Quarterly Market Update

December 31, 2011

Even though market observers saw tremendous daily volatility throughout the last quarter of 2011, and during the full calendar year, the S&P 500 Index closed out 2011 at almost exactly the same level it began. This market behavior brings to mind the image of a roller coaster. It is a ride that has many ups and downs, twists and turns and yet begins and ends at the same level. It is the journey in between those end points that provides the essence of the experience.

In like manner, the individual investment experience and results were dependent on where funds were invested during the year.

Gold, although down from recent highs earlier in the year, was up about 10%. International equities, represented by the European Stoxx 600 was down 11%, while emerging markets, represented by the Shanghai B Index, was down 22%. Blue Chips, represented by the Dow Jones Average, were up more than 5%, while NASDAQ was down nearly 3%. Being well diversified probably meant returns near zero for the year. More than in most years, success was tied to investment selections.

The biggest winner this past year were investments in bonds, with returns being closely related to the length of the maturity - the longer the term of the bond, the better the return. Here it is important to note that the mathematics of bond investing make the continuation of such good results, not just unlikely, but virtually impossible. Interest rate levels on 30 year U.S. Treasury Bonds, currently at 2.9%, would have to decline to well below 2.0% by the end of 2012 to sustain such positive results for bond investors. (Bond prices move inversely to yield levels, so earning a higher overall bond return requires lower interest rate levels). That is why so many market pundits within the financial media are advising individuals to avoid bond investments in 2012.

For 2012 we believe the U.S economy will experience slow economic growth, slowing corporate profits, particularly from European operations of multinationals, and generally better equity returns. Conservative companies with above average dividend yields and with more focus on domestic markets rather than international ones, should do well in the unfolding economic environment. We continue to invest the maximum amount in equities consistent with our client's investment guidelines.

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