



January 1, 2016

Dear Clients and Friends,

As we write this letter on the last day of the year, the stock market looks poised to end 2015 within a percent or so of where the year began. Moving into 2016, FBB Capital continues to focus on the changing trends of currency, China, and crude oil or as we refer to them, “the three Cs”. While maintaining our position of a “slow and low” domestic economic backdrop, we must keep in mind that meaningful shifts in the three Cs drove significant market volatility in 2015. Though in the end, most domestic equity markets were straddling the zero return level for the year, we still believe positioning investments with an eye toward fundamental movements in currency markets, China, and crude oil, remains a priority for 2016.

### **The Three Cs**

FBB expects a rising U.S. dollar amid fluid changes in global interest rates. U.S. economic growth in the second half of 2015 continued to push unemployment figures lower and wages slightly higher; allowing the Federal Reserve to finally sound the “all clear” in December with the first, of what we believe will be a multi-year string of interest rate increases. At the same time, the Eurozone reiterated its commitment to maintaining an easy monetary policy. This divergence of strategies in the two largest developed markets should lead to continued higher relative interest rates in the U.S. which will likely attract global investors, boosting demand for the dollar. We anticipate that these currency changes may pressure U.S. exporters’ results, while benefiting domestic consumers and European exporters.

In 2016, we expect greater stability within the Chinese economy, which should reduce investor concerns about China-driven equity volatility in the U.S. (It is worth noting that economic stability does not necessarily equate to Chinese stock market stability!) While we are open to opportunities in the Chinese market, we continue to prefer to invest in China through multi-national companies selling to Chinese consumers.

A slowing Chinese economy has generally reduced demand for crude oil and other commodities used to build heavy infrastructure, in addition continued oversupply of many of these same commodities led to the sharp price declines experienced in late 2014 and throughout 2015. In 2016, FBB believes that global supply and demand should move prices closer toward equilibrium, if this occurs, then commodity prices should stabilize. However, a stronger dollar may continue to depress commodity prices somewhat in 2016, putting more pressure on commodity exporters.

### **Encouraging Economic Framework**

Even with potential continued volatility across the three Cs, the fundamental U.S. economic backdrop leads us to believe steady market appreciation is more likely than a bear market in 2016. Stocks and bonds should benefit from consistent economic growth, improving corporate profits, reasonable valuations, and rising interest rates. In addition, we view low and declining unemployment, modest inflation, improving housing indicators and steady growth in services and consumption to likely offset manufacturing weakness thus, fueling another year of slow and low GDP growth.

A steady economic expansion, in our view, will help companies continue to beat quarterly profit estimates by roughly 4-5%, in-line with recent trends. We continue to evaluate not only profitability but also quarterly sales results to ensure the quality of the earnings growth is sustainable.



Rising profits, combined with reasonable relative valuations, should support the equity market in 2016. Large U.S. stocks seem reasonably priced, S&P 500 valuations are presently in line with their European counterparts, while Chinese equities are still *more than twice* as expensive.

### **Portfolio Positioning in 2016**

FBB maintains cautious optimism entering 2016. As we navigate changes in currencies, China, and crude oil, we anticipate that broader economic conditions remain favorable for investors. We believe that a continued focus on high quality companies with under-appreciated growth drivers is well suited for investors' portfolios. Based on these themes and our outlook, FBB is positioning clients' portfolios in the New Year with the following in mind:

- **Continue to maintain equity exposure** as stocks are likely to outperform bonds in a rising interest rate environment.
- **Be mindful of headwinds from a stronger dollar;** we are avoiding investing in companies with heavy exposure to export markets, particularly those selling big-ticket items where foreign buyers may delay purchases as their buying power weakens.
- **Underweight portfolio exposure to China and crude oil** along with other commodities.
- **Focus on domestic-oriented U.S. companies,** as well as, world-class multi-nationals selling high quality, high visibility products with minimal competition and high barriers to entry.

With Best Wishes for the New Year,

FBB Capital Partners

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**Note:** Please **SAVE THE DATE** for the following upcoming events, further details to follow via e-mail:

- On January 14<sup>th</sup>, FBB will host a conference call with clients to discuss our Investment Outlook (Time TBD).
- On January 27<sup>th</sup> at 2pm, FBB will co-host the first of four calls this year with our friend Greg Valliere, an expert in political and economic trends who will help enlighten us on potential investment implications of the presidential election.

***P.S. As a reminder, your form 1099s should carry all relevant tax information that you need for your 2015 tax preparation (with the exception of K1s). As in years past, we expect the initial delivery by Charles Schwab and TD Ameritrade to occur by mid-February but with a high likelihood of revisions to follow well into March. Due to these potential revisions, we would suggest avoiding filing early.***

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