ASCENTIAL WEALTH ADVISORS

Fall 2014

Inside:

Performance Review 1
Focus 1
Fixed Income 2
US Equities 2
International Equities 3
Other 3
Looking Ahead 4
Disclosures 4

Slow growth produces modest gains

Index:	Jun 14	2013	2012	2011	2010
S&P 500	+7.1	+32.4	+16.0	+2.1	+15.1
DJIA	+2.7	+29.6	+10.2	+8.4	+14.1
EAFE (Int'l)	+4.8	+22.8	+17.3	-12.1	+7.8
BC Ttl Bond	+3.8	-2.0	+4.4	+7.7	+6.5

Dow Jones Relative Risk Benchmarks					
Conservative	+4.4	+1.4	+5.4	+5.3	+8.5
Moderate	+5.8	+14.5	+11.2	+0.3	+14.0
Aggressive	+6.8	+27.0	+16.8	-5.1	+19.4

Equity and bond prices rose in the first half of the year in spite of weak economic growth and mixed signals as to the direction of the US economy. While US GDP fell by 2.9% in the first quarter due to a harsh winter and lower than expected healthcare spending, many believe this was an anomaly with full year growth projections at around 2%. The unemployment rate continued to decline to 6.1%, as the recovery reached a milestone by regaining the 8+million jobs lost during the Great Recession. However there are questions regarding the quality of the new jobs and whether wage growth will pick up and reignite consumer spending.

US equity markets continue to push to new all-time highs, but earnings have kept pace with stock price increases leaving valuations similar to where they ended 2013. International equity markets posted returns in line with the US.

Surprisingly there was little performance dispersion across asset classes with bond prices also pushing higher as yields fell. The ten year treasury fell to a 2.5% yield after closing 2013 at 3.0%.

Focus:

- ✓ Maintain current asset allocation targets and rebalance portfolios to targets
- ✓ Review pros and cons of our select list of investments against exchange traded funds

Focus

After several years of strong performance, investor expectations are increasing and so is anxiety. While we are positive about the rest of the year, we see risks on the horizon and look to maintain a risk managed approach in our asset allocation.

Though there has been an unexpected rally in the bond market this year, we are concerned about its longevity. Our view is still that interest rates will rise and that we should insulate our portfolios by holding some alternative investments in place of traditional fixed income.

On the equity side, there are not as many bargains after an extended stretch of positive returns; however we do not feel the equity market is overpriced. In the US, equities are valued near their long-term averages, and we are maintaining our recommended allocations.

International equities have had a good start this year, but valuations overseas remain below average and we believe they carry upside potential in a gradually improving economic climate.

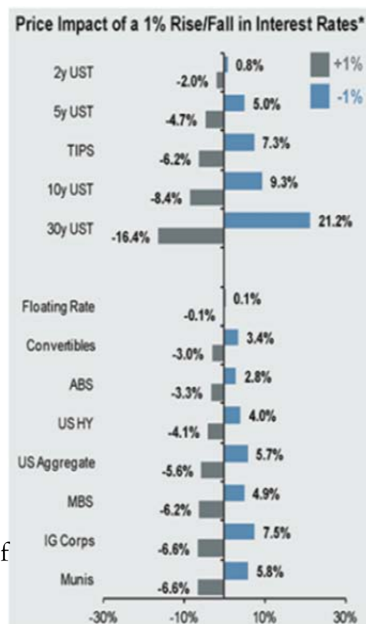
Fixed Income

"…The risk of rising interest rates to a bond portfolio is calculable and should not be ignored, particularly when rates have been held to artificially low levels for an extended period of time."

After posting losses in 2013 as interest rates rose, bonds gained this year as rates unexpectedly fell. While the Federal Reserve has continued to taper its bond purchases, slower economic growth in the US has caused a delay in action to raise interest rates. With the Fed's rate increases on the back burner and the supply of new bond issues down almost 20% through the first half (UBS WMR, June 2014), the bond market responded by pushing prices higher.

