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QUARTERLY PERSPECTIVE

DVI
DAVID VAUGHAN INVESTMENTS

AN EXIT FROM BREXIT?

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On June 23rd, thirty million United Kingdom (U.K.) citizens went to the polls to vote on a non-legally binding referendum pertaining to their country's membership in the European Union (EU). Should we leave or remain was the question. Despite predictions to the contrary, the Leave camp known as the Brexiteers were victorious, receiving 52% of the votes cast. Leading up to the referendum, Britain's bookies were showing the Remain camp as the odds on favorite and even exit polls were indicating that EU supporters were in the majority. To say the investment community was caught off guard by this surprising outcome is an understatement. The British pound (£) dropped nearly 12% vis- a-vis the dollar from a high on the 23rd of 1.50 to a low of 1.32 by market open on the 24th, the lowest level for the pound in nearly 30 years. In terms of order of magnitude, the U.K. housing and banking sectors were both decimated as the potential forced exit from London of the financial services sector would have a devastating impact on the city's highly inflated real estate market.

Though clearly there has been economic fallout from the Brexit referendum, I think we need to continue to view this unsettling development as a political disruption rather than an economic development. There are those that immediately liken the Brexit outcome as the canary in the coal mine for further economic deterioration in Europe. The uncertainty left in its wake will likely cause a pause by most business decision makers as they consider further capital expenditures to support business expansion in the U.K. However, it is also highly likely that very little will change over the next several years as the U.K. wrestles with all of the issues that come with extracting themselves from the largest economic trading bloc in the world. No independent European country has ever left the EU.

The Importance of Article 50

The Lisbon Treaty, which was signed by the U.K. in 2007, was later ratified by all 27-member states and began in full force on December 1, 2009. This legislation has 358 articles, none more important than Article 50, which outlines the process for a member state to withdraw from the Union. Based upon the rhetoric coming from Brussels, most would come to the conclusion that the EU leadership could impose a timeline for the U.K. to invoke Article 50. That is hardly the case. The member state must initiate the process. So in the case of the U.K., is the Prime Minister empowered to individually initiate the process, or does Parliament need to weigh in on the matter? Legal experts have mixed opinions.

Increasingly, analysts are coming to the conclusion that there will be a series of important steps that lead up to a decision on Article 50. First, a new Prime Minister must be selected by the Conservative Party as result of David Cameron's announced resignation. The timeline for this process has a stated deadline of September 2nd. Some have speculated that the next step would be the call for a general election in 2017. This would allow the U.K. citizenry to vote in representation aligned with their Remain or Leave preference. And then what would follow would be a binding vote in Parliament to invoke Article 50.

If Article 50 is invoked, the U.K. then will have a full two years to negotiate the terms of their new relationship with the EU. That could even be drawn out further, beyond the two-year term, if the EU member states agree to an extension.

Political Leadership, What Comes After Brexit?

Frankly, beyond political hyperbole, the leaders of the campaign to leave the EU had never laid out a clear and concrete proposal for what the post Brexit environment would look like. On such hot topics as immigration and the annual membership fee paid to the EU, it appears that in the post-Brexit era these leaders have already reversed or significantly modified their positions.

From the leadership of the EU, an increasing hard line stance is emerging with German Chancellor Angela Merkel suggesting she would not allow any "cherry picking" by the U.K. in their negotiations with the EU. French President Francois Hollande continues to reinforce her position

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2016 "MID-YEAR" CHECKLIST

As we move into the third quarter of 2016, we encourage our clients to get a jump start on financial items that are typically viewed as "year-end" tasks. At DVI, we believe that many of these strategies can be implemented at any time of the year. Now is a great time to start checking them off your "Financial To-Do List" so you can focus on what matters most to you during the holidays.

As a guide, we have compiled a 2016 "Mid-Year" Checklist to help our clients stay organized and on track to meet wealth planning and management goals.

