Mark's Musings

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Investing in a Post-Brexit World

Executive Summary

- Brexit, in itself, is unlikely to have a meaningful impact on the global economy. However, it could precipitate a domino effect, which sees other EU member states push to leave, thereby unraveling the EU edifice.

- The immediate and severe sell-off in markets over the two trading days following Brexit laid bare the fragility of the global economy and the latent risks in financial markets. Brexit was a catalyst for this exposure, not the cause.

- We are in the midst of an ongoing and dramatic decoupling between worsening economic fundamentals and the elevated prices of financial assets, particularly US equities. This decoupling was brought about by, and its perpetuation relies on, unprecedented easy monetary policies by global central banks. Bond yields have thus been brought to heretofore unfathomably low (and even negative) levels, causing investors to bid up risk-assets in a search for yield.

- Investors relying on the "traditional" portfolio of developed market bonds and equities, particularly US equities, are likely to experience disappointing long-term returns with the prospect of severe losses in between. Precious metal and miners may prove to be lucrative assets to own, however.

"In a chronically leaking boat, energy devoted to changing vessels is more productive than energy devoted to patching leaks."

- Warren Buffett

On the morning of June 24th, investors in the US woke up to a rather startling news story. Despite going to bed with odds makers predicting it was 75% likely that Britain would choose to stay in the EU, UK voters defied the odds and opted out. In so doing, they also defied the earnest admonitions from virtually every world leader and most UK politicians, who warned a Brexit would lead to nothing but tears.

Those arguing that a Brexit would be disastrous initially appeared to be vindicated, as global stock markets did not receive the news of a Brexit reality with much alacrity; over the next two trading days **$3 trillion** of stock market losses took place around the planet. I think it is likely that most people have a hard time comprehending the notion of how much money that actually is. It represented $400 in losses for every man, woman and child on the planet. It is actually more than the entire GDP of the UK, which is the 5th wealthiest country in the world! Indeed, $3 trillion was the largest two-day loss in the history of global stock markets. I think it is fair to say that not since the depths of the Global Financial

Crisis was there as much palpable fear in the markets as took place on the 27th of June.

Yet by the end of the week following Brexit, the S&P 500 was trading at the same level it was the day prior to the Brexit vote. It would appear that at least US equity markets rather quickly concluded that Brexit was a non-event and returned to business as usual.

A logical question to pose then is: should you really care that Brexit happened, and what, if anything, does this mean for investing going forward? Let me posit a seemingly befuddling thesis that Brexit changes everything and nothing at the same time.

I believe most people misunderstand the import, or lack thereof, concerning the UK opting to leave the European Union. Despite the fear-mongering propagated by EU officials and the most strident of the Remain proponents, the actual economic impact of a Brexit is unlikely to be earth shattering. Does anybody really think that trade between the UK and Europe will simply vanish? Granted, there is a strong contingent among pro-EU forces in Europe seeking to make an example of the UK for having the temerity to leave the greater European fold. But it is hard to conceive that Europe will act too drastically in terms of economically isolating the UK, as doing so would largely be cutting off its nose to spite its face. I suspect that we will likely see a post-Brexit UK-Europe relationship characterized by fairly favorable, if not the very best, mutual trade terms.

So the actual economic impact to the global economy will be little more than a rounding error. Hardly something in itself warranting a $3 trillion vaporization of paper wealth, however ephemeral it was. Indeed, I think a strong argument can be made that being unshackled from the myriad of constrictive EU rules and regulations that impact everyone from farmers to investment bankers will actually lead to a net economic gain for the UK in the longer run.

So if, as I contend, Brexit will have minimal impact on the global economy, what then is its impact on markets? Here, I believe that Brexit changes everything for investors.

What A Fine Mess You've Gotten Us Into Now, John Bull

The first way in which the UK's decision to leave the EU is a game changer relates to the potential domino effect it could have within the EU. The EU resembles the threadbare, gnarly sweater from my college years that resides at the bottom of one of my drawers; imprudently tugging on the wrong loose string threatens to unravel the entire thing. Immediately after Brexit, politicians in Spain, France, Greece, Denmark and several other European countries proposed cutting loose from the EU. I am sure there are more than a few portly technocrats in Brussels suffering from near perpetual indigestion fearing that their meal ticket that is the massive EU edifice could come apart at the seams.

