



Q4

Quarterly Market Review
Fourth Quarter 2013

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This report features world capital market performance and a timeline of events for the last quarter. It begins with a global overview, then features the returns of stock and bond asset classes in the US and international markets.

The report also illustrates the performance of globally diversified portfolios and features a topic of the quarter.



Overview:

Market Summary

Timeline of Events

World Asset Classes

US Stocks

International Developed Stocks

Emerging Markets Stocks

Select Country Performance

Real Estate Investment Trusts (REITs)

Commodities

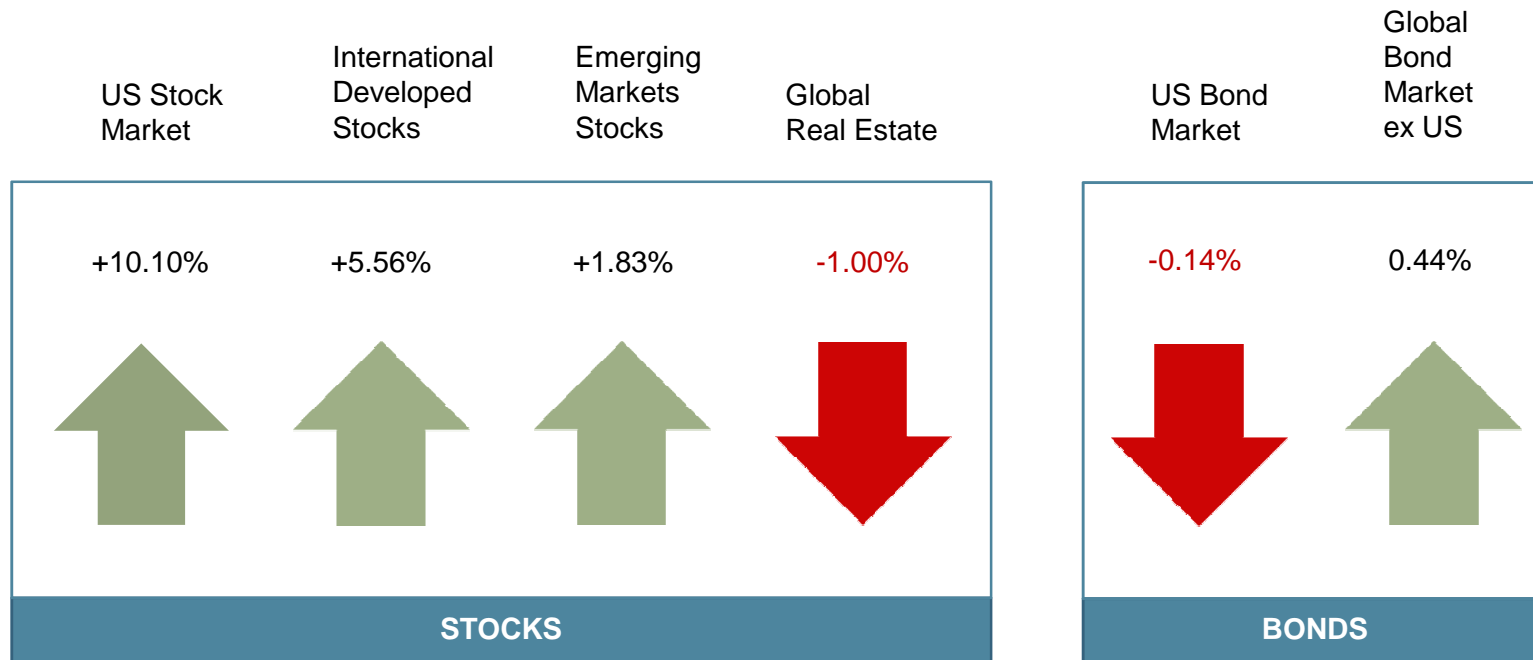
Fixed Income

Global Diversification

Quarterly Topic: Many Happy Returns

Market Summary

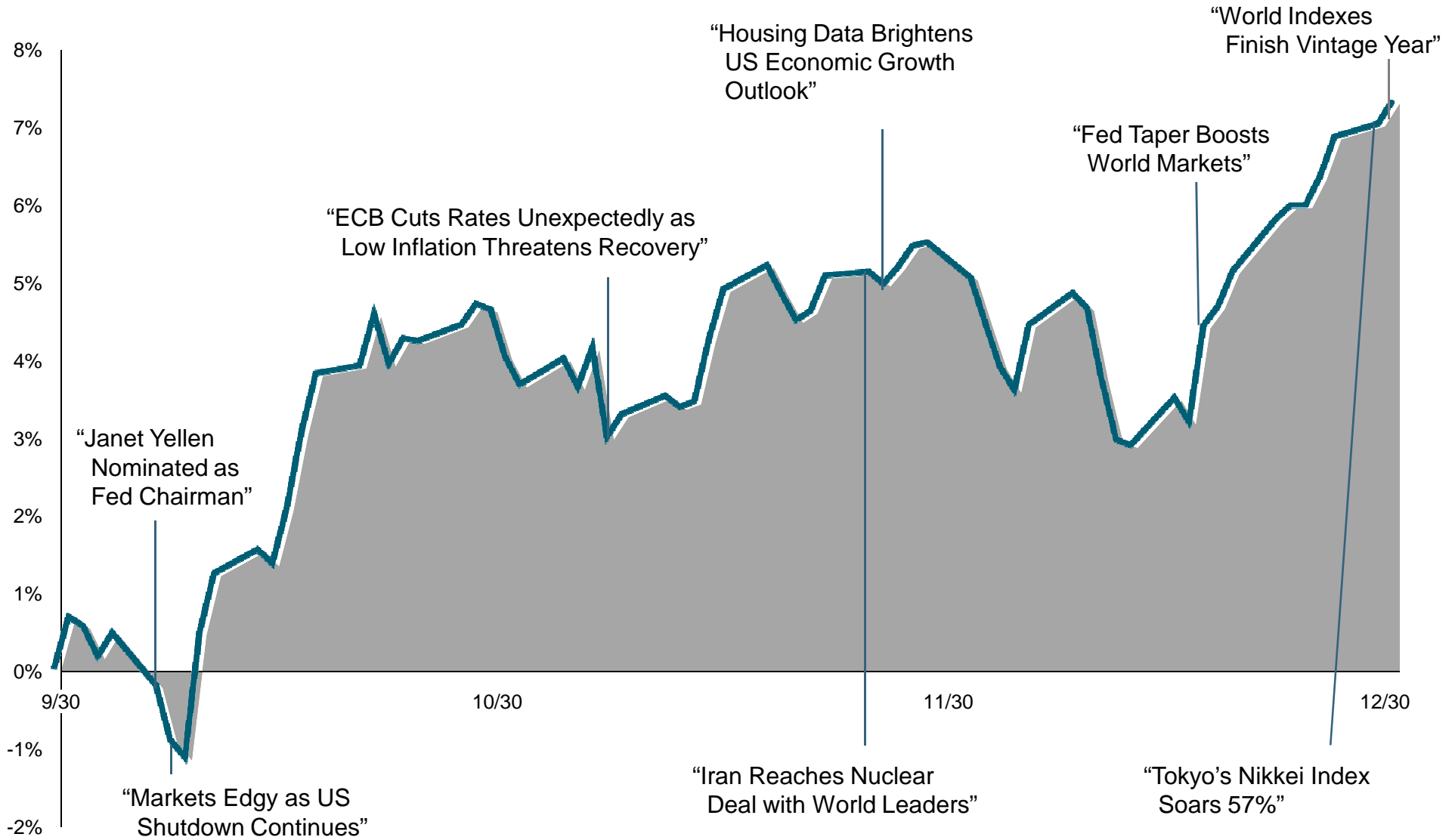
Fourth Quarter 2013 Index Returns



Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Market segment (index representation) as follows: US Stock Market (Russell 3000 Index), International Developed Stocks (MSCI World ex USA Index [net div.]), Emerging Markets (MSCI Emerging Markets Index [net div.]), Global Real Estate (S&P Global REIT Index), US Bond Market (Barclays US Aggregate Bond Index), and Global Bond ex US Market (Citigroup WGBI ex USA 1–30 Years [Hedged to USD]). The S&P data are provided by Standard & Poor's Index Services Group. Russell data © Russell Investment Group 1995–2014, all rights reserved. MSCI data © MSCI 2014, all rights reserved. Barclays data provided by Barclays Bank PLC. Citigroup bond indices © 2014 by Citigroup. US long-term bonds, bills, and inflation data © Stocks, Bonds, Bills, and Inflation Yearbook™, Ibbotson Associates, Chicago (annually updated work by Roger G. Ibbotson and Rex A. Sinquefeld).

