The Ballad of "Fed" Clampett

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There has been a love affair between institutional investors and private equity (PE) over the past few decades. The significant pickup in demand for the investment strategy probably began after L.T.D., featuring Jeffrey Osborne, released their hit song "***Love Ballad***" in 1976. L.T.D. was formed in Greensboro, NC.

PE firms typically raise funds through general partnerships from institutional-type capital sources such as pension funds, endowment, family offices, and high-net-worth individuals. Relatively few people are qualified to participate directly. PE partnerships invest in firms which have not "gone public" and are not listed on any stock exchange. PE is highly illiquid because sellers of private stocks (called private securities) must first locate willing buyers. Investors in PE are generally compensated when: 1) the firm goes public, 2) it is sold or merges with another firm, or 3) it is recapitalized.

"Strengths of PE strategies are that they can generate attractive returns and investors can diversify broadly or target specific industries or geographies."

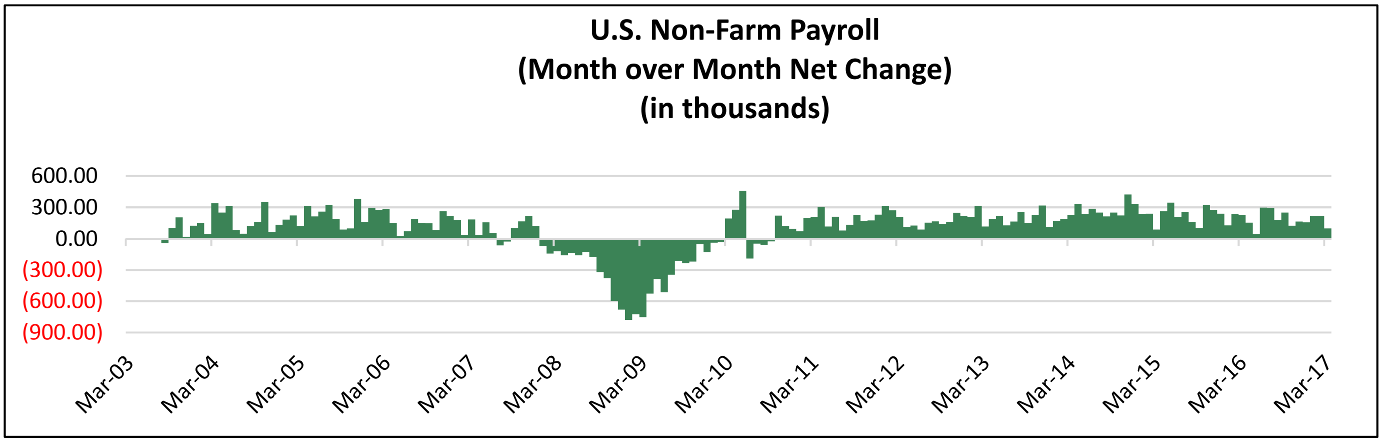
Strengths of PE strategies are that they can generate attractive returns and investors can diversify broadly or target specific industries or geographies. Some weaknesses are the lack of liquidity, especially during a financial crisis, 10-year life of a PE fund, opportunity costs, cyclical performance and manager selection risk.

The Clampett family from the TV series *The Beverly Hillbillies* would be considered an accredited investor after they struck oil, became millionaires and moved out to California from the hills of the Ozarks. Today, Mr. Drysdale, the banker for the Clampetts would most likely invest a good portion of their fortune in PE. Mr. Drysdale would no doubt boast about the historical returns for the asset class while Jed Clampett would stop his whittling long enough to say his catchphrase of "well, doggies!"

