STEWARDSHIP PARTNERS
MARKET COMMENTARY

QUARTERLY COMMENTARY | VOLUME 13 ISSUE 2 | JULY 2013

Authored by Howard J. "Rusty" Leonard, CFA
CEO and Chief Investment Officer, Stewardship Partners Investment Counsel, Inc.

Taper Tantrum Disrupts Bull Market and Crushes Bonds

"Human anger does not produce the righteousness that God desires." James 1:20 (NIV)

So far in 2013 the financial markets have been behaving as we expected with bonds suffering losses and stocks performing well. Still, it has hardly been a normal situation due to the dual impact of government intervention in the markets and the hyper short term focus of often highly leveraged speculators who now dominate trading. In the first quarter of 2013 investors witnessed the strange and nearly unprecedented spectacle of defensive stocks leading a bull market charge while aggressive stocks, such as technology and emerging markets, shares trailed the indices. We thought this oddity, brought about by investors searching for yield outside the Fed-induced bubble in the bond market, was likely to reverse in the second quarter. With the notable exception of a further decline in the emerging markets, it did. Utility stocks were the worst performing sector during the second quarter while NASDAQ's gain exceeded that of the S&P 500, reversing the unusual circumstances seen in the first quarter. As the second quarter was almost two-thirds complete, the equity markets reached new highs as investors increasingly focused on the signs of lasting economic strength in the US and a continuation of stability in Europe. Real yields on US Treasury bonds, which had been deeply in negative territory during the peak of the European financial crisis in late 2011, turned positive in response to improving economic conditions, the passing of the crisis atmosphere and further declines in inflation (Chart 1). Most markets once again seemed to be responding in a more normal, rational fashion to an economic recovery which was slowly gaining strength and durability and where the need for government intervention was now waning. The glaring exception to this, however, was Japan where government intervention on a scale much greater than seen in the US or Europe caused Japanese equities to jump dramatically while its currency value fell nearly as sharply.

Chart 1

Taper Tantrum Leads to Higher Real Interest Rates
10 Year US Treasury Yield Minus CPI

Source: Strategas

Table 1

2Q13 Total Returns

US Indices	2Q13	YTD
S&P 500	2.91%	13.82%
S&P 500 Value	3.36%	15.73%
S&P 500 Growth	2.48%	12.04%
NASDAQ	4.52%	13.43%
S&P 400 (Mid Cap)	1.00%	14.59%
S&P 600 (Small Cap)	3.92%	16.19%
Treasury Bonds	-2.23%	-2.47%
High Grade Corp. Bonds	-3.36%	-3.31%
Gold	-22.69%	-26.31%
Global & International Indices		
MSCI World	0.64%	8.43%
MSCI EAFE	-0.99%	4.10%
MSCI Euro	1.71%	0.70%
MSCI Far East	2.52%	12.81%
MSCI Japan	4.32%	16.55%
MSCI Emerging Markets	-7.88%	-9.57%
US Economic Sectors		
Energy	-0.37%	9.77%
Materials	-1.80%	2.90%
Industrials	2.81%	13.78%
Consumer Discretionary	6.81%	19.79%
Consumer Staples	0.50%	15.15%
Health Care	3.84%	20.25%
Financials	7.25%	19.50%
Information Technology	1.68%	6.35%
Telecom	1.00%	10.55%
Utilities	-2.73%	9.93%

Source: Bloomberg

In mid-May, however, the Japanese central bank sensed their intervention had become unbalanced and sent signals to the market it planned to alter its course of weakening the Yen. This set off a bout of selling, mostly outside the US markets, as hedge funds rapidly unwound trades requiring a weak Yen to remain successful. Emerging markets and risky debt, such as Spanish and Italian bonds were among the casualties of many highly leveraged traders acting in unison to reverse out of their suddenly unattractive speculations. As a result, many markets were hit with profit-taking even though there was no actual change in the fundamental economic circumstances. The only change was the Japanese government's reduced intervention in the financial markets was going to make it tougher for hedge fund trades to work. In mid-June, the US Fed also changed its message to the speculators. Noting the better economic circumstances in the US, Bernanke announced if such improvement continued, the Fed would taper QE by the end of the year and end it in the middle of 2014. On the other hand, he said if the economy remained weak, QE would continue. In essence, this was a win/win situation for the markets. Unfortunately, hedge fund speculators still took this news from the Fed badly. Better economic performance meant artificial Fed forces might no longer hold interest rates low, disrupting their trading strategies. Another rapid sell-off ensued, referred to as the "Taper Tantrum", as hedge funds rushed to exit their positions. Still, the S&P 500 finished the quarter higher while foreign stocks fell slightly and bonds got crushed. Despite this late quarter disruption, the message for long term investors whose investment performance is not reliant on leveraged speculations, is the economy is improving and the future is brightening.

Stewardship Partners' US Equity, Global Equity and our Balanced portfolios outperformed their indices during the quarter, while our defensive portfolios were hurt by the Taper Tantrum.

Table of Contents:

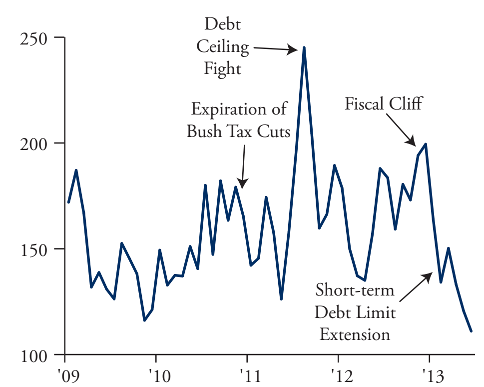
ENCOURAGING SIGNS FOR US ECONOMIC GROWTH

"Encourage others by sound doctrine and refute those who oppose it." Titus 1:9b (NIV)

