Welcome to the (late!) June 2016 Edition of the Martin Bros Monitor.
In this edition of the Martin Bros Monitor:

Expect the Unexpected - Which No One Did With Brexit!

We had flagged Brexit as one possible event in the mid to second half of this year that could add to the volatility we have seen in global markets since the start of 2016. And it didn't let us down! However, by the time the British referendum came around, no one (including us) thought that the Leave campaign would win. Betting odds, which historically are more accurate than the polls, had the Remain campaign at about $1.20 versus roughly $7.00 for a Leave win.

Central banks had prepared responses for a Brexit on the unlikely event Briton's voted to Leave, which they did. Much of this central bank response is unseen, however the visible and most important part is the rhetoric from leaders about being prepared to unleash liquidity if needed and do anything to prevent market crises. This is what we saw. Equity markets on Friday 24th June in Australia were heavily sold down by the end of trading as the outcome of Brexit was known. At market open only a few hundred thousand votes were released and our market opened up some 40+ points. By the end of the day we closed down 160 points after swinging several times between 200 points down and 40 points up. It would have to be one of the most interesting days in front of the screen in our career.

The immediate fallout from Brexit was sharply lower global equity markets for the next couple of days. Many markets though, including the US, Australia and the UK have now recovered most of this lost ground. The majority of European equity markets are still noticeably lower though, including Germany, France, Italy, Spain and Greece.

The ultimate fallout from the British leaving the EU is still an unknown. But in terms of impact on global GDP, you would have to assume it will be minimal. Unless that is, the wider European Union starts to unravel and another participant (i.e. France, Germany, Italy, etc.) decides to question their involvement. Given the huge surprise to global markets that Brexit got up, it is not inconceivable that there might be a European bank or large fund manager that got themselves in trouble betting on the wrong outcome. Only the weeks and months ahead will tell.

We have talked about Bond yields many times in these quarterly updates, including our last edition in March when we talked about NIRP – Negative Interest Rate Policy. The low, in some cases negative, global long bond yields is a phenomenon that has not been seen before. We cannot see how this will end well (for bond holders). This doesn't mean it may not persist for some time yet though. Any fallout in the Bond market would create volatility over all markets, but also an opportunity.

Low long term bond yields imply that growth and inflation will be low for many years. The other reason bond yields rise (fall in yield) is a flight to quality (less risky assets – although we think this is now an oxymoron with rates so low). Since our last MBM in March, global bond yields have moved even lower and many negative interest rates have become even more negative. Please see the below table.

Bond	Yield 31st March 2016	Yield 30th June 2016
Japan 5 year bonds	0.04%	-0.32%
Japan 10 year bonds	0.04%	-0.24%
German 5 year bonds	-0.33%	-0.57%
German 10 year bonds	0.15%	-0.13%
France 5 year bonds	-0.21%	-0.35%
France 10 year bonds	0.48%	-0.19%
UK 5 year bonds	0.84%	0.35%
UK 10 year bonds	1.41%	0.87%
US 5 year bonds	1.20%	0.99%
US 10 year bonds	1.77%	1.45%
Australia 5 year bonds	2.05%	1.63%
Australia 10 year bonds	2.49%	1.97%

In our March MBM edition we wrote:

"The problem now seems to be QE fatigue. More and more market participants are questioning how does this all end? What is the exit strategy for unwinding this massive stimulus and what are the side effects of negative interest rates. No one truly knows, but one effect is an increase in the nicknamed "currency wars" between governments globally. The idea being the lower you can get your currency versus a basket of international peers the more export driven growth you will have and international competiveness for services e.g. tourism and education in Australia.

There is fear that the longer central banks persist with NIRP, the larger the risk becomes to the real economy. At present, it is estimated there are currently $6 trillion dollars of negative yield bond holders globally. If they panic and decide to sell, yields could jump dramatically, back into positive territory yes, but the ramifications of a dramatic bond sell off would be – more volatility."

As mentioned, lower bond yields are normally a signal of rising global risks and / or further protracted low growth. Add to this the upcoming US election, uncertainty over Europe's future prompted by Brexit and the seasonally weak period of equity markets between now and November, we continue to be conservatively positioned, awaiting opportunities that will present themselves due to further volatility.

What is Bitcoin?

Most people would have heard of "Bitcoin" by now however many less would have any idea what it is and how it works.

The below brief summary may help you gain a greater understanding of Bitcoin and it's features:

What is a single unit of Bitcoin?
An extremely complex software code.

Where do they come from?
Bitcoins were designed by an unknown person, or persons, known as Satoshi Nakamoto in 2009. They're held in the Bitcoin network, from which they're extracted or mined by computers. Bitcoins are currently mined in lots of 25, but the number of units in a lot halves approximately once every four years. Mining takes a lot of time for computers to process and the difficulty changes in response to the amount of computing power that miners are direct at the network. Companies and syndicates set up for the sole purpose of Bitcoin mining exist, and yes they consist primarily of rooms full of computers trying to process the

network.

How many Bitcoins exist?
There are currently almost 16 million in circulation and only 21 million will ever be mined, in accordance with the Bitcoin creator's rules.

What are they worth?
The price of Bitcoins wildly fluctuates, but they were worth $899 at the time of publication.

Who decides what they are worth?
The users - the price of bitcoins is determined by market supply and demand. But rather than thinking about the value of bitcoins like real money, they're better viewed as a commodity like gold.

How do people get Bitcoins?
Bitcoins can be bought online with cash from Bitcoin traders and many businesses accept them as a form of payment for goods or services. Bitcoin ATMs also exist where people can insert money to buy them, or sell their Bitcoins and withdraw cash.

Where do you keep them?
Bitcoins are stored in a Bitcoin wallet similar to a bank account, which can be run by third-party websites, mobile apps, computer software or even computer hardware. All Bitcoin users can view a ledger of every transaction in the network, which is known as the blockchain.

(Source: Iress, CoinDesk.com, Bitcoin.org, Bitcoin Foundation, Bitcoinclock.com, Khan Academy and MarketWatch.com)

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