VERE GLOBAL
PRIVATE ASSET MANAGEMENT

Special Report – May 2016

Quote of the Month: *"The Years Teach Much That The Days Never Know"* – **Ralph Emerson**

This monthly research report is intended to provide both Vere Global Wealth Management proprietary research along with third-party raw research we believe are most relevant to the markets' conditions and economic environment. We trust you find our information instructive and useful. Feel free to contact us.

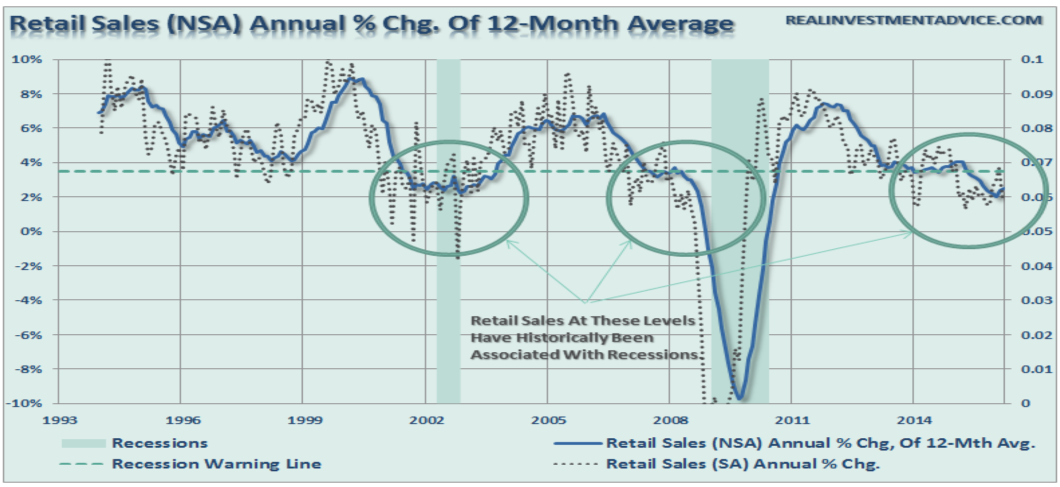
High Points:

- *The Global Economy (and US) is showing signs of slowing, maybe even a potential recession next year.*
- *Stock valuations are high and are being supported by stock buyback programs that are fueled by debt.*
- *$1.4 trillion in troubled European bank loans.*
- *Corporate earnings are falling, historically a good early indicator of recession.*
- *Record amounts of stimulus and 8 consecutive years of GDP below 3% - first time in history that has happened.*
- *Announced job lay-offs are accelerating, 35% increase in lay-offs from March to April and are 24% YOY.*
- *Railroad traffic is down 11% YOY and over 292 trains sit idle in Arizona desert.*