Chart 2

Investors Are Finally More Confident About Economic Policy

US Economic Policy Uncertainty Index



Source: Strategas, Baker, Bloom, & Davis

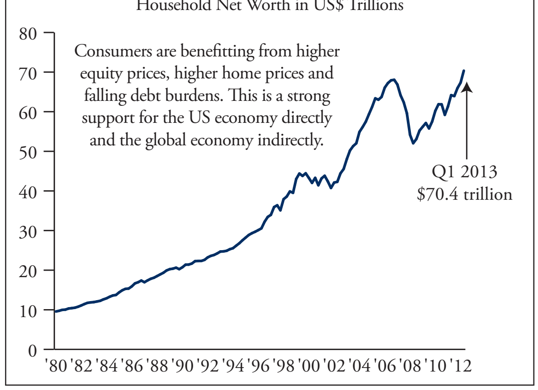
The Taper Tantrum histrionics and other bizarre market behavior seen in 2013 are distorting the average investor's view of real progress being made in economic performance, government finances and corporate wealth creation. Just about every key measure of US economic activity has shown improvement in recent quarters. As each month passes, it becomes more apparent the crisis atmosphere shadowing investors for so long finally seems to be dissipating. As auto sales recover, housing prices rise, employment strengthens and consumer balance sheets mend, a virtuous economic cycle begins to fall into place. It is this trend towards an economic recovery seemingly able to sustain itself which allowed Fed Chairman Bernanke to open the conversation about possibly slowly removing the unusual monetary accommodation known as QE. While speculators viewed this as a threat to their short term trading positions, it actually is a great victory for the US economy that longer term investors should celebrate. The sooner government intervention can be removed from the financial markets, the sooner spectacles like defensive stocks leading the way in a bull market and then also falling harder than the average stock in the subsequent sell-off can be a thing of the past. A more normal economy, free of unusual government interference, means less uncertainty about future economic policies (Chart 2), reduced volatility and more predictable market behavior. Significant US fiscal and monetary policy interventions are now waning and this should contribute to a favorable financial market environment where prices will more often respond to fundamentals versus distortions driven by government intrusions and hedge fund speculative excesses seeking to capitalize on the "free lunch" the Fed was temporarily feeding them.

While the Taper Tantrum did undercut share prices in June, equity prices are higher across the world so far in 2013. Combined with accelerating housing prices and a more cautious approach to debt, consumer net worth has been rising sharply and has regained all it had lost in the 2008 financial markets crash (Chart 3). A healthy consumer backed by a banking system that has also been restored to health is a powerful combination for the US economy. While overall economic growth has been held back so far in 2013 by tax increases and sequester-related federal spending cuts, the increase in wealth in the private sector has clearly overwhelmed the negative impact (Chart 4). While a variety of economic risks remain which could undermine this progress, the foundation for increasingly rapid private sector economic growth is stronger than many investors realize. Even the Federal budget deficit has shown remarkable improvement, further adding to the improving US economic picture. As a result, we would not be surprised if the many economic pessimists are proven wrong in the quarters ahead as US economic growth returns more vigorously than they anticipate. Moreover, there is no better prescription for the economic ills still impacting the rest of the world than a robust US economic recovery. Already, the US trade deficit has begun to expand indicating a stronger US economy is buying more from weaker foreign nations. Should this continue, as we expect it will, it should help pull the whole world out of the slow growth, perma-crisis economic malaise afflicting it since the crash in 2008.

Chart 3

Consumers Looking Very Healthy Again

Household Net Worth in US$ Trillions

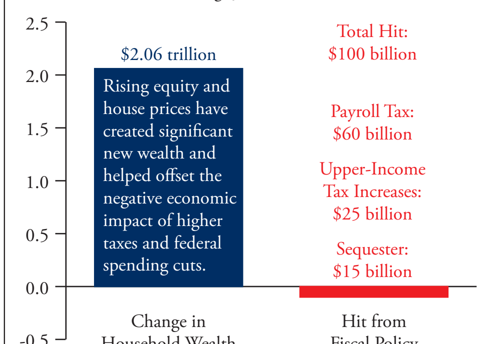


Source: Strategas

Chart 4

Gains in Consumer Net Worth Dwarfing Hit from Fiscal Policy

Change in Household Net Worth vs. Size of Tax Hikes and Spending Cuts YTD through June, $'s in Trillions



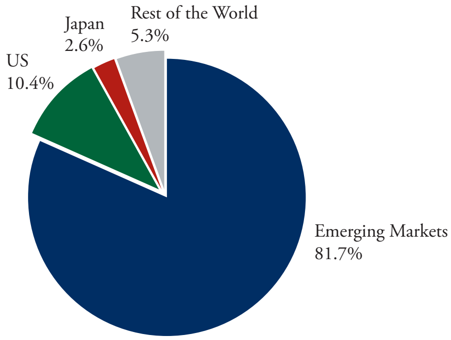
Source: Strategas

While we expect US economic growth to surprise to the upside in the quarters ahead, the drag from sequester-related spending cuts will likely be greatest in 2013's third quarter. As a result, US GNP growth could remain low as slowing federal spending offsets rising private growth. While the US still accounts for over 20% of global GDP, its contribution to the growth of the global economy will only be around 10% this year (Chart 5). The faster growing emerging markets will contribute the lion's share of global economic growth in 2013 while Europe and Japan are virtual non-factors given their continuing economic struggles. In 2014, we suspect the US economy will contribute a significantly greater portion of worldwide economic growth. Europe and Japan, however, are likely to remain

Chart 5

US and Emerging Markets Account for Most Global Economic Growth

% Contribution to 2013's Estimated Global Economic Growth



Source: Strategas, IMF, April 2013 WEO estimates

relatively unimportant in terms of global growth in 2014.

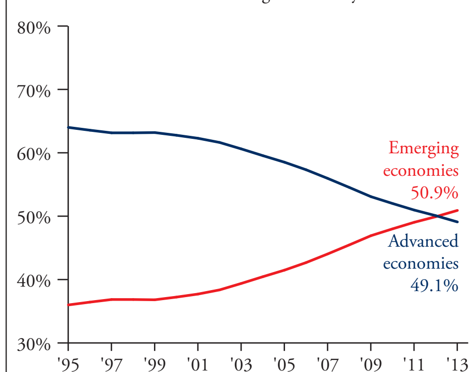
The trend towards the emerging markets being the biggest factor in global growth prospects looks poised to continue, even if faster growth returns in the US, Europe and Japan. Estimates now suggest the emerging economies need a new name as they now account for more than 50% of all global economic activity (Chart 6). It appears they have fully emerged! Perhaps rapidly developing economies would now be a more appropriate designation for these nations. At the same time, there is growing concern these countries may have grown too quickly in recent decades thereby straining their economic systems and institutions. A period of slower growth in China, India and other emerging countries may be required to restore appropriate balance in their development process. Increasingly, it appears China could finally experience the hard economic landing we have long worried about in the near future. Chinese shadow banking operations are clearly dysfunctional at the moment and the government is straining to reign in a variety of economic excesses that have been created during its rapid growth period of the last two decades. Even so, such an unfortunate outcome may still be avoided.

Chart 6

Emerging Markets Have Fully Emerged!

