Foresight
Capital Management Advisors, Inc.

NAPFA-REGISTERED FINANCIAL ADVISOR
AIF® Accredited Investment Fiduciary®

Newsletter 2Q 2016 and Market Summary

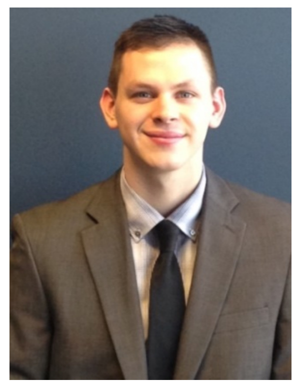
FCMA's Model Portfolios have gains through 2Q 2016 as follows:
Conservative Model +1.48%, Moderate Model +1.34%, and Aggressive Model +1.12%. The remainder of the year looks to be a smoother sail compared to the first half of the year!

<u>Foresight is pleased to introduce:</u>

Our Newest Employees!

Walter Dorosh- WMU Finance Intern

Justin Littleton-EMU Finance Intern



<u>Investment 101 and Beyond-Class</u>

Join us for our upcoming investment training course titled- "Investments 101 and Beyond". We are offering this course through the Community Education at Saline and our last session is August 4th beginning at 6:30 pm. Hopefully you can attend the last session! Bring a friend and see our new office space. This one night course will explain the many different types of investments in the market and how they work. We hope you will join us for an enjoyable interactive evening! Call to reserve your spot as seats are limited 1-877-429-4690.

<u>Low Cost Investing-The Costly Approach?</u>

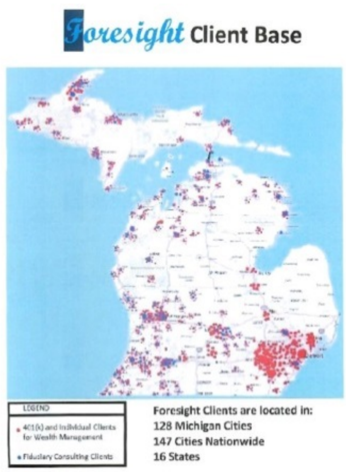
A new Foresight white paper, has been released in 2Q 2016, featuring our research titled "Low Cost Investing: The Costly Approach" We meet people every day that are so focused on only investing in low cost mutual funds that they are missing the real reason they should be investing, and that is to earn a return net of the cost! Our white paper explains that having tunnel vision on only cost can really cost you a lot of return. Please see our website or email us and we will send you this interesting research publication.

<u>HSAs at Foresight</u>

We now offer Health Savings Accounts which can be invested in our Model Portfolio strategies. Please call if you are interested in further details 734-429-4680.

<u>Lunch and Learn-Go To Meeting with Foresight</u>

Beginning in September 2016 we will be hosting a Go To Meeting Webinar monthly as a Lunch and Learn! The goal will be to teach a topic for 15 minutes and then allow questions for 15 minutes on any topic regarding financial planning. Depending on the success we will increase its frequency. Please email us at <u>Consulting@fcmadvisors.net</u> if you would like to receive the invite instructions.



FCMA Model Returns
Jun 30, 2016 YTD

Conservative Model	+1.48%
Moderate Model	+1.34%
Aggressive Model	+1.12%
Indexes:	
S&P 500 Index	+2.69%
MSCI EAFE Foreign	-6.28%
10Yr T-Bond Index	-0.78%

Future performance is not guaranteed; above returns are 2pt actual averages

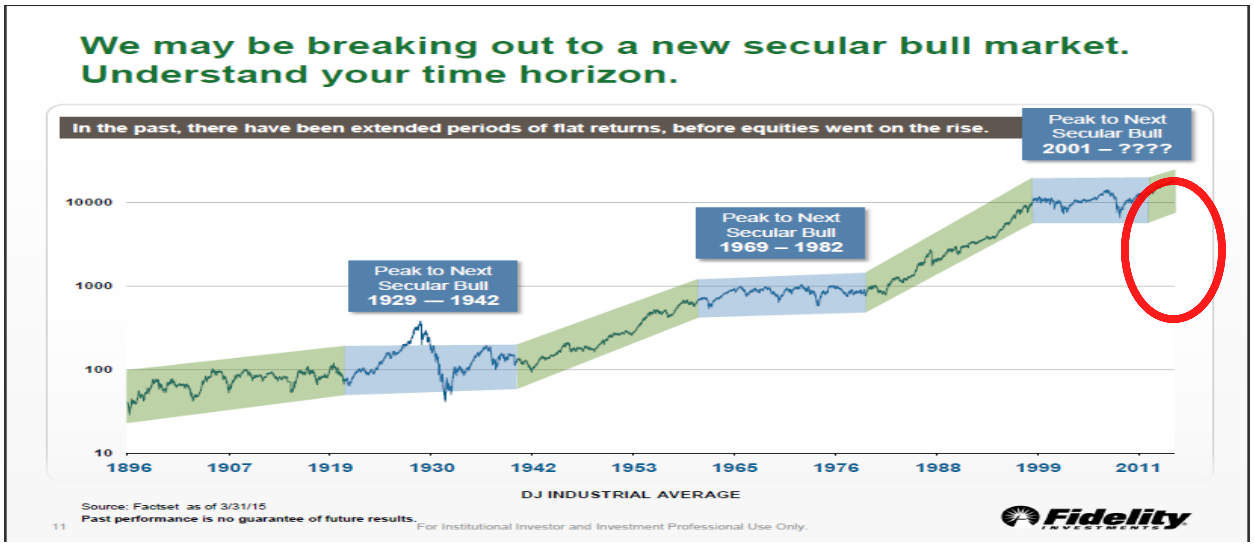
Foresight's Outlook and Portfolio Strategies

The market continues its choppiness and resilience in the US as we weathered the Brexit and have moved to higher highs! The remainder of the year we expect the market to continue its growth due to the following factors: 1.the US is currently the strongest economy globally and has stable footing, 2.the US will remain the go to country for investing, 3.it is a Presidential election year; albeit a unique one which will hold global interest, 4.oil has stabilized around $50 a barrel after an -80% drop in price, and 5.we have encountered a correction in January 2016 which has recovered. All these factors point to a market that is going to rise.

Additionally, a demographer and world renowned researcher, Mike Williams states in a recent webinar, "We are addicted to fear" and "We need to turn off that fear and understand that people make markets". He continues to explain that there is an epic change coming from the Millennials. Its is called Demogronomics=demography + economics. Over the next 50 years as the Millennials (generation Y) enter as the largest workforce and the largest population in the US at 86 million. (baby boomers =78.2 m, and generation X =69.2 m) Generation Y will set new records and influence our world in traditional ways(births, housing, auto and toy sales, etc) as well as new innovative ways we do not understand yet. The growth that is expected is epic! He is a best selling author and his website is demogronomics.com. I wanted to share this with you as it further supports the secular bull market slide and discussion I explained in our 1Q 2016 newletter. See below.

Currently the world has stabilizing commodity prices and material costs are rising. This is a good sign that the industrial growth is continuing. China has quieted and remains in a growth of 6% to 7% GDP. The US $ is now strengthening against world currencies, due to Brexit, which means our exports are going to be more expensive, therefore our global companies will face some headwinds but seem to be reporting better than expected earnings thru 2Q 2016. Unemployment has decreased to 4.9% and expected to reduce lower near 4% before this bull market is complete.

Lastly, the secular view of the market is noted in the chart below. It begins at 1896 and goes through to 2016. The green periods of time are segments of 20+ years and the blue segments are also 10-20 year periods of time. These are called "Secular Periods" because they are generational segments of time. The green are Secular Bull markets (market rises)and the blue are Secular Bear markets (market decreases). Note in the green Bull markets the line is not straight up but there are bumps or recessions within the larger Secular Bull market. The key is the green segment, although it has some "mild recessions", it is an overall growth period of time. This theory is also supported by Mike William's research cited above called Demogronomics!



Notice the right side of the chart is showing, since 2013, that we are likely moving into the next Secular Bull market period of 20+ years of time where the market will rise! If this plays out to be true, then the next couple of recessions will likely be mild and short lived. We need to look at them as opportunities and not panic. It is very unlikely we will see another 2008 during our life times. I hope this leaves you with a bit of comfort and something to really think about…Secular Bull Market and Demogronomics.

Foresight has moved all our portfolios into a cautious lower risk allocation and we will maintain this weighting moving into the fall and election time since the market is fully valued and reaching new highs. This is a precaution in case we experience another correction in 2016. We reduced weightings in foreign bonds as a defensive measure for the Brexit causing financial stresses on banks and companies, healthcare, and market neutral bonds. We have added to large cap stocks, natural resources-water sector, emerging markets, and more short bond positions. We believe these moves will maintain stability in the portfolios but allow for plenty of growth should the market continue to new highs. For clients with stock portfolios we continue to have numerous stop-losses in place as a defensive measure to hold onto gains that have been earned in the stock holdings. We expect the market to level out in 3Q and begin to climb the remainder of the year. Please contact us if you have any concerns or questions about your portfolios.

