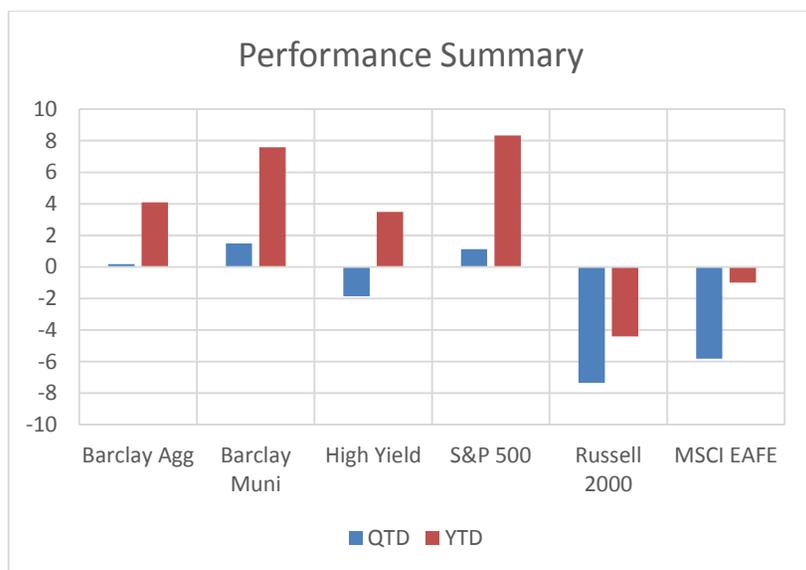


## Q3 Investment Commentary

By the AWM Team

### Our Perspective on the Markets

Key themes during the quarter were an increase in volatility and greater divergence in performance across several asset classes. Divergence was most apparent in the stock market. Large-cap stocks, represented by the S&P 500, were up a modest 1.13% for the quarter, while small-cap stocks (Russell 2000) were down sharply at (-7.36%). Developed international stocks also lagged in the quarter, down (-5.88%), in the face of continued sluggish growth and a strong U.S. dollar. Emerging market stocks were down significantly in the month of September (-7.39%) and finished the quarter with a (-3.36%) loss. Often an increase in divergences between large and small-cap performance and other metrics can be a sign of a “tired” bull market and warrants a close watch for further deterioration.



The U. S. economy held its own despite setbacks in the rest of the world. Economic growth continued to muddle along and we expect it to continue on its path of 2.0 to 2.5% growth for the next year. Mainly a result of continued slack in the global economy, an aging demographic profile, and residual effects from two financial crises in the past decade or so.

Bond performance showed divergences between higher and lower quality markets during the quarter. Municipal bonds were up 1.49% for the quarter and core U.S. bonds (Barclays Aggregate) had a small gain of 0.17%. While high-yield (junk) bonds were down (-1.87%) and more aggressive emerging bonds were down (-5.66%). The 10-year Treasury finished the quarter around 2.4% and continues to look well contained, with little signs of inflation and a still accommodative monetary policy. The Federal Reserve looks ready to conclude its bond purchasing strategy in

October and we will be watching closely for any disruptions in the bond market and changes in interest rates.

### Our Current Views and Portfolio Positioning

Below are some of the key themes that we are recommending in portfolios:

1. We continue to underweight small-cap stocks relative to large-cap.
2. Valuations for foreign stocks are attractive relative to U.S. markets. Short-term they face headwinds from a rising dollar, longer-term we expect them to outperform U.S. stocks
3. Our expectation for bond market returns are low and we are using absolute return and flexible managers to add value.
4. We recommend alternative asset positions that can hedge risk and provide real returns.
5. In a low interest rate environment we still like the theme of high and growing yield stocks, which includes some selective REIT exposure.