% Share of Total Global GNP

Based on Purchasing Power Parity



Source: Strategas, IMF, April 2013 WEO estimates

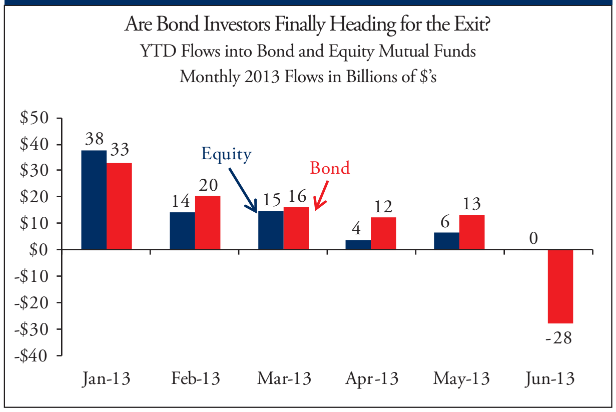
As a result of the possibility of a hard landing in China, weaker trends in other emerging economies and languishing economies in Europe and Japan; worries over a renewed bout of deflation are growing. Outside of some emerging economies, inflation has not been a serious threat as the world has recovered from the 2008 crash. Now, US measures of inflation are falling even against the backdrop of still extraordinary monetary stimulus. Tapering QE by the Fed may soon come off the agenda if Bernanke believes deflation is becoming a real risk. Indeed, Bernanke might actually expand QE to avoid even the thought deflation could become an issue. To be sure, the Fed is not happy about the rise in real interest rates accompanying the fall in inflation and the impact of the Taper Tantrum pushing nominal yields higher. Various Fed officials quickly started trying to talk down rates as the Taper Tantrum pushed them higher, worried about the corrosive impact on US growth of the spike in real rates. Bernanke can also be expected take actions to move inflation towards the upper end of its 1-2% range, thereby reducing real interest rates and keeping the dangerous specter of deflation at bay, if the markets do not move real rates lower soon on their own.

The Bond Bull is Dead – A Great Rotation From Bonds to Stocks?

"Such a person is double-minded and unstable in all they do." James 1:8 (NIV)

The disturbingly rapid increase in real interest rates will likely turn out to be a transitory phenomenon related almost entirely to the habit of hedge funds to all focus on the same trade at the same time. We can recall several such situations previously where hedge funds became overexposed to a particular bet causing overreactions on both the upside, as an overly aggressive bet was being placed, and on the downside as that bet was being unwound. The very rapid spike in oil prices to nearly $150 per barrel in June 2008 occurred as seemingly all hedge funds shorted the US dollar and went long oil is a great example of the hedge fund industry's ability to temporarily distort market prices. In the three months following the peak, oil prices lost all the ground gained in the previous six months and more as hedge funds all scurried to reverse this trade. During the whole period of the spike and the ensuing collapse in oil prices, there were no shortages or excess supply of oil. The whole episode was simply based on the wild imaginations of hedge fund managers, their willingness to mimic each other and their outsized influence in the market, based in part on the use of copious amounts of leverage. More recently, the Fed's policies have made it safe for hedge funds to engage in a variety of strategies which produced easy trading profits, but also had the inevitable effect of creating a huge bubble in bond prices as hedge funds crowded into the same trades. Hedge funds are not dumb, of course. They knew all their colleagues were playing the same game. Accordingly, even the mere hint of a possibility the Fed would no longer have their back in these trades has led to an outsized reaction in various bond and bond-like markets. As hedge funds rushed to close out these trades before their competitors did, a variety of market dislocations arose. Perhaps the most notable has been a significant reduction in liquidity in the emerging markets as the rush to close out trading positions required the selling of long positions in emerging markets stocks and bonds. While emerging markets may be providing nearly all the global economic growth in 2013, their stock and bond markets have dropped considerably, at least partly due to hedge funds pulling in their trades as a result of both the Fed and the Japanese central bank's statements. Because the size of hedge fund trades tied to the Fed's policies is substantial, it is not

Chart 7

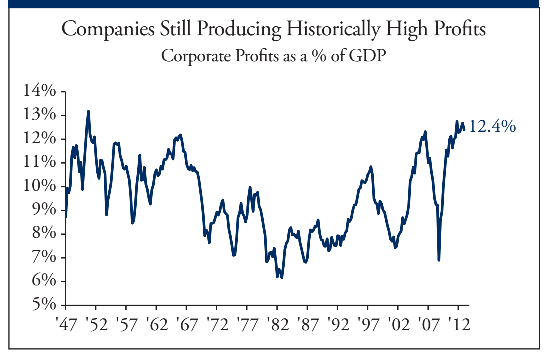


Source: Strategas

clear how long it will take these markets to normalize just as the oil market eventually did after the hedge funds moved onto other speculations. We suspect, however, real interest rates will soon move lower and US and global economic growth will not be meaningfully impacted by the rapid spike higher. Because of the Fed's policies, and the resulting hedge fund overconcentration in trading positions that benefitted from those policies, there has been a temporary dislocation in the relationship between asset and currency prices and the favorable forces at work in the real economy.

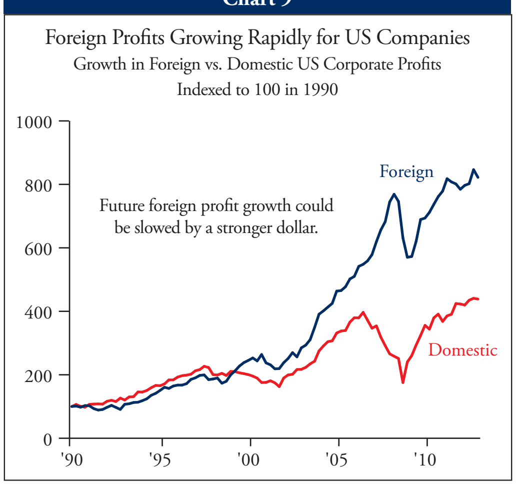
Since what is really going on in the economy is mostly positive, we believe equities will ultimately benefit. Our expectation for 2013 to be a very good year for equities still looks to be on target. We believe a better than expected recovery in the US economy would help boost demand for shares as investors transferred heavily overweight positions in bonds into just as heavily underweighted positions in equities. This weight of money flowing from bonds to stocks may have finally been triggered by the Fed's stated intent to taper its QE bond buying. Despite equities outperforming bonds in 2013, more money still continued to flow into bond funds until Bernanke laid out his tapering plan in June (Chart 7). We suspect this is the tip of the iceberg for bond fund redemptions and the long bull market in bonds may finally be over. With a backdrop of a more robust US private sector, the possibility of much of that money making its way into equity funds is high. Literally hundreds of billions of dollars, maybe even more, will be looking to reallocate away from bonds and into something else in the quarters ahead if we are correct. This could easily spur an outsized rally in equities during the remainder of 2013 and beyond as hedge funds now get overzealous about equities. Should question marks about the Chinese economy begin to clear up, emerging market equities could prove to be the biggest beneficiaries of this hoped for trend as they are now far cheaper than US stocks. Indeed, foreign stocks generally are less expensive than US stocks and could therefore outperform the S&P 500 over the next few years as valuations normalize. Commodities could also be boosted by former bond money looking for a new home should economic success in the US begin to spread around the globe.

