



Quant Coalescence

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Collaborative insight provided by CIO Michael Chapman.

June, 2016: “Brexit Goes Mainstream and More Performance Awards for PCM”

Those of us that work in the financial markets have been talking and pondering about the outcome of the June 23rd “Brexit” vote for several months now. As you probably all know, this is the referendum vote that allowed citizens in the U.K. to decide if they wanted to remain in the European Union or reclaim their independence. It has been big news in financial services, as it was feared that it could greatly impact world economies, bond and equity markets. The story has now become a much bigger and mainstream story because even though the polls showed a close vote, everyone believed that Britain would not vote to leave the EU.

Well, they did vote to leave and as we all saw last Friday and Monday, the markets don’t like surprises. The markets had their biggest opening gap from the previous days close in years with the DJIA down as much as 600 points. The market has since regained some of those losses, but history tells us that surprises like this will see the markets sell off at least 10% in the coming months after this initial “dead cat bounce”. The news has also grown in importance and coverage, as there are now fears that other EU countries will vote to do the same. Now that the sun rose the day after the vote, it may not seem so scary. At the same time, many voters in the U.K. apparently now have “buyers’ remorse” over their vote to leave; wondering if the coming economic turmoil will be worth it. . The majority of voters in Scotland and Ireland wanted to stay in the EU. This could motivate them to have another vote on their independence from the U.K. in an effort to stay in the EU. In the coming months, important votes are already on the calendar in Spain, Italy and our presidential election here in the U.S.; France and Germany follow next year. All of these countries including the U.S. have seen a huge surge in populist’s movements, driven by similar frustrations with the economy, job prospects, regulations and immigration.

Compounding the turmoil and uncertainty that this unexpected outcome has brought about, earnings season for second quarter 2016 begins in July. It is expected that S&P 500 earnings will be down year over year again, and this will be the fifth quarter in a row. This will be the longest stretch of negative quarterly year over year earnings since the span of the 2008-2009 financial crisis. To make matters worse, the “Brexit” has strengthened the U.S. dollar, which will hurt already struggling earnings in the U.S. It has also increased the chances of recession in Europe.



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Before we break down the weightings of the individual strategies, below is a table of our gross composite performance for our models for 1st quarter 2016. Since the last monthly newsletter, we have been notified that we *did indeed* win several “Top Gun” performance awards. The awards recognized our quarterly performance in the PCM Absolute Bond, PCM Absolute U.S. Sectors and 2 performance awards for PCM Absolute Equity Income; being recognized in an ETF category and an equity category. We were very pleased with the quarterly outcome for first quarter, especially in light of the historical *selloff* combined with a historical *comeback*; all in one quarter. An excerpt from our 1st quarter 2016 client letter sums it up:

“So there it was; **a record for the worst open to the equity markets in history for January**. Six weeks into 2016 on Feb. 11, all of the major U.S. stock indexes were down more than 10% for the year. A bear market looked all but certain. That day the Dow Jones Industrial Average closed nearly 15% off its May 2015 record high. The benchmark Standard & Poor’s 500 was down 14.2% and the NASDAQ composite was down 18.2%. Then we had the record “comeback” rally. According to CNBC, the **Dow Jones Industrial Average saw its biggest quarterly comeback since 1933**. Most of the U.S. indexes finished the quarter unchanged or slightly up. Let’s digest that. **For the U.S. equity markets to finish the quarter basically flat, the markets set a record on the downside and on the upside in just one quarter!** Now THAT is volatility....and we LIKE it!

What does this all mean to you and your investments? Let’s start with a barometer of what the average investor experienced during the 1st Qtr. 2016. The NASDAQ composite was down 2.8% and the IBD mutual fund index, which is an index of 19 very large growth mutual funds, closed down 3.14%.”

And the PCM results that garnered these performance awards? See below:

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Provident Capital Management, Inc.