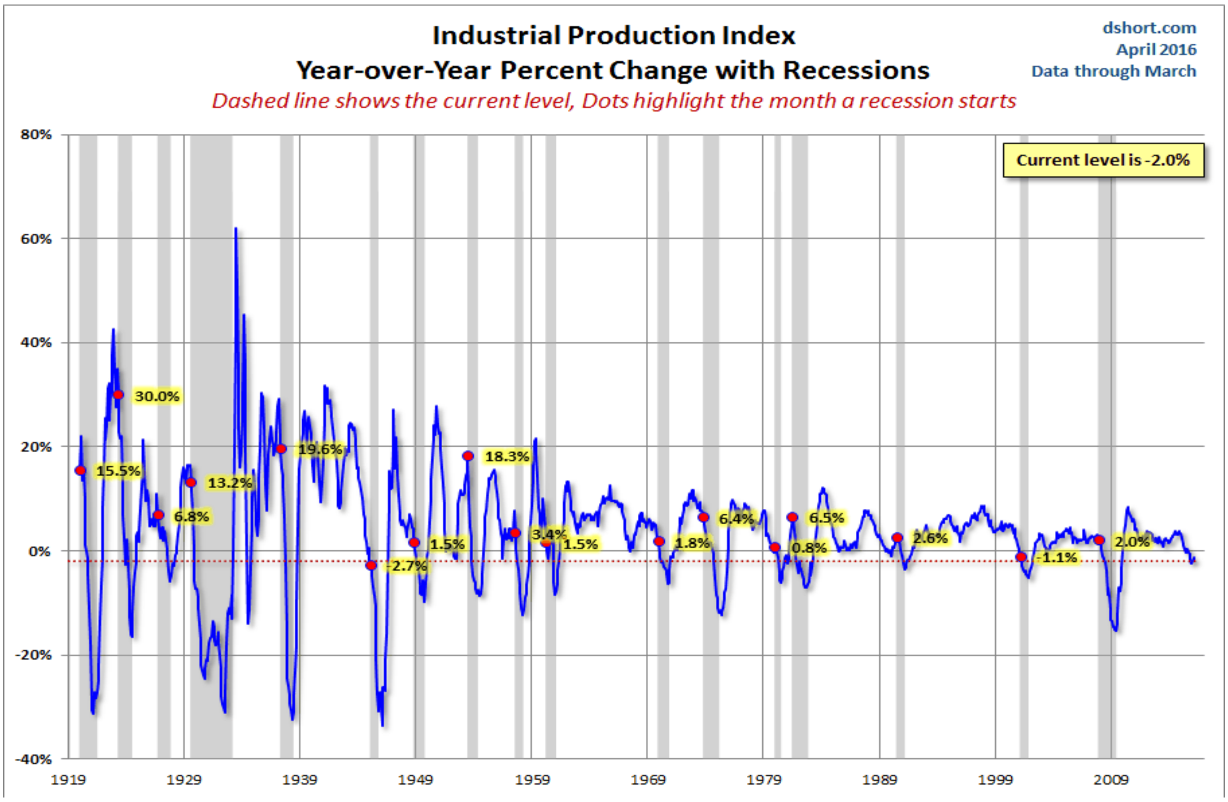
Our Take:

We decided to write this special report to shine some light on issues that for the most part are being ignored by many Wall Street analysts. These problems are a combination of slowing economic data across the board (globally as well as domestically), declining earnings, and the markets tendency to believe that the government will come to the rescue no matter how much risk firms take on. To drive the point home more, look at some recent events. Puerto Rico defaulted on its debt payment (it has $72 Billion in loans), Exxon just lost its AAA bond rating (the last time Exxon lost its AAA rating was in the 1935), corporate defaults are at their highest level since 2009. The list goes on and could get very lengthy. The point here is things are not as rosy as the Federal Reserve and the politicians would like you to believe. If the global economy was doing so well, why are so many countries going to negative interest rate policies and printing money to buy bonds? It is just a matter of time for their problems to become US problems. Below, we want to show some of the issues we see.

Retail Sales – Retail sales have historically been a good/early indicator to recessions. Notice on the cart below (solid blue line), retail sales now have dropped into the zone that foreshowed the 2002 and 2008 recessions. Retail sales contribute 40% to GDP and should not be ignored. Most recently, Aeropostale filed for bankruptcy on May 4, 2016.



Industrial Production: The chart below shows the year-over-year (YOY) percent change in Industrial Production since the series inception in 1919. The current level is lower than at the onset of 16 of the 17 recessions over this time fame of nearly a century. The only lower instance was at the start of the eight-month recession at the end of World War II.