The EU itself is composed of rather strange bedfellows. It is an odd supranational experiment whereby member nations are expected to surrender sovereignty in the hope that the whole will be greater than the sum of its parts. Unfortunately, there is a problem with economic cooperation among nations that is as old as international trade itself. So long as the economic pie is seen as increasing, deeper links are easy to forge. People do not perceive things as a zero sum game. Hence it is possible that everyone can "win" in the same way that a rising tide lifts all boats.

The EU has its origins in the Treaty of Rome, entered into by six Western European countries that established the European Economic Community (EEC) almost 60 years ago. At the time of the late 1950's Europe was experiencing tremendous economic growth and development, and economic cooperation was easy to achieve as prosperity abounded throughout the region. Not only did the EEC grow, but it eventually morphed into the EU with its 28 (soon to be 27) countries. In fact, the UK's decision to depart the EU is the first such instance of a member nation rejecting such integration in its (and its predecessor's) nearly six decades of existence. The UK's decision reveals a lot about the current state of Europe and the economic, fiscal and politi-

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cal challenges it faces.

It should be quite obvious that the place in which Europe finds itself presently is quite different from the go-go growth days of decades gone by. Europe is suffering from some of the most anemic growth in the world, which is made worse by the mammoth debt burdens of the PIGS (Portugal, Italy, Greece and Spain). Schisms have been widening within the EU as the spendthrift Mediterranean countries are in need of huge and painful economic restructuring if they are to have any hope of obtaining some semblance of fiscal sobriety. But there is no political will to achieve any such necessary reform. As such, it has become the burden of the thrifty and diligent Northern European countries (most notably Germany) to accommodate the peripheral laggards. Greece, and its bail out, was just the first instance of this. The EU now faces far more nettlesome issues presented by the significantly larger economies of Italy, Portugal and/or Spain.

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Importantly, Greece's bailout has achieved virtually nothing in terms of structural reform there. In essence, Greece has been making interest-only payments on its credit card bills while doing little to rewrite their social contract so that it is financially feasible. This creates quite a bit of tension within member EU countries. The most recent discussions regarding a potential bailout of Italy's bad-debt-laden banking system indicate Italy is no more willing to shoulder the burden of the adjustment process than Greece has been. This only adds to tensions between Northern and Southern Europe.

Sadly, on top of all of the economic problems facing EU member countries is the immigration crisis that has spawned from the conflict in Syria. This is where politics has been getting ugly. In addition to making it difficult to forge and maintain economic ties between nations when, due to slow or nonexistent growth, people perceive the world as a zero-sum game (hence making one nation's "gain" via trade another nation's "loss"), the darker side of human nature tends to take shape in the form of rabid nationalism, xenophobia and bigotry. While it is not practically possible to assess the degree to which the UK's decision to leave the EU was based upon the issue of immigration, I think it is safe to say that without the immigration crisis the Remain camp would have prevailed. It is distressing to see nationalist political parties making gains in numerous member EU countries, in both Eastern and Western Europe. Thus, a real danger of Brexit is that it will indeed embolden and strengthen extremist, nationalistic political parties that are generally hostile to ethnic minorities, and immigrants most particularly.

Similar to the Great Depression, when the US passed the Smoot-Hawley tariffs, which were replicated around the world leading to a series of beggar-thy-neighbor protectionist policies which further deepened economic misery, with Brexit we could see the beginnings of economic disintegration. This would bode quite poorly for the future health of the global economy. If nothing else, it is clear that the future viability of the EU has been dealt a rather serious blow by a Brexit.

Don't Look Now, But The Emperors Have No Clothes!

The second way in which Brexit changes everything relates to how we see risk and economic fragility. Despite the fact that US markets are now trading above their pre-Brexit levels, we collectively had a tremendous glimpse for two trading days of what real panic and fear look like. Now the important thing to realize is that the actual economic impact outside of England and Europe was going to be quite limited. But the financial world lost its collective mind over the event, not to mention a decent chunk of paper wealth in the process.