First Quarter 2016 Gross Composite Performance

STRATEGY	ASSET CLASS	Jan 2016	Feb 2016	Mar 2016	1st Qtr 2016
PCM Absolute Equity Income Composite	Multi Directional Equities	-0.09	-0.46	4.91	4.33
PCM Absolute U.S. Sectors Composite	Multi Directional Equities	0.21	0.28	3.88	4.39
PCM Absolute International Composite	Multi Directional Equities	-2.28	1.49	2.89	2.04
PCM Emerging Market Equity Composite	Multi Directional Equities	-1.14	-0.53	-1.46	-3.10
PCM Absolute Metals Composite	Multi Directional Metals	-1.07	3.92	1.99	4.85
PCM Absolute Commodities Composite	Absolute Commodity	-0.06	3.53	-1.56	1.85
PCM Emerging Market Bond Composite	Multi Directional Bonds: (Global)	-0.17	0.04	1.97	1.84
PCM Managed TIPS	Inflation Protected Bonds: (Global)	0.59	1.28	1.82	3.73
PCM Global Bond HF Portfolio	Multi Directional Bonds: (Global)	0.26	1.24	2.11	3.65
PCM Emerald Long-Short Debt HF Com	Multi Directional Bonds: (Global)	0.1	0.71	1.63	2.45
PCM Absolute Bonds Composite	Multi Directional Bonds: (Global)	0.66	1.46	2.51	4.69
PCM Absolute U.S. Bond Composite	Multi Directional Bonds: (US)	1.02	0.36	0.45	1.84
PCM Emerging Market Blend Composite	Multi Directional Blend	-0.08	0.62	2.14	2.69
PCM Alpha 1 Composite	Multi Directional Multi Asset Class	0.91	2.03	-0.25	2.70
PCM Global Macro 3M Composite	Multi Directional Multi Asset Class	-0.95	1.35	1.15	1.54
PCM Sapphire Global Macro HF Compos	Multi Directional Multi Asset Class	-1.21	1.76	0.20	0.73
PCM Global Tactical Composite	Multi Directional Multi Asset Class	-3.27	1.51	0.65	-1.17
PCM SuperGlobal Macro Composite	Multi Directional Multi Asset Class	-0.06	1.57	0.07	1.58
PCM Global Macro Index Composite	Multi Directional Multi Asset Class	-0.21	0.77	-0.78	-0.23
PCM Conservative Portfolio Composite	Multi Directional Portfolio	-0.02	1.13	1.15	2.27
PCM Total Return Portfolio Composite	Multi Directional Portfolio	-1.46	0.97	0.91	0.40
PCM Diamond_RubyMulti-Strategy HF Composite	Multi Directional Portfolio	-0.58	1.21	1.12	1.75
PCM Stable Growth Plus Portfolio Composite	Multi Directional Portfolio	-1.19	1.04	0.69	0.53

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Most of our models continue to experience stable and positive performance in the second quarter ending June 30. (Equity models would be exceptions, as they were long equities going into the surprise Brexit vote.) For the week ending June 24th, the S&P 500 is flat (including dividends) year to date, the NASDAQ composite is down 6% and the IBD mutual fund index is down over 4%.

The reach for yield continues, anything paying a dividend or even a small amount of interest has continued to be attractive, as negative interest rates appear to be here to stay for a while.

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PCM Strategies: 06.2016 Allocations*

*(Please note that performance numbers on the website for indexes do not include dividends and are appropriately calculated sequentially.)

1. [PCM US Bond Total Return IndexSM](#): Investment grade corporates and U. S. Treasuries of varying maturities from 3-20 years.
2. [PCM Absolute Bond IndexSM](#): U.S. and International Treasury bonds
3. [PCM Absolute U.S. Sector IndexSM](#): Financials, technology and healthcare
4. [PCM U.S. Industries Total Return IndexSM](#): Medical devices, industrials, technology and insurance
5. [PCM Absolute Equity Income IndexSM](#): Preferred and dividend paying equities, and cash equivalent
6. [PCM Emerging Market Total Return Equity IndexSM](#): BRIC's, Emerging Asia and cash equivalent
7. [PCM Total Return Portfolio IndexSM](#) and [PCM Stable Growth Plus+ Portfolio IndexSM](#): International and U.S. treasuries, utilities, dividend paying equities, healthcare, technology, and the Japanese yen are all themes in these portfolios.
8. [PCM Global Tactical IndexSM](#): Utilities, dividend paying equities, international treasuries, U.S. treasuries, and the Japanese yen
9. [Global Macro IndexSM](#): Broad based commodities, broad based U.S. equities, emerging market bonds and high yield U.S. corporate bonds and cash equivalent
10. [PCM Alpha 1 IndexSM](#): Cash Equivalent
11. [PCM Absolute Commodities IndexSM](#): Natural gas and sugar

And now...our award ceremony....PCM was again recognized as a "Top Gun" for our performance. This time for the volatile 1st quarter of 2016 by Informa Investment Solutions. Four of our models were in the top 10 performers out of hundreds of products and money managers.

