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HAWK Letter

Dear Hawk100 Member,

There and Back Again.

Your Hawk100 wealth advisor wishes you and your family a year filled with prosperity and purpose during 2015 and hopes that you find this letter informative.

In accordance with your Wealth Alignment Plan, we implemented a dynamic investment strategy during 2014 as always. That strategy is dynamic because it can be responsive to changing client circumstances as well as shifting financial market conditions that affect our expectations around investment risk and reward.

Examining our 2014 predictions.

Let's consider the major themes underlying our investment processes during 2014 and develop an understanding of how economic and market conditions affected your portfolio. We had modest 2014 return expectations. Actually, returns varied widely as international markets diverged from US markets. A summary of 2014 actual results versus our start of the year forecast illustrates this difficulty.

December 31, 2014	2014 Actual	Prior Forecast	Difference
Preserve			
Cash equivalents	0.1%	0.3%	-0.2%
Provide			
Government	5.0%	1.7%	3.3%
Corporate	8.5%	3.9%	4.6%
Foreign	0.6%	7.7%	-7.1%
Promote			
Large U.S.	13.7%	4.4%	9.3%
Small U.S.	5.8%	5.1%	0.7%
International	-4.9%	5.8%	-10.7%
Protect			
Commodities	-18.6%	2.7%	-21.3%
Real estate	33.9%	4.4%	29.5%

Ryan Labs, iShares, Morningstar.

Beyond forecast returns, we made several predictions in our prior year letter. Let's briefly review them.

Predicted Event	Was Hawk100 right?	Predicted Market Response	Was Hawk100 right?
US Fed would end Quantitative Easing	Yes	Would constrain investment results for virtually all assets	No
Mid-term elections in the US would affect stocks	No	Stocks would underperform their historic average	Large No Small Yes
Mid-term elections in the US would affect bonds	Yes	Bond yields would decline	Yes
Credit risk would increase	Yes	Credit spreads would widen	Yes
Scotland and Catalonia would hold referenda on independence	Yes	Developed/European markets would lag US	Yes
Equity investor risk preferences would narrow	No	Stock earnings multiples would fall	No
Scotland and Catalonia would hold referenda on independence	Yes	Developed/European markets would lag US	Yes
US dollar would remain under pressure	No	Commodities would have positive affect on portfolios	No

First, we said excessively loose monetary policies throughout the regime of the prior Fed Chairman, Ben Bernanke, had increasingly elevated financial prices which risked a more precipitous fall if not hyper-inflation. We expected that the Fed would further wind down its quantitative easing policy under the leadership of the new Fed Chair Janet Yellen. We said that a muted pace of monetary expansion would likely constrain investment results for virtually all assets.

The Fed would wind down quantitative easing and eventually end regular bond purchases by October. Slowing the pace of monetary expansion significantly strengthened the US dollar and exerted pressure on commodity prices. These trends

By Richard Clemens, CFA CPA, *President*

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merged to form a perfect storm that wrought havoc on emerging markets, especially those that depend on dollar-based borrowing and have commodity driven markets.

Second, a nod to politics, we noted that mid-term elections in the US tend to couple with underperforming years. We observed over 90 years of stock market returns and showed that midterm election years had lagged non-midterm years by 5% on average. Grading our stock prediction depends on which US stocks to evaluate. Large stocks beat their historic average by about 6%. On the other hand, small stocks came up 5% short of their historic average.

US Treasury yields tended to decline during midterm election years. 10-year treasury yields started the year at 3.0% and ended 2014 at 2.2%.

We expected that Scotland would vote on an independence referendum– it did vote but it didn't secede – and that Catalonia would vote whether to separate from Spain – it did vote but it didn't count since Spain's Constitutional Court suspended the official election.

As the year unfolded, those geopolitical events were dwarfed by other rising circumstances. Violence in the Middle East seems to have been exacerbated by declining energy prices. The rise of a militant Islamic State brought the US limping back into the hot zone not to fight but to "contain" ISIS. Pakistan suffered its own evil when Islamic terrorists murdered innocent school children. China suppressed a democratic movement in the streets of Hong Kong perhaps the most significant such display since Tiananmen Square. These events belie a troubled world.

