

INVESTMENT COMMITTEE MARKET COMMENTARY

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U.S. EQUITIES

U.S. stocks suffered their largest weekly drops since late April, as the upcoming "Brexit" vote in the U.K. and persistent worries about the Federal Reserve's reluctance to raise interest rates weighed on the markets.

a) ***Dow Jones -1.00% MTD -0.50% YTD +2.82%*** b) ***S&P 500 -1.12% MTD -1.11% YTD +2.42%***
 c) ***Russell 2000 -1.61% MTD -0.79% YTD +1.47%***

Drivers: I) ***The Federal Reserve last Wednesday left interest rates unchanged and signaled it is likely to take an even slower approach in raising the cost of borrowing against a backdrop of slower U.S. job creation and new worries about economic events abroad.*** The Fed still believe the economy is on solid ground. They lowered its estimate of U.S. growth in 2016 to 2% from 2.2%, but left its long-run forecast intact. Fed officials also expect the labor market to continue to improve, with the unemployment rate remaining below 5% for the next three years.

II) ***Chairwomen Yellen expressed concern after the Fed meeting about the low level of U.S. business investment and said "vulnerabilities in the global economy remain,"*** such as the pending U.K. vote known as Brexit. The renewed sense of caution was evident in the Fed's so-called "dot plot." According to the new dot plot, six of 17 members now expect only one interest rate hike this year. That is up from only one official in March.

III) ***Sales at U.S. retailers rose a solid 0.5% in May after an even larger gain in the prior month, suggesting consumers still feel confident enough in the economy to continue their usual spending habits*** despite a slowdown in hiring. Economists had forecast a 0.3% increase. The sales gains were widespread. Auto dealers, Internet retailers, clothing outlets, gas stations, sporting-goods stores and restaurants all saw a healthy rise in sales.

IV) ***Department stores are in a losing struggle to prevent even more sales from shifting to online rivals. Sales are down 4.4% through the first five months of 2016,*** compared to the same period a year earlier. By contrast, internet and mail-order companies whose business has shifted online have posted a 10% increase in sales through the early portion of 2016.

V) ***Equity prices in June are lower with Mid-Cap, Value, Utilities and Telecom leading equity price performance. The laggards for the month are Large-Cap and Growth Stocks along with Financials.***

Capitalization: ***Large Caps -1.09%*** (YTD +2.37%), ***Mid-Caps -0.75%*** (YTD +4.24%) and ***Small Caps -0.79%*** (YTD +1.47%). Style: ***Value +0.01%*** (YTD +9.23%) and ***Growth -1.39%*** (YTD +3.29%). Industry Groups (Leaders): ***Utilities +3.67%*** (YTD +18.58%), ***Telecommunication +4.26%*** (YTD +18.94%), ***Energy +0.64%*** (YTD +12.37%), ***Consumer Staples +0.53%*** (YTD +6.22%), ***Industrials +0.18%*** (YTD +6.19%) and ***Technology -2.21%*** (YTD +1.42%). (Laggards): ***Financial Services -4.23%*** (YTD -4.14%), ***Consumer Discretionary -2.20%*** (YTD -3.00%), ***Healthcare -1.42%*** (YTD -1.87) and ***Information Technology -2.85%*** (YTD -0.11%).

EUROPEAN EQUITIES

The MSCI Europe index was down last week falling -2.57%. European fell last week, but rallied on Friday as investors reassessed by likelihood of a "Brexit" in the wake of the assassination of a British lawmaker. Year to date the MSCI Europe Index is down -5.29% (MTD -4.91%).

Drivers: I) ***Fears of a U.K. exit from the European Union increased last Thursday, with two respected pollsters showing a solid swing in favor of the "leave" campaign.*** The Ipsos-Mori/Evening Standard survey put support for a Brexit ahead by six points, with 53% wanting to leave the EU and 47% wanting to remain. The poll excluded the do not knows. It is the first time the Ipsos-Mori telephone survey has shown a lead for the "leave" camp.

II) ***The Bank of England last Thursday kept its key interest rate at a record low of 0.5% and made no changes to its 375-billion-pound (\$530 billion) asset-purchase program.*** All nine rate-setting policy makers voted to hold rate unchanged. The decision marked the last before the June 23 referendum in the U.K. on whether the country should stay or exit the European Union. "As the Committee set out last month, the most significant risks to the MPC's forecast concern the referendum.

III) *Performance of European Indexes for the week, month-to-date and year-to-date. The MSCI Europe Index fell -2.57% for the week (MTD -4.91% YTD -5.29%).*

ASIAN EQUITIES

Asian equity markets equity markets were down for the week due to worries about the upcoming U.K. vote on EU membership, as well as the continued strength of the Japanese Yen which hit a two year high against the U.S. dollar. The Dow Jones Asia Pacific Index was down -2.85% for the week, (MTD -1.88), (YTD -3.57%).

Drivers: I) *The Bank of Japan's monetary policy remained unchanged last week, despite a surging yen and low inflation, deciding to wait until after the results of a British referendum next week that could roil global markets. The central bank's decision to maintain its negative interest rate comes despite growing skepticism about the effectiveness of its policies in ending Japan's long cycle of sub-par growth and bouts of deflation.*

II) *MSCI announced last Wednesday that it would for a third time withhold mainland China A shares from its benchmarks, including the widely tracked MSCI Emerging Markets Index. About \$1.5 trillion in assets follow this index, according to MSCI, and with some of that being from passively-managed funds, analysts had expected that billions of dollars would automatically enter China's borders had MSCI said yes.*

III) *Performance of Asian Indexes for the week, month-to-date and year-to-date. The Nikkei was lower by -6.03% (MTD -9.49% YTD -18.04%), the Hang Seng Index declined by -4.15% (MTD -3.00% YTD -7.96%) and the Shanghai Composite fell by -1.44% (MTD -1.08% YTD -18.48%).*

FIXED INCOME

Treasury yields fell for the third straight week recent as investors await the outcome next week's U.K. vote on whether to leave the European Union.