Global Stock Market Performance

Selected headlines from Q4 2013



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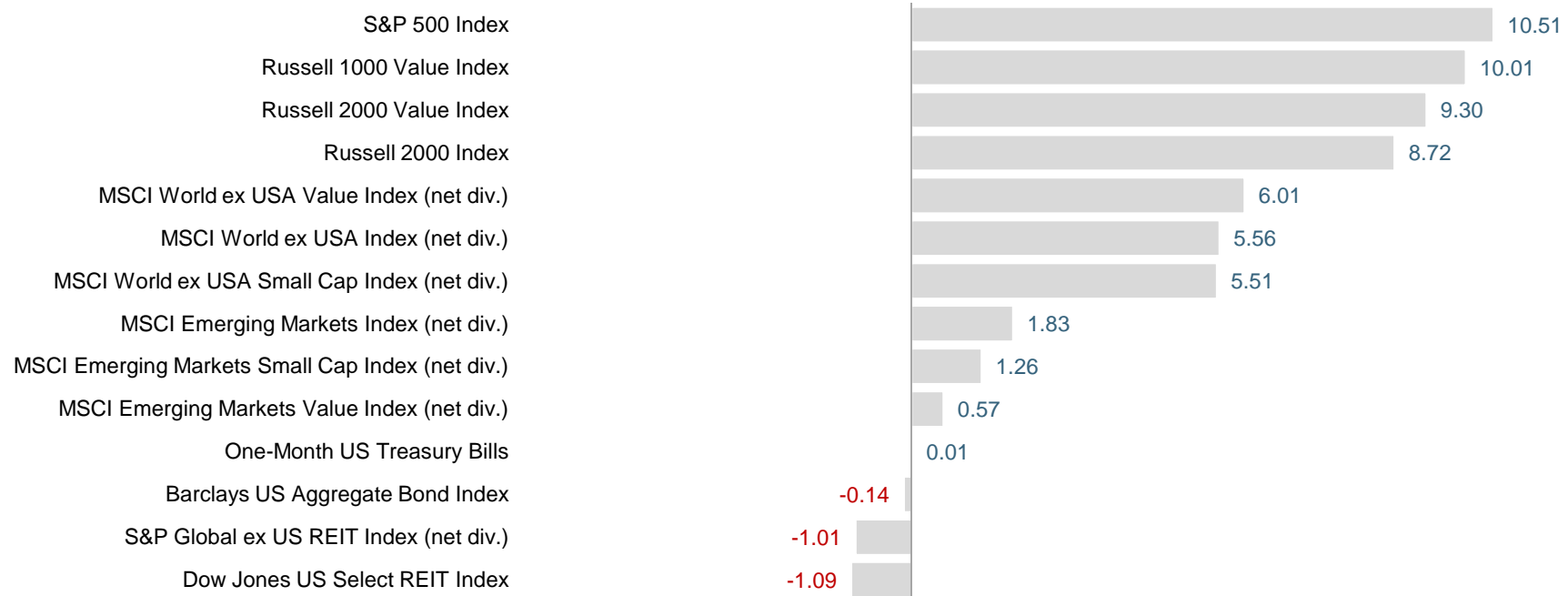
Returns in US dollars. Graph Source: MSCI ACWI Index. MSCI data © MSCI 2014, all rights reserved. It is not possible to invest directly in an index. Performance does not reflect the expenses associated with management of an actual portfolio. Selected headlines are not indicative of any impact they may or may not have had on the market.

World Asset Classes

Fourth Quarter 2013 Index Returns



Strong performance in the US helped developed markets lead equity returns during the quarter. Emerging markets lagged developed markets as commodities continued to struggle. The poor performance of REITs in the US, Australia, and Japan contributed to the negative performance delivered by global REITs.



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US Stocks

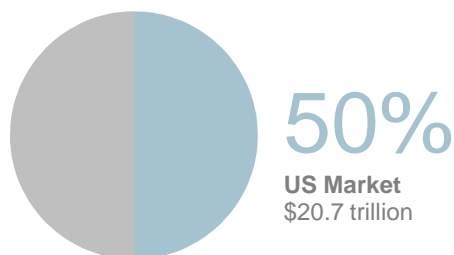
Fourth Quarter 2013 Index Returns



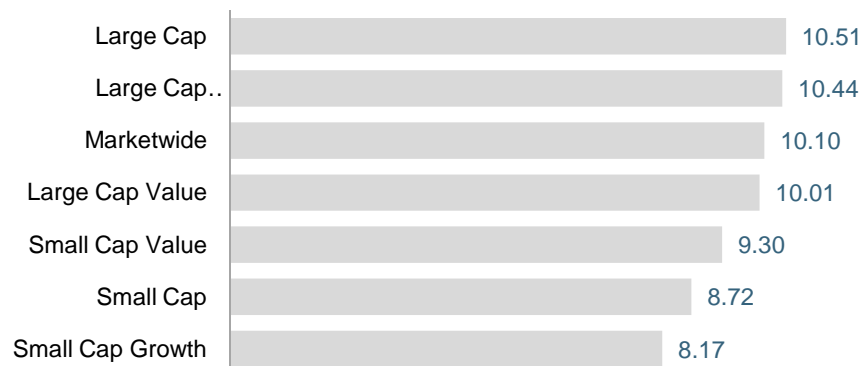
The US equity market delivered a strong performance across style and size indices during the quarter. Large cap growth recorded the strongest performance.

Growth outperformed value market-wide, driven by the strong performance of large cap growth stocks. The effect was reversed in small caps. Across the size dimension, large caps outperformed small caps.

World Market Capitalization—US



Ranked Returns for the Quarter (%)



Period Returns (%)

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Marketwide	33.55	33.55	16.24	18.71	7.88
Large Cap	32.39	32.39	16.18	17.94	7.41
Large Cap Value	32.53	32.53	16.06	16.67	7.58
Large Cap Growth	33.48	33.48	16.45	20.39	7.83
Small Cap	38.82	38.82	15.67	20.08	9.07
Small Cap Value	34.52	34.52	14.49	17.64	8.61
Small Cap Growth	43.30	43.30	16.82	22.58	9.41

* Annualized

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International Developed Stocks

Fourth Quarter 2013 Index Returns



During the quarter, international developed markets continued to post gains. Large cap and small cap stocks posted similar performances in US dollar terms.

