MERITAS ADVISORS
Comprehensive Wealth Management

November 26th 2013

MONTHLY INVESTMENT OUTLOOK

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Meritas Advisors structures portfolios to meet our clients' personal goals and preferences within the scope of their risk tolerance. We strive to manage risk most effectively by utilizing a wider blend of asset classes, with the objective of achieving our client's goals with a reduced amount of overall portfolio volatility.

UPCOMING EVENTS

- Feb ô14: **The Importance of Estate Planning** with attorney Nadine Aarsheim
- 05/07/14: **Top 10 Strategies to Enhance the Value of your Business** with M&A attorney Jessica Karner
- 09/15/14: **Maximizing the Value of your Privately Held Business** with David Ryan of Upton Financial
- Dec ô14: **Vital tax Changes and Your Checklist** with Coree Cameron of Cameron Coffey & Kaye

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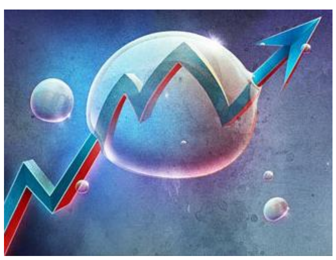
Dear Clients and Friends: Yours truly had the pleasure of attending The 31st Annual Monetary Policy Conference at the Cato Institute in Washington D.C. last week and had the good fortune to garner an invitation to the speakerôs dinner that evening where I dined with Gerald OôDriscoll and his lovely wife Maralene and Jerry Jordan, both former Federal Reserve Presidents. The dayôs discussions had a good deal to do with the current investing climate, so I will do my best in this issue to sum up it up.

As the autumn leaves fall and the morning air takes on the crisp smell of fall, we wish you and yours a wonderful Thanksgiving with plenty of laughter and love and a sprinkling of delightful conversation over some tasty pumpkin pie.
Lenore Hawkins, Principal

Market Update

November has been yet another month full of highs as the Twitter IPO was oversubscribed 30 times, priced at $26/share, opened at $45.10 then jumped up to $50.09 to then close below its opening price at $44.90 in its first day of trading. If you had any doubts that there may be the tiniest bit of a stock bubble, a company that has never turned a profit, generated $320m in sales in 2012 and is expected to generate $637m this year, while still losing money, was valued at $18.1 billion in its first day of trading.

If that doesnôt convince you that equities, and particularly internet equities are getting awfully hot. The 23-year-old CEO of Snapchat, a two year old company with **no revenue**, last week rejected a $3 billion, all cash, buyout offer from Facebook. One canôt help but think back to the heady days of 1999.



The S&P 500 continues to mount up new 52-week highs, while revenue growth has been lackluster and earnings growth rates continue to decline as companies are running out of areas to cut costs. From an aggregate fundamental perspective here is where we stand:

- Companies are running out of places to cut costs, after having spent years trimming after the onset of the financial crisis.
- Profit margins are at all-time highs, with limited opportunities for continued cost cutting.
- Labor costs are on the rise, which will cut into profit margins.
- Interest rates are more likely to rise than fall in the coming years, which will also cut into profit margins.
- This yearôs stock market gains have been driven primarily by expansion of the P/E ratio, recall our discussion of this topic in our August and September 2013 issues.

Bottom Line: *With the current elevated P/E levels and record profit margins, stock price appreciation will have to come from even higher P/E ratios or earnings growth, making further double digit gains from this point less likely without continued stimulus from the Federal Reserve, which of course comes with risk. We would like to see a pick up in earnings in order to justify domestic equity prices as these current levels.*

