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WHAT'S HAPPENING POST BREXIT?

Market Review **August 2016**

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Now that the Brexit vote—Britain's vote to leave the European Union ("EU")—is behind us. It is worth examining the aftermath. At first, investors panicked. Polling data and expert opinions suggested that the vote would fail, so the results were a surprise. As a result, many investors were caught betting on the wrong outcome and needed to work quickly to limit their losses. The resulting flurry of trading produced a small overreaction, which pushed stock prices down around the globe.

Once investors and politicians had time to consider the implications, they realized that most of the consequences of leaving the EU would not arrive until Britain officially notified the EU of its intent to withdraw and that notification was likely months away. For a brief moment, investors seemed to breathe a sigh of relief and stocks started to recover the losses that they had suffered immediately after the Brexit vote. Unfortunately, Britain's Prime Minister, David Cameron, resigned because he campaigned against Brexit and saw the vote as a rebuke of his policies, and the politicians that campaigned for Brexit were caught unprepared. With no plan and no consensus on who would become the next Prime Minister, investors retreated to safety once again and foreign stock markets stumbled again.

The fight over who would be Prime Minister was short and the no-nonsense politician, Theresa May, found herself ascending to the office. Apparently, this was the signal that investors were looking for and they quickly rediscovered the appetites for risk. In fact, some US stock indexes set new record highs by the end of the month.

Meanwhile, the price of oil is a growing cause for concern among investors and analysts alike. The price of oil nearly doubled during the first half of this year and this lead some investors—especially hedge funds—to make some very optimistic investments in this recovery. These investors had some compelling arguments for their optimism. First, the number of active oil rigs had been falling steadily, inventories of crude oil had started to decline, and American gasoline consumption was on pace to its highest level ever. The combination of those three figures gave hope that the oil supply (i.e. rigs and inventories) was coming into line with oil demand (i.e. gasoline consumption) and that prices would continue to rise.

Unfortunately, the market for oil is much more complicated than that. Some US oil producers were watching the price of crude oil and biding their time. Once that price reached a point where they could start to sell at a profit again, they reactivated some of their idle rigs. In addition, while inventories of crude oil were falling, inventories of gasoline were rising. During July, the price of oil softened from nearly $50 per barrel to about $40 per barrel, which may not be enough to drive the rig count back down. As a result, we may see another small dip in oil prices before the recovery really finds its feet.

As the summer winds down in September, we will continue to keep an eye on developments in Britain and the EU. The price of oil will also be getting some increased scrutiny as a real recovery becomes more likely. Also, we will be watching the US Federal Reserve to see whether it decides to lift interest rates again or opts to stay the course that it set in June.

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Market Movers

US Stocks hit new highs in July, even after the hiccups in late June and early July. It is worth noting that investors appear to be reluctantly optimistic. They eagerly seize on bad news and move quickly toward safe haven assets like bonds and precious metals, but they also dutifully buy up riskier assets if no additional threats are publicized. As US equity market highs persist, this makes the need for risk management and broad investment exposure increasingly important. Since the beginning of the year and over the last year, the Core Allocation portfolios have performed exceptionally well. Across all risk levels, these portfolios are keeping pace or outperforming global equities while showing significantly stronger returns relative to Morningstar's World Allocation category.

Asset Categories	*July 2016*	*YTD*
US STOCKS	4.47%	8.77%
FOREIGN STOCKS	4.78%	7.10%
US BONDS	0.76%	5.02%
FOREIGN BONDS	2.51%	12.97%
HARD ASSETS	3.44%	19.96%
HYBRIDS	2.77%	6.77%

*DATA USED IS SOURCED FROM MORNINGSTAR®

While returns for US STOCKS and Foreign Stocks appear similar for the month of July, US Stocks achieved their performance with less volatility than their foreign counterparts. US Small Caps (VB) led the way, followed by US Mid Caps (VO) and US Large Caps (IVV).

FOREIGN STOCKS recovered after their Brexit losses, but they suffered some bumps along the way. In particular, the first week of July saw another dip in Foreign Stock prices, when it became obvious that British politicians did not have a clear plan for handling the aftermath of the Brexit vote. By month end, International Small-Mid Caps (VSS) bounced back to a gain of over 5%, while Emerging Large Caps (VWO) and Developed Large Caps (VEA) returned over 4%.

US BONDS saw investors moving into higher risk assets. Bank Loans (BKLN) and US High Yields (SJNK) saw gains of nearly 2%. These have been some of the best performers year to date, and our portfolios have benefited from an increased allocation to these areas during this time. The more traditional bond markets, such as US Treasuries (SHY) and US Corporates (VCSH), were generally flat during the month of July.

FOREIGN BONDS continue to benefit from our decision to use the higher-yielding bond sectors, as opposed to the bonds issued from developed countries which currently have very low interest rates. Specifically, during the month of July, Emerging Treasuries (PCY) rose by nearly 3% and Emerging High Yields (HYEM) pushed to a gain of over 2%. Since the beginning of the year, these two bond sectors have gained over 12%, generally outpacing even most equity investments during that time.

HARD ASSETS continue to be strong performers, but this hasn't come without volatility. Precious Metals (GLTR) benefitted from concerns about Brexit and posted a strong gain of over 5% for the month. Conversely, Master Limited Partnerships (AMJ) struggled with softening oil prices and fears of another period of oversupply, which left them relatively flat for the month. Year to date, Hard Assets are the top performing category and serve as an important component of our portfolios.

HYBRIDS continue to provide steady and attractive returns, both over the last month and year. As we continue to hit new stock market highs in the US, we believe that the investment characteristics of Hybrids provide attractive benefits for our portfolios.