Foresight Planning Ideas

New Health Savings Accounts-HSAs with Foresight at Schwab: . Foresight now offers HSA accounts for your Company or Individual HSA savings. An HSA with Foresight will allow you to choose the same 3 Model portfolios of risk either Conservative, Moderate, or Aggressive. If you have a High Deductible Health Plan then you can consider opening a HSA = Health Savings Account with Foresight. The HSA will allow you to save in 2016 up to $3,350 for single and $6,750 for a family; if +55 then $4,350 for single and $7,750 for a family. The HSA savings are not subject to Federal Tax and will grow, much like a Roth IRA, with no tax due if used for all qualifying health expenses, note cannot be used to pay health insurance premiums. If you are interested in more information on this strategic investment idea for your healthcare savings please contact us. 2016 HDHP=minimum deductible for single $1,300 and family $2,600 and out of pocket maximum for single $6,550 and family is $13,100.

Did you Know?: Foresight has written two white papers. **Low Cost Investing- The Costly Approach?** and **Target Date Funds-The Next Retirement Dilemma.** Please email us at consultant@fcmadvisors.net if you would like a copies to read.

IRS Contribution Limits for 2016!* *$18,000 deferral max and for 50+ $24,000 deferral, and IRA limits $5,500 and if age 50+ $6,500.

Did you Know? If you have Roth 401(k) it is wise to roll these funds to a Roth IRA before you turn 70 ½ because if the Roth funds are left inside a 401(k) they must take RMD (required minimum distributions) just like the pre-tax funds which defeats the purpose of letting the Roth grow! However if you roll it over into a Roth IRA before 70 ½ then you do not need to take the RMD from the Roth IRA. This is a very important hint to remember!

Exit Planning Newsletter. Foresight recently launched this newsletter which features topics on business succession planning and retirement planning we can assist you with. If you would like to be added to this newsletter list or know someone who would be interested in receiving the information please contact us at consultant@fcmadvisors.net. Did you know about 75% of all businesses do not have a succession plan. Please contact us if you are interested in completing this important planning for your business. Foresight can now assist with transition planning for your business!

Did you Know?: You can take a distribution from your 401(k) or 403(b) prior to age 59 ½ without a 10% penalty; if you have separated from service no earlier than age 55. Funds must be in a 401(k) or 403(b) and cannot be in an IRA. Additionally, if you retire and wish to begin normal distributions prior to 59 ½ then a 72-T calculation can be done to allow funds to be removed from your IRA without a 10% penalty as long as you have separated from service.

Roth IRA Ideas if interested in additional savings ideas consider opening a Non-deductible IRA. This will allow you to save the maximum in your 401(k) and also save an additional $5.5k in a Non-deductible IRA, and $6.5k if age 50+. Then convert the Non-deductible IRA to a Roth IRA! It is a way to obtain a backdoor Roth IRA funding even if you are not able to save directly into a Roth IRA.

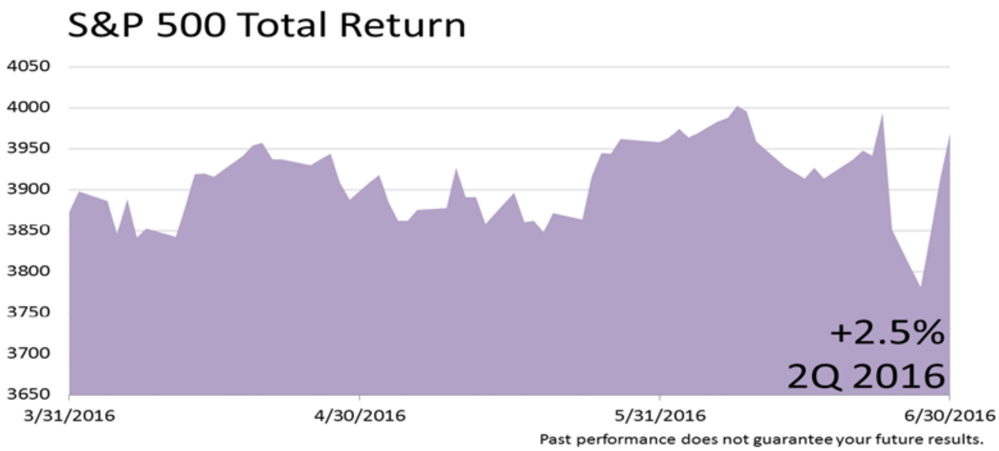
Auto-Enrollment and Auto-Increment Options for Retirement Plans: Please consider adding both or one of these important options to your company's retirement plan. They allow every employee who is eligible to be automatically enrolled at the beginning of the year, and if Auto-increment is added the company can increase the savings of each employee by 1% each year. The employee has the ability to opt out of the "Auto", but history has shown few do. Therefore the company has accomplished something good for the employee by automatically setting up savings for their retirement! Please contact us if you are interested in pursuing these features. They are very inexpensive to amend and add to your current company plan. We recommend adding them when you renew and update your plan document which needs to be done by 2016.

Feeonlynetwork.com: Foresight is now a published advisor on-line at www.feeonlynetwork.com. This is a website to locate fee-only advisors in your communities. Check it out and see a video from the AIF® national conference when Laurie was interviewed about our investment processes at Foresight!

Foresight's New WebPortal Reporting: Are you getting your quarterly reporting from us? If not please let us know so we can help you access it online through our web portal or send you a copy in the mail. We want our communication to be timely and beneficial to you. If you have any access issues please call or email us at 1-877-429-4690 or mgallagher@fcmadvisors.net. Soon we will be sending you a survey to get feedback on the use of the WebPortal.

On-line Access each year we encourage everyone to test your on-line access to your account(s) at the custodian or third party administrator for your plan. Please visit **Journeyrps.com** or **Noblepension.com** if a retirement participant. For individual clients at TD Ameritrade access **Advisorclient.com** for Schwab Institutional Clients access **Schwaballiance.com.** If you have any difficulty accessing your account, please email or contact us

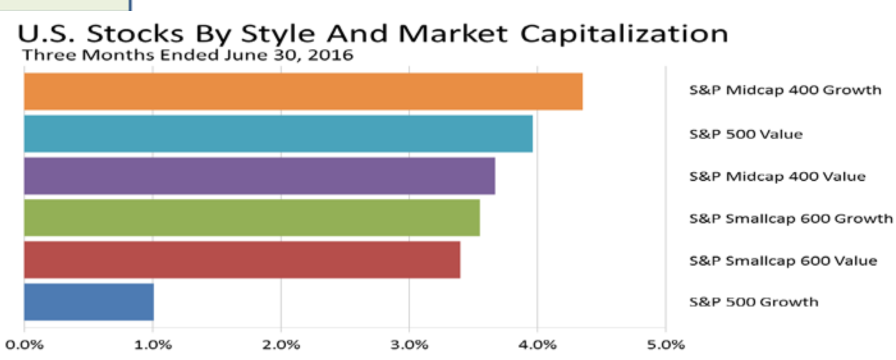
Quarterly Market Summary
2Q 2016



The Standard & Poor's 500 index of large U.S. companies posted a 2.5% gain in the second quarter despite a frightening Brexit 5.3% sell-off and snapback at quarter-end that whipsawed hot-money investors.

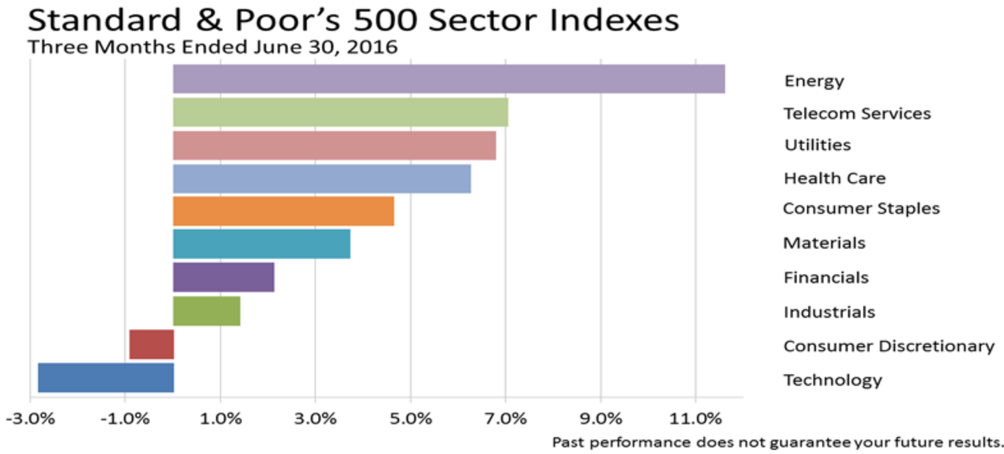
Stocks drifted higher for most of the second quarter. On Friday, June 24, the first day of U.S. stock trading after Britain's vote to exit the European Union, stock prices plunged 3.8%. The following Monday, June 27, it dropped another 1.5%. Then, just as quickly, sentiment changed and the market recovered the last week of the quarter. The U.S. stock market's strength in the second quarter of 2016 reflected a stream of improved data on the economy, including these seven positive signals:

1. Strengthening personal income and spending
2. Strong retail sales
3. Rising index of leading economic indicators (LEI)
4. New low in unemployment
5. Record-high job openings
6. Fed's accommodating monetary policy
7. After a one-year earnings recession, recovery is on



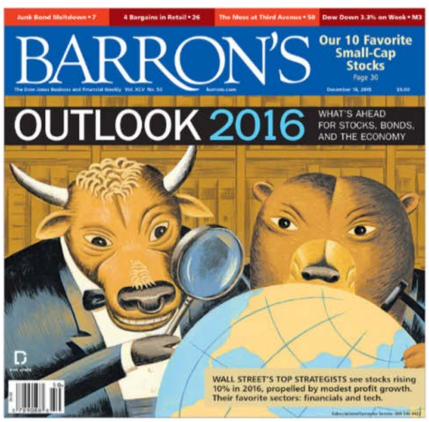
In the quarter ended June 30, 2016, large-cap growth-style investments trailed all other styles by a considerable margin.

Looking at just three months of data often doesn't reveal important intelligence, but it is part of the big-picture perspective in managing a portfolio.



The energy sector came roaring back in the second quarter, as crude oil prices recovered from a historic bottom of $30 per barrel in February.

Telecom services and utilities — the two most defensive sectors and sensitive to interest-rate fluctuation — outperformed the eight other industry sectors.



Source: *Barron's*, Cover, December 14, 2015.

While we're on the subject of the Standard & Poor's 10 industry segments, it's fun to check periodically on how Wall Street's industry forecasts are performing.

Barron's, a venerable weekly financial magazine owned by Rupert Murdoch's American publishing empire, which also owns *The Wall Street Journal*, annually interviews 10 "top" strategists from Wall Street's largest firms, and performance of their industry forecasts is tracked for us by independent economist Fritz Meyer.

Wall Street's Sector Calls For 2016

Survey of 10 stock market strategists' sector picks and pans for 2016

	Consumer Discretionary	Consumer Staples	Energy	Financials	Health Care	Industrials	Information Technology	Materials	Telecom Services	Utilities
Federated Investors			-	+	+	+	+	-		
Blackrock		-		+			+			-
Barclays Capital		-	-	+						
Columbia Management							+	-		-
Goldman Sachs		-	-	+			+	-		-
JPMorgan Chase			+	+		-	+		-	-
Citi Research	-		+	+	-		+	-		
Morgan Stanley	+	-	-	+		-				
Prudential				+			+	-		-
BofA Merrill Lynch										
Net (+/-)	0	-4	-2	+8	0	-1	+7	-5	-1	-5

Source: *Barron's*, Cover, December 14, 2015.

Here are their sector picks and pans for 2016 that were listed in the Barron's cover story of December 14, 2015.

It’s easy to see from this chart that Wall Street’s sector forecasts — shown in color — for the first half of the year were not working out very well.

Energy, telecom, and utilities — the top sectors in the first half of 2016 — were not among those picked to outperform last December by Wall Street’s strategists. Meanwhile, seven of the 10 Wall Street strategists predicted tech would outperform for 2016, making it the second-most popular pick for 2016. Tech, however, was the worst-performing sector in the second quarter.

Fritz Meyer
Independent Economist

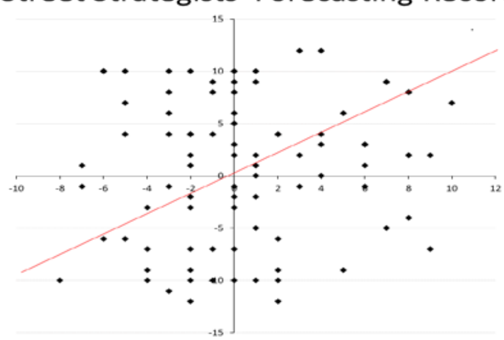
This data is unusual to come by.

Fritz Meyer was the senior strategist at one of the world’s largest investment companies for many years before going independent in 2009. He’s been tracking the performance of the Wall Street’s sector picks in Barron’s annually for over a decade, and he says Wall Street’s picks have performed poorly year after year.

Like us, Meyer is independent of Wall Street and its culture of sales. That’s one of the reasons why we so often quote his research.

Meyer sells no products, just independent analysis.

Barron’s Wall Street Strategists’ Forecasting Record, 2007-2015



Beginning-of-Year Sector Picks Minus Pans (Net) Forecast

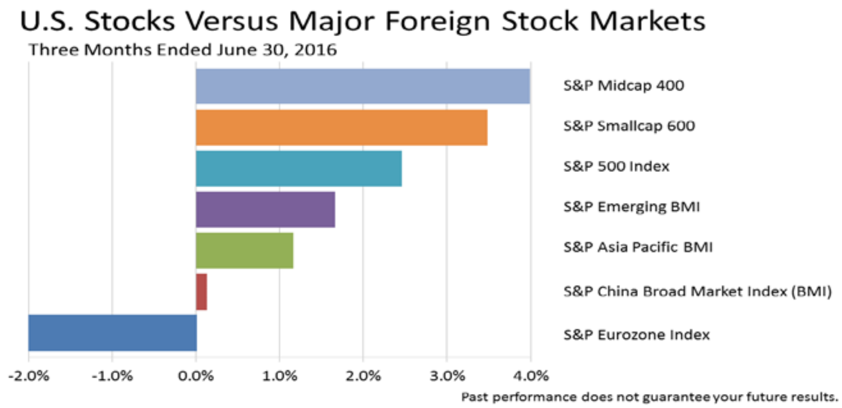
Sources: Fritz Meyer, independent economist compiled this report with data using Standard and Poor’s for actual annual sector performance data and *Barron’s* annual surveys of Wall Street sector picks minus pans.

This chart shows a compilation of all sector picks minus pans versus actual end-of-year sector returns for the eight years from 2007 to 2015 – every year since *Barron’s* began taking this survey of strategists’ picks and pans.

If the strategists surveyed, collectively, were able to systematically give valuable sector-picking advice, then these data points would lie near the 45-degree angle in red.

However, the scattering of data points looks random.

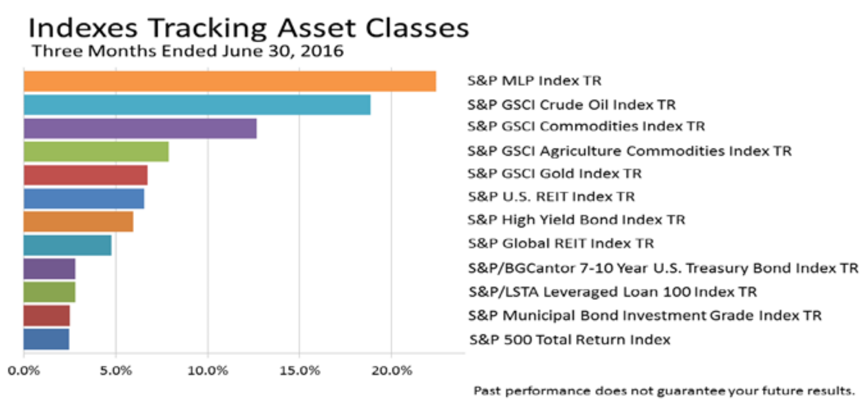
Not to be unkind, the simple truth is that the picks by Wall Street's so-called top strategists in *Barron's* are about as reliable a methodology as monkeys throwing darts.



In what has become a common quarterly pattern, U.S. stock indexes outperformed their foreign counterparts.

Eurozone stocks have suffered a most cruel fate in recent months.

The No. 1 performer in calendar-year 2015, Eurozone bourses fell from first to last place in the first quarter of 2016, and again in the second quarter.

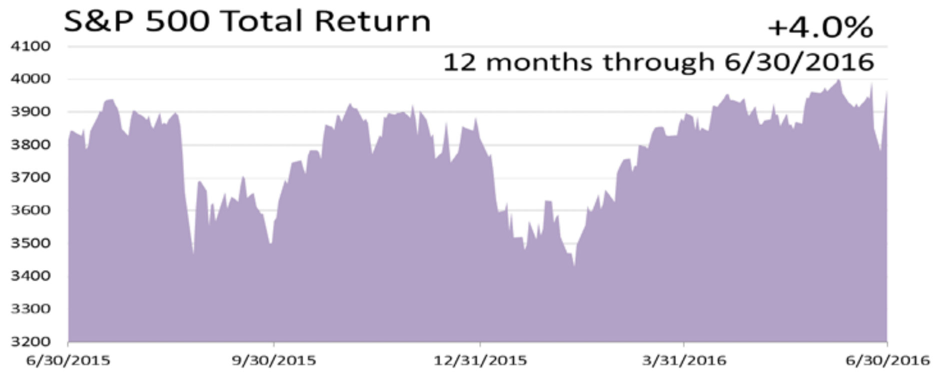


Crude oil, MLPs and commodities all reversed course and soared in the quarter ended June 30, 2016. Oil stock performance has been a virtual "poster boy" for broadly diversifying the core of a portfolio in low-cost vehicles.

