



Monthly Market Commentary June 2015

ECONOMY: Despite Greece & China, Reasons For Optimism

REASONS FOR US OPTIMISM

The rebound from a tepid first quarter is under way, and there are several reasons why second half growth could be an upside surprise.

1. **Housing:** The housing market continues to recover and pick up steam. Homebuilder confidence is the best since 2005, with housing starts and pending sales are well over a million annual rate. Household formation has surged and existing home sales are up over 9% year over year. Housing activity is a powerful economic tailwind.
2. **Consumer & Business Confidence:** The University of Michigan Consumer Confidence Index has risen nearly 70% following the collapse of Lehman Brothers in 2008. Both the ISM Manufacturing & Non-Manufacturing reports continue to demonstrate growth, specifically in new orders. Confident consumers and business leaders should strengthen a recovery.
3. **Wage Growth:** Wages are set to accelerate. Many states are increasing minimum wages, and a tighter labor market should push wages higher. Growth in average hourly earnings has been muted, but low inflation has improved real income.
4. **Consumer Spending:** Despite falling in June, consumer spending surged in May. Consumers spent more in Q2 than Q1 which should benefit growth. The savings from lower oil prices have yet to be reflected in consumer spending as well. Household net worth continues to recover, while consumers financial obligations continue to fall.
5. **Labor Market Recovery:** Job gains have exceeded 100,000 per month for 36 straight months, one of the best records ever. Weekly unemployment claims are below pre-recession levels. Future new hires may slow some as the labor market tightens, making wage gains more likely.
6. **Capital Spending:** S&P 500 companies still have record levels of cash on their balance sheets, and spending on buybacks and dividend payments has come at the expense of capex. Improved capital spending may result in faster sales and revenue growth.

FOCUS ON GREECE

Global stock markets rose and fell on the hopes that Greece would craft a last-minute deal with its creditors. As the month came to a close, it became apparent that Greece would become the first advanced economy to miss a payment to the International Monetary Fund (IMF). The Greek government temporarily closed its banks and stock market, and it imposed capital controls limiting withdrawals from ATMs. Europe's geopolitical dysfunction led to a spike in global stock market volatility, especially in Europe. Greece's future appeared to rest on a referendum set for July 5, in which Greek voters issued a resounding "NO" vote on the European Union's proposed bailout terms that were required for continued financial assistance. The range of possible but unpredictable outcomes has widened including Greece's exit from the Eurozone.

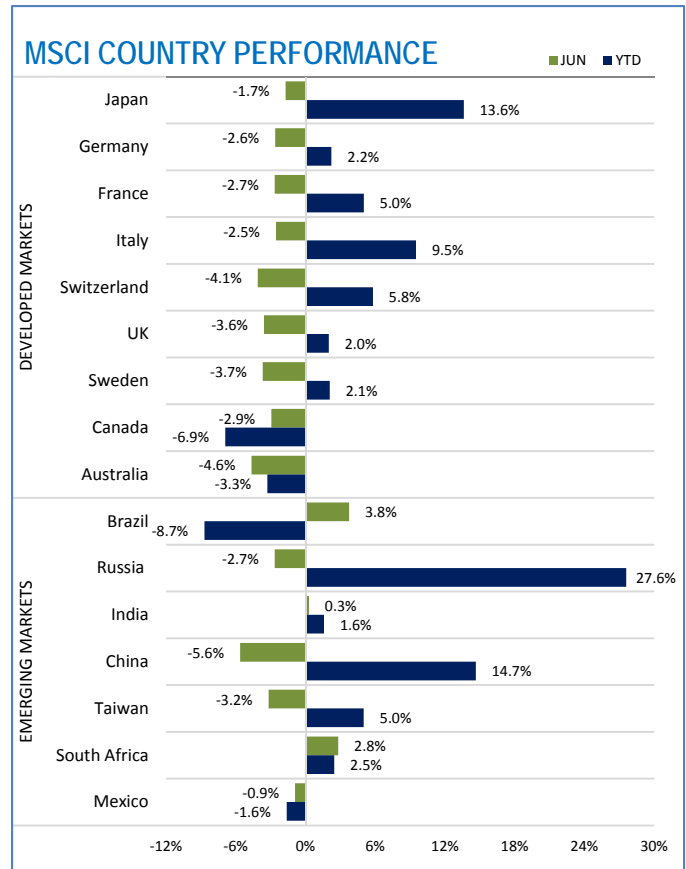
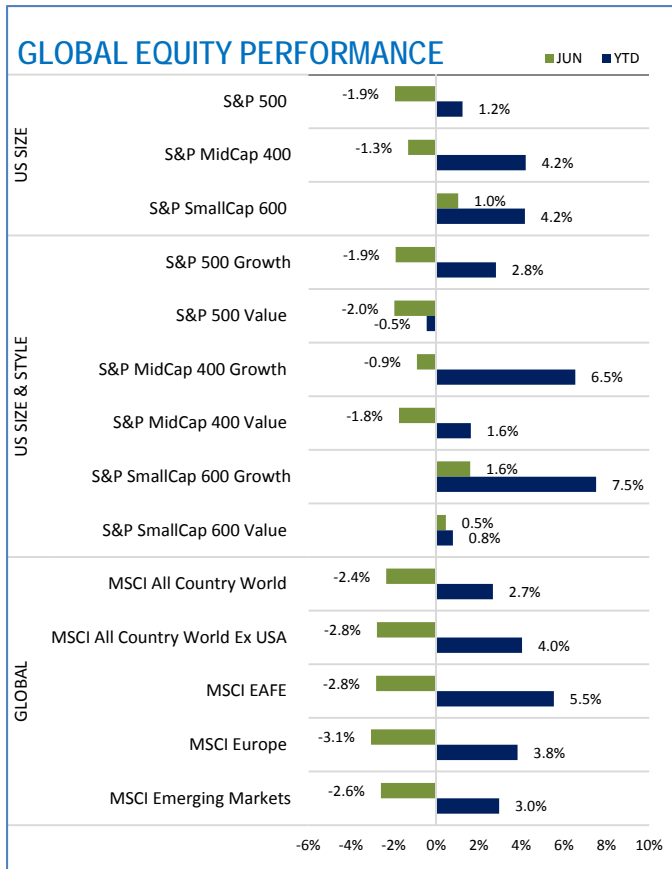
CONTAGION UNLIKELY

