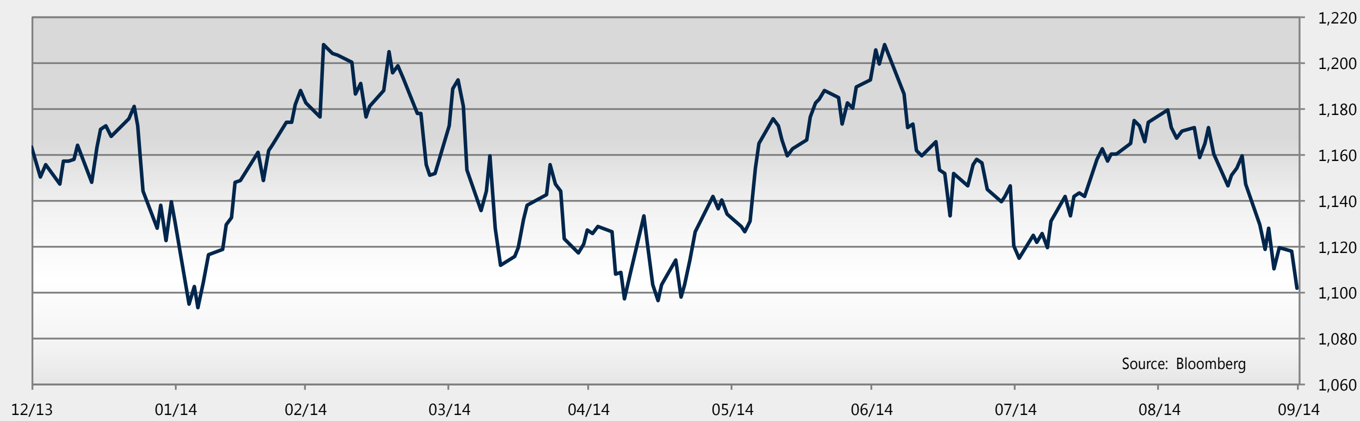
third quarter 2014

INVESTMENT *perspective*

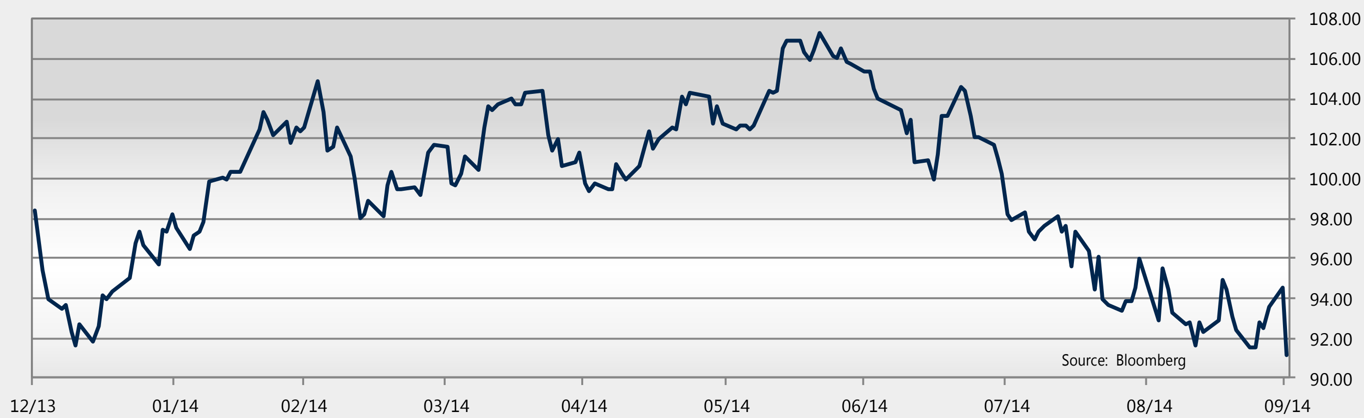
During the third quarter market breadth within the U.S. equity markets continued to deteriorate. Although the S&P 500 managed to gain 1.1%, the Russell 2000 Index of small capitalization stocks declined 7.4% during the quarter. As we mentioned in the prior quarter, we anticipated a decline across markets with an increase in volatility in the credit markets, leading to an equity market correction. To date the correction has been concentrated in the small cap universe; however the increase in volatility across currency, credit, and commodity markets could extend the correction into larger capitalization stocks (S&P 500).

