Hughes Investment Advisory Services LLC

July 8, 2016

Dear Clients and Investors,

I hope that everyone had a good 4th of July and you are enjoying these early summer days. The S&P 500 gained 2.4% for the 2nd quarter and is now up 3.8% YTD 2016. The 2nd quarter was a relatively quiet one for the markets – we'll take that for a change! Today, as I write this quarterly letter the equity market is rallying on a surprisingly positive June employment report, adding 287K new jobs. Stocks are now less than 1% away from a new all-time high on the S&P 500. As I wrote earlier this year, I believe that the S&P 500 will surpass its old high sometime in 2016 and I'm sticking with my 10% full year rise for the S&P 500 in 2016.

What an unusual economic time we are experiencing right now. We are taught to never say "it is different this time" but in my long period of watching the economy and investing I have not seen a period with similar circumstances. The biggest differences are Global and US interest rates. Other markets - equity, currency, and commodity are all within their historic ranges but not the global debt markets. We now have negative, yes negative, interest rates in many debt markets around the world. Here in the US we still have positive but increasingly lower interest rates but negative rates prevail in Japan and many European government bond markets. What do these negative/low interest rates mean for the US economy and our investments? This question is the most important one that investors face now and for the period ahead. How these low and negative rates effect different investment classes will be critical to investment portfolio performance in the future.

In uncertain times there is a global flight to safety, and now, more than ever, when there is a lot of chaos about, overseas investors want the liquidity, transparency and safety of U.S, capital markets. The global reliance on the U.S. as a haven helps make my case for domestic stocks and why they will be more stable than many think during the next recession. Take, for example the latest BREXIT scare, we saw this flight to dollar safety and the US equity markets have already recovered to a higher level than before the BREXIT vote! The U.S. is the biggest, safest, and most liquid pool of capital available to investors around the globe and we will continue to see funds flowing into the U.S.

So what are the chances of a U.S. recession? Lets take a look at my Big 3 economic indicators: Yield Curve, Auto Sales and the Housing Market. The further we get along in this expansion we are, by default. getting closer to the next recession. I have recently seen investment bank models showing a 60% and 38% chance that the US could enter a recession in the next 12 months. I don't disagree with these assessments. I carefully monitor the Yield Curve, which is suggesting the highest likelihood of a recession since the financial crisis in 2008. The difference between the three-month and 10-year U.S. Treasury yields has been narrowing sharply in recent months and is getting closer to being inverted suggesting a slowdown and or recession on the horizon. Conversely, the value of the yield-curve as a recession indicator may not be what it once was due to the low level of short-term rates and huge demand for U.S. bonds coming from overseas as referenced in the above paragraph.

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Auto sales remain strong thanks to historically low interest rates and the ageing of the overall US auto fleet. Current estimates are for 17.5 million US auto sales for 2016, which is a very healthy, and potentially new record number for the auto industry. By comparison, the record was set in 2015 at 17.47 million unit sales. The housing market remains a bright spot as well with sales of new and existing homes remaining healthy as we head into the second half of 2016 supported by low interest rates and pent up demand.

2016 seems to be a year of falling uncertainty. The year began with the business press trying to convince us that low oil prices, China, the Yuan, Brexit, the US elections and now the Italian banks would somehow derail the economy and the markets. As I expected, so far none of these have done much harm. My response: Low oil prices are good for the economy. China has been slowing for 5 years and their currency the Yuan has weakened at our request. Brexit is probably a non-event or quite possibly a long term positive as countries break away from the European socialist model. The Italian banks are another legacy problem with little or no effect on future economic activity, these banks have needed a bailout since 2008 and if it finally happens it will mark the end of the crisis not the beginning. As far as the US election: the uncertainty always exists as we head into this phase of the election cycle and it's a fact that the 8th year of a two term presidency is usually not a good one for the markets so I would call that a known small negative factor as we head into the Fall.

Ultimately I believe that the Bull market continues and whether full-year returns are great or just ok, owning equities, especially dividend-paying stocks is still the right decision. I'm expecting that investors should soon see plenty to cheer as the above-described "phantom" problems disappear. The world continues to grow and corporate profits will follow. Investors are not euphoric or complacent and expectations remain too low.

As mentioned last quarter I have been checking to see if the ISM Manufacturing index would move back above 50 and it has with a June reading of 53.2.

At this time I continue to favor large-cap, dividend paying, multi-national companies with strong balance sheets. Due to the strong rally in dividend/income stocks I am now finding new opportunities in the growth sector rather than value/dividend sectors. Select multi-nationals in Europe that fit into the same category, as our US companies are also attractive. Internationally, I'm finding only select economies in Asia attractive on a risk/reward basis. Risk/Reward continues to favor equities over fixed income. Select MLP's, convertible/corporate and municipal bonds continue to look good as income producers.

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