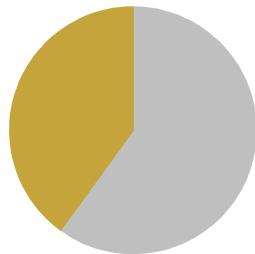
Value outperformed growth across all size segments.

The US dollar appreciated relative to most major foreign developed currencies.

World Market Capitalization—International Developed

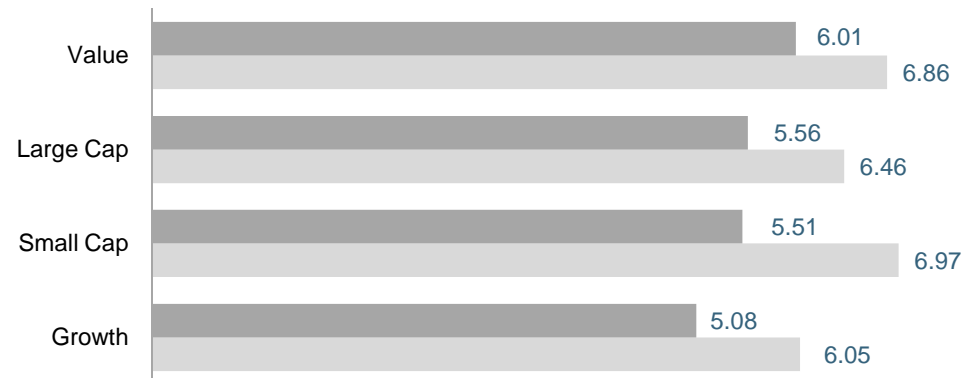
40%

International
Developed
Market
\$16.6 trillion



Ranked Returns for the Quarter (%)

■ US Currency ■ Local Currency



Period Returns (%)

* Annualized

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Large Cap	21.02	21.02	7.34	12.49	7.07
Small Cap	25.55	25.55	7.49	18.45	9.24
Value	21.47	21.47	7.96	12.52	7.08
Growth	20.53	20.53	6.71	12.41	6.99

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Emerging Markets Stocks

Fourth Quarter 2013 Index Returns



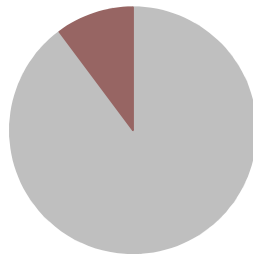
Dragged down by the poor performance of materials and energy stocks, emerging markets lagged developed markets as a group but still finished with gains. Growth stocks outperformed value across large caps and mid-caps but underperformed in small caps. Large caps slightly outperformed small caps.

The US dollar appreciated against most emerging markets currencies.

World Market Capitalization—Emerging Markets

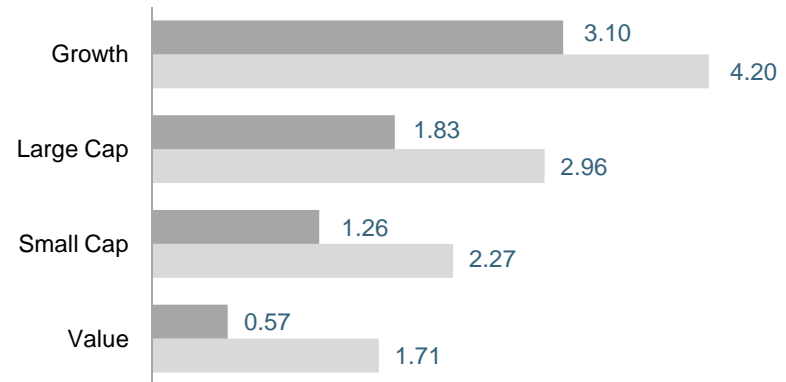
10%

Emerging Markets
\$4.3 trillion



Ranked Returns for the Quarter (%)

■ US Currency ■ Local Currency



Period Returns (%)

* Annualized

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
Large Cap	-2.60	-2.60	-2.06	14.79	11.17
Small Cap	1.04	1.04	-3.48	19.58	11.97
Value	-5.11	-5.11	-3.34	13.88	12.00
Growth	-0.18	-0.18	-0.84	15.67	10.31

