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Thank you for your continued confidence and feedback. As always, we encourage you to share this newsletter with friends, family members and colleagues.

Mid-Quarter Outlook

By John M. Silvis, CFA

Director of Investments

The U.S. economy continues its slow grind forward as growth remains anemic, registering Gross Domestic Product (GDP) growth of only 1.5% in the recently completed second quarter. Unemployment remains high, hovering above 8%, and wage growth has been stagnant for the last several years. After observing weaker economic data over the last few months, we are starting to see signs that the economy may be weathering the storm. The non-farm payroll number for the month of July came in at 163,000 new jobs, beating expectations of Wall Street economists for the second month in a row. Weekly unemployment claims, which tend to be more of a coincidence indicator, have resumed their down trend after spiking earlier in the summer. Retail sales posted a five month high in July, as consumers indicate they are willing to do their part to help the economy in spite of the weaker news of the past few months.

The housing market, which could be a catalyst for better economic growth in the months and years ahead, appears to be creating a true bottom. Several indicators have shown signs of improvement led by a Case-Shiller Home Price Index which increased 2.2% in May. Housing starts in the month of June increased 6.9%, hitting a three and a half year high, far exceeding analyst estimates. Confidence among home builders continues to improve, with sentiment hitting its highest level since February of 2007.

Domestically, inflation has been held relatively in check with the Consumer Price Index (CPI) coming in at an annual rate of 1.4% in the month of July. This should give the Federal Reserve and Chairman Bernanke more flexibility to react to any weaker data in the weeks ahead. All eyes now shift to his annual speech in Jackson Hole, WY at the September meeting of the FOMC at the end of the month to see if he lays the groundwork for more quantitative easing, most likely in the form of additional bond purchases. With a rising equity market and slightly better current economic data, expectations remain fluid as to if they will embark on QE3. Either way, the Fed remains committed to keeping rates low for the foreseeable future as the economy grinds higher in a low growth, low rate environment.

Fairport Global Asset Allocation

Globally, all eyes remain on Europe, as yields on both Spanish and Italian debt remain elevated above levels that many considered unsustainable. Greece and the rest of the periphery continue to struggle with austerity measures while the ranks of the unemployed throughout the region continue to climb higher. The Eurozone economy is sliding toward a recession as GDP contracted by -0.2% in the second quarter, saved from a worse fate only by the fact that Germany's economy posted positive GDP growth of 0.3% in the second quarter. The situation in Europe still has no sustainable path to a long term resolution. However, Mario Draghi, the president of the European Central Bank (ECB), recently bolstered the global capital markets with his comments to do "whatever it takes" to preserve the euro. We believe this will lead to more decisive action from the Eurozone members and the ECB in the coming months.

The MSCI EAFE Index, an international benchmark, was up 3.51% at the midway point of the third quarter and 6.57% year-to-date. We remain underweight Europe and Japan versus the benchmark, as both continue to struggle with stagnant economic growth.

Emerging Markets should see better prospects as we move into the second half of the year. Central banks globally have all moved to easing monetary policy. We have seen interest rate cuts recently from China, India, Brazil and South Korea. This should stimulate better economic growth going forward to combat the global slowdown that is currently plaguing their countries. Inflation in China continues to ease, giving the central bank the ability to be more flexible in the months ahead. An analyst that we follow closely believes the Chinese government will act more aggressively to combat the slow growth in China, and predicts at least two more interest rate cuts by year end. We still believe the Chinese economy will execute a soft landing, GDP growth of 5% or more, over the next few quarters.

Fairport Large Cap

The domestic equity market, led by the S&P 500 Index, looks to challenge their high mark established in early April. At the midway point of the third quarter (August 15th), the S&P 500 Index was up 3.51% for the quarter and 13.34% year-to-date. As we near the end of the second quarter reporting season, earnings came in pretty much as expected with over 66% of companies beating expectations which is in line with historical norms. Most analysts still expect S&P 500 earnings for the year to reach new highs, although some have lowered expectations in response to the overall global uncertainty. We continue to believe that the fundamental outlook for equities remains positive and multiples remain attractive. We continue to tilt towards the cyclical sectors such as Industrials and Technology and maintain our underweight in Utilities. Large caps should remain in a leadership role, as strong balance sheets and global exposure to emerging markets help drive growth going forward. In the short term, the current rally is looking overbought and the market is due for some type of correction in the coming weeks. In an election year, history would tell us any correction at this point should be somewhat shallow opening up a better opportunity heading into the seasonally strong fourth quarter.

Fixed Income Commentary

Emerging market local currency debt has narrowly outpaced high yield as the best performing fixed income sector year-to-date, returning 9.38% vs. 9.31% through July. Investment grade debt has posted strong year-to-date performance as well, returning 7.67% over the same period. While absolute yields across fixed income remain historically depressed, we continue to favor credit related sectors relative to Treasuries due to higher yields and more palatable durations. Underlying fundamentals in the high yield space remain sound as evidenced by the current annual default rate of 2.0%, well below the sector's historical default rate of 4.0%. That being said, we remain watchful as many new issue terms are becoming less attractive, with covenant-lite and call constrained deals becoming the norm. Other higher yielding asset classes such as preferred stocks or floating-rate bank loans are constantly under consideration; however, our philosophy has been to remain selective regarding the amount of risk taking in our fixed income portfolios. Many of these higher yielding asset classes tend to have a higher correlation to equities, providing little diversification at the time when you most need it.

