GREENLEAF TRUST

Perspectives

A Greenleaf Trust Newsletter

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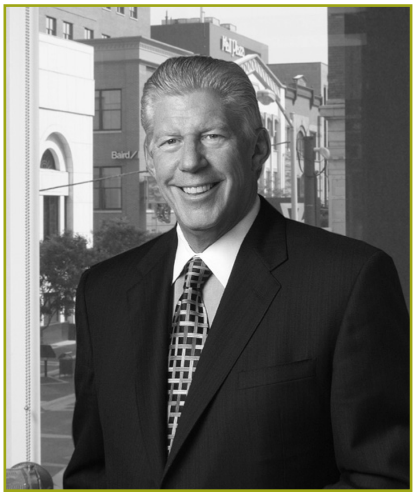

William D. Johnston
Chairman, Greenleaf Trust

Economic Commentary

For the past year, manufacturing data has been lousy and impacted significantly by the steep decline in the energy sector. One month's data is never a trend, but the change in data across a broad spectrum of data points is the first signal that manufacturing may be improving. The Purchasing Managers Index (PMI) is a survey result that is released monthly and generally reported as a percentage of confidence. A result above 50% indicates economic expansion and likewise a report below 50% indicates retraction. As with any survey there are numerous layers of the onion to peel back and examine and so I thought it helpful that we spend some time on it this month.

Who are these purchasing managers and what do they report and why is it important? There are 18 industry sectors reporting data in the monthly survey. The table below provides you a look at what is being reported and how it is assessed.

Index	Feb	March	Change	Direction	Rate	Trend
PMI	49.5	48.2	+ 1.3	contracting	slower	5
New Orders	51.5	51.5	+ 0.0	growing	same	2
Production	52.8	50.2	+ 2.6	growing	faster	2
Employment	48.5	45.9	+ 2.6	contracting	slower	3
Deliveries	49.7	50.0	- 0.3	unchanged	same	1
Inventories	45.0	43.5	+ 1.5	contracting	slower	8
Customer Inventories	47.0	51.5	- 4.5	too low	faster	1
Commodity Prices	38.5	33.5	+ 5.0	decreasing	slower	16
Order Backlog	48.5	43.0	+ 5.5	contracting	slower	9

A PMI index of less than 50% is still contracting but the rate of change of that decline has slowed precipitously and may signal a change that

Commentary, continued

will end the five month slide below 50%. The rest of the data points confirm similar implications. Those that are contracting have slowed their rate of contraction and those that are growing are doing so at either an unchanged rate or a faster pace than previously reported. Commodity prices have now declined for eighteen consecutive reporting periods yet their rate of decline has slowed dramatically.

Of the eighteen reporting industries included in the survey, twelve have reported increases in new orders; two remained stable while four energy-specific sectors reported declines. The employment index grew to 52.8% from January's 50.2% level and that growth of 2.6% was the largest rate of growth in the past five reporting periods as well. Survey comments reflect what we have observed for months. Export is weak but not as weak as it was in the first quarter of 2015. Currency stabilization vis-a-vis the dollar is not likely to be as significant of a challenge to US exporters in 2016 if the currency trend remains in place. Non-energy domestic manufacturing carries a solid backlog of orders and customer inventories are too low for a moderately expanding economy. For the non-energy manufacturing sector this bodes well for 2016. To repeat, one month is not a trend but we will be eager to see the next PMI report.

"We have seen some cooling, in particular metropolitan regions... that may reflect what we are also seeing in the most recent consumer confidence surveys."

The Standard & Poor's/Case-Shiller housing data for the national as well as twenty metropolitan index produced strong results at year end and confirmed the return to 2006 price levels among the regions surveyed. The data revealed the bottom of the market occurred in January of 2012. From that point in time until December 31st of 2015, the S&P 500 Index grew by 46%. Nine of the metropolitan regions grew by rates of greater than the S&P 500 with San Francisco producing a whopping 70% growth in home price during that period of time. In descending order behind San Francisco those regions that reported rates of growth greater than 46% were Las Vegas, Phoenix, Miami, Los Angeles, Atlanta, Detroit, San Diego, Portland and Seattle. Posting growth rates above the national average were Denver, Dallas and Minneapolis while Boston, Charlotte, Chicago, Washington D.C. Cleveland and New York all came in below the national average yet still reported positive growth. Absent artificial stimulation similar to what occurred in the 2003 – 2007 mortgage back security acceleration, rising home prices reflect demand and an underlying stable consumer.

We have seen some cooling, in particular metropolitan regions, in January that may reflect what we are also seeing in the most recent consumer confidence surveys. The recent data out of the Miami region saw an increase in days on market and a growing spread between the ask and negotiated sales price. The Q1 housing data will be interesting to examine.

The Conference Board's survey of households through February 11th revealed a decline of 5.6% from January's strong level of 97.8%. Reflected in the survey's anecdotal comments was an increase in pessimism citing business conditions, financial market volatility and domestic as well as geopolitical conditions. Given the devastating job loss in the energy sector, media concentration on the political primary theater of the absurd and January's market volatility the sentiments are to be understood yet the survey levels are consistent with a moderately expanding economy.

