CRIBSTONE
CAPITAL MANAGEMENT

# First Quarter Newsletter

April 5, 2016

We're happy as anyone that's it's officially spring. But what happened to winter? We're not used to this in Maine. Indeed, most of us hardly if at all got our favorite winter activities in these past months, whether it be it skiing, snowshoeing, ice fishing or snowmobiling.

Likewise, while we are all relieved to see the U.S. stock market end the first quarter of 2016 in positive territory (albeit barely) and recover from its February low, we take pause in recognizing that performance for stocks generally has been anything but typical. The market peaked almost a year ago and since reaching their respective highs over the past 52 weeks, all but nine stocks in the S&P 500 Index are still in negative territory. Nearly three-quarters of stocks in the index are down at least 5% while close to one-third are down 20% or more. Thankfully, this is not a common occurrence.

## A Cautious Spring in Our Step

We'd like to be able to say that we think the worst of the stock market volatility is behind us. While we certainly see reasons to be cheerful, there are enough uncertainties for us to remain somewhat cautious in the near term toward our allocation to stocks. Indeed, in a market that is very event and data driven (hence the volatility), there are plenty of issues that can cause both a positive and negative reaction. Equities should provide very attractive returns over the long term, but we pay very close attention to risk management in the short term as well. Having a little extra cash on hand temporarily allows us to take advantage of that volatility and use it as an opportunity to make great investments at more attractive prices.

## Data and Events are in the Driver's Seat

- *The US economy has been on thin ice until recently*: The quarter just passed was anything but stellar. We expect first quarter GDP to show below 1% growth when it's reported in late April. However, there are encouraging signs that conditions are slowly improving again. Recent data on employment, the consumer, and the manufacturing sector have been better than expected. The housing industry is particularly strong, and shows no signs of slowing thanks to tight inventories and low interest rates. In addition, in contrast to last year when strength in the US dollar provided a significant headwind to earnings of US companies, we are starting to see a gradual reversal as the trade weighted dollar index is down over 2% so far this year. If this trend continues, it could provide a boost to earnings growth later this year.

- *Oil prices have rebounded for now*: Typically, lower oil prices are good for the economy, but when they collapse as they have over the last 18 months, it's a different story. As we have written before, this has unquestionably contributed to the volatility in stocks as fears of bankruptcies and global recession spread. But since reaching their low of about $27 in February (down from $100!), oil prices have rebounded over 45% to close to $40. Trying to predict the price of oil is a fool's errand. Yet it's reasonable to conclude that the stabilization in the price, even if it's at levels below their old highs, should be a positive for stocks. Unfortunately, we don't have a lot of faith that this recent rally in oil will hold.

- *China will continue to weigh on the global economy*: The government is attempting to engineer a smooth transition from an economy driven by an infrastructure boom to one that relies more on consumer spending on goods and services. It will take time before the consumer side of the equation will be able to completely offset a slowdown in the rust belt. As a result, pressure on commodities and growth in the countries that produce them, such as other emerging markets, may continue. Additionally, although the recent decline in the U.S. dollar has provided a temporary reprieve from a weakening yuan, the risk remains that a sharp devaluation could send a shock across global markets as Chinese growth declines.

- *Stateside questions loom large*: Let us not forget two other big issues we have to contend with in the U.S: Federal Reserve interest rate policy and the Presidential election. When the Fed raised rates in December, Chairman Janet Yellen suggested that four rate hikes were on the table for 2016. She's since backed down from that assumption given the uncertainties in the global economy mentioned above. Even so, the Fed seems determined to raise rates, and when that happens, the markets will likely react. As far as the election goes, we can't and won't predict an outcome or what impact it may have on financial markets, but the uncertainty remains a risk.

**Bonds are beautiful**

Fixed income securities may be boring to some, but they've stolen the show this year. The Barclays U.S. Aggregate Bond Market Index, a broad measure of the fixed income market, returned over 3% in the first quarter, leaving stocks in the dust. Slower economic growth in the U.S. and higher risks perceived in overseas markets have kept rates lower and demand for US Treasuries higher. Based on the Fed's recent commentary and headwinds for global growth, we don't see rates moving substantially higher for the remainder of this year. Our view is that inflation will remain contained, and we have been carefully investing a bit further out in maturity schedules to fetch higher yields. As always, we try to match maturities with cash flow needs for all accounts, which limits our interest rate risk. In addition, we continue to look at other securities and asset classes in order to provide better yields and manage risk.

**Tax Time Tips from Cribstone Capital Management**

Along with spring comes taxes, and we're here to help. Please don't hesitate to contact us if you need any questions answered about your taxes, forms, or any other issues. It's not often we get some reprieve from the Internal Revenue Service, but due to a holiday in the nation's capital, this year's filing deadline for 2015 taxes isn't until Monday, April 18th.

While many of you may have already taken care of your taxes or met with your accountant to do so, we wanted to alert you to a few tips:

- IRA contributions for 2015:

  - There is still time to make contributions to your Traditional or Roth IRA accounts. All checks need to be postmarked by April 18th and we recommend that rather than mailing them to us, please mail these directly to Schwab. Also please be sure these checks clearly indicate the year to which the contribution applies and your account number. The address for Schwab is listed below:

    **US Mail**
    Charles Schwab & Co., Inc.
    P.O. Box 982603
    El Paso, TX 79998-2603

    **Overnight Mail**
    Charles Schwab & Co., Inc.
    1945 Northwestern Drive
    El Paso, TX 79912-1108

- IRS tax payment options:

  - Electronic Federal Tax Payment System: This is a service offered on the IRS website that allows you to have tax payments drawn directly from your Schwab account. There is a one-day processing time.

  - Checks: You can authorize Schwab to issue a check made payable directly to the taxing authority. Schwab sends those checks via the United Parcel Service. Overnight cutoff is 2:00 pm daily beginning April 1st through April 18th.

  - Schwab will offer a daily IRS Bulk Overnight shipment of checks payable to the IRS or U.S. Treasury as long as they are not asked to include a tax voucher. This is free of charge as long as a tax voucher is not included. A tracking number will be available.

With warm regards,

Scott Upham, Managing Partner

Odette S. Galli, Partner

John D. Duffy, Partner