Chart 8



Source: Strategas

Chart 9



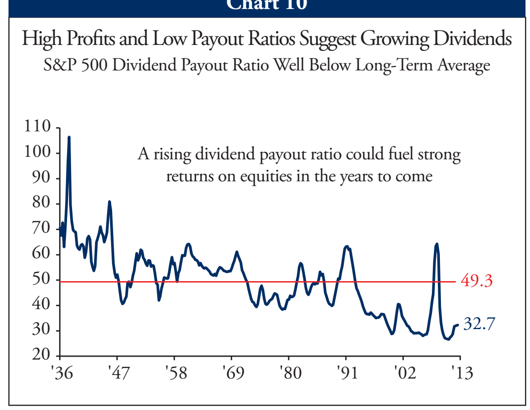
Source: Strategas

Initially, however, US stocks stand to benefit from the move away from bonds. US companies are in excellent financial shape. Most US corporations have more cash on hand than is typical as they have carefully spent on new capital expenditures during a period of weak overall growth. Corporate profits are also near an all-time high relative to GDP (Chart 8) due largely to excellent expense control after the crash in 2008. While economic growth has been in a slow recovery, GNP has already surpassed it pre-crash highs. Employment, however, remains lower than prior to the crash as corporate productivity has made big gains while companies have only hired back workers after they have taken full advantage of their current staff.

Another factor boosting US corporate profitability has been fast rising foreign profits earned by US companies. While the US economic recovery has been subdued, US firms have been able to compete effectively overseas and participate in the more rapid economic growth seen in the emerging markets (Chart 9). Foreign profits, however, can have a tendency to be less certain as economic performance overseas can be more volatile than in the US and because the changes in the value of the US dollar impacts results. Nevertheless, the growing diversity of US corporate profits is a long-term strength and translates into an ability of US corporate profits to grow faster than what might be expected based on US economic performance on its own.

Also supporting the case for long term investment in US equities is the ability for US companies to increase their dividends. With profit margins at high levels, balance sheets in unusually strong position and dividend payout ratios still quite low, it seems reasonable to expect dividend payments to be on the rise in the years to come in the US, providing good support for further gains in equity prices (Chart 10).

Chart 10



Source: Strategas

Which Stocks Are Poised to Benefit Most From Further Upside?

"Blessed is the one who perseveres under trial." James 1:12 (NIV)

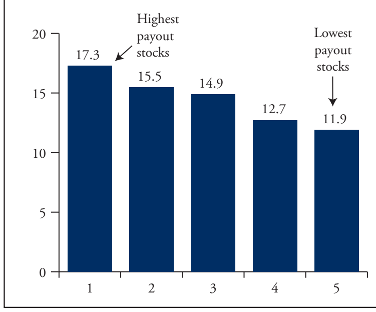
Reflecting growing investor interest in dividends in recent years, companies with the highest dividend payout ratios have been rewarded with the highest price-earnings multiples, while those with the lowest dividend payout ratios have the lowest price-earnings ratios (Chart 11). This is an unusual circumstance and is the exact opposite of what was the case in the year 2000 when growth was most highly valued (perhaps overvalued would be a more appropriate term) by investors. We would expect the willingness to pay up for dividend payers to erode over time as this is just another indication of relative overvaluation of defensive shares relative to growth stocks. Nevertheless, the market's current expressed preference for companies willing to share a high proportion of their earnings as dividends will no doubt encourage many firms to increase their dividends at a faster rate than earnings. This trend has already begun with large cap tech firms, such as Cicso and Apple, starting to pay substantial dividends after years of paying none at all. Higher dividend payouts could also result in a less volatile US stock market anchored by higher dividend yields.

Chart 11

Investors Now Paying Up for High Dividend Payouts

S&P 500 Median P/E by Dividend Payout Ratio Quintile

Paying higher P/Es for high dividend stocks is the exact opposite of what normally is the case. Investors usually pay up for growth stocks.



Source: EIA, Strategas

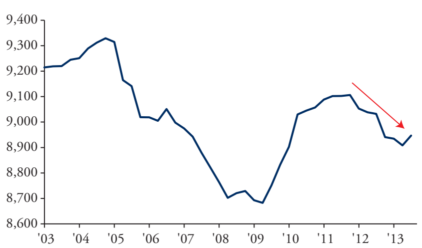
Corporate managers are not only turning towards higher dividends to reward shareholders. In an era of slow revenue growth, many CEOs have found other means to boost earnings and share prices. Such methods include both acquisitions and share repurchases. As a result of both these activities, the actual number of shares outstanding in the S&P 500 has declined even as corporate balance sheets strengthened (Chart 12). These trends highlight the excellent financial position of the average US company. Furthermore, as the pool of investable assets grows over time, a reduction in the number of shares available for purchase suggests price-earnings ratios will be biased higher. It is simply a matter of supply and demand. With the potential for waves of money heading towards stocks from the bond market, this is just another reason to be careful not to sell a rising stock market too soon since valuations could advance higher than many of us would normally think reasonable.

Chart 12

Shrinking Supply of Shares Available is Bullish

S&P 500 Index Shares Outstanding

Shares in Millions



Source: Strategas

Table 2

Utilities Expensive, Technology Cheap

S&P 500 Sector Valuation Analysis

Sector	FY1 Est. P/E	15 Year Avg. P/E	Ratio	Relative P/E	15 Year Avg. P/E	Ratio (sorted)
Utilities	15.2x	13.7x	1.11	1.099	0.879	1.250
Telecom	17.4x	17.5x	0.99	1.262	1.084	1.165
Financials	12.5x	12.7x	0.99	0.909	0.803	1.132
Staples	16.2x	17.1x	0.95	1.175	1.073	1.095
Discretionary	16.5x	18.5x	0.89	1.200	1.153	1.041
Industrials	14.2x	16.4x	0.86	1.026	1.022	1.004
S&P 500	***13.8x***	***16.2x***	***0.85***	***1.000***	***1.000***	***1.000***
Health Care	14.7x	17.8x	0.83	1.065	1.072	0.993
Materials	13.4x	15.7x	0.86	0.975	0.987	0.988
Energy	11.7x	14.4x	0.81	0.845	0.876	0.965
Technology	12.5x	22.6x	0.55	0.903	1.336	0.676

Source: Strategas

Valuations for most sectors remain lower than the fifteen year average (Table 2). Only the utilities sector is selling at a higher P/E than it has averaged over the last fifteen years. Defensive stocks generally are still valued at levels higher than the S&P 500 in total and perhaps therefore offer the least upside. Cyclical and growth shares are valued at below average levels and technology stocks, in particular, stand out as undervalued. Naturally part of the reason for this discrepancy is the insanely high P/Es such stocks commanded in the tech bubble and part is the now more mature growth characteristics of large cap tech stocks. Still, the current P/E of 12.5x for the tech sector is well below the normal premium such stocks enjoy. It would hardly be surprising if the tech sector vastly outperforms the utilities and telecom sectors over the next five years.

If the long bond bull market is indeed over and interest rates are going to be moving higher in the years ahead, history suggests technology stocks and cyclical stocks generally will be the beneficiaries (Table 3). Defensive sectors, such as utilities, telecom and staples tend to lag when interest rates are rising. Accordingly, it is unlikely that we will soon see again the upside down stock market advance that occurred in 2013's first quarter. Moreover, Stewardship Partners' growth oriented portfolios stand to benefit should these trends reoccur if interest rates move higher as the economy recovers in the months ahead.