Lastly, auto sales grew 6.8% in January which on an annualized basis projected a 2016 run rate of 17.55 million units, a level last seen in January of 2006. We finished 2015 at a run rate of 17.32 million units. It is likely that the rate of growth will slow from this level but it remains at a very healthy level.

We are close to discovering who the candidates will be for the Democratic and Republican political parties. Once in possession of that knowledge we can begin to understand their national campaign positions and therefore examine the economic implications if they were to gain the White House.

"We are close to discovering who the candidates will be for the Democratic and Republican political parties"

Michael F. Odar, CFA
President

"The daily mission of our collective Client Centric Team is to provide remarkable service through the delivery of holistic wealth management, advanced financial planning and expert trust administration."

A Client Centric Approach to Service

Greenleaf Trust employs a "Client Centric Team" model when servicing all personal trust and wealth management client relationships. This structure was established to maintain the highest benchmark for personalized service and customized solutions. As part of the Client Centric Team service model, each client receives a dedicated team of three professionals to work on their behalf including a Trust Relationship Officer, a Wealth Management Advisor and a Team Service Coordinator.

The daily mission of our collective Client Centric Team is to provide remarkable service through the delivery of holistic wealth management, advanced financial planning and expert trust administration. We pursue this aim by focusing first and foremost on the needs of our clients. We then leverage the collective wisdom of the broader organization (which is now approaching 100 talented professionals) to provide highly personalized service and conflict-free financial solutions tailored to each client's unique situation.

As a result of our Client Centric Team service model, Greenleaf Trust boasts one of the lowest client-to-advisor ratios in the industry. While it is not uncommon within financial services to see advisors in other firms handling several hundred clients, we intentionally limit the number of relationships serviced by each Client Centric Team. This allows each team of three to be highly knowledgeable about the relationships on which they collaborate and readily serve as a client's primary "go-to" contacts on a day-to-day basis.

As echoed in the pillars of our core culture, we believe the collective wisdom of the group exceeds that of the individual. This is again why each of our clients has a dedicated Client Centric Team serving on their behalf. As a client of Greenleaf Trust, you should feel comfortable contacting any of your Client Centric Team members to answer your questions and accommodate your needs. The following highlights the unique skillsets and responsibilities that each individual brings to your service experience.

Who Is My Client Centric Team?

Trust Relationship Officer

Our Trust Relationship Officers often serve as a client's primary relationship contact. They are not only responsible for understanding and assisting clients in achieving their financial, legacy and lifetime goals, but they are also charged with day-to-day account oversight and fiduciary compliance. Trust Relationship Officers monitor the client service experience and provide a trust perspective to all wealth management discussions. Additionally, Trust Relationship Officers will, as needed, coordinate with the client's other professional advisors such as their tax advisor or estate planning attorney to ensure their wealth is managed in a highly personal and holistic manner.

Wealth Management Advisor

Our Wealth Management Advisors use competent critical analysis to achieve target asset allocations and diversification across asset classes to help clients reach their financial goals. Wealth Management Advisors are responsible for the creation and implementation of personalized wealth management plans and investment strategies in addition to providing day-to-day oversight of portfolio management actions. All such responsibilities are carried out in a team-based environment that includes not only the full team of Wealth Management Advisors, but also the team of Research Analysts. Wealth Management Advisors also work with clients and their other trusted advisors to find solutions to complex financial issues such as debt structuring, income optimization, tax reduction, etc.

Team Service Coordinator

Our Team Service Coordinators focus on delivering comprehensive administrative support through day-to-day servicing of account needs. Team Service Coordinators ensure clear communication with clients by coordinating the team's workflow and serve as an ongoing resource to clients and their families.

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George F. Bearup
Senior Trust Advisor

Triggering a Tax Trap to *Save* on Taxes

I ran into an old client over the weekend, a widower of about 15 years, who had a question about the credit shelter trust that was established for his lifetime benefit when his wife died. He wanted to know if his kids, the remainder beneficiaries of the credit shelter trust, will incur capital gains taxes when they inherit the trust assets upon his death.

I answered his question like most lawyers would — "it depends." I informed him that as a general rule, there would be no 'step-up' in income tax basis of the trust assets on his death, since the assets would not be included in his taxable estate.

However, I went on to explain that there was a way to trigger a "tax trap" that would facilitate a 'step-up' in basis upon his death. I have to confess that his eyes quickly glazed over with my explanation, but I encouraged him to visit with his "new" attorney for a quick update to his estate planning documents that might achieve his objective.

"[My client] wanted to know if his kids, the remainder beneficiaries of the credit shelter trust, will incur capital gain taxes when they inherit the trust assets upon his death."

A brief background of the "trap" and planning technique follows- assuming your eyes have not yet glazed over, too.

The credit shelter trust (a foundational building block of many existing estate plans) that benefited the widower contains a testamentary limited power of appointment, which gives to him the right to direct assets held in the trust on his death, to a group that consists of his descendants. That testamentary limited power of appointment is what can be exploited to allow his children to avoid capital gains tax after his death.

Generally, possessing or exercising a limited power of appointment does not result in a taxable transfer for federal estate and gift tax purposes. But there is one important exception to that general rule. It is known as the "Delaware Tax Trap."

