GREENLEAF TRUST

Perspectives

A Greenleaf Trust Newsletter

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William D. Johnston
Chairman, Greenleaf Trust

Economic Commentary

Oil has been in the news a great deal since our last newsletter and has caused more than a little disruption in the equity markets, so it makes sense to explore the cause for the significant price decline in oil, its impact upon the economy and adjacent impact on the equity markets.

Why are Oil Prices Plummeting?

The answers to this question are both political and economic in nature, and are centered around four constructs. Weak global economic demand has resulted in a surplus of supply. Absent of increased polarization in the Middle East, OPEC (The Organization of Petroleum Exporting Countries) had consistently controlled production to be balanced with anticipated demand. Clearly, the drop in prices from $115.00 per barrel in June of 2014 to its current $52.00 price reveals that something was amiss in either their projections of demand or their ability to gather consensus among members of OPEC to align production rates with demand.

The slowdown in global demand is not likely the primary cause in the precipitous drop in price. Is there a slowdown in Europe, Japan and China? Yes, absolutely — but that slowdown was well known in November when OPEC last met and was forecasted by many global economists for some time. The Eurozone and Japan have been teetering between very slow growth and recession for over six years. China's retreat from 8% GDP growth to its projected 7.1% forecast for 2015 has been baked into most global growth forecasts (ours included) for many months. So why did OPEC miss the mark so widely? That is of course the political, not necessarily economic, side of the issue.

For most of the last two decades, significant turmoil in Iraq, Libya and Syria was disruptive to the perception of global oil supply, and prices of crude were at times quite volatile. This was due to the combined impact of the four million barrels of oil produced daily by these three countries as well as the tightly controlled OPEC agreements of production. China's 10% GDP growth rate, and the failure of the United States to become energy independent, contributed as well. Today, OPEC is not aligned, China has

Commentary, continued

slowed and the US is nearly a net exporter of energy product. Why the lack of consensus in OPEC?

Recall our discussion of the nature of the ISIL emergence in the Middle East in our October newsletter. Sunnis represent about 85% of all Muslims, and Saudi is dominated by Sunnis. Shiite Muslims represent about 15% of the 1.6 billion Muslims in the world, but live in much of the oil producing areas including dominating the Muslim population of Iran. Saudi Arabia and Iran are not friends. The Saudis have other allies in the Gulf region, and have decided not to sacrifice their market share of oil production. This strategy is much easier to implement when they know they are punishing their enemies, Iran and Russia, and also know that their cost for each barrel of production is only a fraction ($5.00 per barrel) of the rest of the primary exporters of oil. With nearly a trillion dollars in reserve, modern efficient production facilities that have not been impaired by twenty year wars and healthy oil fields, the Saudis can well afford to play out this strategy. It is not without impact on other producers and exporters.

Russia, Syria and Libya need cash. Their governments have been destabilized and their economies have been hit with high inflation and economic sanctions, and the plummeting price for crude has hurt their cash flow significantly. Some worry that desperate people who are backed into corners and feel their power eroding will act even more irrationally. Oil exporting countries that will suffer the most if crude remains below $60 per barrel are Venezuela, Russia, Libya, Iran and Syria — none of which are democratically controlled, all of which have some measure of disagreement with the west, particularly the US, and all of which have in the past acted as poor global citizens.

Impact Upon the US Economy

At the pump prices on average at this writing are $2.37 per gallon, which means that US consumers will spend $600.00 per year less on gasoline allowing the equivalent of $90 billion to be spent elsewhere. Someone's gain is often someone else's pain. To assume that dollars not going into the gas tank are automatically going to be spent on consumer durables and non-durables and therefore benefit our economy is not the whole story. While more money available for consumer products could drive demand and therefore production and employment higher, some of that benefit could be offset by reductions in employment in the energy sector. Sixteen states have a healthy portion of their GDP related to oil exploration, production and administration. There have been more than 250,000 jobs added to the energy sector in the last three years. Most of that job growth is in the shale sector of the industry with a relatively minor portion coming from the alternative fuel sector. It is reasonable to assume

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that energy companies will respond to lower revenues with cost savings, and also balance their investment in future infrastructure and exploration projects with their ability to finance it. States benefitting from increased revenue such as the Dakotas, Wyoming, Pennsylvania, Oklahoma and Texas will need to revise their revenue projections and spend less on infrastructure and services. As we know, a major portion of the slow growth in employment over the past three years was the reduction in public sector jobs. For those states with heavy energy concentration, we could expect to see some reduction in workforce. Any job loss is painful, especially to those who lose the job; however, energy represents about 6% of our GDP and less than 4% of our employed population. The total impact of low oil prices translated into lower prices at the pump remains a net positive for the forward economic cycle.

