



A MCCOLL BROS. LOCKWOOD COMPANY

The Intelligent Investor—July 2016

Quick Market Update:

Like many of you, I had a wonderful time celebrating the Fourth of July holiday weekend, in fact it was our first with our new daughter, Olivia, who actually slept through all of the fireworks (Mom and Dad did a silent high five to that). When I was growing up, the Fourth seemed mostly about barbeques, friends, hanging out at the pool, and fireworks.

Through my adult years, however, I've come to better appreciate what Independence Day really means. We have a degree of freedom in our nation that few today and even fewer throughout recorded history have enjoyed. And that freedom came (and still comes) at a steep price.

We have the freedom to speak our mind, the freedom of religion, the freedom to assemble, and the freedom to question our government. In addition, we have the freedom to choose our own leaders – from the local city council to the president of the United States.

Some of us are looking forward to the upcoming election and are excited about the prospect that a woman may lead the greatest nation that has ever graced the face of the Earth. Others may be eager to cast their vote for a political newcomer, hoping to shake things up in Washington. But I am also a realist and am painfully aware that many folks aren't very enthusiastic about the choices that *We the People* have.

It's not always perfect, but if you really reflect on it, we, as a nation, govern ourselves. And this grand experiment in democracy has been exported around the world in many forms.

Political Tremors—Brexit

This leads us to Europe--and the United Kingdom in particular. On June 23, the UK voted in a nonbinding referendum to exit the 28-nation economic and political bloc called the European Union. Though "Brexit" was chosen by a narrow margin, the people had spoken.

Given it's a nonbinding referendum, British lawmakers could ignore the results. While there has been some talk that a UK exit will never happen, at this juncture, it doesn't seem likely the referendum will be ignored. Nonetheless, a victory by the "Leave" camp wasn't supposed to happen. While the vote was expected to be close, pollsters, analysts, and even the bookies who took bets all projected "Remain" would squeak through with a win. In advance of the vote, stocks rallied in anticipation "Leave" would go down to defeat.

Whether good or bad, continuity usually benefits markets because it provides certainty.

Recall from some of my past newsletters that markets hate *heightened* uncertainty. More accurately, short-term traders dislike added uncertainty and are much quicker to hit the sell button than longer term investors, who are more tolerant of disappointments. Why might this be viewed as heightened uncertainty? Well, we're in uncharted waters. No nation has ever asked to leave the EU.

Could Brexit fuel other separatist movements and create additional economic uncertainty in Europe? Might we see the euro currency, which is shared by 19 nations, begin to unravel? How might this pressure an already fragile European banking system? And will the dollar begin to strengthen as global investors see the relative safety of the U.S. as a shelter from the stormy global environment?

The Positives at Home

Many of the themes that have kept stocks near highs continued to play out over the quarter that just ended. On the plus side, U.S. economic growth appears to have accelerated in Q2 and interest rates remain low. While Brexit may muddy the picture, earnings are forecast to begin rising again in Q3 (Thomson Reuters).

Meanwhile, the increase in oil prices has not only reduced the strong headwinds in the troubled energy sector, but it has reversed the surge in yields among junk bonds. Still, a fill-up at the gas station remains quite reasonable.

Moreover, the dollar's recent stability reduces the drag on revenues from firms that do a significant amount of business overseas. When U.S. companies sell goods around the globe, they must translate those sales back into stronger dollars. A rising dollar is a gift for Americans traveling overseas, but it puts a dent in the bottom line of multinationals.

Table 1: Key Index Returns

Investors cannot invest directly in an index

	MTD %	YTD %	3-year* %
Dow Jones Industrial Average	+0.8	+2.9	+6.3
NASDAQ Composite	-2.1	-3.3	+12.5
S&P 500 Index	+0.1	+2.7	+9.3
Russell 2000 Index	-0.2	+1.4	+5.6
MSCI World ex-USA**	-3.3	-4.8	-0.8
MSCI Emerging Markets**	+3.3	+5.0	-3.9

Source: Wall Street Journal, MSCI.com

MTD returns: May 31, 2016—Jun 30, 2016

YTD returns: December 31, 2015—Jun 30, 2016

*Annualized

**in US dollars

What's an Investor to Do?

Control what you can control – the investment plan – and be very careful about making a rash decision based on an emotional selloff. Stocks took a beating in the wake of the Brexit vote but quickly recovered nearly all of their losses by the end of June.

I understand that most investors don't fully understand the impact of what just happened in Europe in relation to their investments. Honestly, many analysts would concede there are unknowns.

My goal, however, is to keep you focused on your financial goals and objectives. Emotionally based decisions rarely work out in your favor.

You may recall that my April letter touched on how markets price stocks.

Whether large or small, whether highly sophisticated or simply a novice, investors price stocks through their collective buy and sell decisions. When new information is disseminated in the marketplace, stocks may react either positively or negatively, depending on how the information is viewed.

By itself, the UK's economy won't send the U.S. economy into a recession.

But Brexit creates a new level of uncertainty and risk. However imperfectly, investors attempt to discount the event, pricing in how it may affect the U.S. economy and corporate profits.

If you ever have questions or concerns, or just want to talk, my team and I are always available.

Bottom Line

Democracies can sometimes be messy. What just happened in the UK and the gridlock in Washington are just a couple of examples.

I believe Winston Churchill described it well when he said, “Democracy is the worst form of government, except for all the others.”

While we do not know where the waves of populism that are swelling in the U.S. and Europe may take us, they represent the will of free citizens. Democratic freedoms enable the ordinary to do the extraordinary; to innovate, create wealth and fuel new economic growth. True, free elections aren’t always neat and tidy, but history strongly suggests they are a vital ingredient for long-term economic success.

I hope you’ve found this review to be educational and helpful. As I always emphasize, as your trusted advisor, my job is you!

Thank you very much for the trust and confidence you’ve placed in my team and my firm, and as always we take our stewardship role very seriously, and are our honored by the responsibility you have entrusted us with.

Luther A. Lockwood

Luther A. Lockwood II
Managing Principal
Luther.lockwood@mbl-advisors.com

David B. Miller

David B. Miller
Managing Director
David.miller@mbl-advisors.com