



Third Quarter 2013

Review and Outlook

The third quarter of 2013 was a mostly repeat of the second quarter as far as stock market trends. The Dow Jones Industrial Average rose 1.5%, and is up 15.5% year-to-date. The Standard & Poor's 500 rose 4.7%, and is up 17.9% year-to-date. The NASDAQ Composite rose 10.8%, and is up 24.9% year-to-date. The Dow Jones Utilities Index is the only exception, declining 0.7%, with a year-to-date positive return of 6.4%. (Note that these are price-changes only for each index as of September 30, and do not include dividends.)

A review of the Barclays Bond indices indicates that bond prices declined, in some instances, precipitously. Although high-quality intermediate bonds declined 0.7%, high-quality long-term bonds plummeted 10.7%, while in the aggregate (taking into account most types of bonds), bonds declined 1.89%.

A survey of the major international markets reveals that stocks in the United Kingdom declined 3% for the quarter, but were up 3.2% after adjusting for currency changes. The German DAX index rose only 0.6%, though was up a 4.6% after adjusting for currency changes. The Japanese Nikkei Dow rose 14.9%, and was up 15.7% after adjusting for currency changes. Year-to-date, those markets rose 9.6%, 12.9% and 39.8%, respectively, in their local currencies.

Moving to currency changes, the dollar declined 6.0% vs. the U.K. pound, declined 3.8% vs. the euro, and declined 0.7% vs. the Japanese yen. Year-to-date, the dollar was up vs. the U.K. pound by 0.3%, down 2.4% vs. the euro and up 13.5% vs. the yen.

Gold increased in value, unlike in the second quarter, and was up 11.3%. However, through the end of September, gold is still down 20.4% for the year. Oil prices rose 6% in the third quarter, while natural gas declined 1.2%. Year-to-date, oil prices rose 11.4%, while natural gas rose 3.3%.

Domestic Stock and Bond Market Outlook

I waited a few days to release this newsletter, in the hopes that some solution to the impasse between President Obama and the Congress would occur. As of this writing, there has been no agreement, but the sides are talking.

Just a mere get together at the White House between the President and the Democrats and Republicans in Congress caused the market to rally over 300 points. I suspect that the stock market weakness in the weeks leading up to October 1 (the start of the new fiscal year for the Federal government) was related, at least in part, to the uncertainty associated with the lack of a Continuing Resolution and the looming threat of bumping up against the debt ceiling.

The stock market so far has experienced some choppy action – the first day of the Federal government shutdown, the market was up. But later on in the week, the stock market declined. How much of this is associated with the turmoil in Washington, D. C. is not determinable, but at least some of the stock market's action is associated with it.

Companies that export to other countries and import raw materials and finished products to the U.S. are finding that the various Federal agencies (which number 40) have shut down for business, so cargo can't move. There is also debate on who will get paid (or not). This affects not only government workers, but employees of companies that do business with the Federal government (e.g. defense contractors, food companies, etc.). No money in the bank means less spending by consumers, which will also be a shock to the economy. Sometimes, spending delayed today is spending that never happens in the future.

As this stalemate drags on, the economic effects will become quickly apparent. It is estimated that the growth rate for the fourth quarter will decline about 0.2% for every week of the government shutdown.

We should also note that emerging markets will be vulnerable to the US Government's shutdown, so I suspect that we will see weakness in that area of the stock market.

After the bond markets reacted poorly to Ben Bernanke's suggestion that at some point, the Federal Reserve Board's bond buying program would taper off, Mr. Bernanke stepped back from those comments. When he did so, the bond market stabilized somewhat. However, at some point, reducing the bond buying program will be an inevitability. The question is not if, but when.

The recent announcement that Janet Yellen is President Obama's pick as new Fed Chair is a positive for the bond market near term, as she is well known to be a proponent of easy money.

Bond yields should rise eventually to reflect a more normal real yield. Along with rising bond yields, we will see bond prices decline and punish anyone who has placed money in the bond market.

Real yields are those that an investor receives after taking into account underlying annual inflation. For example, the 30 year US Treasury typically trades at a real yield of about 3%. The latest inflation rate (as measured by the Consumer Price Index (CPI)) is between 1.5-2.0%. Adding those figures to the 3% real yield, investors should expect the 30 year US Treasury Bond to be yielding between 4.5-5.0%. As of today (October 11), the 30 year US Treasury Bond yields 3.74%, a difference of between 0.75-1.25%.

