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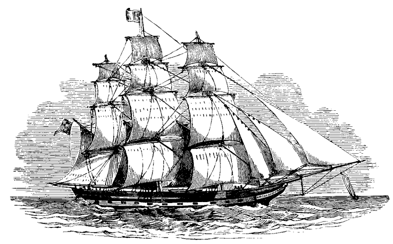

Pilot Capital Management
Quarterly Investment Commentary

Date: July 10, 2016
From: Greg Staub, CFA, Ph.D.; Matthew Staub, CFA
To: Pilot Capital Clients & Friends

Dear Clients and Friends,

Your reports for the second quarter of 2016 are enclosed. This letter gives a review of the quarter and briefly summarizes our current investment views.

Second Quarter 2016 Market Review

Market/Index	2015 Close	As of June 30th	Month Change	*Quarter Change*	Year-to-Date Change
DJIA	17425.03	17929.99	0.80%	*1.38%*	2.90%
S&P 500	2043.94	2098.86	0.09%	*1.90%*	2.69%
Russell 2000	1135.89	1151.92	-0.25%	*3.40%*	1.41%
Global Dow	2336.45	2312.12	-1.18%	*0.20%*	-1.04%
Fed Funds	0.25%-0.50%	0.25%-0.50%	0 bps	*0 bps*	0 bps
10-Yr Treasury	2.26%	1.46%	38 bps	*-33 bps*	-80 bps

In the world of equities, the second quarter of the year was anything but dull. April saw the large-cap S&P 500 and Dow make marginal gains, with the small-cap Russell 2000 and the Global Dow leading the way for the month. The Fed left interest rates at their 0.25%-0.50% range, noting that economic growth had slowed since the beginning of the year. May ended up being another good month for equities as each of the indexes listed here posted positive monthly returns headed by the tech-heavy Nasdaq (3.62%) and small-cap Russell 2000 (2.12%). June started out with relatively lackluster returns for stocks as labor added only 38,000 new jobs and the Fed, once again, reiterated its reluctance to raise interest rates based on lagging inflationary trends, weakening in the jobs sector, and sluggish exports.

But the month and quarter ended with quite a bang, primarily precipitated by the UK's referendum vote to withdraw from the European Union, which sent stocks around the world into a dramatic tailspin, felled the British pound by over 10%, and drastically cut some long-term bond yields (see Japan). Nevertheless, by the last day of the quarter, stocks seem to have weathered the storm and regained much of what they had lost. Of the indexes listed here, only the Nasdaq lost value quarter-to-quarter. On the plus side, the Dow and S&P 500 posted quarterly gains of 1.38% and 1.90%, respectively.

Gold continued to increase in value, closing the month and quarter at $1,324.90. Long-term bond yields hit the skids as investors poured money into bonds, boosting bond prices and narrowing yields.

A Note on Brexit

In the days following the UK's non-binding vote to leave the EU, the British Pound (£) fell by 11.5% and European equities fell 10%. US Equities also followed the downward trend, albeit by a smaller margin. Some reaction was expected as Brexit would affect the non-UK world in several ways. A UK departure from the EU would create friction in global trade, most notably in financial services. It is important to remember, however, that the UK accounts for just 4% of global GDP. So, what's the big deal?

Uncertainty. Brexit raises the level of global uncertainty, and it does so amid a backdrop of frustratingly slow global growth. In this context of tepid global growth, slowing corporate earnings and already volatile financial markets, Brexit has been particularly unhelpful.

On the surface it appears Brexit will be another headwind to global growth, likely leading to increases in or extensions of economic stimulus in many parts of Europe. The big question is whether or not the softening in growth actually brings about a true recession scare, and the answer to this will only be known in time. At this moment, the market seems to be agreeing with the consensus expectation that the impact on growth will be minor and manageable.

Outlook & Positioning

The largest negative contributor to performance in all of our portfolio models over the last 12 months were the positions in the more economically sensitive areas of the fixed income market. Less-than-investment-grade bonds were hurt badly when the price of oil collapsed last year and put repayment of debt owed by energy companies in jeopardy. This carried over into non-energy, lower-quality bonds in general. The energy holdings in funds we own in this sector was and remains very low (<5%). We also learned that post Dodd-Frank, liquidity in the bond market is not what it used to be. About half the drop in value in high yield bonds that occurred in 2015 and early 2016 has been recovered and we believe that a gradual recovery will continue. We believe this for two reasons: 1) The managers that we use in this sector of the bond market are among the best credit analysts in the business and are not often wrong about being paid back over the long run, and 2) This is the only area of the bond market where genuine opportunity exits and we anticipate remaining in a low rate environment for an extended period of time. New issuance of lower grade debt has dropped considerably and demand is picking up due to an influx of foreign funds driven by Brexit chaos in European markets. Shrinking supply and increasing demand inevitably lead to higher prices. We will continue to hold these positions at their current weight but do expect more volatility ahead.

The value portion of our equity portfolio is experiencing the worst period of underperformance to the S&P 500 ever by value strategies versus growth strategies. This has been driven by low growth, low interest rates, and unrelenting uncertainty. We have a long history with our managers in this area and over time they do demonstrate an ability to outperform the S&P. However, at times they can try one's patience. We have confidence in these managers and do not plan on changing the positions. Their weights in the portfolio reflect a market underweight for value strategies, although this can be a moveable feast depending on whose definition of value you use. Both managers have a long track record of being able to compound money at a reasonable cost for their shareholders which we value very highly.

We are currently monitoring three opportunities:

International Stocks
The international portion of the portfolio was neutral to benchmark performance – international stocks did relatively poorly, but our portfolios were generally underweight or at market weight. We could increase our international exposure to a global market weight but are concerned that Brexit has touched off a prolonged period of uncertainty in Europe. European equities are selling at a lower PE than US equities, but given the general economic uncertainty surrounding Europe one could argue that this is deserved. Right now the P/E of developed Europe is about 14x, should it get to the 10x – 11x we saw in 2008 and 2012-13 we would bring the positions to a market weight or overweight.

Small Cap Stocks
We are also considering increasing our small cap exposure to a market weight since we have been underweight (which has helped our accounts) for close to two years. However, unless credit conditions improve it would be difficult to see small companies outperform for more than brief periods of time.

Value Stocks
The most promising opportunity is increasing the value component of the portfolio to a market weight as this has the best chance of outperforming by reverting to the mean in the least amount of time.

Thank you for your continued trust and confidence in Pilot Capital Management. As always, should there be any questions, please don't hesitate to contact us.

Sincerely,

Greg Staub, CFA, Ph.D.
President

Matthew Staub, CFA
Vice President