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Benjamin A. Pace is the firm's Chief Investment Officer and leader of the Investment Committee. He has more than 25 years of experience in investment management. Prior to joining HPM Partners, he was Chief Investment Officer and Head of Global Investment Solutions for Deutsche Bank Private Wealth Management in the U.S. Ben has been featured in the Wall Street Journal and Reuters, and is a frequent commentator on Bloomberg TV and radio, Fox TV and CNBC, appearing regularly on network programs such as Power Lunch, The Closing Bell, Squawk Box, and Worldwide Exchange.

News & Recognition:

FT FINANCIAL TIMES | Top Financial Advisers 2015

FT 300 Ranking June 2015

HPM Partners Named Top Wealth Manager by Forbes

ECONOMIC INSIGHTS /

Response to Market Volatility

Global equity markets experienced another sharp selloff overnight and into this morning, with the Standard & Poor's 500 index now having joined the Dow Jones and NASDAQ indices in a full 10% correction from their Spring highs. This is the first correction in equity prices in an unusually long four years. While we have experienced a number of 3-7% "pullbacks" over this time, these moves have generally resulted in buyers coming in and using cash parked on the sidelines to buy attractively priced stocks. This full blown correction is causing investors to test their convictions about their exposure to global equities in general and US equities in particular.

As is often the case, there are multiple causes of the current market decline, with the primary concern being the heightened probability of a global recession led by China and the other emerging market economies impacted by the sharp slowdown in the Chinese GDP growth rate. The failure of Chinese authorities to announce a fiscal or monetary policy response to this slowdown and equity weakness was viewed with disappointment in overnight Asian trading. The prospect of the US Federal Reserve tightening monetary policy despite this weakening global environment is also causing market consternation. Heightening tensions between the two Koreas also added to this combustible mix.

While we did expect higher market volatility and the probability of a 10% correction as we entered 2015, we viewed these outcomes in the context of a continued secular bull market in US equities. Until the last few days, one of the bigger surprises of the year was the relative tranquility of US markets and their tight trading range this year. As our pre-planned response would be to use any correction as a buying opportunity, let's revisit our conviction around our secular bull market thesis to assure ourselves this is not the beginning of something worse.

Bear markets are always caused by impending economic recession. We view the probability of a US recession as very low at this time. The US consumer is rather healthy, with a rebuilt savings rate of 4-5%. Employment is growing at a 200-250 thousand clip per month and unemployment continues to decline. Granted, wages are not growing at the level the Fed would like to see, but they are increasing at an annualized rate of 2.5%. Lower commodity prices, especially gasoline, act as tax cuts which should further boost consumer spending as reflected in retail sales. The healthier US consumer is also being reflected in the strengthening housing sector which should be additive to GDP after many years in recession.

Capital spending by businesses, while somewhat disappointing in this expansion, has picked up everywhere outside the Energy sector and should be a net contributor to economic growth in the second half of the year. Also, our banking system is characterized by rather healthy balance sheets which minimize the probability of a 2008 type credit freeze. Credit is generally available and it remains very cheap.

The impact of slower global growth on the US economy should not be taken lightly as we are less insular than we were before the emergence of China, Brazil, etc... However, exports in general are a very small portion of US GDP and we believe there is enough internal momentum for the US economy to continue growing at a 2.5-3.0% rate into 2016. This should lead to positive earnings growth for US companies and attractive valuations for US equities given the paltry returns in both cash and investment grade bonds. In fact, valuation, with the S&P 500 trading at roughly 15X prospective earnings, should at least provide a solid floor to prevent much further market weakness. Finally, a Fed tightening, if done gradually and for the right economic reasons, should not derail the bull market.

Looking overseas, we would reiterate our underweight recommendation towards emerging market equities, as the impact of the China slowdown on its Asian neighbors and Latin American commodity producers remains uncertain. We would also reinforce our bullish dollar views against virtually all currencies. The recent dollar weakness against the Yen and Euro is temporary and due primarily to the recent unwinding of so-called carry trades which used these cheaper currencies as funding vehicles. Continued and perhaps increased monetary easing should bolster European and Japanese equities, but hedging the currency risk will be especially important in this environment.

This market correction was widely anticipated, given typical market history. What is never really known are the timing and catalysts for such a decline. Given our current overweight in equities, which we continue to advocate, we would look at this decline as a good opportunity to put any cash on the sidelines to work at more attractive valuation levels.

It is always difficult to predict the exact end of such downturns, but economic and earnings fundamentals lead us to the conclusion that the current decline is a temporary downdraft in a continued bull market and not the beginning of a bear market in US or developed international equities. We will keep you apprised of further developments and any changes in our opinion.

Sincerely,

Ben A Pace III

Benjamin A. Pace
Chief Investment Officer

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