I have a very simple explanation as to why asset markets are prone to huge volatility and manifest such fragility. It is a consequence of the growing realization that the dizzying heights to which US equity markets have risen (more on that later) in no way reflect a connection to the underlying health of the economy. Rather the support for frothy asset prices lies almost solely in investors' (misplaced) faith in the ability of global central bankers to pull the right levers so as to keep the global economy from unraveling again.

I cannot stress the importance of this enough. When rising asset prices are matched by robust economic growth, reasonable valuations and general prosperity, temporary setbacks, whether they be economic or geopolitical in nature, generally do not precipitate market mayhem. This is because there is underlying economic strength in the form of expanding revenues and profits for corporations that match rising stock prices that are not yet overvalued.

However, presently we are witnessing a continued massive decoupling between underlying economic fundamentals and US equity market strength. The only thing left to fill the void are the assurances from the Fed, European Central Bank (ECB), the Bank of Japan (BOJ), and the Bank of England (BOE) that they stand ready to create trillions more dollars, euros, yen and pounds, while keeping interest rates at or, as is increasingly the case, **below** zero. But the problem is that people have heard this noise before. Indeed since the Global Financial Crisis, just the "Big Five" central banks (the Fed, ECB, BOJ, BOE and the People's Bank of China (PBOC)) have expanded their balance sheets, which is another way of saying created money out of thin air, by the equivalent of over **$10 trillion**. Just as shocking, according to JP Morgan Asset Management there have been **650** interest rate cuts by central banks around the world since 2008. That equates to one cut for every three trading days!

But despite central banks collectively nearly emptying their guns into the target of languid global growth for almost eight full years, they have precious little to show for it. We are now into our fifth year of subpar global growth that has been in the 3% range. But that fails to tell the complete story of how ineffectual central bank policies have been. Growth in the developed markets, in which central banks have pursued the most aggressive and expansionary monetary policies, has been almost non-existent. Despite US stocks, as measured by the S&P 500 index, being up 225% since their March 2009 lows, we have had the weakest economic recovery following a recession in over seventy years. Japan is either in recession (again) or perilously close. Europe is growing at less than 2%.

In the end, Brexit's most important legacy could be that it serves as a harbinger of a bear market in the confidence investors have that central bankers and policy-makers can actually steer the global economy from the shoals of recession and further deflation. From this perspective, I see Brexit as a potential Bear Stearns-like event. Bear Stearns was the investment bank that became insolvent in March of 2008, which eventually was acquired by JPMorgan Chase only after the Fed orchestrated a massive $28 billion bailout. This meant that JPMorgan Chase would acquire all of Bear Stearns' assets, while being subject to a tiny fraction of its massive liabilities. If anyone doubts that crony capitalism is an absolute and odious blight upon America, I offer this as Exhibit A. But it is simply one example among many.

Bear Stearns was an extremely important event, as it represented an inflection point of sorts. Prior to Bear Stearns, markets were still within 10% of their all-time highs. While everyone knew about the sub-prime problems, the Fed and most pundits were assuring market participants that economic dislocation would be limited to that sector of the economy. Bear Stearns' collapse preceded the real market melt-down to come by five months. Yet its demise proved that sub-prime lenders were not the only place where massive economic fragility existed. Canny investors could see the writing on the wall and realized, if they had not already, that, Fed assurances aside, a real economic and financial cataclysm was in the offing.

Nevertheless, much like after Brexit, markets rallied strongly after the Bear Stearns bailout/sale, spiking more than 10% in the couple of months that followed. Most peo-

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ple drank the Fed's Kool-Aid, thinking that the successful bailout **proved** the efficacy of the Fed's actions in averting economic dislocation. In reality, it should have been obvious to most that this was a desperate attempt to put a finger in the dike. It did nothing to redress the fact that there were hundreds of billions of dollars in bad loans that had been securitized and offloaded to greedy investors based upon unsustainably high prices in their underlying assets, US homes.

Thus, Brexit could be a similar inflection point. Just as Bear Stearns should have made manifest to investors that Something [wa]s Rotten in the State of Denmark, Brexit and the initial reaction to it should highlight the deep fragility of most asset markets and the precipice upon which the global economy is perched. For in a sense...

