## Dear Clients & Friends of Patriot Investment Management

Drama and market volatility reached new extremes during the first quarter of 2016, as the first ten days of January proved to be the worst ever on record for the Dow, dating back to 1897. The panicked sell-off was driven by a steep drop in oil prices and plummeting stock prices in China, rather than any change in fundamentals at home. This was then followed by a 5-week, 13% rebound, during which the markets erased January's losses and pushed into positive territory. Fears linger over China's slowing economy and global uncertainty in general, but the US economy showed its resiliency in weathering the storm.

US Economy:

US economic fundamentals remain strong despite all the news from abroad. At quarter-end, the unemployment rate stood at 5.0%, and consumer inflation was 0.9% in March, well below the Fed's long-term target rate of 2%. This ultra-low inflation environment has persisted, primarily because of the sharp drop in the global demand for oil. Coupled with an increased surplus, rival producers are unlikely to agree to cut production out of fear of losing market share to one another. The resulting drop in gas prices has benefited consumers, and demand for air travel is at its highest level in 5 years.

The Fed is unlikely to raise the Federal funds rate before December, due to continued global uncertainty, stimulus measures and growth prospects abroad, and low inflation at home. Jobless claims have dropped to a 42-year low, and as hiring strengthens, there is an uptick in personal income and consumer spending. Corporate profits have been less than stellar, but there are some indications in manufacturing and GDP growth that profits may improve when earnings season begins.

Global Markets:

In Europe, we can expect increased volatility ahead of the UK's European Union (EU) membership referendum in June, otherwise known in the headlines as Brexit. The likelihood of the UK exiting the EU is not very high, as many economists calculate the costs to the UK would greatly outweigh the benefits. If it were to happen, the economic ramifications would be largely contained to the UK.

While the drop in oil prices has helped to increase consumer spending, slowing growth in China and emerging economies in Asia have hampered European exports. Determined to keep up the momentum of their recovery, the European Central Bank (ECB) plans to continue it's quantitative easing program, in the form of lower rates, increased bond purchases and keeping borrowing costs low for banks.

Furthermore, both Europe and Japan have gone negative with their interest rates in a bold move to stimulate lending. By setting negative rates, lenders pay borrowers for the privilege of lending. Theoretically, banks would be more willing to lend to businesses and consumers, and would have a disincentive to hold large cash reserves with their respective government's central bank. While these new easing policies may help boost recovery efforts and stimulate equities, they also hurt banks' profit margins and increase volatility in global markets. The long-term impact of this policy is yet to be determined.

In Asia, China's slowing GDP growth continues as the country moves away from an economy driven predominately by manufacturing and investment towards one driven by the consumption of goods and services. While emerging markets are beginning to stabilize, poor earnings prospects, rising corporate debt, and China's growth prospects are keeping many investors away.

<u>In Summary:</u>

After a dramatic start to the New Year, markets have recovered from the sell-off, and are resuming a steady pace of modest growth. The US is faring better than other sectors of the global economy due to strong fundamentals at home. We at Patriot remain guardedly optimistic in our outlook for the year. Going forward, we are likely to see low, but positive returns and slow, steady growth in the US economy, as global uncertainty will continue to drive market volatility in 2016.

<u>2016 First Quarter Returns</u>

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|---|---|
| S&P 500 + dividends | 1.35% |
| Dow Jones Industrial | 1.49% |
| Russell 2000 | -1.52% |
| Emerging Markets | 5.37% |
| EAFE | -3.74% |
| Barclays Aggregate Bond Index | 3.03% |

Returns are price-only unless otherwise noted

10 year Bond yield as of 3/31/16 1.79%

| | |
|---|---|
| Inflation | 0.9% thru March 2016 |
| Unemployment | 5.0% in March 2016 |

## Thank You!

We value the confidence and trust you have placed with us, and we welcome your questions and comments. Our goal is to be our clients' trusted resource for all things financial.

Do you know someone who could benefit from our expertise? We appreciate your introductions and the opportunity to help your family, friends and colleagues meet their financial goals.