PATRIOT INVESTMENT MANAGEMENT

Dear Clients & Friends of Patriot Investment Management

Summer brought more drama and market volatility to global markets during the second quarter of 2016, as the surprising outcome of the Brexit vote sent markets tumbling. The Dow dropped 611 points the day following the vote, and Britain saw its largest one-day drop in the British pound to lows not seen in over three decades. By the quarter's end a week later, markets had recovered, and the Dow has resumed its push into record high territory. As of this writing, the Dow has just hit six consecutive all-time highs.

US Economy:

Overall, US fundamentals remain positive despite the headlines from abroad, and the likelihood of an economic slowdown is remote. Equity valuations are elevated as the stock market posts new record highs. An unusually weak earnings season was compounded by a strong dollar and low energy prices. The labor market continues to tighten and put upward pressure on wage inflation, which will further dampen corporate profit margins going forward.

The Fed is unlikely to raise the Federal funds rate before December, due to continued global uncertainty, low oil prices, the upcoming election and low inflation. Treasuries have maintained their global safe haven status, pushing yields lower. Personal income and consumer spending rose again in the second quarter, and low gas prices have benefited vacation travellers this summer.

Global Markets:

In Europe, the unexpected result of the Brexit vote for the UK to leave the EU, and the political fall-out that ensued, dominated headlines at quarter's end, and created a ripple effect of volatility felt around the globe as investors sought safe haven assets. The British pound dropped to a 31-year low against the US dollar, posting its worst one-day decline on record. The economic outcome of the vote is mixed and uncertain, as the timeframe to exit the EU will take a minimum of two years, and the ramifications will be largely contained to the UK.

While the drop in oil prices has helped to increase consumer spending, slowing growth in China and moderate growth in emerging economies in Asia have continued to hamper European exports. In the wake of the Brexit vote, 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. Overshadowed by the volatility and uncertainty created by Brexit, the Eurozone continues to show positive, although more subdued, economic growth.

In Asia, Japan's experiment with negative rates has run afoul of the surprise Brexit vote, as a global flight to safety has strengthened the yen even further – the exact opposite of the hoped-for outcome. The Bank of Japan had hoped to weaken the yen in order to enhance export competiveness and spur inflation. Deflationary pressures and weak GDP are not likely to change any time soon, as their aging population continues to shrink. Structural reforms are needed before Japan's economy will see any lasting improvement.

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. Data is mixed – positive indicators are a recovery in residential housing and an orderly transition to the new economy, but large increases in public sector spending as private sector investment drops off, pockets of unemployment and an increase in bad debts still warrant investor caution.

<u>In Summary:</u>

After a volatile reaction to the surprise Brexit vote, markets have recovered from the sell-off, posting new record highs in the stock market, and the US economy is resuming a steady pace of modest growth. The US is faring better than other sectors of the global economy due to positive fundamentals at home. We at Patriot remain guardedly optimistic in our outlook for the year. For the second half of the year, we expect to see low, but positive returns and slow, steady growth in the US economy, as global uncertainty will continue to drive market volatility.

<u>2016 YTD Returns</u>

S&P 500 + dividends	3.84%
Dow Jones Industrial	2.89%
Russell 2000	2.22%
Emerging Markets	5.03%
EAFE	-4.42%
Barclays Aggregate Bond Index	5.31%

Returns are price-only unless otherwise noted

10 year Bond yield as of 6/30/16 1.49%

Inflation	1.0% thru June 2016
Unemployment	4.9% in June 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.