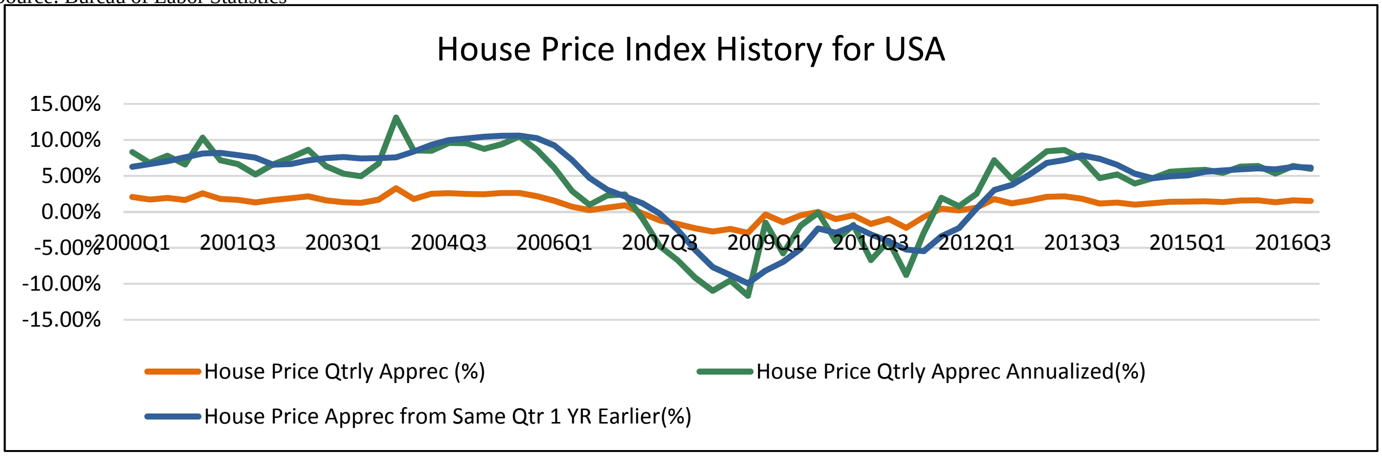
If we were to playfully update and re-write the opening stanzas to the TV sitcom series to fit the investment world, it would narrate a story that's slightly dissimilar from the original. If your memory fails you or you were never a fan, click the below link to hear the original. It'll help you with the Ballad of "Fed" Clampett on page 4.