The current Duration of the 30 year US Treasury is about 18. The definition of Duration is: How much will a bond's price fall (or rise) with a 1% increase (or decrease) in market interest rates. With a difference between 0.75% and 1.25%, investors can expect the price of a 30 year US Treasury to fall between 13.5% and 22.5%. And that is before you factor in that the inflation rate has been near historic lows and could rise!

If you invest in bonds, it is wiser to invest in short term bonds (no more than, say five years to maturity). Avoiding bond mutual funds would be a wise decision. The reason is simple: with individual bonds, the bonds will eventually mature. Even if interest rates increase, you will receive a return of principal equal to the face value of the bond as long as the issuer does not default (fail to pay back the principal amount). However, if you invest in a bond fund, the fund does not ever have a maturity date. So you may lose principal value in your bond fund that you may never get back, even if you decide eventually to sell the bond fund.

Stock valuations look rather full, and even with the modest market declines, stocks do not present great value. There may be selected stocks here and there, but we are not unduly enthusiastic about stocks over the near term, even if President Obama and the Congress hammer out an agreement to allow the government to re-open for business. Energy, Materials, Utilities and Telecommunications Services sectors seem to be the most fertile areas to explore for stock purchases.

Investment Strategy

- We are watching for a reasonable entry point into the fixed-income market, and for now, prefer to buy short term bonds to avoid big declines in bond values should interest rates rise. In fact, for many of our clients, we are keeping cash in money market funds, rather than in short term U.S. Treasury Notes, to preserve investment flexibility. We are also keeping some cash on the sidelines as well as selling stocks that we no longer want to hold, while searching for purchase candidates.
- We will emphasize high-quality bonds (A-rated or better) when buying bonds for clients is appropriate. We have in the past purchased preferred stocks and lower-

quality bonds for income on a limited basis, but only when the risks associated with these types of securities appear reasonable.

- While we may buy bonds from time to time, our emphasis will be on finding quality stocks that will provide a steady, or even rising, stream of dividends for our income-oriented investors. We will be on the lookout for companies with strong financial strength and the ability to raise their dividends.
- Occasionally, there may be interesting stocks that are either undervalued or have huge long-term growth potential that we purchase to boost clients' investment returns but may pay no dividends, or almost no dividends.
- We are looking at the "baby bear" sector of the stock market for suitable stocks that may be less vulnerable to changes in bond yields. (We define "baby bear" stocks as those with mid-range dividend yields.)
- We believe that a long-term strategic position in Materials and Energy stocks is appropriate. We are keeping an eye on China and emerging markets as signs of economic weakness (in China) become increasingly evident, as well as commodity prices.
- We believe that a rise in stock prices will generally be tied to improvements in corporate earnings; and there will be bumps in the road in a generally, though modestly, rising stock market.
- *We believe that this is a stock-picker's market that favors active management of sector weights and is unfavorable to index funds.*
- We will sell stocks when (1.) they appear to be overvalued, (2.) substitution of a stock in one industry sector for another makes sense in order to de-emphasize industry sectors in which there may be fundamental weakness and (3) when it makes sense to increase cash or bonds in a client's portfolio and to de-emphasize stocks.
- In 2012, we saw the beginnings of a reversal of fortune, with high-yielding stocks no longer outperforming, and indeed, starting to trail the market averages. Too, recent tax law changes have reduced the attractiveness of dividends versus capital gains. Investors with high income requirements should come to expect that we may be in for a period of underperformance in stocks paying above-average dividends. Still, investors should consider their goals, first and foremost, and not try to chase market returns, which are notoriously volatile.

Disclosure of Current Individual Stock Holdings

Individual stock holdings in accounts in which I have a direct beneficial interest is noted below. Stocks in *italics* are held in the accounts of a family member. The activity is current as of October 11, 2013.

Holdings:

A T & T Inc.

Altria Group, Inc.

Annaly Capital Mgmt.

Apache Corporation

Bank of America

Baxter International, Inc.

Berkshire Hathaway Cl. B.

CVX Corporation

Canadian Natural Resources

Canadian Pacific Railway Ltd.

Chevron Corporation.

Cisco Systems, Inc.

Conagra

Costco

Cullen Frost Bankshares

Cummins, Inc.

Dominion Resources Inc.

