IdahoTrust

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WealthManagement

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Market Insights

A periodic newsletter from Idaho Trust

The initial reaction to the news that the United Kingdom voted to leave the European Union was a surprise which led to volatility in the financial markets. One major challenge going forward is the economic uncertainty surrounding this unprecedented decision. Trade and financial agreements will have to be renegotiated as the UK completely removes itself from the European Union. This process could take at least two years and some believe it may take as long as a decade until the entire process is finalized.

The European Union

In a late June referendum, voters in the United Kingdom (UK) chose to leave the European Union (EU). The UK has been a very important member of the 28-country European Union. The debate over whether the UK would stay or leave (which became known as Brexit) has been going on for quite some time as many citizens questioned the benefits of EU membership. The British Prime Minister, David Cameron, fulfilled an election promise and put the issue to a referendum even though he was a strong proponent of the UK remaining in the EU.

Most observers thought that the UK would ultimately decide to remain in the EU, which made the vote to leave a huge surprise. After the results were announced, global stocks fell sharply. The UK currency experienced a sharp decline and the British Prime Minister said he would resign his position.

Idaho Trust Bank offers total wealth solutions including its LifeNeeds™ investing process. The LifeNeeds™ investment process utilizes proven strategies and techniques delivered by a highly trained staff of wealth management professionals.

LifeNeeds™ wealth management accounts feature optimized asset allocations, robust security screening and Idaho Trust's unique TacticLogic™ investment process. All of which are tailored to our clients' unique financial needs.

The decision to leave will have a significant global economic impact, but it will take considerable time before that impact is fully felt. In the meantime, uncertainty will persist. Britain will start working out the terms of its exit with the other members of the EU. It could take a long time to work through the mechanics of this process as the UK is the first country to leave the EU.

The results of the referendum will be incorporated into an Act of Parliament in the UK. Under the terms of the Lisbon Treaty (part of the EU's governing framework), the United Kingdom will then give formal notice to the EU after which negotiations will begin on the actual exit terms. These negotiations can span two years and many believe that it may take up to a decade for final resolutions.

The UK Economy

The economic impact of how Brexit will affect the UK economy is a major unknown at this point. A key assumption in any Brexit scenario is what will happen to trade agreements. The EU is the United Kingdom's largest trading partner, receiving about half of all UK exports. Upon leaving the union, the United Kingdom will lose its automatic right to the favorable trade terms that EU membership bestows.

The International Monetary Fund (IMF) projects that UK gross domestic product (GDP) could drop more than 1% by 2021 under its most favorable scenario, which assumes the United Kingdom will retain access to the EU market. If the UK receives unfavorable terms, the IMF projects that GDP could drop by more than 4%.

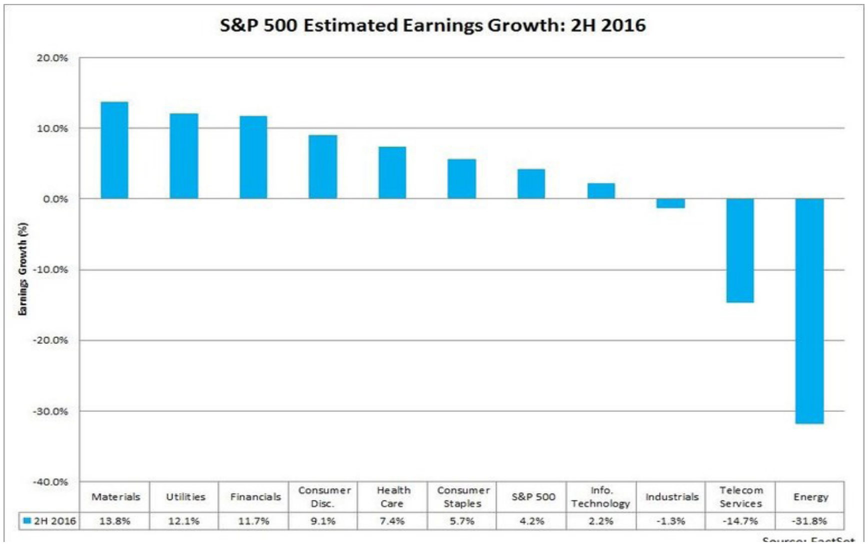
Most economists are calling for a slowdown in growth in the UK and Eurozone, both of which suffered from very slow growth before the vote. Over the next couple of years, the UK will have to re-write laws and trade agreements, which could stifle business investment for the foreseeable future. It may also cause similar movements in other parts of Europe which would create another layer of uncertainty. In general, uncertainty is bad for confidence, which is a big reason why markets reacted negatively to the development. Concern about Brexit has already led to a slowdown in business activity. Less favorable trade terms could also discourage foreign investment in the United Kingdom by firms that might otherwise seek a UK presence to access European customers.

