SIERRA MUTUAL FUNDS

3420 Ocean Park Boulevard,Suite 3060
Santa Monica, CA 90405

National Sales Desk: 1-800-729-1467

OBSERVATIONS AND PERSPECTIVES: GLOBAL CONFIDENCE IS FRAGILE

> " Confidence is a very fragile thing. "
>
> *NFL Hall of Fame Quarterback Joe Montana*

Kicking off the start of the second full week of trading for 2016 did little to calm investors. The year started in an ugly way when The People's Bank of China depreciated the value of its currency, the renminbi, causing shares to tumble in Shanghai. The descent in Chinese stocks was so sharp that circuit breakers were triggered, halting trading. Just like when you are fighting with your spouse, or getting ready to hit the send button in an angry email, a short pause can often stop destruction. Circuit breakers are a tool that stock exchanges use to try and ease panic selling.

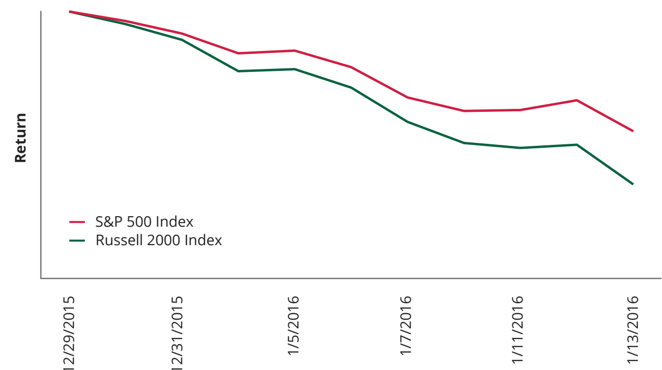
This time it didn't work.

The slump in the renminbi and capital flight from the world's second largest economy has hit the Chinese stock market hard: the Shanghai A-share index is already down 15% on the year. The falling currency isn't China's only woe: slowing economic growth, weaker manufacturing activity, falling retail sales growth, rising bad loans and dropping real estate prices all point to the plummet in its stock exchanges.

What is curious, however, is the global reaction. The weakening Chinese economy has very limited direct impact on the economies of Europe or the United States. Even a sharp decline in the Chinese stock market would per se have almost no impact. The collateral damage may not be caused by the impact of Chinese stock markets, but point instead to how fragile global investor confidence has become.

Here are just a handful of examples:

- Crude oil prices (WTI) have fallen to levels not seen since 2003, plunging another 5% on Monday; that's down 16% for the year on top of a brutal 30% drop in 2015. China is an importer of oil, but only represents about 12% of global consumption.
- Germany's leading stock index, the DAX, fell 4% last Monday alone. Year-to-date, the blue-chip index has fared worse than the rest of Europe, falling more than 7%.
- Exports from the U.S. to China represent less than 1% of U.S. GDP, yet the S&P 500 is down more than 7% since December 29.
- Small stocks, which generally have less international exposure than large stocks, have fared even worse. The chart below maps the performance of the Russell 2000 (small stocks) to the S&P 500 since December 29. The small-cap index has dropped nearly 10%, clocking an even more dire performance than the S&P 500, which tracks much larger companies.



Source: Yahoo!

Small stocks, represented by the Russell 2000 and shown in green, have shed 10% since December 29. The loss is even greater than the 7.4% loss of large stocks, represented by the S&P 500 and shown in red, during the same time period.

While it may be easy to say the "Made in China" stock shakeout is the cause for these other massive declines, it's not so clear if that is the case. Take away the China factor, and there could be many other explanations - supply still outstrips demand for oil on a daily basis worldwide, for example.

The record first week drops in markets here in the U.S. and abroad may indeed indicate that, global confidence has become fragile, in which case, look out below: there could be further downside ahead in the U.S. stock market. Good opportunities may be had in high-grade bonds in the U.S. and Europe, and municipal bonds also offer the prospect of productive investment.

Terri Spath, MBA, CFA, CFP
Chief Investment Officer, Sierra Mutual Funds
January 14, 2016

This publication is for general information only and is not intended to provide specific advice to any individual or institution. Some information provided herein was obtained from third-party resources deemed to be reliable.

Investors should carefully consider the investment objectives, risks, charges, and expenses of the Sierra Mutual Funds. This and other information about the funds is contained in the prospectus and should be read carefully before investing. The prospectus can be obtained on our website www.sierramutualfunds.com or by calling toll free 1-800-729-1467. The Sierra Mutual Funds are distributed by Northern Lights Distributors, LLC, member FINRA/SIPC.

©2016 Sierra Mutual Funds. All rights reserved.

2042-NLD-1/15/2016