Our 2014 strategy.

How did we incorporate those predictions into portfolios and how did the actual events affect results?

Provide. The 10-year US treasury yielded 2.2% at the end of 2014 and since has fallen as low as 1.7%, an 18-month low. Term spreads have narrowed while yields dropped. Among corporate issues, returns to quality have been enhanced by rising credit spreads particularly during the latter half of 2014. Investment grade corporate yields fell from 3.3% to 3.0%. In contrast, junk yields climbed from 5.6% to 6.6%. Emerging market yields gyrated without much affect. They started at 6.1% and now stand at 6.3%. We had predicted wider credit spreads; however, our favoring emerging market positions failed to provide the expected results.

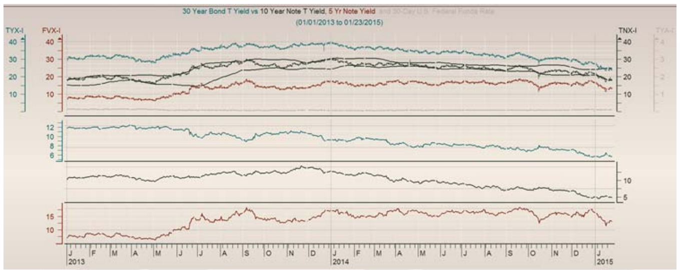

Chart 1—US Treasury Yields and Spreads, 2013-2014.
Telemet.

We started 2014 recommending minimal government bond holdings. Gradually, we increased the advised investment amount and closed the year with a neutral opinion and near policy weight. This benefited the portfolios while the pace of declining yields picked up. In contrast, we held a neutral opinion on corporate bonds for the start of the year and gradually reduced the weight until moving to an underweight position for the last months of 2014. This helped reduce the exposures that coincided with widening credit spreads. Our view for international bonds was bullish to start 2014, but we rapidly lost confidence as the dollar strengthened and as overseas economies failed to keep pace.

Despite falling yields, the dollar was resilient and even strengthened while the Fed wound down quantitative easing.

Chart 2—US Dollar Index, 2013-2014. Telemet.

Promote. We expect equity market returns to continue toward a narrower focus next year. Last year, we explained that earnings multiples (P/E ratios) were 18.0 and would not likely move higher, if at all. Earnings multiples barely rose during 2014 and closed at 18.5. Likewise, stock dividends yielded 1.8% throughout 2014, and we expect little change over the near term. Together, fundamental factors imply equity returns of 5.8% for 2015. This would be consistent with more narrowly focused equity returns.

Throughout 2014, we maintained essentially a neutral opinion on equities with target recommendations just below the policy weights while favoring US large equities over their smaller and international peers.

We remained most confident in large US equities while our view of small stocks was neutral though it steadily improved during the year. Larger stocks offered expected returns relative to risk that we believed were fundamentally and quantitatively advantageous compared with smaller stocks. Indeed, smaller stocks did not perform as well as larger stocks for 2014.

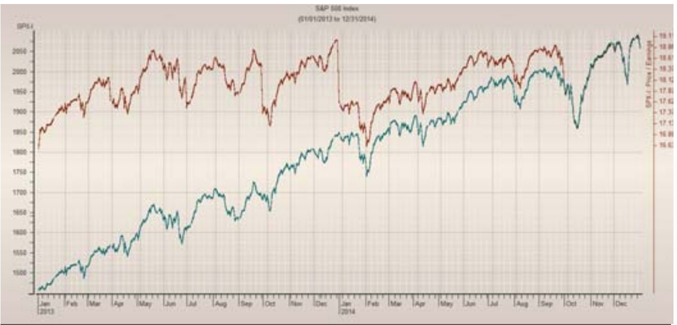

Chart 3—S&P 500 price and P/E Ratio, 2013-2014. Telemet.

We expect 2015 to resume favoring smaller stocks while larger multinational firms face operating and reporting challenges embedded in a stronger dollar.

