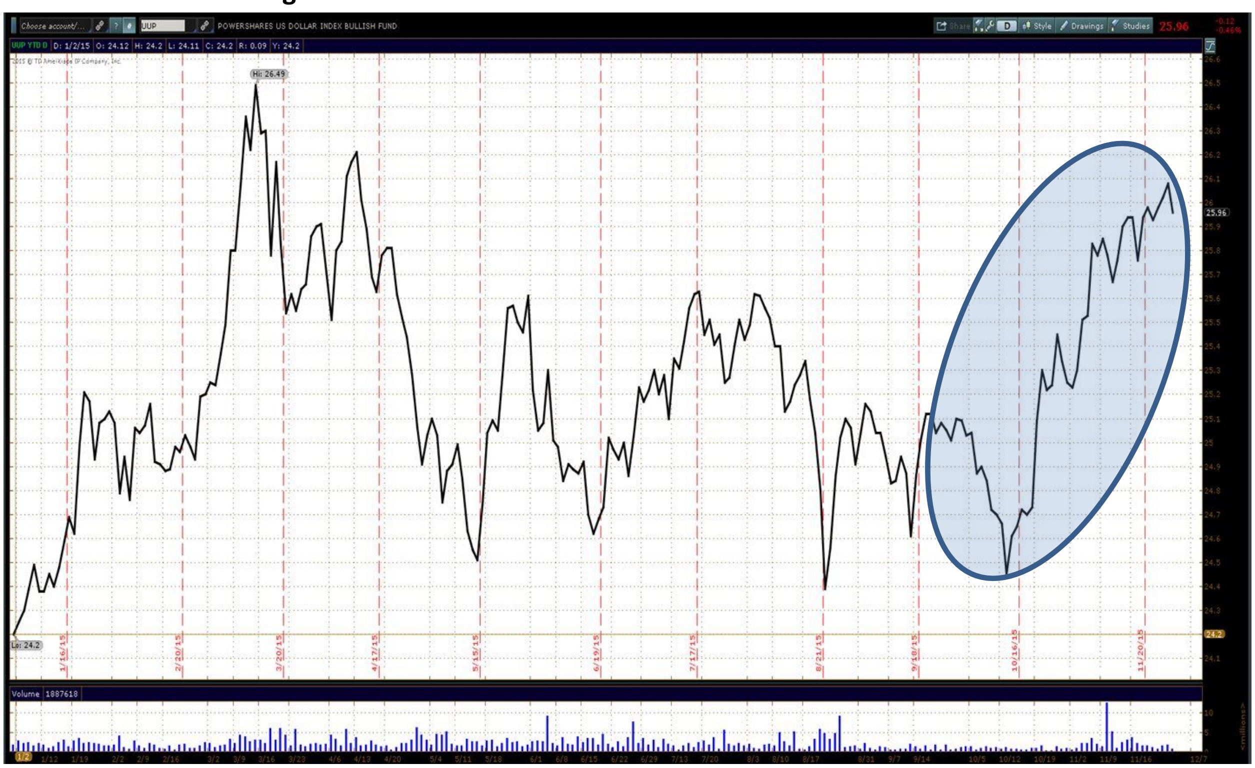
Monthly Market Returns

Index	1 – Month Return	Year to Date Return
S&P 500	-0.42%	1.77%
Russell 2000	1.25%	-0.32%
MSCI EAFE	-0.82%	0.55%
Barclays Bond Index	-0.20%	-1.20%
Brent Crude	-11.08%	-32.66%
Gold Spot Price	-6.48%	-10.20%

The month of November was largely much ado about nothing for both equities and fixed income. Small cap stocks as evidenced by the Russell 2000 did modestly better than their large cap counterparts. The biggest movers were Brent Crude Oil and Gold both driven in large part by a much stronger US Dollar which brings us to our Chart of the Month below:

US Dollar Index: Trailing 12 Months



The above indicates movement in the price of the US Dollar versus a basket of major currencies over the past year and indicates a great deal of volatility and a very strong move higher for the Dollar over the past month in the highlighted area. The Dollar has strengthened simply because the Federal Reserve appears more likely to raise the Federal Funds Discount Rate before year end, albeit modestly. This is occurring amidst a back drop of interest rate cuts occurring in places like Europe and Japan. Generally speaking, it can be profitable to borrow in currencies with low rates, such as the Euro, and buy currencies with higher rates, such as the US Dollar. This is called the "carry trade" and is coming back to life now that the US is increasingly likely to raise rates. It must be underscored that rates have not yet risen and that if they do rise they will likely do so quite slowly. The strong, upward momentum of the Dollar at the prospect of a slight rate increase that hasn't even happened yet is an indicator of how starved for yield many segments of the capital markets truly are.

The Dollar matters for many reasons but in looking at November's commodity performance it is the single biggest factor contributing to the decline in both oil and gold. All else being equal, when the Dollar strengthens, commodities such as oil and gold go down. Given the sharp, upward trajectory of the Dollar this past month it is clear the negative, short-term impact this has had on the commodity segment.

The obvious question is whether or not the worst is over for commodities and is there a buying opportunity in that space. Our view is a firm "maybe" in the short term and a more confident "probably" a few years out. The market is pricing-in virtually no geopolitical risk into the price of crude which, given the state of affairs in the Middle East, is rather counterintuitive. While it is true that the US has grown its production of oil a great deal, rising to north of 9 million barrels/day, we are still reliant on Middle East oil flow to meet the global demand of crude. Were that to be meaningfully interrupted by rogue powers in the region prices could spike dramatically. It is impossible to handicap the likelihood of such events but sufficed to say we feel confident that there are more forces at play that could drive oil and gold up over the long term then not.

Currencies, Currencies, Currencies

Aside from the dramatic move in the Dollar another significant event occurred in the currency markets on 30 November. The International Monetary Fund (IMF) announced that the Chinese Yuan would now be part of its official basket of world currencies which also include the US Dollar, the British Pound and the Japanese Yen. On a practical level, this news has little importance but on a symbolic level it is monumental. It means that China and its currency is moving from being part of the developing world to being a financial world power. It means that its currency can act as a more legitimized store of value. We think this could turn out to be very good news particular in terms of relieving pressure on an already highly-valued US Dollar. A richly-priced Dollar is great if you're travelling abroad but terrible if you're selling your goods overseas as it makes your exports more expensive. In short, having the Yuan as a part of a family of accepted global currencies could be great to US multinational companies struggling with the strengthening Dollar. As with all things, time will tell.

What We're Watching in December

Rate Increase Announcement

ECB Stimulus Announcement

Oil & Commodities Bounce?

Sincerely,

The CAPSTONE Team