***March 2014***

# Monthly Investment Commentary

The U.S. stock market rebounded from its January losses and hit record highs by the end of February with larger-cap stocks gaining 4.6% and tipping into positive territory for the year to date (up 0.9% through February's end). Smaller-cap stocks achieved similar returns. As we saw throughout 2013, these gains occurred despite a continuing stream of mixed (and at times, poor) economic data. In February, some of the more disappointing data releases included a downward revision of fourth-quarter 2013 GDP growth (to 2.4% from 3.2%), which was also sharply lower than last year's strong third-quarter growth number. The month also brought reports of lower-than-expected job growth and retail sales as well as relative weakness in U.S. factory production. (That said, the extreme winter weather in some parts of the country may have affected the data to some extent.) On the positive side, housing, consumer sentiment, and business activity all had favorable updates toward month end. Another reason for market optimism appears to be the Federal Reserve's assessment of U.S. economic strength. As new Fed Chairman Janet Yellen assumed official leadership in February, investors got a sense of her current views through two congressional testimonies over the month. She indicated she expects QE tapering to continue, though this could change given a more significant deterioration in U.S. economic data, suggesting that the Yellen Fed won't be quick to remove its support.

**February Benchmark Returns (Preliminary)**

| | Feb | YTD |
|---|---|---|
| **Large-Cap Benchmarks** | | |
| Vanguard 500 Index | 4.6% | 0.9% |
| iShares Russell 1000 | 4.8% | 1.4% |
| iShares Russell 1000 Growth | 5.1% | 2.1% |
| iShares Russell 1000 Value | 4.3% | 0.5% |
| **Mid-Cap Benchmarks** | | |
| iShares Russell Midcap | 5.8% | 3.8% |
| iShares Russell Midcap Growth | 6.3% | 3.9% |
| iShares Russell Midcap Value | 5.4% | 3.5% |
| **Small-Cap Benchmarks** | | |
| iShares Russell 2000 | 4.8% | 1.9% |
| iShares Russell 2000 Growth | 4.8% | 3.1% |
| iShares Russell 2000 Value | 4.6% | 0.5% |
| **Other Benchmarks** | | |
| Vanguard FTSE Developed Markets ETF | 5.9% | 0.4% |
| MSCI World ex USA Index | 5.5% | 1.2% |
| Vanguard FTSE Europe ETF | 7.3% | 2.4% |
| Vanguard FTSE Emerging Mkts ETF | 3.2% | -5.5% |
| Vanguard REIT Index | 5.0% | 9.4% |
| Vanguard Total Bond Mkt Index | 0.5% | 2.0% |
| BofA Merrill Lynch U.S. High Yield Cash Pay | 2.0% | 2.8% |
| Vanguard Int. Term Tax-Exempt Fund | 1.0% | 2.7% |
| S&P/LSTA Leveraged Loan Index | 0.2% | 0.8% |
| Citigroup World Govt. Bond Index | 1.4% | 2.8% |
| JPMorgan GBI-EM Global Diversified Index | 3.9% | -0.9% |
| DJ-UBSCI (Commodity Futures) | 6.2% | 6.6% |

As always, there is a lot of noise in the short-term data, and while the markets seem to react day-to-day based on new headlines, it's not part of our investment process to do so. We remain of the view that the U.S. economy is recovering at a modest pace, far below the historical average, while stock valuations seem to reflect unrealistically high expectations for future growth. This mismatch is part of the reason we remain modestly underweight U.S. stocks in our strategies. Still, we retain a weighting significant enough that our strategies participated in the month's gains and many of our active managers posted strong relative results. We will provide a comprehensive update on U.S. equities next month as part of our quarter-end commentary.

Stock market gains extended to international markets and both developed-foreign and emerging-markets stocks were positive in February. Among developed markets, European stocks rose based on increased optimism for recovery—and perhaps lessening concern about deflation. Emerging markets were positive in February, even as civil unrest in Ukraine escalated—and resulted in a month-end rally in defensive assets like Treasurys and gold. Despite slowing growth in China—as the government attempts to manage a potential debt bubble—and this year's rate hikes by countries with some of the harder-hit currencies as of late (India, South Africa, Brazil, etc.), stocks rose alongside other risk assets.

Bonds were slightly positive in February and are up 2% for the year-to-date thanks to their strong returns in January. Overall, the yield on the 10-year Treasury has fallen from the end of 2013, hitting 2.66% at the end of February, down from 3.04% at year end. Municipal bonds have been particularly strong in 2014, following a challenging year in 2013 when headline risk such as Detroit's bankruptcy hung over the market. We have maintained our allocations to munis in our tax-sensitive strategies and our active managers participated in the gains.

*—Francis Financial and the Litman Gregory Investment Team (3/3/14)*