Prior to 1995, Delaware had a rule (it has since abolished the rule) against perpetuities which applied to trusts created by the exercise of a power of appointment. The rule measured from the time that the power was exercised, not from the time of the trust's creation (which is the normal rule) to measure when a power of appointment is created. Consequently, it was possible to create a perpetual trust in Delaware simply by creating and exercising successive limited powers of appointment over and over, which could potentially avoid estate and generation skipping taxation in perpetuity.

In response to the possibility, Congress passed regulation to close the loophole. It subjects a trust to federal estate taxation at the lifetime beneficiary's death if that beneficiary exercises a power of appointment "by creating another power of appointment, which under applicable local law can be validly exercised so as to postpone the vesting of any estate or interest in such property or suspend the absolute ownership or power of alienation of such property for a period ascertainable without regard to the date of the creation of the first power." Distilling that wordy tax code rule, if a beneficiary exercises a limited power of appointment that extends the term of the original trust beyond what was originally contemplated, the trust value will be included in the beneficiary's taxable estate. Hence the adjective 'trap' is appropriate.

However, here is where it can work to an individual's benefit. Suppose the 'trap' is intentionally sprung as part of their estate plan to deliberately force the inclusion of trust property in the beneficiary's taxable estate.

In my old client's case, by including the value of the credit shelter trust in the widower's taxable estate, it will not be subject to estate tax due to his estate's available estate tax exemption amount ($5.45 million), and there will be a full basis 'step-up' upon his death. Simply by amending his estate planning documents to exercise his testamentary limited power of appointment to extend the trust for the benefit of his children in lieu of an outright distribution to the children, the continuing trust(s) assets would achieve a step up in cost basis. The trust(s) created for his children can potentially terminate once the assets are sold by the trustee, leading pretty much to the same outcome as the family planned.

Obviously, this might not be a good strategy if the widower already had a taxable estate, but with the dramatic increase in the exemption equivalent over the past few years, even with intentionally triggering the "tax trap" it will not cause his estate to be subject to federal estate taxes.

This discussion is all part of what is known as 'basis bump planning' which is the intersection between estate planning and income tax planning. This can be particularly helpful to a family where the assets held in trust have appreciated substantially since the first spouse died.

The opportunity to obtain a 'step-up' in income tax basis of trust assets for subsequent sale, or where enhanced depreciation deductions by the remainder beneficiaries would be beneficial, should not be overlooked.

While I have related this estate planning technique to a deceased spouse's trust, any irrevocable trust should be reviewed to determine if this strategy could be beneficial. If you are a beneficiary of an irrevocable trust with highly appreciated assets that does not contain a limited power of appointment, consider having a trust protector, if there is one, amend the trust to provide the lifetime beneficiary a testamentary limited power of appointment. Or, consider asking the trustee to decant to another trust where the lifetime beneficiary is given the limited testamentary power of appointment, which is necessary to 'trigger the trap' while also protecting the assets subject to the testamentary limited power of appointment from any creditor claims against the beneficiary or his or her estate.

"This discussion is all part of what is known as 'basis bump planning' which is the intersection between estate planning and income tax planning."

Sharon A. Conran, JD
Vice President
Trust Relationship Officer

"When developing your estate plan, it is a good idea to consider who your beneficiary truly is and, more importantly, what tools they possess."

What a Tangled Web We Weave

Have you ever looked closely at a spider web and thought about the complexity of the web or how much planning must have gone into building the web? If you look closer at the web, you may notice that it has snared an unsuspecting victim who is struggling to gain control and escape the snare of the web.

Using the web as an analogy for estate planning, I think about all the planning and development that goes into an individual's estate plan. When you develop your estate plan you, like the spider, try to tie in all the strings of your life to create a plan that will provide for your beneficiaries as you intended.

In my many years as an estate settlement officer, I have witnessed the struggles of individual beneficiaries who are unprepared or incapable of handling sudden wealth or dealing with a trustee who is not the decedent. These beneficiaries often feel that they are trapped, not unlike the unsuspecting victim in the web. These feelings can result from beneficiaries feeling that they are not in control of the situation, surprised by your estate plan, having unrealistic timelines, or just not being prepared to receive an inheritance.

When developing your estate plan, it is a good idea to consider who your beneficiary truly is and, more importantly, what tools they possess. By doing so, you can determine the best distribution plan for that beneficiary and, hopefully, avoid having the beneficiary feel as if they are "trapped" by the process of your passing rather than appreciative of your efforts in developing your estate plan.

When determining who your beneficiary is you should look not only at the skills the individual possesses but more importantly, the way the beneficiary handles different situations.

First and foremost, you should consider the fact that each and every person will handle the grief of your passing in a different way. There are several stages of grief and each stage is handled differently for each individual. For some individuals, it may take several years to proceed through the stages of grief and may hinder the individual's capacity to properly handle any matters related to your death. That being said, you should look at how your beneficiary has processed various changes during his or her life and determine whether he or she is able to cope with change. Observe whether the individual goes to extremes; do they get angry, or do they deny what has occurred? These observations may help you determine whether or not you decide to distribute your assets outright to a beneficiary, retain those assets in trust for the benefit of the beneficiary for their lifetime (with directives as to when and for what purpose funds should be distributed) or, retained in trust for a period of time and then distributed outright to the beneficiary upon a set time period or other satisfied condition.

