HORAN CAPITAL ADVISORS

Investor *Letter*

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The pessimist complains about the wind; the optimist expects it to change; the realist adjusts the sails.

- William Arthur Ward

Sailing Into The Wind

The sailing analogy noted in our opening quote seems appropriate as we write about the third quarter and provide perspective on the balance of 2014. A sailing fact: in order to make progress into the wind, one must tack back and forth into the face of the wind. This headwind of sorts enables a sailboat to make progress "up wind." As in sailing, a certainty for investors is there will most likely always be headwinds that one must navigate. Index investing is similar to sailing downwind in that the investor is simply along for the ride and may end up at a destination that was not expected. The third quarter presented a number of headwinds for investors to navigate.

Benchmark Returns	September 2014	Third Quarter 2014	Calendar Year 2014
Equities			
S&P 500 Index	-1.40%	1.13%	8.34%
S&P 600 Index (small-cap)	-5.37%	-6.73%	-3.72%
MSCI EAFE Index (Developed International)	-3.84%	-5.88%	-1.38%
MSCI EEM Index (Emerging Markets)	-7.41%	-3.50%	2.43%
Commodities			
Dow Jones UBS Commodity Index	-6.23%	-11.83%	-5.59%
Real Estate			
Cohen & Steers Real Estate Index	-5.92%	-2.55%	16.08%
Bonds			
Barclays Capital U.S. Aggregate Index	-0.68%	0.17%	4.10%
S&P U.S. Issued High Yield Corp Bond	-2.05%	-1.91%	3.53%
*Data provided by Blackrock			

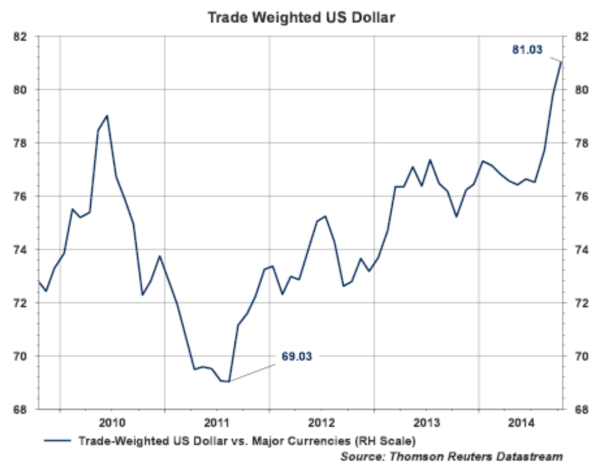
The consensus view at the start of 2014 was interest rates would rise and economic growth would be globally synchronized led by the U.S. Now three quarters of the way through 2014, it is looking like economic growth in the U.S. is the only consensus viewpoint being realized. U.S. economic growth has been volatile as exhibited by Q1 GDP (-2.9%) and Q2 GDP (+4.6%); however, this growth appears better than many developed economies around the world. The 10-year treasury rate at the beginning of 2014 was 3.03%. The 10-year treasury ended the third quarter at 2.3% and just recently hit a low of 1.87% on October 15th. The October 15th rate plunge occurred on a day when the Dow Jones Industrial Average swung 458 points, nearly 3% from high to low. What headwinds served as catalysts for October market volatility? There may be no one specific reason, but the list would certainly include the geopolitical tension in the Ukraine and China, the terrorist threat of ISIS and the Ebola health crisis. While these issues are real and we do not want to discount their ability to escalate, these events are more likely short-term in nature. Generally, it is not profitable to make long term investment decisions based on headline grabbing circumstances. Other factors gaining our attention with potential for a broader, long-term market impact include: weak economic data in Europe, the European Central Bank's lack of specific and forceful monetary stimulus, the rising strength of the U.S. dollar and the end of QE3 in the U.S. We see opportunities in the wake of this recent volatility.

The Third Quarter (and Beyond)

Although we are less than a month past the end of the third quarter, September 30th seems a distant memory. The third quarter ended on a weak note for most asset classes. The previously noted headwinds resulted in equity market performance in the third quarter being the weakest since the third quarter of 2011. The beginning of the fourth quarter has continued to be volatile even with corporate earnings releases progressing better than expected.

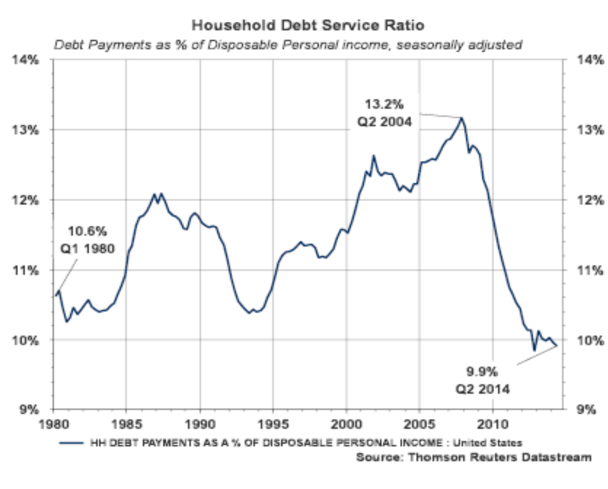
As one reviews the performance of selected market indices on the previous page, September and the third quarter were certainly challenging time periods. The larger capitalization U.S. stocks were the standouts in the quarter. The S&P 500 Index was up 1.13% in Q3 and up 8.34% in the first nine months of the year. Small cap and foreign stocks generated negative returns. The speed with which European economic data weakened in September surprised many and this negatively impacted global equity markets. Also contributing to the volatility in European equity markets is the lack of a clear plan from the European Central Bank (ECB) that deals with the slowing economic environment in Europe. A quantitative easing program in the Eurozone, similar to the one that is ending in the U.S., would likely be a positive for European equities.

