Investment Overview

By Mac Johnston, chief investment officer
Pinnacle Investment Advisory

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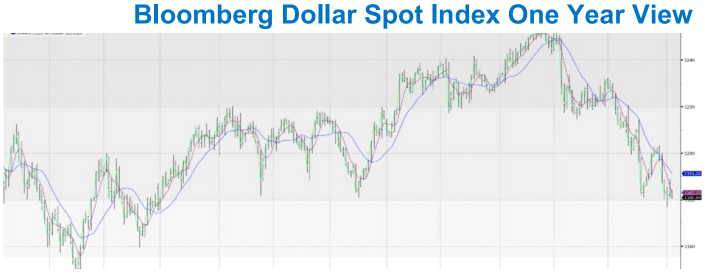
Review of 1Q 2016

During the first quarter of 2016 the S&P 500 rose 1.35 percent, the Dow was flat, and the Nasdaq was down 2.40 percent. The weak results for the first quarter were a result of weak fourth quarter GDP growth and worries over a slowdown in the Chinese economy. The S&P 500 bottomed on February 11, down 11 percent from year end, and rallied into the end of the quarter. One of the biggest developments during the quarter, was that the U.S. dollar weakened as the Euro and other currencies appreciated, thus driving oil prices from their low of $26/bbl to a high of $41/bbl. As you can see below the U.S. dollar has retraced its rally all the way back to June of 2015.

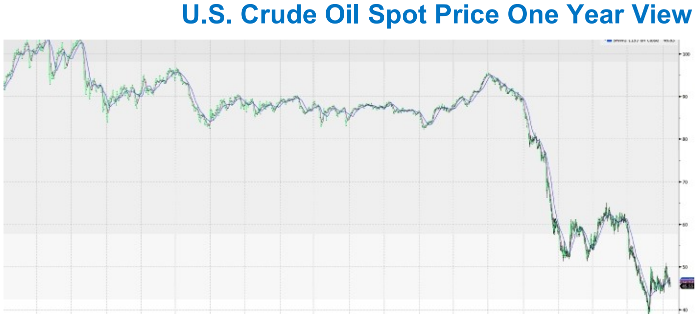
Bloomberg Dollar Spot Index One Year View



Source: Bloomberg

As you can see from the charts above and below, even though oil prices have rallied in the short term they have a long way to go before they approach $100/bbl again. However, when the U.S. dollar started to rally in June 2014, and oil prices began to plunge no one thought that a fall in oil prices would weaken GDP as much as it has. With this in mind, we have lowered our GDP estimates for 2016 and 2017. We expect GDP growth to continue in the 1.5 percent area for the next 2-3 quarters.

U.S. Crude Oil Spot Price One Year View



Source: Bloomberg

As mentioned, above the U.S. economy slowed during the second half of 2015; fourth quarter GDP was finally reported at 1.4 percent which is much weaker than the 3.9 percent and 2.0 percent reported for the second and third quarters, respectively. The fourth quarter miss was driven by an inventory building, slowing manufacturing data, and slowing corporate spending. The bright spot in the GDP report was residential housing starts which were helped by warm weather during the quarter.

U.S. GDP Estimates

'14 Act.	'15 Est	1Q '16E	2Q '16E	3Q '16E	4Q '16E	'16 Est.	'17 Est.
2.4%	2.4%	1.5%	1.5%	1.8%	1.7%	1.7%	1.6%

U.S. Housing Starts

'14 Act.	'15 Est.	1Q '16E	2Q '16E	3Q '16E	4Q '16E	'16 Est.	'17 Est.
1,001	1,107	1,129	1,164	1,164	1,196	1,180	1,261

In thousands seasonally adjusted

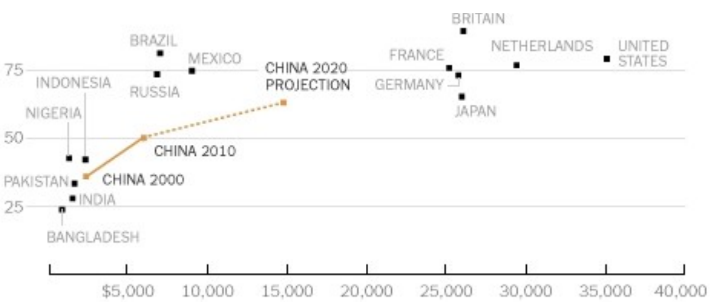
Source: Pinnacle Investment Advisory

In January the markets became concerned over falling GDP growth in China. For the last 10 years or more, the Chinese economy was focused on building out infrastructure and cities. During this process the government could control the GDP growth rate by the level of spending on various projects. As the urban cities and housing were finished, the Chinese government in 2007 began to move approximately 300MM citizens from their rural villages to the new urban cities. Along the way they leveled the rural villages to make the shift permanent. As these citizens became established in the new cities, the government expected the economy to move from a government controlled capital expenditures economy to a consumer economy driven by the new middle class occupants. The greatest risk with the strategy is that the GDP growth is now determined by these new consumers. If they lose their confidence in the government's plan and falter, their spending will decline thus slowing GDP growth. The transition has not been smooth; in July of 2015

Chinese corporate earnings began to slow and the stock market fell over 30 percent. The government's reaction was to eliminate short selling by threat of arrest, stopped initial public offerings and closed many stocks from trading for months. Eventually the Chinese government increased their borrowings from $7 trillion in 2007 to $28 trillion in 2015.