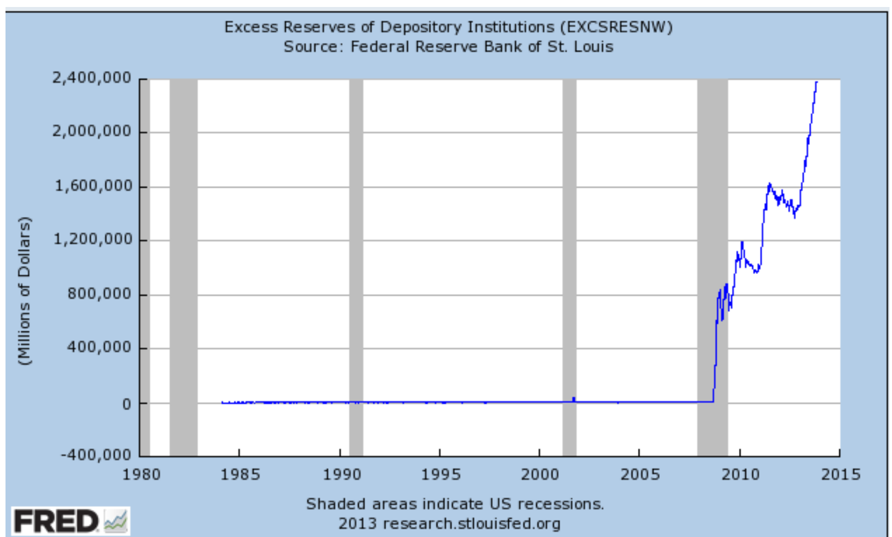
Economic Indicators

☺ GDP beats: On November 7th we learned that 3rd quarter GDP was better than expected at 2.8%, which of course pushed stocks lower in todayös good is bad and bad is good upside down market.

😐 Unemployment beats, but in lower paying sectors. On November 8th the U.S. Bureau of Labor Statistics reported that, ñTotal nonfarm payroll employment rose by 204,000 in October, and the unemployment rate was little changed at 7.3 percent. Employment increased in leisure and hospitality, retail trade, professional and technical services, manufacturing, and health care.ò Later in the day CNBC reported, ñBreaking (11:32AM EST) Europe stocks close lower after US jobs data.ò Remember, good news is bad news these days.

☺ Mortgage delinquency improves: The delinquency rate declines 2.8% in October for mortgages according to Lender Processing Services, making October 2013 10.7% lower than the same period last year. The number of homes entering foreclosure is also down 30% compared to a year ago.

😐 Borrowing returns: The deleveraging cycle in the U.S. appears to have bottomed out, with household debt rising $127 billion in Q3 to $11.28 trillion, which was the largest increase since the first quarter of 2008. Mortgage balances increased $56 billion and auto loans $31 billion, giving Detroit more cause for optimism. Investment-grade U.S. companies have issued a record of over $1 trillion in bonds so far this year. Keep in mind though as borrowing accelerates, all those bank excess reserves sitting at the Federal Reserve (see chart at right) may make their way into the economy, which could result in inflation when the total stock of money in the economy jumps.



😐 The European Central Bank cut its benchmark interest rate to a record low of 0.25% from 0.5% on November 7th, moving more quickly than expected to stimulate the euro zone economy in the face of falling inflation. Inflation in the euro zone unexpectedly declined to an annual rate of 0.7% in October, well below the E.C.B.ös official target of about 2%, raising concerns of deflation, which many believe would be harmful to the economy.

☹ Germanyös economy is continuing to improve, while concerns are growing that France may be heading back into a recession and Italy is still floundering. The latter two are unsurprising since much of their economic malaise can be traced to fundamental fiscal problems such as labor laws that make it risky to hire new employees since letting them go (perhaps because they donöt work out or the business doesnöt grow as much as was expected) is frightfully difficult. Many businesses just donöt want to take the risk. Add to that a mountain of red tape that make starting and growing a business attractive only to those who enjoy the idea of continually pounding their head against the wall.

☺ China appears to still be in expansion mode, but is slowing. Japanôs economy seems to be responding well at the moment to its Central Bankôs policy of continual monetary loosening, with exports posting their largest gain in three years. Looks good for now, but give me a few cups of coffee and a cupcake or two and my engines get revving like nobodyôs business. What serves as a kick start can end in an angry digestion and a cranky post-sugar high.