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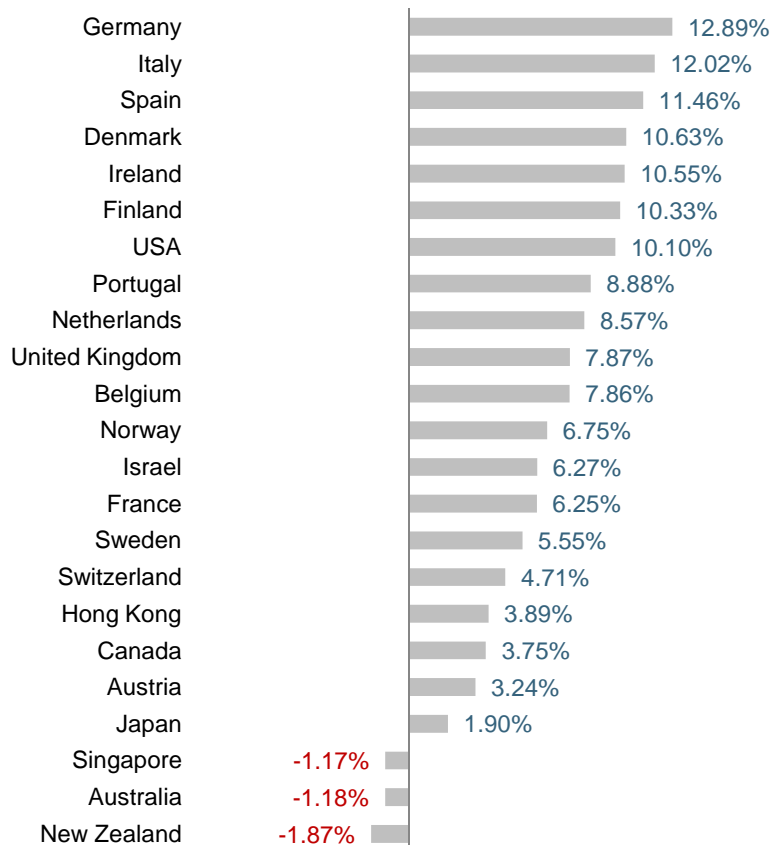
Select Country Performance

Fourth Quarter 2013 Index Returns

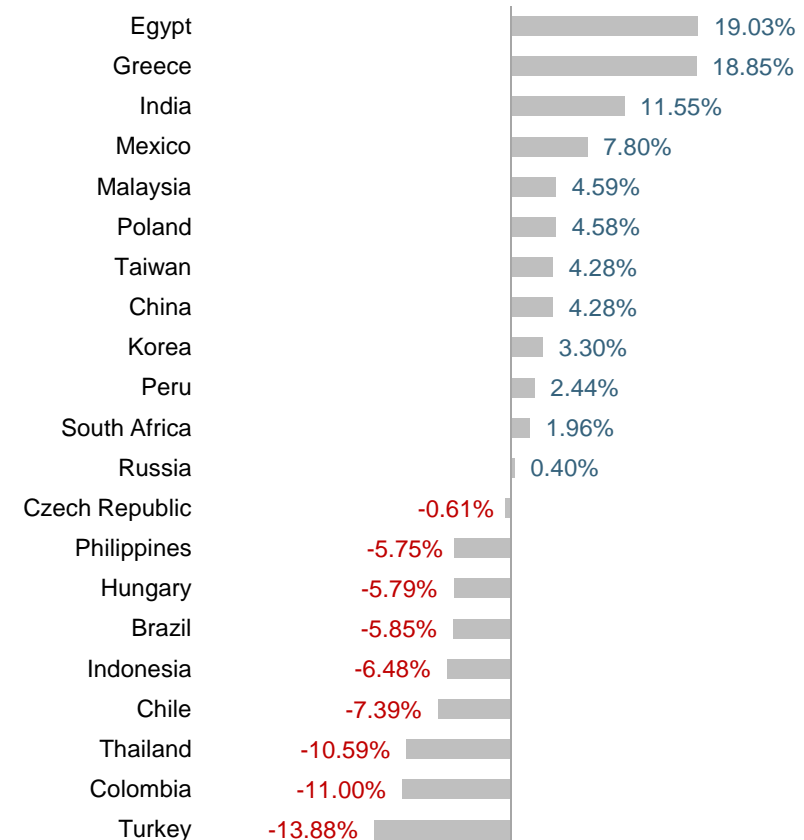


Many European equity markets, led by Germany, recorded strong performances in US dollar terms. Most developed markets posted gains; however, emerging markets countries were mixed. Greece, recently reclassified by MSCI as an emerging market, and Egypt were the top performers. Turkey was the worst-performing market following news of a graft probe.

Developed Markets (% Returns)



Emerging Markets (% Returns)



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Country performance based on respective indices in the MSCI World ex US IMI Index (for developed markets), Russell 3000 Index (for US), and MSCI Emerging Markets IMI Index. All returns in USD and net of withholding tax on dividends. MSCI data © MSCI 2014, all rights reserved. Russell data © Russell Investment Group 1995–2014, all rights reserved. Greece has recently been reclassified as an emerging markets country by MSCI, effective November 2013.