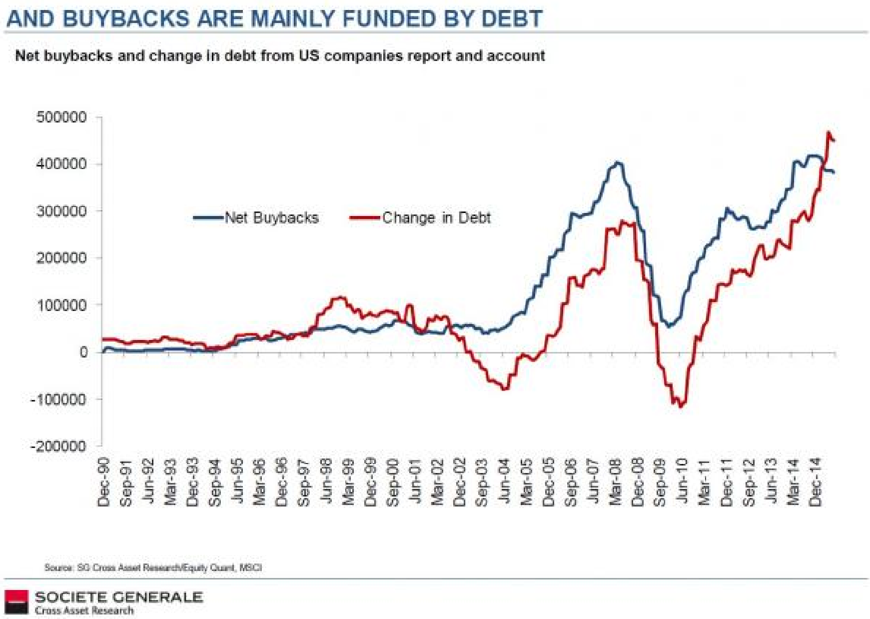
Factory Orders- In the last 60 years, the US economy has not suffered a 16-month continuous YOY drop in factory orders without being in recession. That is precisely what the US economy just did. Factory orders dropped for the 16th consecutive month YOY, after declining 1.7% from last month...

Source: Zero Hedge

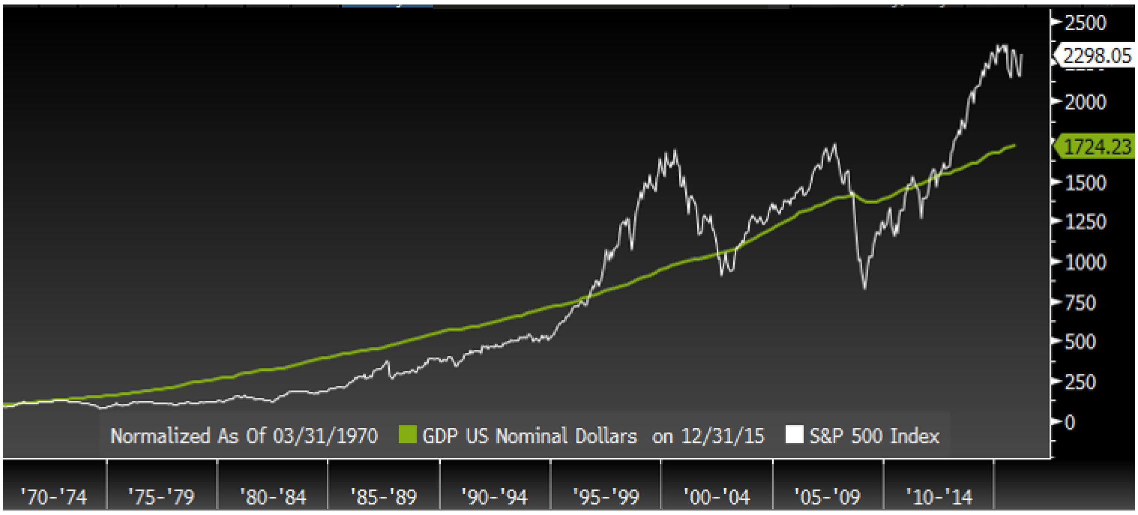
Inventory Build – The inventories of goods are rising (due to weak sales) another sign the consumer is slowly scaling back on purchases**.** Either consumers need to dramatically increase their purchases or companies need to stop producing goods. Even more to the point, this chart explain why firms like Aeropostale went bankrupt – consumers just weren't buying.

