HBK Wealth Management
Haire • Bohmer • Kilcoyne

WEEKLY MARKET COMMENTARY

A Candid Look into the Current State of the Markets

November 2015

Our roads to success may have twists and turns and ups and downs; together we can navigate a course and enjoy the scenery along the way.

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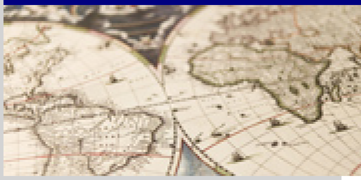
In This Issue



Weekly Market Commentary | Week of November 16, 2015

KEY TAKEAWAYS

- Our thoughts are with the victims of the November 13 terrorist attacks in Paris.
- Here we look back at history to assess potential market impacts of Friday's tragedy.
- History suggests any potential negative stock market reaction to these events may be short-lived.

TRAGEDY IN PARIS

Our thoughts are with the victims of Friday's terrorist attacks in Paris. Events like this stir up many powerful emotions, including anger, fear, sadness, confusion, and regret, and these emotions are not easily suppressed. It is difficult to shift our attention away from this tragedy and toward the financial markets in times like this, but it is our responsibility to do so. Here we look at the potential stock market impact of Friday's tragedy. As this commentary is being written, the S&P 500 is solidly higher in midday trading, with some speculating that terrorist threats mean the Federal Reserve (Fed) may not raise interest rates next month (though we still see a December hike as likely based on what we know now).

HISTORICAL PERSPECTIVE

Regardless of the circumstances when making market forecasts, looking back in history to find similar conditions or events is always part of our process. In this case, unfortunately, we have many terrorist attacks in recent history to look at for a sense of how stocks might react.

Below is a list of events going back to the early 1990s and how stocks performed after these events [Figure 1]. The data are encouraging, as stocks perhaps benefited from the wave of patriotism or, in some cases, possibly the spending associated with the military response. The limited economic disruption from most of these events--with 9/11 a clear exception--is consistent with the generally muted stock market reactions.

These events occurred at different points in market cycles, and certainly other factors influenced stock market movements during these periods; but nonetheless, the stock market's performance after these 17 events over the past 23 years suggests any related weakness in stocks may be short-lived.

It is logical to think defense stocks would get a boost from these events, but the data are mixed. These stocks do no better, on average, than the market during the week and month following the events (they are largely flat). However, the group (represented by the S&P 500 Aerospace & Defense Industry Group) has done better than the S&P 500 over the subsequent three months, gaining an average of nearly 8% compared with the S&P 500 gain of about 4%. Correlation is possible, but the muted short-term reaction suggests these results may not be meaningful.

It is also possible that oil prices may get a bump from the heightened geopolitical risk in the Middle East (West Texas Intermediate Crude Oil is solidly higher in midday trading); although, given how well supplied the global oil markets are currently, we would expect the impact to be relatively limited.

Finally, as has occurred in previous attacks, travel- and leisure-related stocks that are most impacted by travel restrictions may experience additional weakness in the coming days and weeks. Some weakness in these segments is evident in European markets today.

1 STOCKS HAVE PROVEN RESILIENT TO TERRORIST ATTACKS OVER PAST 25 YEARS

		S&P 500 Gain After Event (%):			
Event	Date	1 Week	1 Month	3 Months	Trading Days to Recoup
IRA Truck Bomb – London Financial District	4/10/92	2.97	2.91	2.46	1
World Trade Center Bombing	2/26/93	1.33	0.99	2.04	2
Tokyo Subway Sarin Gas Attacks	3/20/95	0.97	1.77	8.80	4
Oklahoma City Bombing	4/19/95	1.58	2.83	10.60	1
Car Bomb at U.S. Military Headquarters – Riyadh	11/13/95	1.31	4.96	10.82	2
IRA Truck Bomb – London Financial District	2/9/96	-0.12	-3.48	-1.67	1
Truck Bomb Outside Khobar Towers – Dhahran	6/25/96	0.32	-5.58	2.69	2
U.S. Embassy Bombings – Africa	8/7/98	-0.48	-10.61	4.08	7
U.S.S. Cole Yemen Bombing	10/12/00	1.52	2.72	-1.24	1
World Trade Center and Pentagon Terrorist Attacks	9/11/01	0.00	0.45	4.34	19
Bali Nightclub Bombing	10/12/02	5.25	4.89	11.04	1
Madrid Terrorist Attacks	3/11/04	0.35	2.94	2.22	1
London Train Bombing	7/7/05	2.03	2.38	-0.12	1
India Train Bombings	7/11/06	-2.85	-0.06	6.14	13
Jaipur, India Bombings	5/13/08	1.59	-4.50	-6.96	1
Boston Marathon Bombing	4/15/13	0.19	6.86	8.23	1
Charlie Hebdo Shooting	1/7/15	0.12	1.46	2.49	1
Paris Theater, Stadium Bombing, Shootings	11/13/15	?	?	?	?
	Average	0.95	0.64	3.88	3.6
	Median	0.97	1.77	2.69	1.0
	Batting Average	76%	71%	76%	

