



Weekly Market Commentary



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Nine Years Since 9/11

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Highlights

As the combat troops leave Iraq and the proportional response to the threat in Afghanistan is assessed, the United States will likely regain the resources and focus to project more effective foreign policy influence over the rest of its interests.

In response, the currently modest geopolitical risk premiums in oil and some emerging market stocks and bonds may become more volatile as renewed U.S. influence conflicts with nations reluctant to give up their regional authority.

We will seek to protect from threats and profit from opportunities created by the shifting geopolitical landscape.

It has been nine years since the attacks of 9/11 and their immeasurable human toll.

It has also been nine years since the primary focus of American foreign policy became counterterrorism. In addition to a massive investment in homeland security, the United States has engaged in wars in Iraq and Afghanistan intended to root out the threat to Americans. These efforts have consumed a tremendous amount of U.S. resources and focus. This regional focus allowed other nations to take advantage of this distraction to create potential long-term challenges for the United States. For example, the Russians used the United States' distraction to reassert their control over the nations on their periphery. When Russia went to war with Georgia in 2008, the United States did not have the forces with which to counter Russian aggression on behalf of its ally.

As the combat troops leave Iraq and the proportional response to the threat in Afghanistan is assessed, the United States will likely regain the resources and focus to project more effective foreign policy influence over the rest of its interests. This is a potential game changer for many countries such as Russia, Iran, North Korea and even China among others that have gotten used to more regional power than they had prior to 9/11. In addition, with the President's party likely to lose the support of at least one house of Congress in the mid-term elections, the pace of change in domestic policy is likely to slow allowing for more effort to be directed to a President's traditional primary area of influence: foreign policy.

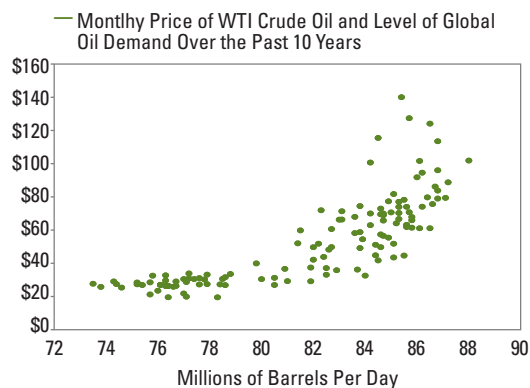
After nine years, the world's sole superpower is getting ready to re-engage a broad number of threats. Last week, Secretary of State Hillary Clinton proposed in a speech to the Council on Foreign Relations that this is a "new American moment" to "lay the foundations for lasting American leadership for decades to come." Clinton pointed to Iran and Russia and stated that the worldview of authoritative regimes "must be confronted and challenged."

While it may sound threatening, military conflict may actually be less likely as the United States redirects its resources. Now that the United States is regaining the military stick it needs to deal directly with threats, it can more effectively use the carrot of policy to address them.

The pace of change on foreign policy may begin to speed up just as domestic policy slows. In response, the currently modest geopolitical risk premiums in oil and some emerging market stocks and bonds may become more volatile as renewed U.S. influence conflicts with nations reluctant to give up their regional authority.



1 Oil Prices and Oil Consumption



Source: LPL Financial, Bloomberg 9/10/10

Oil currently appears to be trading roughly in line with the historical relationship between demand and price. Oil is trading at about \$76. This is within the historical range of \$60-80 when global demand of about 86 million barrels per day, as it is currently [Chart 1]. It briefly broke above this range and entered into the low \$80s in early August when the perceived risk of military action with Iran over Tehran's escalating nuclear program boosted oil prices. We may see more geopolitical-risk-driven volatility in the price of oil in the months and quarters ahead.

On May 20, 2010, following an investigation, the United States called North Korea's sinking of a South Korean warship two months earlier an act of aggression. This was another provocative act from North Korea, which was still under sanctions from last year's nuclear and missile tests. However, top U.S. officials did not call the attack an act of war or state-sponsored terrorism and American forces were not put on a higher level of alert. The lack of action by the United States was anticipated and the widely-watched South Korean stock market index, the KOSPI, had essentially no reaction to the U.S. announcement. This was generally true for other stock markets in the region despite the coincident European debt problems weighing on the markets at that time. However, market participants may become more reactive to the prospects for U.S. action in the months and quarters to come as North Korea further tests the limits of its aggression.

A tactical approach to investing remains prudent. Among the evaluation of many factors impacting the investment environment, we will seek to protect from threats and profit from opportunities created by the shifting geopolitical landscape.

IMPORTANT DISCLOSURES

The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual. To determine which investment(s) may be appropriate for you, consult your financial advisor prior to investing. All performance reference is historical and is no guarantee of future results. All indices are unmanaged and cannot be invested into directly.

The fast price swings in commodities and currencies will result in significant volatility in an investor's holdings.

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