

October 14, 2016

Dear Valued Investor:

Elections elicit strong emotions. High disapproval ratings for both candidates, as well as Donald Trump's unconventional candidacy, have taken these emotions to another level this cycle. Politics is one of many emotional biases that can work against investors trying to achieve their long-term financial goals. Candidates in office may influence how investors feel about the economy and markets and can get them off track. Separating political views from investment decisions is difficult, and while presidents can set an overall tone for the economy and markets, over the long term the underlying fundamentals of the economy and corporate profits matter more.

On that score, the picture is better than some in the media would have us believe. Economic data in September and early October suggest stronger growth in the second half of the year after subdued real gross domestic product (GDP) growth in the first half. A solid 192,000 jobs per month, on average, were created in the third quarter of 2016 (based on Bureau of Labor Statistics data). Consumer confidence has reached its highest level since the end of the Great Recession.¹ Manufacturing activity rebounded in September and is expanding, based on Institute for Supply Management (ISM) data. In addition, the Conference Board's Leading Economic Index (LEI), an aggregate of economic indicators that tend to lead the overall economy, is signaling continued economic growth. All of this data suggest that the odds of a recession in the next year may be low.

Turning to markets, although stocks were basically flat in August and September, the S&P 500 returned a solid 3.9% in the third quarter and has not suffered a losing month since February of 2016 based on total returns. In short, financial markets have largely shrugged off political uncertainty, in both the U.S. and in the U.K. ahead of its planned separation from the European Union (i.e. "Brexit"). Stock market breadth has been strong (many stocks have participated in recent gains) and economically sensitive sectors of the market, most notably technology,² have performed well, both of which are positive signs of stock market health. We expect the third quarter corporate earnings season may mark the end of the "earnings recession" and revenue growth to resume after an 18-month drought. Finally, markets appear comfortable with the prospects for a December 2016 Fed rate hike based on the gradual rise in interest rates.

All in all, economic and market fundamentals generally look pretty good to us. We all know there are risks including a policy mistake by a government or central bank, Brexit, China's bad debt problem, and above-average stock valuations. And despite a calm summer, stock market volatility has picked up in September and early October. But remember, stocks have historically done well in the fourth quarters of election years and have performed well under many different party leadership combinations.³ Despite the emotions this election may bring, we encourage you to stick to your plan and stay invested.

¹The Conference Board Index

² S&P 500 Technology sector 3-month return of 7.9% as of October 13, 2016.

³ The S&P 500 is up an average of 3.6% during fourth quarters of election years, excluding 2008, and has been higher 87% of those quarters.

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Economic forecasts set forth may not develop as predicted.

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

Investing in specialty market and sectors carries additional risks such as economic, political, or regulatory developments that may affect many or all issuers in that sector.

Gross domestic product (GDP) is the monetary value of all the finished goods and services produced within a country's borders in a specific time period, though GDP is usually calculated on an annual basis. It includes all of private and public consumption, government outlays, investments, and exports less imports that occur within a defined territory.

The S&P 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.

The Institute for Supply Management (ISM) index is based on surveys of more than 300 manufacturing firms by the Institute of Supply Management. The ISM Manufacturing Index monitors employment, production inventories, new orders, and supplier deliveries. A composite diffusion index is created that monitors conditions in national manufacturing based on the data from these surveys.

The Leading Economic Indicators (LEI) Index is an economic variable, such as private-sector wages, that tends to show the direction of future economic activity.

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