



Quarterly Market Review: April - June 2014

The equity and bond markets continued to defy our expectations in the second quarter with both registering gains. The stock market indexes continued to set new highs and at the same time bond yields fell, not something that happens together very often. Enjoy this quarter's review and have a wonderful summer.

The Markets

After a rocky start, the quarter eventually made up for domestic equities' earlier losses. As winter weather finally lost its chokehold on the U.S. economy, investors also grew increasingly comfortable with the Federal Reserve's slow-and-steady approach to unwinding quantitative easing. As a result, they were willing to take on risk again, handing the Dow and S&P their 11th and 22nd all-time record closes of the year. As tech and biotech stocks rebounded from their early-spring slump, they helped push the Nasdaq back to a level it hadn't seen since March 2000. By June, the small caps of the Russell 2000, which suffered the most in April, had managed to climb back into positive territory for the year, and the Global Dow's year-to-date performance was more than triple that of its U.S. counterpart.

Bond investors continued to confound Fed-wary pundits, sending the benchmark 10-year Treasury yield down as demand pushed up prices. With Iraq joining Ukraine as a source of geopolitical anxiety, concern about oil supplies helped send the spot price above \$107 a barrel. And despite some volatility that took the price of gold down to roughly \$1,240 an ounce, a June rally allowed it to end the quarter at roughly \$1,320.

Market/Index	2013 Close	As of 6/30	Month Change	Quarter Change	YTD Change
DJIA	16576.66	16826.60	.65%	2.24%	1.51%
NASDAQ	4176.59	4408.18	3.90%	4.98%	5.54%
S&P 500	1848.36	1960.23	1.91%	4.69%	6.05%
Russell 2000	1163.64	1192.96	5.15%	1.70%	2.52%
Global Dow	2484.10	2605.62	1.61%	4.11%	4.89%
Fed. Funds	.25%	.25%	.25%	0 bps	0 bps
10-year Treasuries	3.04%	2.53%	5 bps	-20 bps	-51 bps

Chart reflects price changes, not total return. Because it does not include dividends or splits, it should not be used to benchmark performance of specific investments.

The Month in Review

- The end of winter weather brought greater relief than usual this spring, especially after gross domestic product was shown to have contracted strongly in Q1. The Bureau of Economic Analysis's final 2.9% GDP estimate was the worst reading since early 2009 and a far cry from the 2.6% growth of the previous quarter. The BEA said most of the decline was caused by cuts in exports, business investments/inventory, and state and local government spending, while consumers spent more on higher heating costs. The slump caused the Federal Reserve to cut its economic growth forecast for all of 2014 to 2.1%-2.3%. Meanwhile, corporate profits were down 9.1% during the quarter--the largest drop since the end of 2008, according to the BEA.
- The U.S. economy finally regained all of the jobs lost since the recession officially began in late 2007, and total employment was higher than when it previously peaked in January 2008. Also, the unemployment rate inched downward to 6.3%--its lowest level since September 2008.
- By the end of the quarter, the housing market had begun to rebound from its winter slowdown as more homes came onto the market. According to the Commerce Department, sales of new single-family homes leaped 18.6% in May, and the National

