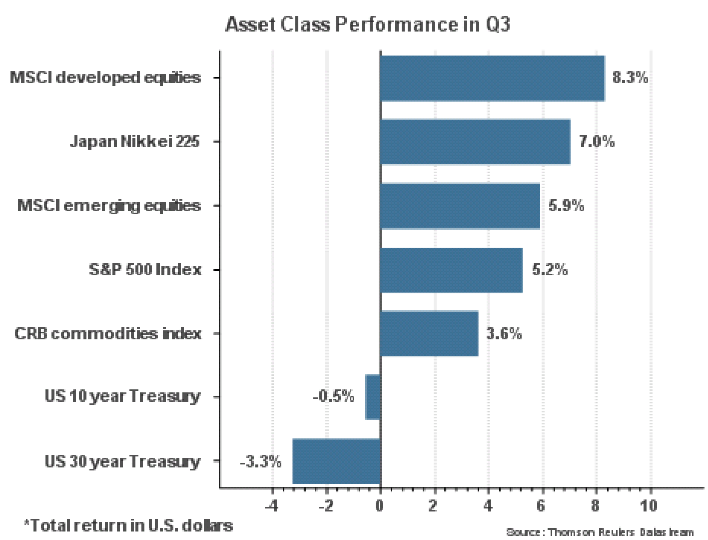
"We are nicely above the old high, and we're just getting to a point where the economy is getting back on line. There's another leg to come in this bull market."
- John Stoltzfus, chief market strategist at Oppenheimer & Co.

The Quarter

The third quarter of 2013 delivered another period of positive equity returns. The S&P 500 Index was up 5.2% for the quarter. In fact, most asset classes were positive excluding U.S. Real Estate Investment Trusts and long-term bonds. Eight of the ten economic sectors in the S&P 500 posted positive returns while top-performing sectors included materials, industrials and consumer discretionary. Our second quarter decision to decrease consumer staple exposure and add to more cyclically sensitive stocks such as Fluor (FLR) and Schlumberger (SLB) proved rewarding with each returning more than 20% during the quarter.



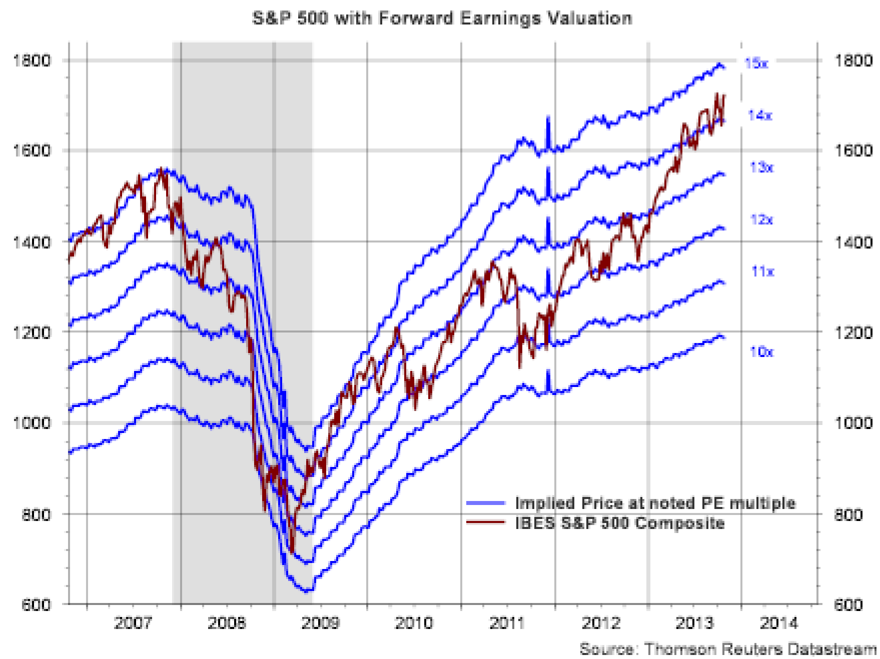
As noted in the accompanying chart at right, international developed equities and emerging equities had a strong quarter reflecting improved economic reports in both developed and developing market economies. We have increased exposure to these markets and plan to add to these investments over a reasonable timeframe. European multinationals generally sell at discounted valuations and could be revalued higher as positive sentiment builds. Additionally, from a defensive perspective, companies with discounted valuations tend to hold up better in corrective markets. The element of higher dividend yields in European equities adds some downside protection as well.