Perhaps of more concern than the economic impact of lower crude prices is the potential to derail the progress our country has made in energy independence. While we still import petroleum, it is now a matter of economic choice rather than necessity. We are very near being a net exporter of energy which is a remarkable difference from our country's energy status twenty years ago. At least part of the economic equation that got us to this status was the production value of the product. The incentive to develop efficiencies in exploration and production was directly related to the profitability of oil field development in an environment of $100 per barrel prices. Shale can be less costly to explore than deep oil fields, but once found is far more labor and capital intensive to produce "clean" product with. There is more than a little speculation that OPEC's willingness to live below $60.00 per barrel is meant to defer and or decrease exploration if not outright production of the increasing flow through from the shale sector.

It would be nice to have evidence that Americans' consumption habits are centered in egalitarian desires and that the desire to be energy independent would drive our carbon footprint. Any automobile manufacturer and dealer will tell you that it just isn't so. Choices in the car buying public are indeed very elastic in relationship to fuel prices. Above $4.00 per gallon at the pump and the demand goes to hybrids and small, more fuel-efficient vehicles. Below $3.00 per gallon and the large SUVs and pickup trucks fly off the lots. Manufacturers have learned this lesson well and thus they have attacked the issue with a wide bandwidth of fuel type and efficiency; in fact, the largest gain in fuel efficiency has been targeted at the fastest growing and most profitable sector of the industry, full sized pickup trucks. The political will of the general population to subsidize alternative fuel development — such as hydrogen, wind and natural gas depots — has faded in recent years and therefore is more dependent upon

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Commentary, continued

the incentives of the marketplace to stimulate the creative exploration of possibilities. This is a reality that will defer, if not derail, some exciting possibilities that would enhance our independence and be kinder to the environment, but it is also a behavior that we have practiced in the past. Cheap oil is very likely to retard our desire to produce alternative fuels.

"Though we think oil prices will remain low (not this low) we are probably close to the area where investors will warm up to them again..."

Why is the Stock Market Reacting Negatively to Low Oil?

Energy stocks are generally high dividend stocks and in an environment of low interest rates investors often look for higher yielding stocks to replace bond investments. This is an example of chasing yield. Some investors do it by buying lower quality bonds while others accept some volatility in riskier assets. The strongest sector of the S&P 500 in 2014 was high yielding utilities. As global economic forecasts began to model up a weak Eurozone, slowing China and imploding Russia, energy stock investors began to examine fairly rich multiples in their higher yielding energy sector stocks. The November OPEC meeting affirming members' willingness to maintain production caused the repricing of oil stocks that has continued to date. Energy stocks represent about 11% of the S&P 500 index and thus the repricing of these stocks has weighed heavily on the rest of the S&P index. Consumer staples, industrials, consumer discretionary, health care, financials and technology all benefit from lower oil prices and make up over 80% of the S&P 500 index. Markets overreact to uncertainty and this price reduction in oil stocks is probably overdone and the capital fleeing the energy sector has little place to go other than equities. Though we think oil prices will remain low (not this low) we are probably close to the area where investors will warm up to them again and also model in the net positive impact on the remainder of the economy and S&P 500 sectors that benefit from lower oil prices.

How Long Will it Last?

Michael F. Odar, CFA
President

Welcome, 2015! I hope everyone had a joyous and meaningful holiday season. The last month of the year can be a whirlwind, so I hope you found some time to slow things down a little and reflect on the things important to you.

This Christmas I received a Colonel Littleton pocket knife from a friend with my initials on the case and the Greenleaf logo etched on the blade. Since I had never heard of the manufacturer, I sat down and read the brief marketing narrative that was written from the founder's perspective. It cleverly drew comparisons between the lasting power of the knife with that of a well-made leather saddle (will last longer than your horse and your ability to get on it) and a true friendship. What resonated with me the most was the founder's remarks on his desire to start a business that would "make things that would last and become more meaningful as time goes by… things that would be around long enough to be handed down to your children and grandchildren and be cherished as family heirlooms."