Financial contagion beyond Greece should be limited, despite an increase in volatility in global financial markets. The Eurozone economy, ex Greece, is in much better shape now. Spain & Portugal are growing, deflation fears are receding, and unemployment is falling. Lower oil prices, a weaker currency, cheap interest, and banks willing to lend are benefitting the region. Second, most Greek sovereign debt is in official hands. Approximately 10% or so is held by the private sector, so Euro-area banks are no longer heavily exposed, and the broader Eurozone is not imperiled. Third, Greece only accounts for about 2% of Eurozone GDP and exports to Greece from within the union are small.

CHINESE EQUITIES

The 28.6% crash in the Shanghai Composite and the 33.2% nosedive in the Shenzhen Composite from the June 12th peak through July 3rd represents markets that simply went too far too fast. Despite these heavy losses, the indices are still up 80% and 90% respectively over the trailing 1 year. Chinese officials unleashed a torrent of measures to support the market, including cuts to interest rates and reserve requirements, temporary trading halts, and sale restrictions.

GLOBAL EQUITIES: Nowhere To Hide



GREECE RATTLES U.S. EQUITIES

Worries over a Greek debt default and its broader implications for the European common currency and financial system took a toll on U.S. and other global markets in June. The S&P 500 fell 1.9% in June, while the S&P Small Cap 600 eked out a 1% gain.

GLOBAL EQUITIES HIT HARD

Every developed market in the MSCI EAFE Index except for Ireland declined in June amid renewed uncertainty about Greece's future in the Eurozone. Most developed markets in Europe and Asia declined more than 2%.