Brexit Changes Nothing And THAT Is What Should Scare People

Brexit, as surprising of an event as it was, will likely have minimal impact on global output, total prices or anything else of direct economic significance to the world. The real economic boogeyman is the same one that I and numerous other financial thinkers and investors have been highlighting for a few years now – the wild decoupling that has occurred between the health of the global economy, or lack thereof, and almost unfathomably expensive global bonds and US stocks.

The words, mentioned here before, of value-investing godfather Benjamin Graham are worth remembering: "In the short-run the stock market is a voting machine; in the long run it is a weighing machine" (although I might broaden this to include all investible assets). This is where thinking about the manner by which one makes, or loses, money investing is incredibly illuminating. Pretend for a moment that your entire stock and bond portfolio, however great or small, is frozen for three decades, and you find yourself unable to trade in and out of these instruments. After thirty years, by what do you think one's returns would be dictated?

For stocks it would almost certainly be dictated by the degree to which companies were able to grow earnings and distribute them to shareholders. This in turn is affected by the ability of the economy as a whole to be growing at a favorable rate. For bonds, it would be determined by the current interest rate (at record lows) and modified unfavorably should inflation be higher in thirty years than it is today, and further modified unfavorably by the odds of bond-issuers not meeting their obligations.

Unfortunately, people often treat securities, and stocks in particular, as more akin to placing a bet at the sports book of a Las Vegas casino than obtaining fractional ownership in a business enterprise. Just like when the NBA team, the Golden State Warriors, went on a 24-0 tear to start the season and its fan base exploded nationally, so too do investors pile into the hottest and most popular stocks and sectors when deploying their capital (the voting machine phenomenon). Yet if we take a hard look at various assets, Brexit has nothing to do with their rather dim prospects. Poor future returns were already baked in the cake and **this** is what should concern investors.

Bonds — Financial Plutonium?

It may seem odd to start a tour of financial assets with bonds. After all, stocks generally get both more money and more attention from investors. But if you are an investor and are not aware of developments in the bond market and their likely import, you may be in for some very unpleasant surprises in the future. The bond market may have become the most hideously deformed bubble, certainly in terms of scale, ever seen in the history of asset markets.

A little over a year ago I devoted a quarterly report to asset allocation in which I mentioned that bonds looked to be a terrible investment for any medium- to long-term investor. At the time, somewhere around $2-3 trillion in government bonds globally were trading at **negative** yields. I noted that it was beyond my comprehension as to why an investor would buy an instrument guaranteeing that, if they held it to maturity, they would receive **less** than their principal back after **any** length of time. But some of these bonds were of durations of up to 10 years!

Well, in the last 12-15 months the global bond market has gone further down the rabbit hole. At the end of June, Bloomberg estimated that approximately **$11.7 trillion** worth of sovereign bonds were now yielding less than zero. Almost certainly to their long-term detriment, bond investors have wholeheartedly substituted the uncertain potential of capital gains for actual income generation. Venerable bond guru Bill Gross recently warned that this creates the prospect of a "financial supernova."

Broadly speaking, I believe bonds fall into two extremely undesirable camps. The first is debt instruments whose principal is generally deemed to be quite secure (at least until investors realize the extent to which developed nations have created trillions and trillions of dollars in unfunded liabilities). So owning these will allow you to sleep at night, sort of.

The problem is that "safe debt" is universally yielding less than domestic rates of inflation, at best. At worst investors are receiving yields below 0%. Switzerland is an extreme case worth noting. After Brexit, the *entire yield curve* of Swiss sovereign bonds went negative. That means that since Switzerland is one of the few countries issuing fifty-year bonds, one could tie up their money for *half a century* and receive less than one's principal back! Frankly I never dreamed such a thing could ever happen. Why would someone ever invest in "safe" debt instruments if their yield is virtually the same as holding cash, or in many instances worse?