Table 3

Technology Stocks Best When Rates Rise, Utilities Worst

Annualized Sector Performance When Rates Are Rising

Sector	Average	9/30/93 - 11/30/94	12/31/95 - 8/31/96	9/30/98 - 1/31/00	5/31/03 - 6/30/06	12/31/08 - 12/31/09
Technology	**37.9%**	19.4%	20.8%	83.5%	6.1%	59.9%
Discretionary	**17.5%**	-2.9%	10.9%	33.3%	7.5%	38.8%
Materials	**17.3%**	8.2%	9.3%	8.4%	15.5%	45.2%
S&P 500	***13.5%***	***-1.0%***	***8.9%***	***26.7%***	***9.4%***	***23.5%***
Industrials	**12.4%**	-3.5%	13.8%	20.6%	13.9%	17.3%
Energy	**10.9%**	-4.4%	9.2%	10.7%	27.9%	11.3%
Health Care	**10.0%**	16.9%	8.5%	5.2%	2.3%	17.1%
Financials	**8.3%**	-12.4%	14.7%	14.9%	9.3%	14.8%
Staples	**7.7%**	11.5%	13.4%	-4.1%	6.4%	11.2%
Telecom	**1.7%**	-13.4%	-19.6%	31.7%	7.0%	2.6%
Utilities	**-1.8%**	-20.3%	-7.4%	-1.5%	13.3%	6.8%

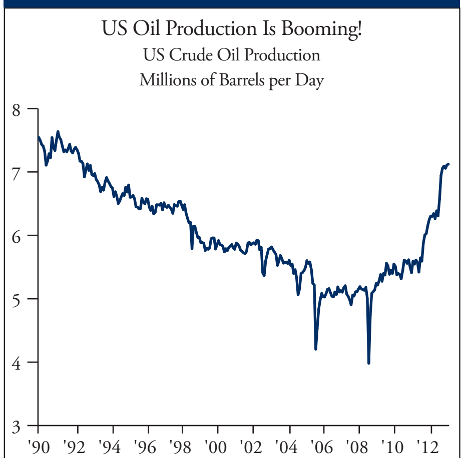
Source: Strategas

SHOULD THE LORD TARRY, GOOD TIMES MAY BE AHEAD

"In just a little while, he who is coming will come and will not delay." Hebrews 10:37 (NIV)

Despite increasing good news on the economy and the now reduced risk of another bout of financial calamity, Stewardship Partners' clients generally remain skeptical about the prospects for the United States as a nation, let alone economically. These concerns are mostly well-founded given the many disturbing trends in our culture and politics which seem to be inviting our Lord's judgment to come upon us. Given advances in technology, events in the Middle East and rising threats to religious liberty in the US, it is not surprising that some have become concerned we are closing in on the end times period of history as described in the Bible. While we admit we have noticed these same disturbing developments, we believe it is possible many are so focused on these unfortunate trends they are unable to see several more favorable situations occurring at the same time. Since Jesus Himself told us we cannot know when the end times will begin, it is unlikely we will guess correctly. Accordingly, we are to remain watchful and stay spiritually prepared while carrying on with our lives, seeking as best possible to be a blessing to others and win as many to Christ as possible.

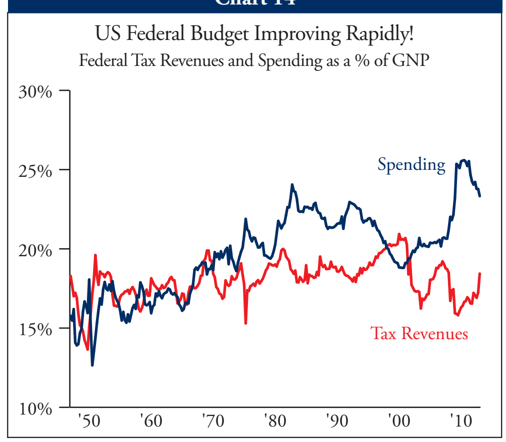
Chart 13



Source: Strategas

One positive trend that many have missed, beyond those already mentioned earlier, has been the resurgence of oil and gas production in the US (Chart 13). Most assume the Obama administration's animus towards carbon based fuels has meant the US energy situation is deteriorating rapidly. Actually, the opposite is happening. Despite Obama's negative stance towards the energy industry, oil and gas production are exploding to the upside and oil imports from the Middle East and Venezuela are declining sharply. How can this be? While Obama has been able to slow energy development considerably on federal lands through regulatory action, new technology has opened the doors wide on finding new sources of oil and gas on private lands. It may not seem fair that Obama can claim success on this front while simultaneously doing everything he can to undermine the industry, but he can. Oil production has soared during his time in office after declining continuously on Texan Bush's and Halliburton Cheney's watch! Life can certainly be weird at times, but this fact demonstrates presidential power is limited and the impact of technological advances in a still largely free market is impressive. Needless to say, as we discussed in our last commentary, moving closer to energy independence is very positive and its economic and geopolitical significance should not be underestimated.

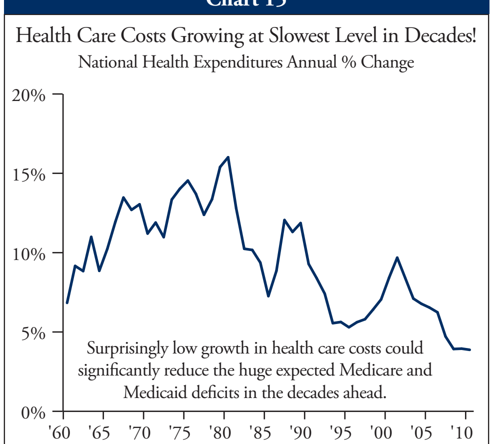
Chart 14



Source: Strategas

Another area where many of our clients are missing out on the complete picture is in the area of our government finances. As a result of the tax increases, continued economic growth, reduced defense spending on Iraq and Afghanistan and sequester-related spending cuts both federal spending and federal revenues have seen dramatic improvements when measured versus GNP (Chart 14). As a result, the federal budget deficit has fallen much more quickly than many believed possible and further significant improvement now looks likely over the next two years. Additionally, total federal debt as a percent of GNP has stabilized. While conservative pundits will continue to raise the alarm over the debt and deficit issues, the financial markets are more comfortable with the current positive trends on both fronts. Nearly everyone would like to see even more progress in this area but neither the debt nor the deficit is a compelling issue for investors at this time.

Chart 15



Source: Strategas, CMS

Moderating health care costs are another trend with important long term favorable consequences for the US (Chart 15). Recently, spending on healthcare has grown at the lowest rate on record. Should this continue, the long term Medicare and Medicaid spending assumptions may need to be lowered, perhaps making both programs solvent for many more years than currently expected. The delays in various aspects of Obamacare we thought would happen may also prove helpful in reducing long term healthcare cost assumptions. As a result, should the Lord in His mercy tarry in bringing judgment on our nation, the long term economic situation facing investors may turn out better than many now anticipate.

