

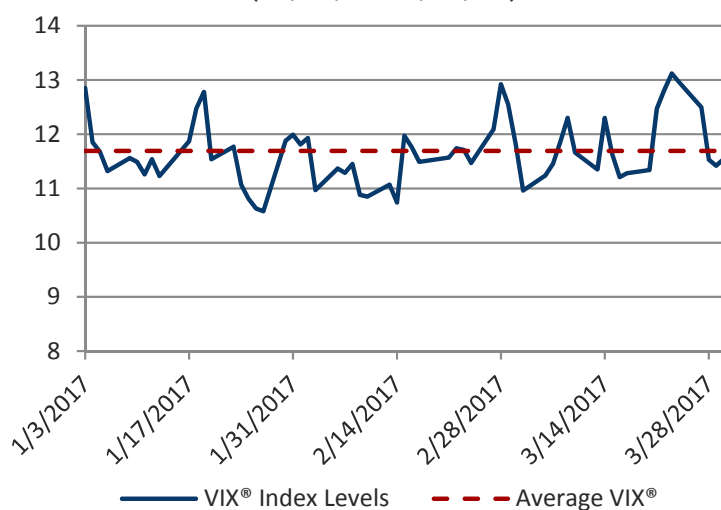
## EQUITY MARKETS

The S&P 500® Index gained 6.07% for the first quarter of 2017. The equity market posted positive returns each month of the quarter with the S&P 500® Index returning 1.90%, 3.97% and 0.12% for January, February and March, respectively. The equity market's advance was steady over the first two months and reached a year-to-date closing high on March 1<sup>st</sup>. The S&P 500® Index declined 2.16% from March 1<sup>st</sup> through March 27<sup>th</sup> before advancing to month-end. Realized volatility and implied volatility were persistently low throughout the quarter.

The equity market's advance in January and February was fueled by strong corporate earnings, positive economic data and optimism that the Trump administration would quickly enact its agenda of reducing regulations and reforming the tax code. The January release of the Purchasing Managers Manufacturing Index was the strongest since March 2015 and the January employment and retail sales reports exceeded expectations. Measures of business and consumer confidence reached multi-year highs. Though the Federal Reserve raised the Fed Funds rate by 25 basis points (bps) as expected in March, rhetoric about future rate increases was relatively dovish – as noted during Chairman Yellen's press conference after the rate hike and during her semi-annual testimony to Congress in February. Nearly 78% of S&P 500® Index companies reported fourth quarter earnings that met or exceeded analyst estimates and aggregate operating earnings grew 4.77%, the fastest rate since the fourth quarter of 2013. Market weakness in March was driven in part by the failure of Congress to pass a healthcare bill that repealed or modified the Affordable Care Act, calling into question the ability of the Trump Administration to enact other portions of its policy agenda. At the end of March, the final estimate of fourth quarter GDP growth came in at 2.1%, an upward revision that beat consensus estimates.

Implied volatility, as measured by the Chicago Board Options Exchange Volatility Index® (the VIX®), averaged 11.69 for the quarter, exceeding S&P 500® Index realized volatility (as measured by its annualized standard deviation of daily returns) of 6.84%. The VIX® oscillated in a narrow range throughout the quarter with a low of 10.58 and a high of 13.12.

**VIX® Levels**  
(12/31/16 - 3/31/17)



Datasource: Bloomberg, L.P.

Performance data shown represents past performance and is no guarantee of, and not necessarily indicative of, future results.

## FIXED INCOME MARKET

The Bloomberg Barclays U.S. Aggregate Bond Index returned 0.82% for the first quarter. The yield on the 10-year U.S. Treasury Note ended 2016 at 2.44% and ended the first quarter at 2.39%. The bellwether interest rate reached a low of 2.31% on February 24th before climbing to a high of 2.63% on March 13th, its highest level since mid-2014.

## COMPOSITE PERFORMANCE

The Gateway Index/RA Composite (net of fees) (the Composite) returned 2.86% for the first quarter, underperforming the S&P 500® Index by 321 bps. With monthly net returns of 1.04%, 1.37% and 0.43% for January, February and March, respectively, most of the Composite's underperformance relative to the S&P 500® Index came in February when the Index had a sharp advance of 3.97%.