With respect to our global allocation model, our opinion on stocks resembled that held for bonds. We were less confident in developed market equities, though Hawk100 entered 2014 with a bullish view of emerging markets. Our opinion became bearish as the year developed, and we avoided much of the negative performance from international markets generally.

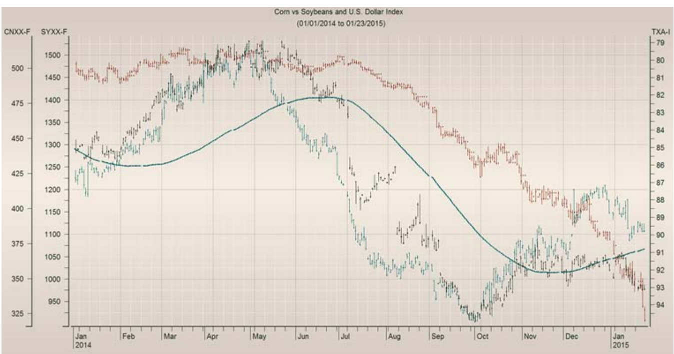

Chart 4—Corn and Soybean Futures and US Dollar Index (inverted), 2014. Telemet.

Protect. We continue to firmly hold that diversification enhances long-run investment results. We therefore will continue to advise investment positions in alternative assets. During 2014, markets for alternative securities were most difficult to navigate.

Throughout the year, we recommended below policy weights for commodities; however, we increased those weights just as commodity prices accelerated to the downside.

Our real estate target was appropriately just above the policy amount. However, where member portfolios held real estate, our selected asset represented global markets rather than narrowly looking to domestic assets. Dollar strength constrained realized returns for those global assets.

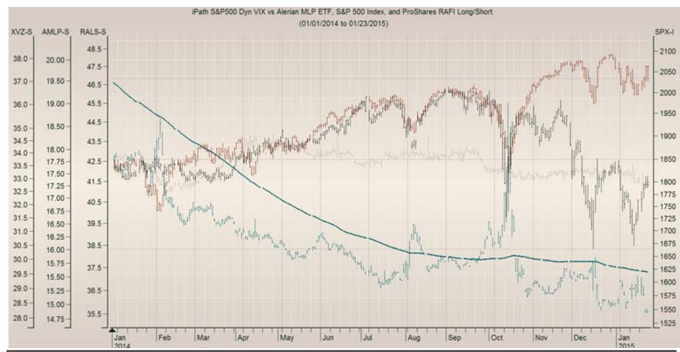

Chart 5—Select alternative assets and S&P 500, 2014. Prices normalized as of 1/1/2014. Telemet.

Lastly, we consistently held high regard for hedging risk with alternative assets including master limited partnerships (AMLP) and volatility (XVZ) that tend to mitigate portfolio risks. As stocks generally advanced through 2014, various hedge positions reduced overall performance.

Remain mindful however that the purpose for these assets in portfolios is to reduce risk not to increase returns. Reducing risk can improve results over long investment horizons.

Chart 6—Oil, Natural Gas, Coal, and Gasoline Futures,

Peering into 2015.

We see opportunity albeit with risk in the year ahead. Dollar strength increases the affordability of global assets. However, if the dollar continues to get stronger, that would diminish returns from those global assets.

Returns from assets that are denominated in local currencies would translate to fewer $US, an external pressure on returns. Foreign issuers of assets denominated in dollars would face internal pressure to continually repatriate their local currency into expensive dollars to service their obligations. It is a good time to be a US investor.

Hawk100 is generally bullish on 2015 economic prospects for the private sector and consumer. Cheap energy and food commodities should improve the bottom line for companies and consumers alike. Potentially favorable operating results could justify higher valuations. Consumers would benefit from spending less of the household budget on everyday items that families have come to expect.

We advise caution though because when prices shift too swiftly chaos can ensue. Under chaotic conditions, businesses withhold long-term capital decisions awaiting either resolution of risks or further clarity. Consumers delay purchases as they evaluate erratically changing decision factors. Chaos can destabilize financial markets while investors grapple to gauge their cost of capital and expected returns.

We welcome your questions and appreciate your membership.

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