- Association of Realtors® said that the 4.9% increase in home resales was the biggest monthly gain in nearly three years. Also, April was a strong month for both housing starts and building permits, though they had tapered off by the end of the quarter.
- U.S. manufacturing also showed signs of strength. Industrial production rose for three months out of four, according to the Federal Reserve. And after three straight months of increases, durable goods orders slumped in May, but the Commerce Department said non-defense orders were up 0.1%. And once winter weather abated, retail sales also showed gains.
 - By quarter's end, consumer inflation had risen at the fastest monthly pace (0.4%) in more than a year. The Bureau of Labor Statistics said the increases were driven by higher prices for housing, food, electricity, and gas. However, Fed Chair Janet Yellen called recent upticks "noisy" data and said the 2.1% inflation rate for the last 12 months isn't a concern. The past year's 2% increase in wholesale prices is substantially higher than the 1% of last May, but also within the Fed's comfort zone. However, one of the Fed's favorite inflation gauges--personal consumption expenditures--saw its biggest 12-month gain since October 2012, raising questions about possible future inflation.
 - The Federal Reserve's monetary policy committee continued to unwind its economic support by cutting \$10 billion worth of bond purchases each month. The committee now predicts that additional improvement in the economy and job market in coming months will allow it to increase the current near-zero target rate to 1.2% by the end of 2015 and 2.4% in 2016. Longer-term, however, it sees that rate leveling out around 3.75%.
 - To stimulate lending, the European Central Bank's key interest rate was cut to -.01%; it's now essentially charging banks to hold their funds rather than paying interest on deposits. The ECB also said it's prepared to take additional steps later if necessary. The action is designed to stimulate lending, stave off the threat of deflation, and help jump-start the European economy, which grew 0.3% or less during Q1.
 - The Chinese economy showed signs of slowing. According to the country's National Bureau of Statistics, the annual growth rate dropped below the official 7.5% target to 7.4%, the HSBC Purchasing Managers' Index of Chinese manufacturing showed a slight contraction, and housing sales prices fell in half of 70 major cities.

Eye on the Month Ahead

The Fed will be watching the housing market this summer as it considers the timing of future interest rate increases. Also, the second week of July marks the unofficial start of the Q2 corporate earnings season. After the dismal Q1 GDP final reading, those reports may assume even greater significance than usual, as will the Bureau of Economic Analysis's initial estimate of Q2 economic growth.

Key dates and data releases:

- 7/1: Auto sales, ISM manufacturing report, construction spending
- 7/2: U.S. factory orders
- 7/3: Unemployment/payrolls, balance of trade, ISM services report
- 7/9: Federal Open Market Committee minutes
- 7/15: Retail sales, Empire State manufacturing
- 7/16: Wholesale inflation, international capital flows, industrial production, Fed "beige book" report
- 7/17: Housing starts, Philadelphia Fed manufacturing
- 7/18: Leading economic indicators, options expiration
- 7/22: Consumer inflation, existing home sales
- 7/24: New home sales
- 7/25: Durable goods orders
- 7/28: Dallas Fed manufacturing survey
- 7/29: Home prices
- 7/30: Federal Open Market Committee announcement, Q2 GDP initial estimate

Data sources: Economic: Based on data from U.S. Bureau of Labor Statistics (unemployment, inflation); U.S. Department of Commerce (GDP, corporate profits, retail sales, housing); S&P/Case-Shiller 20-City Composite Index (home prices); Institute for Supply Management (manufacturing/services). Performance: Based on data reported in WSJ Market Data Center (indexes); U.S. Treasury (Treasury yields); U.S. Energy Information Administration/Bloomberg.com Market Data (oil spot price, WTI Cushing, OK); www.goldprice.org (spot gold/silver); Oanda/FX Street (currency exchange rates). All information is based on sources deemed reliable, but no warranty or guarantee is made as to its accuracy or completeness. Neither the information nor any opinion expressed herein constitutes a solicitation for the purchase or sale of any securities, and should not be relied on as financial advice. Past performance is no guarantee of future results. All investing involves risk, including the potential loss of principal, and there can be no guarantee that any investing strategy will be successful.

The Dow Jones Industrial Average (DJIA) is a price-weighted index composed of 30 widely traded blue-chip U.S. common stocks. The S&P 500 is a market-cap weighted index composed of the common stocks of 500 leading companies in leading industries of the U.S. economy. The NASDAQ Composite Index is a market-value weighted index of all common stocks listed on the NASDAQ stock exchange. The Russell 2000 is a market-cap weighted index composed of 2,000 U.S. small-cap common stocks. The Global Dow is an equally weighted index of 150 widely traded blue-chip common stocks worldwide. Market indices listed are unmanaged and are not available for direct investment.