Abel Financial Strategies
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Annual Market Review 2014

S&P 500 Total Return 2014: 13.7%

Overview

The United States emerged from 2014 as the best house on a troubled block. Civil war in Ukraine, a slowing Chinese economy, a stagnant Europe worried about potential deflation, a new recession in Japan, the threat of a new Russian economic meltdown triggered by plummeting oil prices--it all made an improving situation at home look even brighter by comparison.

Even apart from the troubles overseas, the United States by almost any measure was stronger than it's been in years. The labor and housing markets improved, corporate profits were solid, Congress managed to avert another government shutdown, and the Ebola threat had little impact domestically. All in all, it was a Goldilocks economy: not too hot, which could have brought on higher interest rates from the Federal Reserve, and not too cold, which let the Fed end the QE3 bond purchases begun in the wake of the 2008 financial crisis.

That domestic strength fueled more gains for domestic equities than had been envisioned for the fifth year of this bull market. The S&P 500 ended 2014 up more than 200% from its March 2009 low, and the Dow saw its sixth straight yearly gain. However, in the coming year, investors will almost certainly be faced with the start of long anticipated interest rate increases. Though the Fed has promised patience in implementing rate hikes, higher borrowing costs and a strong dollar that makes U.S. goods more expensive overseas could create a headwind for domestic corporations. The question is whether that wind might blow the economy off its current promising course or will merely keep the game interesting.

Market/Index	2013 Close	As of 9/30	As of 12/31	Month Change	Q4 Change	2014 Change
DJIA	16576.66	17042.90	17823.07	-.03%	4.58%	7.52%
Nasdaq	4176.59	4493.39	4736.05	-1.16%	5.40%	13.40%
S&P 500	1848.36	1972.29	2058.90	-.42%	4.39%	11.39%
Russell 2000	1163.64	1101.68	1204.70	2.68%	9.35%	3.53%
Global Dow	2484.10	2534.47	2501.66	-2.71%	-1.29%	.71%
Fed. Funds	.25%	.25%	.25%	0 bps	0 bps	0 bps
10-year Treasuries	3.04%	2.52%	2.17%	-1 bps	-35 bps	-87 bps

Chart reflects price changes, not total return. Because it does not include dividends or splits, it should not be used to benchmark performance of specific investments.

Snapshot 2014

The Markets

- **Equities:** After a discouraging start, large-cap domestic equities spent much of the year climbing to new heights. Though they didn't come close to matching last year's fireworks, the S&P 500 and Dow industrials set 53 and 38 new record highs respectively during the year. However, little of that love spilled over to the small caps. The Russell 2000, which had soared in 2013, had trouble scaling the

proverbial "wall of worry" and spent much of 2014 either flat or down before a Q4 rally returned it to positive territory. The Nasdaq proved the strongest of the four indices; by December it had come within 242 points of its all-time closing high of 5,048.62, set in March 2000. Beset by weakness worldwide, the Global Dow barely managed a positive return for the year.

- **Bonds:** The bond market confounded those who had feared bond prices would suffer from the unwinding of Federal Reserve support. Challenges overseas lured investors to the safety of U.S. Treasuries; prices rose as the benchmark 10-year yield dropped more than 3/4ths of a percentage point, especially after the threat of an imminent Fed rate hike faded and falling oil prices threatened the economies and currencies of several oil-dependent countries.
- **Oil:** A drop in crude prices that began in July accelerated in Q4 after Saudi Arabia chose market share over profit by deciding not to cut supplies. Prices promptly plummeted to levels not seen since the depths of the financial crisis, falling roughly 45% from the July high of $107 a barrel. The plunge in oil prices helped fatten consumers' wallets but renewed concerns about oil-dependent economies.
- **Currencies:** Falling oil prices coupled with the expectation of higher interest rates helped boost the U.S. dollar, which rose almost 11% over the course of the year. The dollar also benefitted from interest rates abroad, some of which were even lower than those for Treasuries. The strong dollar raised new concerns that countries and foreign corporations hurt by lower oil prices might have trouble repaying debt in currencies that were substantially weaker against the U.S. dollar.
- **Gold:** After plummeting in 2013, gold managed to stabilize a bit last year. The precious metal ended the year at roughly $1,180--not far from where it began in January despite a spring rally prompted in part by the crisis in Ukraine.