Source: Zero Hedge

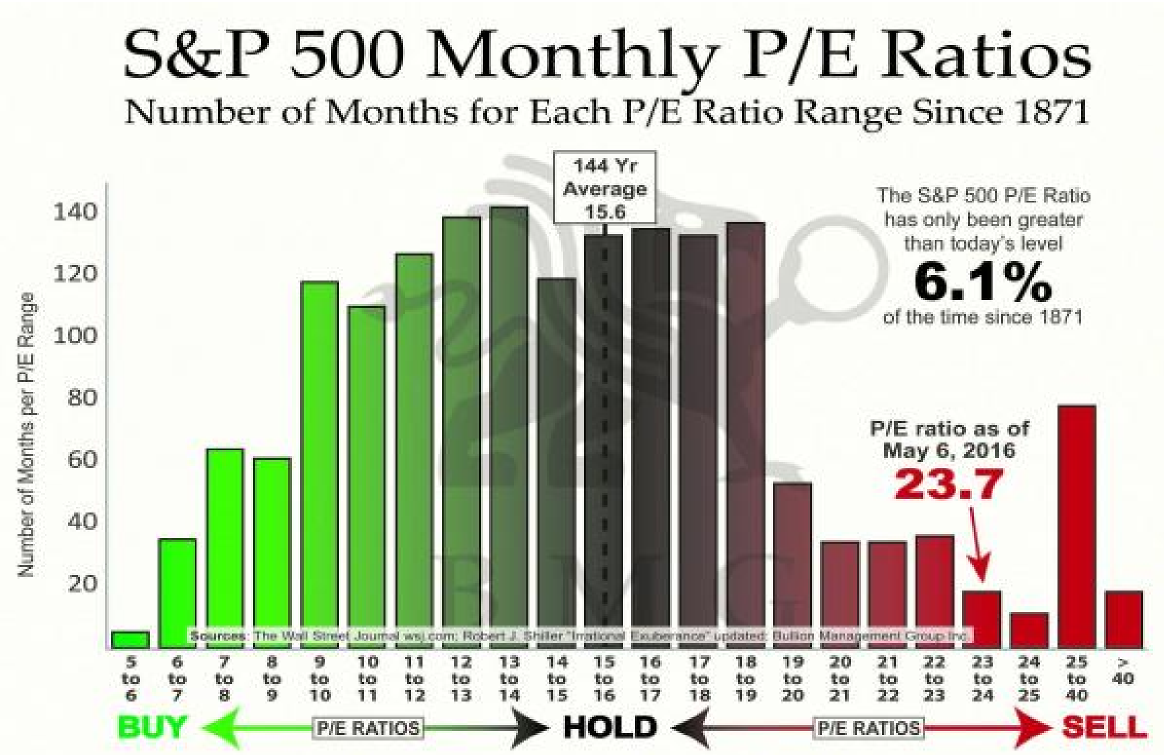
The Bull Market – The current rally over the last few years has been filled by stock buybacks, which in turn has been filed by debt and now firms have more debt than any other time in history. Notice that the stock buybacks are starting to slow, just like in 2007, but with one caveat – more debt!!



Stock Market Valuation – The solid green line is GDP compared to the value of the stock market. The idea is that the economy and stock market always revert back to each other. This indicator was made famous by Warren Buffet who uses it as well. Notice how much more the stock market has gotten ahead of GDP. Market valuations have been higher only 6% of the time since 1871(2nd graph).