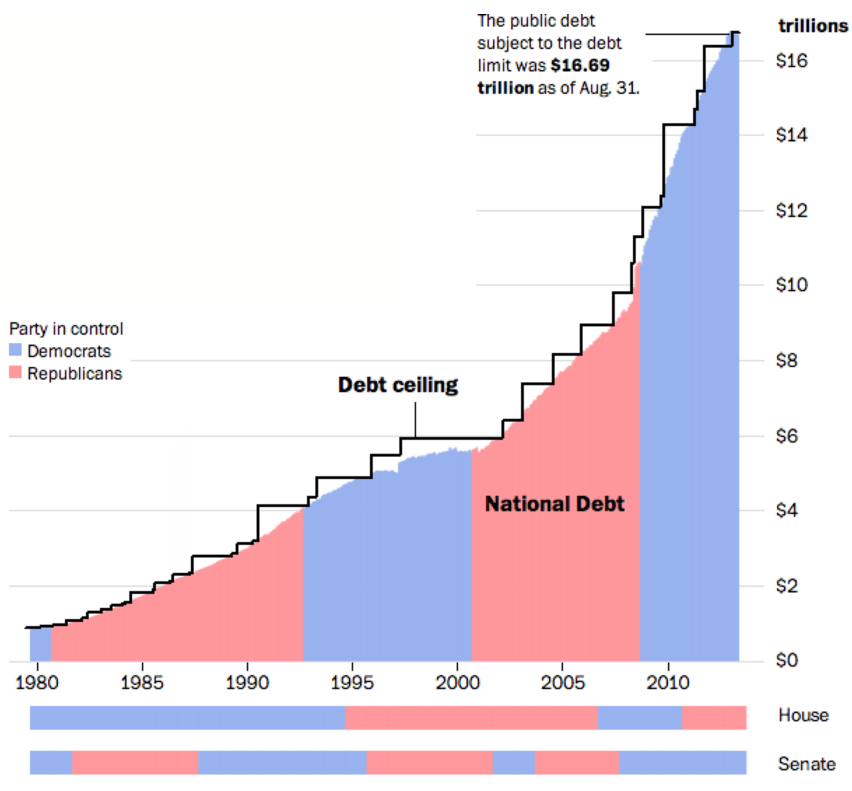
☹ Emerging market stocks are struggling as whispers of taper talk continue to linger, bringing to mind Don Coxeôs observation that, ñEmerging markets are markets you canôt emerge from in an emergency.ò Still wary from the last market crash, investors seem to be seeking areas where they think they can escape quickly if there is a rush for the exits. However, emerging market equities are currently priced at more attractive valuations than their developed world counterparts.

☺ U.S. energy sector rising: Petroleum exports as of July, according to the U.S. Commerce Department, are up 11% year-over-year, which is nearly 10 times the pace of total exports. Imports of petroleum products have dropped 6% year-over-year, which puts the nation back to mid-1990s levels. Oil related imports are now at a record low of 10% of all imports, compared to 12% last year and 15% five years ago.

100 Years of the Fed

There was a time when no one, outside perhaps the most esoteric economic geek circles, could name the current Chairman of the Federal Reserve. Those days are now long gone as the Fed has taken a much more active role in the economy and the various Fed Presidents and Chairman have evolved into media cult figures, perhaps less riveting than the latest Kardashian marriage collapse, but financially far more provocative.

The Fedôs current focus is clearly helping Uncle Sam reflate out of the governmentôs enormous mountain of debt. The chart on the next page shows the mountain of debt that has been created by impressive levels of spending from both sides of the aisle for a truly bi-partisan mess. The deficit is now almost three times what it was seven years ago, while debt service costs are at about the same level, thanks to Fed sponsored suppression of interest rates. The Fed effectively has complete control of the market for longer-dated Treasuries, with its holdings of bonds with a maturity greater than 10 years increasing by $154 billion through June of this year, (latest data available from the Fed) to a total of over $500 billion. Meanwhile the total outstanding level of such debt, privately held interest-bearing, grew a measly $9.6 billion for a total of $809 billion.



SOURCES: Congressional Budget Office, U.S. Treasury.

For those of you who enjoy a monetary policy geek-fest, the following summary of comments from the various speakers at the Cato Instituteôs Monetary Policy Conference on November 14th, including current Philadelphia Fed President Charles Plosser may be of great interest. Iôll do my best to keep it lively.

Charles Plosser opened the conference with a discussion of how many of the both implicit and explicit limits on central banks around the world have been challenged over the past few decades and most dramatically since the financial crisis. He believes the Fed entered into the realm of fiscal policy when it began purchasing non-Treasury securities such as mortgage-backed securities and referenced Milton Friedman's warning in 1967 that, **"We are in danger of assigning to Monetary Policy a greater task than it can accomplish."** Over the past 40 years, it is clear that we have failed to heed Friedman's warning, with the Fed doing a poor job of aligning expectations with what it is actually capable of accomplishing. Plosser warned that increasing the scope of the Fed's mandate opens the door for highly discretionary policies, acknowledging that a rules-based approach is unattractive for the majority of policy makers as it ties their hands. Discretion is the antithesis of commitment, something most politicians loathe. If the Fed gave itself less discretion, it would be held more accountable. He pointed out that the current climate of guess-my-mood communication on the Fed's part leads investors to make unwise gambles, as they try to read the mysterious tea leaves of Fed speak, such as the recent market tumult over taper talk.