Gold gained another 7% in the second quarter. That came on top of a huge first-quarter gain of 17% — following its multiyear decline through 2015.

Notably, *every* asset class gained in the second quarter. The S&P 500 gained the least among the 12 asset classes listed, which makes complete sense because of the nature of indexed investing.

Overall, this chart is a classic picture, showing how the most broadly diversified index, the S&P 500, always underperforms more concentrated constituent sectors in the short run. It's an argument for patience and avoiding seductive short-run outperformance of the hottest sectors.

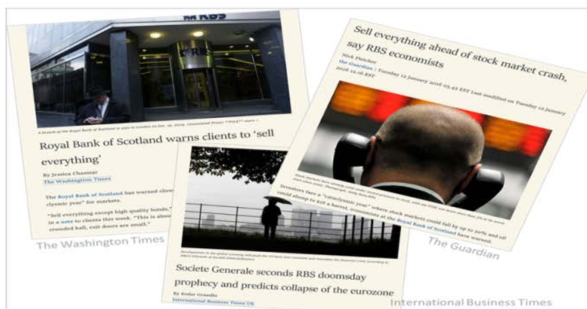


Past performance does not guarantee your future results.

Let's review factors impacting the performance of America's blue-chip companies in this 12-month period ended June 30th.

The S&P 500 index gained just 4% over the 12 months ended June 30, 2016. A collapse in profits hit energy and mining companies hard, and hurt earnings of the S&P 500.

A four percent return is less than half the average annual return of about 10% on U.S. large-companies' equities since 1926.



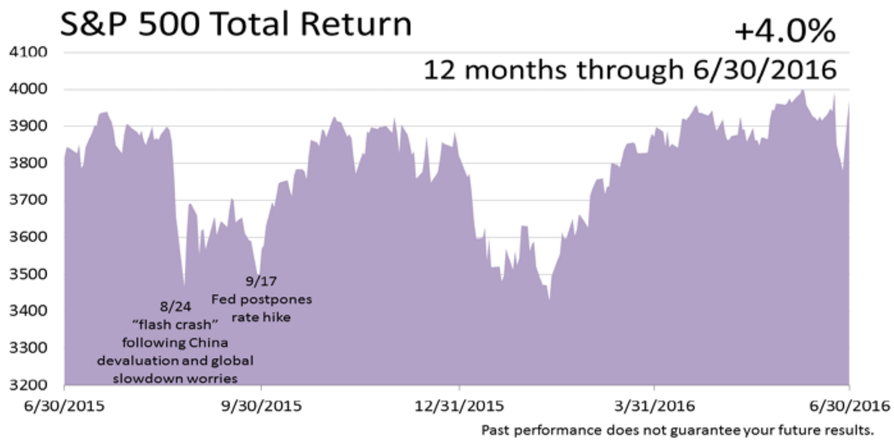
Excerpted from our email update in 1Q2016.

2016 started poorly. Within two weeks, the Standard & Poor's 500 stock index had fallen almost 10% from a December 29th high, and the financial press was filled with dire predictions.

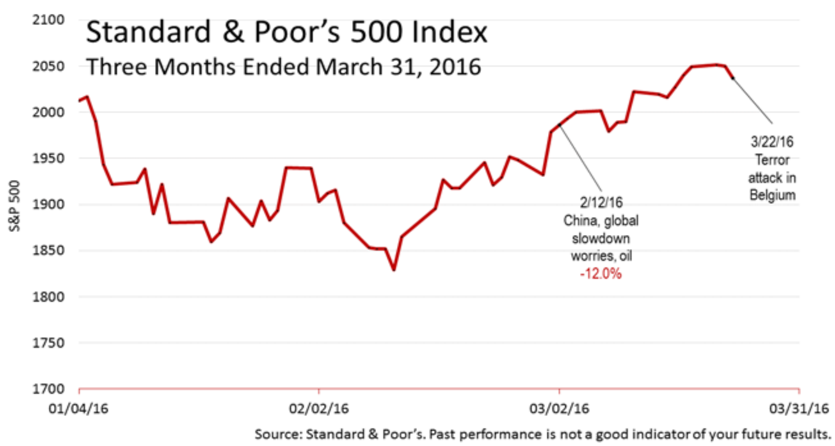
While it may seem like a long time ago, these were the headlines excerpted in our update in January 2016. Pessimism abounded to start the year and it fueled Wall Street's worst start ever to a new year in Wall Street's history.

Bad news hit U.S. markets at the opening on August 11, 2015, after China slightly devalued its currency, the yuan.

Combined with fears that the low in commodities prices might trigger a global economic slowdown, the devaluation set off an unexpected chain of events, cited as contributing to an infamous "flash crash" of August 24, when Wall Street opened, as usual, at 9 a.m. and in seconds plunged 11%.



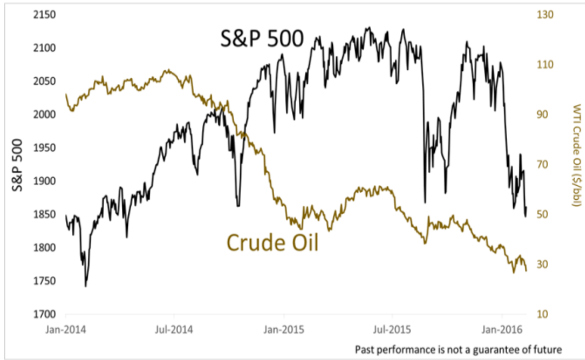
Stocks rebounded from the August flash crash, and before nervously stumbling ahead to end the year not far from its all-time high.



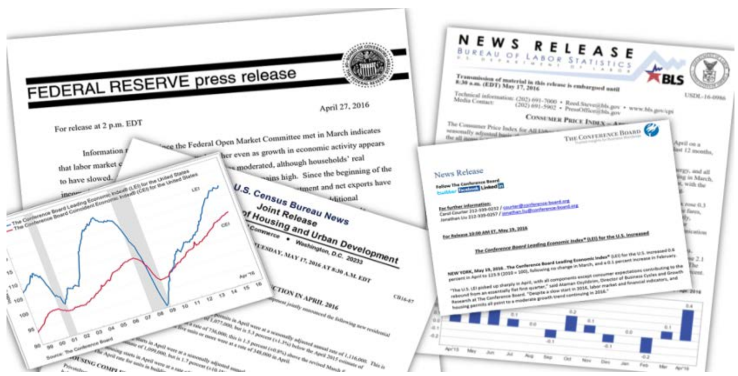
Then, in the first quarter of 2016, almost the same confluence of bad events that triggered a selloff in August, occurred once again. China announced a weak Purchasing Managers Index figure; fears of a global slowdown spread after crude oil prices hit a bottom; and stocks plunged 12% in yet another correction. It was widely reported to have been Wall Street's worst start to a new year ever.

The first three months of 2016 were a seesaw ride for stock investors.

While you could almost see the bears moving in to end the bull run on Wall Street, something about this picture did not make sense.



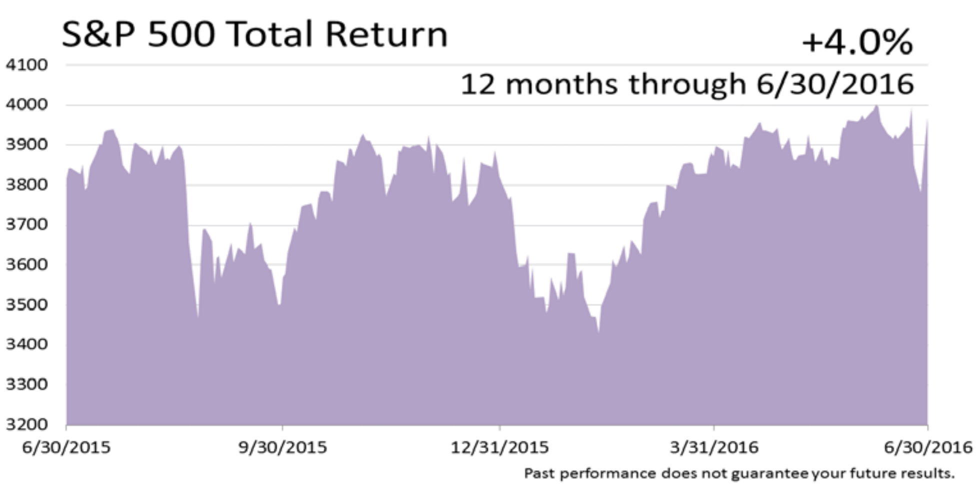
On February 12, 2016, when stocks were trading down in lock step with oil prices, we reported here that the "sudden correlation of stocks and oil prices is remarkable for revealing just how irrational and emotional the stock market can be."