In my reflective mindset, the founder's narrative made me immediately think of Greenleaf Trust. We use the phrase "from generation to generation" to describe our services. That phrase has always meant something to me as well as everyone that works here. And, its meaning goes beyond our financial strength or how we are privately held and protected from any kind of future big bank acquisition. It means, just like Colonel Littleton, we plan on serving our clients, our clients' children, and our clients' grandchildren.

In order to do that, we spend the necessary time to select the right people. People who thrive working as part of a team and who are problem solvers, achievers, and relationship driven. We then develop those people in a culture that multiplies them and aligns their efforts with what our clients need first; not what the company needs first. This helps ensure that team continuity is the norm in an industry where that may not always be the case.

> "We use the phrase 'from generation to generation' to describe our services."

Generational wealth management also requires continuous improvement. Adaptation to changes in generational needs, technology, and family dynamics is critical. Just as important is the ability of those people we select and develop to continuously "up their game" because it's not good enough to simply meet our clients' expectations; our goal is always to exceed them.

In simple terms, we want future generations to feel the comfort of a team that has worked on behalf of their family for a long time with the knowledge that the same team has the sophistication and longevity to help them with their unique needs and desires.

Finally, I would be remiss if I did not mention the Michigan State Spartan's dramatic come from behind win in the Cotton Bowl on New Year's Day. I'm impressed not just because I am a Spartan, but because that was a true TEAM effort. Go Green!

Karen A. Bouche, CTFA
Executive Vice President
Family Office Advisor

For Purpose

I have worked with wealthy families for many years, long enough to shape my perception of the wealthy as an incredibly generous and caring group of people. Year after year, many continue to share their wealth with organizations that work to make a difference in the lives of others. Whether it is an outright gift of cash or securities, or a grant made by their Family Foundation, we help families facilitate and fulfill their charitable giving to the causes that are near and dear to their hearts. Increasingly, however, there is interest in doing more by way of volunteering, raising awareness, and having more direct involvement with the charities. There is a strong desire to not only give wealth, but to become involved — to give time, passion and energy to benefit the cause as well.

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At a recent conference, I listened to a presenter who refused to refer to charitable organizations as "non-profits" and instead inserted the term "for-purpose" organizations throughout his presentation. The rationalization was that profits are, in fact, made by these organizations, but that they are then put to work toward a meaningful and charitable purpose. Further, the presenter recognized that, in the charitable world, this distinction is important as perceptions are changing and the organizations most effective at fundraising are those that are able to demonstrate impact and purpose. While that is not surprising, the trend of measuring and reporting on impact is increasing as the non-profit sector continues to grow. According to the Urban Institute, between 2001 and 2011 the number of non-profits has increased 25%, a growth rate that has surpassed both the business and government sector growth rates. Simultaneously, there is a significant shift in control from the baby boomer generation to their children when it comes to deciding where the family wealth is given, and this generation is extremely focused on purpose.

Another presenter, at the same conference, educated the audience on the characteristics of this upcoming 20-something-year-old generation, often referred to as "Gen-Y" or "Millennials." The US Census Bureau, 2010, defines this generation as those born between 1982 and 2000. This translates to a population of approximately 79 million, or 25% of the US population. Specifically, we were informed that the millennials will not be involved in anything, including a career, unless they feel good about the purpose that it serves in the world. Events that have shaped their lives include the Oklahoma City Bombing, 9/11, Columbine and Virginia Tech. They value constant communication, relationships with their co-workers, and aim not for a work/life balance, but a blended life. They are technology natives, the first generation where all they have ever known is instant information, real time updates and live feeds.

They are influenced by the decisions and behaviors of their peers. They treat all of their assets (time, money, network, etc.) as having equal value. They engage with causes to help other people and support issues rather than organizations.

What this means for the well run "for-purpose" organizations is that they have an opportunity to engage with a new donor base in new and unique ways. Social media, and specifically crowd-funding, has grown from raising awareness and funding of an estimated $89 million in 2010 to $5.1 billion in 2013. Popularity in alternative investment ideas such as Impact Investing, where private foundations make investments in local organizations as opposed to publicly traded companies, is growing. It is also likely that more donors will be on-site and involved prior to fully committing to a cause. The landscape of the philanthropic world is changing because of this powerful combination of the Millennial generation becoming more involved with family philanthropy, together with their general nature to be skeptical and strong desire to ensure that the organizations are doing impactful work.

"What this means for the well run 'for-purpose' organizations is that they have an opportunity to engage with a new donor base in new and unique ways."