The returns, portfolio performance contributions, annualized standard deviation and portfolio statistics quoted for the Composite in the following paragraphs are those measured by a representative account.\*

\*Represents supplemental information to the GIPS-compliant presentation. This representative account was selected as it is the largest account in the Composite.

The Composite delivered 181 bps of downside protection when the market declined from March 1<sup>st</sup> through March 27<sup>th</sup>, resulting in outperformance during the final month of the quarter. Both the relative and absolute performance of the Composite throughout the quarter were consistent with expectations in a period of equity market advance with low volatility.

For the first quarter, the Composite's underlying equity portfolio contributed a total return of 6.18%, resulting in a positive performance differential of 11 bps relative to the S&P 500<sup>®</sup> Index. Although the Composite's index call option portfolio generated risk-reducing cash flow throughout the quarter, it detracted from returns in January and February primarily due to call premiums earned in January and February being insufficient to keep pace with the equity market's rapid mid-quarter advance. Index call options added to the Composite's return in March.

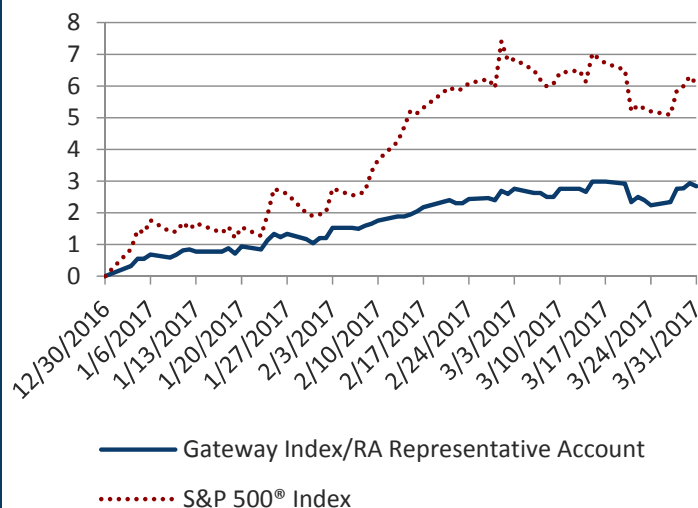
Index put options detracted modestly from the Composite's return in each month of the quarter. The Composite's annualized standard deviation of daily returns for the quarter was 2.58% as compared to 6.84% for the S&P 500<sup>®</sup> Index. The Composite exhibited a beta to the S&P 500<sup>®</sup> Index of 0.32 for the quarter.

Gateway's index call option activity during the quarter focused on increasing the weighted-average strike price of the Composite portfolios as the market advanced while keeping weighted-average time to expiration relatively extended. Certain longer-dated contracts offered more attractive protection in the event of a market reversal than shorter-term contracts due to their higher dollar premiums and lower market sensitivity.

Gateway's investment team took advantage of low volatility throughout the quarter by trading select index put options well in advance of their expiration dates and keeping weighted-average time to expiration extended in an effort to maintain downside protection at attractive prices.

As of March 31<sup>st</sup>, the Composite's accounts' diversified equity portfolios were over 95% hedged with index call options with average strike prices between 1.5% in-the-money and 1.5% out-of-the-money, average time to expiration of 29 days and annualized premium to earn of 5% to 7.5%. Portfolios within the Composite ended the quarter hedged with index put options on over 95% of the notional value of its portfolio with average strike prices between 7.5% and 10% out-of-the-money, average time to expiration of 57 days and annualized cost of less than 2.5%. Relative to the beginning of the quarter, this positioning represented increased market exposure and lower net cashflow potential.

Cumulative Performance (%)  
(12/31/16 - 3/31/17)



Datasource: Bloomberg, L.P.

Performance data shown represents past performance and is no guarantee of, and not necessarily indicative of, future results.

