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Dear Friends:

This month's newsletter is a guest piece written by Mr. Steven Albrecht, President and CEO of Charter Trust Company, Concord, NH. I hope you enjoy his 2014 assessment of the financial markets. Mr. Albrecht can be reached at 603-224-1350, or via email at salbrecht@chartertrust.com.

Best wishes, Ray Pinard

Portfolio Review

This is the time of year when nearly every investment management firm, research organization, professional news agency and media site start to produce economic and market forecasts. Writers and forecasters predominately focus on either the economy or the markets depending on their expertise. They mostly avoid merging the discussions to avoid the danger of attempting to rationalize the relationship between the two forces. Throughout history it has been extremely difficult to bring logic to these seemingly rationally intertwined pieces of our lives.

The reason both economic activity and the markets are not perfectly in sync, is about the relative timeframe in which they operate. Don't get me wrong. I am a big believer in the position that markets are driven and react to economic activity. Let's start with the premise that markets are forward looking and economics operates in the current time frame. Available information about these two important topics also operates in two different time frames. Information about the economy is available partially in the current time period, but most is not available until much later. Information about the markets is in the current time frame, nearly instantaneous and can be measured in nanoseconds.

If the economy and markets are related, but operate and are influenced at various timeframes, how do you examine the economy and use it to benefit your investments? We believe the link is in understanding how much the current and expected future economic condition influences future market prices relative to current market positions. Stated in a different manner, we need to understand the difference between what investors expected to happen relative to what is happening today, because the markets and the economy are operating under two different time periods.

In 2013 the markets performed better than they should have in a slow growth economy. Throughout the year GDP forecasts were revised downward several times for every major region of the world. Investor expectations ran much higher than reality. The Federal Reserve and every other central banker admitted to being over optimistic for the past several years. The market might be accused of the same with an annual return that was 3.7 times better than the long-term average. Great expectations ran rampant in the market of 2013. What about 2014?

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Economic conditions are improving globally. Employment is and has been a major concern for several years as Americans look for a return to low unemployment rates and higher earnings. Employment has improved steadily for the past several years as fewer people are showing up for unemployment benefits and more and more people are working at full times jobs. The unemployment rate has fallen from above 10% to 7%, well ahead of the Federal Reserve Bank's expectations.

Housing is also an important component of the American economy as more citizens own their own home than anywhere in the globe. House values influence wealth, which relates to consumer confidence. New home sales in the later part of 2013 reached an annual rate of 469,000, a five-year high. Housing values are up 13.6% since last year adding significantly to household wealth, along with improved stock prices reflected in investment portfolios and retirement plans. When combined with low inflation rates of 1.%, housing affordability has actually improved. More houses are being built and prices are improving which has contributed to consumer confidence improvements.

Housing and employment are not the only areas of improvement. Consumers are deleveraging by reducing debt. Consumer's financial condition is much improved and able to take on financial shocks better than a decade ago. Energy is no longer considered an economically constraining factor as the U.S. now extracts more energy related resources than ever before. Energy related supplies and revenues are boosting economies in the Middle East, Europe and Americas without constraining growth. Europe is also improving economically where corporate earnings improvements may fuel expansion. Earnings per share at European companies are expected to climb as much as 14% in 2014. This has led to an expectation of European GDP growth in positive territory by 1%. Mexico has strongly improving exports.

With such promising economic conditions and outlook why would an investor not expect 2014 to be better than 2013? Much of 2014's market activity will depend upon how much of 2014 expectations are imbedded into 2013 market prices. Remember, the markets are forward looking and may have anticipated much of what is going to happen already.

The economy drives corporate earnings. In a good economy, earnings are expected to improve while a slow economy makes it more difficult to generate profits. A public company's ability to generate earnings is reflected in the stock price and creates a fair value. If market prices move ahead of fair values it can be argued that expectations for earnings and correspondingly the economy are favorable. But, what happens if the market moves ahead too fast, faster than reality? Several things can happen if the market gets ahead of the economy. If it is only slightly ahead the market can wait (move sideways) while corporate earnings catchup to market expectations. Another possibility is that new favorable economic data comes into play and the fair values also move upward and begin to match the market values. Caution begins to prevail when economic conditions do not improve as well as expected and the delay in reaching the expected economic levels is far ahead. The market may move back to fair value and as a result loose value in the short term. A disappointing condition to be sure, but not as bad as a misevaluation such as that which took place in the mortgage crisis where housing values and the mortgages surrounding them were initially valued a much higher prices only to find that the real value was at a deep discount. In such cases, the market will make a quick change and move to an undervalued position. I do not

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believe 2014 will be a year of robust growth, but it will also not be a year of negative value. As you can see from the charts and my previous comments, the market continues to move higher into overvalued territory. Market values are outstripping fair values. We are in a caution area, but not to an extreme where we would begin to expect a large correction. I believe we will see sideways to slightly upward movement through most of 2014; it will not be a repeat of 2013. The economy will continue to improve, but the market is a bit ahead of the economy right now.

While this is mostly positive news we still have several major negative influences that could surprise the market. The Federal Reserve holds more debt on the balance sheet that ever before, some $4 trillion now and adding every day. Japan may not be able to stimulate the economy with the increase in sales taxes. Wars and unrest in Syria, Iraq, Turkey and Korea could all spill into major confrontations and inflation could surprise the central banks just as it has many times previously. It is all about probabilities and I believe we have a 60% probability for continued slow growth and a positive market, just not as positive as 2013, a 20% chance of exceptional growth and market, and a 20% probability of economic surprise and negative markets.

If you have any questions regarding the information presented or wish to ask any specific portfolio questions, please do not hesitate to write me at salbrecht@chartertrust.com.