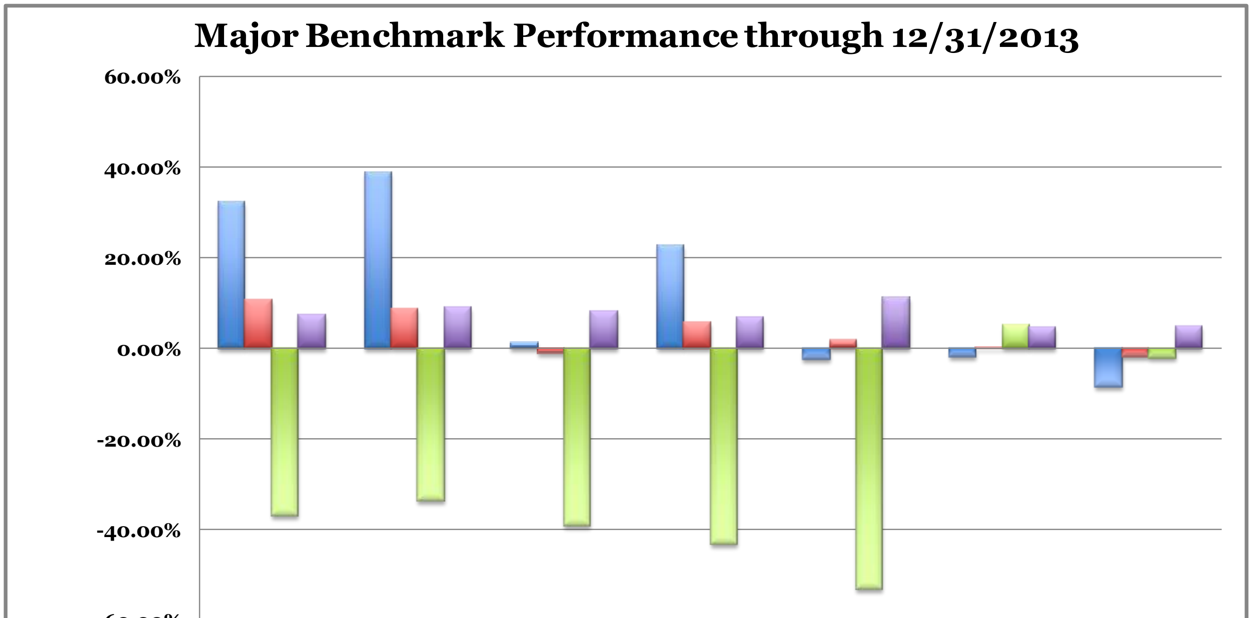
Market Summary and Outlook

4th Quarter 2013

2013 was a stellar year for US stocks. The S&P 500 was up over 11% in the final quarter, and over 32% for the year, the best showing in 16 years. US small cap stocks did even better with an almost 39% rise in 2013. Developed markets trailed US equities but were nonetheless up over 20% for the year. Other categories such as emerging markets, REITs and fixed income were flat or negative for the year. This was the first negative year for high quality fixed income since 1999, due mainly to the long anticipated increase in interest rates.

Below is performance for broad asset categories. We included performance for 2008, as well as for 10 year annualized, in order to remind you why we continue to recommend being invested in all categories of the market.



	S&P 500	US Small Cap	US REITs	Foreign Developed	Emerging Markets	US High Quality Bonds	TIPS
2013	32.39%	38.82%	1.22%	22.78%	-2.60%	-2.02%	-8.61%
4Q13	10.51%	8.72%	-1.09%	5.71%	1.83%	0.14%	-2.00%
2008	-37.00%	-33.79%	-39.20%	-43.38%	-53.33%	5.24%	-2.35%
10 Year (ann.)	7.41%	9.07%	8.22%	6.91%	11.17%	4.55%	4.86%

Source: DFA

It is hard to believe that investors started the 4th quarter apprehensive over the government shutdown. Though the shutdown lasted for 3 weeks and did wreak havoc over vast areas of the economy, the market accurately anticipated the resolution of budget and debt ceiling disagreements.