## MARKET PERSPECTIVE

Despite high equity market valuations, cautious long-term investors should consider the possibility that equity investments may still outperform fixed income investments over their investment horizons. Although elevated equity valuations have persisted in the market landscape over the last 20 years, the current combination of very low bond yields and very high equity market valuations is historically rare. The last time interest rates were similarly low and equity market valuations were similarly high was the early 1960s. On January 1<sup>st</sup>, 1961, the yield on the 10-year U.S. Treasury Note stood at 3.84% while the trailing 12-month price-to-earnings ratio (P/E) on the S&P 500<sup>®</sup> Index was 18.60 and climbed to a high of 22.64 by November of that year. Those figures compare to a yield of 2.35% and P/E of 26.48 at the end of the first quarter of 2017.

Investors looking for lessons from the early 1960s will find a mix of good and bad news. Economic growth was above average. Corporate earnings were above average and outpaced the market's return, which was below average. The S&P 500® Index had a cumulative total return of 38.24% (5.54% annualized) from December 31<sup>st</sup>, 1960 to December 31<sup>st</sup> 1966 while the cumulative growth of S&P 500® Index earnings was 53.72% (7.43% annualized). The high market valuation at the beginning of the period was a signal that significant earnings growth was already priced into the market. But the below average market return wasn't the only evidence that earnings growth did not meet expectations—there were also two bear markets in the six-year span.<sup>1</sup> Remarkably, despite below average returns and two bear markets, investors who remained in the equity market from 1961 through 1966 fared better than intermediate government bond investors who earned an annualized return of just 3.12% as the yield on the 10-year U.S. Treasury Note climbed from 3.84% in January 1961 to a high of 5.16% in November 1966.

**Equity Valuation, 10-Year U.S. Treasury Note Yield and Bear Markets**  
1/1/1946 – 4/1/2017



Datasource: Multpl.com for P/E and yield, Bloomberg, L.P. for bear market periods

Performance data shown represents past performance and is no guarantee of, and not necessarily indicative of, future results.

Historically, bear markets materialized in 1946, 1961 and 1987<sup>2</sup> – soon after the trailing 12-month P/E ratio on the S&P 500® Index climbed above 20. At other times, however, high equity valuations were normalized through earnings growth rather than deep market declines. The early 1990s was one such time, when earnings growth was sufficient to catch up to the market price and significant downside volatility was avoided.

Specifically, from December 31<sup>st</sup>, 1991 through December 31<sup>st</sup> 1994, S&P 500® Index earnings grew more than 20% annualized. The trailing 12-month P/E began the period at 15.35, climbed above 20 by mid-1991 and stayed above that threshold until the first quarter of 1994. Due in part to the market's high starting valuation, however, the annualized total return of the S&P 500® Index was only 6.25% over that three-year period. Despite this below average return, robust earnings growth appeared to have contributed to keeping significant downside volatility out of the market. The worst peak-to-trough decline in the S&P 500® Index over this period was a drawdown of 8.47% from February 2<sup>nd</sup> to April 4<sup>th</sup>, 1994.

Interestingly, earnings growth forecasts for 2017 are similar to the earnings growth rate of the early 1990s. Consensus bottom-up estimates as of March 23<sup>rd</sup> for S&P 500® Index operating profits are currently about \$130, an increase of more than 20% over S&P 500® Index operating earnings as of December 31<sup>st</sup>, 2016. Earnings growth and market action of the early 1990s suggest S&P 500® Index companies may need to sustain that level of earnings growth for more than one year if equity investors are to avoid a significant downside event. Optimistic equity investors may want to temper their outlook with the possibility that robust earnings growth going forward may only serve to keep downside volatility out of the market, rather than drive average to above-average equity market returns.

It is also worth noting that, despite higher yields on investment grade bonds relative to today and the 1960s, the stock market still performed better than the bond market from 1991 through 1994. The Bloomberg Barclays U.S. Aggregate Bond Index returned just 4.60% annualized over the three-year period, underperforming stocks by more than 1.5% per year on average. This happened despite the 10-year U.S. Treasury Note yielding over 8% at the beginning of 1991 and total-return boosting rate declines over the next two years. Rising rates during 1994 drove losses in the bond market that erased a portion of the gains generated in the first two years of the period.