See next page for more details

## Asset Class Views

Asset Class	View*	Comments
<b>Equities</b>		
U.S. Large Cap	↔	Markets have reached a moderately overvalued level, with pockets of good values still available in select in high quality stocks
U.S. Small/Mid Cap	↓	We believe this segment of the market is overvalued and should be underweighted, the recent underperformance of small-caps has helped but likely has further to go
International Developed	↑	Valuations are more attractive and should be over-weighted relative to U.S. stocks, short-term the higher U.S. dollar may pressure these markets
Emerging Markets	↔	We think valuations are reasonable and long-term potential is good; however we are concerned near-term about currency and liquidity risk
<b>Fixed Income</b>		
Investment Grade	↓	Valuations look rich; keep exposure for risk management and diversification
High-Yield Bonds	↓	Valuations are rich and we would reduce positions; they are likely to have substantial risk if economy slows down or we enter another recession
Municipal Bonds	↔	Valuations are fair, however they look attractive for high tax-bracket investors
TIPS	↔	Valuation is rich, however they can make sense as a hedge against inflation
Floating-Rate Loans	↔	Investors flooded into this asset class in '13 and started to mildly exit in '14, we are cautious near-term but would upgrade our rating on pull backs
Emerging Markets	↔	Valuations have increased based on this year's strong performance; rather than dedicated exposure we prefer to invest with diversified Int'l manager's that have a broad mandate
<b>Alternatives</b>		
Absolute-Return/Alternatives	↑	We like this asset class and believe it can improve the risk/reward profile of portfolios that hold traditional asset classes
REITs	↔	Valuations for the general asset class look overvalued; selectively we see opportunities in individual health-care related REITs
Commodities/Gold	↔	We view gold as an "insurance" asset and recommend holding small positions, if the dollar continues to appreciate and gold breaks support we would suggest a stop/loss

\* ↔ Neutral weight   ↓ Underweight   ↑ Overweight

**U.S. Stocks****Market Performance, Third Quarter 2014**

Index	Q3 2014	YTD
S&P 500	1.33%	8.34%
Russell 1000	0.65%	7.97%
Russell 1000 Value	(-0.19%)	8.07%
Russell 1000 Growth	1.49%	7.89%
Russell Midcap	(-1.66%)	6.87%
Russell 2000	(-7.36%)	(-4.41%)

Source: Morningstar

- Stocks experienced a wide divergence in performance during the quarter. The S&P 500 was up a modest 1.33%, while small-cap stocks were down a sharp (7.36%).
- Small cap stocks were down over (6%) in September and are now down (5.46%) YTD. Small-caps are lagging large-caps by over 12% this year, this is often a sign that a bull market is getting “tired”.
- Growth outperformed value for the quarter, up 1.49% vs, down (.19%), respectively. YTD the returns are similar (up about 8%), our outlook is neutral.

**International Stocks****Market Performance, Third Quarter 2014**

Index	Q3 2014	YTD
MSCI EAFE	(-5.83%)	(-0.99%)
MCSI EME	(-3.36%)	2.75%
MSCI BRIC	(-3.14%)	1.55%

Source: Morningstar

- International stocks sold off sharply, down (5.83%) as economic growth remained sluggish and the U.S. dollar strengthened relative to global currencies. Valuations look attractive relative to the U.S., and longer-term we expect them to outperform.
- Emerging markets had a terrible month of September, down over (7%), leaving them down (3.36%) for the quarter. Near-term we expect volatility to remain high, longer-term we believe they are valued attractively relative to U.S. stocks and should outperform.

**Fixed Income****Market Performance, Third Quarter 2014**

Index	Q3 2014	YTD
Vanguard Total Bond Index	0.13%	3.99%
Barclays Muni Bond	1.49%	7.58%
Barclays US Corp High-Yield	(-1.87%)	3.49%
JPM GBI- EM Global Diversified	(-5.66%)	(-0.01%)
iShares TIPS Bond	(-2.07%)	3.58%
BofA Merrill Lynch 3 month Treasury Note	0.01%	0.04%

Source: Morningstar

- Fixed income also saw big divergences during the quarter, with Muni and core bonds up 1.49% and 0.17%, respectively. While lower quality high yield bonds were down (1.87%) and more volatile emerging market bonds were down (5.66%).
- The Federal Reserve is scheduled to conclude its bond purchasing in October, we will be watching closely for disruptions in the bond markets and changes in interest rates.
- We own bonds mostly for diversification and have low expectations for returns in the coming years. We are selectively using absolute return and flexible bond managers to add value.

