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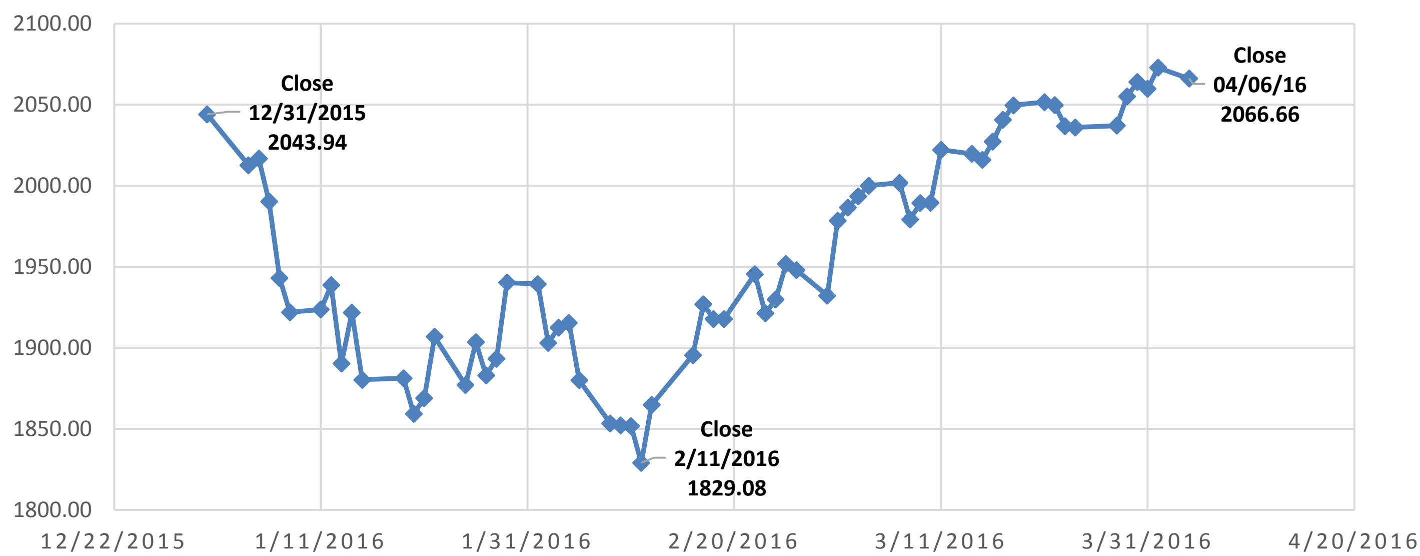
Q2-2016 Letter to Investors April 7, 2016

Take warning of the misfortunes of others
— Aesop

A lion, unable from old age and infirmities to provide himself with food by force, resolved to do so by artifice. He returned to his den, and lying down there, pretended to be sick, taking care that his sickness should be publicly known. The beasts expressed their sorrow, and came one by one to his den, where the Lion devoured them. After many of the beasts had thus disappeared, the Fox discovered the trick and presenting himself to the Lion, stood on the outside of the cave, at a respectful distance, and asked him how he was. "I am very middling," replied the Lion, "but why do you stand without? Pray enter within to talk with me." "No, thank you," said the Fox. "I notice that there are many prints of feet entering your cave, but I see no trace of any returning."

S&P 500 YEAR-TO-DATE PRICE MOVEMENT



Global economies have been in a game of tug-of-war between healthy consumer consumption and weak industrial output. The dichotomy between the two has created investor anxiety. On February 11th the S&P 500 fell to 1,829.08, down 10.5% from its 2015 close. It was the lowest point the market traded in 2 years. The market got off on the wrong foot at the start of 2016. Stocks sold off hard as investors moved from risk-on to risk-off. The first quarter was not profitable and neither was the past year for that matter. Looking back to April 7, 2015 the S&P 500 closed at 2,076.33, slightly above the current level. So, here we are today, a year later with miniscule price appreciation.