<sup>1</sup> From December 12<sup>th</sup>, 1961 to June 26<sup>th</sup>, 1962 the S&P 500® Index lost 27.97% and from February 9<sup>th</sup> to October 7<sup>th</sup>, 1966 the S&P 500® Index lost 22.18%.

<sup>2</sup> S&P 500® Index bear market returns and dates: May 29<sup>th</sup>, 1946 to June 13<sup>th</sup>, 1949: -29.61%, August 25<sup>th</sup>, 1987 to December 4<sup>th</sup>, 1987: -33.51%, See Note 1 for bear market returns in 1961 and 1966.

Analyzing equity and bond market returns in these high valuation periods illustrate that while high market valuations don't always presage bear markets, neither does above average earnings growth always result in above average equity market returns. This is especially true when high valuations are an indicator of priced-in future earnings growth. Moreover, bear markets can occur even during a period of expanding earnings. The early to mid-1960s period shows that, perhaps surprisingly, equities can outperform bonds over multi-year periods even when equity market returns are below average and the period includes a bear market. Low and/or rising bond yields can be a key contributor to such outcomes.

Long-term investors face an asset allocation conundrum over high equity market valuations and the possibility that interest rates may soon rise. Namely, exposure to equity market risk may not be rewarded with typical equity market returns, and an overweight position in bonds could mean sacrificing long-term equity returns. Realizing this conundrum is only a small step toward solving it.

Long-term investors may benefit from seeking approaches beyond just blending traditional asset classes to achieve the optimal middle ground between stocks and bonds. Adding equity correlated investments that combine reliable downside protection and greater long-term return potential than bonds may be particularly beneficial.

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# Standard Performance

Average Annual Performance							Risk** Since Inception*
As of March 31, 2017							
	1 Year	3 Years	5 Years	10 Years	20 Years	Return Since Inception*	
Index/RA (Net)	9.21%	4.67%	4.98%	3.27%	5.09%	7.25%	6.30%
S&P 500 <sup>®</sup> Index	17.17%	10.37%	13.30%	7.51%	7.86%	10.46%	14.21%
Bloomberg Barclays U.S. Aggregate Bond Index	0.44%	2.68%	2.34%	4.27%	5.36%	6.44%	3.76%

\*Inception of Gateway Index/RA Composite is January 1, 1988

\*\* Standard deviation is based on monthly performance

Periods over one year are annualized.

Datasource: Morningstar Direct<sup>SM</sup> and Gateway Investment Advisers, LLC

Past performance is no guarantee of future results.

For important disclosures, please refer to page 5.



