NORTHWESTERN MUTUAL WEALTH MANAGEMENT COMPANY

MARKET COMMENTARY

FOR THE WEEK OF NOVEMBER 24, 2014

Anyone for 18,000?

Since the late September swoon that dragged the Dow into the red for 2014 and saw the S&P 500 flirting with a correction, both indexes have stormed back, reaching new highs almost as often as not, and last week was no exception, with the Dow turning the trick three times while climbing to 17,810.06 and the S&P 500 four times – for the year, the Dow is now up 7.4%, and the S&P 500 is up 12%. Much of the rebound has been the result of the resurgent American economy, but late last week, words and actions by foreign central banks added to the momentum. However, all of the progress could be undone by the political tension that's been cranked up in the wake of the midterm elections that saw the GOP win the Senate.

In 2012, Mario Draghi, the president of the European Central Bank, reassured investors when he declared that he would do "whatever it takes" to save the euro. On Friday, with the euro alive but on life support, he introduced a variation on the theme, saying the ECB would do "what we must" to boost growth and avoid deflation, which some believe can only happen with a Fed-like round of bond buying. He said the ECB was ready to "step up the pressure" and "broaden even more channels through which we intervene." On the same day, reacting to its recent slowdown and the failure of earlier measures taken to stimulate borrowing and lending, China's central bank unexpectedly cut its benchmark rate from 6% to 5.4%. The first rate cut since the summer of 2012, the hope is that it will help revive the housing market and also increase China's demand for commodities. Stock indexes around the globe soared on the news from the two central banks.

Key Market Data

Week ending...	11/14/2014	11/21/2014	Change
S&P 500 Index	2,039.82	2,063.50	+1.16%
MSCI EAFE Index	1,813.19	1,831.20	+0.99%
BarCap U.S. Aggregate Bond Index		1,902.57	
10-Year Treasury Note Rate	2.320%	2.317%	-0.3 basis pts.
Trending			
NYMEX Crude Future (Barrel)	$75.82	$76.51	+0.91%

The showdown in Washington

The republicans won't take over Congress until January, but President Obama took a step designed to make the new political order more fraught, choosing what *The New York Times* described as "confrontation over conciliation" by

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issuing a directive that would allow up to five million illegal immigrants to work legally (though they weren't offered citizenship). The GOP had already begun to flex its muscles, with the House passing the Keystone XL pipeline (it died in the Senate), and last week it filed a lawsuit aimed at overturning Obamacare, casting doubt on the prospect of any bipartisan progress on such issues as the deficit and trade during the president's last two years in office.

Japan's latest recession

Japan unexpectedly fell back into recession, calling into question the dramatic steps to revive the economy that have been taken by Prime Minister Shinzo Abe. With estimates running as high as 2%, GDP instead fell 1.6% in the third quarter from a year earlier after a 7.3% decline in the second (two consecutive quarters of contraction is considered to be a recession). Mr. Abe promptly dissolved Parliament and called for new elections, while also suggesting he might put off the second sales tax hike scheduled for October 2015 – the first hike, in April, is seen as the main reason for the second-quarter contraction. Mr. Abe said, "Raising the consumption tax is supposed to increase government revenues, but if we fall back into deflation it will all be for nothing." It is Japan's fourth recession since 2008.

The Fed shifts its sights

The Fed released the minutes of its last meeting on Oct. 27 and 28, and it seems as if rates will remain low until inflation nears the 2% mandate, now that employment is not as pressing. Thanks in part to lower gas prices, the annual rate of inflation has now been below 2% for 29 months. In addition, the minutes indicated that Fed members were not especially concerned about economic weakness in Europe and Asia, nor the recent stock market volatility, describing "the effects of recent developments on the domestic economy as likely to be quite limited." The minutes also said the Fed would hold its short-term rate at its current record low for a "considerable time," interpreted as mid-2015.

As evidence of the low rate of inflation, consumer prices were flat in October, while core prices, excluding food and energy, rose just 0.2%. Over the last year, consumer prices have risen 1.7% and core inflation 1.8%. The producer price index increased 0.2%, while core PPI climbed 0.4%; for the past 12 months the PPI was up 1.5% over the last year, with core prices having gained 1.8%.