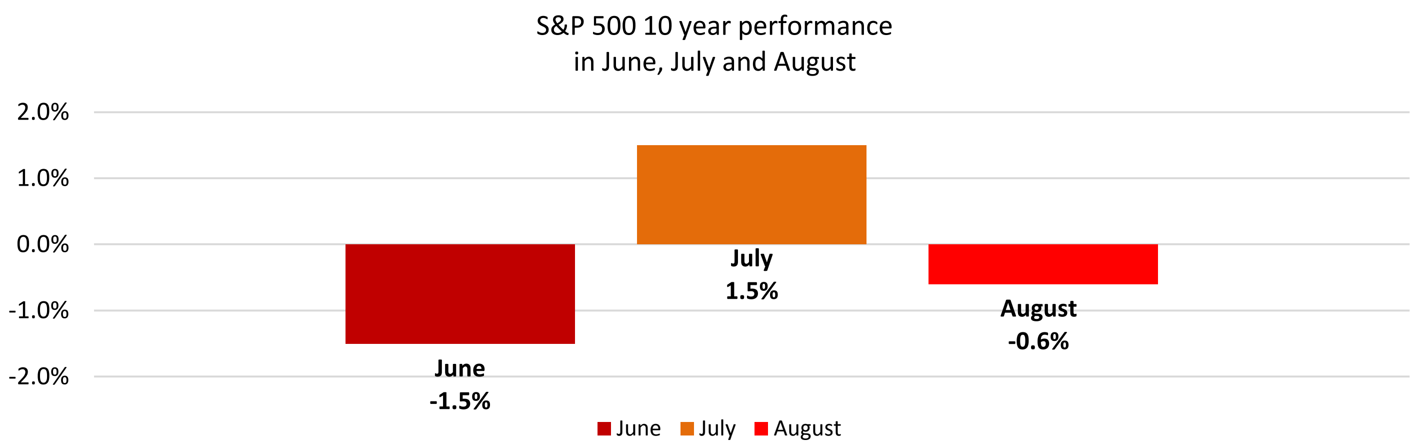
What are the reasons for the market's lingering malaise? The causes of today's less than ideal economic environment are our usual suspects: slowing global growth, dollar appreciation, rising debts, feeble manufacturing, burgeoning healthcare cost, stagnant wages and salaries, Puerto Rico bonds, Chicago pensions, unprovoked violence and expansive government. It also seems that America is under siege from predatory legal practices, an issue conveniently unaddressed by those making the rules. Jobs, low interest rates, an accommodative Fed, cheaper gasoline, housing strength and favorable sentiment are the fuels keeping things moving forward. It is the consumer that is driving this economy.

On March 29th Janet Yellen addressed the members of the Economic Club of New York. Wall Street and the financial media parsed Yellen's every word to guestimate the timing and magnitude of the Fed's next rate increase. The Fed chair said it was appropriate to "proceed cautiously." One sentence later she stated, “Caution is especially warranted.” In December Yellen noted that interest rate increases would be gradual. A footnote in the text of her speech stated that when the Fed’s policy rate is so close to zero uncertainty and greater downside risk call for greater gradualism. The Fed’s language evolution from gradual to greater gradualism is a form of Fed speak. Fed speak is the language central bankers use to contain excess market reaction. Fed speak is an essential tool that the Fed uses to influence market behavior, and in turn achieve its primary objectives of full employment and stable prices. If you are asking yourself what this mumbo-jumbo actually means, the answer in my opinion is that interest rates will be moving up very slowly, if at all.

In the chart below are the Fed’s 2016 – 2018 projections for GDP growth, unemployment assumptions and inflation estimates. Take a look at the GDP growth forecast for 2016 and beyond; it starts at 2.2% and wanes to 2.0%. When the economy just sputters along it becomes difficult for corporations to increase profits. The market needs higher demand for its goods and services. The way to increase demand is for companies to innovate new products and to provide better services for consumers. With increased demand comes higher prices, followed by higher wages, followed by consumer spending - a virtuous cycle.

Variable	*Median Projection*			
	2016	2017	2018	Longer run
Change in real GDP	2.2	2.1	2.0	2
Unemployment rate	4.7	4.6	4.5	4.8
PCE inflation	1.2	1.9	2.0	2

“Sell in May and walk away” is an old adage that alerts investors to the woes of market action during the worst six month period. Sam Stovall, in his book *The Seven Rules of Wall Street,* informs stock market participants that since 1945 the worst period to own stocks has been May through October. The S&P 500 posted an average return of 1.3% for this six month span; that compares to a 7.0% average return for the next six months. Recently, I was asked how the market performed in June, July and August for the last 10 years. The average return for the past decade in the June through August period was -0.2%. Considering the market had 24 occurrences of 1% or more of intraday volatility in 2016, -0.2% looks less than desirable. Mark Twain quoted, “History doesn’t repeat itself, but it does rhyme.” In closing, I remain bullish on the stock market, just less so.



Respectfully,

William "Chip" Corley, MBA, RFC