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Nauset Market Commentary
Third Quarter 2014

Market Performance Recap: **Markets Flatten amid Global Concerns**

Despite a stronger US economy, global growth concerns and geopolitical conflicts led to a flat return of 0.0% for the Russell 3000 broad U.S. stock index. Slight gains in large cap stocks were offset by a selloff in small cap equities as investors became more risk adverse. Stocks in international developed and emerging markets were both lower as a result of weak economic data. In fixed income, the Barclays Intermediate Gov't/Credit Index was unchanged at 0.0% due to a dip in bond prices.

Economic & Market Discussion: **Birding at the Fed**

The U.S. economy continues to grow, albeit modestly, while the latest unemployment rate of 5.9% is at a six-year low. This positive environment coincides with the scheduled end of the Federal Reserve's latest quantitative easing program in October. So, Fed watching is now in full swing with the focus on when the Janet Yellen-led Fed will begin to raise the Fed Funds rate from its zero level. Will the Fed hawks push up rates with a series of increases starting in early 2015? Or will the Fed doves hold sway by delaying the first rate increase until later in 2015? Expectations and predictions are already creating volatility in the markets.

In September, the Fed provided a rough outline of how it will unwind the zero interest rate policy of the past several years. The timing of its move toward "normalization" is dependent on several key factors, particularly labor participation data and GDP growth. Given the Fed's aim of rate normalization, the concern of investors is that any Fed Funds rate increase will dampen modest US growth and/or drive up inflation, and thereby send financial markets in a tailspin.

To some observers, the Fed will not risk upsetting the financial markets, and any Fed Funds rate increase may be over a year away. Others believe that stronger-than-expected growth will force the Fed's hawks into near term action. Our view is the Fed will prove to be dovish by moving at a cautious, deliberate pace. We also believe that the first rate increase or two will neither spike inflation, nor drive the stock market into a major correction. While we do see potential for market gains over the next 12-18 months, stocks will likely endure a bumpy ride and bonds will be exposed to increased risks.

Portfolio Strategy: **Diverse Sources of Return**

Our current strategy favors large cap, higher quality equities with a full allocation to real asset holdings in energy infrastructure and real estate. Our general income allocations are underweight and slightly defensive against the prospect of rate volatility. That said, in this low growth environment we are seeking multiple sources of return and see modest default risk for higher-yielding bonds. As a result we have added positions with exposure to non-core credit strategies. We also continue to see alternative and hedged investments as a good way to provide positive returns, while buffering risk.

Market Performance **% Change for Periods Ended 9/30/2014**

Market Index	Third Quarter	2014 YTD	1-Year	3-Year Annual.	5-Year Annual.
Russell 3000	0.01	6.95	17.76	23.08	15.78
MSCI EAFE – Non-US	-5.88	-1.38	4.25	13.65	6.56
MSCI Emerging Markets	-3.50	2.43	4.30	7.19	4.42
DJ US Real Estate	-2.67	13.31	13.25	15.99	15.00
BarCap Intermediate Gov't/Credit Bond	-0.03	2.22	2.19	2.01	3.42
IQ Hedge Multi-Strategy	-0.66	3.50	6.49	5.56	3.82
3-Month T-Bill	0.01	0.03	0.04	0.05	0.08

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