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"We're from the Government and we're here to help you."

Global Markets and Regions

	3rd QTR	2013 YTD
US	5.7%	20.5%
Developed Europe	13.7%	16.7%
Asia	6.3%	10.5%
Emerging Markets	13.9%	0.5%

US Markets

	3rd QTR	2013 YTD
Dow 30	2.1%	17.6%
Large Cap Cos.	5.3%	19.8%
Mid. Cap Cos.	7.5%	23.2%
Small Cap Cos.	10.7%	28.7%
Bonds	0.76%	-1.82%

Bond investors are beginning to wonder if that is still the case. Quantitative Easing, Open Market bond purchases, extended unemployment benefits and disability payments. Is this economic stimulus or financial repression? The fate of interest rates and bond prices appear to be under the direction of the Federal Reserve. This in turn has kept borrowing costs low. Some aspects of the economy appear to have benefitted. Then they mention the "Taper" word and all of a sudden the "safe haven" of bonds doesn't seem so much anymore. Now our elected officials are playing open and close the Government and the stock market starts to resemble a roller coaster. Have you heard that the Government run Health Insurance Exchanges are open for business?

In 1982 ten year Treasury bonds yielded 14.5% after having risen from under 2% in the 1940's. Earlier this year the rate dipped under 2% again. It has been a very long run. Bonds have only delivered negative returns twice in the last 30 years when the long decline in interest rates was briefly interrupted. In 1994 there was a Government debt ceiling battle, not unlike the current dust-up in Washington. Interest rate declines and positive annual bond investment returns soon resumed.

Given that long history and the current Government dysfunction, is it time to be worried about the direction of interest rates? Should we be concerned about the future growth prospects for the economy and the Federal Reserve's efforts to promote growth with their easing strategies? Or have the Fed's actions laid the groundwork for a return to a trend of ever higher interest rates? Can our elected officials make adjustments to fiscal policies that promote growth?

The Federal Reserve and central banks around the world have been in the business of influencing interest rates for quite a long time. Their benign objective is to create monetary conditions conducive to a healthy economy. The Federal Reserve has a statutory mandate for monetary policy to promote “maximum employment, stable prices and moderate long term interest rates”. Since the Global Financial Crisis, that role has taken on new dimensions as they have become more or less the primary tool for maintaining a healthy economic environment. The fiscal activities of the rest of the Government in helping maintain a healthy economic environment have been problematic. Business surveys have repeatedly cited the lack of fiscal and regulatory clarity as major concerns. Are they really here to help?

Despite all of that, the economy both domestically and globally continues to move forward. One of my favorite economists, Brian Westbury, refers to our “Plow Horse Economy”. GDP growth is tepid at around 2% annual growth. Auto sales are strong and home prices are positive though nowhere near where they were in the recent past. Payroll reports continue to improve, both new jobs and layoffs. Business surveys indicate that hiring intentions are up and the availability of applicants is tightening. There appears to be no booming economy, but just enough to ward off the gloom.

We are entering earnings season with 3rd Quarter estimates subdued but mildly positive. Revenue growth for companies has been particularly tepid. US stocks have been the one asset class that has delivered consistent gains so far this year. It appears that companies don’t need to deliver robust growth of sales and earnings to move their share prices. Federal Reserve policies have also been an assist. Every other asset class has shown returns all over the place. International stocks have been negative much of the year but are back to positive territory, barely. Bonds have been negative and look poised to deliver their first yearly negative return since 1999. Diversification has not been the path to great returns this year, nor has it necessarily reduced investment volatility. A very challenging environment to say the least.

But our Government is on the case!

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