CK
ADVISORS, LLC

July 19, 2016

Dear Clients:

CK Advisors gave back some of its strong start to the year, with our composite rising 1.4% (after fees) versus a 2.5% advance in the S&P 500. For the year, we are clinging to a slight lead over the Index with our composite up 4.3% against the benchmark's gain of 3.8%. We had been having a good quarter until June 23rd, when the United Kingdom held its referendum related to staying in the European Union.

In the aftermath of the surprise "Brexit" result, U.S. stocks fell sharply for two days, followed by a near complete reversal in the waning days of the quarter. While the market averages did not suffer any noticeable damage over that period, the vote outcome did have a pronounced adverse impact on several of our cyclical holdings. Moreover, the recovery was driven by defensive sectors (Utilities, Telecom & Consumer Staples) where we lack exposure. Valuations of stocks in these groups were already rich and rose to even loftier levels after the vote.

Going into the vote, the U.S. Federal Reserve was signaling additional steps to normalize interest rates. After Brexit, the Fed got cold feet and U.S. interest rates fell sharply. This decline was exacerbated by foreign buyers looking for safety and positive yield compared to the negative rates that are popping up elsewhere.

We continue to believe bond investors are chasing miniscule returns for the risks they are assuming. Consequently, we are steadfast in our belief that keeping our balanced account clients in shorter dated maturities will eventually prove to be wise. Although we aren't foregoing much yield, our defensive posture certainly looks premature in the wake of Brexit and a Fed that seems perpetually stuck in neutral. There is a growing chorus of criticism that the Fed is creating asset bubbles that could pop without warning.

Investors have a lot to worry about these days. In addition to the impact of Brexit on business activity in Europe and on the cohesiveness of the remaining EU members, investors continue to grapple with sluggish global growth, growing terrorism fears and depressed energy markets. The U.S. election is an added element of concern, with populism driving unhealthy anti-trade and anti-business rhetoric.

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It appears stocks are increasingly being supported by the easy money policy of the Fed. Fortunately, the domestic economy continues to chug along and market participants are very bearish with record amounts of cash. This situation is not typically a harbinger for a bear market in equities. Finally, though early in the reporting season, second quarter corporate earnings have been surprisingly good.

Shifting to individual securities, our best performing stocks were UnitedHealth Group, Medtronic, Johnson Controls and Tyco International. Our energy stocks also contributed, helped by a modest recovery in oil. United's stock did well partly because investors rotated into defensive groups but also because of the company's bright prospects. United is generally executing in its health care insurance businesses, driving share gains across the commercial, Medicaid and Medicare markets. United's well-publicized failure to serve the health care exchanges under the Affordable Care Act has been a costly endeavor. However, the company plans to exit most of these exchanges, eliminating the potential for sizeable ongoing losses.

A key differentiator for the insurer is its ownership of Optum, which should soon contribute about half of company earnings. Optum provides health care services such as urgent care centers and pharmacy benefit management. It also offers consulting, data analytics and other technologies which help customers operate more efficiently and improve their quality of care. Optum is growing more rapidly, has higher margins and is less cyclical than United's health insurance business. Accordingly, investors deservedly give the insurer a higher multiple than its peers.

Medical device maker Medtronic's shares were spurred by an upbeat investor meeting where management projected accelerating long-term earnings growth. There are several reasons for this improvement. Most importantly, Medtronic has increased R&D productivity and developed a robust new product pipeline, boosting the outlook for top line growth. There is also an opportunity to expand margins due to cost of goods reduction, SG&A leverage and synergies derived from the recent acquisition of device maker Covidien. Finally, tax benefits from this acquisition will allow Medtronic to access cash in a much more tax-efficient manner. The deployment of this additional cash for share buybacks or acquisitions should enhance the company's earnings.

Earlier this year, Johnson Controls and Tyco International entered into a merger agreement which is due to close this fall. Investors appear to be warming to the transaction as they glean more information about the combination. The merger has strategic merit. JCI is a leader in building products, controls and services. Tyco is one of the top providers of fire and security products and services. Their offerings are highly complementary, creating the most comprehensive portfolio of building products and services with tremendous cross-selling potential. Shortly after the merger JCI will spin off its cyclical auto segment but retain an attractive battery business, which has good growth prospects and mainly serves stable aftermarket customers. Post spin, JCI will have a multi-industrial portfolio of businesses with strong competitive positions and a high component of stable, recurring service revenues.

Carnival, Manpower and Ametek detracted from performance during the period. Cruise operator Carnival sold off despite reporting good quarterly earnings and providing an upbeat outlook for the remainder of the year. Investors feared that the Brexit vote and recent terror events could negatively impact Europe's economy as well as travel within the continent. This is a real risk since Carnival has meaningful exposure to Europe. Investors are also worried about oversupply in China's cruise market. China is currently small for Carnival but is an important source of long-term growth. Significant new industry capacity is being added to this market, raising concerns that cruise prices in the region could come under pressure.

Without minimizing the risks from a worsening macro environment, we are pleased that Carnival management is executing well. After stumbling several years ago, the company has done a good job in restoring its brand name and controlling expenses. This turnaround is evidenced by the above average yield gains that the company has been recently enjoying.

Similarly, Manpower's stock was hammered by fears that Brexit could cause a hiring slowdown in Europe. The region accounts for nearly two-thirds of the staffing firm's revenues. Though a decline in European economic activity remains a risk, Manpower's long-term fundamentals still seem attractive. The company is well positioned to benefit from the continued growth of the staffing industry, as employers use employment services to enhance flexibility, increase efficiency and reduce labor costs. We also think highly of Manpower's management, which has maintained pricing discipline, slashed costs and improved business mix by acquiring higher margin companies.

Ametek, a diversified industrial, projected reduced profits due to a soft industrial economy with particularly weak energy and metals markets. The company is a good operator with strong competitive positions in high margin, niche markets. It has also been a highly successful acquirer, substantially increasing the sales and profitability of acquired companies by leveraging an extensive distribution network and applying operating prowess. We see this year's shortfall as a cyclical blip rather than a function of any new competitive challenges or execution issues.

During the quarter, biopharmaceutical Shire completed the purchase of our position in Baxalta for cash and stock. We now own a small position in Shire, which is based in the U.K. but has a global footprint. Since being appointed three years ago, Shire's CEO Flemming Ornskov has engineered a successful turnaround of the company. Under Ornskov, Shire has significantly improved its R&D productivity and pipeline, streamlined what was a bloated cost structure and reshaped the portfolio. The result is a company with much higher growth and profitability. Indeed, Shire forecasts double digit top and bottom line growth over the next five years.

Shire's legacy was in specialty drugs in areas such as neuroscience, gastrointestinal and renal. Over time it has built a strong franchise in rare diseases as well. Rare diseases is an attractive business as barriers to entry are high, competition is limited and pricing for the drugs used to treat these diseases is favorable. Shire's acquisition of Baxalta appears to make sense since it will increase the proportion of revenues generated by rare diseases while providing scale, diversity and cost savings. We could potentially add to Shire given our favorable initial view of the company.

You should have recently received your individual account performance, an inventory of quarter-end positions and a statement of management fees. We also debited the quarterly fee from your account.

We appreciate your continued support and always welcome your comments, questions or concerns.

Sincerely,

Dan

Daniel K. Cantor
Managing Member

Jeff

Jeffrey C. Kinzel
Managing Member

Enclosure