Performance: I) *The 10-year Treasury yield was lower last week ending at 1.611% down from 1.642%. The 30-year yield fell last week falling from 2.455% to 2.423%.*

II) *The yield on the 30-year Swiss bond became the longest-dated maturity to fall into negative territory last Thursday, as government bond prices continued to rally due to rising concerns over the impending vote in the U.K. on whether or remain or leave the European Union. The 30-year yield declined 5.5 basis points to negative 0.055% last Thursday.*

III) *Performance for the week, month-to-date and year-to-date. Barclays US Aggregate Bond was up +0.05% last week, MTD +1.04% and YTD +4.53%. The Barclays US MBS TR rose by +0.05% last week, MTD +0.44% and YTD +2.72%. The Barclay's US Corporate HY Index declined by -0.72%, MTD +0.21% and YTD +8.34%.*

COMMODITIES

The DJ Commodity Index was lower last week falling from 275.77 to 274.86 and is up month to date +3.64% (YTD +13.71%) prompted by the fall in oil which was hampered by the potential of increased production.

Performance: I) *The price of oil suffered a weekly loss, the largest since early May, on signs of a potential recovery in crude production. For the week oil declined -1.27% from \$48.88 to \$48.26 per barrel (MTD -1.71% YTD +18.54%).*

II) *The ICE USD Index, a gauge of the greenback's movement against six other major currencies, was negative falling -0.55% from 94.66 to 94.14 for the week (MTD -1.73% YTD -4.61%). The USD fell last week as investors have pulled back their expectations for an early rate increase by the U.S. Fed. For the week the Yen strengthened climbing from ¥106.97 to ¥ 104.16 and the Euro rose from 1.1251 to 1.1276 against the USD.*

III) *Gold climbed 1.98% for the week ahead of next week's U.K. referendum on whether to leave or stay in the European Union. For the week gold was higher by +1.98% rising from \$1276.3 to \$1301.60 (MTD +6.90% YTD 22.62%).*

HEDGE FUNDS

Hedge funds returns in June are mixed, with core strategies Event Driven, Distressed, Macro and Relative Value all in positive territory while Equity Hedge is down for the month.

Performance:

- I) **The HFRX Global Hedge Fund Index is lower at -0.11% MTD and -1.13% YTD.**
- II) **Equity Hedge is down at -1.64% MTD and has fallen -4.09% YTD.**
- III) **Event Driven is up MTD +0.75% and is up YTD +2.62%.**
- IV) **Distressed Debt is higher at +0.80% MTD and is positive YTD +6.31%**
- V) **Macro/CTA has risen by +0.50% MTD and is down -0.82% YTD.**
- VI) **Relative Value Arbitrage is positive at +0.26% and is down -1.76% YTD.**

ECONOMIC DATA WATCH AND MARKET OUTLOOK

Heading into next week, markets will be greatly affected by the fear surrounding the risk of the U.K. leaving the European Union. Adding to the "Brexit" fears was the Federal Reserve's decision this week to cut U.S. growth expectations and its outlook for interest rates. While this shifts any near-term rate increase into the future, it shows that policy makers do not expect growth to break out to the upside any time soon.

Market uncertainty has prompted investors to raise cash positions to 5.7%, the highest level since November 2001, as fund managers have become increasingly bearish, according to a Bank of America Merrill Lynch survey. **Historically, when the average cash level is above 4.5%, this tends to serve as a contrarian buy signal for stocks** whereas when it drops below 3.5%, it is a contrarian sell sign.

On the economic data front, Federal Reserve Chairwoman Janet Yellen travels to Capitol Hill for her semiannual congressional testimony, after the U.S. central bank's decision to hold interest rates unchanged. She will appear on Tuesday before the Senate Banking Committee and testify Wednesday before the House Financial Services Committee. In conjunction with her testimony, the Fed will release its latest Monetary Policy Report.

The National Association of Realtors on Wednesday will release its monthly report on existing-home sales (expected to rise from 5.45 to 5.60 million units). The Commerce Department on Thursday will report on sales of newly built homes (projected to drop from 619,000 to 560,000), which account for a much smaller portion of the U.S. market. Sales of both new- and previously owned homes rose in April from the prior month.

Weak business investment remains a drag to the U.S. economy and major concern for Fed policy makers. Next Friday the May durable-goods report from the Commerce Department will be released (estimated to decline from 3.40% to -0.70%), and will be subject to close scrutiny. A proxy for business spending on new equipment, new orders for nondefense capital goods excluding aircraft, declined on a year-over-year basis in 15 of the past 16 months.

An increase in consumer spending has raised expectations for U.S. economic growth in the current quarter. Whether households will keep it up remains an open question. **The University of Michigan on Friday will release its final consumer-sentiment report for June (expected to remain unchanged at 94.3);** an early reading found confidence in current economic conditions rose to the highest level in 11 years but that expectations for the future deteriorated.