https://www.youtube.com/watch?v=NwzaxUF0k18

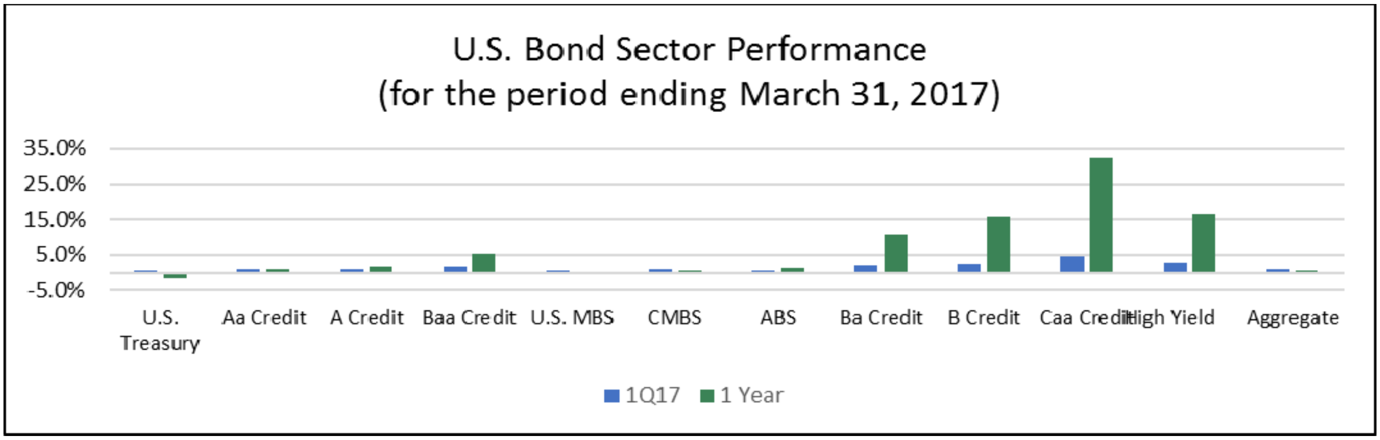
Please see "Ballad" on page 4



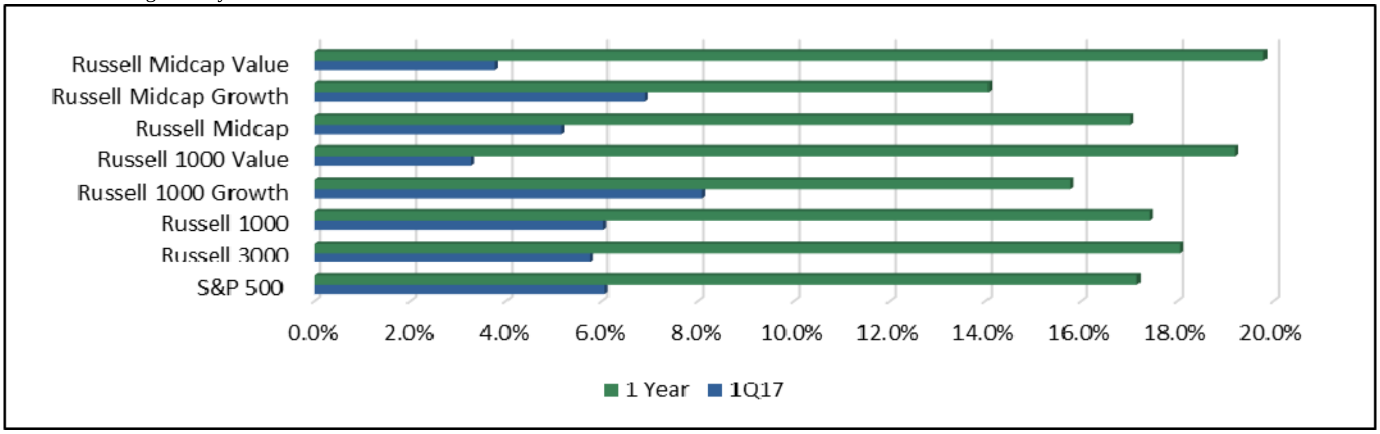
Source: Bureau of Labor Statistics



Source: FHFA



Source: Bloomberg Barclays Indices



Source: Bloomberg

Review and Outlook

Domestic equities continued their post U.S. elections rally into 1Q2017. The S&P 500 posted its largest quarterly increase since 4Q2015. The S&P 500 was range-bound between late 2014 and mid-2016 and has rallied nearly 13% from those levels. Information technology, health care and consumer discretionary were the sizable S&P 500 sector winners for the period. The energy and telecommunication services sectors were the laggards for the quarter.

The rally began to fade in early March and became vulnerable as investors were looking for new information and some results from the Trump Administration to keep markets going upward. The implementation of the administration's tax and reform policies are likely to take a lot longer than promised. As such, any other programs like infrastructure spending are likely to get pushed further out into the future.

"The Federal Reserve hiked U.S. interest rates by another 25 basis points in March, the second time in three months."

The Federal Reserve hiked U.S. interest rates by another 25 basis points in March, the second time in three months. It was also the third upward move since the financial crisis. Federal Reserve officials are expected to raise rates twice more this year per market forecasts.

The major domestic fixed income indices posted solid positive return numbers for 1Q2017, given the 4 basis point decrease in yield on the 10-year Treasury. The U.S. Aggregate index improved 1.31% during the quarter. High yield bonds posted positive returns while investment-grade debt also gained during the first quarter, according to Barclays Capital indices. The total returns from corporate high yield were 1.65% for the quarter, while returns from investment-grade corporate debt produced total returns 1.01%. High yield debt is rated below Baa3 by Moody's Investors Service and lower than BBB- by S&P.