Implications of a Strong U.S. Dollar



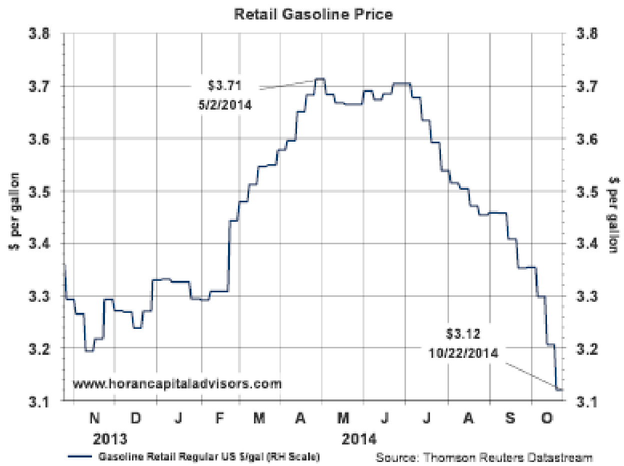
As can be seen in the chart at right, since August of 2011 the trade weighted U.S. Dollar has strengthened over 17%. The strength of the Dollar has accelerated in the last several months which is a signal of a potentially strengthening U.S. economy. A strengthening U.S. economy is one reason the Federal Reserve has stated it will end the current quantitative easing (QE) program in October. Along with the end of QE, it is anticipated the Fed will begin the process of normalizing interest rates towards a neutral 3-4% target range beginning sometime in 2015. Higher interest rates in the U.S. would create an environment where the dollar might strengthen further. Interest rates in the U.S. are currently higher than in many countries around the world; thus attracting foreign investment into U.S. Dollar denominated assets.

In the short-term, the stronger dollar will pressure multinational earnings growth. A rising dollar reduces the foreign portion of a U.S. domiciled company's earnings when converting back to U.S. dollars from the foreign currency in which they were earned. If U.S. corporations wish to earn the same amount in this environment, they must raise prices in foreign currency terms. This would make their products and services less competitive.



The Consumer Driven Economy

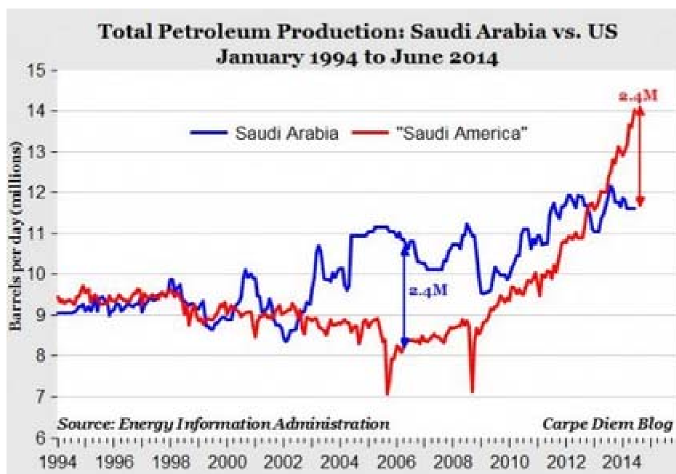
Consumers account for nearly 70% of U.S. GDP. Since the end of the financial crisis in 2008, the consumer has taken steps to improve their own



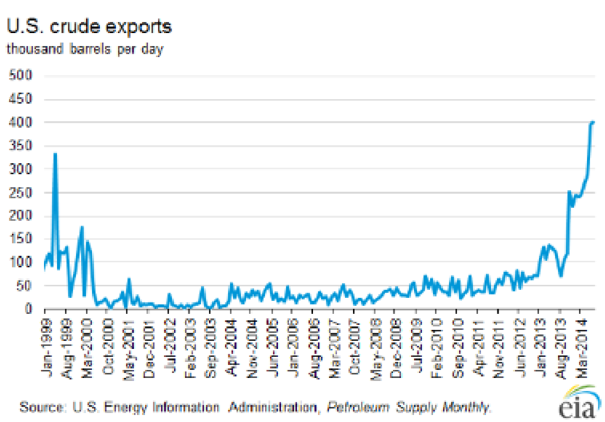
financial condition: household debt service ratios (debt payments as a percentage of disposable personal income) are the lowest they have been since pre-1980, unemployment continues to decline, credit is accessible and loan growth is building in real estate and commercial/industrial loans. It is our belief we are in the middle of a potentially long post-recession recovery. The slow but steady nature of the recovery is helping to prolong it.