We at Stewardship Partners continue to be grateful for the opportunity to serve your investment needs. Please do not hesitate to contact us if you have any questions or if we can be of assistance.

Biblically Responsible Investing (BRI) – Investing as Jesus Would

"Blessed are they that maintain justice, who constantly do what is right." Psalm 106:3 (NIV)

Stewardship Partners, founded in 2000, is a leader in the field of investing with a Christian perspective, a form of Socially Responsible Investing (SRI) known as Biblically Responsible Investing (BRI). Rusty Leonard, CFA, Stewardship Partners' founder and CEO, practiced this investment philosophy while managing over $3 billion of assets as a portfolio manager during his decade of service with the Templeton organization. He also had the privilege of working directly with world-renowned global mutual fund manager, Sir John Templeton. **By employing a BRI approach to investing, Stewardship Partners seeks to achieve long-term capital gains through ownership in securities of companies that are a blessing to mankind. Conversely, we seek to avoid profiting from owning companies engaged in sinful activities which bring physical and spiritual loss to our fellow man. Our heart's desire is to do no harm to our fellow man in the process of being the best possible guardians of the wealth the Lord has given us stewardship over.** Simply put, a "what would Jesus do" approach to portfolio management is what we seek for our clients.

Below are just some of the issues of concern to Stewardship Partners and the specific sinful activities that fall into each category:

1. **We desire *justice and mercy for the defenseless* so we seek to avoid companies involved in:**
   - Abortion
   - Life destroying or distorting scientific research
   - Human rights issues such as religious persecution, terrorism and political oppression

2. **We desire *justice and mercy for the poor* so we seek to avoid companies involved in:**
   - Greed-based marketing techniques
   - Discrimination and unjust labor practices
   - Any abuses of the poor, children and/or the elderly

3. **We have *compassion for those addicted and/or engaged in sinful lifestyles* so we seek to avoid companies involved in:**
   - Alcohol, Gambling and Tobacco
   - Pornography
   - Homosexuality (those companies deemed to be the most active supporters)

4. **We desire to *protect marriage and the family* so we seek to avoid companies involved in:**
   - Entertainment that seeks to destroy biblically-based attitudes
   - Efforts to promote lifestyles the Bible indicates are sinful

Additionally, we favor companies that clearly embrace:

- Honesty, Compassion, Diligence, Prudence and Creativity
- Support for quality products at fair prices and constructive stakeholder relations
- Support for a sustainable and healthy environment
- Support for charitable giving
- Support for the Jewish people and the state of Israel

We obtain information on both the objectionable practices and the exemplary attributes of corporations from our affiliate **The Biblically Responsible Investing Institute** (www.BRIInstitute.com). We believe BRII gives Stewardship Partners the most comprehensive database of BRI information that currently exists and utilize much of it to realize our goal of investing in a manner that most honors our Lord. Equipped with this information, we are then prepared to make as strong an effort as possible to build investment portfolios which best reflect our clients' biblically-based Christian worldview.

Like all people, all companies are sinners. Therefore, we attempt to use the BRI information at our disposal to eliminate the worst offenders from our portfolios. At times, this is easy. For example, a company involved in making drugs used in the abortion process will always be excluded from our portfolios. In many cases, however, we need to utilize judgment, such as when a company has operations in a country that is a known violator of human rights. The type and size of that exposure, among other considerations, are taken into account before eliminating the company from our portfolios. When judgments must be made we are guided by the principal of trying to do what we believe Jesus would do if He were making the decision.

For a more in depth study of the topic of Biblically Responsible Investing (BRI), please see our paper entitled ***"The Scriptural Basis for Biblically Responsible Investing"***.

BRI in Action – Comparing Good and Bad Corporate Behavior

"Love must be sincere. Hate what is evil; cling to what is good." Romans 12:9 (NIV)

Below you will find an example of both a company exhibiting exemplary attributes, First Solar, and one we avoid, Google. First Solar is a holding in some of our Stewardship Partners portfolios while we actively avoid ownership in Google in order not to be co-owners in enterprises engaged in or supportive of activities which are harmful to our fellow man and our Lord's creation. **We believe, in the long run, both countries and companies that best align their activities with biblical principles will achieve the greatest success.**

The Good – First Solar – Excelling at Good Corporate Citizenship

"Instruct them to do good, to be rich in good works, to be generous." 1 Timothy 6:18a (NIV)

Formed in 1999, First Solar quickly rose to a position of leadership in the global solar energy industry. The company is now considered the leading global supplier of comprehensive solar energy solutions. First Solar has vertically integrated its operations in order to maximize value creation throughout the solar energy value chain. Additionally, the company seeks to mitigate their customers' risk as well in adopting a solar energy project. The company's mission is to create enduring value through helping the world to become increasingly powered by clean, affordable solar electricity. The company has a long list of "firsts" in the solar industry and is best known for its cost efficient Thin Film technology which has allowed First Solar to become the solar company closest to achieving cost parity with fossil fuels. First Solar has now designed and constructed over 1.5 Gigawatts of solar power production including the world's largest solar power generation facility located in Arizona. First Solar was the first solar company to produce over 1 Gigawatt of power in a year and the first company to breach the $1 per watt cost barrier. The company holds the world record for efficiency in a solar module and a solar cell. It is the gold standard in the industry and no other company really comes close to its capabilities. When the solar industry went through a downturn in 2012, First Solar was the only company able to remain profitable.

While a relatively new company that has grown very rapidly, First Solar still has quickly learned how to embrace good governance policies. Independent directors make up 80% of the board and the company has an extensive Code of Conduct and Ethics which applies to all employees. In order to help employees interpret and abide by this comprehensive document the company has put in place an Office of Compliance and Ethics. Additionally, the company has hired an independent third party whistleblower service to allow employees to anonymously report ethical concerns. This firm maintains an 800 phone number and can also be contacted via e-mail. The Code of Ethics and Compliance covers, among other important issues; conflicts of interest, interactions with government employees, insider trading, discrimination, harassment, protection of proprietary information and political contributions. First Solar's board has five committees. In addition to the normal audit, compensation and governance committees the company also has two unusual board committees, Project Development Risk and Technology. This forward-thinking committee structure is indicative of management's wisdom. Not surprisingly, First Solar has twice won the MIT Technology Review's Award for being one of the World's 50 most innovative companies. So far in 2013, First Solar has already won eight separate awards including Africa Energy Award for best renewable Technology. The company has consistently set high standards in all facets of its operations and has been able to meet them as well. Few companies have achieved so much so quickly.