We don't expect a prolonged increase in rates given the Fed's current stance; however, it is interesting to note that since July 24th, the price of the 10-year Treasury note is down 3.75%, essentially wiping out two years worth of coupon payments. Interestingly enough, the beginning of the back-up in yields coincided with ECB President Draghi's pledge that the ECB would do "whatever it takes" to save the euro.



Welcome to the Fairport Team!

Earlier this month, we announced Jonathon McAwley's appointment as advisory member of Fairport's Investment Committee. Jonathon currently serves as PPG Industries' Director, Benefits Investment and Financing with responsibility for the investment activity of the U.S. defined benefit and defined contribution plans and oversight of international plans in Canada, the U.K., and the Netherlands with assets totaling over \$7 billion.

"I am really looking forward to having Jonathon join the committee. In his role of Director, Benefits Investment and Financing at PPG he is aware of the challenges facing both U.S. and European pension management," said J.T. Mullen, Fairport's Chief Investment Strategist. "I believe his perspective will be an excellent addition to the investment committee." [Click here to read more.](#)

Fairport News

Fairport believes in supporting the community as a company and through encouraging employees to participate and hold leadership positions in charitable, professional and community organizations. Read about our most recent community involvement.

The Holden Arboretum in Kirtland named **Paul Abbey** as its new Board Chairman. Paul serves on Holden's Development and Finance and Investment committees and is chairman of Holden's New Leaf capital campaign. The Holden Arboretum is an outdoor living museum that promotes the beauty and importance of trees and other woody plants to create sustainable and healthy communities in the Great Lakes region and beyond.

Ken Coleman was recognized for his contributions to Midtown's revitalization with the Leadership Award at the Annual Meeting of Midtown Cleveland, Inc. in June. He was awarded the distinction for his passion and vision over the last two years as he served as Board Chairman. As his term has concluded, he remains on the Board as Vice-Chair.

Andrew Connors recently completed the 10-month leadership development and civic engagement program, Cleveland Bridge Builders. Participants develop their civic leadership capacity through a highly interactive curriculum including individual leadership assessments, small group discussion, presentations from community leaders, engagement in team projects and review of best practices in leadership across sectors.

Last week, over 1000 industry professionals across the country participated in an *Investment News* webcast featuring **Heather Ettinger**. Heather was one of three panelists asked to participate in a discussion on attracting women clients. In addition to sharing her strategies, Heather expertly answered questions received from the audience. Her reputation as a subject matter expert was further illustrated when she was quoted in several *Investment News* articles subsequent to the webcast.

Laurel Lawrence coordinated another employee volunteer trip to the Bishop Cosgrove Hunger Center in July. **Laurel, Ken Coleman, Kendall Exline, Erin Fleming, Kristen Gall, Chris Isabella** and **Rachel Margulis** worked in the kitchen to help serve over 200 homeless or working poor individuals during the lunch hour. The Bishop Cosgrove Center is the largest day drop-in center in our community, serves approximately 500 meals in any given day (breakfast and lunch) and provides food bags through their pantry program. This is Fairport's second trip to the center and Laurel hopes to continue to schedule additional opportunities for more employees to get involved.

J.T. Mullen was a presenter on multiple webinars this summer sponsored by the Kansas Association of Community Foundations. Topics included roles and responsibilities for investment management within community foundations and the role of the audit in addressing the financial responsibilities of trustees.

John Silvis has been appointed Treasurer of the CFA Society of Cleveland for the 2012-13 term.

Fairport Continuing Education

Fairport employees frequently attend conferences, continuing education seminars and informational webinars to keep up-to-date with new strategies and industry trends relating to the wealth management needs of our clients. From investment management to client service to technology, read more about the conferences we've recently attended.

In July, **Andrew Connors** attended the Greater Cleveland Middle-Market Forum presented by GCP. The goal of this half-day event was to connect middle-market CEOs with meaningful data on the middle market. In addition, forum attendees engaged in thought-provoking discussions with middle-market CEOs who are leading the way in talent, innovation, globalization, customer focus and culture.

Heather Ettinger attended the Schwab EXPLORE conference in June and met with the members of the Family Wealth Advisors Council (FWAC) in Portland in August.

Later this week, **Kristen Gall** will be attending the 2012 Social Media Conference for Financial Services in Boston. Participants will meet to examine best practices for growing market share and enhancing service using social media.

John Silvis kept current on investment and asset allocation strategies by attending the Morningstar Investment Conference in June in Chicago. One of the industry's most respected annual events, the conference focuses on providing advisors with knowledge, insights, and resources by addressing key financial topics, investment strategies, and perspectives on the economy.

Paul Zappala attended the Schwab SOLUTIONS 2012 Conference in Columbus in August. The annual SOLUTIONS workshop trains attendees how to best utilize Schwab technologies and tools to streamline workflow and help deliver exceptional client service.

Newsletter Disclosures

This newsletter represents an assessment of the economic and market environment at a specific moment in time and is not intended to be a forecast of future events or any guarantee of future results. It is for informational purposes only and should not be relied upon as research or investment/financial planning/tax advice. It should not be considered as a solicitation or recommendation by Fairport to buy, sell or continue to hold securities or other investments. Past performance is not a guarantee of future results, and is not indicative of any specific investment. It should not be assumed that the investment process and strategy discussed herein has been or will prove to be profitable. Diversification and strategic asset allocation do not assure profit or protect against loss in declining markets.