If you'd like to join us in our efforts to conserve natural resources and create a greener environment, you may choose to save paper by receiving email notifications to view your statement online. Simply give us a call at 269.388.9800 and ask to speak with a member of your client centric team.

Chris A. Middleton, CTFA
Executive Vice President
Director of Retirement Plan Division

The Case for Retirement Plans & IRAs

"Although many individuals rely exclusively on Social Security for retirement income, the system was never intended to be an entire retirement solution."

Approximately 40% of the current retiree population depends on Social Security for more than 90% of their income! Although many individuals rely exclusively on Social Security for retirement income, the system was never intended to be an entire retirement solution. Moreover, our current Social Security system is actuarially unsustainable over the long term. The Congressional Budget Office has recently reported that, under current law, the largest Social Security fund (the Old-Age and Survivors Insurance trust) will be exhausted by 2033. How to solve this issue is a political football often kicked around but rarely progressing toward a solution.

We desperately need to amend Social Security legislation and enhance financial stability for retirees, but true progress through our governmental ranks is unreliable. Some would even claim that when legislators realize they cannot get any real solutions passed into law, they feel validated to pass ancillary ones so as to appear to be doing something. Don't misunderstand, many of the recent regulatory reform efforts have good intentions, they just focus on tertiary issues. For instance, a recent push in the retirement plan industry has been for fee disclosures and other edicts of transparency for participants — a noble cause. Unfortunately, it is rare to find a participant willing to read through even the most succinct fee disclosures being provided. As a result, there is a lot of regulatory action triggering added administrative requirements yet minimal impact toward the most important issues.

Beyond the fact that the current Social Security system is on a mathematical crash course, it is quite clear that no governmental program can successfully provide full retirement benefits for the entire American retirement community into perpetuity. This is the ultimate case for the existence of qualified retirement plans (e.g. 401(k)s, profit sharing plans, pension plans etc.) and IRA's. These tax-qualified accounts are the great hope of a private industry solution to a complex problem that our politicians will not, and arguably cannot, solve. Fortunately, these vehicles are already a massive success by almost any measure. Consider that since the original 401(k) legislation in the late 1970s, there are now hundreds of thousands of them representing more than $21 trillion in assets. IRAs alone hold well over $5 trillion, most of it from retirement plan rollovers. We went from zero to trillions in just 30 years!

A growing number of people have been asking if governmental action is likely to violate the existing tax qualification benefits of retirement plans and IRAs. Since these accounts have become such a critical mechanism for retirement income, our politicians would first have to come together with a better public solution. Because of the reasons mentioned above, it is highly doubtful either political party has the ability to offer a better solution than that which private industry can provide through qualified account arrangements. As a result, it would be unconscionable for governmental action that would take aim at weakening these vital tax qualified accounts.

The single most important step toward accomplishing even better retirement security for American retirees is more coverage and higher participation in qualified saving vehicles. The main focus should not be about new Form 5500's, new definitions of "fiduciary," or even transparency. Enhancing the coverage and participation is the elephant in the room — transparency, by comparison, is a mouse. Improving the number of participants and the amounts being saved can help take the long-term strain off public resources, so we need retirement plans to be more widespread. The number of US workers currently covered by a retirement plan is around 50%. As a society, we need to shoot for 80% or more. The math is simple, more coverage and participation leads to more long-term savings, which is the primary solution to the global pension crises. To be fair, there have been efforts to improve coverage by our politicians. The Bush administration proposed several changes (all were rejected), and now the Obama administration is proposing the myRA program, which has been well documented through the later part of 2014. Hopefully some of these efforts will begin to gain traction.

In order for qualified accounts to have the systemic impact desired, we must increase the number of people covered by retirement plans and the amounts individuals are contributing to the accounts. It is a dual responsibility. Public legislation and private industry need to produce structure for individuals to be covered. Individuals need to accept the fact that Social Security can help in retirement but it was not originally intended to be a full retirement solution. Everybody should be personally motivated to save sufficiently to pay for retirement and retiree healthcare. Accumulating assets in the private pension system is the difference between subsistence and dignity in the retirement years. With a commitment from all parties involved, retirement plans and IRA's can prove to be the bridge for the well documented gap between Social Security benefits and the real desires of a retired life.

Greenleaf Trust is devoted to this noble cause through our retirement plan services division. The task is large but the direction is clear and we are up to the challenge.