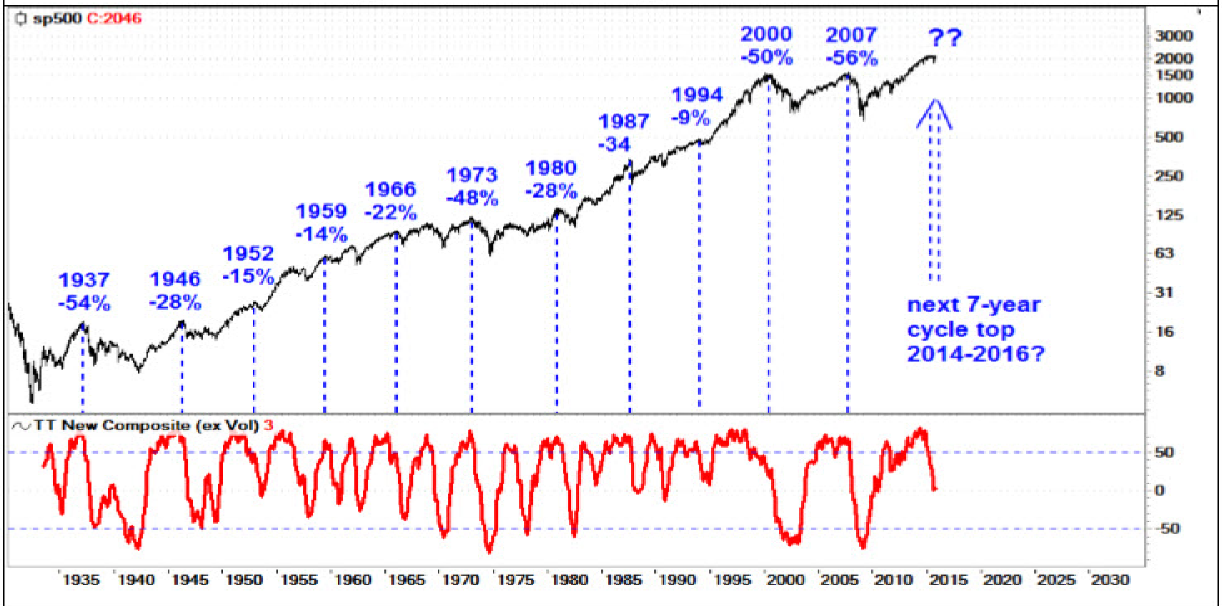
Source: Zero Hedge



Source: Burning Platform

Here's one of our favorite charts (if you truly believe numbers are the key to the universe). Notice that the market tends to have a market correction every 7 years. You could argue that this is 2016 and the chart would suggest 2014 would be the top. The S&P 500 is still trading at the levels it was at in 2014 and in February of this year it was trading at the same levels it was in 2013. It also interesting to note that the "Baby Boomers" entered their peak investment years in the early 80's by contributing to 401(k) plans, AKA the S&P 500. 2016 will mark the year that the first "Baby Boomers" are required to begin making their mandatory distributions from retirement accounts.

Chart 5.) S&P-500 Monthly Chart with 7-Year Cycle



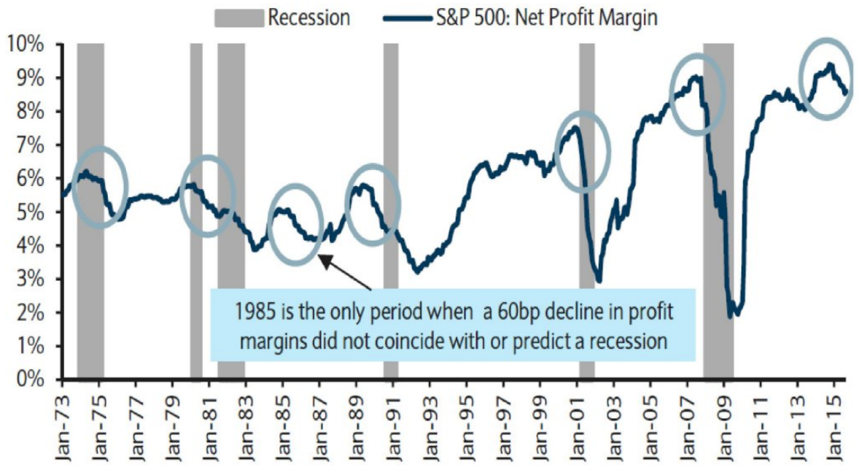
Source: UBS Technical Research

Corporate Profits – The chart below says it all. There has only been 1 occurrence where profit margins contracted 60 basis points without a recession. Analysts estimate earning will decline further in 2016. To be honest, a lot of that profit margin has been a result of commodities. However, commodities (copper, oil, iron) are the basic building blocks of a growing economy. That reinforces the idea that the global economy is entering dire straits.

