

THE YEAR 2016



This has been a fascinating and eventful year for investors. It's been a year of challenges, philosophical debate and struggle. There's also been a great deal of progress. Traditional norms are being tested and reassessed. We're seeing it politically, socially and economically. Change has been a multi-year theme. It continues.

Globalization is being re-thought. Nationalism is on the rise while free trade seems to be losing friends. There is a power shift around the globe. The West is being challenged by the East. Europe and

America are also facing challenges from within. The Brexit vote and our Presidential election are direct reflections. Emerging Markets are on the rise while Mature Markets continue to evolve.

2016 will leave a permanent mark on what the future of planet Earth becomes. It will have profound influence on global markets. Despite all of these issues, the Bull Market has been alive and well, with the DOW and S&P reaching new, all-time highs in volatile fashion.

We expect the volatile price action to continue through the election. Having a clear understanding of who will occupy the White House the next 4 years will be a positive development, even if it isn't clear what the policies will be. Knowing the fate of the European Union and whether Great Britain remains a part of it will be critical too. As we all know, the Market hates uncertainty.

US ECONOMY IS STILL GROWING

United States Gross Domestic Product (GDP) officially grew at 1.4% in the second quarter. It isn't strong growth, but it's moving in the right direction again. The first quarter saw a weak 0.8% increase which followed 0.9% growth in the fourth quarter of last year. The US economy likely accelerated over the summer, helped by strong consumer spending. Consumer spending accounts for approximately 70% of economic activity. Things appear to be ramping ahead of the holidays.

EARNINGS GROWTH HAS BEEN ABSENT

Generally, stock prices are driven by corporate earnings. The problem is, earnings growth has been absent for much of this Bull Market. In fact, the S&P 500 has seen an earnings contraction for over a year now. That's why there's been strong demand for stocks that are experiencing growth. Amazon and Google come to mind. Innovative and tech-savvy companies are generally thriving in the digital age. Mature companies that haven't evolved have struggled.

LOW INTEREST RATES = CHEAP MONEY



So why has the Stock Market hit new highs despite no earnings growth you ask? Low interest rates and a supportive Fed has been the magic elixir for this Bull Market. It's been a unique characteristic

unlike previous Bulls. Central banks around the globe have been extremely aggressive with monetary policy to help support struggling economies. Interest rates are low and in some cases negative. Money has been cheap, and it's been buying American assets. Stocks, bonds and real estate have all done well.

The Fed has a big decision ahead, whether to raise rates again or not. The US economy is experiencing slow but stable growth. The unemployment rate is quite low, at 5%, something the Fed tracks closely. Fed Chair Janet Yellen is on record saying a rate hike is likely before year's end. It's the international issues that seem to have been holding them back. Even though we expect interest rates to rise, we don't see them taking off. We believe this "lower for longer" interest rate environment continues.

THE PRICE OF OIL MATTERS



Plummeting oil prices precipitated the January selloff. After falling to \$26, the price of oil has doubled to \$50 again. This is important for a number of reasons. There are many companies and countries that are dependent on oil and have debt denominated in US Dollars. There was tremendous stress in the financial system last winter when oil prices fell. Higher oil has provided substantial relief to the system. Rising oil prices also speak to global demand and overall economic activity picking up. The world still runs on crude. Lastly, there has been a strong correlation between the price of oil and the stock market. Higher oil has led to higher stock prices. This trend should continue.

M&A MEANS DEALS



Here at home in the United States as well as overseas, deals continue to take place. And it's been pretty broad-based. There have been big deals in health care, the consumer industry, Telecom and Tech. The flow of deals is in fact accelerating. Mergers & acquisitions (M&A) are very positive for the Market. It shows that companies are focused on long-term growth and they still find value in today's prices. Tech continues to be a big leader for growth. We are always in search of underappreciated value. It continues to be a stock picker's market.

DESPITE ALL OF THE ISSUES, THE BULL IS ALIVE AND WELL



Globalization is under assault. Nationalism is on the rise. Free markets are facing great resistance. People aren't against innovation and efficiency. They want it. They demand it. Our modern lives depend on it. However populations seem to be increasingly against free trade. You really can't have one without the other. Innovation feeds off free trade. Investment and risk taking are required. Globalization has created so much wealth and opportunity. It's also left many behind. This issue is being addressed in political elections and votes around the world. We are studying these trends very closely. They will have significant influence on investments.

Bull Markets never die of old age. It's generally a recession or crisis that takes them down. The volatile price action speaks to the many issues that plague investors today. We expect things to remain volatile through the Presidential election and believe selloffs are still buyable. We see plenty more room to run for this Bull.

S&P 500 HISTORIC AND ANTICIPATED PATH