Real Estate Investment Trusts (REITs)

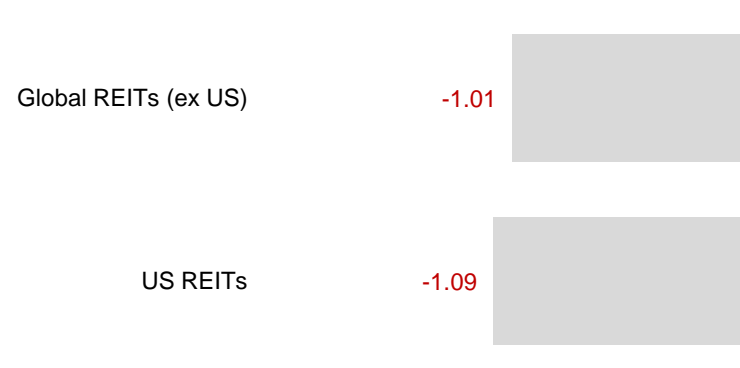
Fourth Quarter 2013 Index Returns



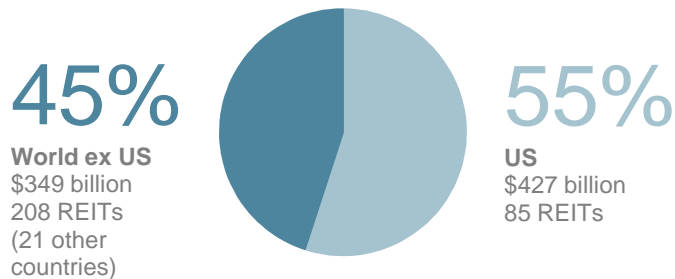
The poor performance of REITs in the US, Australia, and Japan contributed to the losses delivered by global REITs during the quarter.

This was the third consecutive quarter of negative performance for US REITs.

Ranked Returns for the Quarter (%)



Total Value of REIT Stocks



Period Returns (%)

Asset Class	YTD	1 Year	* Annualized		
			3 Years*	5 Years*	10 Years*
US REITs	1.22	1.22	9.04	16.36	8.22
Global REITs (ex US)	2.36	2.36	7.26	14.79	6.62

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Number of REIT stocks and total value based on the two indices. All index returns are net of withholding tax on dividends. Dow Jones US Select REIT Index data provided by Dow Jones © 2014. S&P Global ex US REIT Index data provided by Standard and Poor's © 2014.

Commodities

Fourth Quarter 2013 Index Returns



Commodities ended the year on a negative note as the DJ-UBS Commodity Index returned -1.1% during the fourth quarter, finishing the year down 9.5%.

With the improvement in the economy pushing up interest rates, precious metals were hit hard, finishing down 9–11%.

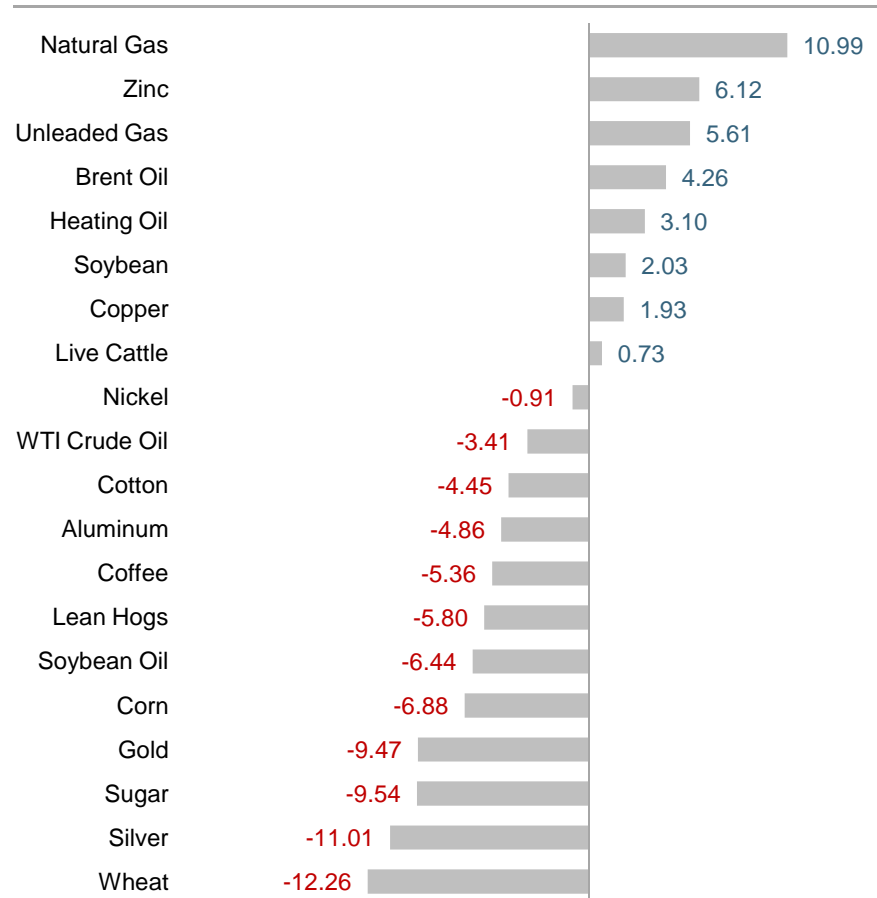
Soft commodities, with the exception of soybeans, finished down 4–12%. The energy complex, with the exception of WTI crude oil, had a good quarter, with natural gas leading the way, finishing up approximately 11%.