"Individuals need to accept the fact that Social Security can help in retirement but it was not originally intended to be a full retirement solution.... Accumulating assets in the private pension system is the difference between subsistence and dignity in the retirement years."

Dan J. Rinzema, CFA, CFP®
Chief Client Officer

Survey Says...

Continuous improvement is one of Greenleaf Trust's core values — it is a pillar of our culture and has become part of our DNA. Every tangible improvement we have made on behalf of our clients stems from a disciplined review of our practices. As we look for opportunities to serve our clients better, we begin by listening to those who matter most — our clients.

Client satisfaction surveys, which we have historically conducted every other year, allow us to focus our efforts. The aim is to listen to client comments and suggestions so that we can improve the services provided on their behalf. Simply put: when our clients speak, we listen.

"Client satisfaction surveys, which we have historically conducted every other year, allow us to focus our efforts."

For example, the 2013 client satisfaction survey revealed that the format of our investment performance reporting could be improved to better meet the individual needs of our clients, as only 84% of respondents found the benchmark meaningful. Given this feedback, we made it our goal to provide more customized, relevant and meaningful performance reporting. We heard what our clients wanted and responded with updated performance reports tailored to their specific needs. As a result, satisfaction with our quarterly investment performance report format jumped to 97%.

It is in this spirit of continuous improvement that we redesigned the 2014 client satisfaction survey to better gauge our collective efforts from the clients' perspective. The survey itself was distilled down to 10 essential questions with space for free-form client comments, and we decided to increase the survey frequency from every other year to annually. The changes were designed to improve survey participation, more closely align the voice of our client with our daily impact, and better understand how our clients feel about Greenleaf Trust's personalized service and customized solutions.

The aforementioned design changes appear to have worked, as participation was up 60% this year! We asked for candid responses, which are always desired and appreciated. The following is a summary of what we heard our clients say:

2014 Client Satisfaction Survey Results: Personal Trust & Wealth Management

- 99.6% find our team members to be easily accessible
- 99% feel their questions and concerns are answered in a prompt and satisfactory manner

- 96% are satisfied with the frequency of contact
- 96% feel as though they are treated as a very important client
- 97% believe we listen to and understand their goals and objectives
- 97.5% believe their accounts are tailored to meet their financial goals and objectives
- 97% believe we're successful in meeting their investment needs
- 96% say they would refer an individual to us

Satisfaction scores with our account statements, performance reports and newsletters uniformly exceeded 94%.

While I am pleased with the generally high marks received, we recognize there is always room for improvement. So in order to enhance the value of our relationship with our clients, and to achieve our standing goal of 100% client satisfaction on all fronts, we will intently focus on the specific suggestions and comments received. This includes individual client requests ranging from updates to our website, to more resources for talking to the next generation about the stewardship of wealth, to consolidation of monthly statement packaging.

In fact, I am pleased to report that our team is already diligently putting the final touches on a consolidated statement option as requested. This quick turn response will reduce the number of envelopes many of our clients with multiple accounts receive each month. The team expects to put this continuous improvement idea voiced by our clients into production for the January statement mailing cycle, which goes out the first week of February.

Thank you to all of our clients who took the time to respond to our recent client satisfaction survey. The overall response rate was gratifyingly high and the comments overwhelmingly positive. My colleagues and I are always receptive to your suggestions, and we hope you will never hesitate to share your candid opinions with us. Providing personalized service and customized solutions to you, as an integral part of our continuous improvement process, is a core value of the Greenleaf Trust team. Thank you for allowing us the continued privilege of serving on your behalf.

"Thank you to all of our clients who took the time to respond to our recent client satisfaction survey. The overall response rate was gratifyingly high and the comments overwhelmingly positive."

Dave P. Mange, CFA
Vice President
Senior Research Analyst

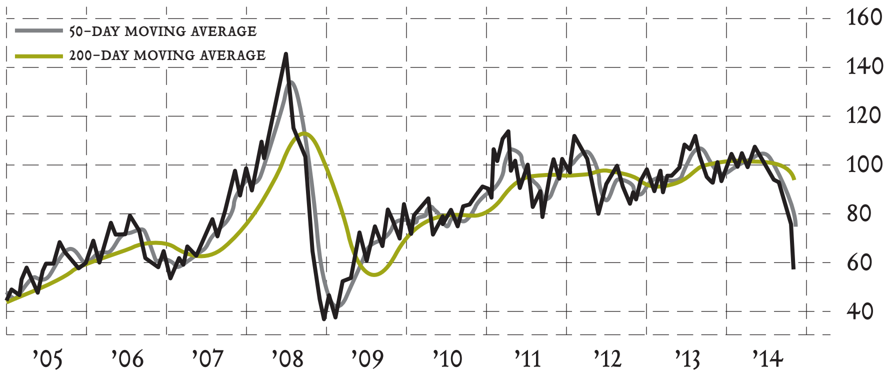
This Time, It *Is* Different — a Look at the 2014 Oil Price Crash