Duke Energy Corp.

eBay, Inc.

Enbridge, Inc.

Ford Motor Company

Immersion Corp.

Intuitive Surgical

Kansas City Southern

Kimberly-Clark Corp.

Lincoln National Corp.

Mac-Cali Realty Corp.

McDonald's

Merck & Co. Inc.

MetLife, Inc.

MTS Corporation

Newmont Mining Corp.

Norfolk Southern Corp.

Patriot Coal Corp.

PepsiCo Incorporated

PetSmart

Pfizer Incorporated.
Philip Morris International, Inc.
Potash Corp.
Qualcomm, Inc.
Range Resources
Rio Tinto PLC Spon. ADR
Schlumberger Ltd.
Spectra Energy (Added)
Target Corporation
The TJX Companies, Inc.
Verizon Communications
Vertex Pharmaceuticals
Wells Fargo & Co., Inc.
Whiting Petroleum Corp.

New purchases include Alexandria Real Estate Equities, Conagra, eBay, Immersion Corp., MTS Corp., Realty Holdings Corp. and Vertex Pharmaceuticals. Eliminations include Mac-Cali Realty Corp., and Target Corporation.

Offer of Form ADV: As always, clients are welcome to request our form ADV, Parts 2A and 2B.

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October 11, 2013

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Labrador Investments, LLC
Financial Market Trends
September 30, 2013

U.S. Treasury Yields	6/30/13	9/30/13	3rd Qtr. Change	12/31/2012	Yr.-to-Date Change
90 day T-Bill	0.04%	0.02%	-0.02%	0.05%	-0.03%
2 Year T-Note	0.36%	0.33%	-0.03%	0.25%	0.08%
10 Year T-Note	2.49%	2.62%	0.13%	1.76%	0.86%
30 Year T-Bond	3.50%	3.69%	0.19%	2.95%	0.74%

Stock Market Indices	6/30/13	9/30/13	3rd Qtr. Change	12/31/2012	Yr.-to-Date Change
Dow Jones Industrial Average	14909.6	15129.67	1.5%	13104.14	15.5%
Standard & Poor's 500	1606.28	1681.55	4.7%	1426.19	17.9%
Nasdaq Composite	3403.25	3771.48	10.8%	3019.51	24.9%
Dow Jones Utility Index	485.9	482.29	-0.7%	453.09	6.4%

Bonds Market Indices		Yr.-to-Date Change
Barclays Corporate Intermediate		-0.74%
Barclays Corporate Long Term		-10.71%
Barclays Aggregate		-1.89%

Foreign Stock Markets	6/30/13	9/30/13	3rd Qtr. Change	3rd Qtr. Currency Adjusted	Year To Date
FTSE100 (United Kingdom)	6215.47	6462.22	-3.0%	3.2%	9.6%
DAX (Germany)	7959.22	8594.4	0.6%	4.6%	12.9%
Nikkei Dow (Japan)	13677.32	14528.9	14.9%	14.1%	39.8%

Foreign Currencies	6/30/13	9/30/13	3rd Qtr. Dollar's Perf.	12/31/2012	Year To Date
British Pound (\$/Pound)	1.5211	1.6189	-6.0%	1.6242	0.3%
Euro (\$/Euro)	1.301	1.3521	-3.8%	1.3196	-2.4%
Japanese Yen (Yen/\$)	99.15	98.47	-0.7%	86.765	13.5%

Commodities	6/30/13	9/30/13	3rd Qtr. % Change	12/31/2012	Year To Date
Gold Spot Price/Oz.	\$ 1,192.00	\$ 1,326.50	11.3%	\$ 1,667.48	-20.4%
West Texas Int. Crude Oil/bbl	\$ 96.56	\$ 102.33	6.0%	\$ 91.82	11.4%
Natural Gas	\$ 3.56	\$ 3.52	-1.2%	\$ 3.40	3.3%

