



# ABULS, BONE & ELLER GROUP OF RAYMOND JAMES®

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## HINDSIGHT IS 20/20

*“It isn’t the mountain ahead that wears you out; it’s the grain of sand in your shoe.”*

- ROBERT W. SERVICE

The equity markets climbed to their highest levels in history during the third quarter. The third quarter 2014 saw the return of volatility in the financial markets. We have talked about an absence of downside volatility in the equity markets for several quarters. With hints of evidence that global GDP may be slowing, notably the Eurozone, the global markets experienced wide swings in price changes. Additionally, the markets seem to be pricing risks with more discretion as riskier assets such as US small cap stocks (Russell 2000 index -7.40%) experienced significantly larger losses during the quarter than the US broader market (S&P 500 1.10%).

As we complete this writing on October 10, the equity markets have continued their sell-off. The major averages are approaching a 5% decline from the peak. Long-term an annual peak to trough decline of approximately 14% is average. We are not alarmed by this move. In fact a move down of 10-15% from peak levels may be helpful to attract some capital that remains on the sidelines and serve as a reminder that the equity markets do experience price swings.

Due to the economic concerns in Europe, the international equity markets were under-performers for the quarter. Germany is the driver for the European economy. There was weakness in economic output for Germany during the 3rd quarter and it dragged markets down with it. The German market in dollar terms was down -11.20% during the quarter.

Index	Description	3Q14	10-Yr Annualized
Russell 2000	Small US Stocks	-7.40	9.10%
S&P 500	Large US Stocks	1.10	7.40%
MSCI EAFE	International Stocks	-5.80	7.40%
Diversified EM	Emerging Markets Stocks	-3.40	11.50%

Drilling down to a deeper view of the US equity markets shows an even larger disparity in US equity returns. For the quarter, there was a 10.10% return differential between large cap growth 1.50% and the least performing small cap growth -8.60%. Year to date performance differences are even larger with large blend stocks at 8.30% and small cap growth stocks at -4.70%.

### 3Q2014 US EQUITY RETURNS

	Value	Blend	Growth
Large	-0.20%	1.10%	1.50%
Small	-8.60%	-7.40%	-6.10%

### YTD 2014 US EQUITY RETURNS

	Value	Blend	Growth
Large	8.10%	8.30%	7.90%
Small	-4.70%	-4.40%	-4.0%

We have been actively over-weighting our US equity allocation in our model portfolios to large cap stocks during the current market cycle. With the sale of the balance of our small cap growth position in July of 2014, we have the smallest allocation to small cap stocks in our memory. To date we have only a 1.50% allocation to US small value stocks in our 100% equity allocation. This has proved to be a positive for performance year to date and our expectations are for continued large cap stock out-performance for the for-seeable future.

US fixed income experienced positive returns in the 3rd quarter. The 10-year treasury yield was relatively flat during the quarter; i.e. 9/30/2014 yield of 2.52% versus a 6/30/2014 yield of 2.53%. Surprisingly to most, the 10-year treasury has provided a strong return of 6.93% year to date. Dropping yields across the board have boosted bond prices and provided more attractive total returns than many anticipated beginning 2014.

Year to date total returns for fixed income investors have been attractive. Emerging market returns are leading all asset classes with a total return of 8.0%; followed by municipals 7.20% and mortgage -backed debt at 4.20%.

Index	Bond Description	3Q14	YTD
Gbl High Yield	Global Low Quality	-3.3	2.6
MBS	Mortgage Backed	0.2	4.2
Gbl Corporate	Global Corporate	-2.3	2.9
Barclays Agg.	A Market Weighted Blend	0.2	4.1
Municipal	Intermediate-Term Municipals	1.5	7.2
Treasury	US Treasuries	0.3	3.1
EMD	Emerg Markets Local Currency	-5.7	0.0
TIPS	US Treasury Inflation Protected	-2.0	3.7
EMD USD	Emerg Market Debt - US \$	-0.6	8.0
Gbl Sov	Global Government Debt	-5.3	0.3

## REQUIRED DISCLOSURES

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Diversification and strategic asset allocation do not ensure a profit or protect against a loss. Investments are subject to market risk, including possible loss of principal. Gross Domestic Product (GDP) is the annual market value of all goods and services produced domestically by the US. Alternative investment strategies involve greater risks and are only appropriate for the most sophisticated, knowledgeable and wealthiest of investors. High-yield bonds are not suitable for all investors. When appropriate, these bonds should only comprise a modest portion of your portfolio.

The S&P 500 is an unmanaged index of 500 widely held stocks. The MSCI Emerging Markets Index is designed to measure equity market performance in global emerging markets. The Russell 2000 index is an unmanaged index of small cap securities which generally involve greater risks. Barclays Capital U.S. Aggregate Bond Index is made up of the Barclays Capital U.S. Government / Corporate Bond Index, Mortgage-Backed Securities Index, and Asset-Based Securities Index, including securities that are of investment grade quality or better, have at least one year to maturity, and have an outstanding par value of at least \$100

million. The MSCI EAFE (Europe, Australia, and Far East) index is an unmanaged index that is generally considered representative of the international stock market. These international securities involve additional risks such as currency fluctuations, differing financial accounting standards, and possible political and economic instability. The Dow Jones-UBS Commodity Index aims to provide broadly diversified representation of commodity markets as an asset class. It is not possible to invest directly in an index. The Vanguard REIT Index is a real estate investment trust fund that offers investors wide exposure in the real estate sector at a low price. The fund holds each of its stocks in approximately the same proportion as the weighting in the MSCI US REIT Index. It is not possible to invest directly in an index.

The NASDAQ Composite Index is an unmanaged index of all stocks traded on the NASDAQ over-the-counter market. The Dow Jones Industrial Average is an unmanaged index of 30 widely held securities.

The value of fixed income securities fluctuates and investors may receive more or less than their original investments if sold prior to maturity. Bonds are subject to price change and availability.

This analysis does not include transaction costs and tax considerations. If included these costs would reduce an investor's return. As federal and state tax rules are subject to frequent changes, you should consult with a qualified tax advisor prior to making any investment decision. Raymond James does not provide legal or tax advice on these or any other transactions.

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