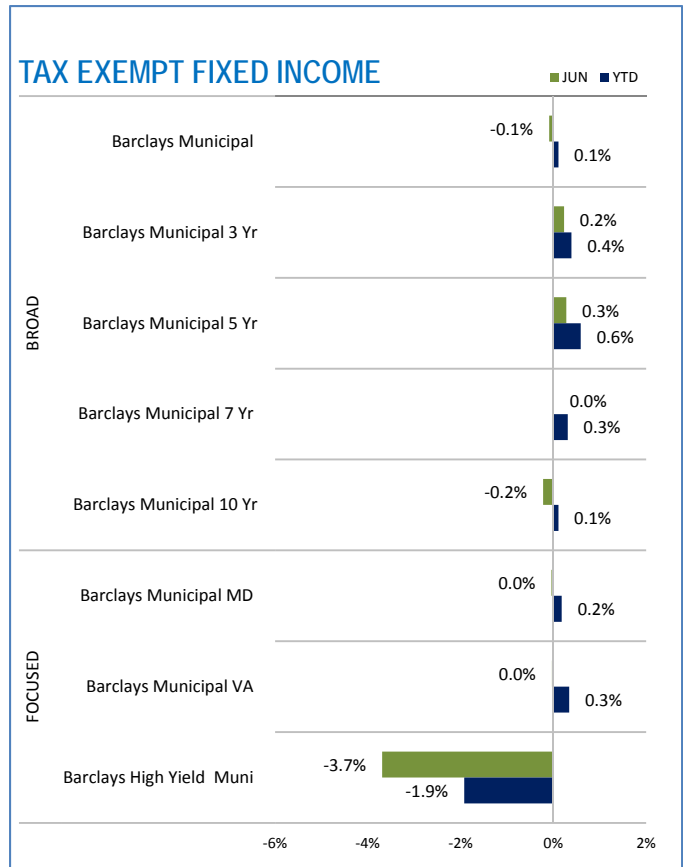
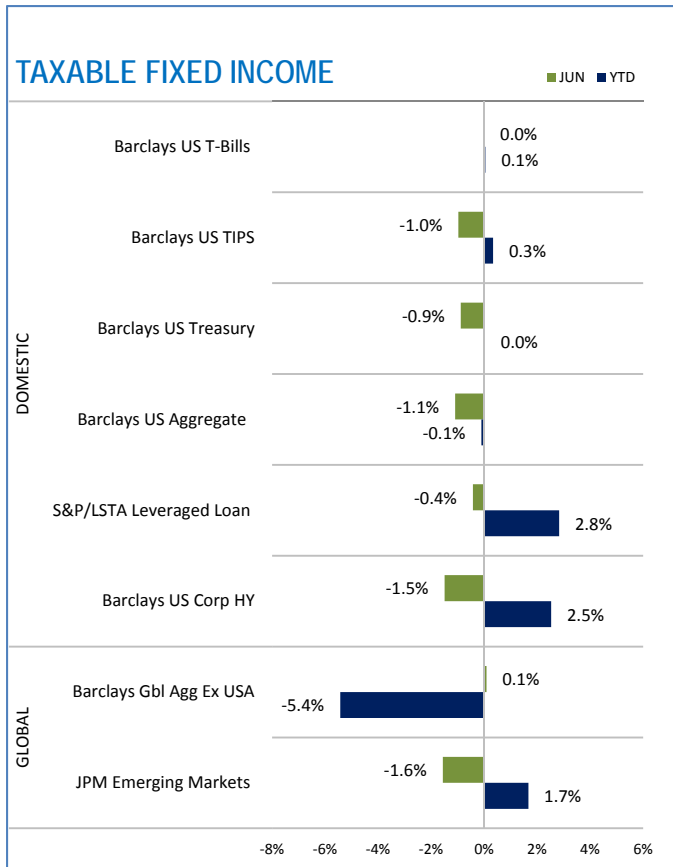
EMERGING MARKETS FOLLOW THE TREND

Performance across emerging markets was mixed, but the overall trend was lower. The MSCI Emerging Markets Index fell 2.6% in June. Markets in emerging Europe and Asia fell sharply, while the Latin America region advanced. The largest emerging markets performed in line with the broad emerging markets index. Brazil generated a solid gain, India was flat, and Russia & China both posted declines.

CHINA'S A SHARES CONTINUE TO FALL

China's restricted A-shares market (Shanghai) is up approximately 110% in the past 12 months, even after its nearly 8% fall in June. This market has been extremely volatile and late in the month fell 16.4% from its June 12 peak. The mainland A-shares are generally only available to Chinese citizens and qualified institutional investors.

FIXED INCOME: Hikes & Greece Impact Treasuries



VOLATILE MONTH FOR TREASURIES

U.S. Treasury prices were volatile in June as investors look towards rate increases from the Federal Reserve, while Greece moved closer to defaulting on its debts. These factors pushed and pulled the market in opposite directions. In the end, Treasury yields increased for the month as pressure from the impending Fed tightening cycle outweighed the “flight to quality” trade. The yield on the 10-year Treasury note increased to nearly 2.50%, the highest level in 2015, before falling somewhat by month’s end.