INCOME TAX

1. Maximize your retirement contributions

- While April 15th, 2017 is typically the deadline for 2016 contributions, there's no need to wait until April. In fact, the earlier you make your contribution, the more time it has to work for you.
- In 2016, the annual contribution limit for employees who participate in 401(k), 403(b), most 457 plans, and the federal government's Thrift Savings Plan, is $18,000. For self-employed and small business owners, the amount you can save in a SEP IRA or solo 401(k) is $53,000, which is based on the amount you can contribute as an employer and as a percentage of your salary. The limit on SIMPLE retirement accounts is $12,500.
- If you are 50 years old or older, take advantage of the "catch-up" provisions.

2.. Roll over your old 401(k) into an IRA

If you left a job and your old 401(k) behind, take the time now to think about consolidating accounts. In order to avoid mandatory tax withholding, make sure to opt for a direct rollover distribution to an eligible retirement plan, including an IRA. You'll have more control over your asset allocation, total contributions and fees.

3. Consider a Roth IRA conversion

Even if your income exceeds the limit to contribute directly to a Roth IRA, you can still achieve tax-free investment growth for your retirement. Create this opportunity by first making a non-deductible contribution to a traditional IRA and then converting the funds to a Roth IRA.

4. If applicable, take your Required Minimum Distribution (RMD)

If you are 70½ years old or older, you must take Required Minimum Distributions (RMD) by December 31st or you might incur a hefty penalty. The only exception is your very first RMD, which you can delay until April 1st of the year following the year you turn 70½. This rule isn't to be treated lightly. If you miss the deadline, the penalty is 50 percent of the amount that should have been withdrawn.

5. Defer income and maximize deductions

- If you want to defer income until next year, consider deferring your year-end bonus, the sale of capital gain property and receipt of distributions until after January 1, 2017.
- Consider maximizing tax-deductible expenses this year. For example, you could consider paying your medical bills early if your medical costs exceed 10 percent of your adjusted gross income in a single year or prepay recurring expenses like property taxes before January 1, 2017.

6. Harvest capital losses to balance gains

For DVI managed portfolios, we engage in harvesting capital losses to offset gains on your behalf every year. If you have additional needs in outside investment accounts, please let us know so we can provide assistance in maximizing this opportunity.

TRANSFER TAX

1. Give to those in need

Giving to charity has tax advantages. You may want to consider opening a Donor Advised Fund for an immediate tax deduction yet provide the gifts to charity over time. If you fund your account with appreciated stock in place of cash, you'll get the added advantage of reducing capital gains in your portfolio while generating an income tax deduction.

2. Consider a Grantor Retained Annuity Trust (GRAT)

Given the continued low current interest rate environment, a GRAT provides a tremendous opportunity to transfer wealth to children and other family members.

3. Give to Loved Ones

Currently, an individual can gift up to $14,000 a year to anyone — and any number of people —without incurring gift taxes in 2016.

4. If applicable, consider making a tax-free IRA transfer to eligible charities

If you are over 70½ in 2016 and would like to make a donation to charity from your IRA, you may be allowed to directly transfer, tax-free, up to $100,000 per year to an eligible charity.

SAVINGS & INVESTMENTS

1. Discuss major life events and short term liquidity needs

With any major life event, such as marriage or divorce, births or deaths, job or employment changes or any other significant discretionary expense (real estate purchase, college tuition, etc.), it is prudent to re-examine asset allocation to ensure adequate planning.

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2. Optimize asset location for achieving best long-term balance of liquidity and tax efficiency

As a part of your on-going relationship with DVI, we will review asset location to make sure we are optimizing your financial situation. If you would like us to review your outside investment accounts to make sure the liquidity and tax-efficient strategy is in place at all financial firms, we would be more than happy to provide guidance and incorporate it into our DVI quarterly reporting and annual meetings.

3. If applicable, consider a College Savings Account (529) for your children or grandchildren

College Savings Account (529) is a tax-advantaged savings plan operated by a state or educational institution designed to make it easier to save for college and other post-secondary training for a designated beneficiary. Earnings in a 529 plan grow federal tax-free and will not be taxed when the money is taken out to pay for higher education expenses.

