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Eye on the Market Express: July 2016

MARKET DATA				
	June	3 Mo.	YTD	1 Year
S&P 500	0.09%	1.90%	2.69%	1.73%
Russell 2000	-0.25%	3.40%	1.41%	-8.14%
NASDAQ	-2.13%	-0.56%	-3.29%	-2.89%
MSCI EAFE ($ basis)	-3.56%	-2.64%	-6.28%	-12.70%
MSCI EAFE (local)	-3.98%	-1.92%	-9.02%	-12.73%
UK (FTSE)	4.39%	5.33%	4.20%	-0.26%
Germany (DAX)	-5.68%	-2.86%	-9.89%	-11.56%
Japan (NIKKEI)	-9.63%	-7.06%	-18.17%	-23.03%
MSCI Emerging Markets ($ basis)	3.30%	-0.32%	5.03%	-14.21%
Barclays Aggregate	1.81%	2.21%	5.31%	6.00%

All market data as of the end of June 2016. Quoted index returns are based on month end index prices (in local currency except where noted) and do not include dividends.

U.S. ECONOMIC DATA				
	June	Prior Month	Beginning of Year	1 Year Prior
10 year Treasury Yield	1.49%	1.83%	2.27%	2.34%
Gold (London pm fixing per ounce in dollars)	1,321	1,212	1,062	1,171
Oil ($ per barrel)	48.57	49.10	37.13	58.33
VIX Index	15.63	14.19	18.21	18.23

All economic and market data as of the end of June 2016.

The Federal Open Market Committee (FOMC) met in June and elected to maintain the benchmark Federal Funds rate in a range of 0.25-0.50%. The decision was largely anticipated as the month opened with an unexpectedly weak jobs report, and the British vote to remain in or leave the European Union (Brexit), a source of considerable economic uncertainty, was scheduled after the FOMC meeting. It appears the FOMC's projections for future rate increases may be converging with those of the market. The market has consistently indicated expectations that there will be fewer rate increases than the Fed has communicated, and while at the April meeting, just one member indicated that the year would end with only one hike, that number jumped to six at the June session. After the June FOMC meeting and before Britain voted to leave the E.U., Federal Reserve Chair, Janet Yellen, testified before Congress where she generally struck a cautious but upbeat tone on the U.S. economy. She called the probability of a recession in the U.S. "quite low," commenting that "we've seen a strong pickup in consumer spending and growth in the economy," and adding "the kind of conditions that have been associated in the past with U.S. recessions…we don't have any such conditions in play now." However, she did acknowledge that there has been a slowing of growth in the labor market calling it "not a deterioration but a loss of momentum in terms of the pace of improvements." When asked about the potential impact of Brexit, she called it uncertain but predicted "we might see flight to safety flows that could push up the dollar or other so-called safe-haven currencies." Yellen's forecast proved largely accurate after 51.89% of British voters elected to leave the European Union and U.K. Prime Minister David Cameron resigned from office.