Other factors to consider when determining a distribution plan for your assets to beneficiaries include, but are not limited to:

- Does the beneficiary like to be in control of a situation or more content to sit back and let someone else handle the situation? The answer to this question could determine whether or not you put this beneficiary in an additional role or alert them in advance that they will not be in charge of the administration of your estate.
- Will the beneficiary know what to expect? If you are planning on establishing a trust for a beneficiary, are they aware that they are not receiving the assets outright? Do they know what will be required of them to receive funds from the trust?
- Will the beneficiary have realistic timelines for the estate administration? Often, beneficiaries assume that with a trust the assets are distributed immediately. They feel trapped and at the mercy of the trustee when they don't get their inheritance immediately. Beneficiaries who do not understand the process feel they are not being treated fairly and often blame the decedent for creating a "bad" situation for them.
- Does the beneficiary have the knowledge/tools to manage an inheritance? Has the beneficiary been active in financial matters? If your spouse is the beneficiary does he or she know what your assets are and what the income stream of those assets is? Does the beneficiary take an active role in managing the household finances and are they fiscally responsible? Is the beneficiary working with you and your advisors and does he or she know where information on your assets is located? If the beneficiary is not active in financial matters is he or she willing to educate themselves in financial matters or will they need guidance or need to prove themselves knowledgeable prior to receiving a large distribution?
- What are the spending habits of the beneficiary? Is the beneficiary the type of person who is thoughtful about purchases or one that buys first and then thinks about how to pay for a purchase? Does the beneficiary borrow money to obtain items rather than plan for the purchase by saving? Have you loaned money to the beneficiary for the purchase of an item and has the loan been paid back in a timely manner? Has the beneficiary struggled with credit card debt or filed for bankruptcy?
- Does your beneficiary have a pattern of gifting to others without thought to his or her own needs? This consideration usually occurs when one spouse gifts money to children upon their asking. Does the beneficiary have a tendency to be kindhearted and would give all to

"Has the beneficiary been active in financial matters? If your spouse is the beneficiary does he or she know what your assets are and what the income stream of those assets is? Does the beneficiary take an active role in managing the household finances and are they fiscally responsible?"

Tangled Web, continued

others without a thought to his or her own needs? Does the beneficiary give money to family members upon request because they can't say no under the pressure of the requests?

- Is the beneficiary earning an income through employment? Does the beneficiary have a strong work ethic? Does the beneficiary jump from one job to the next? Does the beneficiary earn enough income to support him or herself? Is the beneficiary likely to stop working upon receipt of a large inheritance? Is the beneficiary unable to work due to health or other reasons?
- Does the beneficiary have health concerns? Is the beneficiary in good health or is the beneficiary facing a health crisis? Do you anticipate the beneficiary will need long-term care and how would an inheritance affect any governmental benefits? Is the beneficiary a special needs individual and, if so, how would an inheritance affect current governmental benefits?
- Does the beneficiary have debt issues? Is the beneficiary carrying a large amount of debt (credit card/mortgages)? Has the beneficiary ever filed for bankruptcy or currently facing a potential bankruptcy?
- Do you believe the beneficiary may file for divorce? Has the beneficiary encountered marital problems in the past?
- Do you believe the beneficiary may be a candidate for a lawsuit or other court action? Has the beneficiary encountered legal problems in the past?
- How will the beneficiary handle working with a Successor Trustee who requires documentation for discretionary distribution requests and questions the purpose of the request as part of the Trustee's fiduciary duty? When assets remain in trust for the benefit of a beneficiary, the beneficiary often feels like a victim, or as if being punished, but if provided with good advisors who can educate and work closely with the beneficiary the beneficiary more often than not will understand the thoughtfulness you took in developing your plan.
- What are your wishes for the beneficiary? Do you want the inheritance to pay for the beneficiary's education or other specific purpose? Do you want to ensure that the beneficiary has an income stream for their lifetime? Do you want to provide peace of mind to your beneficiary?

"The ultimate decision for the distribution of your assets lies with you. Your estate planning documents can… provide your guidance to your beneficiaries after you are gone."

The ultimate decision for the distribution of your assets lies with you. Your estate planning documents can be drafted in a way that not only distributes your assets but can also provide your guidance to your beneficiaries after you are gone. Like the spider web, you can develop and create an estate that will allow your beneficiaries the capabilities to handle the inheritance and appreciate the gift you have left for them.

Brexit: Will the United Kingdom Leave Europe?

John Graham
Guest Contributor

As a long-time friend of Greenleaf Trust specializing in foreign economic and financial markets, John Graham shares his global investment perspective as a guest contributor in this month's *Perspectives*. John is a founding member of Rogge Global Partners headquartered in Great Britain and former head of JP Morgan's Multicurrency Asset Management Practice in London.

On June 23rd, the United Kingdom will vote on whether or not to remain in the European Union, an event dubbed "Brexit" – British Exit from Europe. Will the UK decide to leave the European Union and, if so, what does that mean for the US investor?

