SOUND INCOME STRATEGIES

January 2016

Markets*:

Index	Month / Year to Date
DOW Jones:	-5.38%
S&P 500:	-4.96%
NASDAQ:	7.81%

We believed 2015 was kind of a bumpy ride for markets, but it looks like 2016 might be even rougher! Financial markets in China were roiled earlier this month and the Hang Seng, Shanghai and Shenzhen finished the month down -10.2%, -22.6%, and -26.8%. This massive sell-off, which caused several days of circuit breakers to shut down their markets, has affected global markets more in sympathy than due to a direct relationship. At the risk of over simplifying a complex system, we'll state the Communist government (China, not ours) only allows foreigners to own about 1.5% of all shares in their markets. So a direct relationship probably isn't too material, but if their economic growth really is slowing, which we believe it is, then there will be a ripple effect on the countries that sell to China. This will especially be the case for commodity sellers, and this does have a direct relationship to many industrial countries, including the U.S.

Commodities, such as oil, which has been in the news lately, have a serious supply/demand imbalance. This over supply versus slowing demand is **very deflationary; asset prices fall.** China slowing down means further demand weakness amid a supply glut. Sectors within energy, such as exploration and production, have been borrowing a lot of capital the last 5 years and selling oil at $75 to $100 per barrel. Now they still have the debt and can only sell their oil at around $32 per barrel and this is affecting many energy firms and energy-related firms very negatively.

For oil/natural gas prices, China's economic slowdown, coupled with China's devaluation of their currency to boost their exports, should put the Federal Reserve on hold for increasing rates further during the first half of 2016, if at all. These deflationary pressures will make it difficult for the Federal Reserve to stick to their plan of increasing interest rates when the rest of the world is cutting rates to deal with weakening deflationary economies.

In fact, the Fed talk has already become a little more dovish this month, and with China devaluing their currency, other countries will depreciate in comparison to the U.S. dollar as well. The 10-year U.S. Treasury bond increased by 3.2% during the month, as the yield fell from 2.27% down to 1.92%. In any case, we expected the markets to remain volatile and we'll continue looking for opportunities to purchase income generating assets at a discount.

**Reported for the month of January 2016.*