Economic data released in June was mixed, but the month began with a very disappointing jobs report as non-farm payroll additions for May came in at just 38,000 when 162,000 had been forecast. The unemployment rate dropped from 5.0% to 4.7%, but the decline was due to a reduction in the labor force participation rate, which edged down to 62.6%. Although labor market data has generally been positive in recent months, there has been a trend of declining growth in payroll additions since last fall, so May's weak reading stoked concerns about the general health of the economy. However, weekly initial unemployment claims have remained muted with all readings coming in below 300,000, and wages were a bright spot in the labor market data, growing at a 2.5% rate on an annualized basis, which is above the rate of inflation, meaning workers have seen real increases in their pay. Inflation, as measured by the Fed's preferred metric, the Personal Consumption Expenditures index, rose 0.2% in May from the month prior, but from a year earlier it is only up 0.9%. Even when more volatile food and energy prices are excluded the index was only up 1.6% from a year ago, still well below the rate of wage growth and the Fed's 2.0% target. Data regarding the U.S. consumer released in June was generally positive. Personal spending and retail sales followed up strong growth in April with steady gains in May, rising 0.4% and 0.5% respectively. In another sign of stronger consumer confidence, the personal savings rate in May was 5.3%, the lowest level of the year and well down from a near-term peak of 6.0% in March. Data regarding inventories also indicated a healthy consumer as the time it would take to clear wholesale and business shelves, the inventory turnover ratio, moved lower due to strong increases for the month in both wholesale and business sales, which grew 1.0% and 0.9% respectively. However, consumers purchased 2.2% fewer durable goods last month after robust purchases in April. The two primary measures of consumer attitudes, the University of Michigan's consumer sentiment index and the Conference Board's Consumer Confidence index, moved in opposite directions again in June. The University of Michigan measurement declined due to diverging views of present and future economic conditions, with the future outlook declining and the present outlook actually increasing to its highest level since 2007. The Conference Board reading moved up to its average level for 2015 after an unexpectedly large decline the month prior. Neither takes into account the impact of the Brexit vote as it happened too late in the month. Housing continues to be an area of strength in the economy. New home sales for May posted their second best month since the recession ended with a seasonally adjusted annual rate of 551,000 units, and existing home sales hit a nine year high to an annual rate of 5.52 million units. Home prices, as measured by the S&P/Case-Shiller 20-city composite index rose 5.4% year-over-year with seven cities now seeing new highs for home prices. However, data for June may indicate a decline in home sales as pending home sales for May declined 3.7%, mainly due to low inventory since the supply of homes for sale is 5.7% smaller than it was a year ago. Finally, the Commerce Department once again raised its estimate of the pace of growth in the first quarter from 0.8% to 1.1% with the improvement largely coming from stronger net exports than previously estimated. Companies also spent more than expected on software and research and development.

Domestic equity returns in May were mixed, with the benchmark S&P 500 index nearly flat, rising 0.09%. Small-cap stocks mildly underperformed the broader market, losing 0.25% in June, and the tech-heavy NASDAQ composite lost 2.13% over the same time period. These relatively muted returns belie considerable intra-month volatility as equity markets dropped precipitously in reaction to Britain's vote to leave the European Union then snapped back up a few days later, allowing the quarter to end on an uptick. For the second quarter the S&P 500 and the Russell 2000 delivered positive returns, 1.90% and 3.40% respectively, but the NASDAQ declined 0.56% over the same period. Financial stocks were the sector hardest hit by Brexit, losing 3.21% for the month, and it is the worst performing sector for the year. Financial stocks were vulnerable to Brexit since it reduced the likelihood of the Fed raising rates, and financial companies such as banks and insurance companies have seen their profits challenged by the low interest rate environment. In general, corporate profits have been pressured by low energy prices and the strong dollar, and FactSet, a data provider, forecasts profits will decline 5.3% for the second quarter from the year prior, which would be the fifth quarter in a row of year-over-year declines in earnings, although they are currently predicting a return to earnings growth in the third quarter.

International stocks were mixed in June with the MSCI EAFE Index losing 3.98% for the month on a local currency basis, and for the year it is down 9.02%. When translated into dollars, the index declined a slightly less 3.56% since the dollar declined over the course of the month as the FOMC elected not to raise interest rates, although it strengthened later in the month after the Brexit vote. Of the indexes covered in this commentary, Britain's FTSE 100 index had the best performance for the month, growing 4.39% when measured in pounds because the index is mainly comprised of multinational companies. Measured in pounds, the more locally focused FTSE 250 declined 5.32% over the month. In general, international equity indexes reacted to Brexit similarly to domestic equity indexes, selling off for a few days immediately following the vote, then paring back losses, but currency declines have endured so far. The British pound lost 7.47% and the euro lost 2.56% against the dollar between the vote and the end of the month. Investors view the Japanese yen as a safe haven currency, and it appreciated even more than the dollar, rising 13.14% against the pound and 4.54% against the euro over the same period. This was an unwelcome development since the Bank of Japan has been attempting to stimulate growth in the export-driven Japanese economy by weakening the yen, which was a leading cause of the Nikkei losing 9.63% in June. Emerging markets were a relative bright spot this month for international equities with the benchmark MSCI Emerging Markets index gaining 3.30% in June, and for the year it is up 5.03%.