The Hot Button — Immigration

The UK must by EU law allow EU citizens to work in Britain. This has led to a wave of immigration from recently admitted Eastern European countries. Not only do these immigrants compete with the domestic population for jobs, but are they entitled to social benefits which must be paid for from the UK tax base. Moreover, EU law and EU agreements have forced the UK to accept many non-European Union immigrants who, again, are entitled to benefits and compete for jobs. All this comes on top of Britain's Commonwealth legacy which has brought many immigrants from ex British colonies to live in the UK. While this immigration flow is, over the long run, beneficial for the UK economy, improving productivity and reducing the dependency ratio (see below), on the ground, immigrants are real people competing for real jobs in an economy which has seen a long term decline in traditional manufacturing and heavy industry jobs. Moreover, the social benefits to which these immigrants are entitled are paid from the UK taxpayer's pockets. Images from the Calais refugee camp and the recent Syrian migration are played daily on UK and European television keeping the immigration issue hot.

"… opponents of the UK's continued membership in Europe point to the erosion of British sovereignty…"

This situation has outraged many working class voters in both the Labour and Conservative parties. In fact, there is now a political party solely dedicated to this issue: UKIP (the United Kingdom Independence Party) which draws voters from both sides of the political spectrum. Critics of the EU also point to several other issues:

Brexit, continued

Sovereignty

Closely allied to the issue of immigration, opponents of the UK's continued membership in Europe point to the erosion of British sovereignty in things like fighting terrorism. EU law and the European Court of Justice via the European Human Rights Convention have prevented the imprisonment and/or deportation of several high profile terrorist suspects. Continued frustration with her inability to exercise control over domestic affairs has led the parts of the British political establishment, egged on by the right wing press (The Daily Mail and Telegraph among others) to seek ways of loosening the governance bonds between London and Brussels.

Cost

Britain joined the EU in 1973 by governmental assent, a move ratified in 1975 by the Heath Government. Since then, the UK has become more and more closely tied to the EU receiving many benefits, but at a cost. The UK is the third largest net contributor to the EU budget, paying in £14 billion per year while receiving £7 billion per year in benefits and subsidies.

> "While it is clear that EU membership provides many benefits, the cost of "red tape" (reporting, registrations, etc.) is estimated at £33 billion per year."

Red Tape and Loss of Competitiveness

Those in Britain who wish to leave Europe also point to the business costs of EU membership. While it is clear that EU membership provides many benefits, the cost of "red tape" (reporting, registrations, etc.) is estimated at £33 billion per year. It is argued that not being subject to EU regulations would significantly enhance the competitiveness of the UK in world trade. As we all know, though, there are no free lunches. So, what would it cost Britain to leave the EU? The disadvantages to Brexit are as follows.

Loss of Access to the European Trading Area

Europe represents 44.5% of the UK's exports of goods and services. Some "UK Out" campaigners argue that Britain would be able to negotiate membership in the European Economic Area giving her full access to the internal European Market as Norway has done. This is far from given especially considering the fact that the rancour induced by the referendum campaign will reverberate throughout Europe (see the costs to Europe below) encouraging the EU to put a heavy cost on withdrawal in order to prevent others from leaving.

Need to Replace Benefits and Subsidies

The British economy receives a huge swath of subsidies and benefits from the EU. On a net basis, the UK would be better off outside the EU, but individual sectors, like agriculture, would be very hard hit once subsidies were withdrawn.

Lower Inflows of Investment and Labour

It is clear that once the UK loses its access to European markets, investors who use the UK as base for European manufacturing and distribution may want to relocate. This applies to both the industrial sector and the financial sector, Britain's largest earning industry. Moreover, the UK, like all of Europe, has an aging population (UK median age – 40.4, Germany – 46.1, Italy – 44.5, versus India – 27 or Iran – 28). However controversial, immigration is particularly beneficial to these "older" countries as it brings in young, tax paying workers thereby improving the dependency ratio (the ratio of the working age population to the retired population). Were this flow to be cut off, it would exacerbate the UK's demographic problems.

Breakup Pressure

In September 2014, Scotland voted narrowly to stay in the United Kingdom. Given the recent drop in oil, Scotland is, more than ever, dependent of fiscal transfers from the UK and Europe. Should the UK part from Europe, it is likely that further pressure on the Union would occur leading, perhaps, to another vote in Scotland and "English votes for English laws" legislation Parliament. In recent weeks, intense negotiations have been taking place across Europe to address UK concerns and create a package of reforms which will satisfy not just Britain, but other countries with objections to how the EU is run. The reason for the intensity of conversations is that migration has become a Europe wide issue and the cost of Britain leaving is high for Europe herself. The main European worries are as follows.

EU Breakup Pressure

The EU, already split on how to deal with Greece (a situation which is likely to become hot again this year as little progress is being made on economic reform), will face further calls for referenda on membership — Denmark, Finland and Portugal are all candidates. Moreover, Brexit would increase regional pressure for separation. Places like Catalonia

"The EU… will face further calls for referenda on membership – Denmark, Finland and Portugal are all candidates."

Brexit, continued

and Northern Italy already have significant movements which support a looser federation or outright independence from their home countries.

Loss of Access to the UK

The UK is a significant trading partner for Europe. The EU has a £61 billion pound surplus in its trade with the UK. This trade is dominated by the goods sector. Hence, loss of access to the UK as market would be very problematic for European manufacturers and European jobs.

Loss of Income

Britain pays 0.5% of its GDP to Europe each year in Value Added Tax. This is the second highest contribution to the European budget after Germany. Why though, should US investors care about this European problem? As we saw during the recent periods of crisis in Europe over Greece, uncertainty in Europe can have a destabilizing effect on the US markets via the banking, trade and financial market links between the two countries. The main points of concern for the US investor would seem to be:

> “One longer term impact of Brexit would be a further extension of the regulatory pressures that are currently severely impacting market liquidity.”