The 2-year Treasury yield climbed 7 basis points while the 10-year Treasury yield decreased 4 basis points during the quarter to yield 1.26% and 2.41% for the period, respectively. Financial Institutions and Utility and were the best performing sectors within the U.S. Aggregate index. The two sectors returned 1.13% and 0.98%, respectively, for the quarter. U.S. Treasury bonds produced total returns of 0.54%. Baa bonds were the best-performing investment-grade credit quality during the first quarter, posting a 1.44% gain. Other Industrial, Transportation Services, Chemicals and Health Care were the best performing industries within the high yield corporate sector.

The Bloomberg News monthly survey of bond yields – which includes input from more than 60 economists – forecasts that U.S. Treasury 10-year yields will increase to 2.96% in 1Q2018 and then rise to 3.08% in 2Q2018. All the yields are more than the forecasted yields of the February survey. Market volatility is on the rise, with the equity indexes experiencing recent wide swings. Sentiment is undergoing alternating increases and decreases, in large part on the coming and going of news out of Washington, D.C. The stock market averages are still at near record levels, but challenges remain, especially in the areas of legislative reform, global relations, and the upcoming earnings reporting season.

We will continue to manage portfolios that tend to exhibit less volatility than their relative index and strive to deliver attractive risk-adjusted returns. Our portfolios are designed to perform over a full market cycle with a focus on downside risk, a style we believe will succeed over the long term.

"Ballad" from page 1

> *"Will pension funds and other investors continue to pump more money into PE funds as the lack of targets to deploy that money continues to climb?"*

The Ballad of "Fed" Clampett

Come and listen to a story 'bout a woman at the Fed
Poor pension plan could barely keep portfolios out of the red
Then one day the PM was shooting for some bonds with accrued
And up from the elevator comes two suits that are shrewd
(Investments that is, capital gold, private equity)

Well the first thing you know old Plan drafts a questionnaire
Consultant folks said Plan move away from there
Said Private Equity is the place you oughta be
So they loaded up the truck and allocated to fixed income rarely
(Buyouts that is, holding periods, IPOs)

The return from PE investments should equal the stock market returns (i.e., Russell 3000 index) plus a risk premium typically equal to 300 basis points (3 percent). This is the "benchmark" that limited partners (LPs) that invest in private equity expect to meet or beat. This is a benchmark widely used by pension funds. There is no perfect solution and no single PE benchmark that meets the definition of a good benchmark.

"Follow the money" has been a phrase to get to the root of money flow and direction of funds in the political and big business areas for years. According to Preqin, a PE research firm, "48% of respondents plan to increase their allocations to private equity over the long term, while a further 46% will maintain their allocations. Similarly, 49% of LPs are looking to invest the same amount of capital and 40% are looking to invest more capital in private equity in the next 12 months than they did during 2016."

Private equity has benefitted from a 25-year long-term trend of disinflation (from the mid-1980s to the Great Recession). Disinflation is the slowdown in the rate of inflation. The central bank's zero interest rate policy (ZIRP) and quantitative easing (QE) are policies that enabled the PE firms ascent. This cheap money is akin to a shot of Granny's "White Lightning". It feels good while you're throwing it back, but pay for it later with the hangover. Central banks have pushed investors into riskier assets in search of yield. As interest rates slowly increase over the next few years it could depress equity markets valuations, increase the cost of money and make it more difficult to achieve high levels of leverage for buyouts. Will pension funds and other investors continue to pump more money into PE funds as the lack of targets to deploy that money continues to climb?

Pitchbook's Global 2017 Crystal Ball Report noted that 53% of survey respondents said they are not planning to raise a new fund because they are still investing from a current fund. Currently, private equity firms worldwide have a combined $852 billion in dry powder (money to be invested).

Separately, net cash flow to limited partners — the difference between distributions of profits and contributions of capital to funds — is expected to continue to decrease in 2017.