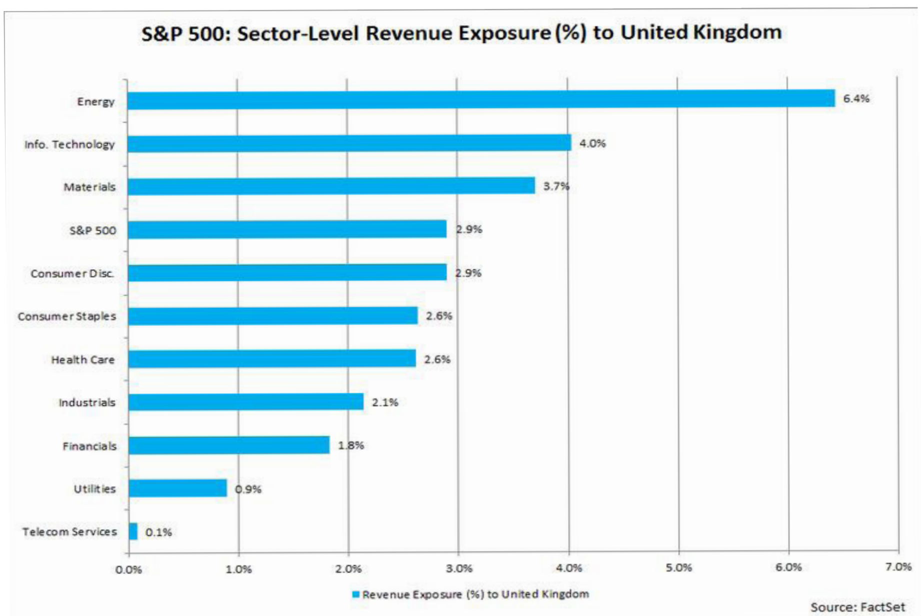
Corporate Profits

Although the final tally is not in for the second quarter, corporate earnings are expected to fall which would make five quarters in a row of earnings declines. Analysts currently expect the S&P 500 index to report a year-over-year reduction in earnings of 5.2% in 2Q. However, current exceptions are that earnings will rebound in the second half of 2016. Earnings are expected to expand by 4.2% in the second half of this year. Most of this earnings growth is projected to occur in the final quarter of the year. The sectors that are expected to experience the strongest growth are: Materials, Utilities, and

Financials. Three groups are projected to report profit declines, led by Energy.

The exit of the UK from the EU will likely have some negative near-term impact on profits. It is estimated that the aggregate revenue exposure of the S&P 500 to the United Kingdom is 2.9%. This is the third highest country-level revenue exposure for the index, trailing only the United States (68.8%) and China (4.9%).





Conclusion

The decision of UK voters to leave the EU will have a significant impact on the UK and European economies, with global implications. These impacts will likely take years for the effects to be fully understood. The most immediate ramifications will be continued uncertainty and political change in the United Kingdom. Given that it may take several years for the specifics of Brexit to play out, and markets may be volatile as the plans take shape. We recommend the best protection for investors is to hold a well-diversified portfolio across all major asset classes and regions. The major impact in the United States is likely a push back in the timing of any interest rate increase by the Federal Reserve Bank, as a stronger dollar will dampen inflation and hold back exports, and lower global growth will pressure the U.S. economy. The likelihood of an interest rate increase in the fall has dropped significantly.

S&P 500 Index

3 Month	1.81%
Year-to-Date	3.84%
1 Year	3.24%
3 Year	11.44%
5 Year	11.76%

MSCI EAFE Net Index

3 Month	0.69%
Year-to-Date	-4.42%
1 Year	-10.83%
3 Year	1.71%
5 Year	1.58%

Barclays Aggregate Bond Index

3 Month	2.26%
Year-to-Date	5.31%
1 Year	6.41%
3 Year	4.04%
5 Year	3.79%

As of 6.30.2016

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