The Lam Group

Investment Management

On June 23rd, the U.K. surprised the world and voted to withdraw ("Brexit") from the European Union (EU). While this is a significant economic and political event for the U.K., the economic ramifications for the rest of the world, if any, are still not clear. The abruptness of the vote notwithstanding, the actual process of the U.K. detaching itself from the EU will likely be slow and deliberate (if it happens at all) with the required negotiations of new treaties on trade, labor mobility, regulations and immigration taking several years to complete.

The Brexit was the unexpected news of 2Q 2016 which caused the performance of non-US developed market stocks to turn negative for the year. However these declines were more than offset by strong performances by the world's bond, global real estate, and domestic and emerging market stock markets. In the first half of 2016, performance contributions came from a broad range of asset classes, providing a welcome reminder of the importance of disciplined portfolio diversification. 2Q 2016 was led by commodities which were up +12.78% (+13.25% YTD).

It is worth noting that for 2016 YTD fixed income markets outperformed their corresponding stock markets globally. This is especially noteworthy as 2016 began with market pundits proclaiming the widespread certainty of the inherent doom in the US bond market (which has been an unfulfilled prediction for the last several years) and with the forecast of multiple interest rate increases by the Federal Reserve.

Table 1: Periodic Asset Class Returns as of 6/30/16	A	B	C	D	E	F	G
EQUITY ASSET CLASSES	**2Q 2016**	**YTD 2016**	**12 Months**	**3 Years**	**5 Years***	**10 Years***	**15 Years***
S&P 500 Index - *Domestic Large Cap Stocks*	+ 2.46%	+ 3.84%	+ 3.99%	+11.66%	+ 12.10%	+ 7.42%	+ 5.76%
Russell 2000 Index - *Domestic Small Cap Stocks*	+ 3.79%	+ 2.22%	- 6.73%	+ 7.09%	+ 8.35%	+ 6.20%	+ 6.96%
MSCI EAFE Index - *International Large Cap Stocks*	- 1.46%	- 4.42%	-10.16%	+ 2.06%	+ 1.68%	+ 1.58%	+ 4.32%
MSCI EAFE SC Index - *International Small Cap Stocks*	- 2.60%	- 3.18%	- 3.67%	+ 7.26%	+ 4.84%	+ 3.57%	+ 8.32%
MSCI EM Index - *Emerging Markets Stocks*	+ 0.66%	+ 6.41%	-12.05%	- 1.56%	- 3.78%	+ 3.54%	+ 9.12%
DJ US Select REIT Index - *Domestic Real Estate*	+ 5.42%	+10.82%	+22.85%	+13.55%	+12.30%	+ 6.86%	+11.12%
S&P Global (ex-US) REIT Index - *International Real Estate*	+ 1.31%	+10.02%	+ 7.25%	+ 6.96%	+ 5.91%	+ 3.31%	+10.19%
FIXED INCOME ASSET CLASSES	**2Q 2016**	**YTD 2016**	**12 Months**	**3 Years**	**5 Years***	**10 Years***	**15 Years***
BarCap Aggregate Bond Index - *US High-Grade Bonds*	+ 2.21%	+ 5.31%	+ 6.00%	+ 4.06%	+ 3.76%	+ 5.13%	+ 5.08%
BarCap High-Yield Bond Index - *US High-Yield Bonds*	+ 5.52%	+ 9.06%	+ 1.62%	+ 4.18%	+ 5.84%	+ 7.56%	+ 7.93%
BarCap TIPS Index - *US TIPS*	+ 1.71%	+ 6.24%	+ 4.35%	+ 2.31%	+ 2.63%	+ 4.76%	+ 5.50%
Bloomberg Commodities Index - *Commodities*	+12.78%	+13.25%	-13.32%	-10.55%	-10.82%	- 5.59%	+ 0.45%
Citigroup Non-$ World Govt Bond Index - *Non-$ Bonds*	+ 4.04%	+13.50%	+13.85%	+ 2.36%	+ 0.31%	+ 3.97%	+ 5.81%
JPM EMBI Global Diversified Bond Index - *Emerging Markets Debt*	+ 5.02%	+10.31%	+ 9.79%	+ 7.20%	+ 6.45%	+ 7.97%	+ 9.16%

Sources: Morningstar, JP Morgan & Dimensional.

*annualized

Despite the current crisis of “Leave” leadership (which may cast doubt on how quickly, if at all, Article 50 will be invoked), it is likely other European countries are questioning the viability of the EU and the value of continued membership. While the market uncertainty introduced by Brexit brings into question global growth issues, it also makes central bank monetary policy more important (and perhaps more clear cut) in the near-term.

The Brexit vote may reflect dissatisfaction with the status quo and the rise of populist politicians is also being seen in other countries. In that vein, our own Presidential election may introduce additional uncertainty, and perhaps challenges, for the global markets.

With the recent volatility we have initiated some portfolio rebalancing (opportunistic increases to international stocks) and lengthened the duration of our bond exposures globally.

Overall, 2Q 2016 was not a bad quarter and we are pleased with our YTD results. The US Presidential election will soon be upon us. Global diversification and portfolio balance may be the best running mates.