Institutional investors want to invest more in the strategy, but PE firms are having some difficulty in finding attractive opportunities with returns that investors have become accustomed to. There could be more opportunities in healthcare sector specific deals because of the changes (or non-changes) to the Affordable Care Act (ACA).

Are PE firms a good investment? The IPO is an exit strategy for the company founders and early investors to profit from their early risk taking in a new venture. Table 1 depicts publicly traded asset management firms' and publicly traded private equity firms' stock price returns over various time periods. Four of the ten PE firms went public within the past 5 years on a rising stock market to cash out on a portion of their ownership.

"There could be more opportunities in healthcare sector-specific deals because of the changes or non-changes of the Affordable Care Act (ACA)."

TABLE 1 Period Ending 03/31/2017

Name	1 Year	2 Years	3 Years	4 Years	5 Years	7 Years	8 Years	10 Years
BlackRock Inc	15.4%	5.0%	9.5%	13.3%	16.4%	11.4%	17.4%	12.1%
State Street Corp	39.0%	6.3%	6.7%	9.7%	14.0%	10.3%	14.3%	3.6%
Franklin Resources Inc	10.2%	-7.7%	-6.3%	-2.8%	2.3%	3.9%	13.7%	2.4%
T Rowe Price Group Inc	-4.4%	-4.3%	-2.7%	0.8%	4.2%	6.2%	14.5%	6.6%
Invesco Ltd	3.3%	-9.1%	-3.1%	4.5%	5.9%	7.9%	13.4%	6.1%
Affiliated Managers Group Inc	1.1%	-12.6%	-6.4%	1.7%	8.0%	11.0%	18.7%	4.2%
Legg Mason Inc	6.9%	-17.2%	-7.9%	4.8%	7.2%	4.9%	12.3%	-7.6%
Eaton Vance Corp	38.0%	6.9%	8.6%	4.5%	13.1%	7.5%	12.0%	5.1%
Janus Capital Group Inc	-6.7%	-9.8%	9.6%	11.9%	11.3%	1.2%	11.3%	-2.8%
Federated Investors Inc	-1.6%	-6.9%	-0.2%	7.4%	9.5%	5.5%	8.3%	2.8%
Equally-weighted Returns	**10.1%**	**-4.9%**	**0.8%**	**5.6%**	**9.2%**	**7.0%**	**13.6%**	**3.2%**
Blackstone Group LP/The	11.9%	-5.7%	3.4%	18.3%	20.5%	17.7%	26.6%	-
KKR & Co LP	29.6%	-5.5%	-1.0%	5.1%	11.4%	-	-	-
Carlyle Group LP/The	4.2%	-15.4%	-15.9%	-7.6%	-	-	-	-
Oaktree Capital Group LLC	-3.0%	-1.8%	-3.3%	2.9%	-	-	-	-
Apollo Global Management LLC	52.8%	14.2%	0.0%	14.0%	23.5%	-	-	-
Prospect Capital Corp	40.3%	17.6%	7.3%	8.4%	8.9%	8.1%	13.9%	6.0%
Ares Management LP	29.8%	6.5%	-	-	-	-	-	-
Fortress Investment Group LLC	81.7%	6.5%	11.2%	13.3%	25.4%	15.9%	20.5%	-8.3%
Main Street Capital Corp	32.2%	21.1%	14.4%	13.4%	18.3%	23.3%	28.8%	-
Fifth Street Asset Management	63.4%	-29.3%	-	-	-	-	-	-
Equally-weighted Returns	**34.3%**	**0.8%**	**2.0%**	**8.5%**	**18.0%**	**16.2%**	**22.5%**	**-1.2%**
S&P 500 Index	**17.2%**	**9.2%**	**10.4%**	**13.1%**	**13.3%**	**12.9%**	**17.0%**	**7.5%**
Russell 3000 Index	**18.1%**	**8.5%**	**9.7%**	**12.8%**	**13.2%**	**12.9%**	**17.2%**	**7.5%**
Russell Midcap Index	**17.0%**	**6.0%**	**8.5%**	**12.1%**	**13.1%**	**13.1%**	**18.8%**	**7.9%**

Source: Piedmont Investment Advisors and Bloomberg

Traditional asset management firms have underperformed the broad equity markets partly because of deteriorating profit margins from fee pressure. Alternative investments are the industry's high margin strategies.