Source: LPL Research, FactSet 11/16/15

Batting average is the percentage of times the index is higher relative to the total number of observations.

POTENTIAL POLITICAL IMPACT

Here are some of our thoughts on potential political impacts from the intensifying global war on terror:

U.S. election. Voters recognize that the war on terror is a global fight, and just because the latest attack occurred in Europe does not mean terrorism is not a risk for U.S. citizens. Accordingly, immigration and national defense, which were already key issues for the Republican presidential candidates, are even bigger issues now and could easily sway Republican primary voters in February 2016. Generally, the Republican Party is considered stronger on defense, while likely Democratic candidate Hillary Clinton has foreign policy experience as former Secretary of State.

European elections. This event may also alter elections in Europe, with more hardline governments, with respect to immigration, having greater influence. Populist and Nationalist parties have been gaining support across Europe based on their stances on immigration and European integration. To the extent these issues impact--or even dominate--political conversations, additional uncertainty is created around economic policies that may heighten market volatility.

Defense spending. The military response has begun, with France bombing Islamic State targets in Syria over the weekend. The U.S. and most, if not all, G20 nations will provide support of some kind for this fight and, even though the war on terror was already well underway, the response will likely put additional upward pressure on defense spending. The G20 meetings over the weekend were dominated by discussions of a global coordinated response.

CONCLUSION

While we mourn those who lost their lives in Friday's terrorist attacks, we also do our best to help you navigate a challenging investment landscape. In this case, a look back at history for perspective offers reassurance. Still, as always, we remain watchful for risks that may warrant a change in our asset allocations. We see further modest gains ahead for stocks in the months ahead as the U.S. economy and corporate profits improve, but we acknowledge that geopolitical risk may contribute to heightened near-term stock market volatility.

IMPORTANT DISCLOSURES

The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual. To determine which investment(s) may be appropriate for you, consult your financial advisor prior to investing. All performance referenced is historical and is no guarantee of future results.

The economic forecasts set forth in the presentation may not develop as predicted and there can be no guarantee that strategies promoted will be successful.

Investing in stock includes numerous specific risks including: the fluctuation of dividend, loss of principal, and potential liquidity of the investment in a falling market.

Investing in foreign and emerging markets securities involves special additional risks. These risks include, but are not limited to, currency risk, geopolitical risk, and risk associated with varying accounting standards. Investing in emerging markets may accentuate these risks.

Commodity-linked investments may be more volatile and less liquid than the underlying instruments or measures, and their value may be affected by the performance of the overall commodities baskets as well as weather, geopolitical events, and regulatory developments.

All investing involves risk including loss of principal.

INDEX DESCRIPTIONS

The Standard & Poor's 500 Index is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

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Weekly Economic Commentary | Week of November 16, 2015

KEY TAKEAWAYS

- We continue to expect housing may add to GDP growth in 2015 and for the next several years, as the market normalizes following the severe housing bust of 2005-2010.
- Housing affordability, housing supply, home mortgages supply, and home prices may largely determine the pace at which housing adds to GDP growth in the years ahead.
- At only around 3% of GDP, housing is not large enough to carry the economy by itself.

