LAUREATE
WEALTH MANAGEMENT

2013 Investment Outlook
January 18th, 2013

Dear Clients and Friends,

I would like to focus this commentary on three trends which I believe will have a larger positive impact on the US economy going forward than the broader investment community expects:

1) **America's Energy Revolution**
2) **A Consequent Manufacturing Renaissance**
3) **Stabilization of the Real Estate Market**

America's Energy Revolution: The US Energy Information Administration (EIA) estimates that 750 trillion cubic feet of recoverable shale gas exists and 24 billion barrels of recoverable shale oil exists within US borders. The EIA further estimate that US oil imports will decline by 50% over the next 30 years. In fact, the trends in the above estimates have been moving higher as more shale plays are being discovered around the country. Skeptics maintain that shale wells deplete more quickly than conventional wells and are far more expensive to drill. In spite of these reasonable objections, I believe this shale work is going to have a major positive impact on the US economy. For one thing, this trend is likely to gain political support from both Republicans and Democrats --- more jobs, more taxes, and greater independence from foreign oil. It seems likely that shale drilling will continue for a number of years and have a revolutionary impact on our economy.

A Consequent Manufacturing Renaissance: An unintended consequence of this shale work will likely be the healthy deflationary impact on natural gas prices and potentially on oil prices caused by this increase in supply. Manufacturing processes which carry high energy costs will naturally be incentivized to move production toward lower cost energy sources --- back to the US. "Made in the U.S.A." is likely to again become a strong political and marketing theme in such industries going forward.

Stabilization of the Real Estate Market: Real estate valuations do not need to rise substantially to become attractive investments --- they merely need to stabilize and are doing so now. Banks hate to lend on assets which are declining in value. As valuations have begun to stabilize, bank underwriters can now appropriately underwrite risk and loan money. Accordingly, with interest rates at historic lows, there are numerous real estate investment themes yielding significant cash flows while also providing an inflation hedge. These investments compare very favorably to the yield opportunities currently available in the bond market. I believe that substantial capital will rotate into real estate from the bond markets over the next couple of years. This will, in turn, spur significant economic activity in the construction industry enabling the re-employment of "unskilled" labor --- one of the hardest hit population segments in the 2008 recession.

In contrast to this exuberance, there are certainly substantial risks in the investment universe. Most of them are widely known and discussed ad nauseam in the financial press. As a quick review, I list them below.

1) Eurozone recession: We have mostly forgotten about Europe in the last 90 days or so. As nothing has been legitimately solved in Europe, it is likely we will again be reading about Greece, Spain, Italy, and perhaps even France this year.
2) Middle East geopolitics: While outright war does not appear imminent, the role of the US in the Middle East is being vastly redefined. Regardless of your view on this redefinition --- change creates the potential for instability.
3) Japan: Unsustainable. In the words of John Mauldin --- "Japan is a bug in search of a windshield." They are 20 years further down the road of deficit spending than the US without any viable solutions.
4) Debt ceiling / deficit spending: As a nation we simply cannot continue to overspend our resources. We are beginning to head toward a Japan scenario.
5) Demography: The US birth rate is now at the lowest it has ever been at 63.2 per 1,000 women of child bearing age. This equates to 1.9 children born per woman which is nearly 50% less than 50 years ago. More importantly, it is less than the 2.1 rate needed to maintain the current population of the US. Consequently, the baby boomer generation is retiring into a shrinking wage-earning population. This risk is rarely understood and even more rarely discussed in the financial press.
6) Risk-off charts: On a more near-term basis, short interest on the NYSE is cyclically low and thus technically bearish for stocks. Long term mutual fund and ETF flows last week topped $22 billion, which is the second highest tally on record. The highest tally occurred in September of 2007 at $22.8 billion --- just before the 2008 recession. Third place was recorded in March of 2000 --- on the edge of the tech bubble.

Conclusion: Overall, I am more constructive on the medium term outlook for the US economy than I have been in quite some time. While there are certainly substantial headwinds which will undoubtedly cause market pain at points along the way, I believe there are now some undervalued tail winds which are creating excellent risk adjusted opportunities in specific market segments. As always, please feel free to contact me with any thoughts or questions.