The second camp into which bonds fall is those producing meaningful yield, but whose principal risk is simply too high. Interest rates are supposed to be a reflection by the market of the inherent risk in loaning money to a particular borrower. When interest rates are allowed to "normalize," that is when central banks do not suppress rates, market forces have proven to do a very effective job of assessing the risk and reward elements of loans. Financially secure borrowers receive relatively low interest rates (although never zero!) while more speculative loans are made at significantly higher rates. The problem with living in a world of financial repression, where central banks have kept rates artificially low for over seven straight years, is that it distorts borrowing everywhere, allowing even the financially fragile to borrow at unprecedentedly low interest rates.

The result of this is "yield starvation," whereby investors feel forced, in a zero and increasingly negative interest rate world, to go out on the risk curve, bidding up the prices of these riskier assets. What this does is both drive up stock prices (and who doesn't want to see Financial Bubble Episode III: Revenge of US Equities?) as well as drive down yields on instruments like riskier sovereign debt and high-yield corporate debt.

While this is a fantastic deal for spendthrift governments and corporations with speculative futures, it means that bond investors are now shouldering far greater risk while obtaining significantly lower returns than has ever been the case before.

A final word about bonds. There are a few lucky nations in the EU whose bonds, I would argue, fall into both camps. Recently, Italian and Spanish 10-year government bonds were yielding 1.23% and 1.14%, respectively, which is below the rate of US 10-year Treasuries! Now these are two of the most indebted countries in the EU with moribund growth prospects, bloated public sectors and rapidly aging populations. Prior to joining the Eurozone it was not uncommon for Spain to pay approximately *ten times* the rate it currently pays to borrow. It is only because of the perception that Germany will essentially stand at the ready to serve as a financial backstop of last resort should one or both of these countries slip into insolvency, *ala* Greece, that their bond rates are anywhere close to being this low.

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The problem with that assessment is the converse to what we saw during the Global Financial Crisis when certain financial institutions were deemed to be "too big to fail" and were bailed out (a moral outrage, in my opinion). For if Italy, with an economy and debt burdens well in excess of five times those of Greece, were to stop paying its debt obligations, it may well be "too big to bail."

To conclude the financial tour of bonds, I came across a sober assessment of the prospects for government bonds from a very insightful source. Swiss Re is one of the two biggest reinsurance companies in the world, sporting a giant market cap of more than $35 billion. The reinsurance industry essentially acts as the insurance companies for insurance companies, allowing them to offload risk. Accordingly, I would posit that there is no better market sector in the world than the reinsurance industry in terms of assessing and managing risk.

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Recently Guido Fuerer, Swiss Re's chief investment officer, commented that the ECB has turned government bonds into one of the **riskiest** asset classes in the world. He noted that with, "government bonds, you're not adequately compensated for the risk you are taking," and went on to say, "if you're looking for a bubble, here you go." Financial writer and prodigious intellect James Grant has described investing in bonds at this time as a way to obtain "return free risk." I could not agree more strongly, and as such I would continue to have no more than 5% of one's portfolio in bonds.

US Stocks — Beware The Siren Call Of TINA!

Stock bulls here in the States have taken a great deal of solace from the fact that while other developed markets around the globe have seen meaningful corrections, US equity markets are trading at all-time highs. Apologists for US stocks go on to note that compared to the rest of the developed world the US continues to have the best growth prospects, as well as the single most dynamic sector in the world – US tech. Furthermore, with the aforementioned crash of bond yields everywhere, it is not as though investors have attractive prospects in the universe of bonds.

All of this has led to a popular refrain among investment advisors and many pundits: ongoing and robust US stock gains should be expected as "there is no alternative" (TINA) to owning US stocks as an investor. This is a *very* specious argument for buying (or continuing to hold) US stocks for two reasons.

First, the very logic of TINA is flawed. Essentially bulls argue that US stocks have risen to such dizzying heights because investors are crowding into the trade due to poor prospects everywhere else. But by bidding up US stocks well in excess of levels they would be trading at were there better alternative investments, this in no way guarantees that *future* US stock returns will continue to be robust. In fact, I would argue that common sense says the exact opposite is true.