A strong dollar provides downward pressure on commodity prices as most commodities are transacted in U.S. Dollars. This downward pressure on prices, particularly for energy and foreign made products, benefits the U.S. consumer. For example, according to the U.S. Department of Energy, every one cent drop in the price of a gallon of gasoline saves consumers $3.65 million per day or $1.33 billion over a year. Since May 2nd the retail price of a gallon of gasoline has declined by 59 cents. This equates to an annual savings of $78.5 billion for consumers. This savings acts like a tax cut and may lead to an increase in discretionary spending.

U.S. Energy Revolution

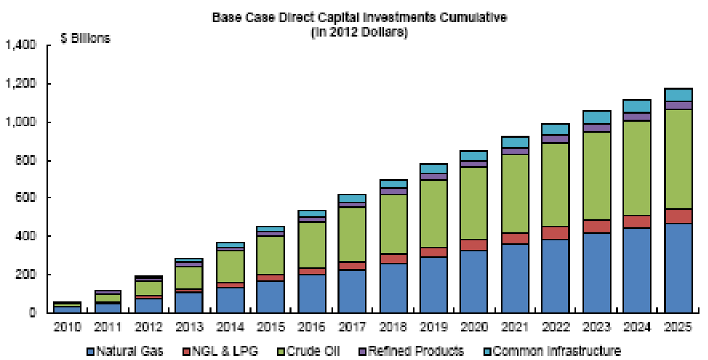


As noted above, a strong tailwind benefiting consumers is the recent decline in oil prices which translates to lower prices at the gasoline pump. The energy revolution in the U.S. has resulted in a dramatic shift both politically and economically. Whereas the U.S. was at the mercy of a once dominant OPEC, that controlled supply and prices, we now produce more petroleum equivalent than Saudi Arabia. The increased supply in the U.S. has overwhelmed U.S. demand needs and refining capabilities. As a result, the U.S. government has reduced export restrictions for U.S. oil. Last month oil was exported to South Korea from Alaska for the first time since 2004. As noted in a recent *New York Times* article, “Oil exports (including condensates) remain small, but they have already surged from 67,000 barrels a day in 2012 to 120,000 barrels a day in 2013 to more than double that currently. Citi Research estimates that under the new condensates ruling, exports could hit a million barrels a day by next year.”



The increase in oil production is contributing to growth in other areas of the economy as well. Much of the pipeline and energy infrastructure in the U.S. is owned or managed in corporate structures know as master limited partnerships (MLPs). As our clients know, we have allocated a portion of our alternative investments in an index type investment consisting of a basket of MLPs. Given the anticipated growth in energy infrastructure in the U.S., we continue to believe MLPs can provide our clients with diversified exposure to this area of the energy complex. In a report written by IHS Global Inc. and provided by the American Petroleum Institute it is noted, “The IHS forecast of oil and gas infrastructure investment over the next 12 years (2014 – 2025) estimates a cumulative spending of $890 billion (in 2012 Dollars)…”

Oil & Natural Gas Transportation & Storage Infrastructure: Status, Trends, & Economic Benefits



Source: API and IHS Global Inc.

Process, Positioning & Volatility

Increased market volatility increases investor anxiety. This type of sentiment change is a normal reaction and should lead all investors to evaluate their comfort level with their overall asset allocation. Nonetheless, we rely on our process and continuously evaluate portfolio risk. James Montier of GMO said it nicely when he commented, “People often judge a past decision by its ultimate outcome rather than basing it on the quality of the decision at the time it was made, given what was known at that time. This is outcome bias. We must concentrate on process. Process is a set of rules that govern how we go about investing. When every decision is measured on outcomes, investors are likely to avoid uncertainty, chase noise, and herd with the consensus. Sounds like a pretty good description of the investment industry to me.”

Our disciplined process leads us to continue to avoid small company stocks for our clients, although the recent significant underperformance has us watching this asset class closely. Other portfolio changes we have implemented in an effort to reduce the risk of client investments: recently exited high yield bonds, which had generated better than 10% annualized returns over the past four years, added a real estate fixed income fund during the quarter focused primarily on real estate debt and real estate investment trusts, on the margin we have transitioned several individual equity positions to be more U.S. earnings centric and taken advantage of the underperformance of a few cyclical stocks. Lastly, we recently took a step to incrementally reduce the long underweight exposure to emerging markets. Our thoughts on our recent changes might best be summed up in this Howard Marks (Oaktree Capital Management) comment: “In order to achieve superior results, an investor must be able – with some regularity – to find asymmetries: instances when the upside potential exceeds the downside risk. That's what successful investing is all about.”

We thank our clients and corporate partners for their continued confidence and support. We hope everyone is looking forward to the holidays and a strong market finish in 2014.

Please visit us at www.horancapitaladvisors.com.

Warm regards,

HORAN Capital Advisors

* HORAN Capital Advisors, LLC is an SEC Registered Investment Advisor.

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