Jerry Jordan, the former President of the Cleveland Federal Reserve expanded on Plosser's comments, pointing out that the existence of a Central Bank with discretionary power essentially guarantees the emergence of moral hazard with the resulting power to grant permission and regulate with discretion, opening the door to crony capitalism. To large banks, their PACs, (Political Action Committees) are often more impactful on their bottom line than their own management. (Shocker, businesses as well as individuals respond to incentives!) He referenced the Fed's recent report on the impact of quantitative easing on the economy stating that if there is any relationship between economic growth and quantitative easing, it is a remarkably well kept secret, instigating a round of chuckles from the audience. He pointed out that most economists understand that monetary policy cannot correct the mistakes of the rest of government, even though the Fed is currently doing its best to defy that assessment. He argued that central bank independence is a myth, at least during a financial crisis, because once a central bank takes its first steps to support the economy, there is no way out that does not involve collateral damage. That, by definition, prompts pressure from bureaucrats. He believes that exiting the current zero interest rate regime will be exceedingly complex and it will be impossible to escape without considerable financial market volatility. He seconded Plosser's assessment of the Fed's move into fiscal policy, asserting that traditional views of monetary policy and its impact are no longer useful as monetary policy has become fiscal policy. This move into fiscal policy has served to increase market volatility as no one can say with certainty, which entities will receive support during a crisis and for how long. Once again, discretion comes at a price.

Cato President and CEO John Allison, (former CEO of BB&T Corp, a U.S bank with over $180 billion in assets) discussed the impact he saw of government actions on his former bank. He pointed out that the Patriot Act and the federal privacy policy are in conflict with each other, leading to discretionary enforcement and application by regulators, which opens the door for corruption. He observed one of the great fallacies of current conventional wisdom is that there was financial deregulation under President George W. Bush which led to the crisis. Instead, Allison stated that there was actually a net increase in regulation if you look at the quantity and complexity of the regulations before and after his term. He believes that regulators greatly exacerbated the panic that hit the markets during the financial crisis by effectively suspending the rule of law and greatly increasing their level of discretion. No one had confidence in just what were the rules of the game, nor was there any clarity on who would be bailed out, who wouldn't, and at what cost and for how long.

Kevin Dowd, Professor of Finance and Economics, Durham University, reinforced John Allison's assertions, pointing out that the original Federal Reserve Act is about 32 pages long. The Glass-Steagall Act is under 40 pages long. The Volker Rule is just under 550 pages. Dodd-Frank, so far, is nearly 850 pages with most expecting it to total around 20,000 pages or more when all the discretionary bits are worked out. Notice a trend in the timeline here? The more complex the regulations, the more costly it is to enforce them, and to comply with them, creating a bias towards ever larger financial institutions, and increasing the opportunity for corruption.

For those of you who'd like a bit more, aside from suggesting you look into therapy as my family reiterates every holiday, I recommend going to this site to watch clips of some of the presentations. Despite the gloomy potential, there were frequent rounds of boisterous laughter, albeit the geeky economist style which I enjoy more than I ought to admit.

Things are better than you think

Alrighty then Ms. Sunshine! Yes, there is a lot to be worried about these days, but thatĝs what we get paid to do. There is an awful lot to be optimistic about as well, so letĝs close on a more upbeat note. I read a great article the other day about how most people have a warped view of the condition of the world and how things arenĝt nearly as bad as one would think from reading or watching the news. This seems rather intuitive as news content providers, whether in paper, on the web or on television, need to provide a certain amount of content every day and letĝs face it, do truly newsworthy events occur daily? The best way to garner attention, and they all compete for your attention, is to generate a sense of crisis. So when you are sitting down for Thanksgiving this year, if you have a naysayer at the table, here are a few questions to pop and get everyone in a cheerier mood. (Answers on the bottom of the last page)