PROTECTION

1. Review property and casualty insurance coverage

Gather insurance records and review the adequacy of your insurance policies. Be sure to evaluate all coverages, including life insurance, disability income insurance, homeowners insurance, auto insurance, liability insurance, long-term care insurance, etc.

2. Double check beneficiary designations

It is important to review beneficiary designations for your retirement accounts, personal accounts and life insurance. Also, make sure that the company has an updated beneficiary designation on file. Many people make the mistake of not updating their beneficiaries during significant life events (i.e. birth, divorce or death), which could result in an unexpected and/or unwanted passing of assets.

3. Complete an annual review of all trusts and trust documents

Review trusts and wills to make sure they reflect your personal wishes for the disposition of your assets. If your personal or financial circumstances have significantly changed over the past year, consider consulting with your estate-planning attorney to make sure your documents are up to date.

4. Review your health insurance

- Review Health Savings Account (HSA) contributions and determine if an adjustment is needed.
- If applicable, review Medicare Part D plan and make changes during open enrollment, which begins in October.

5. Spend down your Flexible Savings Account (FSA)

Unlike a Health Savings Account (HSA), you generally have to use the money you put into your FSA during the calendar year or you lose it. While new rules allow an employer to let you carry over $500 or provide you an extra two and a half months to use the funds, it's not required. Find out whether your company offers a grace period into the next year to spend down the account. Many people schedule appointments in the last few months of the year to make the most of their FSA--- schedule with your doctors early.

At DVI, many of these topics will be discussed during your annual meeting regardless of the time of year. Also, if desired, we typically work in conjunction with your accountant and estate attorney to accomplish your goals. If you have any questions or would like to discuss any of these items in further detail, please contact your DVI Relationship Manager.

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"To access the internal market a country must respect the four liberties, liberty of circulation of goods, of capital, of services and people and it must contribute to the EU budget."

A Few Realities

- It is estimated that two million U.K. citizens reside in the EU and that three million EU citizens make the U.K. their home. What rights will these individuals have going forward?
- The U.K. sends to Brussels roughly £13 billion per year and is the third largest net contributor to the EU's annual budget. The majority of member states are net recipients of economic subsidy support from the EU. Where will this additional support come from in the U.K.'s absence?
- According to the Office for National Statistics, 47% of U.K. exports went to other EU countries. But just as important to the EU, 54% of the U.K.'s imports came from the EU.

In absence of sound political leadership prior to the Brexit vote on June 23rd, we are left purely speculating as to the timing and eventual outcome of the relationship between the U.K. and EU. Additional U.K. specific developments such as Scotland independence and the reunification of Ireland are also out there to contemplate. In this sea of uncertainty we know two things: 1) the time line for the events to unfold is likely years rather than months and 2) as a consequence of all of this economic uncertainty caused by political disruption, Central Bankers around the globe will continue to maintain a very accommodative monetary policy for the foreseeable future.

WHY INVEST NOW?

This has been a frequent question asked of me lately. Market volatility, political uncertainty, geopolitical turmoil, "Sell in May and Go Away", a full moon….all creating uncertainty in an investor's mind. There continues to be tremendous amounts of cash sitting on the sidelines earning virtually nothing. My best response focuses on a couple long standing premises of the DVI investment philosophy.

First, we do not believe investors have the ability to effectively time markets. We prefer to manage risk through portfolio construction and stock selection. Timing requires the investor to be correct on two counts – when to get in and when to get out. In my thirty years of following markets and the people who work in them, I've yet to see anyone consistently make those two decisions accurately. We prefer to be opportunistic, working to find attractive values in whatever the market environment may be.

The table below is a hypothetical illustration showing the risk of trying to time the stock market. By missing just a few of the stock market's best days, you could see your portfolio returns reduced by half or more.

