SELECTOR® Money Management
2016 Second Quarter Review

Domestic Equities Moved Quietly Higher In The Second Quarter

After a tumultuous first quarter, domestic equities had a relatively calm second quarter with the exception of some brief 'fireworks' the last week of June, courtesy of Great Britain. Large cap equities settled back into their trading range, hovering just below the resistance that has capped prices for the last eighteen months. Midcap and Smallcap equities enjoyed a slightly better quarter but also remain trapped below their 2015 highs. Total returns for the second quarter of 2016 compared to total returns for the last eighteen months are surprisingly similar. The S&P 500 Index gained +2.46% in the second quarter. In the past eighteen months ending June 30, 2016, the total return for the S&P 500 Index was +3.49%, including dividends. The current annual dividend yield for the S&P 500 is 2.09%, so it appears there hasn't been much price movement over the past eighteen months.

However, those numbers don't tell the whole story. Domestic equities' relatively flat performances the last eighteen months disguise their resilience. Domestic equity markets experienced and successfully recovered from two moderate corrections and one mild correction over this period. The third quarter of 2015 and the first quarter of 2016 both included very sharp corrections of over -10%, followed by very impressive recoveries. In the second quarter of 2016, Great Britain's surprise exit vote from the European Union triggered a correction of almost 5% in just two days, which had fully rebounded three days later. While it is frustrating being held in a trading range, domestic equities' ability to rebound so strongly and move back to the upper end of the trading range command respect.

International Equities Had A More Complicated Quarter Thanks To Great Britain.

Developed international equities broke a long-term downtrend in the second quarter and were in the process of establishing a new base going into the end of June. Then the surprise vote by Great Britain to exit the European Union jolted markets, especially European equity markets. They dropped twice as far as domestic equity markets, and rebounded half as much. The net effect is that European markets will need to plow out of a much deeper trading range than before the vote. Emerging markets equities did much better then developed international equities in the second quarter. The Russell Europe Index fell -2.90% in the second quarter, while the Russell Emerging Markets Index gained +1.14% for the quarter.

Bond Markets Enjoyed A Very Good Second Quarter

Bond markets have been the real 'sleeper' sector of the financial markets. Conventional wisdom predicted that bond markets would suffer as the Federal Reserve increased interest rates. But the Fed only increased rates once, then held off. Surprise. Conventional wisdom predicted that bond markets would suffer as inflation rates increased. But inflation, as measured by the Fed, has been quiet. Surprise. So bond markets have not been experiencing either one of the pressures which had been forecast, and instead have been interacting with equity markets, their natural role. Those bond sectors which have links to equities, such as high yield and convertible securities, have been the strongest to rebound, after suffering significantly in 2015. But high quality, U.S. Government, floating rate, and municipal bonds have been performing well, too. The flat equity markets, with their occasional sparks of volatility, have also been contributing to bond market performance. And it looks like more of the same in the immediate future.

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