On December 20, 2014 retail gasoline prices hit $1.99 in Kalamazoo. While retail gasoline prices are strongly but imperfectly correlated with global oil prices, the price at the pump is the most visceral connection most of us have to the energy markets of the world. After a period of relative stability since 2010, the recent rapid price decline has stimulated our imaginations as to what is possible.

Looking at the chart below, many of us will be able to recall the much more pronounced volatility of the crash of 2008–2009 oil prices. That amazing trip, from a high water mark of $143/barrel down to $34, was caused by a relatively small demand slump due to the severe global recession either caused by or juxtaposed with the financial crisis of that same period.

> "While retail gasoline prices are strongly but imperfectly correlated with global oil prices, the price at the pump is the most visceral connection most of us have to the energy markets of the world."

Crude Oil WTI (NYM $/bbl)
57.25
2004/12/13 – 2014/12/19



SOURCE: FACTSET

To clarify some potentially confusing terminology: although there are several grades of crude oil in the world, the two most frequently quoted prices are Brent, which is a variety of oil produced from North Sea platforms, and West Texas Intermediate or "WTI." Brent crude is normally slightly more valuable than is WTI. The chart above references West Texas crude, which is commonly referenced in US media stories.

Before offering some thoughts on how long the current sub-$60/barrel oil prices might last, I would like to journey into the past to find the roots of oil price volatility in the modern era.

On October 17, 1973 OPEC announced an oil export reduction to countries that had supported Israel during the October 1973 Yom Kippur war. By December this became a full embargo against the United States. The price of oil rose from approximately $3/barrel to $12/barrel in a matter of months, and the impact was long lasting — including the "second oil shock" of 1979. Many of us can recall gas stations closing and gasoline being unavailable at times in 1973–1974 and the later imposition of the national 55 mile per hour speed limit. That 1973 embargo broke a period of stability stretching back more than twenty years.

Now that our memories and/or imaginations have been stirred, the present volatility seems unusual but not as extreme. The current oil price collapse is driven by over-supply. Today, OPEC is a much smaller factor in setting prices, since it now comprises only about 30% of total global production. The change in the past four years has been the explosion in North American supply due to the ability to unlock oil in shale formations through hydraulic fracturing or "fracking." Oil production in the United States has risen by a total of four million barrels per day over the past four years. This accounts for almost all the entire global supply increase over that same period.

In the first paragraph I noted that the dramatic oil price collapse of 2008-2009 was caused by a relatively mild decrease in global demand. To be precise, global demand dropped from 87.1 million barrels per day to a low of 85.6 million barrels per day, or less than 2%. As we reach the end of 2014, the world has too much supply due to a combination of US supply increases and to a much lesser extent, a slow-down in the growth rate of global demand. Total demand/consumption has risen every year since 2009.

Global oil demand in 2014 is approximately 92.4 million barrels per day according to the US Department of Energy/Energy Information Administration. This is a modest 600,000 barrel per day increase over 2013. There is probably a two million barrel per day over-supply available to the market today. Until the November OPEC meeting, that imbalance was expected to reach equilibrium through a combination of continued growth in global demand and an OPEC production cut of approximately one million barrels per day. OPEC emerged from the meeting with production slated to run at full

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This Time, It Is *Different, continued*

"Typically, the world does not have a large inventory of stored oil. Even with excess production today the US holds less than twenty-five days of inventory, and global inventory is less than thirty-five days. It may not take much to bring the global over-supply back to equilibrium..."

speed regardless of falling prices.

Typically, the world does not have a large inventory of stored oil. Even with excess production today the US holds less than twenty-five days of inventory, and global inventory is less than thirty-five days. It may not take much to bring the global over-supply back to equilibrium, and the longer oil prices stay under $70/barrel the faster some incrementally expensive production will come off the market. Globally, there is already a very significant reduction in deep sea drilling activity since the cost of production is generally highest in deep water.

