Dear Friends: December 6, 2013

Home Stretch

The much anticipated Holiday Season is upon us and the markets are racing to record closings in 2013!

The global markets have been supported by many factors including: improving corporate earnings, recovering global economies, robust leading indicators from the US, and the continued support from the Federal Reserve Bank (FRB) and its ongoing quantitative easing program.

So far in 2013 the S&P 500 Index is up 25 percent, poised for the best annual gain in 15 years. The S&P 500 climbed 2.8 percent in November for its third straight monthly gain. The MSCI All-Country World Index reached its highest point since January 2008 on November 29th while rising 18 percent overall in 2013, heading for its best annual return since 2009. Japan's Nikkei 225 has also advanced the most since 2007 due to efforts by the Prime Minister to devalue the Yen and spur economic growth.

The boom to the equity markets, however, is being achieved amid the weakest domestic employment recovery in seven decades. Five years into a rally that has restored $14 trillion to share prices, U.S. payrolls remain 1.5 million below the level in 2008, according to data compiled by Bloomberg.

According to Janet Yellen, at her November 14th confirmation hearing, unemployment is "still too high, reflecting a labor market and economy performing far short of their potential." More than half the gauges the FRB uses to track the labor market are still below pre-recession levels. More recently however we received positive news with the November unemployment showing a drop in the unemployment level to 7.0%. The FRB said after its October meeting that it will press on with its $85 billion in monthly asset purchases and continue to hold short-term rates near zero at least as long as unemployment is above 6.5 percent and forecast inflation is below 2.5 percent. Economists in a Bloomberg survey expect that the central bank won't begin reducing its monthly bond purchases until March at the earliest because of unemployment concerns.

If employment does not continue to accelerate, stocks will likely be harmed in the long run, even with the FRB's support. There is an intangible effect of prolonged unemployment on consumer morale that will ultimately impact consumer confidence when poor employment reports persist in the press.

While American workers struggle, investors are benefiting in the short term as expense reductions and record low borrowing costs drive profits and underpin a 167 percent advance in the S&P 500 over the past 57 months.

Entering 2014, indications support further advances to the global equity prices well into 2015, assuming the renewed issue of the Fiscal Cliff doesn't rear its ugly head in 2014. Notwithstanding possible fiscal issues, ongoing Fed support and Analysts' expectations that corporate profitability has room to improve will keep the equity market buoyant well into 2015. Incrementally, economic strength (as measured by GDP growth), both in the US and developed Europe, is showing improvement and governments are beginning to loosen their purse strings. The age of austerity may be nearing an end. Economists at Goldman Sachs and Deutsche Bank AG say this relaxation will help industrial economies almost double their rate of expansion next year to 2.2 percent, the most since 2010.

The 10 year Treasury rate is currently at 2.86% after backing up over 100 basis points in the second quarter. We do not anticipate a dramatic rise in rates the near term but are continuing to monitor the situation and keep our duration towards the shorter end of the yield curve.

We hope that this news helps make this a lovely Holiday season for you and your families.

Happy Holidays,

Locust Capital Management, LLC