In other economic news, the Commerce Department said that single-family home starts, which account for more than two-thirds of the market, rose 4.2% to 696,000, the fastest pace since last November. Multifamily homes fell 15.4%, so overall starts were off 2.8% to 1.009 million. Building permits jumped 4.8% to 1.08 million, the highest rate since June 2008. The National Association of Realtors reported that sales of existing homes were up 1.5% to 5.26 million compared to 5.18 million in September. It was the first month this year that sales rose on a year-to-year basis, climbing 2.5% from October 2014. Manufacturing output increased 0.2% in October, the Fed reported, and is up 3.4% over the last year. Total industrial production dropped 0.1%, while capacity utilization was off 0.3% to 78.9. First-time jobless applications fell 2,000 to 291,000 as the four-week moving average was ticked up to 1,750 from 287,500. And the Conference Board said its index of leading indicators increased 0.9% in October.

A look ahead

This week's releases will include Markit's services and composite purchasing managers' indexes, the first revision of third-quarter growth (forecast to be revised down from 3.5% to 3.3%), and the latest on personal consumption, pending and new home sales, the S&P/Case-Shiller home price index, durable and capital goods orders, personal income and spending, and consumer confidence. The markets will, of course, be closed Thursday – Happy Thanksgiving – and the week will end with that annual shopping frenzy, Black Friday.

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Please remember that all investments carry some level of risk, including the potential loss of principal invested. Indexes and/or benchmarks are unmanaged and cannot be invested in directly. Returns represent past performance, are not a guarantee of future performance and are not indicative of any specific investment. Diversification and strategic asset allocation do not assure profit or protect against loss. Although stocks have historically outperformed bonds, they also have historically been more volatile. Investors should carefully consider their ability to invest during volatile periods in the market. The securities of small capitalization companies are subject to higher volatility than larger, more established companies and may be less liquid. With fixed income securities, such as bonds, interest rates and bond prices tend to move in opposite directions. When interest rates fall, bond prices typically rise and conversely when interest rates rise, bond prices typically fall. This also holds true for bond mutual funds. When interest rates are at low levels there is risk that a sustained rise in interest rates may cause losses to the price of bonds or market value of bond funds that you own. At maturity, however, the issuer of the bond is obligated to return the principal to the investor. The longer the maturity of a bond or of bonds held in a bond fund, the greater the degree of a price or market value change resulting from a change in interest rates (also known as duration risk). Bond funds continuously replace the bonds they hold as they mature and thus do not usually have maturity dates, and are not obligated to return the investor's principal. Additionally, high yield bonds and bond funds that invest in high yield bonds present greater credit risk than investment grade bonds. Bond and bond fund investors should carefully consider risks such as: interest rate risk, credit risk, liquidity risk and inflation risk before investing in a particular bond or bond fund.

All index references and performance calculations are based on information provided through Bloomberg. Bloomberg is a provider of real-time and archived financial and market data, pricing, trading, analytics and news.

Standard and Poor's 500 Index® (S&P 500®) is a capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

Standard & Poor's offers sector indices on the S&P 500 based upon the Global Industry Classification Standard (GICS®). This standard is jointly maintained by Standard & Poor's and MSCI. Each stock is classified into one of 10 sectors, 24 industry groups, 67 industries and 147 sub-industries according to their largest source of revenue. Standard & Poor's and MSCI jointly determine all classifications. The 10 sectors are Consumer Discretionary, Consumer Staples, Energy, Financials, Health Care, Industrials, Information Technology, Materials, Telecommunication Services and Utilities.

The MSCI EAFE Index measure international equity performance. It comprises the MSCI country indices that represent developed markets outside of North America: Europe, Australasia and the Far East.

Barclays Capital US Aggregate Bond Index is a benchmark index composed of US securities in Treasury, Government-Related, Corporate, and Securitized sectors. It includes securities that are of investment-grade quality or better, have at least one year to maturity, and have an outstanding par value of at least $250 million.

The 10-year Treasury Note Rate is the yield on U.S. Government-issued 10-year debt.

NYMEX Crude Future is the futures price on a barrel of oil on the New York Mercantile Exchange.

The European Central Bank (ECB) is the institution of the European Union (EU) which administers the monetary policy of the 17 EU eurozone member states.

The U.S. Department of Labor Consumer Price Indexes (CPI) program produces monthly data on changes in the prices paid by urban consumers for a representative basket of goods and services.

The U.S. Department of Labor Producer Price Index (PPI) program measures the average change over time in the selling prices received by domestic producers for their output. The prices included in the PPI are from the first commercial transaction for many products and some services.

The National Association of Realtors (NAR) is a real estate trade association involved in all aspects of the residential and commercial real estate industries. NAR also functions as a self-regulatory organization for real estate brokerage.

The Conference Board Leading Economic Index is intended to forecast future economic activity and is calculated by The Conference Board, a non-governmental organization, which determines the value of the index from the values of 10 key variables. These variables have historically turned downward before a recession and upward before an expansion.