First Solar has six very sensible core values which guide the firm's operations: Safety First, Environmental Responsibility, People First, Deep Customer Relationships, Continuous Improvement and Results Matter. The company's track record indicates First Solar has taken these core values seriously. With both Safety First and People Matter making up one-third of the core values, the emphasis on its biggest assets, its employees, is obvious. First Solar employees also enjoy a variety of benefits that they surely are blessed by. Included among these are medical and dental insurance and an employee assistance program to assist workers who are struggling with personal or workplace issues on a confidential basis. A flexible spending account is offered for both healthcare and dependent care expenses (such as elder care and child care). This allows employees to pay for such expenses using pretax dollars. Each employee also has a minimum of $50,000 in life insurance provided to them and can also sign up their spouse and children for life insurance as well. Short and long term disability insurance is also provided. The company helps employees plan for their retirement by offering a 4% match in its 401(k) plan and either a traditional or Roth 401(k) can be chosen. There is also a stock purchase plan where employees can purchase First Solar shares at a discount using as much as 10% of their salary to do so. Impressively, the company has been designated as a military friendly employer by GI Jobs magazine. The company also offers tuition reimbursement and provides customizable in-house training and development. There is little doubt First Solar lives up to its People First core value.

First Solar's charitable efforts to aid the communities in which it operates are also laudable. The company runs the First Solar Corporate Charitable Fund which focuses on "green" education initiatives, providing access to clean energy and water in underserved areas and furthering the development of innovative and sustainable technologies. The company has awarded grants to the National Park Trust for its environmental education program and to a Malaysian grade school for books, uniforms for underprivileged students, motivational workshops for parents and financial incentives for teachers to lead after school programs. The company has also supplied solar modules to operate a water pump in order to bring safe and clean water to remote villages in India. As a solar power company, First Solar's main business activity has a very positive environmental impact. In line with its core value of Continuous Improvement, the company also is seeking to make every aspect of its operations as environmentally friendly as possible. Advances in product design, materials sourcing, the manufacturing process, how its products are used and recycling have all contributed to reducing the environmental impact of the company's operations.

First Solar's good works are, of course, no guarantee of long-term investment success. As Biblically Responsible Investors, however, the company's commitment to excellent stewardship and its impressive treatment of its employees allows us to know we are shareholders in a company seeking to be a blessing to all. While no company, like no person, is perfect, this is clearly a company that we can be proud to own!

The Bad – Google – Homosexuality and Porn

"Things that cause people to sin are bound to come, but woe to that person through who they come." Luke 17:1 (NIV)

Google is one of the greatest success stories in the history of the technology sector. Its Internet search engine is the most popular and the company's domination of the space has afforded it the ability to move successfully into many other areas as well. It is a formidable innovator that has the financial capability to take over smaller competitors if it is unable to defeat them in the marketplace. Its ability to collect and track internet user data is legendary, making many less frightened of the National Security Agency's spying as they figure Google already has their information anyway! Despite its many successes and its domination of its business, Google's stock is one that we have avoided. The company is one of the most active corporate supporters of homosexuality and its co-founder, Sergey Brin, posted a blog in 2008 throwing the company's support behind defeating California's attempt to define marriage as between a man and a woman. Due to the company's extensive backing of homosexuality it has received numerous awards from a variety of groups supporting homosexuality. It has supported numerous gay pride parades throughout the US and also makes the gay programming from LOGOTV.com available on the Google Video marketplace. Google is also a leader in supporting transgender issues. As the world's leading Internet search engine, the company also enables users of its product to easily locate and view pornography on the Internet. While an admirable company in many respects, these activities prevent us from investing in Google.

Excluding Google from our list of potential investments is not a difficult decision. As BRI investors seeking to please and honor our Lord, we naturally look elsewhere to achieve investment success as we do not want to be associated with a company using shareholder resources in a manner which have a negative impact on individuals and society in general.

STEWARDSHIP PARTNERS MINISTRY COMMENTARY

Our Ultimate Goal – Funding the Lord's Work

"Therefore go and make disciples of all nations." Matthew 28:19a (NIV)

It is our hope that Stewardship Partners' ability to create an abundance for you will help you to share with those who are in need and assist in fulfilling the Great Commission. Our non-profit ministry affiliate, Wall Watchers, provides a free service to help you educate yourself about the many wonderful Christian giving opportunities available to wise donors. We invite you to join the thousands of visitors to our ministry's website at www.MinistryWatch.com, as best we can tell, the Internet's top site for donors to Christian ministries to gather critical information about the ministries they are considering supporting. The site contains a variety of helpful information about hundreds of the largest US-based Christian ministries including ministries statements of faith, the history of the ministry, program accomplishments, ministry financial statements and financial efficiency ratings. Please feel free to utilize this free resource as you seek to be a wise and effective donor to Christian ministries. We would be pleased to help you bless God's people who are in need, and clients of Stewardship Partners have access to further resources from MinistryWatch.com. It is our sincere desire to see Christians leading the way in giving generously, wisely and effectively so that the Lord's work on earth can be completed and many can be both blessed and saved.

Featured Ministry – Bright Hope International

"So the poor have hope, and injustice shuts its mouth." Job 5:16 (NIV)

Bright Hope's mission is to bring hope to those living on less than $1 per day. Their goal is to help under-resourced local churches transform their communities thereby bringing hope to those living in extreme poverty. Bright Hope has been serving local churches for 45 years and now has operations in nine countries. Their three tiered model of providing Hope for Today, Hope for Tomorrow and Hope for Eternity strikes a good balance between meeting current and eternal needs. The ministry was founded by Dr. Kevin Dyer who travelled regularly to the Soviet Union and Eastern Europe in the late 1960s and 1970s bringing food, medicine and bibles to Christians suffering under the yoke of communism. Once these countries broke free from communism, the ministry began serving the local church in other parts of the world. Today the ministry is run by Dr. Dyer's son who formulated the innovative operating model the ministry uses. The nine countries where Bright Hope currently has operations are: Haiti, Cuba, India, Peru, Uganda, Kenya, Chile, Bolivia and Zambia.

Through Hope for Today, the ministry provides feeding programs, aid to orphans and other vulnerable children, medical assistance, clean water initiatives and crisis response teams. With its Hope for Tomorrow programs, the ministry provides job training programs, micro-lending, educational support, church training and assistance and rehabilitation for those impacted by human trafficking. The ministry's Hope for Eternity efforts encompass pastor and leadership training, bible distribution and evangelism and discipleship. Bright Hope describes its approach to working with the local church in this manner: "Through our years of experience we have seen the church be courageous in loving those considered unlovable, be generous in times of crisis, and willing to help all peoples regardless of religion. We have found building into an already existing unit like the church is more effective in life transformation and helping lift the extreme poor out of their situation than trying to establish something new."

Bright Hope International, while only a mid-sized ministry, has had an outsized impact on those in extreme physical, emotional and spiritual poverty in a variety of countries around the world. It has a well thought out approach to meet as many needs as possible of our brothers and sisters facing the worst the world has to offer. Bright Hope International also has a five star Financial Efficiency Rating from MinistryWatch.com, indicative of its wise use of donor resources. We believe Bright Hope International is worthy of consideration for your financial support.