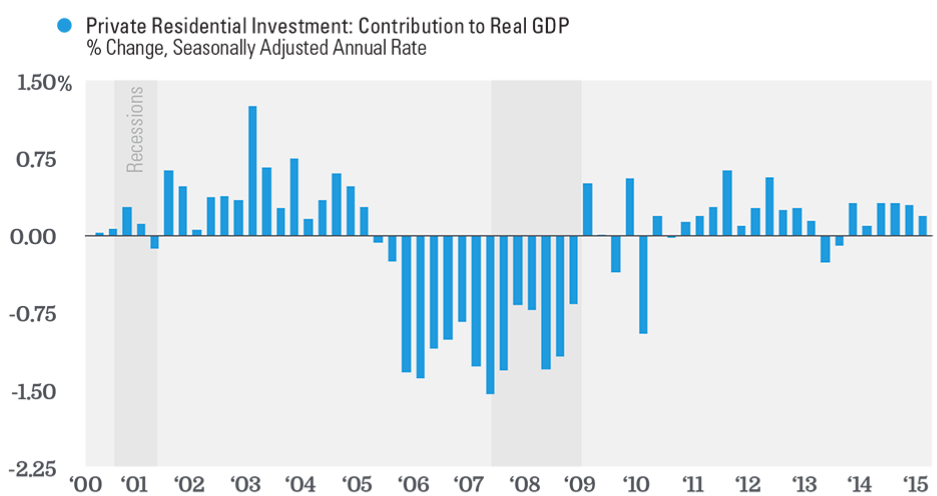
IS HOUSING ENOUGH?

Economic data released in the next two weeks will shed light on the state of the housing market in late third quarter and early fourth quarter of 2015. Several key housing-related economic data releases are due this week (November 16-20, 2015) including the National Association of Homebuilders Home Builder (NAHB) Housing Market Index for November 2015 and housing starts and building permits for October 2015. Next week (November 23-27), reports on existing home sales for October 2015, the Case-Shiller Home Price Index for September 2015, and new home sales for October 2015 are due.

In addition, the revised figure for gross domestic product (GDP) for the third quarter of 2015 will be released on Tuesday, November 24, 2015. This report will provide an update on the impact housing had on the economy in the third quarter and in 2015 so far. The initial report on third quarter GDP (released in late October 2015) found that housing--as measured by residential fixed investment--added 0.2 percentage points to GDP growth in the third quarter after adding 0.3 percentage points in each of the first two quarters of the year [Figure 1].

With the solid performance in the first three quarters of 2015, housing has now added to GDP growth in 16 of the 18 quarters since early 2011. Prior to that, between late 2005 and late 2010, housing had been a drag on the overall economy in 17 of the 20 quarters (or five years), as the economy endured the housing-induced Great Recession and its aftermath. We continue to expect (per our long-held view) housing may add to GDP growth in 2015, 2016, and for the next several years, as the market normalizes following the severe housing bust of 2005-10, but acknowledge that housing alone cannot carry the U.S. economy.

1 HOUSING HAS CONSISTENTLY ADDED TO GDP GROWTH SINCE 2011 AND WE EXPECT HOUSING TO CONTINUE TO ADD TO GDP IN THE COMING YEARS



Source: LPL Research, Bureau of Economic Analysis 11/16/15

KEY DRIVERS OF HOUSING IN 2015 AND BEYOND

Several factors will likely determine the pace at which housing adds to GDP growth in the coming years. Among them are:

Housing affordability. Housing affordability, the ability of a household with the median income to afford the payments on a median-priced house at prevailing mortgage rates, hit an all-time high in early 2013, before the big run-up in mortgage rates that began in mid-May 2013, as a result of what is now known as the "taper tantrum." Since then--despite another sharp drop in mortgage rates since late 2013--a combination of rising home prices and sluggish income growth have driven affordability some 20% lower. Although mortgage rates have moved lower since the end of the taper tantrum, they remain 50-75 basis points (0.50-0.75%) higher than the 2013 lows that preceded the taper tantrum.

Despite the drop, affordability is well above its long-term average [Figure 2] and also well above the levels during the mid-2000s housing boom. The three components of affordability--incomes, home prices, and mortgage rates--may all continue to move higher, potentially driving affordability lower back toward its long-term average, but not much below.