The Economy

- **Unemployment:** Improvement in the U.S. job market was slow but steady. The unemployment rate ended the year at 5.8%, its lowest level since July 2008 and better than last December's 6.7%. According to the Bureau of Labor Statistics, the unemployment rate is now down 4.2 percentage points from its October 2009 high of 10%. And after a slow start, job creation accelerated; by December, the number of new jobs added during the previous 12 months was the highest it's been since April 2006.
- **GDP:** After a slump during the first quarter, when the U.S. economy contracted by 2.1%, by Q3 the U.S. economy was growing at its fastest pace in 11 years. The Bureau of Economic Analysis said the 5% annualized growth of gross domestic product outpaced Q2's 4.6% and represented the strongest growth since Q3 2003's 6.9%. After-tax corporate profits also were up, rising 2.8% from Q2 and more than 5% from a year earlier.
- **Inflation:** Inflation remained well under historical averages, which allowed the Fed to postpone any interest rate hike until 2015. By December, the Bureau of Labor Statistics said consumer inflation for the previous 12 months stood at 1.3% while wholesale prices gained 1.4% over the same time. The lower gas prices that kept inflation in check also helped spur retail sales and consumer spending.
- **Housing:** The most recent home prices measured by the S&P/Case-Shiller 20-City Composite Index were up 4.5% from a year earlier, and the National Association of Realtors® said that by November, new home sales were slowing but still up 2.1% year over year. However, both year-over-year figures were lower than in previous months, and slippage in both housing starts and building permits suggested that the pace of gains may be slowing.
- **Manufacturing:** Manufacturing was a fundamental component of the economy's strength during the year. The Federal Reserve said that by the end of the year, usage of the nation's industrial capacity had finally reached its long-term average. Meanwhile, higher exports helped shrink the U.S. trade deficit to $43.4 billion.
- **International markets:** Economic problems overseas contributed to the Fed's caution with interest rates. Though the European Central Bank cut a key interest rate to -0.1% and continued to say it was prepared to take stronger measures to try to avoid potential deflation, Europe entered the new year still waiting for additional stimulus. In Japan, two consecutive quarters of contraction marked an official recession, calling so-called "Abenomics" into question. Meanwhile, faced with growth that had slowed to 7.3% by Q3, China's central bank cut two key interest rates to try to stimulate domestic consumption; it also agreed to work with the United States to cut greenhouse gases. Finally, President Obama took steps to reestablish diplomatic relations with Cuba, though ending the trade embargo would require congressional action.

Data sources: Economic: Based on data from U.S. Bureau of Labor Statistics (unemployment, inflation); U.S. Department of Commerce (GDP, corporate profits, retail sales, housing); S&P/Case-Shiller 20-City Composite Index (home prices); Institute for Supply Management (manufacturing/services). Performance: Based on data reported in WSJ Market Data Center (indexes) and Barron's (S&P 2014 total return); U.S. Treasury (Treasury yields); U.S. Energy Information Administration/Bloomberg.com Market Data (oil spot

price, WTI Cushing, OK); www.goldprices.org (spot gold/silver); Oanda/FX Street (currency exchange rates). All information is based on sources deemed reliable, but no warranty or guarantee is made as to its accuracy or completeness. News items are based on reports from multiple commonly available international news sources (i.e. wire services) and are independently verified when necessary with secondary sources such as government agencies, corporate press releases, or trade organizations. Neither the information nor any opinion expressed herein constitutes a solicitation for the purchase or sale of any securities, and should not be relied on as financial advice. Past performance is no guarantee of future results. All investing involves risk, including the potential loss of principal, and there can be no guarantee that any investing strategy will be successful.

The Dow Jones Industrial Average (DJIA) is a price-weighted index composed of 30 widely traded blue-chip U.S. common stocks. The S&P 500 is a market-cap weighted index composed of the common stocks of 500 leading companies in leading industries of the U.S. economy. The NASDAQ Composite Index is a market-value weighted index of all common stocks listed on the NASDAQ stock exchange. The Russell 2000 is a market-cap weighted index composed of 2000 U.S. small-cap common stocks. The Global Dow is an equally weighted index of 150 widely traded blue-chip common stocks worldwide. The U.S. Dollar Index is a geometrically weighted index of the value of the U.S. dollar relative to six foreign currencies. Market indices listed are unmanaged and are not available for direct investment.

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