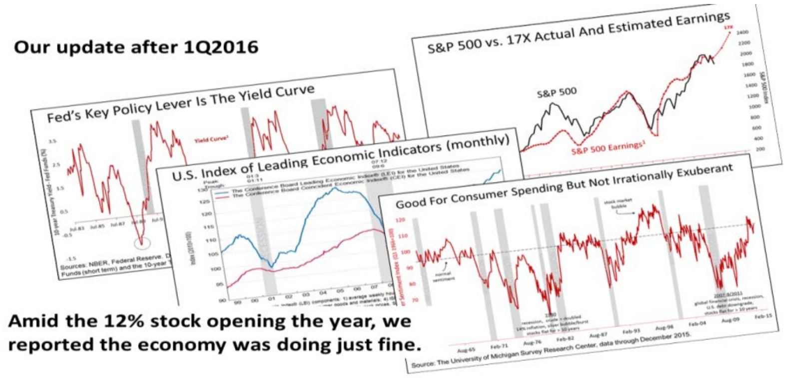
Throughout the past 12 months, despite the market volatility, in these weekly email updates, we have continued to focus on economic fundamentals.

This slide from our email update on May 20, 2016, reported on the slew of positive economic news, which, already at that time, had been coming in for months.

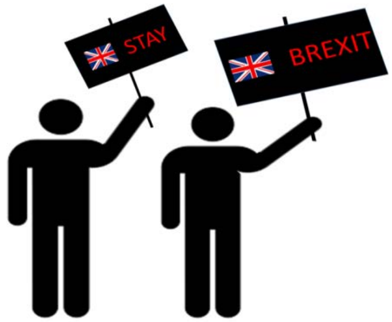
Housing starts, the consumer price index, and the index of leading economic indicators — were all on an even growth path.



By the end of the first quarter of 2016, however, as global economic data firmed up, U.S. economic data led the way.



New-job formation was soaring, the rate of unemployment declined to lows not seen in over a decade, and the forward-looking index of leading economic indicators (LEIs) was forecasting growth just ahead.



Our 12-month tour ends with Britain's stunning vote to exit the European Union. In the final week of the second quarter of 2016, history was made when Great Britain surprised the world by exiting the four-decade old effort to create a common market with Europe.

Within hours of the 3.8% sustained on June 24, we reported the June 24 "Brexit selloff" was a political crisis and not an economic one.

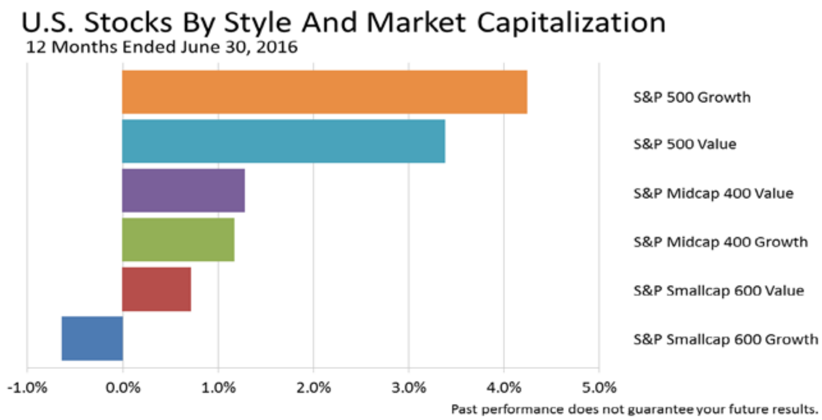
Great Britain and the European Union account for 2% of U.S. gross domestic product, according to Shehriyar Antia, a former senior analyst at the New York Federal Reserve Bank.

If <u>all</u> trade with Great Britain and the E.U. were to <u>end</u>, the impact on the U.S. economy would be <u>marginal</u> — and even <u>that</u> is not happening!

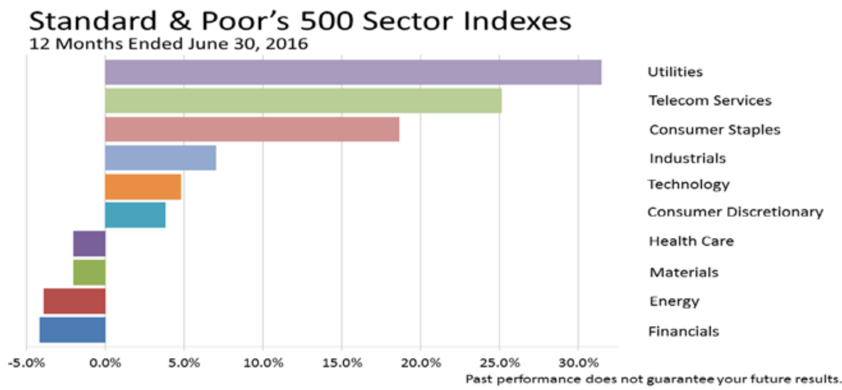
Britain and Europe will go on trading as they have been doing.

Immigration policy and politics are all that's changed.

Brexit may cause a recession in Great Britain, but that does not change the forecast for the American economy, which is uniquely insular compared to other nations.



For the 12-month period ended June 30, 2016, the large-cap growth and value stocks substantially outpaced mid-cap and small-cap companies.



Utilities, telecom, and consumer staples led all sectors in the 12 months ended June 30, 2016.

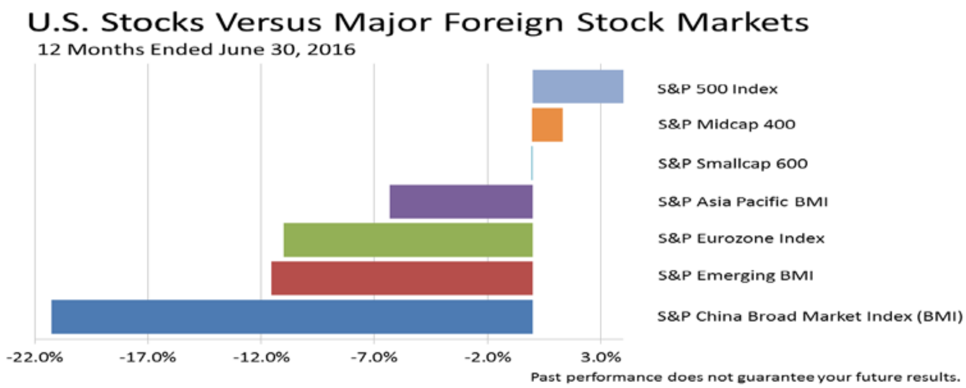
Utilities, telecom, and consumer staples are the most defensive sectors, and they outperformed.

Meanwhile, over the 12-month period, the broad market went sideways.

The one-year sector performance figures are a bad surprise for most Wall Street strategists, as these three sectors were "panned" by the strategists in 2015, and again in 2016.

This is based on research by independent economist Fritz Meyer, whose research we often share with our network. Meyer has tracked Wall Street's top strategists every year since 2005 in an annual *Barron's* cover story in which the venerable financial weekly asks Wall Street's "top" strategists to forecast which sectors will wax rich and which shall suffer a loss.

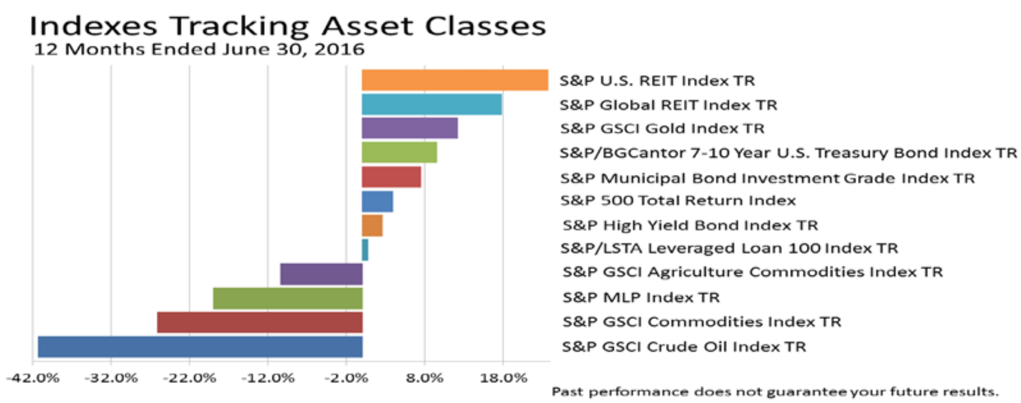
Over the years, Meyer, a strategist at one of the world's largest investment companies for a decade before going independent in 2009, says Wall Street experts are consistently bad at predicting performance of a sector one-year hence.