Period Returns (%)

* Annualized

Asset Class	YTD	Q4	1 Year	3 Years*	5 Years*	10 Years*
Commodities	-9.52	-1.05	-9.52	-8.11	1.51	0.87

Individual Commodity (% Returns)



Fixed Income

Fourth Quarter 2013 Index Returns

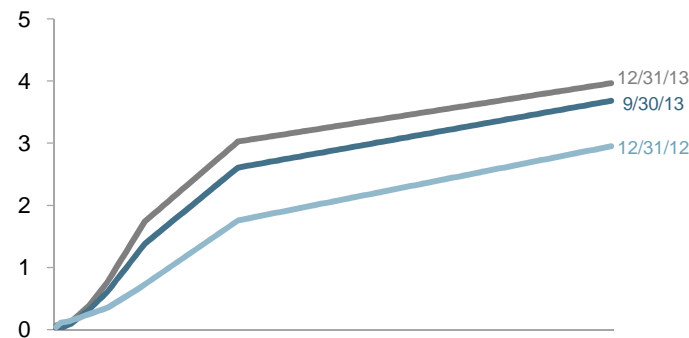


Bond investors got a bit of bad news at the end of the quarter with the US Federal Reserve announcing the tapering of its monthly bond purchases from \$85 billion (current level) to \$75 billion beginning in January 2014. This move was not a surprise to the market. The Fed signaled earlier in the year that, with continuing improvement in the economy, it would begin to taper the bond purchase program. However, the initial reduction in purchases was much less than expected. During the quarter, the market reacted to the impending news by taking bond yields from 2.61% on the bellwether 10-year at the end of September to a close of 3.03% at year end.

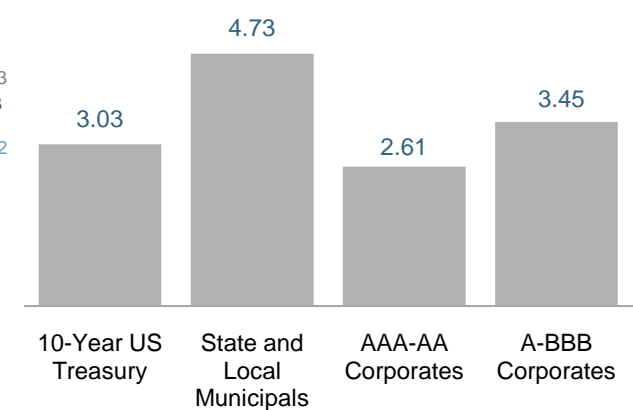
The continuing improvement in the economy also spilled over into the TIPS market. Real rates across most of the maturity spectrum rose quarter over quarter.

Yield-seeking investors were rewarded as credit spreads narrowed.

US Treasury Yield Curve



Bond Yields across Different Issuers



Period Returns (%)

Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
BofA Merrill Lynch Three-Month US Treasury Bill Index	0.07	0.07	0.10	0.12	1.68
BofA Merrill Lynch 1-Year US Treasury Note Index	0.25	0.25	0.35	0.54	2.07
Citigroup WGBI 1-5 Years (hedged to USD)	0.62	0.62	1.67	1.86	3.19
Long-Term Government Bonds	-11.36	-11.36	5.50	1.94	6.06
Barclays US Aggregate Bond Index	-2.02	-2.02	3.26	4.44	4.55
Barclays US Corporate High Yield Index	7.44	7.44	9.32	18.93	8.62
Barclays Municipal Bond Index	-2.55	-2.55	4.83	5.89	4.29
Barclays US TIPS Index	-8.61	-8.61	3.55	5.63	4.86

* Annualized

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Global Diversification

Fourth Quarter 2013 Index Returns



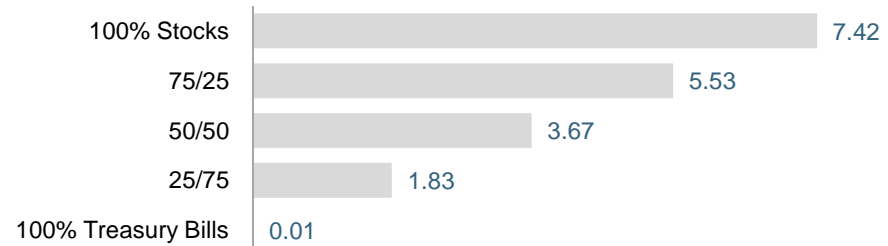
These portfolios illustrate the performance of different global stock/bond mixes and highlight the benefits of diversification. Mixes with larger allocations to stocks are considered riskier but have higher expected returns over time.