Russell 2000 Index (12/31/13 to 9/30/14)



The current market volatility should continue as capital markets adjust to global shifts in central bank policy. The ECB is committing to easier monetary policy at the same time the U.S. Federal Reserve is ending quantitative easing and discussing the potential for interest rate increases in 2015. These opposing policy initiatives are directly impacting currency markets with the Euro falling approximately 8% against the U.S. Dollar and the U.S. Dollar rising approximately 7.5% against a basket of global currencies. These currency moves have resulted in a 13.5% decline in oil prices and an 8.5% decline in the price of gold.

West Texas Intermediate (12/31/13 to 9/30/14)



The increased volatility, combined with rising global geopolitical concerns, is providing ample reason for short term traders to sell liquid assets and increase short positions. Short interest on the NYSE is approaching the highs reached in 2008, which is sowing the seeds for future purchases of such positions once traders need to cover. Some of the concerns affecting the global markets include Russia's dispute with Ukraine and the U.S. sanctions that followed. The recent flare up in Hong Kong where protesters are demanding more independence from China and specifically the right to elect their own leader without interference

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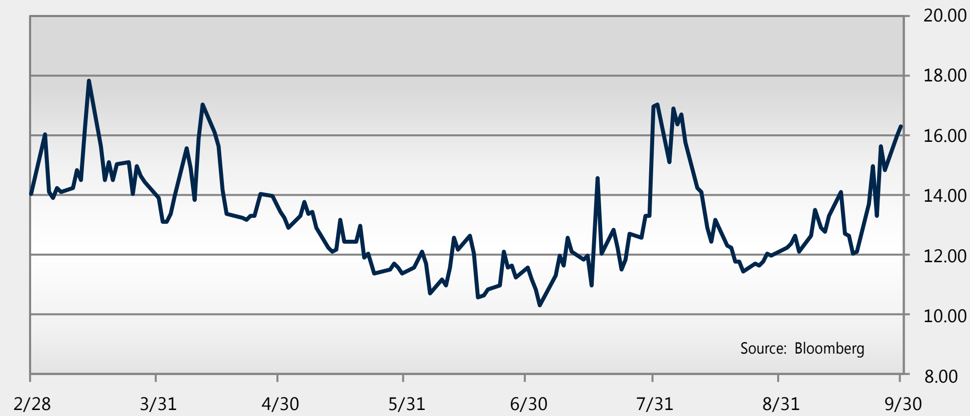
from Beijing. The ongoing unrest in the Middle East has led to ISIS controlling a large territory while continuing their advance on Baghdad. These geopolitical events may keep the U.S. 10 year Treasury from gravitating higher even with the Fed continuing to taper, especially considering that the U.S. 10 year bond has a more attractive yield and risk profile than many of its European counterparts. The strengthening dollar may be the canary in the coal mine that leads to a correction in large cap stocks since many of these companies generate a significant portion of their revenues overseas.

VIX Index -Volatility (2/28/14 - 9/30/14)



In addition to geopolitical events creating uncertainly, economic growth in the United States and internationally remain tepid. We continue to expect U.S. companies to face margin pressures as the Fed raises interest rates in the back half of 2015, coupled with acceleration in capital expenditures that will challenge modest revenue growth.

Despite the potential for a near term correction in the equity markets, we expect the credit market to remain supportive of equity values over the medium term and will welcome any correction as an opportunity to make attractive investments. While the nature of the bull market is changing, there are still individual stocks that will perform well despite the increasing market headwinds. This positive outlook continues to be stock-specific and not reflective of opportunities in specific industries, regions of the world, or broader market indices.

The backdrop for the fixed income market remains fairly constructive despite the modest rise in interest rates in the third quarter. Economic growth in the U.S. should range between 2% to 3% and inflation will likely remain subdued. Both metrics are below levels that would cause the Fed to pull forward its timeline for raising short term rates in 2015. While U.S. Treasury yields rose in the third quarter, the fact that the global recovery has slowed and is now more U.S.-driven should place a relative bid under Treasuries and hold long term rates within a fairly narrow trading range. Relative to Treasuries, U.S. investment grade credit was weak through most of the third quarter, driven in part by a steady increase in supply. However, future supply should not accelerate given U.S. banks and other financial institutions are still reducing risk and deleveraging to meet stricter regulatory guidelines. Also, in the current merger and acquisition cycle, such deals are rarely being accomplished with excessive debt. We are comfortable maintaining an overweight position to credit in client portfolios.