Recovery

For some, the financial crisis of 2008-2009 might seem long ago. On March 6, 2009, the S&P 500 Index closed at 683. Four and a half years later the S&P has increased a total of 1071 points or a total of 156%. In July of 2009, we wrote an article which appeared on our blog, regarding markets climbing the proverbial "wall of worry." This recent market advance may be one of the longer "wall of worry" climbs in history. A quote by one equity trader may sum up investor sentiment when he noted, "The market has only three things it can do: annoy buyers, torment sellers, or frustrate everyone. Currently, the market is testing sellers and those who have not bought in yet."

Multiple Expansion

Stock prices can increase by a phenomenon called multiple expansion, especially during a low inflation, slow growth economic environment. This is where the price earnings ratio (P/E) for a stock, a widely used calculation for valuing companies, increases due to the share price increasing faster than a company's earnings. This tends to occur because the market is placing a higher value on future earnings due to the fact these earnings, in part, are not diminished by a higher rate of inflation. Ed Yardeni, PhD of Yardeni Research recently demonstrated this influence with a similar version of the valuation chart at right. Analysts' earnings estimates for 2014 look positive, but an important variable asks whether or not corporate earnings can continue to increase. Importantly, analysts tend to be overly bullish at market tops and overly bearish at market bottoms.



One significant factor pushing equity prices higher is the Federal Reserve's multiple liquidity programs, i.e., quantitative easing. This past quarter, Ben Bernanke announced his retirement and his replacement, Janet Yellen, who will likely continue to keep the Fed liquidity spigot on. We are paying close attention to valuations in both equity and fixed income. When the Fed's liquidity programs slow, i.e., taper, a rough patch in equity and bonds could follow.

Investment Overview

Some recent investment decisions, beyond the previously noted additions to international investments, focus on specific individual equity positions. These positions, in particular, are names that benefit from the U.S. energy renaissance; companies involved in the exploration and development of oil and gas and those companies that benefit from lower energy costs. Chemical companies are a good example of this. We believe Dow Chemical (DOW), a recent addition, is a company that will benefit in this regard with access to cheap natural gas while also displaying other favorable business prospects. The company is relocating overseas production to the U.S.

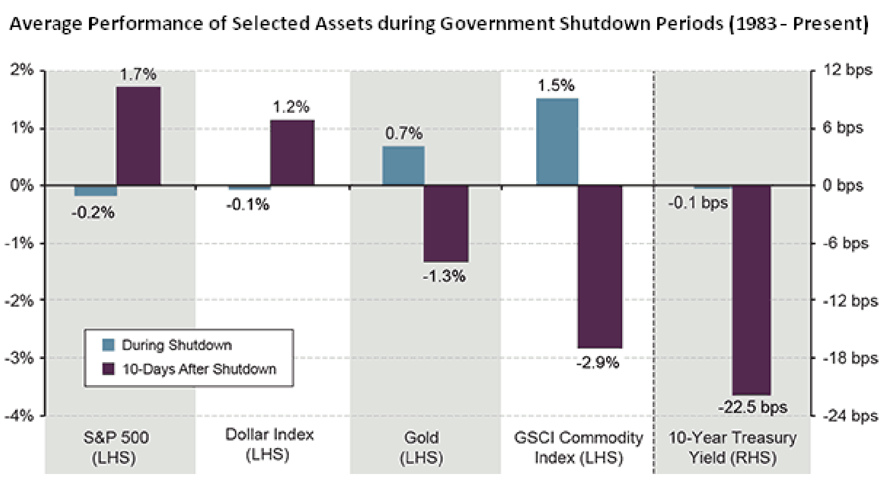
Also, we recently initiated a position in Clean Harbors (CLH). CLH provides environmental and hazardous waste management services primarily within the U.S. The company recently acquired Safety-Kleen which is a company that collects waste oil from industrial firms. The waste oil provides a low cost input for CLH's refining business. Clean Harbors' business is expanding into treatment and remediation of oils/water used in oil shale/fracking businesses. We believe Dow and Clean Harbors have beneficial tailwinds as industrial companies expand in the U.S. This expansion is being driven by rising wages overseas and lower energy input costs in the U.S.

We have maintained our biases in fixed income with a continued focus on shorter maturity bonds along with taking advantage of credit investments which include floating rate loans. We continue to remain underweight in bonds across our strategies in favor of alternative investments. Year to date as of October 22, our alternative investments have returned an average of 18.2 % and have provided clients with an important bridge to higher returns than fixed income in this low interest rate environment. Year to date the 20+ Treasury Index (TLT) is down 11% on a price only basis. Although alternative investments carry different risk/reward profiles, we believe the reward prospects favor the incremental volatility relative to longer term-bonds. It seems many agree with our assessment. According to the Investment Company Institute (ICI) data, net outflows for bond mutual funds were $60 billion during the third quarter. Investors added over $30 billion to equity mutual funds during the same time period.