DoubleLine

S&P 500 Net Profit Margin

January 1, 1973 through March 31, 2015



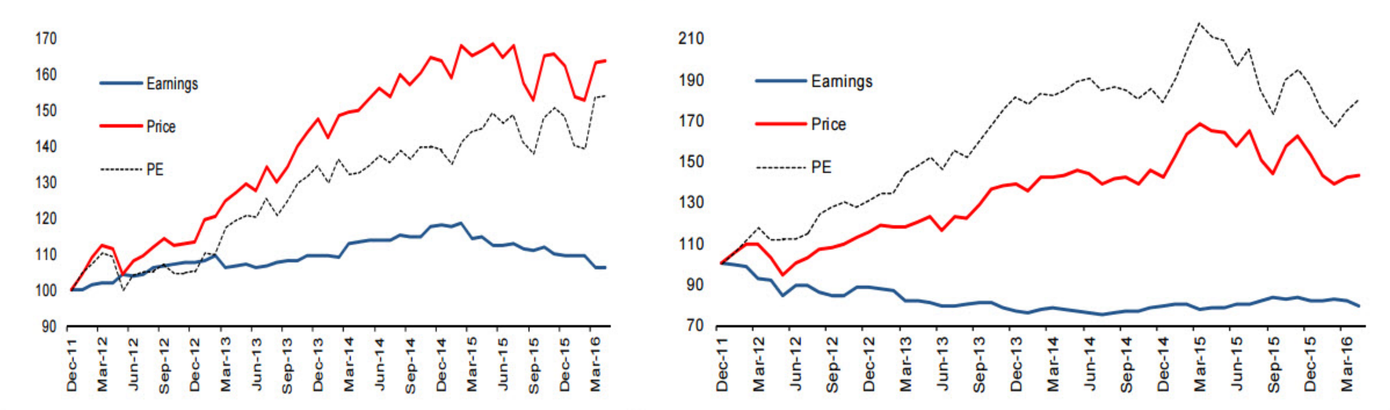
Source: Thomson Reuters, Barclays Research

Source: S&P 500 Index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. Bp = basis point. You cannot invest directly in an index.

1.12.16 Just Markets Webcast - 45

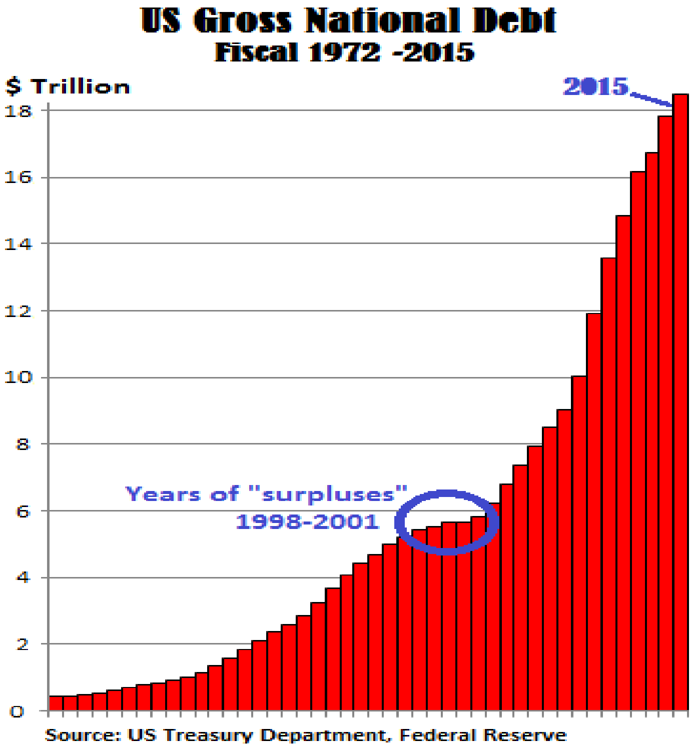
Notice that earnings (solid blue line) have been declining. However prices (solid red line) are going up making stocks more overvalued (dotted line) on average. As an owner, do you feel comfortable paying more for a company that it's making lower and lower profits? In Europe (left chart), it is worse.