For the 12 months ended June 30, 2016, U.S. stocks outperformed the rest of world's major regional stock indexes.

Among the U.S. indices, the large-caps making up the S&P 500 outperformed mid- and small-caps.

China's fledgling and government-rigged stock market lagged badly. Emerging markets and Eurozone indices continued their long-held pattern of volatility.



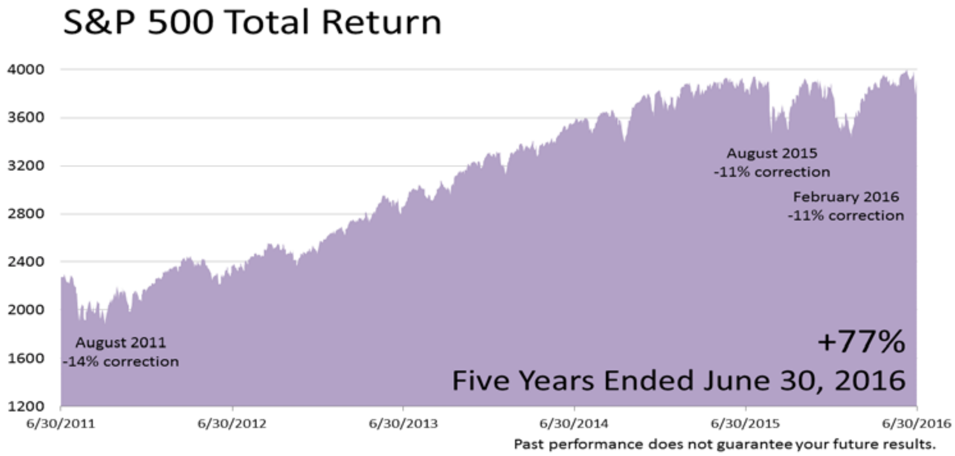
Asset classes are important components in diversification and this chart is a picture of why that is so.

The dispersion of returns in this rainbow of investments is why savvy investors don't try to pick the next hot sector.

For the 12 months ended June 30, 2016, REITs, both U.S. and global, tallied the best returns.

In a reversal of a five-year slide, gold rose by 12% over the past year.

At the bottom of the one-year ranking, crude oil and related MLPs posted major losses, as did commodities.



From the start of 2015 through mid-July 2016, the stock market has been level — although the period was punctuated by two corrections in the low double-digits.

America's largest publicly held companies — the S&P 500 — had tripled in value from a March 2009 bear-market bottom to their highs, and the seven-year economic expansion, one of the longest in modern U.S. history, is still intact.

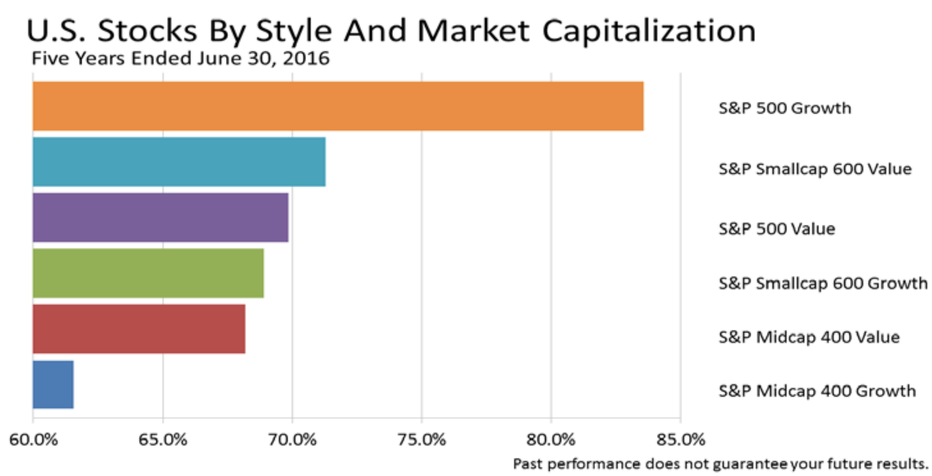
In past 11 months, the stock market experienced two 10% corrections. Those setbacks had been long-anticipated following four years of relatively low downside volatility in share prices.

Over the last five years, including dividends, the S&P 500 total return index has gained 77%, compared with a gain of 59% in the commonly quoted S&P 500 price index. The 18% difference is attributable to reinvested dividends.

Since 1900, only three of 23 bull markets have lasted six years or longer. The likelihood of a bear market — a correction of at least 20% — increases as the bull market grows older.

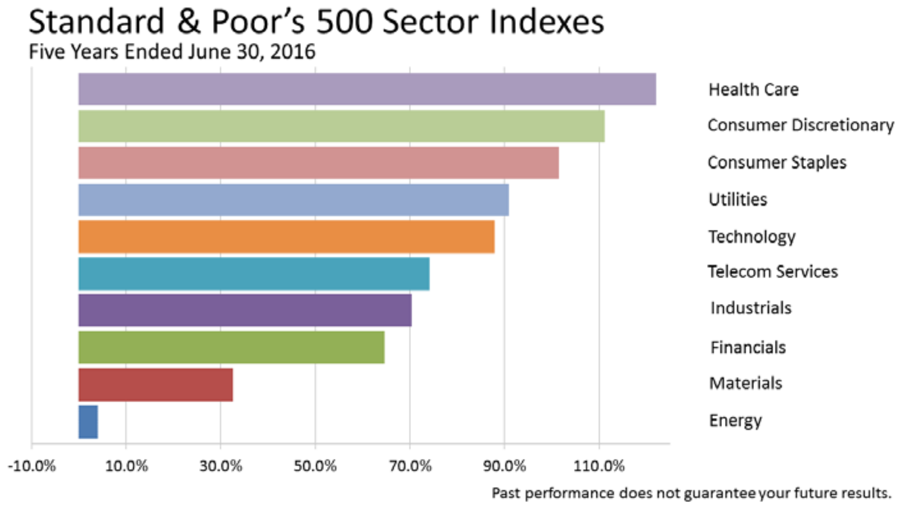
However, fundamental economic conditions that have accompanied bear markets in the past were on the horizon as of mid-July 2016.

None of the signs of an economy about to slow — restrictive Fed policy, stock market overvaluation, or irrational exuberance — are threatening to end the expansion. In fact, the economy was gathering steam as the third quarter approached.



For the five years ended June 30, 2016, what particularly stands out is how large-cap growth so substantially beat the five other styles of U.S. stock investments. The 84% total return on large-growth company share prices over the five-year period was much higher than the other styles of U.S. stocks.

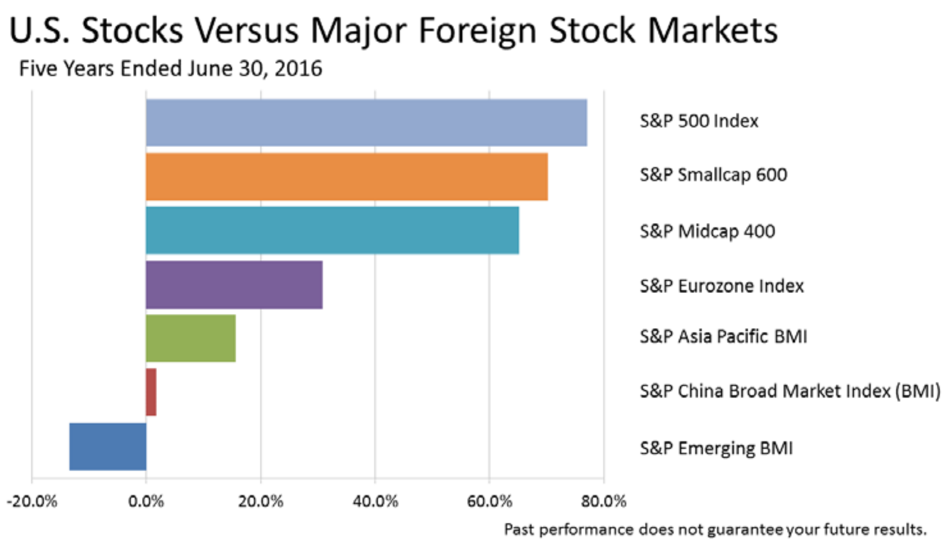
The 10 most influential stocks on the performance of the S&P 500, as of June 30, were: Apple, Microsoft, Amazon, Facebook, Alphabet, Johnson & Johnson, General Electric, Home Depot and Walt Disney. Apple, Amazon, Facebook and Alphabet (Google) are pre-eminent leaders of the new information technology economy.



Health care, consumer discretionary, and consumer staples — growth areas — all were the leaders in the five years ended June 30.

Conversely, the lagging sectors were those classified as value-style investments — energy, materials, financials, and telecom services.

