Quarterly Market Update

June 30, 2012

Just about everything is slowing down in the global economy and as a result, capital markets declined in the second quarter of 2012. The S&P 500 was down 3.3%, the NASDAQ was down 5.1%, International Developed Markets were down 6.9% and Emerging Markets were down 6.7%. In each case, these markets are still positive on a year-to-date basis, but only NASDAQ is still up by more than 10% (12.7% to be more precise).

Ten year US Treasury Bonds declined in yield by more than 60 basis points (a basis point equals 0.01%) and finished the quarter at a stated yield of 1.60%. Since this was down from the 1.8% level at December 31, 2011, and bond prices move inversely with yield levels, bond investors are now comfortably positive in their year-to-date results.

The pace of economic expansion has slowed from 3.0% GDP growth in the 4th quarter of 2011 to 1.8% growth in the first quarter of 2012 and consensus estimates are for another 1.8% growth in the second quarter of 2012. A warm winter apparently helped boost economic data early in 2012 but with the result that the second quarter has slowed markedly.

Europe continues to grapple with what seems to be an ongoing succession of bail out requests from European Union member nations but they have yet to find a workable process. Meanwhile, the Eurozone continues to see slowing economic data and rising unemployment. Japan continues to stagnate economically and China has begun taking steps to mitigate the slowing that they are experiencing.

A notable exception to all these observations is that corporate earnings generally held up better than anticipated by security analysts and market strategists. Traditionally, the second quarter is when many companies hold their annual shareholders meeting. This year, as in most other years, company managements announced dividend increases. The surprise this year is the percentage of companies announcing dividend increases and the size of the increases, both being above the average of the past several years. This would ordinarily be taken as an indication that companies are confident of their capital position and the sustainability of their earnings. Even with all the regulatory and tax related uncertainty, I believe this represents the best indicator of corporate managements' assessment for their individual business going forward.

We remain fully invested in equities in spite of the uncertainty in economic and political arenas. Equities remain the single most adaptable investment in an uncertain environment and valuations reflect fully the risks facing the U.S. and world economies.

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