signature
FAMILY WEALTH ADVISORS

TO	Signature Clients
FROM	Signature Investment Committee
DATE	May 4, 2016
RE	First Quarter 2016 Investment Review

Market Observations

David Jallits, Chief Investment Officer

"Some people see the glass as half full. Others see it as half empty.

I see a glass that is twice as big as it needs to be."

George Carlin (1937-2008)

So is the market's glass half full or half empty? As of the end of the first quarter, global equity markets are sitting almost exactly where they started the year. In the United States, a fall of more than 10% in the first six weeks of 2016 was followed by a rapid recovery of more than 13%, allowing the market to finish up slightly for the quarter. Similar V- shaped moves can be found in multiple volatility measures, inflation forecasts, bond yields, and commodity prices. In short, the world experienced a scare about global recession and deflation and then recovered from it – all in the space of three months. China, as always, found itself in the middle of the maelstrom by allowing its currency to weaken and then forcing it higher through central bank intervention. Although the markets may seem to have righted themselves, it can still be instructive to attempt to ascertain what exactly happened; and what, if anything, fundamental has truly changed?

First, crude oil prices have risen roughly 50% from their January low while the U.S. dollar has broadly weakened. Some of this price movement can be laid at the feet of markets that overshot in the direction of lower oil prices and a stronger U.S. dollar throughout 2015. Some of this price movement, as well, must be laid at the feet of the Federal Reserve, as they have once again told the markets to ignore their forecasts for higher domestic policy rates - if it meant those higher rates would unsettle the financial markets along the way. As the Fed walked back its forecasts for higher rates, commodity and currency prices reversed course appropriately. This in turn has relieved some fears over bankruptcies in the energy and emerging markets sectors as well as reducing a bit of the headwind for domestic equity earnings. Additionally, the move by China to force its currency higher against the U.S. dollar has allayed fears of a currency war breaking out into the open.

Elsewhere in central bank-land, Japan and Europe have both moved their policy rates deeper into negative territory with the European Central Bank now paying banks to borrow funds from them as long as they loan it into the "real economy." Unfortunately, while the central banks have potentially created more loanable funds, we will have to wait and see if there is demand to borrow the money. This "micro-allocation" policy of central banks may be the focus of one of our future quarterly notes as monetary policy becomes more

and more directive over time while fiscal policy – whose job it is to target specific outcomes (infrastructure, tax incentives) remains inert globally.

Some other items to notice include gold, having its best quarter in 30 years, being up over 15% and Treasury Inflation Protected Securities having roared back to life as inflation forecasts in the U.S. have gone from predicting the Fed would never get to its 2% target to thinking they may be there by the end of this year. Core inflation (excluding food and energy) is running at 2.3% - its highest level since September of 2008. If sustained, this is clear justification for the Fed to raise rates over their current level of between .25 and .50. Equity markets meanwhile, while back from the edge, still have disappointing profits expectations. Corporate profits in the fourth quarter of 2015 fell 11.5%, largely due to the energy sector, but they also declined 3.1% over all of 2015, the largest decline since 2008. Pressure on corporate profits may be tempered by a lower U.S. dollar and higher oil prices, if they are sustained, but we are still in an environment of profit margins being squeezed as growth and productivity remain tepid while inflation and wages rise in tandem.

While we saw the financial cracks open wide in the beginning of 2016 and then begin to close, they are still deep. Central banks remain active and investors remain nervous about how it all ends. The U.S. equity market seems fully priced and bond yields are still distorted by central bank actions. This dance will only go on for as long as confidence in the power of the central banks remains. While we would all prefer to see strong, organic growth ride to the rescue, that seems unlikely until the global debt deleveraging cycle has run its course. In the meantime, targeted fiscal policies and a rational regulatory environment would be additive to both domestic and global growth but those levers are held hostage to the upcoming elections in the U.S. and Europe. Stay tuned.

The following commentary encompasses SFM Capital Markets, SFM Global Strategies QP, SFM Opportunities, SFM Private Equity I, SFM Opportunities III, SFM Opportunities IV, SFM Opportunities V, Yield Pool and other private partnerships. Although these investments do not make up anyone's entire portfolio, the intent in consolidating the information is to give you a broader understanding of the holdings in your portfolio and how they complement and diversify your investment returns.