Stock gains are essentially being *pulled forward* by global investors who see the US and companies residing therein as the "least dirty shirt." But by pulling these gains forward, they are actually reducing *future* expected gains, making meaningful longer-term real returns all the more difficult to achieve. It is similar to the old adage when it comes to investing, "the difference between a great company and a great stock is price." The same is true for specific asset markets in general. The US may very well be the most attractive equity market in the developed world, but even assuming that is true, its premium to other markets fully reflects this and then some.

The second logical problem with TINA as a basis for expecting ongoing gains in US stocks is that simply because US equity markets look more attractive than other investments does not mean they look *objectively* good. This is a critical point for anyone trying to plan for such things as retirement or educating their kids by attempting to estimate future gains from their investments. If indeed bonds are going to offer next to no inflation-adjusted returns (or possibly negative returns should inflation pick up) in the coming decade, US stocks might very well offer better returns. But "better" might mean low single-digit returns between now and the middle of the 2020's with the prospect of significant downside movements in between.

Money manager John Hussman continues to provide compelling analysis indicating that 10-12 year total returns for US stocks will very likely fail to even keep up with today's inflation rate. This is based upon extremely comprehensive data going back more than seventy-years using measurements of current US stock values that have had a 93% correlation to future returns. His work, maybe more than any other of which I am aware, makes crystal clear the fact that the primary determinant of long-term investing returns is not based upon market sentiment, trend following or technical analysis, but rather the price of the asset in question. Buying stocks when they are cheap has *always* led to superior returns over the subsequent 10-15 years while buying them when they are expensive has *always* led to poor returns over the next 10-15 years.

Ignored during the relief rally in US stocks since Brexit is the fact that fundamentals for US stocks continue to deteriorate. It is not just that year-over-year combined S&P 500 company profits per share declined at an 11%+ clip as of Q1 2016. *Revenues* are actually declining year-over-year as well. According to Fred Hickey, far from being a safe harbor, the tech sector is actually seeing its revenues fall about three times faster than the market as a whole.

So despite deteriorating fundamentals, both in the broad economy and for US corporations, we are trading right at all-time highs for US stocks. For anyone holding significant amounts of US equities, it is worth noting that at the end of 2007, the P/E ratio for the S&P 500 was roughly 21.5. From there stocks declined **more than 50%** over the next fifteen months before beginning their seven-year ascent to present levels. Today the P/E ratio for the S&P 500 is fully **15% higher** at nearly 25. The only non-recessionary times in which the S&P 500's P/E ratio was this high was during the tech bubble era of the late 1990's and early 2000's. Not surprisingly, subsequent 10-15 year returns were abysmal. To expect anything different this time would be to eschew reason, history and sound analysis.

I would continue to underweight equities, and especially US stocks. US small- and mid-cap growth stocks appear the most precarious, as the median US stock is as overvalued as ever has been the case, and growth stocks have uncharacteristically outperformed value stocks for most of the last seven years. Emerging market stocks up until this year have underperformed rather dramatically for some time. They appear to be priced much more attractively than developed market equites, and I suspect value stocks will also outperform in emerging markets.

Precious Metals Are Shinning Once Again

When I last discussed portfolio allocation issues a little over a year ago, I stressed that precious metals and mining stocks were trading at very low historical levels, and as such represented a very attractive investment opportunity. I specifically recommended overweighting precious metals and mining stocks from what I believe is a sound generic allocation of 15% of one's portfolio to 25% based upon the value proposition I thought the sector offered after enduring a grinding multi-year bear market. Twenty-five percent was larger than any other asset class in my recommended portfolio. At the time gold was under $1200 an ounce and silver was around $16.70 an ounce.

Investing in and dollar-cost averaging one's precious metals and mining positions back then and throughout 2015 proved to be a very profitable strategy. Gold is up 13% since then and silver has gained more than 20%. But that pales in comparison to what mining stocks have done. Large gold miners

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are up in excess of 55% while "junior miners" (exploration stocks) have nearly doubled in value.

One logical question to pose is whether now is the time to trim positions. After all, I just detailed how rich prices in US equities justifies avoiding them (or at least severely underweighting them). But unlike what is true for US equities, the recent rise in the price of gold, and particularly gold mining stocks, was from extremely depressed levels. Furthermore, there is probably not 5 in 100 investors that has any significant exposure in their portfolios to gold. Gold is thus still unloved and under-owned.