Municipal bonds have rebounded strongly, gaining 5.9% in 2014 and outperforming the aggregate bond market, after being beaten down in 2013 by rising rates and default fears.

Despite the recent activity in the bond market, we remain wary of the impact of rising interest rates on bonds in the longer term. Our recommendations to maintain an underweight position in traditional fixed income and hedge against rising interest rates are unchanged from the beginning of the year. While this strategy weighed down performance in the first part of the year, the risk of rising interest rates to a bond portfolio is calculable and should not be ignored, particularly when rates have been held to artificially low levels for an extended period of time.



Source: JP Morgan "Guide to Markets" April 2014

US Equities

"For those who fear equity indices at all-time highs, it may be helpful to note that since 1940, on a month end basis, the S&P 500 has been at record highs 22% of the time, and the average price gains in the 12 months following these highs has been 8%." (UBS WMR, June 2014)

US equity indices have repeatedly set new all-time highs. Although this rekindles some anxiety among investors, we believe valuations remain at reasonable levels. Based on forward earnings, at mid-year the S&P 500 traded at about 15.5 times estimated earnings, only slightly above its long term average of 15. Earnings and profit margins for S&P 500 companies are at all-time highs, while corporate debt is well below average. The continued rise in equity prices appears justified by these metrics, indicating equities are for the most part fairly valued.

For those who fear equity indices at all-time highs, it may be helpful to note that since 1940, on a month end basis, the S&P 500 has been at record highs 22% of the time, and the average price gains in the 12 months following these highs has been 8%. (UBS WMR, June 2014)

We still believe that growth stocks hold more potential than value stocks going forward. Currently the P/E premium for growth stocks is only 21%, well below the 40% average premium we have seen the past 30 years. (UBS WMR, June 2014) We also believe rising interest rates could put pressure on dividend paying value equities as income seeking investors may reposition to fixed income as rates increase.

The lack of compelling competing investments has helped US equities continue their climb. Bonds are offering paltry yields, and international equities can carry more risk than some investors are willing to accept.

International Equities

International equities had a positive first half, with developed (MSCI EAFE) and emerging markets (MSCI EM) up 4.8%. The biggest change so far this year has been a lessening in the volatility of emerging markets. After severely lagging in 2013, emerging market equities have been healthier, delivering gains more closely in line with global markets.

Source: JP Morgan "Guide to Markets" April 2014

Real GDP growth for emerging markets is expected to come in around 4% for 2014, as opposed to just under 2% for developed markets including the US. (Source: JP Morgan) In addition, on a relative basis, P/E ratios for emerging markets are below that of developed markets, indicating potential for continued price appreciation. Long term we believe emerging markets hold opportunities for investors that can tolerate wider price fluctuations.

Within developed international markets, we continue to suggest overweighting small to mid-sized European companies. Although we have seen these assets perform well in the first half of 2014, the valuations still remain below their long-term average, and we expect additional appreciation. While Europe's economy has not fully recovered with unemployment still above 10%, there are signs of continued improvement in other indicators such as the cost of government debt and residential housing prices.

"Long term we believe emerging markets hold opportunities for investors that can tolerate wider price fluctuations."

Other (Real Estate, Commodities, and Alternatives)

We have recommended greater allocations to alternatives in place of US traditional fixed income, under the belief that rising interest rates will damage bond portfolios. So far in 2014, interest rates have fallen resulting in positive performance from bonds. We do not feel this trend is sustainable, and remain convicted that using alternatives to help manage risk will prove to add value over time.

The alternative strategies we have selected focus on reducing portfolio volatility and risk while attempting to preserve capital and deliver modest returns under most market conditions. We accept that alternative strategies will underperform when equity markets are strong; however, we also expect lower price volatility when equity markets falter or interest rates rise. One of the risks in owning alternatives is they rely on the talent of their managers to deliver the results we expect. We have conducted significant due diligence to identify managers that we believe can meet our expectations and are comfortable taking the talent risk versus interest rate risk in traditional fixed income given the current environment.

