HARBOR VIEWS

HARBOR ADVISORY QUARTERLY NEWSLETTER

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HARBOR ADVISORY

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A LOOK INSIDE HARBOR VIEWS

- *Thoughts on the Economy* – Expect…full year 2016 GDP growth closer to the 2% rate.
- *Our View of the Financial Markets* – After the Brexit vote…European shares outperformance in 2016 is optimistic at best.

LATEST NEWS FROM HARBOR ADVISORY

- You can visit us at: www.harboradvisory.com. Take a look and let us know your feedback.
- Jack De Gan continues to make news with his regular guest appearances on CNBC's top rated financial shows "Squawk Box", "The Call", "Closing Bell" and on Bloomberg TV, Fox Business News and National Public Radio.

THOUGHTS ON THE ECONOMY

The U.S. economy finished the first half of 2016 with a low GDP growth rate of 1% on an annualized basis. We continue to expect growth to pick up during the second half of the year with full year 2016 GDP growth closer to the 2% rate that has prevailed throughout the recovery from the credit crisis.

Our confidence in a slightly stronger rate of growth is based in part on the strength of consumer spending which continues to advance at a greater than 2% rate. This is driven by greater job growth than might be expected this late in the recovery.

The economy has produced an average of over 200,000 non-farm jobs per month all year. The private economy needs about 100,000 new jobs each month to hold the unemployment rate constant. The U-6 unemployment rate remains close to double digits as it includes discouraged and underemployed workers and the labor force participation rate is near an all-time low of 62.8%. Demographics certainly play a role as baby-boomers are retiring at a record rate but the skills gap has clearly forced many to exit the workforce altogether.

Business investment remains weak as the latest month shows investment is lower by .5% year over year. The lack of investment by businesses impairs productivity growth which in turn reduces potential GDP growth and longer term reduces the ability of corporations to grow margins and earnings.

Auto sales appear to have plateaued at about 1.75 million domestic units per year and housing starts are running at 1.1-1.2 million units annually. There remains pent-up demand for both autos and new homes which will tend to extend the economic recovery.

We prefer not to put too much effort into trying to guess the effects of politics on the economy or on equity returns but Great Britain recently gave us an object lesson in why political events remain a risk. The Brits voted to exit the European Union (EU) after being a member of the common market for almost 50 years. The British pound quickly lost 12% of its value against the dollar and shares briefly sold off. We hope to see political events this fall in the U.S. provide less excitement!

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OUR VIEW OF THE FINANCIAL MARKETS

The U.S. equity markets are now running at a total rate of return consistent with our expectations of 6-8% for the full year. We expect volatility as the election approaches but we hope to end the year at these levels or better.

Our expectation that there would be reversion to the mean in emerging market shares seems to be playing out. Emerging market equities have more than doubled the return of U.S. equity indices year-to-date.

The European markets were taken by surprise as Great Britain voted to exit the EU and shares there have not yet fully recovered from the shock. We remain believers in a reversion to the mean with European shares but now believe our expectations of an outperformance in 2016 are optimistic at best.

Bond yields globally were driven even lower after the Brexit vote and more aggressive central bank easing. Returns on broad-based fixed income indices are running at mid-single digits year-to-date which is much above our expectations.

MONEY FUND UPDATE

The Federal laws governing money market funds are changing significantly in the near future. At Harbor we will be changing the money market fund selection within your accounts to one which only holds U.S. Treasury securities. This will allow the securities within your money market funds to be backed by the 'full faith and credit of the U.S. Treasury' as well as hold securities in the most liquid market in the world. These shares will continue to be priced at a fixed $1 per share with no fluctuation in value and have no exit fees or liquidity restrictions.

Many other funds that hold commercial paper or other securities will be priced in shares that can vary in value and could be subject to exit fees or 'gates' which can restrict the liquidity of the shares by imposing a waiting period to cash out shares in the fund.

This action by Harbor on your behalf reflects our desire to provide the highest level of capital preservation and availability for your cash balances.

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