in-demand” positions continue to go unfulfilled despite their best efforts.

Consumer spending represents 68% of the U.S. economy. Oil and gas capex represents about 1% of U.S. GDP and less than 9% of U.S. total capex (which in turn represents about 12% of U.S. GDP). Therefore, the benefit of lower energy prices to the consumer and many businesses greatly outweighs the significant hit to energy companies and/or energy-oriented capex, especially in energy-oriented states.

U.S. domestic capex has grown by more than \$600 billion over the past four years, with \$100 billion of that being energy-oriented. One can argue that much of non-energy capex would benefit from reduced operating costs courtesy of lower energy prices.

Lower energy prices also hold down overall inflation, which is a plus for both the U.S. economy and stock market. Lower inflation has historically meant higher equity valuations. In fact, there is a direct inverse correlation between the energy sector’s weighting in the S&P 500: a lower weight, typically as a result of lower energy prices, has led to higher overall S&P 500 P/E ratios, and vice versa.

Nonetheless, there are risks to the U.S. growth economy. Geopolitical tensions could intensify and rattle global demand, even with strong GDP numbers in the U.S. we feel a reversal could come quick and unexpected. Lastly, a quicker-than-expected Fed tightening could bring about unwanted market volatility, particularly when equity valuations are already expensive and portfolio managers are always looking to sell and lock in profits.

In summary, for U.S. equity exposure we favor large over mid and small caps but maintain nominal weights in mid and small in most portfolios. While not value players, we appreciate the value of dividends and would prefer dividend paying large caps over speculative high multiple companies that tend to be more volatile and have larger trading swings.

We continue to split our S&P 500 allocation into a traditional S&P 500 ETF and a Low Volatility S&P 500 ETF with additional exposure to Consumer Staples and Utilities. While these sectors all sport aggressive valuations and carry hidden duration risk, or interest rate sensitivity, we feel the good outweighs the bad and feel there is some potential safety in these areas if we see an unexpected slowdown in GDP. However, if bond yields increase even moderately in 2015, Staples and Utilities sectors could potentially underperform in the short-term.

SECTOR ALLOCATIONS

We continue to have additional exposure to the Materials, Industrials, Energy, and HealthCare sectors in our Tactical TimeBand. With the U.S. economy continuing to rebound from the 2008/2009 recession these sectors have proven over the last 50 years to perform better during middle to late parts of the economic recovery cycle. Experts can debate where we are in the cycle, but we feel confident that we are not in an early cycle recovery phase, nor deep late recovery. Therefore, Materials, Energy, Industrials, and HealthCare continue to remain a focus in most portfolios.



THE DETAILS CONTINUED

We have continued to allocate to our Energy sector weighting on dips and pullbacks and did that twice during the fall sell-off. At this point we would not allocate any additional funds to Energy and would look to lighten the weighting into rallies. With Oil at its current levels we feel that there could be substantial opportunities for patient investors that believe oil under \$60 is more of a short-term abnormality than long-term fundamental.

INTERNATIONAL DEVELOPED MARKETS

We maintain a slight underweighting to the Eurozone. The Eurozone economy continues to lag, showing little sign of catching up with the rest of the world.

Outright deflation is a real risk as all member countries have undershot the European Central Bank's 2% inflation target especially given the currently lower energy prices. The central bank has vowed to combat the threat of deflation by expanding its balance sheet by 50%, and market participants are hoping for broader monetary easing measures. Leaving aside numerous political barriers to a sovereign quantitative easing (QE), the jury is out on whether the QE measures will create enough of a wealth effect to restart the currency union's economy. While similar policy undertakings worked well in the United States, the Eurozone economy is structurally different, with low equity and home ownership rates atop the list.

Still, given depressed growth expectations, even a moderate cyclical rebound would be a positive surprise for European assets, therefore most WTWM portfolios have some nominal allocation to developed international markets. Meanwhile, recovering demand from overseas combined with a cheaper euro could boost earnings for Eurozone companies, particularly export-oriented large caps.