Currency

Brexit will most likely put further upward pressure on the US Dollar as global investors with exposure to the UK and Europe seek out a safe haven for their assets. The negotiation period over the final details of Brexit (if approved) extends out to 2019 so there will likely be periods of intense uncertainty until then. As the US Dollar is already overvalued on a trade weighted basis, Brexit could have a further negative impact on the trade in US goods and services putting pressure on stock prices for those companies in the international sector.

Credit Market Volatility

In the run-up to the referendum, if the polls are close, Gilts, Bunds and Treasuries will all likely rally while peripheral european countries’ bonds will likely suffer. In the credit markets, Financials are likely to be especially vulnerable as London’s dominant position in these markets will be under threat. It is likely that European share markets would also be affected though it is reasonable to assume a differentiation between the core markets and those on the periphery. In the past, volatility in Europe has spilled into the US stock market via the financial sector.

Market Barriers

One longer term impact of Brexit would be a further extension of the regulatory pressures that are currently severely impacting market liquidity. It is hard to envision a post-Brexit world where trade and capital flows are not negatively impacted both by the events of Brexit itself and the threat of further decentralization of power across the globe.

Will Brexit Happen?

The impetus for this referendum has the right wing of the Conservative party as its power base. As such, the Prime Minister, David Cameron, was forced to promise a referendum for the sake of party unity during the June 2015 election. However, it is clear that within the Labour Party there are also unionist and working class elements which are both unhappy with the current levels of immigration and the proposed US-EU Transatlantic Trade and Investment Partnership (TTIP). The pro Brexit camp is terribly divided at this point, wrangling among themselves about who should lead the "Out" campaign. While the bookmakers here in the UK remain confident that Britain will remain in the EU (odds now at 9-4 against leaving), public opinion is much more divided with most polls showing at least 50% for leaving and some showing a higher percentage than that. David Cameron has recently negotiated a deal with the EU to relax some of the restrictions on the UK. Importantly, this includes a "brake" on immigration both in terms of numbers and payment of benefits. Opinions are divided on whether this deal is a good one. However good the deal though, it is clear that with immigration and illegal migration in the mix, Brexit is a terribly emotive issue, not just in the UK, but also in Europe. (Angela Merkel has used up all the political capital she gained by successfully dealing with Greece by trying to be "reasonable" about migration.) With the right wing press keen to drive Brexit forward, it will be a long, tense spring for David Cameron and the markets.

"The pro Brexit camp is terribly divided at this point, wrangling among themselves about who should lead the 'Out' campaign."

Lorey L. Matties
Participant Services Specialist

Coming Soon for Our Retirement Plan Clients…

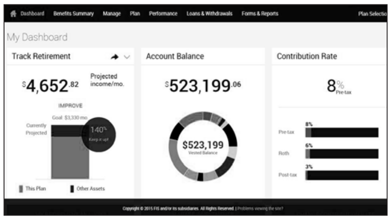
At Greenleaf Trust, our core values are the foundation for the way we work and do business, and are an integral part of how we conduct ourselves in the service of our clients. We are Client Focused. First and Foremost. We believe in Continuous Improvement.

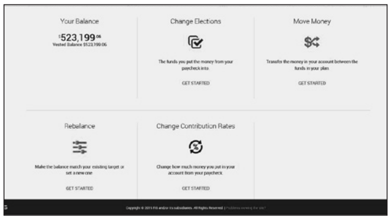
With our core values in mind, the Retirement Plan Division is pleased to announce an enhanced web experience for both participants and plan sponsors coming Spring 2016.

> "… the Retirement Plan Division is pleased to announce an enhanced web experience for both participants and plan sponsors…"

Key enhancements for the Participant

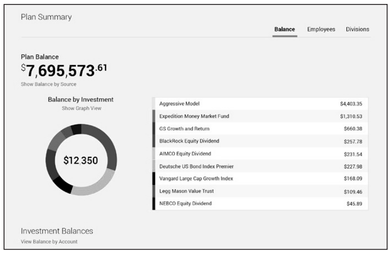
- User friendly dashboard illustrating participant retirement goals, account balances and performance
- Informative transaction landing pages and guided wizards to assist participants with managing their plan accounts
- Automated contribution increases, account rebalancing and recurring distributions
- Real time account recording and transactional alerts





Key enhancements for the Plan Sponsor:

- Consolidated and comprehensive plan information
- Full participant emulation supporting view-only and full access capabilities
- Error-free, automated payroll processing via the Data Validation Center
- On-demand plan level and participant reporting



Communications will be provided to both our plan sponsors and participants over the coming weeks. In the meantime, please contact our Retirement Plan Division with any questions.

Could Rising Inflation Deflate Equity Prices?

Daniel C. Haines, CFA
Fixed Income Analyst

With commodity prices falling dramatically and inflation struggling to reach 2%, many investors forget about the double-digit inflation experienced during the 1970's and early 1980's. In fact, inflation (as measured by CPI) has not increased at a rate over 5% year over year since 1990. Recently, there has been more talk of deflation than rampant inflation. However, it is worth considering how either of these situations would impact equity markets. In this article we will look at the complex drivers of this relationship.