Six of the ten publicly-traded PE firms (Blackstone, Carlyle, Prospect Capital, Ares, Fortress Investment Group and Fifth Street Group) were trading below their IPO opening price as of March 31, 2017. Only Apollo Global Management, KKR, Oaktree Capital and Main Street Capital were trading higher than their opening price.

The $410 million 2013 purchase of Hostess out of bankruptcy by Apollo Global Management and C. Dean Metropoulos & Co would have made Granny smile. She could deep fry some state fair winning Twinkies that Jethro, Elly May and Jed would love. The two PE firms brought Hostess public in November 2016 and the share price is up nearly 23% year-to-date. Simple investments can make money too.

This is the eighth anniversary of the rally in risk assets that began in March 2009. Over that time the world has been dominated by macroeconomic factors. The steady economic expansion, restrained inflationary environment, and supportive monetary policies that have encouraged the late stage of this rally are still in place. While economic and political policy risks remain, they appear manageable.

"This is the eighth anniversary of the rally in risk assets that began in March 2009."

Investors who have focused on stock-specific trends rather than macro-driven ones have missed the forest for the trees. Choosing an appropriate asset allocation strategy has been the most important step in the investment process to manage macroeconomic risks.

Following the money continues to point to heaping helpings of higher yield risky asset. Too much money coming into the market and driving returns down is a constant buzzword of investors, as was the case in many ways in 2007. The sustained risk rally has led to elevated valuations in a range of asset classes.

Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) is an approximate measure of a company's operating cash flow based on data from the company's income statement. A PE deal that makes economic sense at 8.0x EBITDA may be unjustifiable at 10.5x EBITDA. This is an established concern. Investors have been questioning whether to retreat from risk assets for a while now. They are as nervous as a long tail cat in a room full of rocking chairs! There is a greater focus on chasing risky asset returns by investors today. The concern that we are at the top of a market cycle with elevated P/E ratios leaves little room for disappointments or missteps.

It is getting near the time to tail off the risk rally, in our opinion. High valuations should suppress medium-term returns and could magnify any downside moves. A sustained flight from risky assets is likely only if there is material weakening in the global economy. The Fed is reluctant to communicate a more aggressive normalization of policy and will continue to follow its game plan of measured rate hikes for a variety of reasons. An obvious one is fiscal policy uncertainty. It appears likely over the remainder of the year that the Fed will follow its plan and continue to normalize policy gradually.

Well now it's time to say goodbye.

Y'all come back next quarter, ya hear?

DISCLOSURE STATEMENTS

Additional Disclosure - A copy of Piedmont Investment Advisors, LLC Form ADV Part 2A, which describes our investment advisory services, fees and operations in more detail, is available upon request.

Investment Risk Disclosure - Fixed income securities are subject to the following investment risks:

Interest rate risk. Interest rate risk is the risk that debt securities will decline in value because of changes in market interest rates. Generally, when market interest rates rise, the value of debt securities declines, and vice versa. An account's investment in such securities means that the value of the account will tend to decline if market interest rates rise. The prices of long-term debt obligations generally fluctuate more than prices of short-term debt obligations as interest rates change.

Credit risk. Credit risk refers to an issuer's ability to make payments of principal and interest when they are due. Bond prices typically decline if the issuer's credit quality deteriorates. Lower grade securities may experience high default rates, which could mean that an account may lose some or all of its investments in such securities. If this occurs, the account's value would be adversely affected.

Investment grade bond risk. Investment grade bonds are considered less risky than bonds whose ratings are below investment grade; however, ratings are no guarantee of quality. The credit quality of these bonds can decline which would normally cause the prices of these bonds to decline.

