Chart of the Month

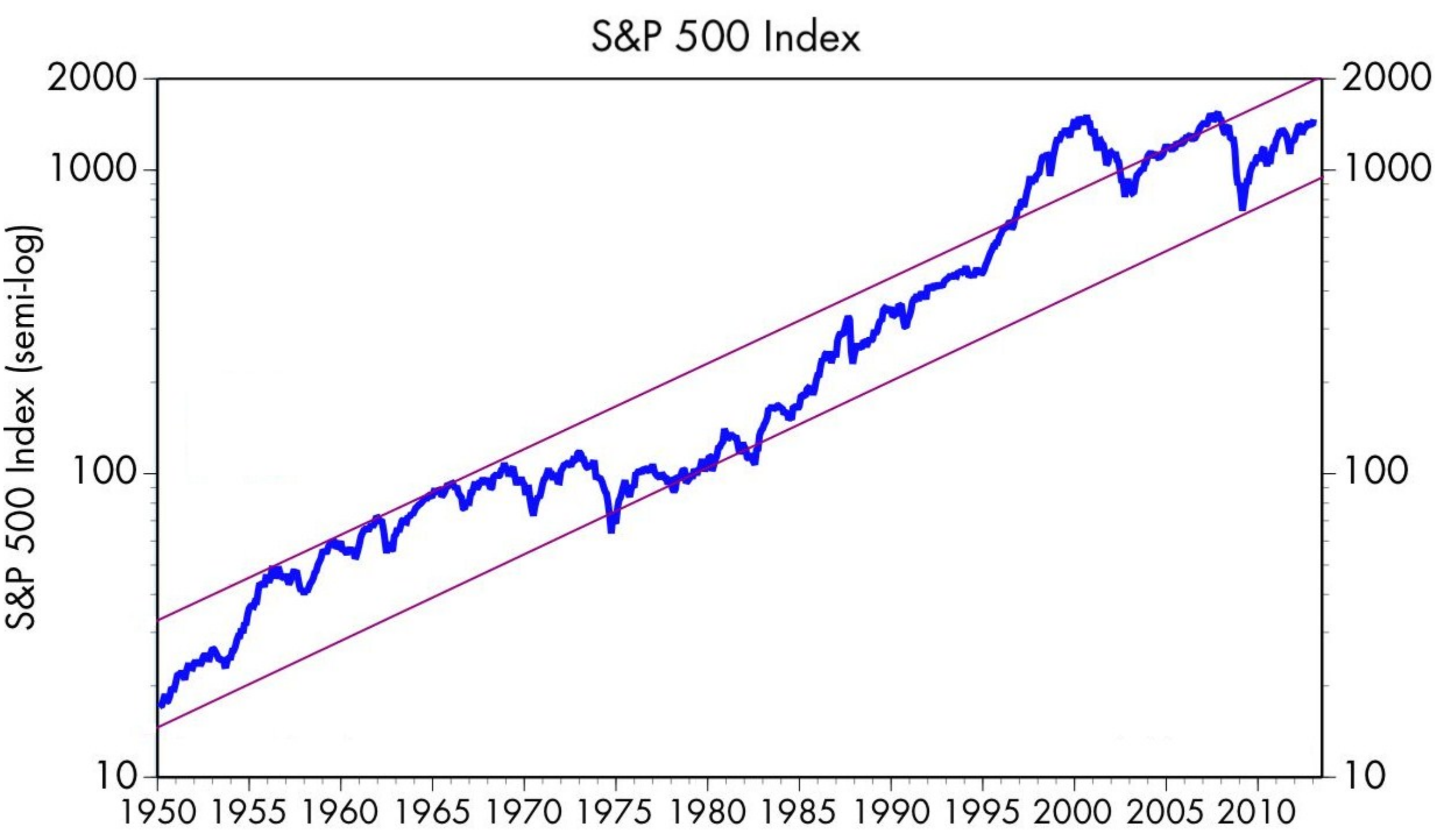
January 2013

We believe that the next leg of the bull market, which is about to celebrate its four-year anniversary in March, will be spurred by money rotating out of bonds and cash into stocks. Investors have been net buyers of fixed-income mutual funds and exchange-traded funds and net sellers of equity funds for each of the past five years. However, the Investment Company Institute estimates that investors put $23.6 billion more into stock funds than they withdrew during the first two weeks of January. As a result, it appears that the trend toward redemptions from stock funds may be in the early stages of reversal. Should this be the case, stock prices will likely benefit from the increase in demand, especially if the supply of outstanding shares continues to decrease due to the proliferation of corporate buybacks and the potential for an escalation in mergers and acquisitions.

While the downturn in 2008 was significant, it is important to note that the major stock market indexes have shown gains for nine of the past 10 years. In fact, the Dow Jones Industrial Average and the Standard & Poor's 500 are both within a few percentage points from their all-time highs.

As shown in the chart below, the S&P 500 is trading in the middle of its channel dating back to 1950. On the surface, it would seem as if stocks are fairly valued. In fact, at about 15x trailing earnings, the index is trading at roughly its average valuation. Therefore, stocks, on their own merits, are neither rich nor dear. Nonetheless, stocks are cheap when compared to alternative investments such as bonds and cash. The yields on the former are at historically low levels while checking, savings, and money-market funds are earning next to nothing.

Although stocks are not without risks, we believe they just may be the best-performing asset class going forward. Should the rise in stock prices keep pace with the trend line over the past 60-plus years, they will generate nearly 7% average annual capital appreciation and approximately 2% in dividend yield for a total return of just under 9%.



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