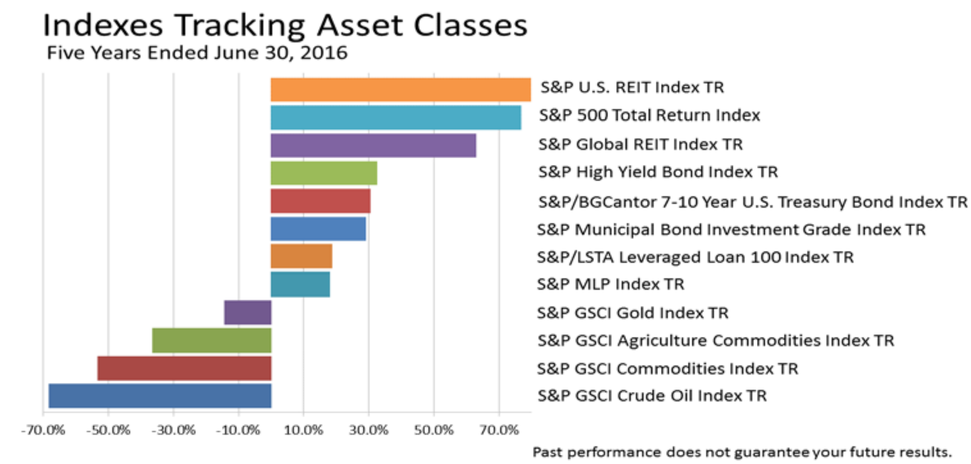
The energy and material sectors were slammed by the collapse in crude oil prices and the price of most other commodities.



In what seems at times to be a bleak period in history, when terrorist atrocities are reported almost daily, and America's enemies are absolutely frightening, the U.S. continues to be the world's capitol of capital.

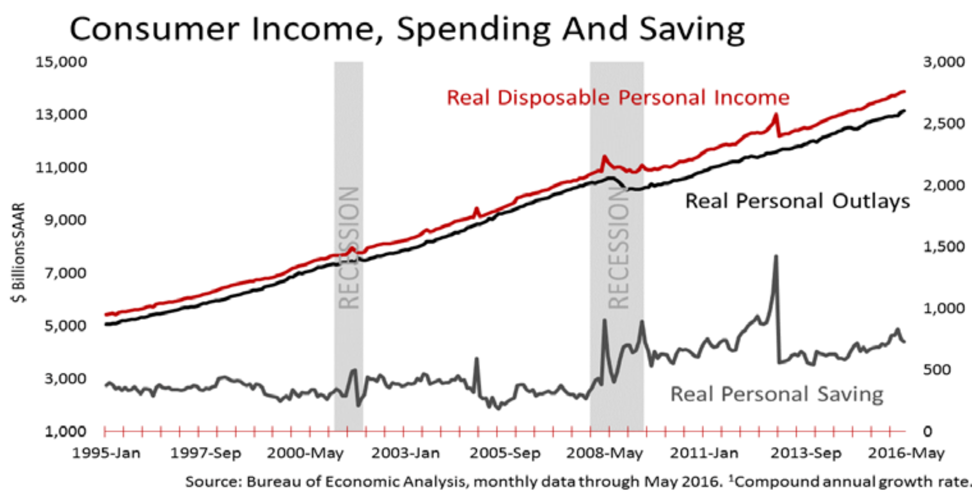
For the five years ended June 30, 2016, the stock U.S. indexes — small-, mid-, and large-cap — outperformed the rest of the world's major indexes.

The U.S. economy has been leading the world economy since the global financial crisis seven years ago.



REITs, both U.S. and global, were the top performers, for the five-year period ended June 30, 2016, along with U.S. large-cap stocks.

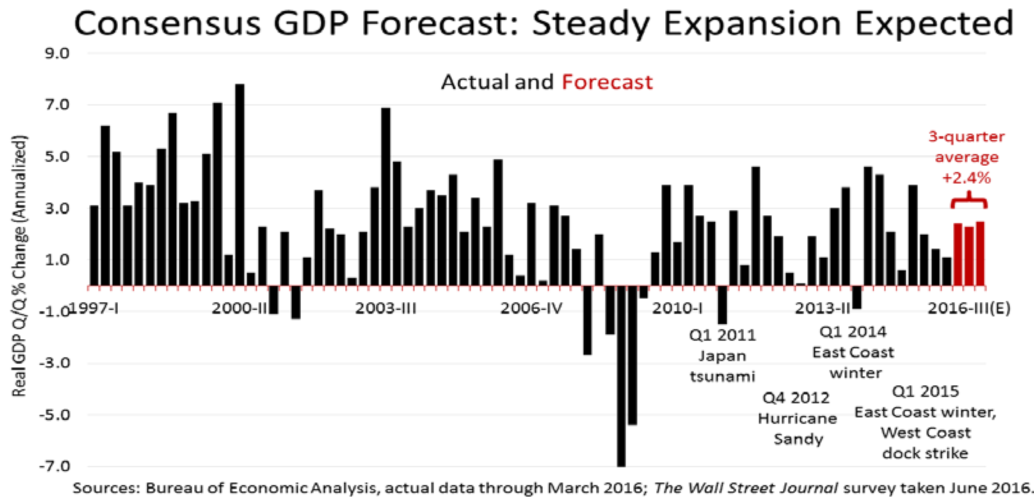
Among this broad array of asset classes, crude oil took last place. Commodities and gold have been losers over the five years.



It's an election year and, from both sides of the Congressional aisle, politicians are saying Americans have not had a pay raise in many years. At best, they're uninformed.

Real disposable personal income and spending have been growing at a healthy clip. To be precise, between May 2015 and May 2016, the growth rate in real DPI was 3.2%. What does that mean?

The 3.2% growth rate in DPI is better than the 2.8% rate from July 2002 to July 2007, an expansion built on too much debt.



Consumer spending accounts for 69% of U.S. economic activity. It is the key driver of GDP growth.

What drives consumer spending?

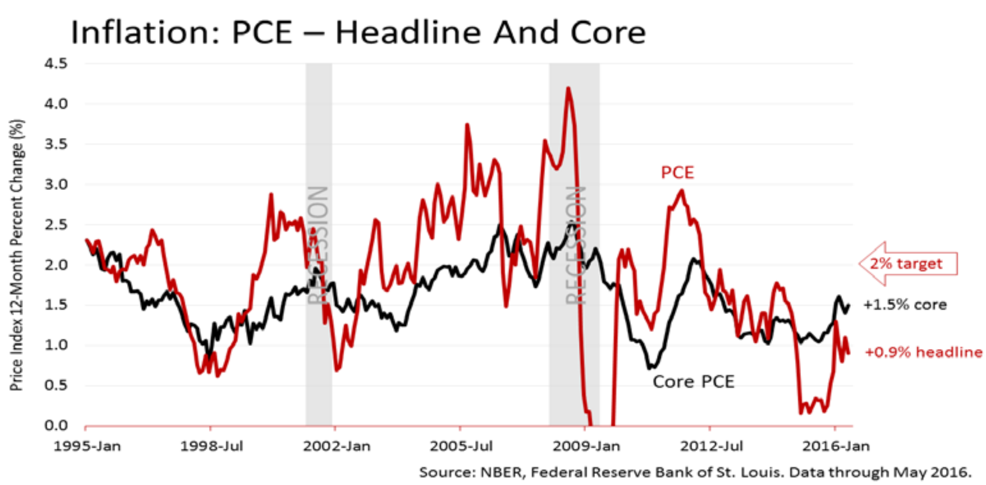
Real disposable personal income.

On this score, the economy is looking fairly strong.

Real disposable personal income growth is expected to continue to drive a 2.4% rate of real GDP growth over the final three quarters of 2016.

In early June, *The Wall Street Journal* surveyed approximately 70 economists on their quarterly GDP growth forecasts through 2016. The resulting consensus forecast is illustrated in this chart.

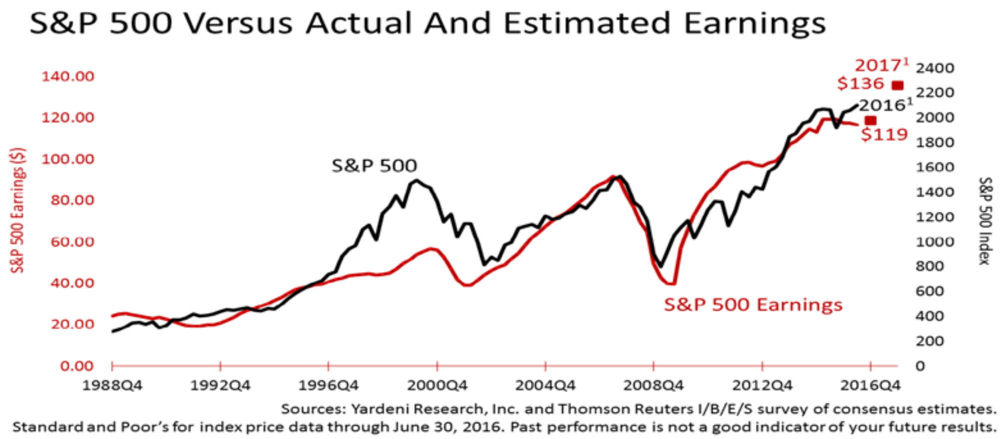
Strength in the rate of GDP growth is expected for the quarters immediately ahead.