Below investment grade bond risk. These bonds, commonly known as "junk bonds", involve a higher degree of credit risk.in the event of an unanticipated default, an account would experience a reduction in its income, a decline in the market value of the securities so affected and a decline in the account's value. During an economic downturn or period of rising interest rates, highly leveraged and other below investment grade issuers may experience financial stress that could adversely affect their ability to service principal and interest payment obligations, to meet projected business goals and to obtain additional financing. The market prices of below investment grade bonds are generally less sensitive to interest rate changes than higher-rated investments but are more sensitive to adverse economic or political changes or individual developments specific to the issuer. Periods of economic or political uncertainty and change can be expected to result in volatility of prices of these securities. NRSROs consider these bonds to be speculative in nature.

Equity Market Risk – Overall stock market risks may affect the value of the investments in equity strategies.Factors such as U.S. economic growth and market conditions, interest rates, and political events affect the equity markets.

Sector Focus Risk - The portfolios may be heavily invested in certain sectors, which may cause the value of its shares to be especially sensitive to factors and economic risks.These risk specifically affect those sectors and may cause the value of the portfolio to fluctuate more widely than a more broadly diversified benchmark.

Mortgage-backed securities risk. Mortgage-backed and securities are subject to prepayment risk. When interest rates decline, unscheduled prepayments can be expected to accelerate, and an account would have to reinvest the proceeds of the prepayments at the lower interest rates then available. Unscheduled prepayments would also limit the potential for capital appreciation on mortgage-backed securities. Conversely, when interest rates rise, the values of mortgage-backed securities generally fall. Since rising interest rates typically result in the decreased prepayments, this could lengthen the average lives of such securities, and cause their value to decline more than traditional fixed-income securities.

Performance Disclosure - Past performance is no guarantee of future results. Therefore, no prospective or existing client should assume that the future performance of any specific investment, investment strategy recommended and/or purchased by Piedmont Investment Advisors, LLC will be profitable or equal to corresponding indicated performance levels. Historical performance results do not reflect the deduction of transaction charges, investment advisory fees and/or other expenses, which, if included, would decrease the historical performance results. The collection of fees produces a compounding effect on the total rate of return net of management fees. As an example, the effect of investment management fees on the total value of a client's portfolio assuming (a) quarterly fee assessment, (b) $1,000,000 investment, (c) portfolio return of 8% a year, and (d) 1.00% annual investment advisory fee would be $10,416 in the first year, and cumulative effects of $59,816 over five years and $143,430 over ten years.

Index Comparison - Barclays Capital indices have been used as comparative benchmarks because the goals are to provide fixed income like returns. These indices are some the world's most recognized indices by investors and the investment industry for fixed income markets. These indices, however, are not managed portfolios and are not subject to advisory fees or trading costs. Investors cannot invest directly in these indices. These indices' returns also reflect the reinvestment of interest. Piedmont Investment Advisors, LLC is aware of the benchmark comparison guidelines set forward in the SEC Clover No-Action Letter (1986) and compares clients' performance results to a benchmark or a combination of benchmarks most closely resembling clients' actual portfolio holdings. However, investors should be aware that the referenced benchmark funds may have a different composition, volatility, risk, investment philosophy, holding times, and/or other investment-related factors that may affect the benchmark funds' ultimate performance results. Therefore, an investor's individual results may vary significantly from the benchmark's performance.

Forward Looking Statements

This newsletter may include forward-looking statements. All statements other than statements of historical fact are forward-looking statements (including words such as "believe," "estimate," "anticipate," "may," "will," "should," and "expect"). Although we believe that the expectations reflected in such forward-looking statements are reasonable, we can give no assurance that such expectations will prove to be correct.

Past Performance

Past performance is not indicative of any specific investment or future results. Views regarding the economy, securities markets or other specialized areas, like all predictors of future events, cannot be guaranteed to be accurate and may result in economic loss to the investor.

Risk

Investment in securities, including fixed income instruments, involves the risk of loss.