Fixed Income

US high quality fixed income experienced a rare downturn. After several years of predictions that interest rates would rise, they did increase in May and June. The 10 year Treasury bond yield went from a low of 1.6% to 2.5% in about a month, and increased to 3% by the end of the year. While increasing rates mean a drop in bond prices, we are still at historically low yields. An increase indicates that our economy is continuing to improve; this is also evident in lower unemployment numbers, better housing and factory orders data. Recent Federal Reserve actions indicate rates will increase in a controlled manner.

While it is disconcerting to have any negative performance in the perceived safe category of your portfolio, consider the following:

1) The high quality fixed income benchmark returned -2.02% in 2013. Compared with other down years for equity markets, -2% is a relatively small drop
2) Past performance is no guarantee of future performance; if there is unexpected shock to the markets in 2014, you will be happy to have high quality fixed income in your portfolios. Please refer to the graph on page 1 and specifically 2008 performance
3) Correlation with equities is low - meaning that when equities decrease, fixed income increases much of the time. Conversely, equities increased dramatically in 2013 and fixed income dropped slightly. Low correlation is something we want to see in portfolios, as we would not want every category to drop in a down market
4) If interest rates continue to rise slowly, some offsetting factors are the bond's yield as well as the fact that short term funds will have cash to buy cheaper bonds as the other bonds in the fund mature. Vanguard has written an informative paper which reflects our philosophy on keeping high quality bonds in your portfolio

A recap of well respected economist and pundit predictions for 2013 shows most of them were very wrong. For example, the consensus from a year ago predicted 2013 would be an uneventful year for stocks. While some respected industry figures are advising that investors dump high quality fixed income, we are skeptical of such advice, given how unsuccessful their previous predictions have been.

Our approach, as always, is to act in a slow and steady manner in order to meet your long term goals. If we look at mutual fund flows for two very broad categories, US equity and US taxable bonds, investors were leaving bonds and buying stocks in 2013. The data going back to the early 1990's shows investors generally chase returns, which we do not see as a good reason to drastically change a portfolio allocation. This is also why individual investors' portfolios consistently trail – because they are trying to time the markets.

Looking Forward

We expect to see continued modest economic growth in 2014 manifested by the following trends:

- Good GDP growth. 3rd quarter growth was an impressive 4.1%, up from 2.5% in the 2nd quarter

- A continued drop in unemployment (currently 7%)
- Housing continues to rebound
- US energy production is expanding
- The manufacturing sector is showing signs of revival
- Exports should increase as the world economies improve

We believe the Federal Reserve will continue to taper back its bond purchases although they will do so in a slow and controlled manner. Under the leadership of Janet Yellen, economists expect the Fed to keep short term interest rates near zero for 2014.

After having such a banner year in the stock market, it is statistically probable that we won't see those returns again in 2014. We hope we are wrong, but in the meantime, we advise you to maintain well diversified portfolios and focus on what you can control such as financial planning.

Nobel Prize in Economics

We would be remiss in neglecting to mention Professor Eugene Fama of the University of Chicago, who recently won the Nobel Prize in Economics for his work on the Efficient Markets Hypothesis. His research showing how markets absorb new information quickly in relation to share price provides the basis for our philosophy that individual investors cannot outperform the market, and should therefore invest in a diversified mix of mostly passive investments. As many of you know, Professor Fama is affiliated with Dimensional Fund Advisors, a very well respected provider of passive mutual funds. DFA is the 8th largest mutual fund family but is not well known by the public because they do not advertise. DFA funds are only available through approved advisors like IFS. Based on their diversified approach and low costs, their funds are included in most of our client portfolios. For more information on DFA, please either call us or refer to their website www.dfaus.com.

For **2014 tax information**, please refer to our website www.ifsplanners.com under "Suggested Reading".

We appreciate your continued confidence in us and encourage you to call anytime.

Janet & Barry

Sources: DFA, JP Morgan, Morningstar, WSJ, PIMCO, BlackRock, New York Times, Barrons