To start our discussion, let's think about the equity market as a business where the value of the business is determined by the present value of its future expected cash flows. To determine this value we must estimate the growth rate of the future cash flows and the appropriate discount rate. The growth rate depends on inflation, real economic growth and changes in profitability. The discount rate depends on a risk-free rate (usually a US Treasury security) which is influenced by inflation and an additional risk premium for the risk of owning equities. As we look at inflation it's helpful to consider how it impacts growth expectations and the discount rate.

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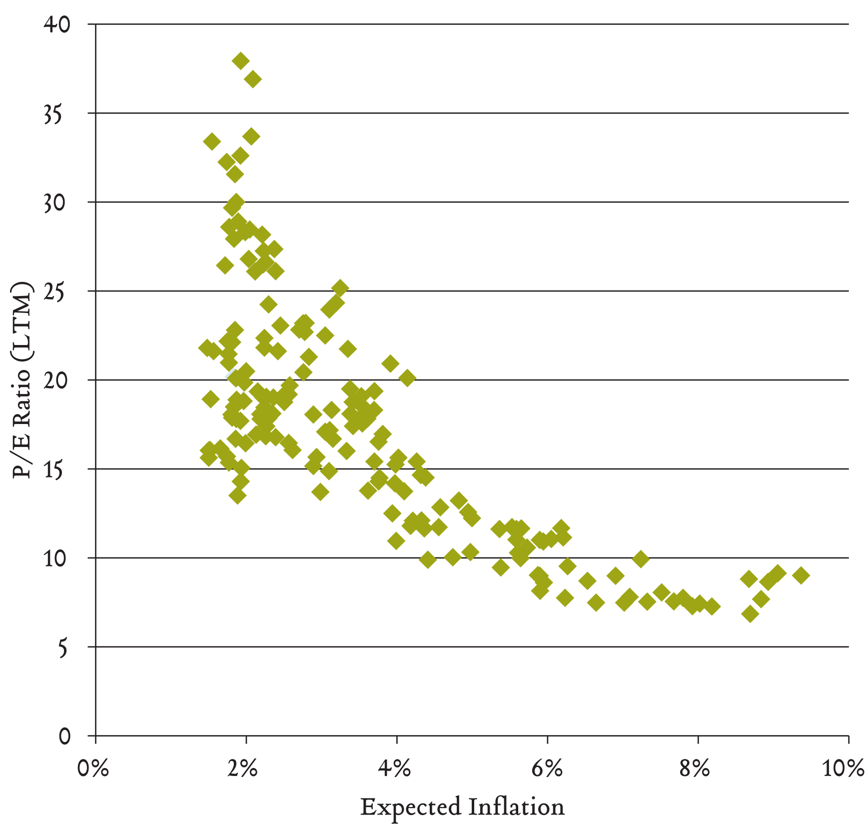
First, let's look at the case of high inflation (for the purpose of this exercise, we will consider high inflation to be over 5%). From an economic perspective, high inflation could indicate an overheated economy and lead the Federal Reserve to enact restrictive monetary policy. This restrictive economic policy will likely slow down economic growth which lowers the growth rate of expected future cash flows in our example. Another way to look at this is that higher inflation will raise the discount rate used to find the present value of future cash flows. On its own, this would be a negative; however, it could be offset by higher growth rates. This is not often the case though as businesses may not be able to pass along higher costs to their customers. A third way to think about high inflation is that it can lead to more uncertainty in the markets which also increases the discount rate as investors become more risk-averse. In general, high and rising inflation has a negative impact on equity market returns.

Next, let's look at the case of very low inflation or deflation (inflation under 1% for our purposes). From an economic perspective, very low inflation can signal that economic growth is very weak, leading to a lower growth for expected future cash flows. Easy monetary policy will likely be in place as the Federal Reserve attempts to stimulate the economy. This could boost the expected growth rate, depending on how much confidence the market has in the central bank's ability to stimulate economic growth. Looking at the discount rate side of the equation, the impact can be mixed. Lower inflation would likely reduce the risk free rate, while weak economic growth would likely increase investor risk-aversion and drive up the risk premium for owning equities.

In the middle of these two extremes is what is considered a more "normal" range for inflation. Inflation of 2%-4% is often seen as the healthiest level for higher equity valuations. The chart below graphs the P/E Ratio of the S&P 500 against the expected level of inflation for the next year for the period of 1970-2015. As you can see, expected inflation between 1.5% and 4% has been the sweet spot for higher equity multiples. When expected inflation has been above 5%, P/E multiples have been under 12x.

"In general, moderate levels of inflation have been most conducive for equity valuations."