**Alternative Assets****Market Performance, Third Quarter 2014**

Index	Q3 2014	YTD
PIMCO All Asset All Authority	(-3.85%)	2.21%
AQR Diversified Arbitrage	(-2.62%)	(-1.28%)
Gateway	0.54%	3.07%

Source: Morningstar

- In general, alternative strategies underperformed our expectations for the quarter. The All Asset All Authority fund was hurt by its exposure to emerging market and inflation protection asset classes.
- We continue to recommend a moderate allocation to alternatives for their diversification benefits and expected contribution to overall portfolio risk-adjusted return.

## Appendix:

### Benchmark Definitions

U.S. Equity		Description
S&P 500	Index	The index includes 500 leading US companies and captures approximately 80% coverage of available market capitalization.
Russell 1000	Index	The Russell 1000 Index measures the performance of the large-cap segment of the U.S. equity universe and includes approximately 1000 of the largest securities. The Russell 1000 represents approximately 92% of the U.S. market.
Russell 1000 Value	Index	The Russell 1000 Value Index measures the performance of the large-cap value segment of the U.S. equity universe. It includes those Russell 1000 companies with lower price-to-book ratios and lower expected growth values.
Russell 1000 Growth	Index	The Russell 1000 Growth Index measures the performance of the large-cap growth segment of the U.S. equity universe. It includes those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values.
Russell Midcap	Index	The Russell Midcap Index measures the performance of the mid-cap segment of the U.S. equity universe. It includes approximately 800 of the smallest securities based on a combination of their market cap and current index membership.
Russell 2000	Index	The Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership.
International Equity		Description
MSCI EAFE	Index	The EAFE (Europe, Australasia, Far East) index consists of 21 developed market country indexes, excluding the US & Canada. It is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets.
MCSI EME	Index	The index is a free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets and includes 23 emerging market countries in the index.
MSCI BRIC	Index	The index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the following four emerging market country indexes: Brazil, Russia, India and China.

Fixed Income		Description
Vanguard Total Bond Index	Index Fund	This index measures a wide spectrum of public, investment-grade, taxable, fixed income securities in the United States—including government, corporate, and international dollar-denominated bonds, as well as mortgage-backed and asset-backed securities, all with maturities of more than 1 year.
Barclays Aggregate Bond	Index	The U.S. Aggregate Index covers the USD-denominated, investment-grade, fixed-rate, taxable bond market of SEC-registered securities. The index includes bonds from the Treasury, Government-Related, Corporate, MBS (agency fixed-rate and hybrid ARM pass-through bonds), ABS, and CMBS sectors.
Barclays Muni Bond	Index	The U.S. Municipal Indices cover the USD-denominated long term tax exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds, and pre-refunded bonds.
Barclays US Corp High-Yield	Index	The index covers the USD-denominated, non-investment grade, fixed-rate, taxable corporate bond market and excludes Emerging Markets debt.
JPM GBI- EM Global Divers	Index	The index tracks returns for actively traded external debt instruments in emerging markets. Included in the index are US-dollar denominated Brady bonds, Eurobonds, and traded loans issued by sovereign entities.
iShares TIPS Bond	ETF	The iShares TIPS Bond ETF seeks to track the investment results of an index composed of inflation-protected U.S. Treasury bonds.
BofA Merrill Lynch 3 month Treasury Note	Index	The 3-month US Treasury Note Index is comprised of a single issue purchased at the beginning of the month and held for a full month. At the end of the month, that issue is sold and rolled into a newly selected issue.
Alternative Assets		Description
PIMCO All Asset All Authority	Mutual Fund	The investment seeks maximum real return, consistent with preservation of real capital and prudent investment management. The primary benchmark for the fund is the S&P 500, with a secondary objective of Consumer Price Index +650 basis points.
AQR Diversified Arbitrage	Mutual Fund	The investment seeks long-term absolute (positive) returns. It invests in a diversified portfolio of instruments, including equities, convertible securities, debt securities, loans, warrants, options, other types of derivative instruments.
Gateway	Mutual Fund	The investment seeks to capture the majority of the returns associated with equity market investments, while exposing investors to less risk than other equity investments. The fund invests in a broadly diversified portfolio of common stocks, while also selling index call options and purchasing index put options.