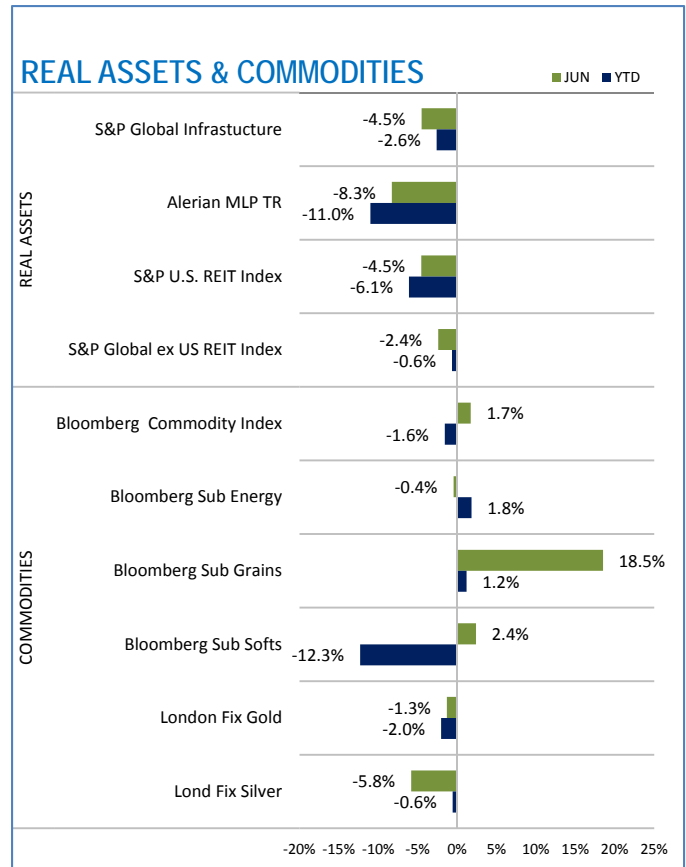
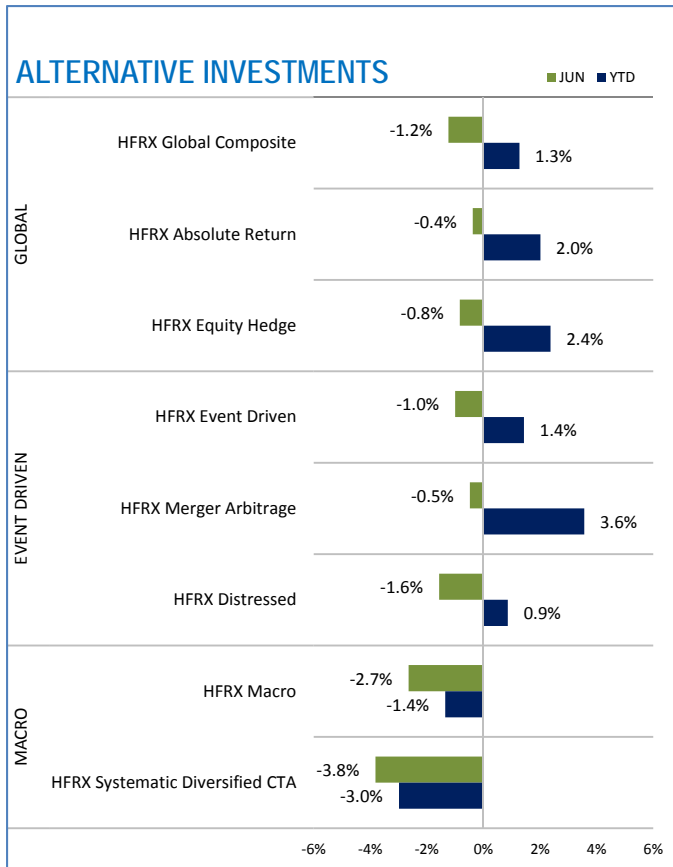
HIGH YIELD FALLS

High yield spreads widened in June, and the high yield market posted its worst monthly returns so far this year (-1.5%). Distressed debt and defaults continue to be a concern in the high yield market, specifically in the energy and mining sectors. According to JP Morgan, nearly \$26 billion of corporate debt is not trading at distressed levels (at or below 50% of par).

PUERTO RICO CAN'T PAY

At the end of the month, the governor of Puerto Rico announced that the U.S. territory will not be able to repay its debt obligations. The Puerto Rican government had previously maintained that it could pay its debt when due despite the island's many financial troubles. Prices of Puerto Rico's municipal bonds dropped steeply following the announcement. However, the overall municipal market only fell slightly for the month.

ALTERNATIVES: Big Gain in Grain Benefits Commodities



HEDGE FUNDS SUCCUMB TO VOLATILITY

Hedge funds followed the market trends downward for June amidst the increased volatility caused by both Greece and China. Macro and Commodity Trading Advisors (managed futures) led the declines, falling 2.7% and 3.8% respectively. This was the worst decline for the HFRX Systematic Diversified CTA Index since October 2011.

RATE HIKES IMPACTING REITS?

REIT returns lost ground in the first half of 2015, in part over expectations of the potential market impact of rising interest rates. Through the end of June, the S&P US REIT Index fell 6.1% while the S&P Global ex US REIT Index fell 0.6%. Both U.S. and global REITs are trailing equities year to date.

COMMODITIES STRONG IN JUNE & Q2

The Bloomberg Commodity Index gained 1.7% in June and 4.7% in Q2. Agriculture prices drove broad commodity benchmarks higher in June on the back of USDA reports that stockpiles were smaller than expected. Grains and Softs were the best performing sectors in June, up 18.5% and 2.4% respectively. For the month, 11 out of 22 index constituents traded higher.