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But there is another compelling reason to own precious metals, and particularly gold, even apart from their attractive prices. For most of the last 100 years, gold has tracked the general rise or fall in money supply rather closely. As central bankers continue to flood the world with paper money, precious metals stand to benefit. As James Grant has noted, "gold is the reciprocal of faith in central banks."

Perhaps bond guru Jeffrey Gundlach summed it up best when discussing how holding gold makes sense by saying that, "gold is a play in a bear market in confidence." If nothing else, since most people's investment portfolios contain assets that generally need such confidence among investors to remain high in order to profit, I believe gold continues to be one of the best means of diversification. As such, maintaining 20-25% of one's portfolio in precious metals and mining stocks strikes me as a way to obtain an insurance policy against future economic dislocation whereby one would likely *receive* premium payments via potential capital appreciation.

Putting It All Together: When (Recent) Past Is Not Prologue

As an investor, I have seen and personally profited from the bursting of two major asset bubbles. Quite frankly the challenge is not in identifying their existence. Rather it is weathering the way in which asset markets can become completely untethered to any economic fundamental reality, existing in a state that defies financial gravity, prior to the eventual bubble bursting. If there is one iron principle applicable to investing, it is reversion to the mean. Thus, it is not a question of whether US stocks and global bonds will unwind, it is a question of when. As a strategic, long-term investor, I have always maintained that it is better to simply avoid (or at least seriously underweight) expensive assets rather than trying to eke out the final gains and risk getting caught in a severe market downdraft. Brexit has done nothing substantial to change the fact that a traditional portfolio of 60% US stocks and 40% bonds will likely obtain very low single-digit returns over the next 10-12 years.

What Brexit has done is make manifest the deep fissures and overall fragility that are at the root of global financial markets. It may also hasten the demise of broader European economic integration, and perhaps even threaten the viability of the EU and/or the euro. In some ways Brexit may have been the best thing to have happened for bulls. By having what was seen as a dramatic and unexpected event for global markets turn out to be a non-event for financial markets here in the US within a couple of weeks after Brexit, it gives the appearance that markets are bullet-proof. As such, the realities of declining earnings and revenues, potentially insolvent European banks, universally weak growth and shrinking global trade can be conveniently ignored, at least for now. But as we saw in 2000 and again in 2007, while markets can ignore egregious overvaluations or even weak economic fundamentals for what can seem like an interminably long time, the "weighing machine" to which Benjamin Graham refers eventually asserts its hand, normalizing valuations at the cost of vaporizing huge sums of paper wealth.

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[*] Past results are not necessarily indicative of future results. You should carefully consider whether your financial condition permits you to participate in a commodity pool. In so doing, you should be aware that commodity interest trading can quickly lead to large losses as well as gains. Such trading losses can sharply reduce the net asset value of the pool and consequently the value of your interest in the pool. References to specific securities and issuers are for illustrative purposes only and are not intended to be, and should not be interpreted as, recommendations to purchase or sell such securities.

WHITMORE CAPITAL MANAGEMENT

About Whitmore Capital Management, LLC

Whitmore Capital Management, LLC was formed in 2012 to offer investors access to a proprietary foreign exchange investing program (the Fund, Whitmore Capital LP). This program focuses on cash currencies but may also include futures, forwards and currency options. The objective of the Fund is to achieve long-term returns superior to the Credit Suisse Hedge Fund Index.

At the very core of the investing program is a mathematical model developed by Mark Whitmore. This proprietary calculus for determining the "fair value" of exchange rates aims to identify long-term opportunities to profit from temporary currency market mispricing. The outcome of these quantitative analyses are supplemented by qualitative analyses of the circumstances surrounding each currency to determine the configuration of the portfolio itself. Finally, sentiment indicators are reviewed as an additional analytical overlay. Currencies traded for the Partnership's account may include, but are not limited to, pairs of the following currencies: AUD, CAD, CHF, CNH, CZK, DKK, EUR, GBP, HKD, HUF, ILS, JPY, MXN, NOK, NZD, PLN, RUB, SEK, SGD, TRY, USD, ZAR.

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