"We accept that alternative strategies will underperform when equity markets are strong; however, we also expect lower price volatility when equity markets falter or interest rates rise."

Heads Up:

- **Money movement-** Identity theft and computer hacking present unique challenges for the financial services industry. Due to the rise of incidences where individuals have gained access to personal information or email accounts, we take extra caution to make sure that requests to transfer funds are legitimate before processing them. While sometimes this may feel inconvenient or excessive, please know that our efforts to verify your requests are simply to protect your assets.
- **Please excuse the dust!** Our office is under construction; we are expanding at our current location to make room for future growth in our firm.

Ascential Wealth Advisors:

11 East Superior Street
Suite 508
Duluth, MN 55802

Web:
www.ascentialwealth.com

Phone:
Local 218-336-2500
Toll Free 888-840-8299

Email:
Brad Christiansen - Financial Advisor
bchristiansen@ascentialwealth.com

Dave Kohlhaas - Financial Advisor
dkohlhaas@ascentialwealth.com

Kristin Rognerud - Financial Advisor
krognerud@ascentialwealth.com

Gayle Froelich - Registered Sales Assistant
gfroelich@ascentialwealth.com

Lori Greenwalt – Administrative Assistant
lgreenwalt@ascentialwealth.com

Ascential Wealth Advisors is an independent firm. Securities offered through **Raymond James Financial Services, Inc.** Member FINRA/SIPC.

Looking Ahead

With little dispersion in performance across asset classes this period, and relatively little change in the economic outlook, our view and corresponding recommendations for asset allocation are unchanged from the end of 2013. While our position on asset allocation remains the same, we have done significant due diligence on our select list of investments and will be recommending changes. Specifically, we have examined how exchange traded funds (ETFs) compare with our current select list of investments and look forward to discussing this topic in your review meeting.

Disclosures

Any opinions are those of the professionals at Ascential Wealth Advisors and not necessarily those of Raymond James. Inclusion of indices and benchmarks is for illustrative purposes only. Investors cannot invest directly in an index or benchmark. Past performance may not be indicative of future results. Bond prices and interest rates have an inverse relationship. The recommendations included in this newsletter are designed for clients. Please consult an investment professional concerning your unique situation. The information has been obtained from sources considered to be reliable, but we do not guarantee that the foregoing material is accurate or complete. U.S. government bonds and Treasury bills are guaranteed by the U.S. government and if held to maturity, offer a fixed rate of return and guarantee principal value. Please note that international investing involves special risks, including currency fluctuations, differing financial accounting standards, and possible political and economic volatility. Investing in emerging markets can be riskier than investing in well-established foreign markets. Investing involves risk and investors may incur a profit or a loss. The S&P 500 index is a broad based measurement of changes in US stock market conditions based on the average performance of 500 widely held common stocks. The Dow Jones Industrial Average covers 30 major NYSE industrial companies, representing approx. 25% of the NYSE market capitalization and less than 2% of NYSE issues. The MSCI EAFE Index is a free float-adjusted market capitalization index designed to measure the equity market performance of developed markets. The Barclays Capital Aggregate Bond Composite Index measures investment grade, fixed-rate, taxable bond markets of roughly 6,000 SEC registered securities with intermediate maturities averaging approx. 10 years. The S&P Dow Jones Relative Risk Indices intend to measure total portfolios of stocks, bonds, and cash, and represent investor risk profiles assigned based on efficient frontier risk analysis. They track the three asset classes represented by sub-indices tracked by Dow Jones and Barclays (ex Dow Jones Large Cap Growth Index, Barclays Corporate Bond Index), and are reweighted monthly. This is not a complete description of the securities, markets, or developments referred to in this material. Diversification does not ensure a profit or guarantee against loss. Investing in small cap stocks generally involves greater risks, and therefore, may not be appropriate for every investor. There are additional risks associated with investing in an individual sector, including limited diversification. Investments mentioned may not be suitable for every investor.