FAIRPORT ASSET MANAGEMENT
A WEALTHTRUST COMPANY

Fairport Perspectives

June 24, 2016

A Message to Our Clients from John M. Silvis, CFA | Chief Investment Officer

Markets around the world are reacting to the vote in the U.K. to leave the European Union. With the votes officially tallied, 51.9% of the U.K. voters elected to "Leave the European Union" versus 48.1% who voted to "Remain a member of the European Union." While events are certainly fluid at this time, we wanted to share our current thoughts.

The polls got it wrong. Most public opinion polls over the last few days leading up to the vote were predicting a close race but with the "Remain" option prevailing on the 23rd. Bloomberg has been aggregating the results of all public polls taken over the last few weeks with emphasis on pollsters who have historically been the most accurate. As of the 22nd, they had 46.2% electing to remain versus 44.3% optioning to leave with just under 10% undecided (it's obvious now that the undecided broke heavily to the "leave" camp). While it was a close vote, market participants were expecting the populous to stay in the EU as markets (following the lead of the betting sights in England who were giving 80% odds) rallied though out the day yesterday (the 23rd). Evercore ISI, one of the leading macro-economic research firms, had 65% odds that the U.K. would "remain" in line with most of its competitors.

Expect market volatility. Global equity markets were not expecting an "exit" victory when markets closed on Thursday. As we can see by the negative reaction (markets in Asia and Europe are already seeing heavy losses and high volumes this morning) around the globe, it's going to take some time for the markets to re-calibrate to the economic reality that changes will be coming and with that an increased level of uncertainty. The next steps will be defined over the coming weeks/months, however the political fallout has begun with British Prime Minister Cameron announcing he will be resigning.

Fed is likely on hold for a while. The Fed mentioned recently that they were watching geopolitical events. It is likely they will be on hold for the near future as rates have all moved lower in the last few hours. The 10-year Treasury has moved down to 1.53% while the 10-year German Bund has firmly moved negative to -0.07% (you pay them to take your money...). The fed fund futures now do not have a hike factored in at all this year. This could be a knee jerk reaction today but the odds have definitely declined. We could see a hike later this year but would not be surprised if they remained on hold through this year.

Political fallout in Europe. Europe has been struggling with a rise in political populism and could see more surprises in the future. Spain's election on Sunday could be a good indication if this is a spreading concern. Other countries could see this as a blueprint for exit was well. Spain, Italy and France could see an increase in the "exit" dialogue with yesterday's results.

Dollar could reverse course. We have been of the belief that the U.S. Dollar would continue its decline which started in March of 2015. While one day does not make a trend, the Euro, the Yen and the British Pound have come under pressure resulting in a rise in the Dollar overnight. Should this continue, it could add pressure to corporate earnings (large multinational companies benefit from a weaker dollar) a few quarters down the road.

Remain cautious on International Equities. We remain underweight international equities relative to our benchmark the MSCI All Country Index which currently has 47% invested outside the U.S. It is too early to measure the economic fallout in the EU. Keep in mind this could be a two year process if taken to the likely conclusion of the U.K. ultimately leaving the EU. The market usually overreact to events like we are seeing today and the long term prospect for Europe and the U.K. are not as dire as it seems today. Opportunities will emerge as there is more clarity on the situation. Central banks around the global may announce further stimulus in the coming days which could be a catalyst down the road for global equity markets.

Remain constructive on U.S. equity markets. In spite of the reaction we will witness today, we still remain constructive on U.S. equity markets. In the short term, technical levels on the S&P 500 Index to watch are 2,020 (the 200 day moving average), 2,000 and 1,980. We still believe the bottom in earnings occurred last quarter and we should see better results in the coming months. Oil, while down today, has likely put in a bottom and energy companies will again add to earning going forward. With the Fed on hold and yields below 2%, we still prefer equities over bonds and maintain our overweight to stocks.

Longer term. Selling into equity market corrections has historically never been a good strategy for long term investors. Nothing yesterday/today has been a structural game changer. We continue to believe the U.S. economy is on firm ground and the threat, although slightly elevated, of a global slowdown or recession is still relatively low. Since 1950, returns for rolling 5- and 10-year periods for the S&P 500 Index have been overwhelmingly positive and have never been negative for the 20-year time period.

We will continue to share our thoughts as events unfold. As always, please feel free to contact a member of the Fairport team if you have additional questions, comments or concerns.

Confident navigation for high net worth clients.

1350 Euclid Avenue, Suite 400 Cleveland, Ohio 44115-1833 PHONE 216-431-3000 TOLL FREE 800-2227459 FAX 216-431-3681 WEB www.FairportAsset.com