**GATEWAY INVESTMENT ADVISERS, LLC**  
**GATEWAY INDEX/RA COMPOSITE**  
**ANNUAL DISCLOSURE PRESENTATION**

Year End	Annual Performance Results				3-Year Standard Deviation			Number of Composite Accounts	Composite Dispersion	Composite Assets (millions)	Firm Assets (millions)
	Composite Gross	Composite Net	S&P 500®	Bloomberg Barclays US Aggregate Bond Index	Composite	S&P 500®	Bloomberg Barclays US Aggregate Bond Index				
1993	8.44%	7.75%	10.08%	9.75%	N/A	N/A	N/A	15	0.7	\$ 348	\$ 408
1994	6.27	5.62	1.32	-2.92	N/A	N/A	N/A	14	0.5	303	660
1995	12.52	11.75	37.58	18.47	4.07%	8.34%	4.30%	12	1.6	283	473
1996	11.83	11.11	22.96	3.63	4.44	9.72	4.65	27	0.9	329	360
1997	13.34	12.58	33.36	9.65	3.83	11.30	4.06	27	1.1	399	476
1998	13.21	12.49	28.58	8.69	5.53	16.24	3.58	44	1.2	686	805
1999	12.94	12.27	21.04	-0.82	5.39	16.76	3.25	76	1.4	1,348	1,470
2000	6.55	6.08	-9.10	11.63	5.30	17.67	3.06	107	1.2	2,052	2,206
2001	-2.69	-3.28	-11.89	8.44	6.29	16.94	3.40	85	0.5	1,853	1,944
2002	-3.87	-4.45	-22.10	10.25	9.41	18.81	3.40	67	0.4	1,651	1,744
2003	12.53	11.84	28.68	4.10	9.70	18.32	4.26	59	0.4	2,029	2,160
2004	7.84	7.22	10.88	4.34	8.35	15.07	4.34	53	0.5	3,350	3,636
2005	5.86	5.17	4.91	2.43	4.09	9.17	4.12	35	0.5	3,879	6,134
2006	11.06	10.35	15.79	4.33	2.64	6.92	3.25	29	0.5	4,569	6,946
2007	8.67	7.99	5.49	6.97	3.10	7.79	2.80	25	0.5	4,780	7,892
2008	-13.39	-13.95	-37.00	5.24	8.41	15.29	4.03	22	1.0	5,073	7,071
2009	7.37	6.70	26.46	5.93	10.36	19.91	4.17	15	0.4	5,054	7,188
2010	5.76	5.11	15.06	6.54	11.01	22.16	4.22	12	0.1	5,552	7,699
2011	3.82	3.16	2.11	7.84	8.27	18.97	2.82	11	0.3	5,729	8,081
2012	5.41	4.74	16.00	4.22	5.84	15.30	2.42	10	0.2	7,424	10,517
2013	9.35	8.64	32.39	-2.02	4.23	12.11	2.75	11	0.2	8,899	12,475
2014	4.23	3.59	13.69	5.97	3.45	9.10	2.67	10	0.3	8,997	12,239
2015	3.20	2.54	1.38	0.55	3.97	10.62	2.92	11	0.2	8,783	12,210
2016	6.23	5.57	11.96	2.65	4.30	10.74	3.02	10	0.3	8,159	11,601

N/A: The three year annualized ex-post standard deviation of the Composite and benchmarks is not presented as 36-month returns are not available.

**Gateway Index/RA Composite contains fully discretionary hedged equity accounts which hold common stock and sell index call options on at least 95% of the underlying stock value. This call activity reduces volatility and provides cash flow. The accounts typically buy index put options that can protect the Composite from a significant market decline that may occur over a short period of time. Indexes utilized for call and put option activity are U. S. domestic equity indexes that include all sectors of the economy. The Gateway Index/RA Composite was created January 1, 1993. As of June 1, 2009, the Composite definition was refined to more accurately reflect the criteria used to determine membership. No membership changes resulted from the revision.**

For comparison purposes the Gateway Index/RA Composite is measured against two indexes, the S&P 500® Index (a popular indicator of the performance of the large capitalization sector of the U. S. stock market) and the Bloomberg Barclays U. S. Aggregate Bond Index, previously the Barclays U. S. Aggregate Bond Index (an unmanaged index of investment-grade bonds with one- to ten-year maturities issued by the U. S. government, its agencies and U. S. corporations). Prior to April 2008, the Lehman Brothers U. S. Intermediate Government/Credit Bond Index was utilized for comparison. The bond index change was made as the Bloomberg Barclays U. S. Aggregate Bond Index is widely viewed as more broadly representative of the fixed income markets and was considered to be more in line with the historical volatility associated with the Composite's investment strategy.

Performance results are based on fully discretionary accounts under management, including accounts that may no longer be with the firm, and are expressed in U.S. dollars. Performance returns are presented gross and net of management fees and include the reinvestment of all income. Past performance is not indicative of future results. The annual Composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the Composite the entire year.

Net of fee performance was calculated using actual management fees. The current investment management fee schedule is as follows: 0.85% on the first \$5 million; 0.65% on the next \$5 million; 0.50% on the next \$40 million; and 0.45% on assets in excess of \$50 million. Actual investment management fees incurred by composite accounts may vary.

Gateway Investment Advisers, LLC (Gateway) is an independent registered investment adviser and a successor in interest to Gateway Investment Advisers, L.P. as of February 15, 2008. Gateway claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS® standards. Gateway has been independently verified for the periods January 1, 1993 through December 31, 2016.

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS® standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS® standards. The Gateway Index/RA Composite has been examined for the periods January 1, 1993 through December 31, 2016. The verification and performance examination reports are available upon request.

Policies for valuing portfolios, calculating performance and preparing compliant presentations are available upon request. A list of composite descriptions is also available upon request.