Inflation remains well below the Fed's 2% target rate. Coupled with Brexit jitters, these two fundamentals make a Fed rate hike less likely in 2016.

Headline inflation (PCE) — the inflation metric reported most often in the financial press — has plunged, and partially recovered from the historic lows in gasoline, diesel, and fuel oil prices in February 2016.

The less-quoted but more influential inflation metric, Core PCE, excludes food and energy expenses in its monthly calculation. At 1.5%, it's higher than the headline inflation rate. However, the core inflation rate, which *is* a metric used by Fed policymakers in setting interest rates, is also below its 2% target rate.



Following a flat 2016, earnings are forecast to surge 14% in 2017 over 2016. The stock market already has priced what amounts to an earnings recession for 2016. The forward-looking earnings projections are a significant improvement over 2016.

Of all the charts we analyze every month, this one best illustrates how the stock market works. The black line represents stock prices. It tracks with the red line, which represents earnings on America's blue chips since the last quarter of 1988.

The latest consensus forecast of economists for S&P 500 earnings in 2017 is for operating earnings to average $136 per share of the S&P 500.

Despite the terrific run of stocks for over five years, valuations compared to underlying earnings are not stretched, particularly when compared to the second half of the decade of the 1990s when irrational exuberance really took over.

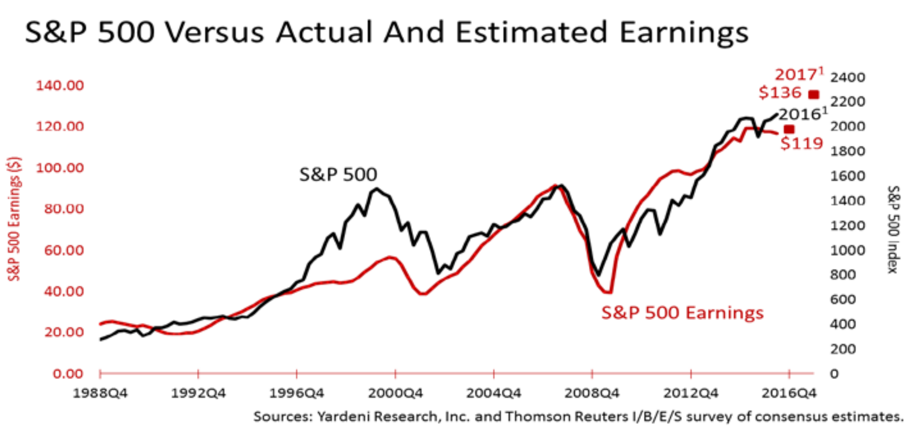
The gap that opened between earnings and stock prices in 1998 and 1999 was much wider than any other period on this chart, dating back to the end of 1988. While a gap between prices and earnings has opened in the last couple of quarters, it remained small as of June 30, 2016.

No one can predict what will happen.

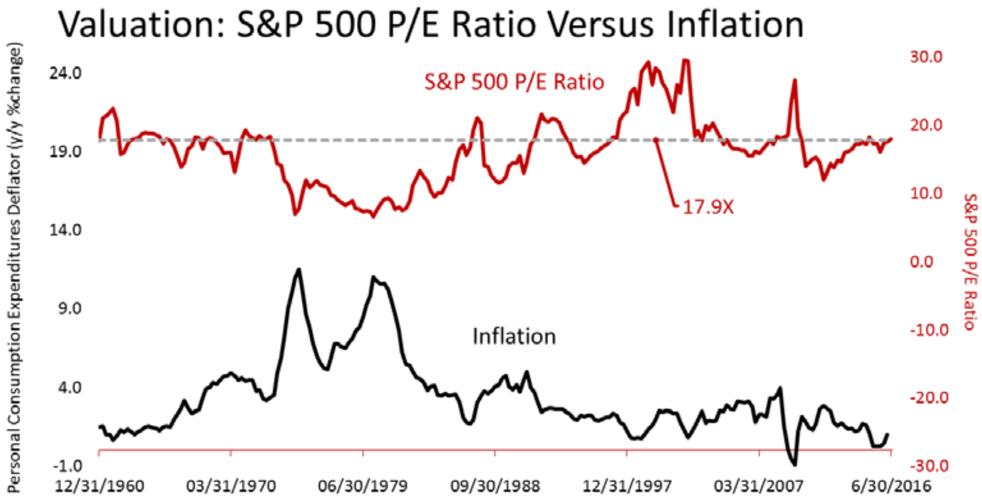
Terrorism, natural disaster, political strife, and so-called black swan events that no one ever expects, can become reality and change financial markets dramatically at any given moment.

That's always been true, although it seems harder than ever to believe.

Over long periods of time, however, we know humans make progress. We learn and make things better.



Unless some unexpected event steers earnings or prices off course — if history is a guide — the black line representing stock returns, always in the past, was pulled toward the red squares. That's not a forecast. Past performance is not a guarantee of future results. However, it is a possible outcome in the future — assuming the world works according to a plan, which we all know rarely happens.



Sources: Standard & Poor's Corporation and Thomson Reuters I/B/E/S earnings estimates, BEA. Stock price data through June 30, 2016; inflation data through Q1 2016. Top panel, latest data point: 2099 ÷ trailing earnings of $116.61 through 3/31/16 = 18.0.

Historically, when inflation is low, investors are willing to pay <u>seventeen dollars and ninety cents a share</u> for a dollar of earnings on the Standard and Poor's 500 index.

And the latest P/E ratio, as of June 30th, was exactly 17.9.

Stocks are not overpriced, but they also are not underpriced.

The valuation placed on stocks is <u>exactly</u> the same as the <u>average</u> P/E ratio on the S&P 500 over the past 55 years. Stocks are <u>fairly</u> priced.

Disclosures

This research report was compiled by Fritz Meyer, an independent economist, in collaboration with a veteran financial journalist. While these are sources we believe to be reliable, this information is not intended to be used by as financial or tax advice without consulting a professional for advice about your personal situation.
Indices are unmanaged and not available for direct investment. Past performance is not indicative of future results. This information is from sources we believe to be reliable, but we cannot guarantee or represent that it is either accurate or complete.
Investments with higher return potential carry greater risk for loss.
Investing in small companies involves greater risks not associated with investing in more established companies, such as business risk, significant stock price fluctuations and illiquidity.
Foreign securities have additional risks, including exchange rate changes, political and economic upheaval, the relative lack of information about these companies, relatively low market liquidity and the potential lack of strict financial and accounting controls and standards.
Investing in emerging markets involves greater risk than investing in more established markets, such as risks relating to the relatively smaller size and lesser liquidity of these markets, high inflation rates, adverse political developments and lack of timely information.
Fluctuations in the price of gold and precious metals often dramatically affect the profitability of the companies in the gold and precious metals sector. Changes in political or economic climate for the two largest gold producers, South Africa and the former Soviet Union, may have a direct effect on the price of gold worldwide.

Data for the CPI, Unemployment Rate, and Non-farm Payrolls are from the Bureau of Labor Statistics. Data for the GDP are from the Bureau of Economic Analysis. The Purchasing Managers Diffusion Index is a release of the Institute of Supply Management. Retail spending data are from the Bureau of the Census. Data for Consumer Confidence are from the Conference Board. Historic Treasury yields are from the U.S. Treasury; global and U.S. equity index performance numbers are from the respective index vendors, as are commodity benchmarks. Currency numbers are from OANDA.com. Sector and dividend statistics are from Standard & Poor's.
The Conference Board Leading Economic Index® (LEI) components: 1) average weekly hours worked, manufacturing; 2) average weekly initial unemployment claims; 3) manufacturers' new orders – consumer goods and materials; 4) ISM index of new orders; 5) manufacturers' new orders, nondefense capital goods; 6) building permits – new private housing units; 7) stock prices, S&P 500; 8) Leading Credit Index™; 9) interest rate spread; 10-year Treasury less fed funds; 10) index of consumer expectations. Source: The Conference Board runs through August 2015 and released September 18, 2015.
Average hourly earnings compound annual growth rate for March 2006 through December 2008 was 3.4% versus CAGR December 2008 through August 2015 rate of 2.0%. March 2006 average hourly earnings of $20.05 inflated by the personal consumption expenditures deflator (PCED). AHE exclude benefits and employers' share of payroll taxes.
[1] 2015 (actual), 2016 (estimated) and 2017 (estimated) bottom-up S&P 500 operating earnings per share as of June 29, 2016: for 2015, $117.46; for 2016(e), $118.62; for 2017(e), $135.63. Sources: Yardeni Research, Inc. and Thomson Reuters I/B/E/S survey of consensus estimates. Standard and Poor's for index price data through June 30, 2016; and actual earnings data through 2015.