Labrador Investments, LLC
Focus and Holdings List
September 30, 2013

NAME	06/30/13	09/30/13	% CHANGE	YIELD
CF Industries Holdings, Inc.	\$ 171.50	\$ 210.83	22.9%	0.8%
E. I. du Pont de Nemours and Company	\$ 52.50	\$ 58.56	11.5%	3.1%
Freeport-McMoRan Copper & Gold Inc.	\$ 27.61	\$ 33.08	3.8%	3.7%
Nucor Corporation	\$ 43.32	\$ 49.02	0.0%	3.0%
Praxair Inc.	\$ 115.16	\$ 120.21	0.0%	2.0%
Rio Tinto plc	\$ 41.08	\$ 48.76	18.7%	3.4%
Weyerhaeuser Co.	\$ 28.49	\$ 28.63	0.5%	3.0%
CSX Corp.	\$ 23.19	\$ 25.74	11.0%	2.3%
Eaton Corporation plc	\$ 65.81	\$ 68.84	4.6%	2.4%
Fluor Corporation	\$ 59.31	\$ 70.96	19.6%	0.9%
General Electric Company	\$ 23.19	\$ 23.89	3.0%	3.2%
Honeywell International Inc.	\$ 79.34	\$ 83.04	4.7%	2.0%
Illinois Tool Works Inc.	\$ 69.17	\$ 76.27	10.3%	2.2%
Kansas City Southern	\$ 105.96	\$ 109.36	3.2%	0.8%
The Manitowoc Company, Inc.	\$ 17.91	\$ 19.56	9.2%	0.4%
Norfolk Southern Corporation	\$ 72.65	\$ 77.35	6.5%	2.7%
Union Pacific Corporation	\$ 154.28	\$ 155.34	0.7%	2.0%
AT&T, Inc.	\$ 35.40	\$ 33.82	-4.5%	5.3%
Frontier Communications Corporation	\$ 4.05	\$ 4.18	3.2%	9.3%
Verizon Communications Inc.	\$ 50.34	\$ 46.67	-7.3%	4.5%
Darden Restaurants, Inc.	\$ 50.48	\$ 46.29	-8.3%	4.7%
Ford Motor Co.	\$ 15.47	\$ 16.87	9.0%	2.3%
Frisch's Restaurants, Inc.	\$ 18.66	\$ 24.13	29.3%	3.0%
The Home Depot, Inc.	\$ 77.47	\$ 75.85	-2.1%	2.1%
Leggett & Platt, Incorporated	\$ 31.09	\$ 30.15	-3.0%	4.0%
Lowe's Companies Inc.	\$ 40.90	\$ 47.61	16.4%	1.5%
McDonald's Corp.	\$ 99.00	\$ 96.21	-2.8%	3.3%
Target Corp.	\$ 68.86	\$ 63.98	-7.1%	2.7%
Tractor Supply Company	\$ 58.78	\$ 67.17	14.3%	0.8%
V.F. Corporation	\$ 193.06	\$ 199.05	3.1%	1.8%
Wal-Mart Stores Inc.	\$ 74.49	\$ 73.96	-0.7%	2.5%
Walgreen Co.	\$ 44.20	\$ 53.80	21.7%	2.3%
Altria Group Inc.	\$ 34.99	\$ 34.35	-1.8%	5.5%
Anheuser-Busch InBev SA/NV	N/A	\$ 99.20		1.9%
The Coca-Cola Company	\$ 40.11	\$ 37.88	-5.6%	2.9%
ConAgra Foods, Inc.	N/A	\$ 30.34		3.3%
Flowers Foods, Inc.	\$ 22.05	\$ 21.44	-2.8%	2.1%
The J. M. Smucker Company	\$ 103.15	\$ 105.04	1.8%	2.2%
Kellogg Company	\$ 64.23	\$ 58.73	-8.6%	3.1%
Kimberly-Clark Corporation	\$ 97.14	\$ 94.22	-3.0%	3.4%
Pepsico, Inc.	\$ 81.79	\$ 79.50	-2.8%	2.8%
Philip Morris International, Inc.	\$ 86.62	\$ 86.59	0.0%	4.3%
The Procter & Gamble Company	\$ 76.99	\$ 75.59	-1.8%	3.1%
Reynolds American Inc.	\$ 48.37	\$ 48.78	0.8%	5.1%
BP plc	\$ 41.74	\$ 42.03	0.7%	5.0%
Canadian Natural Resources Limited	\$ 28.26	\$ 31.44	11.3%	1.5%
Cenovus Energy Inc.	\$ 28.52	\$ 29.85	4.7%	3.1%