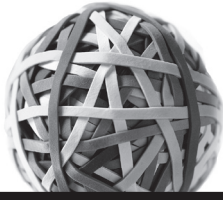
Japan and China remain two of our favorite picks, and we stay overweight in these two countries. Even after an autumn rally mostly derived from earnings gains, the valuation multiple for Japanese equities is still one of the lowest among developed markets. Despite structural challenges such as deteriorating demographics and a high debt burden, there are solid investment drivers supporting the market in the near term: the Bank of Japan (BoJ) massive monetary stimulus, further earnings upside thanks to a cheaper yen, and the possible delay of the second part of a major sales tax hike.

Also driving the uptrend is the Government Pension Investment Fund (GPIF), the world's largest government pension fund, doubling its domestic equity allocation, which could nudge other pension funds into equities. Meanwhile, Japan Inc. is displaying an increasing appetite for stock buybacks, dividends and spin-offs, which should help return on equity.

EMERGING MARKETS

We advocate for a benchmark weighting in Emerging Market (EM) equities along with a nominal allocation to Frontier Markets (FM). Our outlook for Asian economies, such as China and India, and certain Eurozone satellites is positive. In the past month, central banks in South Korea, Sweden, Vietnam, Iceland and Romania all have cut interest rates. While monetary policy garners a lot of attention, it is likely to remain broadly "dovish".

Valuations on emerging market stocks are relatively inexpensive when compared with stocks in the United States and other developed markets. Emerging market stocks — as measured by the MSCI Emerging Markets Index — are trading at a price-to-earnings (P/E) ratio of only about 10. In comparison, U.S. stocks — as measured by the Standard & Poor's 500-stock index — traded at a P/E of more than 15. Other developed market stocks as represented by the MSCI EAFE Index (excluding Japan) had a P/E of about 14. The relatively low valuation implies that investors have already priced in a pessimistic outlook for emerging market stocks, making them better positioned, in our opinion, than stocks of developed international markets.



THE DETAILS CONTINUED

Although nominal growth in many EM economies is likely to be stagnant in 2015, relatively attractive valuations, improving current account imbalances and dissipating inflation pressure (leaving room for local monetary policy accommodation) make for better economic conditions compared to a year ago.

Emerging market stocks may benefit from an improvement in global growth, especially if the Eurozone gets their act together. Global exports appear ready to accelerate from the recent quarterly pace of about 1%. Emerging market stocks historically have outperformed their developed country counterparts when global exports improve. Over the past 10 years, when global exports grew faster than 2.5% in a quarter, returns from emerging market stocks were almost double than those of international developed country stocks.

Commodity prices also contribute to Emerging Market hope. Falling oil prices will benefit oil-importing countries through lower cost of living, easing inflation, as well as reduced current account and fiscal deficits. On the other hand, oil exporters, such as Russia, Brazil, South Africa and Middle East countries, will likely struggle with rising budget deficits and downward pressure on currencies. In addition, prospects for economic reform will play a material role in determining performance and opportunities.

We are optimistic about Asia and look forward to seeing positive changes in China, India and Indonesia in the coming year.

FIXED INCOME

The focus of attention in the fixed income markets is likely to be on the Federal Reserve's move toward tighter monetary policy, which we think will have significant effects on the markets, but not perhaps in the way most people think. It's not just about interest rates –but more about volatility and valuation.

The Fed has already exited quantitative easing (QE) and assuming the economy continues to perform reasonably well, as we expect, then a rate hike seems likely mid-year. We are assuming that the rate of Fed tightening will be slower than the Fed has indicated and more in line with the trend implied by the bond futures market. While we believe the domestic economy will continue to improve, there are strong disinflationary pressures coming from Europe and Asia, which could hold down inflation and bond yields. Additionally, we expect the dollar to continue to rise as the Fed shifts policy.

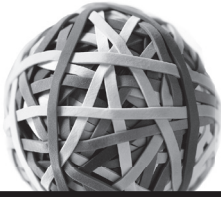
As the market hones in on the timing and trajectory of the Fed tightening cycle, volatility in the two- to five-year part of the curve will likely increase. Rates are likely to trend higher, with the 10-year Treasury yield grinding toward 2.75-3% range as we move deeper into 2015. However, we felt the same way last year and were dead wrong.

We remain exposed to higher yielding instruments, Preferred stocks, bank loans and REIT's as low default rates and firming U.S. economic growth continue to be supportive. While we still see high yield investments as relatively attractive compared to other more conservative fixed income instruments, we are increasingly selective regarding creditworthiness and duration and prefer the short end of the yield curve in an effort to lessen volatility although the short end carries interest rate risk.