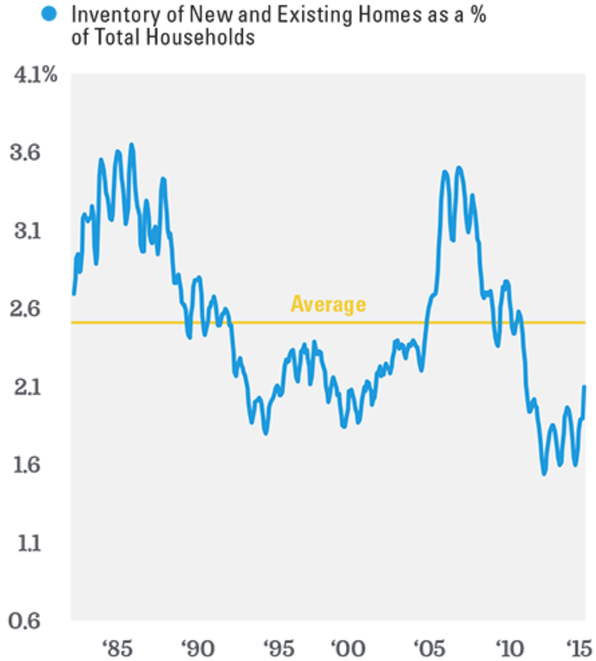
2 DESPITE RISING INCOMES AND FALLING RATES, THE RISE IN HOME PRICES HAS REDUCED HOUSING AFFORDABILY IN RECENT YEARS, BUT IT REMAINS WELL ABOVE AVERAGE

Source: LPL Research, National Association of Realtors 11/16/15

Housing supply. At just over 200,000 units, the number of new single-family homes for sale at the end of September 2015 was well below the peak of nearly 600,000 units for sale in 2006, but above recent lows (140,000-150,000 units). The number of existing single-family homes for sale (1.98 million in September 2015) is nearly 1.5 million units below the peak of 3.4 million set in mid-2007. Combined, the level of new and existing homes for sale remains well below average [Figure 3], relative to the number of households in the economy--and the low level of inventory is likely to be a big factor in driving housing construction in the coming years. We'll get an update on both new and existing home inventories in the last full week of November.

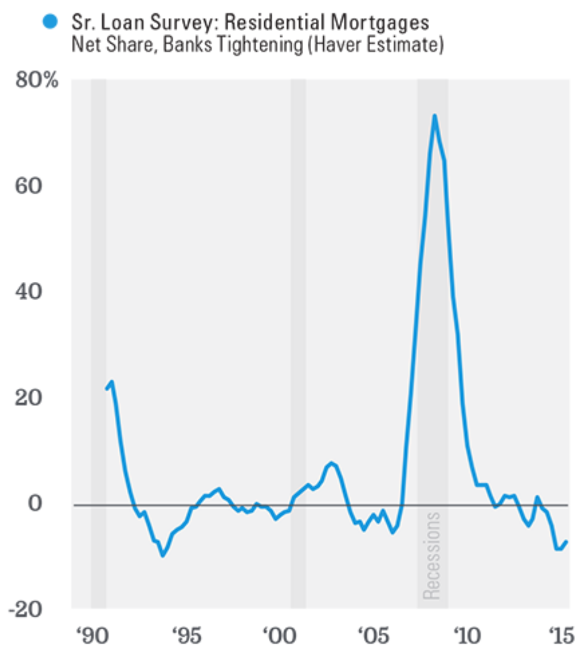
Home mortgages supply. From the mid-1990s through late 2006, bank lending standards (required down payments, credit scores, work history, etc.) for residential mortgages were relatively easy. Coupled with low rates and rapid innovation in financial products backing residential mortgages, this easy credit helped to fuel the housing boom. The banking industry began tightening lending standards in late 2006 and continued to tighten standards for more than two years. Lending standards eased in 2009 and 2010, but remained more restrictive than they were in the peak boom years from 2004-06. The latest survey (fourth quarter 2015) revealed that although bank lending standards for home mortgages tightened a bit between the third and fourth quarters of 2015, over the past four quarters they have been the easiest since mid-2006 [Figure 4]. The improvement in this indicator in recent quarters is a good sign and may help to offset the recent rise in the rates banks are charging for mortgages. The market will get an update on this metric, via the Federal Reserve's Senior Loan Officer Survey, in early 2016.

