MURRAY
INVESTMENT MANAGEMENT

3rd Quarter 2014 Update

Economic Review

After very strong 2nd quarter growth (up 4.6%), the U.S. economy likely grew around 3% in the 3rd quarter. While still showing improvement, the economy is not growing at its long-term potential, and the recovery is still believed to be below average.

The employment situation continues to improve with the unemployment rate falling to 5.9% at the end of the quarter and average monthly job growth of 227,000 year to date. Job growth is very important to the overall economy as consumer spending makes up around 70% of GDP growth.

The Federal Reserve kept interest rates at historically low levels but has been winding down its long-term bond buying program. In addition, the Fed will likely be looking to raise short term rates in the next 12 months but has stated that it intends to keep rates low for "a considerable time after the asset purchase program ends." When the Fed changes this language in its statements, we will have a better idea of when rates should rise.

Equity Market Performance

	QTD	YTD
S&P 500	1.13%	8.34%
MSCI EAFE (International index net return)	-5.88%	-1.38%
Rusell 2000 (small cap)	-7.36%	-4.41%

The S&P 500 advanced 1.13% during the quarter and is up 8.34% for the year. As a large cap U.S. stock benchmark, the S&P 500 does not reflect the entire market. The small cap space is down (-4.41%) for the year while the broad international benchmark is down (-1.38%). Both were down significantly in the 3rd quarter. Taken together, overall equity performance has been somewhat of a mixed bag.

Bond Market Performance

	QTD	YTD
BarCap US Aggregate Bond (Broad Bond Market)	0.17%	4.10%
BarCap Municipal	1.49%	7.58%
BarCap US Treasury Long	2.69%	15.15%
BarCap US Corporate	-0.08%	5.60%
BarCap US Corporate High Yield	-1.87%	3.49%

The 10 year Treasury rate (2.52%) did not change much from the end of June, and the broad bond market was slightly up during the quarter. The corporate high yield space was down for the quarter but has posted positive results year to date.

Economic Outlook

The general view is that the U.S. economy will continue to show improvement but grow at below trend levels. We should expect mixed data reports (strong and weak) with the balance tilting toward improving growth.

Employment is expected to continue to improve, but flat wage growth is serving as a drag on overall consumer spending. Lower oil prices could offset this concern as consumers should have more cash to spend.

U.S. corporations appear to be in decent shape and should continue to grow revenues at levels consistent with nominal GDP growth. This should translate into solid earnings growth which could drive equity markets higher.

Market Outlook

Market volatility will likely pick up in the 4th quarter as geo-political events and a potential 2015 interest rate move by the Fed weigh on equity markets. A growing economy and improving earnings should be good for stocks, but we will not likely get much more P/E expansion which will limit stock performance. A grind-it-out type of market with modest returns would not be a surprising path in the shorter term.

As mentioned last quarter, domestic equity valuations do not appear overly stretched, but they are not considered cheap, and it is becoming difficult to find attractively priced asset classes to put money to work. Consequently, looking for opportunities to rebalance back to equity targets and keeping some less risky assets to balance out portfolios may be a good strategy at this time.

The fixed income sector is still generally not attractive as the risk / reward profile for many fixed income securities is not favorable. Given these limited opportunities, maintaining a disciplined investment approach that sticks to stated objectives and goals is very important at this time.

Murray Investment Management

If you would like help with establishing an investment plan or would like to schedule a portfolio review, please give us a call. Also, please pass along our name to anyone that may be in need of investment advice.

Source: bls.gov, Morningstar, bea.gov, federalreserve.gov and treasury.gov
The performance data shown represents past performance, which is not a guarantee of future results.
Return data is as of 09/30/2014. Except as noted, index returns are total returns.

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