Goodman Financial
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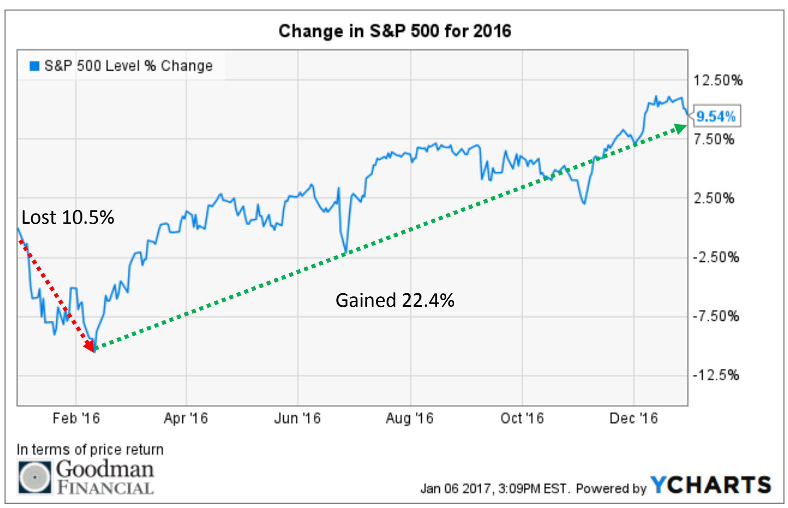
FOURTH QUARTER 2016 MARKET & ECONOMIC REVIEW

Major Equity Market Indices: Fourth Quarter 2016

Index	Description	Fourth Quarter 2016*				
		9/30/16	High	Low	12/31/16	QTD Return
S&P 500	A market-capitalization weighted index of 500 large U.S. companies.	2,168.27	2,277.53	2,083.79	2,238.83	3.25%
DJIA	Dow Jones Industrial Average or "The Dow"; A price-weighted average of 30 major U.S. companies.	18,308.15	19,987.63	17,883.56	19,762.60	7.94%
Nasdaq Composite Index	A market-capitalization weighted index comprised of over 3,000 companies, mostly in the technology and biotech industries.	5,312.00	5,512.37	5,034.41	5,383.12	1.34%
NIKKEI 225	A price-weighted index comprised of Japan's top 225 most established companies.	16,449.84	19,592.90	16,111.81	19,114.37	16.20%
MSCI Emerging Markets	An index comprised of 23 MSCI indices from emerging economies including Brazil, China, India, Mexico, Russia, South Africa, and the UAE.	903.46	918.68	838.96	862.28	-4.56%
Stoxx Europe 600	An index comprised of 600 companies based in one of 18 EU countries including Austria, Belgium, Denmark, France, Germany, Ireland, Spain, and the United Kingdom.	342.92	361.66	327.02	361.42	5.39%

* Excludes effects of dividends — Sources: YCharts, Wall Street Journal

- The **Dow was the best performing U.S. index**, led by financial stocks. Outperformance can be attributed to the Trump Rally and expected regulatory changes. The worst performing industries were consumer goods and pharmaceuticals.
- The **NASDAQ was the worst performing U.S. index**, possibly due to its concentration in technology companies and those companies' concerns about what a Donald Trump presidency may mean for imports from China and skilled immigrant labor.
- The **Nikkei 225 was one of the best performing major indices in the world**. A stronger U.S. dollar helped Japanese exports, which in turn aided manufacturing. The Bank of Japan (BOJ) issued an improved outlook for the Japanese economy after its December meeting. Though, some concerns in the market exist due to the growing share of Japanese stocks and bonds owned by the BOJ.
- **Emerging markets suffered** from the strong U.S. dollar, still-low commodity prices, and a sluggish global economy.
- **European stocks finished the year down** about 1.2%, a decrease that was pared down thanks to a strong fourth quarter. Government support for Italian banks served to buoy the European financial sector in December.
- For the year, **all three major U.S. indices finished with gains**. The S&P 500 finished up 9.5%, the Dow finished the year up 13.4%, and the NASDAQ gained 7.5%. These are respectable gains in a year that began with falling oil prices, endured Brexit, and saw the culmination of one of the most contentious U.S. presidential elections in recent memory.
- A deeper look at returns shows that the **S&P 500 staged an impressive turnaround** from its low point in mid-February through the end of the year. To the right is a graph of the S&P 500 for 2016 with its performance before and after the low point emphasized.
- 2016 was a volatile year in the market, but due to recovering energy prices, lower unemployment, and improved consumer confidence, it also proved to be **a good lesson in the value of long-term, patient investing**.