If we believe fixed income is at the end of a secular bull market, does this imply the continuation of a secular bull market in equities? We still like equities from here. There are tailwinds to help support long-term equity outperformance as we have discussed in the past. We continue to experience low inflation and low interest rates. The FED, with newly appointed Janet Yellen, will likely continue its dovish stance on fiscal policy. Earnings estimates have been lowered over the past year setting a lower bar for companies to "beat" expectations. We see broad economic data that supports world economic growth, albeit slow but improving, while the decline in energy costs is supporting growth in many countries, especially the U.S.

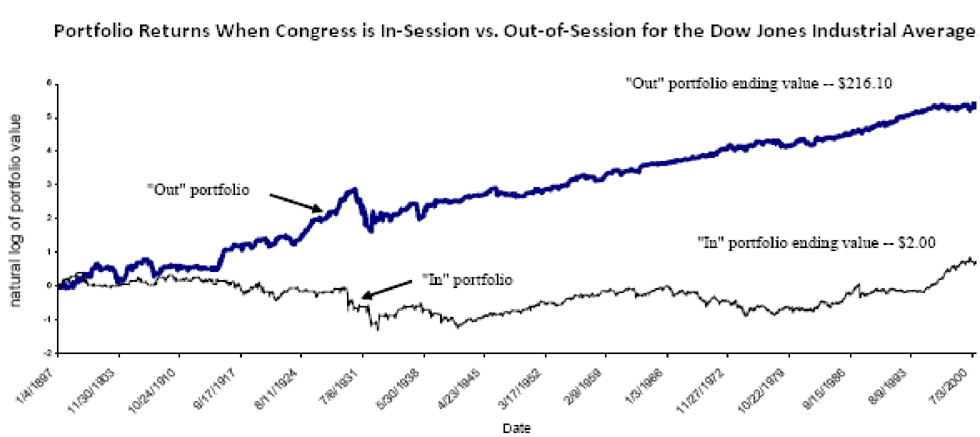
Washington Dysfunction Redux

The focus on issues in Washington, DC continues to be top of mind for investors. The recent budget showdown and debt ceiling impasse led to a government shutdown, the eighteenth since 1976. Investors shrugged off the dysfunction and the market rose 2.4% during the sixteen day period. However, Congress' negotiated agreement simply pushes the debt ceiling deadline to February 7, 2014. At that time, another round of sequestration budget cuts goes into effect. This second round of cuts reduces the government's discretionary spending from $1,058 trillion to $967.5 billion. Investors should keep in mind these shutdowns tend to be more noise than catastrophic market events as seen in the previous chart.



Source: Guggenheim Partners

In a research paper titled *Congress and the Stock Market* by Michael Ferguson of the University of Cincinnati and H. Douglas Witte of The University of Missouri they outline the returns of the Dow Jones Industrial Average (DJIA) based on whether Congress is in or out of session. They call this the "Congressional Effect." In their research, dating back to 1897, the authors uncover that "more than 90% of the capital gains over the life of the DJIA have come when Congress is out of session." The chart at right represents *Out-of-*



Session versus *In-Session* strategies on $1 invested. Data would seem to suggest the actions of congress do more harm than good as it relates to financial markets.

Headlines

Other notable storylines from the third quarter included continued political and military action in the Middle East (Syria). The sudden and significant move in interest rates, which occurred during the second quarter, may have spurned broader M&A activity. Large transactions financed through debt could carry heavier long-term borrowing costs if interest rates continue to move higher. It's no coincidence that companies like Microsoft (Nokia acquisition) and Verizon (acquiring Vodafone's remaining stake in Verizon's wireless business) engaged in significant acquisitions. Verizon's $49 billion bond offering on September 11th was the largest corporate debt sale in history. Long-term borrowing cost coupled with challenges to create top line sales growth and acceptable levels of return on equity are encouraging deal flow.

The finishing months of 2013 will most certainly not move higher in a straight line. A report form JP Morgan states, "Stay constructive as we see 1775 on the S&P 500 Index by year-end. Maintain a cyclical tilt premised on expectations of improving economic momentum in Europe, pent-up U.S. demand and stabilizing conditions in China." We subscribe to this thinking but hope our politicians can find middle ground in the coming months.

We continue to thank you for your business, referrals and confidence. As a quick note, we are finding more and more of our clients taking advantage of our corporate partners. HORAN has a great deal of expertise in personal planning, executive benefits, Medicare and social security strategies. Please don't hesitate to leverage our knowledgeable experts in these areas.

Respectfully,

HORAN Capital Advisors