The Christian Ministry Marketplace – Helping Donors Give Wisely

"A generous man will prosper, he who refreshes others will himself be refreshed." Proverbs 11:25 (NIV)

Much like the stock market provides for a sensible and efficient allocation of capital in our economy, the rise of a Christian Ministry Marketplace is providing donors with a myriad of helpful resources to maximize the impact and joy of giving to the work of the Lord. As donors begin to take their giving as seriously as their investing, they will find the assistance offered by the groups listed below to be invaluable. By utilizing these resources, donors are not only likely to make better personal giving decisions, but are also contributing to the growth in the marketplace itself. By so doing, they are helping to lay a foundation for wiser giving for all who follow in their footsteps. Accordingly, we encourage donors to investigate how these groups might help you to give more wisely, achieve a greater impact and create increased joy for both yourself and receivers of your gifts.

The Christian Ministry Marketplace
Resources for Christian Donors

WHY
to give to Christian ministries?

Teaching on Stewardship:

- Crown (crown.org)
- Eternal Perspectives (epm.org)
- Generous Giving (generousgiving.org)
- Global Generosity Movement (generositymovement.org)
- Sound Mind Investing (soundmindinvesting.com)
- The Gathering (thegathering.org)
- MaximumGenerosity.org (maximumgenerosity.org)
- Stewardship Ministries (stewardshipministries.org)

HOW
to give with a discerning mind?

Professional Advisors:

- Kingdom Advisors (kingdomadvisors.org)
- National Association of Christian Financial Consultants (nacfc.org)
- WaterStone (waterstone.org)
- National Christian Foundation (nationalchristian.com)

Donor Advisors:

- Excellence in Giving (excellenceingiving.com)
- Calvin Edwards & Company (CalvinEdwardsCompany.com)
- Kardia (kardiaplanning.com)

WHERE
to invest in kingdom ministries?

Ministry Research:

- ECFA (ecfa.org)
- MinistryWatch.com (ministrywatch.com)
- Samaritan's Guide (acton.org/cec/guide/)
- Intelligent Philanthropy (intelligentphilanthropy.com)

Ministry Mutual Funds:

- National Christian Foundation (nationalchristian.com)
- Strategic Resource Group (srginc.org)
- Sovereign's Wealth Fund (swfund.org)

Featured Ministry Marketplace Participant – Stewardship Ministries

"You will be made rich in every way so that you can be generous on every occasion." 2 Corinthians 9:11 (NIV)

Stewardship Ministries was founded by Jay Link as a means of taking his seemingly unlimited energy and abundant stewardship teaching resources to a variety of Christians who can benefit from them. Among these are Christian financial advisors. Jay offers a variety of teaching resources which Christian financial advisors can utilize to be adequately prepared to serve their clients' stewardship needs. Jay's teaching materials lay out the fundamentals of biblically-based stewardship and the unique stewardship dilemmas that wealthy Christians, in particular, face. These teaching materials help advisors to realign their practice in a manner that will enable them to best implement the Family Wealth Counseling process, something Jay has developed during his 30 years of working with wealthy families.

Jay also offers training for fundraising executives of Christian ministries. Many ministries struggle in their efforts to attract and/or retain major donors. Again calling on his extensive experience in dealing with high net worth Christians, Jay uses his "Bridging the Gap" seminars to help ministries learn how to change their paradigm of getting something from their major donors to giving them something significant.

Individuals can also benefit from Jay's extensive teaching on biblically-based stewardship via the many free resources available on the Stewardship Ministries website (http://www.stewardshipministries.org/), including Jay's training curriculum for children. Additionally, two of Jay's five books are available for free on the website.

Finally, Jay offers a one day leadership training seminars to pastors to help them clarify and broaden their understanding of stewardship as well as equip them to confidently teach it to their congregations.

Financial advisors, ministries, individuals and pastors can all benefit by utilizing Stewardship Ministries' excellent training. We recommend you take full advantage of Jay's work.

Knowing Jesus Christ as Your Lord and Savior

While most of those reading this will have already established a personal relationship with Jesus as their Lord and Savior, it is very likely that many have not. If you are someone who has not yet turned your life over to your Creator, we would have failed you miserably if we presented only information relating to your investments yet did not share with you the most important information of all: truths which have eternal significance for your soul and that will have an overwhelmingly positive impact on your life on this earth.

The gospel message is a simple one, far less complicated than the global impact of rising oil prices or the effect of a revaluation of the Chinese currency. For most people, the first part of it is easy to relate to – you are a sinner. If you are anything like the rest of us (and you are) more often than you probably would like to admit, you either do, say or think something that is clearly wrong and which you are ashamed of. "But what's the big deal", you might say. "If everyone has this problem with sin, can't we all just accept the fact and try our best to get along?"

Well, on this earth, that is exactly what we try to do. We forgive one another's faults and press on with life. From an eternal perspective, however, there remains a problem. Our Creator, who loves us with a love that can only be described as extravagant, has prepared an eternal home for us that He very much desires to share with us. Unfortunately, in our sinful state, we are unable to enter into heaven, which is by its very nature perfect. Desperate not to be separated from us for an eternity, our God devised the only possible solution – a divine exchange. He sent His very own son, who was perfect and thus without sin, as a sacrifice to pay the penalty for our sins. In this exchange, Jesus bore, through His death, all of our sins, so that we in turn could receive all the glory that was due to Him. He was made sinful while we were made perfect and, in our now perfect state, we are able to enter into the eternal home our Lord has prepared for us.

What then gives each of us access to participate in this divine exchange? By responding to this incredible demonstration of extravagant love by our God through an amazing act of your own. As you let the realization of just what your Lord has done for you filter through your heart, mind and soul, you will unavoidably desire to humbly come before Him, acknowledging that it was your sin that led to His sacrifice and recognize His Lordship in your life. And with this step of faith, the divine exchange is completed in your life, and along with it, the assurance of eternal life with a Lord whose love for you knows no bounds. If you have not done so already, we encourage you to take this time to contemplate the issue of your eternal destination and to take that step of faith that will make all the difference in your life, both now and eternally. Based on my experience and the experience of literally millions of others throughout history, it is the most satisfying, enriching and worthwhile choice you will ever make. Years of wonderfully inspiring spiritual growth await you and, if the Bible ever seemed confusing to you in the past, you will now find its wisdom leaping off the pages and into your heart.

If we at Stewardship Partners can be of any assistance to you in this all important matter of your eternal destiny, please do not hesitate to contact us. Like Jesus, we also greatly desire to share an eternal heavenly home with you!

STEWARDSHIP PARTNERS

Stewardship Partners Investment Counsel, Inc.
PO Box 157 Matthews, NC 28106-0157
Phone: (800) 930-6949 Fax: (800) 930-6949

E-mail: cgoddard@stewardshippartners.com
Website: www.stewardshippartners.com