Fixed income prices for both the U.S. and developed economies rose in response to Brexit. The yield on the 10-year Treasury note moved from 1.83% at the beginning of the month to near historic lows of 1.49% at its close and the best performing domestic fixed income sector was long dated Treasuries, which rose 6.14% as measured by the Barclays Long Term US Treasury index. Other developed markets which have been struggling with deflationary pressures saw yields on their 10-year bonds move to or decline further into negative yields. The 10-year German bund yield moved into negative territory after the Brexit vote to yield -0.13% at the end of the month, and the 10-year Japanese government bond declined to -0.22%. Credit-sensitive domestic fixed income underperformed the general bond market, but still delivered positive returns with the Barclays U.S. High Yield index growing 0.92% for the month. The worst performing sector was short-term Treasury Bills, which were essentially flat.

Commodity returns for June were mixed. The benchmark Reuters/Jefferies CRB index moved up 3.45% for the month, and for 2016 it has gained 9.33% for the year. Oil prices edged down modestly this month to close at $48.57 per barrel, but gold appreciated 8.96% in June, benefiting from currency volatility and its perceived status as a safe haven in times of uncertainty. Finally the VIX index, which is a measure of volatility, began the month at 14.9, spiked to 26.72 after the Brexit vote, then moved lower to end the month at 15.63.

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INDEX	DESCRIPTION
10 Year Treasury	The closing yield on 10-year Treasury notes calculated on a daily basis. Data sourced from the Federal Reserve.
Barclays Capital Aggregate Bond Index	A broad based index used to represent performance of investment grade bonds traded in the United States. The index includes Treasury securities, government related and corporate securities, mortgage-backed securities and asset-backed securities.
Barclays Municipal Bond Index	An unmanaged index considered representative of the tax-exempt bond market.
BofAML Masters II High Yield Index	An unmanaged index tracks the performance of below investment grade, but not in default, U.S. dollar-denominated corporate bonds publicly issued in the U.S. domestic market, and includes issues with a credit rating of BBB or below, as rated by Moody's and S&P.
Conference Board Consumer Confidence	An indicator used to measure consumer confidence in the economy produced by the Conference Board on a monthly basis based upon a survey of 5,000 households.
DAX (Germany)	A total return index of 30 selected German blue chip stocks traded on the Frankfurt Stock Exchange.
Dow Jones Industrial Average	An unmanaged index of 30 widely held securities.
Federal Funds Rate	Targeted interest rate at which depository institutions lend to each other overnight. The rate is targeted by the Federal Open Market Committee (FOMC).
FTSE (UK)	A capitalization-weighted index of the 100 most highly capitalized companies traded on the London Stock Exchange.
FTSE NAREIT All REITs Index	Market capitalization weighted index that includes all tax-qualified REITs listed on the New York Stock Exchange.
GDP	A measure of broad economic output in the United States produced by the US Bureau of Economic Analysis on a quarterly basis with revisions made monthly.
Gold	Value of gold based upon the afternoon fix (15:00 GMT) in London each afternoon.

ISM	A measure of manufacturing activity reported by the Institute of Supply Management each month. A reading over 50 signifies growth in manufacturing during the month.
MSCI EAFE	A widely accepted benchmark of foreign stocks. It comprises 21 MSCI country indices, representing the developed markets outside North America: Europe, Australasia and the Far East.
MSCI Emerging Markets	A widely accepted benchmark of emerging markets stocks. It is a float-adjusted market capitalization index designed to measure equity market performance in the global emerging markets.
NASDAQ	An unmanaged index of all stocks traded on the NASDAQ over-the-counter market.
Nikkei (Japan)	An unmanaged price-weighted index of 225 widely held stocks listed in Japan.
Oil	Closing value of light, sweet crude oil futures in the near month.
Retail Sales	A measure of retail sales compiled monthly by the US Department of Commerce
Russell 2000	An unmanaged index of small cap securities.
S & P 500	An unmanaged index of 500 widely held stocks.
Shanghai Composite	Index of all listed (A and B share class) stocks traded on the Shanghai Stock Exchange.
Thomson-Reuters Jefferies CRB Index	A widely accepted benchmark of commodity prices. The index is designed to provide a representation of long-only broadly diversified investment in commodities.
Unemployment	A measure of unemployment compiled monthly by the US Bureau of Labor Statistics.
VIX Index	Measure of market expectations of near-term volatility based on S&P 500 stock option prices.

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