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Q2 2016 – Market Overview Newsletter

Economic Update

The first six months of 2016 have certainly been tumultuous. By February 11, 2016, the S&P 500 had dropped more than 10%. It was one of the worst starts to a year on record. However, if you persevered through to mid March, investments were back in positive territory. At the end of the second quarter there was “Brexit”, a term I’m sure we are all familiar with by now. After the votes were tallied and the UK decided to leave the European Union (EU), we saw a negative impact on markets worldwide. Yet a few days later, markets had already started to recover and finished the quarter on the positive side.

The S&P 500 closed up nearly 2.5 percent for the quarter and 3.8 percent for the first half of 2016. Value stocks performed better than growth during the quarter, and mid- and small-caps outpaced their large-cap brethren. Energy company stocks also did well during the period thanks to a rally in oil prices, while technology and financial stocks generally underperformed for the quarter.

Naturally with the Brexit news affecting U.K. and European investors, market indexes in Europe suffered greater losses than the U.S. While markets in Europe and the U.K. also recovered from the sharpest losses by quarter-end, they finished the first half of 2016 in negative territory.

Perhaps the biggest impact Brexit has had so far is in the fixed income markets, where government bond yields closed lower again for the quarter. After the Brexit announcement, U.S. 10-year yields fell below the 1.5 percent level then tumbled to record lows in the early days of July. More world governments saw the yields on their long-term bonds go negative in the 2nd quarter, notably in Germany where 10 year bond yields dropped below zero.

No one is really talking about interest rates rising anytime soon either, which is a distinct difference from previous quarters. Fixed income analysts had continually warned that higher interest rates were just around the corner and the long rally in the bond market was coming to an end. Although that is still a possibility, it seems a long way off at this point.

In the current environment of political uncertainty and market volatility, the Federal Reserve (Fed) won’t likely take any steps that would jeopardize the economic recovery. During the quarter, expectations for Fed rate hikes this year had already fallen but once Brexit happened the possibility for any Fed action in the near future was seemingly off the table. Although some economists would argue this is a mistake and the Fed’s inaction will create uncertainty which could have a negative impact as well.

The Economy! Brexit! The election! Oh my!! There certainly seems to be plenty of reasons to worry but that is nothing new. If you look at history there have always been reasons not to invest and plenty of bad news. A Nielson study found that CNBC had its best ratings day ever on September 29, 2008 when the S&P 500 had its worst single day drop since 1987. We have all heard the saying “Bad news sells.”

Are things really all bad? The US economy appears to still be growing, just slowly. The UK has voted to leave the EU but the process of negotiating their exit will take at least a couple of years. Keep in mind, when the UK joined the EU in the 70’s it was also controversial but not necessarily bad. Maybe their decision to again be independent won’t either. Then there is the upcoming election which no one seems particularly excited about, except for maybe Hillary and Donald. No matter who you are for or against, history has shown that the resident of 1600 Pennsylvania Avenue will have little impact on your portfolio.

As always, staying the course and having a financial plan are two of the best ways to stay positioned for your long-term goals.

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For more market details from the second quarter, see the "Capital Analysts Q2 2016 Market Review" in the commentaries page on our website at www.langdonshaw.com/commentaries.

Disclosures and Definitions

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All indexes are unmanaged; it is not possible to invest directly in any index.

The Treasury yield is derived from available U.S. Treasury securities trading in the market and is provided directly by the Federal Reserve. U.S. Treasuries are regarded as the "risk-free rate" and are typically used as an approximation of general interest rate levels in the U.S.

Growth investments focus on stocks of companies whose earnings/profitability are accelerating in the short term or have grown consistently over the long term. Such investments may provide minimal dividends which could otherwise cushion stock prices in a market decline. Stock value may rise and fall significantly based, in part, on investors' perceptions of the company, rather than on fundamental analysis of the stocks. Investors should carefully consider the additional risks involved in growth investments.

Value investments focus on stocks of income-producing companies whose price is low relative to one or more valuation factors, such as earnings or book value. Such investments are subject to risks that their intrinsic values may never be realized by the market, or such stock may turn out not to have been undervalued. Investors should carefully consider the additional risks involved in value investments.

Large Cap refers to companies with a market capitalization value of more than $10 billion. Large cap is an abbreviation of the term "large market capitalization." Market capitalization is calculated by multiplying the number of a company's shares outstanding by its stock price per share. Small and mid-cap stocks may be subject to a higher degree of risk than larger, more established companies' securities, including higher risk of failure and higher volatility. The illiquidity of the small and mid-cap markets may adversely affect the value of these investments so those shares, when redeemed, may be worth more or less than their original cost.
International investing involves special risks, including, but not limited to, the possibility of substantial volatility due to currency fluctuation and political uncertainties.

In general, the bond market may be volatile, and fixed income securities carry interest rate risk. (As interest rates rise, bond prices usually fall, and vice versa. This effect is usually more pronounced for longer-term securities). Fixed income securities also carry inflation risk, liquidity risk, call risk and credit and default risks for both issuers and counterparties. Lower-quality fixed income securities involve greater risk of default or price changes due to potential changes in the credit quality of the issuer. Any fixed-income security sold or redeemed prior to maturity may be subject to loss.

S&P 500 consists of the common stocks of 500 large-capitalization companies, within various industrial sectors, most of which are listed on the New York Stock Exchange. It is considered a broad measure of U.S. domestic equities. The stocks represented by this index involve investment risk which may include the loss of principal invested. The prices of small and mid-cap stocks are generally more volatile than large-cap stocks.