PERFORMANCE RECOGNITION: 1st Quarter, 2016

Informa Investment Solutions' (PSN) Ranks PCM "Top Gun" Products

- **PCM Absolute U.S. Sectors** - (Top 5/#1) ETF US Equity Universe (*out of 112 products*)
- **PCM Absolute Bonds** - (Top 5/#1) ETF Global Fixed Income Universe (*out of 25 products*)
- **PCM Absolute Equity Income** - (Top 5/#4) ETF Global Balanced Universe (*out of 204 products*)
- **PCM Absolute Equity Income** - (Top 10) Overall Global/Intl Balanced Universe

PCM was also recognized as a "Top Gun" for our performance during the volatile 3rd quarter of 2015 by Informa



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Investment Solutions. Four of our models were in the top 10 performers out of hundreds of products and money managers.

PERFORMANCE RECOGNITION: 3rd Quarter, 2015

Informa Investment Solutions' (PSN) Ranks PCM "Top Gun" Products

- **PCM Protective Equity** - (Top 10/#5) All Cap Universe *(543 products in the All Cap universe)*
- **PCM Diamond** - (Top 10) US Balanced Universe *(314 products in the US Balanced universe)*
- **PCM Global Macro** - (Top 10/#2) Global/Intl Balanced Universe
- **PCM Global Tactical** - (Top 10/#8) Global/Intl Balanced Universe *(297 products in the Global/Intl balanced universe)*

***We have enhanced our website AGAIN at <http://www.pcminvestment.com>. You can now see performance of our indexes (previous day and month to date) on our streaming ticker. We include performance for both our indexes and our composites, as applicable. You will be asked to enter your email address to get into the website. There will be no password required, so you won't have to worry about forgetting it. This is partly due to helping us stay in compliance with requirements in our industry that we know who has reviewed our website content. Please use the website link above to see all of our indexes and composites.

In addition to the above mentioned "Top Gun" performance awards from Informa Investment Solutions, PCM composites have been previously recognized for performance by Informa Investment Solutions; the [PCM Absolute Bond Compositesm](#) for the three year performance ending the 4th quarter of 2014, as well as previous awards for 1-year trailing performance and 3-year trailing performance. As of 2nd quarter 2014, the [PCM Absolute Bond Compositesm](#) and the [PCM Absolute Commodities Compositesm](#) both won a "Top Gun" award for performance in their respective category for the 1-year trailing performance period, with the [PCM Absolute Bond Compositesm](#) also winning the "Top Gun" award for 3-year trailing performance. The [PCM Alpha 1 Compositesm](#) was awarded the "Top Gun" performance award for the 1st quarter of 2014. We are very pleased to see these particular multi directional strategies being recognized, as the [PCM Absolute Bond Strategysm](#) and [PCM Alpha 1 Strategysm](#) are particularly timely for where we are in the current market cycle.

To view Morningstar Fact sheets of all of our index models, please visit our website at www.pcminvestment.com



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under the [“PCM multi-directional Strategies” tab](#).

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About "PCM Quant Coalescence"

Welcome to Provident's "Quant Coalescence" communication. We suspect that many of you are no different than us. That is to say that when our quantitative models rebalance every 2 weeks for some indexes or once a month for other indexes, you sometimes find yourselves asking "What is behind a rotation into that ETF?" This communication is our opportunity to "unite for a common end" with our clients and partners; keeping you updated on our thoughts and perspectives. As you know, our indexes are based on an absolute approach: we strive to make money in up markets or down markets, while trying to greatly minimize loss in any market environment.

Our indexes are also quantitative, reflective of our systematic, unbiased and technical approach. Since our indexes are unbiased, the quantitative models would obviously at times rotate into positions that cause us to scratch our heads. Nevertheless, being so close to the analysis as it unfolds, allows us to quickly begin to validate the fundamental reasons behind the quantitative "following of the money." At other times, the trades are not validated right away; the story unfolds as the days pass. We have been very excited about many of these "validations" and "ah ha" moments. We had another "ah ha" moment when we decided that these insights would also be interesting to those who have entrusted us with their financial peace of mind. Our goal is to be short and to the point, specific to what is happening in our indexes rather than a lengthy macroeconomic perspective.

For further disclaimers and disclosures, see our website for [index disclosures](#) and [composite disclosures](#).