US equity prices almost all driven by PE expansion… …..and more than all price rise driven by PE in the Eurozone!



Source: SG Quant

US Debt – We have over $19.2 trillion in debt, the interest on that debt adds an extra $700,000 every 40 seconds to the total. The $19.2 trillion does not include liabilities for Social Security or Medicare. Social Security and Medicare payments are about $1.8 Trillion.



Putting it into perspective - As you can see from all the information above (and there's a lot more that we did not cover) the economy is definitely slowing. That does not mean that we are in a recession, but if the trends do not change quickly, we expect the US economy to fall into a recession next year. Recessions in election years are rare, since politicians like to "cheerlead" how great things are. You hear a lot of politicians brag about we have had 84 months of positive economic growth, they fail to mention that that growth is the weakest 84 months of growth in US history or that unemployment has fallen to 5%, yet they forget to mention that the number is falling because a record number of people have stopped looking for jobs and are no longer classified as "unemployed". If we had to guess the most likely time frame for a recession will be 2017 since most recessions occur in the first 18 months of a new President's term.

Let us not forget that 84 months of weak economic growth has resulted in multiple QE programs (both here and abroad), record low interest rates, and record amounts of government spending. Economic growth has become so dismal in the last few months, people are forecasting the Fed to have to go negative on rates just like other countries. Some top money managers like Stanley Druckenmiller and Carl Icahn are getting out of stocks (FYI - Icahn has bet $4 billion of his personal money that the stock market will collapse). We do not want to hit the panic button because we feel like we have some time, but at the same time we do not want to get caught with 200 million other people trying to exit the door at the same time when they hear the magic words "FIRE"! Based on history, this will end poorly at some point in the near future.

The question does come up about what would change our view. There are a few things that the government could do, but most of these tactics would be short-term in nature. The only long-term viable option would be to pass a bill in congress that cut corporate taxes, but those cuts would only apply to companies that used a majority of the tax saving to hire new employees. Additionally, the US Government would have to pursue a balanced budget law, but both those options are unlikely since the country is becoming much divided. Below are some of the steps we are going to be taking in the next few weeks.

Conservative Portfolio – The model currently holds approximately 80% in bonds and 20% in dividend paying equites. We feel this is good allocation and the only major change will be an increase in longer dated bonds. Long-term bonds (especially US bonds) do very well during recessions/market sell-offs.

Moderate Portfolio – Normally this model holds a 40% bond, 60% equity allocation. We plan on increasing long-short exposure and increasing bond exposure to long-term issues. We have already started increasing cash in these portfolios and plan to hold above average levels. That cash will be re-deployed once we see a better risk/reward environment.

Growth Portfolio – This strategy is a little more aggressive due to his 80% weighting to "growth" stocks and small-caps. Over the next several weeks we will be increasing bond maturities and moving away from "growth" stocks to "value" stocks. Growth stocks rely on a growing economy whereas value stocks tend to pay dividends. Also, we will be increasing cash.

All Equity Portfolio – This has 100% equity exposure. We will raise some cash, but clients wanted this strategy to remain more invested at all times. The allocation holds an above average exposure to small-caps and we do plan on reducing that and adding large-caps.

Because The Future Is Not What It Used To Be