PROFESSIONAL FINANCIAL MANAGEMENT, INC.
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Dear Client,

We hope this letter finds you well. Enclosed, please find your 1st Quarter performance report.

In this letter we will delve into a discussion about the concept of diversification, providing you an explanation of the concept and how it works in your portfolio to benefit your investment performance over time. First, however, is a First Quarter market summary.

1st quarter 2015 in Review

Global stock and bond markets continued to move in favorable directions over the three months ending March 31st. However, a few major asset classes saw a reversal of trend from their previous quarter and year end results. US Stocks, which led the way in 2014, lagged their International and Emerging Market counterparts, even when adjusted for the strong dollar.   Bond interest rates generally declined across all US fixed income markets during the quarter. Actual results across all markets are compared against those of last quarter to provide some perspective:

	US Stock Mkt.	International Dev. Mkts	Emerging Mkts	Global Real Est.	US Bond Mkt.	Global Bond–ex US
Q1 ‘15	+1.80%	+3.83%	+2.24%	+4.36%	+.1.61%	+2.25%
Q4 ‘14	+5.24%	-3.69%	-4.50%	+9.68%	+1.79%	+3.02%

Source: Russell, MSCI, Barclays and Citigroup

On the size and relative price spectrums, Value and Small Cap stocks underperformed Growth and Large Cap stocks across the board in 2014. However, we saw a partial reversal of that trend this past quarter. While the Value premium failed to materialize (Value underperformed Growth across all asset classes), the Small Cap premium came through as Small Cap stocks bested Large Cap stocks across U.S., International and Emerging Market asset classes.

Diversification explained and why it works

Diversification, a key element of Modern Portfolio Theory fathered by Harry Markowitz back in 1952, is a risk management technique that combines different investment assets and asset classes (not perfectly correlated or that do not move in lock step with each other) with the purpose of yielding higher long-term returns while reducing risk or overall portfolio volatility (simply put, not placing all your eggs on one basket). This means spreading risk across multiple asset classes (stocks, bonds, REIT’s), investment styles (value vs. growth), capitalizations (large vs. small) and equity markets (U.S., International Developed and Emerging Markets).   This core element of portfolio construction, along with emphasis to value and small cap stock exposure, is built into your investment strategy and provides you with a globally allocated and diversified approach.

Now, we should expect that in any given period, some asset classes will perform better than others. Being able to determine the winners ahead of time, however, has been proven impossible. Therefore, the broad exposure of your portfolio will allow you to reap the benefits of those asset classes that do well. While the “underperformers” appear to drag overall performance down, they are still playing a

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valuable role as risk reducing components. Even more important, however, is that just when you think you should ban them from your portfolio, they often turn around to become your best performers – this concept is a key factor to achieving the best possible long-term returns.

Though a very short-term example, the comparison of the past two quarters above explains a great deal about the benefits of diversification. At the end of 2014, when it appeared that owning International and Emerging Market stocks was a bust, they turned around and became the best performing asset classes in the first quarter. Abandoning these asset classes based on their standing at the end of the year would have had adverse effects on portfolio returns in the current quarter (not to mention increased portfolio risk).

An example of how this concept plays out over longer time periods can be found in what is called the "Periodic Table of Investing". This chart resembles a patch work quilt and depicts the annual returns of various asset classes, ranked from best to worst (if you are interested in seeing this, please contact the office and we will get one to you). The chart demonstrates that asset classes move randomly and in a totally unpredictable fashion, making it nearly impossible to outguess the markets. Therefore, as stated above, it is prudent to be continually invested across *all* of these asset classes as you are able to capture returns whenever they occur.

Admittedly, your portfolio may underperform for some periods and will experience losses. As well, being diversified does not mean your portfolio will be protected during market corrections or extended bear markets (such as the 2007 – 2008 downturn). However, the benefits of being diversified far outweigh any detriments. As a long-term investor, maximization of your returns (within your risk parameters) is your primary goal - maintaining a diversified approach will be necessary in helping you achieve this goal.

One last related point: When the investment media refers to "the market", they usually are quoting the S&P 500. The S&P 500 measures the performance of the 500 largest US stocks, which, as the owner of a globally diversified portfolio, represent only a portion of what you hold. Comparing your results to the S&P 500 is like comparing a basket of apples to a basket filled with multiple varieties of fruit…it makes no sense. Realizing that the performance of a globally diversified portfolio should not be measured against an index that represents a single asset class component is an important concept. While individual asset class components will outperform the portfolio in a given year (i.e. US Large Cap stocks as represented by the S&P 500 in 2014), they typically won't over long time periods. If still not convinced, then consider this: annualized returns of a globally diversified portfolio outpaced the S&P 500 from 1973 – 2014 by almost 3.5%....diversification does work.

We hope you have found this information useful. As always, thank-you for the opportunity to serve as your financial advisor.

Sincerely,

Doug Babcock, CFP®

Bob Frey, MS, CFP®