MURRAY
INVESTMENT MANAGEMENT

2nd Quarter 2014 Update

Economic Review

After contracting (2.9%) for the first three months of the year, the U.S. economy bounced back during the 2nd quarter with expected growth around 3%. The slowdown during the 1st quarter was largely weather related and is not expected to reflect a longer term trend as the economy has regained its footing.

During the quarter, the U.S. Federal Reserve maintained its accommodative stance but continued to reduce its long-term bond purchases with plans to end this program at the end of the year. The Fed kept short term rates at historically low levels.

The employment situation continued to show improvement, but many remain unemployed or underemployed which is constraining consumer spending, inflation and overall GDP growth. At the end of May, the unemployment rate was 6.3% (6.7% at year-end), and average monthly job growth increased to 214,000 (current year) compared to 194,000 in 2013.

Equity Market Performance

	QTD	YTD
S&P 500	5.23%	7.14%
MSCI EAFE (International index net return)	4.09%	4.78%

The S&P 500 had a very strong quarter (up 5.23%) while hitting all-time highs and producing its 6th consecutive positive quarter. These results were achieved against a backdrop of very low volatility (up and down price movement).

For the quarter, the energy and utility sectors were among the better performers, and large cap names generally outperformed small caps. Broad International markets were also strong (up 4.09%) with Emerging markets performing particularly well (up 6.71%).

Bond Market Performance

	QTD	YTD
BarCap US Aggregate Bond (Broad Bond Market)	2.04%	3.93%
BarCap Municipal	2.59%	6.00%
BarCap US Treasury Long	4.70%	12.14%
BarCap US Corporate	2.66%	5.68%
BarCap US Corporate High Yield	2.41%	5.46%

Fixed income markets rose during the quarter as the 10 year Treasury fell from 2.73% to 2.53%. Falling rates were somewhat of a surprise and have produced unexpectedly strong performance this year with long term Treasuries posting particularly good results.

Economic Outlook

Limited wage growth, a less accommodating Fed and the potential for a geopolitical event are economic concerns for the 2nd half of the year while low interest rates, a positive wealth effect (better housing and equity markets) and an improving employment situation will serve as tailwinds for GDP growth. Taken together, the U.S. economy should continue to improve with expected growth around 3% for the second half of the year.

With inflation and GDP growth at modest levels, the Fed will continue its balancing act of restraining inflation but not raising rates too quickly to derail the recovery. The general consensus is that the economy is improving enough for the Fed to begin to raise short term rates in 2015.

Market Outlook

As investors have become confident that the Fed will remain accommodative (low rates), equity markets have moved higher and higher with low volatility this year. High returns and low volatility can lead to too much risk taking, and with low interest rates, riskier assets can become more and more attractive.

In this type of environment, it's important to remember that risk matters. Some type of event (geopolitical, Fed raising rates, etc.) will likely cause volatility to return and equity markets to retreat. Now, as always, maintaining a disciplined investment approach that sticks to stated objectives and goals is very important.

While domestic equity valuations are not overly stretched, 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.

But at current interest rate levels, finding opportunities in the fixed income space is challenging too. As such, for the more stable portion of an investor's portfolio, holding cash and shorter term bonds seems to be a reasonable approach.

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, cnbc.com, wsj.com, iShares and treasury.gov
The performance data shown represents past performance, which is not a guarantee of future results.
Return data is as of 06/30/2014. Except as noted, index returns are Total Returns.

www.murrayinvestment.com | 713.850.7444 | sammurray@murrayinvestment.com