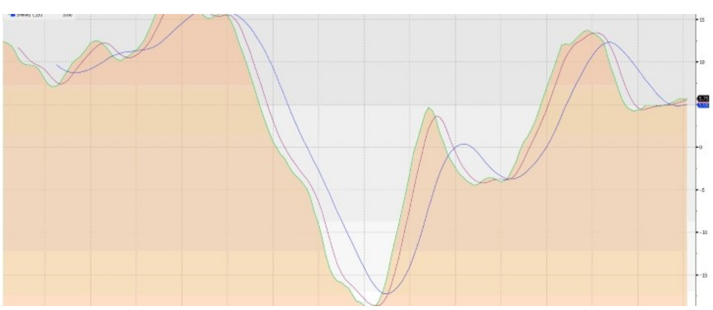
When you look at the Chinese economic situation it is troubling; China is the second largest trading partner of the U.S. so any shock to the Chinese economy creates waves for the U.S. economy. The goal of the Chinese is to increase economic growth by increasing per capita GDP. As you can see from the chart below through this process they have improved their citizens economic standing significantly during the last few years.

Projected Chinese GDP Per Capita Growth



Source: Organization for Economic Cooperation and Development

Case-Shiller Home Price Index 20 Fifteen Year View



Source: Bloomberg

Unemployment Rate

'14A	'15A	1Q '16E	2Q '16E	3Q '16E	4Q '16E	'16E	'17E
5.7%	5.0%	5.0%	4.8%	4.7%	4.7%	4.7%	4.7%

Economic Outlook

As we look at the U.S. equity markets for the balance of the year, we remain optimistic. While the S&P 500 earnings are only growing around 4-5 percent, we believe that a transition is underway in Europe which will positively affect U.S. investors. In January, when the European Central Bank announced that they were going to make overnight bank rates negative and announced a new round of quantitative easing, investors believed that the Euro would weaken allowing the Euro zone to increase exports. What really happened was that their stock market fell 15 percent in the first quarter and government spending rose as the different countries dealt with the Syrian refugee crisis and the Euro rose against most major currencies. Why? The U.S. dollar was too expensive for Europeans to make the conversion, banks were over capitalized, the Euro was undervalued and then the Euro rallied strongly surprising most investors. The effect of this is that the overpriced dollar started to fall as investors realized that the Euro was a more attractive value versus the pricy dollar.

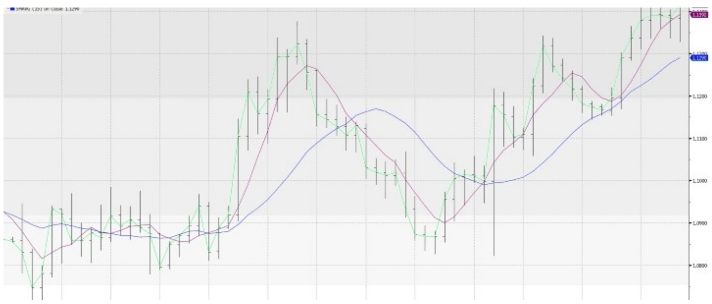
Based on the moves in the market year to date, we have considered our options and have come up with a "bull" and "bear" case for our clients in 2016.

Our "bull" case is for the dollar to continue to weaken, thus driving energy prices higher, creating higher core inflation, increasing U.S. GDP growth and allowing for the FOMC to raise Federal Funds rates more than once in 2016. With this scenario, we expect Chinese economic growth to accelerate. In our "bull case" S&P 500 earnings would accelerate allowing the Equity market to rise 8 percent-12 percent in 2016.

Our "bear" case is for the dollar to strengthen, driving energy prices lower, leading to slower and slower GDP growth allowing deflation to creep back into the picture and cause S&P 500 stocks to only rise 3 percent-5 percent. China economic slowdown would continue and the U.S. economy could enter a recession as early as 2018.

A depreciating U.S. dollar really is the most important goal for investors over the next couple of years. A weak dollar would cause GDP and S&P 500 earnings to grow by healing the distressed energy companies, would cause U.S. exports to grow more rapidly, and would create an accelerating U.S. GDP. Without a depreciating dollar, U.S. GDP would slowly grind to a halt with a recession likely in 2017-2018 and a continuation of low returns for investors.

Euro One Year View



Source: Bloomberg

Consumer Price Index Estimates

'14A	'15A	1Q '16E	2Q '16E	3Q '16E	4Q 2016E	'16E	'17E
1.6%	0.1%	1.1%	1.2%	1.5%	1.5%	1.2%	1.9%

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