New Albany
Investment Management

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Market Insight: Wrapping up 2013…. Feast or Famine

Many would say 2013 has been a banner year for investors. With the headlines touting multiple new highs in the financial markets, anyone with an investment portfolio should be feeling a bit jollier this season. By many measures this is true, but underneath the headline numbers a different story is revealed, telling a tale of huge differential in performance across asset sectors both here in the US and globally. Much of the difference is due to risk, where the magnitude of risk has been directly proportional to the size of return. But other differentials are due to sentiment and economic shifts. Thus the story of investing in 2013 has been even dicier and more perilous than meets the eye. For many investors, it has been either feast or famine.

Below are highlights of some of the best and worst markets of 2013.

The 'Conservative' investor penalized: By definition, a 'conservative' investor's level of risk (measured as potential future volatility of value) is low which means their portfolio typically has at least 70% to 90% of their portfolio invested in investment grade bonds. Now, with the expectation of the Fed eventually pulling back from supporting bonds, the bond market has been in retreat such that for the first time in over fourteen years, the return is negative, both in nominal and real (inflation adjusted) terms. The implication of this has been far reaching to anyone near or entering into retirement or who has prudently reduced risk in anticipation of a draw down (ie: college or major purchase). In particular, for those investors who own mostly bond funds or 'age-based structured investments' where the allocation to bonds increases as the draw down date approaches, the returns have been very poor. Below is a comparison of year-to-date returns for various weighted Risk Strategies, Corporate & US Treasury Bonds (source Morning Star). It is clear by the returns in bonds, that the more heavily weighted the strategy is in Bonds, the worse the total return.

Risk Strategy/ Bond Allocation	YTD Return	Bond Index	Corporate	US Treasuries
Conservative (71% Bonds)	+2.6%	Short Term	+0.7%	+0.4%
Moderate (40% Bonds)	+12%	Intermediate Term	-0.7%	-1.7%
Aggressive (9% Bonds)	+20%	Long Term	-6.7%	-8.8%

Global Divide: What do Japanese and Asian markets have in common? NOTHING!! After ten years of dormancy, the Japanese stock market has awakened. This is a result of new and extraordinary quantitative easing policies by the Bank of Japan aimed to devalue the yen and promote a rise in inflation to +2% (yes, that is the mandate of Japan's monetary policy). Unfortunately this easy money has not spilled over into other Asian countries who are struggling with rising interest rates and slowing international investment demand. The performance differential between the two is startling, nearly +37% difference in return when compared on a $Yen basis

Japan Stk Index:	Asian Pacific Stk Index Ex-Japan:
+25% $US; +45% $Yen	+1.2% $US; +7.8% $Yen

Fools Gold and other Precious Metals loose their luster: The original premise for owning gold was as a hedge against a falling dollar and rising inflation resulting from the Federal Reserve's massive money printing policies. This sentiment pushed the price of gold +82% from 2009 thru 2012 and also caused the prices of other precious metals such as silver and platinum to rise. But this year with the expectation of the Fed to begin pulling back, sentiment has shifted drastically, pressuring all precious metal prices significantly lower. Below are the YTD 2013 returns.

Gold: -27%	**Silver**: -26%	**Platinum**: -13%

Emerging Markets are sub-merging: From 2009-2011, China, India, Brazil, and Chile strongly benefited from the easy US monetary policy. But since 2011 these markets stalled as the US economy has gained traction. A combination of weak global demand, slowing international investment flows, rising local interest rates, and falling commodity prices have culminated into very slow growth in 2013 for these export driven economies and resulted in dismal stock market returns. Below are YTD 2013 Returns:

Emerging Market Stk Index: -5%	**Latin American Stk Index**: -16%

Europe and the US Stock Markets on a tear! Call them the best houses in a bad neighborhood, these two markets have a huge tail wind comprising of cheap money, firming economic growth, and positive domestic and international investment flows. Two broad indices summarize a very positive investment climate.

US Stk Index: +27%	**Europe Stk Index**: +19%

US Champions and Dogs: The performance of the broad US Market Index (above) masks a broad range of returns in various sectors. Of most significant note:

Real Estate: -0.3%	**Mid Cap Value**: +36%
Basic Materials: +14%	**Large Cap Value**: +23%

Summary: The broad range of performance in these markets in 2013 illustrates the importance of diversification and the need for active management. Client portfolios are structured to minimize volatility but still capture return in accordance with established risk parameters and investment goals. 2014 will be another challenging year of recognizing profitable markets and avoiding the pitfalls.

As always, please contact me with any concerns or questions.

Kind Regards,

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