Period Returns (%)

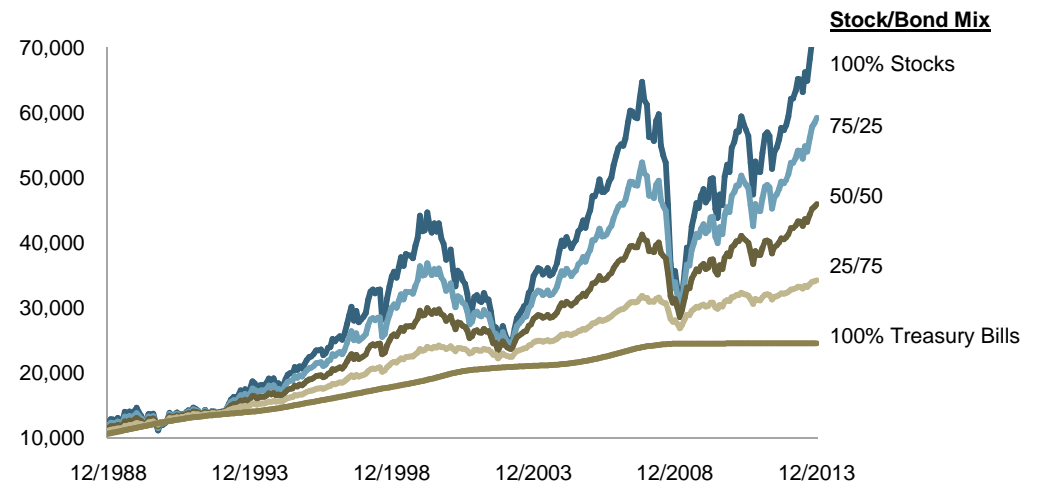
Asset Class	YTD	1 Year	3 Years*	5 Years*	10 Years*
100% Stocks	23.44	23.44	10.33	15.53	7.72
75/25	17.24	17.24	7.87	11.79	6.43
50/50	11.27	11.27	5.33	7.95	4.96
25/75	5.54	5.54	2.71	4.04	3.33
100% Treasury Bills	0.02	0.02	0.04	0.07	1.54

* Annualized

Ranked Returns for the Quarter (%)



Growth of Wealth: The Relationship between Risk and Return



Diversification does not eliminate the risk of market loss. Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect expenses associated with the management of an actual portfolio. Asset allocations and the hypothetical index portfolio returns are for illustrative purposes only and do not represent actual performance. Global Stocks represented by MSCI All Country World Index (gross div.) and Treasury Bills represented by US One-Month Treasury Bills. Globally diversified allocations rebalanced monthly, no withdrawals. Data © MSCI 2014, all rights reserved. Treasury bills © Stocks, Bonds, Bills, and Inflation Yearbook™, Ibbotson Associates, Chicago (annually updated work by Roger G. Ibbotson and Rex A. Sinquefeld).

Many Happy Returns

Fourth Quarter 2013



It's that time of the year when the talking heads of television and the prognosticators of print issue their sage outlooks for the coming 12 months. While this crystal ball gazing is always entertaining, it becomes even more so a year later.

In journalism, this is known as the "silly season." Lots of people are on vacations, and the flow of news slows to a crawl. So the wide open spaces are filled with forecasts about the economy, markets, and anything else you can think of.

Think back a year ago, when politicians in Washington were in the grip of one of their now familiar "fiscal cliff" standoffs. As has become the custom, the theater of brinkmanship kept everyone guessing until a last-minute resolution.

For some, the excitement was just too much. The publication *Financial News* told its readers that "political storm clouds loom over the global economy. From Washington to Beijing, the financial markets are in thrall to seismic political events."¹

In *The Economist* magazine, the tone about 2013's prospects was equally skeptical, if not quite as florid. The magazine noted that while surveys showed investors were optimistic, the coming year was unlikely to be a one to remember.

The reason was that the past year's gains partly reflected relief that the worst fears about the euro zone

had failed to materialize, the magazine said, which meant that reality might intervene as investors judged shares as expensive.

"Although investors are not as complacent as they were heading into 2000 or 2007, say, it is still hard to believe this will be a bumper year for returns," the columnist Buttonwood said in his column.²

It's easier to see from all this forecasting that many investors might have taken fright at the developments around the turn of the year and sought to trim their exposures to risky assets because of what the media pundits were saying.

That would have been a shame because, as of early December 2013, many global equity markets were notching record-breaking years. In local currency terms, the S&P 500 total return index, for instance, was up by just under 29% at time of writing, on track for its biggest annual gain in more than a decade.

In Japan, the Nikkei 225 total return index was 53% higher as of early December, heading for its best yearly gain since 1972. In the UK, the FTSE 100 total return index reached a 13-year peak in May this year. It has come off a little since then, but was still nearly 15% higher for the year by December.

As the year came to an end again, there were still plenty of gloomy stories to fill the newspapers—including ongoing speculation of what happens when the US Federal Reserve begins tapering its monetary stimulus program.

This isn't to say these stories are necessarily incorrect. Most of them accurately reflect the sentiment prevailing at the time they were written and the uncertainty about the future, as expressed in prices.

But as an individual investor, there is not much you can do about that. These expectations and uncertainties are already built into the market. Investing is about what happens next. We don't know what happens next. That's why we diversify.

And think about this: If any of the gurus who regularly appear on financial television or in the newspaper really had a crystal-clear view of the future, why would they bother sharing it with the world?

It makes more sense to focus on what's in your own control.

In the meantime, many happy returns!

1. *Financial News*, January 7, 2013

2. "Hope Springs Eternal," *The Economist*, January 5, 2013.