APPLETON PARTNERS, INC.

QUARTERLY MARKET OVERVIEW
QIV 2013

For many, 2013 will be remembered as the year of the taper. The Fed's decision on whether or not to scale back asset purchases dominated trading in both equity and fixed income markets for most of the year. Both stocks and bonds sold off in the summer when Fed Chairman Bernanke first mentioned the mere prospect of tapering, and rallied in September when the "dreaded" taper was put on hold. In December, by the time Bernanke and the Fed announced their decision to reduce their asset purchases by $10 billion, or a mere 12%, most investors welcomed the news. Stocks took another leg up to continue the rally, as the S&P 500 ended the year with a total return of 32.39%. Bonds sold off moderately to end the year, but nothing like what they experienced in May and June when the 10-Year yield increased almost a full point in two months. Although the yield on the 10-Year Treasury was approaching the key 3% level, the speed of the move made all the difference. The steady move up throughout the fourth quarter was much more palatable for investors than the breakneck pace seen six months earlier. Municipals, as measured by the Barclays Managed Money Municipal Short/Intermediate Index, finished at -0.60% for the year, and taxable bonds, as measured by the Merrill Lynch US Corp/Gov't 1-10 Year A or Better Index, finished -1.21%.

Stocks slumped to start the fourth quarter as the debt ceiling spectacle played out in Washington. As was the case most of the year, however, the dip proved to be a buying opportunity as the stock market rallied to close the year at an all-time high, only the fifth time that has happened since 1930. Cyclical sectors, such as Industrial and Consumer Discretionary, led the way in the fourth quarter and finished the year among the top performing of the index. We continue to favor these sectors as the global economy slowly recovers, and believe that a number of positive catalysts potentially remain. Valuation levels on stocks have risen and no longer can be considered cheap, though by no means expensive either. We expect a pickup in M&A activity as company management looks to make deals ahead of a potential increase in their cost of capital should interest rates rise. The IPO market picked up noticeably in 2013, and we believe that will continue into 2014. In our last letter, we mentioned the remarkable increase in money returned to shareholders through buybacks and dividends as a tailwind for stocks. We believe that this will continue to be the case, but look for company management to hopefully redirect some of their stockpiled cash back into their businesses as they move beyond some of the uncertainties of 2013, and look to bolster top-line growth.

The fixed income markets spent most of 2013 hyper-focused on the Fed's action, or lack thereof. As inflation remained benign and unemployment data began to gain steam in the second half of the year, the Fed felt comfortable enough to begin a staged tapering of its open market asset purchases. With the start of the taper and continued dovish forward guidance on short-term rate policy, we expect some steepening of the yield curve in 2014. In the municipal market, we expect favorable supply and demand dynamics to provide some stability. While there will be limited, "headline" pockets of stress (e.g. Puerto Rico, Detroit) we continue to expect improving municipal credit conditions. The taxable market remains strong, with corporate spreads hitting all-time lows in December. While it's becoming increasingly difficult to find favorable risk-reward situations, we are redoubling our research efforts to find good relative value in the taxable marketplace. In general, less uncertainty around Fed decision making and modest economic growth should be a positive heading into 2014.

As we move into this new year, investor focus will continue to be on the Federal Reserve and monetary policy. Given the elevated importance of the Fed in recent years, the transition to a new leader of the central bank will be closely monitored by all. Incoming Chairman Janet Yellen has been a champion of greater transparency at the Fed, and will likely follow in Chairman Bernanke's footsteps in keeping an open line of communication with investors. The Fed has already taken steps to shift the market's attention away from asset purchases and towards forward rate guidance. With moderate improvements seen in the jobs market, the Fed will most likely shift their emphasis on their other primary mandate, price stability. Swooning commodity prices and nonexistent real wage growth have been a drag on nominal prices. With inflation trending below target levels, the Fed will be tasked with fighting deflationary pressures in the year to come.

The upcoming year will not be without challenges. With stocks sitting at or near all-time highs, we'll need to see some of the new catalysts mentioned earlier to propel them higher, while bonds will be challenged by the possibility of rising rates. While we would agree that cash will continue to flow into equities, we would argue that the likely source will be money market funds and other cash equivalents. Not to be ruled out, with further political debate inevitable, there is always the potential for our elected officials to upset the applecart. The economy has not fully turned the corner, and with the aforementioned deflationary pressures, we expect the easy monetary policy of the Fed to continue to be a tailwind for both stocks and bonds in 2014.

As always, we welcome your comments and questions. Please contact us if there are any changes to your financial situation or investment objectives.

APPLETON PARTNERS, INC ONE POST OFFICE SQ, BOSTON, MA 02109 TEL. 617.338.0700 WWW.APPLETONPARTNERS.COM