THE POTENTIAL COST OF MARKET TIMING

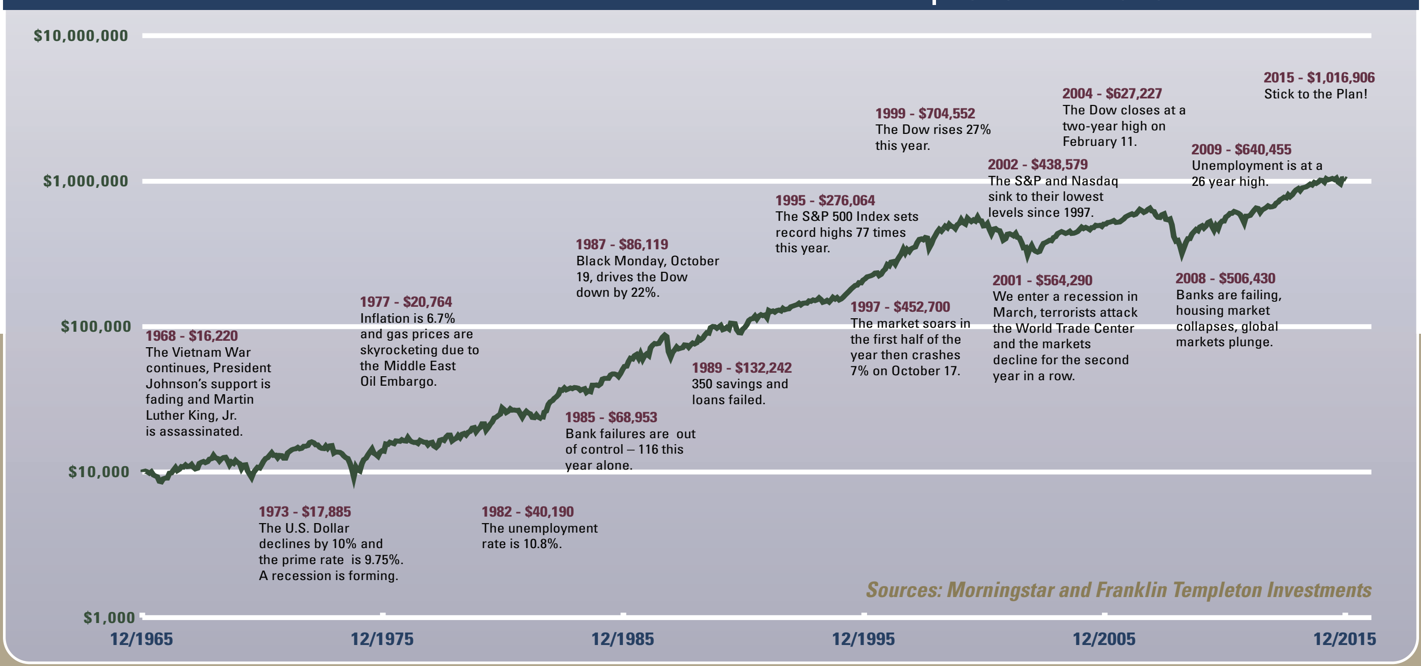
20 Years Ended December 31, 2015

Period of Investment	Average Annual Total Return of S&P 500 Index
Stayed Fully Invested	8.19%
Missed the 10 Best Days	4.50%
Missed the 20 Best Days	2.06%
Missed the 30 Best Days	-0.04%
Missed the 40 Best Days	-1.97%

Source: Standard & Poor's

Second, when looking back at history we see similar periods of uncertainty where economic concern, social unrest, and market volatility all plagued our minds. A $10,000 investment made in the S&P 500 a little more than fifty years ago, on December 31, 1965, would today be worth more than $1 million dollars. Below is a timeline highlighting some of the events a long-term investor overcame along the way.

S&P 500 INDEX PERFORMANCE OVER THE PAST 50 YEARS | 12/31/1965 - 12/31/2015



The ride would have occasionally been bumpy but patience, discipline, and sticking to the plan were rewarded.