Upcoming Events

Lucien, Stirling & Gray invites you to attend our

22nd Annual
Holiday Party and Open House

Thursday, December 12, 2013
3:30 to 7:00 pm

RSVP: 512-458-2517 or by email to info@lsggroup.com

General Market Results

	2nd Quarter	YTD	One Year	Three Year	Five Year	Ten Year
CPI	0.16%	1.86%	1.07%	2.30%	1.34%	2.36%
Barclays Agg Bond	0.57%	-1.89%	-1.68%	2.86%	5.41%	4.59%
S&P 500	5.25%	19.81%	19.35%	16.26%	10.02%	7.56%
DJI	2.12%	17.64%	15.59%	14.94%	9.93%	7.74%
S&P 400	7.54%	23.23%	27.68%	17.45%	13.08%	10.84%
Russell 2000	10.21%	27.69%	30.06%	18.29%	11.15%	9.64%
NASDAQ	10.82%	24.90%	21.03%	16.77%	12.51%	7.76%
MSCI EAFE	11.61%	16.59%	24.29%	8.97%	6.85%	8.50%
MSCI EM	5.9%	-4.05%	1.33%	0.00%	7.56%	13.16%

Lucien, Stirling & Gray Advisory Group, Inc. is a Registered Investment Advisory firm providing fee-only asset management, fiduciary-level advice and financial planning services to individuals, corporations, trusts and foundations.

For more information about our firm, please visit our website at www.lsggroup.com • Model holdings may change due to ongoing management • Sector and style breakdown is constructed with the best available information and therefore is only as accurate as the available information • Past performance is no guarantee of future results • It is impossible to invest directly in indices • Percentages may not equal 100 due to rounding

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Lucien, Stirling & Gray Advisory Group, Inc.

Third Quarter Report 2013

October 2013

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A MESSAGE FROM THE PRESIDENT

Thomas G. Twombly

We're pleased to provide you with our report for the period ending September 30, 2013.

First, I'd like to say "Thank you" to all of you for maintaining patience and discipline throughout the provocations of the last six years, and also the last few months. We continue to be subject to a rolling series of real or imagined "crises" that test that resolve, I know, and I want to acknowledge the fantastic job you've done in following our advice and sticking to your long-range plans when many others have succumbed to the ever-present temptation to react to the news of the day.

Maintaining an imperturbable calm and a resolute focus on the practices we can control, such as thoughtful asset allocation, broad diversification and periodic rebalancing has not been easy in the face of all the challenges we've faced together. Nevertheless, it has paid off handsomely in the long run, and it certainly paid off in the last quarter as well – as you can tell from the second half of this report. No doubt, given the likelihood of on-going provocations, we must all be prepared to exercise those principles and practices some more as we move forward. But rest assured it is a pleasure, and a real reward, for us to serve so many great clients who "get it." Thanks.

"If it weren't for Washington…" is a phrase repeated so often recently that it's become a national joke. (Have you heard about the social effort to change the name of the Washington Redskins – and drop "Washington" because it's so offensive..?) But in many ways that phrase sums up the primary roadblocks that are retarding what might otherwise be impressive growth in the domestic and global economies. A clumsy "sequestration" that was never really intended to be implemented, gridlock in Congress, and massive political uncertainty surrounding U.S. Government policy here and abroad have kept individual investors and consumers on edge, and they've led to muted capital spending by cash-rich corporations that otherwise might be expanding and hiring.

"It is a pleasure, and a real reward, for us to serve so many great clients who "get it." Thanks."

In spite of these considerable headwinds, what we've experienced so far is a continued strengthening in the U.S. economy. Unemployment has been steadily declining, and jobless claims are now at 5-year lows. Household net worth is now at a record high, up $18 trillion dollars since the lows seen in the first quarter of 2009. Home prices continue to climb higher – up 19% in the last eighteen months according to the S&P Case Shiller index. And automobile sales are experiencing a powerful rebound, up 72% since the June 2009 lows based on three month moving averages.*

On balance, there is still room for continued gradual improvement in spite of the significant gains we've seen already. Corporate cash as a percentage of assets is still very high in historical terms, and cautious companies have not replenished their workforces. Additionally, labor costs are quite manageable thus far, with little indication of inflationary pressures. Housing affordability is quite high in an historical context, with low mortgage rates and comparatively high rental rates. And new household formation, which had been retarded significantly in recent years, is now outpacing current construction rates and thus exerting long-term upwards pressure on real estate prices.

In turn, rising home values and improving labor conditions are gradually helping to lift consumer confidence, suggesting that continued confidence may lead to further strengthening in new car sales as the average age of light vehicles on the roads today is still quite high in an historical context. In other words, in spite of the dire headlines and in spite of the lack of leadership in our nation's capital, our powerful economic engine is showing continued signs of wanting to rumble. Imagine what might happen if we could get out of our own way.

Against this backdrop, and because of the number of recent articles and pundits referring to bonds as among today's riskiest asset classes, we have had a few inquiries about whether they should be eliminated entirely from long-term portfolios. Though we have reduced allocations in this asset class considerably during the last few years, and while we continue to be cautious about the long-term outlook for interest rates, our answer to this question is an emphatic "no." Equity markets are inherently volatile, and the law of market cycles has not been repealed. At some point we will surely experience a sharp downdraft in equity prices, however temporary that may ultimately prove to be, and reasonable allocations to fixed income securities can provide a valuable buffer against that volatility. Maintain that patience and discipline, and carry on.

Thank you for your confidence and trust.

