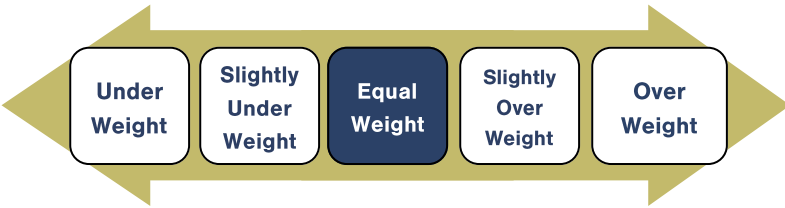


## SFMG MARKET RISK SIGNAL—EQUITY ALLOCATION

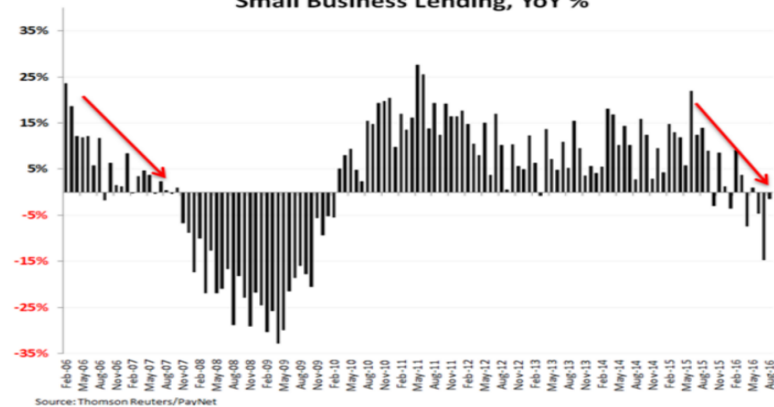


## ECONOMIC NEWS

- ◆ Inflation accelerated +1.5% year over year in September, the largest gain in 5 months. Janet Yellen recently stated though that the Fed would tolerate higher than target inflation, which gives her flexibility to keep rates low even if inflation increases.
- ◆ Much like the U.S. over past several months, Chinese economic data has been volatile. Last month showed a 10% drop in exports. This raises questions on the accuracy of their GDP data, which has held steady at 6.7% for 3 straight quarters.
- ◆ The European Central Bank's monetary stimulus is set to end in March 2017. Investors overseas are focused on their own central bank's actions too, as an extension of the stimulus program could be a tailwind for the markets.

## SMALL BUSINESSES PLAYING IT SAFE

Small Business Lending, YoY %



Even with such low interest rates, the demand for loans from small businesses has been declining for the past year. Businesses usually originate loans for capital expenditures when they feel confident in the business environment, which seems to be in question.

## CURRENT THOUGHTS

Global bond yields have been on the rise lately as investors sell bonds in anticipation of higher rates taking hold in upcoming months. The ending of the European Central Bank's bond purchasing stimulus would remove the pressure keeping rates artificially low. Central Bank President Mario Draghi hasn't given any indication of a program extension past the March 2017 deadline, but until that decision is announced in December, the possibility of additional stimulus is keeping markets in limbo. Higher inflation is strengthening the case for a December rate hike in the U.S., despite slowing economic data. Assuming 3rd quarter earnings don't hold too many negative surprises and the economic data doesn't turn over much more, higher inflation may force the Fed's hand in hiking rates, albeit at a slow pace if deemed necessary. Fed policy remains the focal point in the U.S., but a myriad of items abroad are raising caution. Issues with the European banking system could throw their economy even further off course if the stability of big players like Deutsche Bank worsen. In Italy, political disputes hold important implications for the country and the entire European region. Italy's current Prime Minister, Matteo Renzi, has vowed to resign if the constitutional reforms he is pushing don't get approved through a country-wide referendum. If the country votes no and he leaves office, the door would be open for a new party to be voted in; specifically the "Five State Movement" party, which has been vocal about wanting to leave the European Union. The domino effect of repeated "Brexit" type events would certainly shake markets. These Eurozone headwinds along with weakness in Japan and uncertainty in China make international investment riskier compared to the U.S.

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The purpose of the update is to share some of our current views and research. Although we make every effort to be accurate in our content, the datum is derived from other sources. While we believe these sources to be reliable, we cannot guarantee their validity. Charts and tables shown above are for informational purposes, and are not recommendations for investment in any specific security.

## CURRENT ASSET CLASS ALLOCATIONS

The U.S. equity markets remain in a long-term uptrend. We are maintaining our equity exposure and are **Equal weight** to stocks. The allocation mix of bonds vs. equities depends on our risk signals that shift our weightings accordingly.

## MARKET NEWS

- ◆ The British Pound reached a 31-year low against the U.S. Dollar on news that the "Brexit" process will begin early 2017. A weaker currency makes U.K. exports more competitive, so U.K. markets have rallied as a result. The losers in this situation are importers and U.K. citizens that lose their purchasing power.
- ◆ U.S. Treasuries are seeing 'safe-haven' inflows amid global concerns and also rate hike expectations. U.S. banks benefit from higher rates, giving the financial sector a recent boost.
- ◆ Last month, OPEC produced 33.64 million barrels per day. This is the most the group of countries has ever produced in a month, reiterating that as much as producers would like to reduce supply to increase prices, their actions are quite the opposite.

## U.S. DOLLAR REVERSING COURSE



The tailwind of a weakening U.S. dollar, which would hopefully help the earnings of large multinationals, is beginning to fade. The Dollar has begun to appreciate in May as a potential rate hike at the end of the year looms and other global currencies weaken.