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Fixed Income: Fourth Quarter 2016

Fourth Quarter 2016						52-Week Range	
Description	9/30/16	12/31/16	QTD Change in Basis Points*	Description	12/31/16	Low	High
90 Day Treasury Bill	0.29%	0.51%	22	Federal Funds Rate Target	0.50%-0.75%	0.25%-0.50%	0.50%-0.75%
10 Yr. Treasury Note	1.60%	2.45%	85	Prime Rate (U.S.)	3.75%	3.50%	3.75%
30 Yr. Treasury Bond	2.32%	3.06%	74	LIBOR (3-Month)	1.00%	0.61%	1.00%
15 Yr. Mortgage Rate	2.72%	3.42%	70	5-Year CD	1.22%	1.17%	1.41%
30 Yr. Mortgage Rate	3.42%	4.21%	79	HELOC ($30,000)	4.60%	4.29%	5.01%

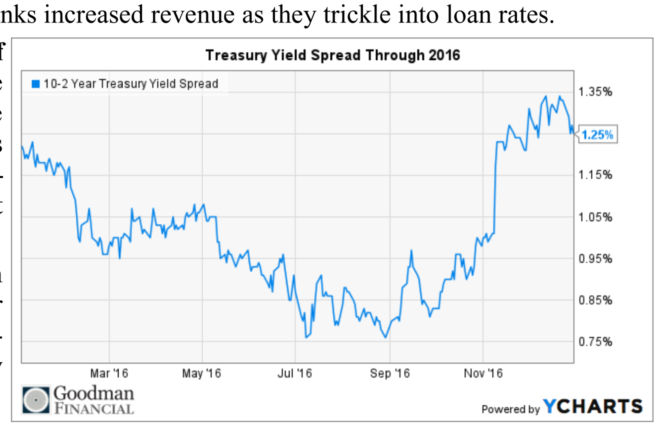
* One basis point is equal to 1/100th of 1%, or 0.01% Sources: YCharts, Wall Street Journal

- The Federal Reserve's decision to **raise the federal funds rate** target by 25 basis points, while anticipated by many in the market, was greeted with a wave of news headlines and rate increases. Fixed income yields had declined throughout the year until the November meeting, when the Fed decided to leave the rate unchanged setting the stage for the rate hike in December.
- Per the minutes of the Fed's December meeting, **inflation is expected to rise** but not to the long-run target rate of 2%, and the economy is expected to "expand at a moderate pace." **The labor market is expected to continue to strengthen**. No change to the Fed's bond buying activity is expected in the near term. Further increasing of the federal funds rate is expected in 2017.
- Of great relevance to many readers are **mortgage rates**. The increased cost of borrowing due to the change in the federal funds rate caused some concern among homebuyers and analysts following homebuilders. The two figures below illustrate the difference in monthly payments on a theoretical $300,000 loan using the above rates:

WSJ 15-year Mortgage Rates	Rates	Monthly Payment
As of 9/30/2016	2.72%	$2,032
As of 12/31/2016	3.42%	$2,133
Change	**70 bps**	**$101**

WSJ 30-year Mortgage Rates	Rates	Monthly Payment
As of 9/30/2016	3.42%	$1,334
As of 12/31/2016	4.21%	$1,469
Change	**79 bps**	**$135**

- The impact of increased rates has been cited by some in the financial press to be a headwind for home buying. While this may hold true in the short-term, the actual change in monthly payments in dollar terms is frankly not all that substantial. Given pent-up demand for homes, a generally improving economy, and the emotional nature of homeownership, modest, anticipated increases to the federal funds rate ought not dampen the housing market. Strict lending standards are more likely to be the issue.
- The **increase to the prime rate and 3-month LIBOR**, commonly used reference rates in commercial lending, come at time of growing confidence in the economy. These increases may provide banks increased revenue as they trickle into loan rates.
- Of importance in the bond market is the **spread between bonds of different maturities**, meaning the difference in yield between the two bonds. A commonly cited spread is the relationship between the 2-year and 10-year U.S. treasury bonds. This spread is sometimes used as a measuring stick to determine investor short- and medium-term expectations. Generally, the larger the gap, the more confident investors are about future growth. The spread has recently widened.
- The graph to the right shows this spread throughout 2016. Expansion began in the third quarter and continued through the fourth quarter with a dramatic uptick right after the presidential election. This coincides with the post-election rally. The tapering off at year end may have been in recognition of overexcitement.



