

***Virtus Vital Signs, July 2016***  
**Market Insights from Joe Terranova, Chief Market Strategist**  
**Interview conducted on June 29, 2016**  
**Transcript edited for clarity**

*Brian Portnoy: Welcome to Virtus Vital Signs for the month of July 2016. I am Brian Portnoy, Director of Investment Education at Virtus Investment Partners and always I have my friend and colleague Senior Managing Director and Chief Market Strategist Joe Terranova. Hi, Joe.*

Joe Terranova: Good morning, Brian.

*Brian Portnoy: How are you?*

Joe Terranova: I am doing well. Markets are facing the turning point, midway point for the year, and I am excited for the second half.

*Brian Portnoy: Absolutely. No lack of news, and I think we can summarize recent events with one word: "Brexit." Please talk to us about your view on the implications of Brexit for number one, the macro environment – what does it mean for the economy, globally? And, secondly, how should investors be thinking about Brexit?*

Joe Terranova: I think bank credit analysts perfectly described the situation as it relates to the vote last Thursday evening. It was the capital markets' "Dewey vs. Truman" moment, and many including myself, expected for "Bremain" to be the condition. If you think about on the after-market on Thursday, S&P futures traded very close to their all-time highs.

It was more of a short-term phenomenon as it relates to trading. As it relates to investing, I do believe there's an impact, but first I think it is important to understand the conditions. I think the market caught a break so to speak, meaning the market was trading up at the highs. You had very strong bullish momentum, and that's been in place since February. The trend has been very strong. What has happened since Thursday is that trend has been neutralized. Historically markets do not shift from a bullish trend to a bearish trend. They go from a bullish trend to more of a consolidation sideways trend and then they determine, based on the fundamental and technical conditions in the marketplace, whether they will resume the bullish trend or whether a down trend will unfold.

I think where we are right now is back to what David Kostin at Goldman Sachs correctly identified as 'flat being the new up;' the market will consolidate, I would expect, over the coming summer months, and I think a lot of the elevated volatility that we witnessed surrounding last weekend – Friday and Monday's trading activity – that was a trading condition that was a lot of folks were positioned from the long side, neutralizing risk.

Overall, the fundamental impact of Brexit is not really clear to most. It will play out over time. It might put the United Kingdom in recession, but there is an opportunity if that does occur in Europe, and that would be for German equities, which have been out of favor this year, to become in favor.

*Brian Portnoy: Right. It seems like we are in a wait and see moment from a fundamental prospective. There is so much uncertainty, there is no historical precedent for*

*what is taking place right now, so in terms of the impact on global trade, on GDP and various countries, I think it's difficult to say what the impact is going to be.*

Joe Terranova: You are talking about economic forecasting, which is incredibly difficult to begin with. Yes, you correctly identified the situation. Again, you are fortunate that the market was near all-time highs. We broke the trend, now you look for visibility; you may get some visibility in some important economic releases. China PMI is very important. We will be putting something out on Twitter in the next 24 hours directing our followers and clients to take a look at the upcoming important economic calendar dates, that being China PMI, U.S. ISM Manufacturing, U.S. ISM Services and, of course, the jobs report which we are forgetting about – that was the exogenous event that put the Federal Reserve on hold, with only a 38,000 [jobs] gain last month. Consensus estimate is looking for +180,000 [jobs]. Those are four very important dates.

And then, of course, we have earnings, and the question becomes, when are we coming out of the earnings recession? Is it going to be this quarter? The expectations are probably not, but the guidance suggests that we come out of it in the following quarter.

*Brian Portnoy: Right. We talk all the time about an investor's playbook, so here we sit at the midway point of 2016, you just ticked off a number of really important data points or inputs that are going to be coming down the pike. Anything else you would stress as we enter the dog days of summer and look at the back half of 2016 that investors should have in their playbook, risks they should be thinking about, not necessarily taking action on, but things to put on the watch list?*

Joe Terranova: For me, the U.S. dollar and the prevailing trend in the U.S. dollar is always important. So far year to date, and you and I talked about this coming into the year, the expectation was for further appreciation of the dollar. Fortunately for capital markets, the U.S. dollar actually had a nice little correction. That correction lent itself for the commodities rally that we witnessed, it lent itself for multinationals to get a little bit of relief. I think we are going to see that show up in the earnings. I am always looking at the value of the U.S. dollar; obviously the conditions as it relates to Europe are important. I mentioned German equities before. I want to see what the Bank of Japan does, again this is a surprise. Bank of Japan needs to respond to an appreciating yen, which is uncomfortably high. I think at some point they will. I think that is very important because a lot of the work that they have done since 2012 is unraveling. It is certainly surprising me.

Let's highlight for the second half some important things for investors. The conditions coming into the first half of the year that was so concerning to the capital markets, that being commodities credit and Chinese derivatives. We have seen a healing process in each of those conditions and that's something that I want investors to focus on. I think it is important, and I think it lends itself when you look at your portfolio too. Let's be invested. The good thing about where we are is that there is no herd mentality in any particular asset class, so that gives you the distinction of making a compelling argument for ownership of all of the asset classes themselves.

It is really what do we want to do with the discretionary portion of the portfolio – that 5-10%, where is it that you want to overweight that 5-10%? I think in that process you need to get a little clarity as it relates to earnings season as I

mentioned, and let us not forget we are going to be faced in the month of July with the U.S. presidential respective conventions. A little bit of contention will come out of that, so we might be in for a period of sideways consolidation, a little bit of elevated volatility, but overall it will be earnings that ultimately will prove to be whether or not we can resume the bullish uptrend.

*Brian Portnoy: We look forward to summer as being a quiet time, I do not think either of us expect a quiet time in the months to come and so as always really appreciate your guidance and look forward to speaking to you in a month or so.*

Joe Terranova: Thank you Brian. Enjoy the Fourth of July.

**This commentary is the opinion of Joe Terranova. Virtus Investment Partners provides this communication as a matter of general information. The opinions stated herein are those of the author and not necessarily the opinions of Virtus, its affiliates, or its subadvisers. Portfolio managers at Virtus make investment decisions in accordance with specific client guidelines and restrictions. As a result, client accounts may differ in strategy and composition from the information presented herein. Any facts and statistics quoted are from sources believed to be reliable, but they may be incomplete or condensed and we do not guarantee their accuracy. This communication is not an offer or solicitation to purchase or sell any security, and it is not a research report. Individuals should consult with a qualified financial professional before making any investment decisions.**

2113 6-16 © 2016 Virtus Investment Partners, Inc.