October 2, 2013

Dear Client,

I have recently been thinking a lot about concerns related to expected upcoming events and the effects on investment markets. More importantly, I am trying to gauge how much mental energy I should put into analyzing or forecasting the possible outcomes and placing probabilities on market impacts. I have come to a conclusion, but before I disclose it, I want to review the last year's list of uncertainties.

- A year ago, we were awaiting the outcome of the Presidential election.
- In December, there was concern over the fiscal cliff - the sequester, tax increases, debt limit increase.
- In March, Cyprus taxed bank deposits and anxiety arose about a possible run on other Euro banks.
- After the April Fed meeting, apprehension increased about a change in policy, known as the Taper.
- May saw a dramatic increase in interest rates, which triggered unease in the stock market.
- Courtesy of the Federal Reserve Bank, there was agitation about who would be the new Chairman.
- August and September have typically been difficult months in the stock market in recent years.
- A United States attack on Syria could well start a cascade of disruption in the Middle East.
- Germany is holding elections and Merkel's reign may end putting pressure on the Euro.
- Congressional divisions could lead to a partial Government shut down.
- Failure to raise the U.S. Government debt ceiling might prompt a default on debt payments.

Concerns about any of the items in the above list could be deemed reason to sell investments to mitigate the risk of market uncertainty. However, through each of these episodes the market has climbed higher. I have come to the conclusion that it makes sense to be informed about current events and to be prepared for possible outcomes, but in spite of this, attempting to forecast event outcomes and the impact on the market allows for two prediction errors, making it a fool's errand. Complex systems make it unlikely that an analyst could string together enough successful calculations to add value to an investment portfolio. And history shows that many market declines are the result of one-off events that were not even contemplated. Therefore, we need to accept that life and investment markets are uncertain and that forecasts and predictions are mostly to help us feel more comfortable, even if they are likely incorrect.

There are four guideposts I use to get comfortable investing capital in the markets, and I think it's a good time to reiterate them. First, I develop a general sense as to the attractiveness of the various assets classes as related to my individual client's needs. Second, I form an opinion as to the quality of the investment based on current and expected future cash flows available to the investor. Third, I analyze the price of the investment compared to those cash flows and alternatives. And finally, I evaluate the possibility of a permanent loss of capital. I hope this helps shed some light on my investment selection process.

Enclosed please find your most recent portfolio report. Year-to-date, the stock portions of portfolios are nicely higher and the bond positions are a fraction of a percent positive. Please call if you have questions, concerns or just want to catch up.

Best regards,

Peter V. Hedberg