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Economic Indicators: Fourth Quarter 2016

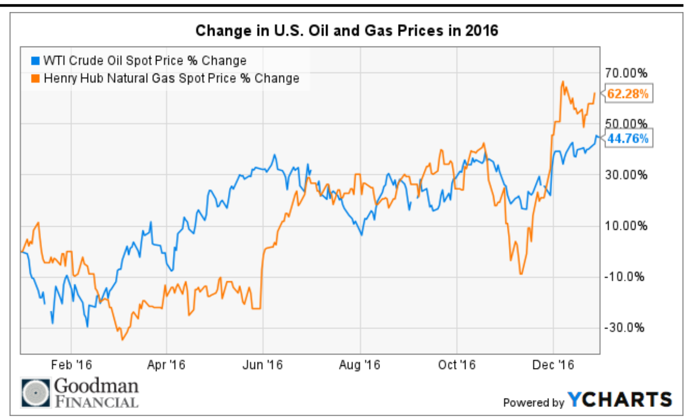
Indicator	Description	9/30/16	12/31/16	QTD Change
Average Weekly Initial Claims for Unemployment Insurance	The number of new filings for unemployment insurance benefits. **A decrease in the number of claims suggests fewer layoffs.** *Most economists believe claims below 300,000 indicate a healthy labor market environment.*	249,000	235,000	↓ -5.62%
Unemployment Rate	The percentage of total labor force that is unemployed but actively seeking employment. **The unemployment rate edged down below 5%.** *The U.S. Federal Reserve targets a long-run unemployment rate of between 4.5% and 5%.*	5.00%	4.70%	↓ -30 bps
Average Weekly Earnings	The average weekly salary earned by private, nonfarm employees. **Average weekly earnings slightly increased. This suggests more disposable income for consumers and could be the result of a tightening labor market.**	$887.86	$891.80	↑ 0.44%
Index of Consumer Sentiment	This index reflects consumer attitudes towards the state of the economy. **Consumer confidence has increased, suggesting consumers may spend more.**	91.20	98.20	↑ 7.68%
Manufacturers' New Orders for Consumer Goods and Materials (Millions) *	The number of new orders placed for consumer goods. **New orders increased, indicating higher demand for U.S.-produced consumer goods and validating increased consumer sentiment.**	$186,544	$187,568	↑ 0.55%
Manufacturers' New Orders for Nondefense Capital Goods, Excluding Aircraft (Millions) *	This index is the producer's counterpart of new orders of consumer goods and materials. **New orders for nondefense capital goods increased during the quarter, suggesting increased business confidence in the economy.**	$62,710	$63,642	↑ 1.49%
US Capacity Utilization: Manufacturing *	The ratio of production capacity being used to produce finished products compared to the total capacity available. **Capacity utilization increased slightly, in line with increased new orders and confidence.**	75.2%	75.4%	↑ 12 bps

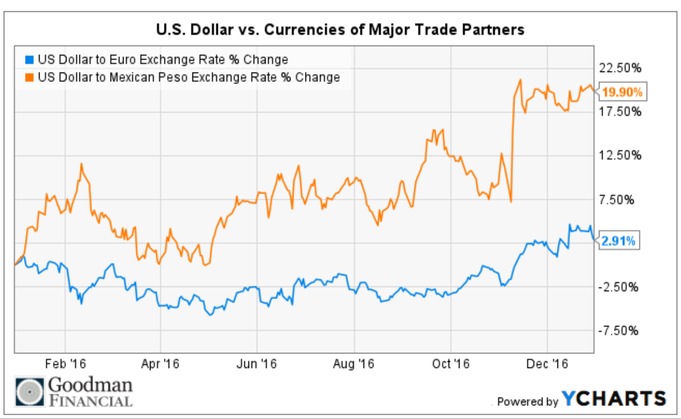
*These items are as of 11/30/16, the date of the most recently published statistics. Sources: YCharts, Federal Reserve Bank of St. Louis, The University of Michigan, U.S. Census Bureau, Department of Labor

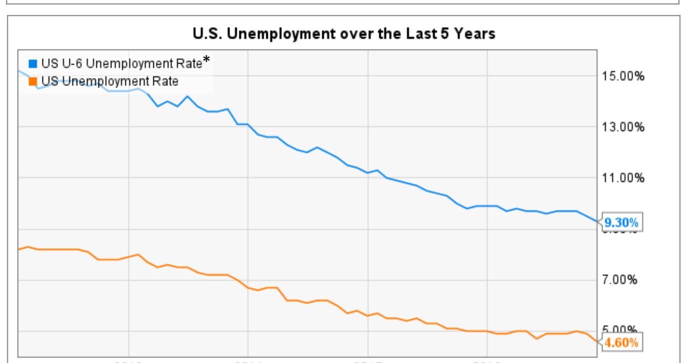
U.S. Economic Health

The two graphs to the right depict **positive trends in the U.S. economy**. Oil and gas prices support the energy industry, which employs many people across the country and across the socioeconomic spectrum. Falling unemployment has been discussed here in previous quarters, and the Fed's decision to raise rates serves to validate the theory the labor market is improving.

However, growth comes with consequences. Due to the relative strength of the economy, the U.S. dollar has appreciated, as shown below. To an extent, a strong dollar is a positive for consumers, but a very strong dollar hurts U.S. exports and emerging markets dependent upon oil that is priced in U.S. dollars. It also hurts reported corporate earnings if sales occur overseas.







* also referred to as "underemployment"