Thomas G. Twombly
President

* Deutsche Asset & Wealth Management – 3rd Quarter Market Outlook

INVESTMENT COMMENTARY

In an interesting counter-balance to our investment commentary of last quarter, one of the most significant developments of the July – September period was the Federal Reserve's decision not to "taper" their purchases of U.S. Government debt quite as quickly as many market participants had expected. Perhaps in a prescient reflection that continued acrimony in Congress, and the rising risk of additional debt-ceiling fights might place substantial burdens on economic growth and consumer confidence towards the end of the 3rd quarter, Fed Chairman Ben Bernanke confirmed in early in September his previous announcements that so-called "quantitative easing" would likely continue into 2014.

The effects of this were immediate. Interest rates on the 10-year Treasury, which had reached a 2-year highpoint of almost 3% on September 5th, fell sharply to just above 2.6% by the end of the month as short-term traders sought to cover their bearish bets on bonds. The net effect of this was that all sectors of the domestic bond markets experienced positive, though muted, results for the quarter. The one exception to this was the high-yield bond sector, which provided total returns of 2.3% for the quarter, and helped augment solid results in the fixed income portion of many of our more growth-oriented portfolios. While we continue to remain cautious on the outlook for interest rates and overall returns in the fixed-income marketplace, we are quite pleased to note that each of our select fixed-income managers has performed in the top quintile of their respective peer groups for the recent quarter and for the year so far.

Equity markets in general also responded positively throughout the quarter, with particular late-quarter strength noted in sectors such as emerging market stocks, natural resources, and domestic and international real estate, which had suffered in the previous quarter due to concerns about Fed tightening and a strengthening dollar. Each of our modest holdings in these sectors performed nicely, adding welcome benefit to what had otherwise been very solid performance from our core domestic and international equity holdings.

The most noted strength of the quarter came from developed international equity markets. The MSCI EAFE Index rose by 11.6% for the period, aided significantly by resurgence in European equity markets. Europe-ex the UK rose by 14.5% in U.S. Dollar terms**, demonstrating once again that long-term investors can benefit substantially by maintaining broad diversification outside of U.S. equity markets. We're particularly pleased to note that, in addition, several of our select international money managers trounced their respective benchmarks for the period.

While U.S. Large-cap stocks as represented by the S&P 500 also did very well for the quarter, they were far outstripped by small-cap and mid-cap U.S. equities, which continue to benefit from increasing asset flows as investors recognize that values in these sectors remain quite attractive relative to their large-cap brethren. The S&P 500 rose by 5.25% for the quarter, while the small-cap Russell 2000 index jumped by 10.21% and the mid-cap index rose by 7.7%. Notably, the growth portion of each of these indices provided the lion's share of the overall gains, with large-cap growth providing 8.1% gains, mid-cap growth providing 9.3% and small-cap growth providing 12.8%**. Again, we were particularly pleased to see these results as we have taken great care to make sure each of our portfolios has ample allocations to small and mid-cap equities in addition to large-cap stocks, and the select money managers we have chosen in each of our model portfolios has tended to be overweight in the growth portions of their respective holdings. Looking forward, despite recent outsized gains in these growth-oriented holdings, these sectors remain considerably less expensive than their value and blend counterparts based on historical averages.

As a final note, it's worth mentioning that despite repeated and on-going media negativity, we have experienced one of the most powerful bull markets in history during the last 4 1/2 years. While generally we view this persistent negativity as a good sign, as it suggests there are still plenty of non-believers with lots of idle assets still on the sidelines, it's nevertheless the case that the S&P 500 has provided total returns of 174% since the lows of March 2009, and the Russell 2000 is up a whopping 233%.** With those types of returns in the rear view mirror, investors would do well to prepare themselves for an inevitable correction at some point in the future. Though we believe we may still be in the relatively early stages of a long-term growth phase that could encompass another 12-15 years, markets never go straight up in those environments forever. Wise investors make sure to temper their expectations, and prepare their emotions for periodic short-term setbacks. As always, please call us if you would like to discuss your particular situation.

** JP Morgan Asset Management – 9/30/13 Guide to the Markets

Conservative Growth Model

3rd Quarter	YTD	1Year	3 Year	5 Year	10 Year
3.89%	10.27%	11.79%	5.70%	4.93%	5.75%

Inception Date 06/03/1999

Core Growth Model

3rd Quarter	YTD	1Year	3 Year	5 Year	10 Year
5.97%	11.55%	13.63%	7.29%	6.85%	6.43%

Inception Date 05/31/2003

Growth Model

3rd Quarter	YTD	1Year	3 Year	5 Year	10 Year
8.86%	15.04%	16.04%	7.59%	7.34%	8.23%

Inception Date 10/16/1992

Specialty Model
Diversified Growth Model

3rd Quarter	YTD	1 Year	3 Year	5 Year	10 Year
7.04%	18.63%	21.14%	11.65%	8.29%	7.90%

Inception Date 10/31/00

Education Models
UT ORP

3rd Quarter	YTD	1Year	3 Year	5 Year	10 Year
6.03%	12.90%	15.34%	8.73%	5.73%	6.22%

Inception 08/10/1999

Retirement Growth

3rd Quarter	YTD	1 Year	3 Year	5 Year	10 Year
5.61%	13.30%	15.55%	9.83%	7.19%	7.68%

Inception Date 06/03/1999

Growth & Capital Preservation

3rd Quarter	YTD	1 Year	3 Year	5 Year	10 Year
5.25%	10.09%	10.54%	6.70%	6.22%	6.22%

Inception Date 11/30/2001