OPEC is not at all politically unified. Due to its status as both the production leader and arguably the most politically stable member, Saudi Arabia is the de facto leader of OPEC. Some have speculated that the Saudis want to inhibit US shale oil production to retain their shrinking export market to the US. It seems more likely that discouraging US production growth is merely the Saudis third most important objective. Saudi Arabia may be more interested in asserting power over Russia and Iran, which will suffer far more than US shale producers if oil prices remain low.

Most of the world's private sector major producing companies have already announced plans to restrict exploration and production capital spending next year. Some of the world's state-owned oil companies and quasi-state-owned companies simply cannot earn sufficient profit with oil prices below $70/barrel, and their production will decrease. Even with reduced capital spending, US crude oil production is likely to rise in 2015. There is quite a difference between not drilling any new wells, drilling fewer new wells and at the most extreme, capping or shutting down wells already in production.

Realized oil prices for producing companies will fall sharply year over year in 2015. It may be that investors will "look through" the lower revenue and earnings in anticipation of a return to higher oil prices once supply and demand rebalance, possibly not until 2017. Even so, the watchword for producing companies is preserving balance sheet quality by reducing capital spending to make sure that there is adequate cash flow to avoid the need to borrow via either increasing bank debt or tapping the bond market. Most producing companies will budget their capital spending based on an assumption that oil prices will not reach more than $80/barrel for several years.

While investors in the energy sector may lament the recent turn to lower oil prices, there should be positive implications for energy-intensive manufacturing, transportation and consumer discretionary sectors. It seems likely that the implications of lower oil prices will be net positive for the global economy in 2015. For countries that fund their government budgets through state-owned oil production, the lower prices may create significant social disruption. For the rest of the world, lower oil prices will convey the advantage of a de facto tax cut.

Within the energy sector, Greenleaf is seeking to gain relative advantage to the Standard & Poor's index by slightly overweighting our participation to the sector to play an oil price rebound over the next two years. The global oil market is likely to feature abundant supply over the next decade, at prices that allow the majority of non-OPEC suppliers to profit. The current spot price in the mid-fifties will cause a rapid response by more marginal producers that will bring the relatively small over-supply back into balance over the next two years. Energy producers and service companies that wisely balance operating cash flow and capital expense, and those who maintain strong balance sheets will ride out the storm and come back stronger. We expect that production will show signs of slowing by the third quarter of 2015. Oil prices can certainly hit new lows until then.

"The global oil market is likely to feature abundant supply over the next decade, at prices that allow the majority of non-OPEC suppliers to profit."

Stock Market Pulse

Index	12/31/2014	Total Return Since 12/31/2013
S&P 1500	475.80	13.08%
DJIA	17,823.07	10.03%
NASDAQ	4,736.06	13.40%
S&P 500	2,058.90	13.69%
S&P 400	1,452.44	9.77%
S&P 600	695.08	5.76%
NYSE Composite	10,839.24	4.22%
Dow Jones Utilities	618.08	30.67%
Barclays Aggregate Bond	110.12	6.00%

P/E Multiples	12/31/2014
S&P 1500	17.3x
DJIA	14.7x
NASDAQ	22.4x
S&P 500	17.1x
S&P 400	19.6x
S&P 600	21.2x

Key Rates

Fed Funds Rate	0% to 0.25%
T Bill 90 Days	0.02%
T Bond 30 Yr	2.75%
Prime Rate	3.25%

Current Valuations

Index	Aggregate	P/E	Div. Yield
S&P 1500	475.80	17.3x	1.93%
S&P 500	2,058.90	17.1x	2.00%
DJIA	17,823.07	14.7x	2.11%
Dow Jones Utilities	618.08	NA	3.22%

Spread Between 30 Year Government Yields and Market Dividend Yields: 0.82%

MAIN OFFICE:
211 South Rose Street
Kalamazoo, MI 49007
office: 269.388.9800
toll free: 800.416.4555

TRAVERSE CITY OFFICE:
130 South Union Street
Traverse City, MI 49684
office: 231.922.1428

BIRMINGHAM OFFICE:
34977 Woodward Ave., Suite 200
Birmingham, MI 48009
office: 248.530.6202

PETOSKEY OFFICE:
406 Bay Street
Petoskey, MI 49770
office: 231.439.5016

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e-mail: trust@greenleaftrust.com
www.greenleaftrust.com