3 INVENTORY OF UNSOLD NEW AND EXISTING HOMES REMAINS WELL BELOW AVERAGE



Source: LPL Research, U.S. Department of Commerce, National Association of Realtors 11/16/15

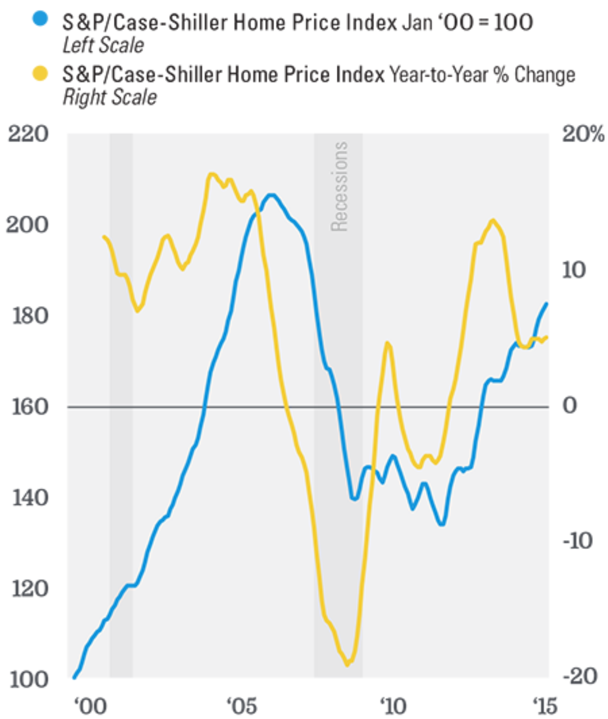
4 ALTHOUGH THEY TIGHTENED IN THE PAST QUARTER, BANKS' LENDING STANDARDS FOR MORTGAGES ARE EASIEST SINCE MID-2000s



Source: LPL Research, Federal Reserve Board 11/16/15

Home prices. The market will have to wait until next week (November 23-27, 2015) to get an update on home prices via the new and existing home sales reports for October 2015 and the S&P/Case-Shiller Home Price Indexes for September 2015 and the third quarter. There are various measures and sources for home prices--which, as noted above, are a component of housing affordability. In general, home prices rose rapidly (much faster than inflation or income growth) in the early 2000s, peaked in 2004-06, fell between 25 and 30% through 2009-10, and have been in recovery mode since then. The Case-Shiller Index [Figure 5] is a good proxy for home prices nationwide. It shows the big run up in prices in 2000-06, the big drop in prices from 2006-09, the sideways move in house prices in 2009-12, and more solid gains in 2013-15. On a year-over-year basis, the Case-Shiller Home Price Index has been moderating in the past two years, after peaking at an unsustainable 14% year-over-year increase in late 2013, to a more sustainable 4-5% pace over the past year. We would view price increases in that range--which is consistent with the average housing price gain in the past 35 years--as a sign that the housing market is stable, and poised to be a consistent contributor to GDP growth in the quarters and years ahead, without the boom bust cycle of the 1990s and 2000s.

5 HOME PRICE APPRECIATION TRENDING BACK TO LONG-TERM AVERAGE NEAR 4% PER YEAR



Source: LPL Research, Standard & Poor's 11/16/15

CONCLUSION

We continue to expect that housing may add to economic growth in the years ahead. Although interest rates could move higher in the coming years, we expect the trends that have helped the housing market out of the housing bust to remain in place. Still, like other segments of the economy that have struggled to recover from the Great Recession, the housing recovery remains choppy and uneven.

IMPORTANT DISCLOSURES

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The S&P/Case-Shiller U.S. National Home Price Index measures the change in value of the U.S. residential housing market. This index tracks the growth in value of real estate by following the purchase price and resale value of homes that have undergone a minimum of two arm's-length transactions. The index is named for its creators, Karl Case and Robert Shiller.

The Composite Housing Affordability Index is published monthly by the National Associate of Realtors and measures median household income relative to the income needed to purchase a median-priced house.

The National Association of Home Builders Housing Market Index is based on a monthly survey of NAHB members designed to take the pulse of the single-family housing market. The survey asks respondents to rate *market conditions for the sale of new homes at the present time and in the next six months as well as the traffic of prospective buyers of new homes.*