Market Update

September 30, 2014

The only word to describe the geopolitical atmosphere in the third calendar quarter of 2014 is "tumultuous." The downing of a Malaysian passenger jet over the Ukraine/Russian border in July increased military tensions in Eastern Europe. The deadly outbreak of Ebola in West Africa captured U.S. headlines as two medical missionaries were airlifted from Liberia back to the U.S. in August for life saving treatment of the virus. The Middle Eastern terrorist group ISIS, exploded into an enormous international threat in August, after they released videos showing the horrific beheadings of two American journalists and a British aid worker. In September, massive numbers of students in Hong Kong began protests about future governance in the territory. These protests have sparked worldwide concern that the mainland Chinese Government could respond with Tiananeman Square type force as occurred in 1989.

Despite this worldwide chaos, and somewhat counter intuitively, U.S. capital markets seemed generally insulated from the ongoing crises. The S&P 500 was up 0.6%, the Dow Jones Index was up 1.3% and NASDAQ was up 1.9%. During the third quarter, the market favored large, conservative companies because they were perceived to have lower risk, an important attribute. Also, U.S. markets easily accommodated Initial Public Offerings of stocks, Merger & Acquisition activity and corporate bond issuance, all with record setting volumes. None of these records would normally occur during global chaos. The ongoing policy of accommodation by the Federal Reserve, particularly in keeping interest rates low, was the primary driver of all this capital markets activity.

Global capital markets were more unsettled during the third calendar quarter of 2014 than they were during the second quarter. This reflected their reliance on international trade to bolster their economy, however the global turmoil negatively impacted trade. Some U.S. based markets did well as noted above. This was due to better economic fundamentals in the U.S., as measured by GDP data, and its role as a "safe haven" during troubled times globally. For example, U.S. based mid-cap stocks were down 1.2%, small cap stocks were down 5.5%, while large cap non-U.S. stocks were down 6.2% and emerging markets were down 3.9%.

So far this year, within commodity markets worldwide, oil prices are down 7% and gold prices are flat. The U.S. dollar is strong, up 7.5% in comparison to the Euro and the Yen in just the past six weeks, and this is a contributing factor to the commodity price weakness.

In spite of the worldwide chaos, I remain optimistic that U.S. equities and particularly large capitalization U.S. equities will continue to do well. Consequently, we continue to be fully invested in equities within client portfolios.

Raymond A. Beplat, CFA
Chief Investment Officer