1) In the year 2000 the total number of children (age 0-14) in the world reached two billion. How many do UN experts estimate there will be by the year 2100?
    a. 4 billion
    b. 3 billion
    c. 2 billion
    d. 1 billion
2) What percentage of adults in the world today are literate?
    a. 20%
    b. 40%
    c. 60%
    d. 80%
3) What is the life expectancy in the world as a whole today?
    a. 40 years
    b. 50 years
    c. 60 years
    d. 70 years
    e. 80 years
4) In the last 30 years, the proportion of the world population living in extreme poverty hasé
    a. Increase
    b. Remained more or less the same
    c. Decreased
5) What percentage of total world energy comes from renewable sources? Is it approximatelyé
    a. 2%
    b. 5%
    c. 11%
    d. 19%

Greg Tull's Your Money

As a comprehensive wealth management firm, we include many financial services in our offer to clients. Some examples of our capabilities include account consolidation and streamlining, letters of explanation to the IRS, tax planning, coordination with clientĝs team of advisors (such as attorney, CPA, banker, insurance agent), retirement planning and projections, outside investment return calculations, required minimum distributions, lending, and restricted stock and incentive stock option management. Give us a call when you have a financial opportunity youĝd like help pursuing, a financial problem youĝd like help solving, or a goal youĝd like help reaching. In many cases, weĝll be the last call you need to make. If we cannot provide the service you need, weĝll refer you to a trusted specialist who can.

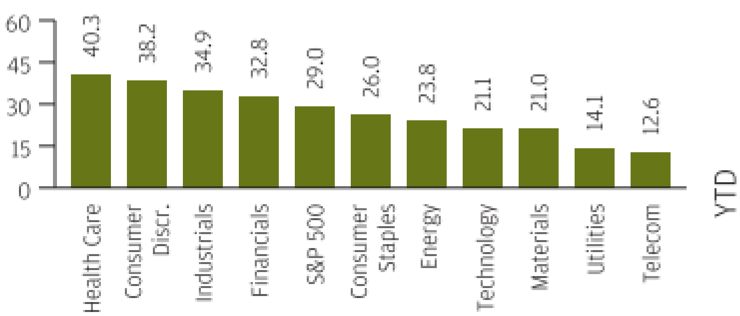
Market Recap
(as of November 22nd, 2013)

Weekly Data Center

Equities	Level	1 week	QTD	YTD	1 year	3-yr. Cum.
		Index Returns (%)				
S&P 500	1805	0.41	7.68	28.99	32.62	60.76
Dow Jones 30	16065	0.69	6.48	25.30	28.26	55.31
Russell 2000	2796	0.79	4.91	33.95	42.88	61.18
Russell 1000 Growth	553.44	0.09	6.82	29.11	31.87	59.33
Russell 1000 Value	561.72	0.48	7.63	29.67	34.64	62.59
MSCI EAFE	1874	-0.01	3.32	20.46	26.97	28.68
MSCI EM	1009	0.42	2.41	-1.74	5.32	-1.27
NASDAQ	3992	0.21	6.09	33.79	38.33	63.42

Fixed Income	Yield	1 week	QTD	YTD	1 year	3-yr. Cum.
U.S. Aggregate	2.32	-0.06	0.36	-1.53	-1.40	9.39
U.S. Corporates	3.19	0.14	1.00	-1.64	-1.28	15.66
Municipals (10yr)	2.94	-0.11	0.02	-2.05	-2.93	14.90
High Yield	6.42	0.29	2.64	6.46	9.15	30.69

Key Rates	11/22/13	11/15/13	9/30/13	12/31/12	11/22/12	11/22/10
	Levels (%)					
2-yr U.S. Treasuries	0.31	0.31	0.33	0.25	0.27	0.49
10-yr U.S. Treasuries	2.75	2.71	2.64	1.78	1.69	2.80
30-yr U.S. Treasuries	3.84	3.80	3.69	2.95	2.83	4.20
10-yr German Bund	1.75	1.70	1.78	1.31	1.43	2.65
3-mo. LIBOR	0.24	0.24	0.25	0.31	0.31	0.28
3-mo. EURIBOR	0.23	0.22	0.23	0.19	0.19	1.05
6-mo. CD rate	N/A	N/A	N/A	0.31	0.33	0.35
30-yr fixed mortgage	4.46	4.46	4.49	3.52	3.54	4.50
Prime Rate	3.25	3.25	3.25	3.25	3.25	3.25



Quiz Answers: 1.c 2.d 3.d 4.c 5.d

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