Chevron Corporation	\$ 118.34	\$ 121.50	2.7%	3.3%
Encana Corporation	\$ 16.94	\$ 17.33	2.3%	4.6%
Exxon Mobil Corporation	\$ 90.35	\$ 86.04	-4.8%	2.9%
National Oilwell Varco, Inc.	\$ 68.90	\$ 78.11	13.4%	1.3%
Range Resources Corporation	\$ 77.32	\$ 75.89	-1.8%	0.2%
Stone Energy Corp.	\$ 22.03	\$ 32.43	47.2%	
American Express Company	\$ 74.76	\$ 75.52	1.0%	1.2%
Annaly Capital Management, Inc.	\$ 12.57	\$ 11.58	-7.9%	12.0%
Cullen/Frost Bankers, Inc.	\$ 66.77	\$ 70.55	5.7%	2.9%
Equity Residential	N/A	\$ 53.57		2.9%
Fifth Third Bancorp	\$ 18.05	\$ 18.05	0.0%	2.7%
Liberty Property Trust	\$ 36.96	\$ 35.60	-3.7%	5.3%
Mack-Cali Realty Corp.	\$ 24.49	\$ 21.94	-10.4%	5.5%
Sun Life Financial Inc.	\$ 27.29	\$ 31.97	17.1%	4.2%
The Toronto-Dominion Bank	\$ 80.37	\$ 89.98	12.0%	3.7%
U.S. Bancorp	\$ 29.62	\$ 36.58	23.5%	2.5%
Vornado Realty Trust	\$ 82.85	\$ 84.06	1.5%	3.5%
Wells Fargo & Company	\$ 41.27	\$ 41.32	0.1%	2.9%
Abbott Laboratories	\$ 34.88	\$ 33.19	-4.8%	1.7%
AbbVie Inc.	\$ 41.34	\$ 44.73	8.2%	3.6%
Amgen Inc.	\$ 98.66	\$ 111.93	13.5%	1.7%
Baxter International Inc.	\$ 69.27	\$ 65.69	-5.2%	3.0%
Bristol-Myers Squibb Company	\$ 44.69	\$ 46.28	3.6%	3.0%
Hospira Inc.	\$ 38.31	\$ 39.22	2.4%	
Intuitive Surgical, Inc.	\$ 506.13	\$ 376.27	-25.7%	
Johnson & Johnson	\$ 85.86	\$ 86.69	1.0%	3.0%
Eli Lilly and Company	\$ 49.12	\$ 50.33	2.5%	3.9%
Medtronic, Inc.	\$ 51.47	\$ 53.25	3.5%	2.1%
Merck & Co. Inc.	\$ 46.45	\$ 47.61	2.5%	3.6%
Meridian Bioscience, Inc.	\$ 21.50	\$ 23.63	9.9%	3.2%
Pfizer Inc.	\$ 28.01	\$ 28.73	2.6%	3.3%
St. Jude Medical Inc.	\$ 45.63	\$ 53.64	17.6%	1.9%
Teva Pharmaceutical Industries Limited	\$ 39.20	\$ 37.78	-3.6%	2.9%
Vertex Pharmaceuticals Incorporated	\$ 80.06	\$ 75.82	-5.3%	
Zimmer Holdings, Inc.	\$ 74.94	\$ 82.14	9.6%	1.0%
Immersion Corporation	N/A	\$ 13.20		
Intel Corporation	\$ 24.23	\$ 22.92	-5.4%	3.9%
Microsoft Corporation	\$ 34.54	\$ 33.28	-3.6%	3.4%
MTS Systems Corporation	\$ 56.60	\$ 64.35	13.7%	1.9%
Texas Instruments Inc.	\$ 34.85	\$ 40.29	15.6%	3.0%
American Electric Power Co., Inc.	\$ 44.78	\$ 43.35	-3.2%	4.5%
Dominion Resources, Inc.	\$ 56.82	\$ 62.48	10.0%	3.6%
Duke Energy Corporation	\$ 67.50	\$ 66.78	-1.1%	4.7%
Entergy Corporation	\$ 69.68	\$ 63.19	-9.3%	5.2%
Exelon Corporation	\$ 30.88	\$ 29.64	-4.0%	4.2%
NextEra Energy, Inc.	\$ 81.48	\$ 80.16	-1.6%	3.3%
Spectra Energy Corp.	\$ 34.46	\$ 34.23	-0.7%	3.6%

Notes:

Added: Anheuser-Busch InBev, ConAgra, Equity Residential, Immersion Corp.