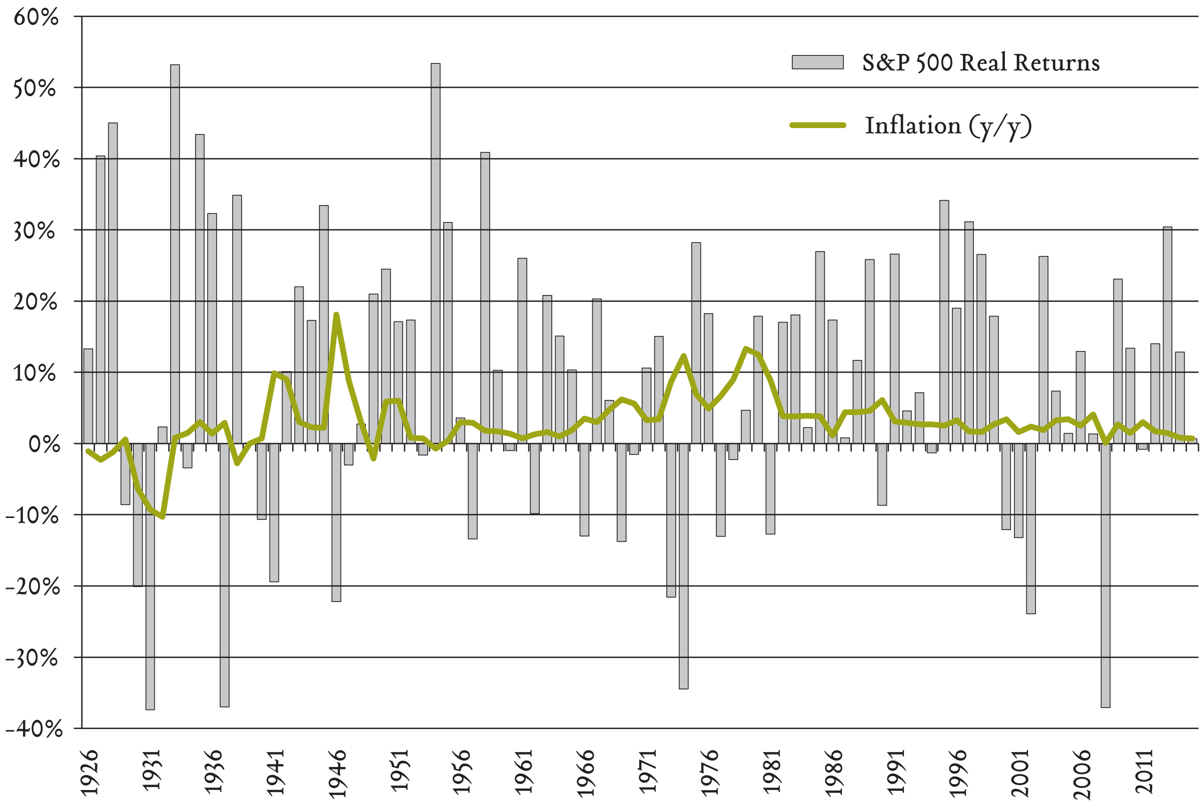
P/E Ratio vs Expected Inflation



Source: Robert Shiller, Federal Reserve Bank of Philadelphia

Inflation can interact with equity prices in numerous ways and there is not an exact relationship, as other factors have a large impact on equity returns. On the other hand, high and rising inflation and outright deflation have been negative for equities. In looking at history, high and increasing inflation accompanied poor equity returns at periods during the 1940's and the 1970's. Around the great depression, deflation was present as equity markets sold off. On the other hand, the stable inflation levels seen since the early 1980's provided the base for strong equity returns during the 1980's and 1990's.

Inflation and Equity Real Returns



The Federal Reserve currently expects long-run inflation of around 2%. We do not expect rampant inflation or deflation in the near future but either is possible. Inflation in the low-single-digits should be supportive of equity multiples, although, we believe multiples could still contract from currents levels as they are above historical averages.

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Stock Market Pulse

Index	2/29/2016	Total Return Since 12/31/2015
S&P 1500	445.49	-5.04%
DJIAK	16,516.50	-4.68%
NASDAQ	4,557.95	-8.76%
S&P 500	1,932.23	-5.09%
S&P 400	1,334.20	-4.36%
S&P 600	636.03	-5.12%
NYSE Composite	9,559.53	-5.76%
Dow Jones Utilities	620.70	8.11%
Barclays Aggregate Bond	110.09	2.14%

P/E Multiples	2/29/2016
S&P 1500	16.6x
DJIAK	15.4x
NASDAQ	19.7x
S&P 500	16.5x
S&P 400	18.0x
S&P 600	17.9x

Key Rates

Fed Funds Rate	0% to 0.25%
T Bill 90 Days	0.32%
T Bond 30 Yr	2.62%
Prime Rate	3.50%

Current Valuations

Index	Aggregate	P/E	Div. Yield
S&P 1500	445.49	16.6x	2.25%
S&P 500	1,932.23	16.5x	2.31%
DJIAK	16,516.50	15.4x	2.71%
Dow Jones Utilities	620.70	NA	3.39%

Spread Between 30 Year Government Yields and Market Dividend Yields: 0.37%

MAIN OFFICE:
211 South Rose Street
Kalamazoo, MI 49007
office: 269.388.9800
toll free: 800.416.4555

TRAVERSE CITY OFFICE:
125 Park Street, Suite 495
Traverse City, MI 49684
office: 231.922.1428

BIRMINGHAM OFFICE:
34977 Woodward Ave., Suite 200
Birmingham, MI 48009
office: 248.530.6202

PETOSKEY OFFICE:
331 Bay Street
Petoskey, MI 49770
office: 231.439.5016

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e-mail: trust@greenleaftrust.com
www.greenleaftrust.com