KINGS POINT
CAPITAL MANAGEMENT LLC

THE WORLD IS GETTING MORE UNPREDICTABLE – BUY STOCKS?

QUARTERLY REVIEW AND OUTLOOK

Through the first half of 2014, virtually every "expert" has been wrong with his or her interest rate forecasts as bond yields declined in the first six months. Moreover, Gross Domestic Product (GDP) turned negative in the fourth quarter of 2013 followed by a weak first quarter of 2014. Indeed, the IMF has cut full year 2014 economic growth to approximately 2.5% from the prior estimates of 3-4%. Projected global economic growth has also been reduced in recent weeks. Despite these reductions, the U.S. and to a lesser degree the global equity markets continue to grind higher. To complicate the picture further, consumer demand in the U.S. and Europe has dramatically slowed. Originally, this slowing in consumer purchases was blamed on the severe weather in the U.S. and Europe this past winter. While this was an impact, it is clear that consumer buying slowed for additional reasons.

The resilience in the global equity markets is impressive given the recent geo-political risks. While the Israel/Hamas fighting is disturbing, the markets appear to disconnect much of the risk of rising oil prices. More importantly, the recent Russian/Ukrainian problems now exacerbated by the downing of a commercial airliner, also seems to have little negative impact as well.

Importantly, geo-political issues don't really have a significant long-term negative impact on the global equity and fixed income markets. Rather, the global business cycle and its implications to job growth, economic prosperity and corporate profits are far more likely to impact stock prices over an economic cycle. Those key variables still point to a rising trend overall in the global economy.

Thus, we believe there are two distinct trends which are combining to move the equity market higher. First is that the global business cycle is slowly beginning to show signs of acceleration. Anecdotally, evidence from a number of large multinational companies supports this assumption. Secondly, corporate profits are rising at a slightly better rate of increase than originally expected. It now appears that corporate profits growth may average closer to 7-8% in 2014, versus the 4-5% expectations originally anticipated. Equities also appear to be fair to fully priced based on valuation. The stock market is trading at approximately 16 times projected profits for 2014. Given the current interest rate environment, valuation does not appear to be excessive.

As a result, we believe that equity appreciation over the near to intermediate term is more likely tied to earnings growth rather than valuations (P/E ratios) moving higher. If we assume 7-8% corporate profit growth, it suggests that the overall equity market has reached fair value near term.

Looking at the most recent set of companies reporting earnings, it appears that an economic recovery is likely. Key companies, such as Honeywell, JP Morgan, Microsoft and Kimberly-Clark are implying that global business on the margin continues to slowly recover. As we enter the second half of 2014, we are beginning to see most companies report good to strong results. Healthcare companies are particularly strong due to Obamacare. Technology and industrials are also reporting good overall profit growth. Only broad based consumer sensitive companies are reporting mixed results. Overall, however, corporate profits appear to be coming in a bit better than expectations. More importantly, we are seeing signs that European operations are either achieving or modestly exceeding general expectations. This gives us encouragement that economic trends are moving in the right direction on a global basis.

We expect consumer demand, both in the U.S. and in most overseas markets, to begin to improve as the year progresses. Aside from the easy comparisons against the severe weather issues in the fourth quarter of 2013, the political mid-term election should help Congress focus on creating a better job environment in the future. Thus, we enter the second half of 2014 with guarded enthusiasm that this bull market will continue (at a reduced pace of expansion) well into 2015.

The equity market has not had a 10% or larger correction in quite some time. We believe the combination of quantitative easing along with rising corporate profits were the two major factors creating this positive trend.

However, quantitative easing is likely to end by the fourth quarter of 2014. Should the U.S. continue to add jobs during this period, we suspect that interest rates could move higher as we enter 2015. This could potentially create an environment where a market correction could ensue. However, at this juncture, there is little evidence to support the beginning of a recession or bear market.

<u>Our Core Portfolio</u>

We continue to be focused on capital preservation in good times and bad. Thus, we do not tend to change the portfolio a great deal once we find the right equities for our clients. Our orientation toward consumer companies with good yields has created a headwind in short term performance due to the equity market's current focus on growth first and valuation second. Our more conservative approach tends to work well over a cycle. Regardless, the expected pickup in consumer demand in the next few months should have a very positive impact on our portfolio. Companies such as Newell Rubbermaid, Jarden, E-Bay and CBS should benefit from these expected trends.

We also tend to seek out companies that will benefit from the global improvement in the macro economy. Freeport McMoran, the world's largest copper producer and a big supplier of gold and oil is well positioned for such a trend. Within our financial positions, Starwood Properties and Brookfield Infrastructure Partners (a global investor in power generation, toll roads and other infrastructure assets) are also well positioned to benefit from any rising interest rates in the future. Overall, we also plan to add one or two new companies in the next few months as opportunities arise. On balance while the overall equity markets sit at fair value, we expect continued gains as the global economic environment begins to accelerate in late 2014 and into 2015.

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Fixed Income

As mentioned, the fixed income markets continued to rally as yields generally moved lower. While the Federal Reserve has reduced the amount of monthly purchases of treasuries and mortgages from $85 billion to $35 billion, the unanticipated drop on GDP (-2.9%) coupled with the additional stimulus programs via the ECB carried more impact. As such, the 10-year US Treasury hit 2.45% and remains near this depressed level. Yields for other fixed income securities have moved lower in concert. We continue to highlight specific opportunities in the High-Yield market as a complement to our short duration municipal portfolios. At some point in the next few quarters, we would expect rates to move higher as a result of better economic reports or the expected increase in the Federal Funds rate sometime during the summer of 2015. As such, we will maintain a relatively short duration and look for better opportunities in the coming quarters.

KPCM Update

We are pleased to announce two new members to the Kings Point Team:

Jason Beaird
Jason is Goldman alum from the Houston area where he served as an Investment Advisor in the Wealth Management Division. More recently, he was instrumental in helping to build a boutique institutional money management firm located in Tennessee. Jason joins us as an Investment Advisor.

Leah Jones
Leah joins our firm after serving as an Executive Assistant with the State of Tennessee and Southwind, A Division of The Advisory Board Company. She will assume the role of a Client Service Specialist for all the firm's clients.

We are always pleased to announce additions to the firm and new ways we can be of service to you. Do not hesitate to contact our offices as needed.

Jack L. Salzman
Senior Managing Partner

Jeffrey P. Bates
Managing Partner

John A. Marshall, IV CFA, CFP®
Investment Advisor

Beth C. Webb, CFP®
Investment Advisor

Nathan T. Fend
Investment Advisor