We remain underweight with virtually no exposure to non-U.S. developed markets and Emerging Market debt.

Our yield curve expectation is that as the Fed raises rates, the major trend will be a flatter yield curve, particularly if inflation remains below the 2% target level. The yield curve has already flattened quite a bit from the 5-year to 30-year maturities. With rate hikes, the front end of the curve – from 3-month bills to 5-year notes – should flatten. The market has already priced in a lot of the increase in rates. A flatter yield curve would be consistent with the pattern of the 2004 cycle, which was signaled in advance and unlike the early response to the 1994 tightening cycle, which was not.

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THE DETAILS CONTINUED

It is not clear that QE has been solely responsible for the drop in interest rates we have seen in the last 6 months. We think falling inflation and inflation expectations have been a big contributor. In fact, the evidence suggests that during periods of QE, long-term rates have risen along with inflation expectations. When periods of QE have ended, rates and inflation expectations have generally trended lower. Therefore, the absence of QE doesn't necessarily mean rates will rise by much unless there is stronger growth and/or an increase in inflation expectations. So, our rate expectations would be for a moderate rise from current levels.

WHAT COULD GO WRONG IN 2015?

Although we hold a generally positive view of the outlook for 2015, the potential for shocks is always there. With assets ranging from fully valued to expensive, investors may be vulnerable to any potential setbacks. Here are some scenarios that we believe could cause bumps in the road:

Geopolitical tensions intensifying. While investors tend to worry more about all things economic, one exception should be the conflict between Russia and the West over Ukraine. Should it escalate, more sanctions and anxiety over the gas supply could disrupt markets in Europe. Less, we forget the sell-off that gripped the world over Ebola fears and in today's new world anything could happen at any time.

Europe is also vulnerable to pressure points from the inside. We trust the will of European policymakers to keep the Eurozone together, though euro pessimists argue that over the long term a breakup is inevitable without radically greater economic and financial integration. One near-term risk: a possible win by the far-left populist party in an early Greek election.

Higher and faster interest rate hike from the Fed. If stronger economic growth leads the Fed to raise rates sooner—or higher—than the market expects, a short and intense burst of volatility in both stocks and bonds is highly possible. An added challenge: Under this scenario, the correlation between stocks and bonds would likely rise, impacting the hedging value of bonds.

U.S. growth slower than anticipated. The U.S. economy is in a cyclical upswing, one of the few major economies expected to accelerate in 2015. But the economy has its share of vulnerabilities in the aftermath of the 2008 global financial crisis. Should slow income growth undermine consumption, there is a chance growth would disappoint. This has happened before and would most likely lead to higher volatility, especially with equities already on the pricey side.



DISCLOSURE

WT Wealth Management is a manager of Separately Managed Accounts (SMA). Past performance is no indication of future performance. With SMA's, performance can vary widely from investor to investor as each portfolio is individually constructed and allocation weightings are determined based on economic and market conditions the day the funds are invested. In a SMA you own individual ETFs and as managers we have the freedom and flexibility to tailor the portfolio to address your personal risk tolerance and investment objectives – thus making your account “separate” and distinct from all others we potentially managed.

An investment in the strategy is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.

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In addition to the normal risks associated with investing, narrowly focused investments, investments in smaller companies, sector ETF's and investments in single countries typically exhibit higher volatility. International, Emerging Market and Frontier Market ETFs investments may involve risk of capital loss from unfavorable fluctuations in currency values, from differences in generally accepted accounting principles or from economic or political instability that other nation's experience. Emerging markets involve heightened risks related to the same factors as well as increased volatility and lower trading volume. Bonds, bond funds and bond ETFs will decrease in value as interest rates rise. A portion of a municipal bond fund's income may be subject to federal or state income taxes or the alternative minimum tax. Capital gains (short and long-term), if any, are subject to capital gains tax.

Diversification and asset allocation may not protect against market risk or a loss in your investment.

At WT Wealth Management we strongly suggest having a personal financial plan in place before making any investment decisions including understanding your personal risk tolerance and having clearly outlined investment objectives.

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