



“If, Then” 2012 Forecasts

Monthly Outlook: January 2012 Another year has passed and it’s time to review the past and predict the future. 2011 was a tough year for investors due primarily to continued concerns about over-indebtedness from the US to Europe. The U.S. lost its AAA status, and now all eyes are on Europe’s debt

Market Indices	YTD 2011
S&P 500 large cap	-0.00%
Russell 1000 large cap	- 0.51%
Russell 2000 small cap	- 5.45%
MSCI All World Index	- 9.91%
Europe	- 15.60%
Japan/Asia	- 16.57%
Emerging Markets	- 20.64%
U.S. Intern. Bonds, w/ interest	+ 7.73%
Commodity Index	- 14.01%
Global REITs	- 5.88%

and how they plan to avoid their own banking crisis. As you can see in the table above, global equities were down nearly 10% in 2011, with the U.S. faring better than International. U.S. bonds, however, produced a positive return in 2011. It was an upside down year where risk taking provided no reward. In addition to putting up with losing markets, we had record volatility both up and down throughout the year. As we put 2011 behind us, what can investors look forward to in 2012?

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We’ve read dozens of analyst forecasts for 2012 and there is one theme that we see. Most forecasts are well hedged with “If, then” clauses. If Europe doesn’t agree to a cohesive plan for their debt, then the markets could sell off dramatically. If Europe does agree on a debt restructuring plan, then markets could go higher. More than most years at this time, the forecasters see a wide range of potential outcomes. Each year, Barron’s interviews 10 well-known analysts and asks for their predictions. David Kostin of Goldman Sachs represents the group well with his “if-then” forecasts for the S&P 500 of 900 (if Europe stalls) and 1,400 (if it doesn’t). So he’s

predicting a 900-1,400 range, 1,250 target. Really? How is that helpful? As a group, the Barron’s roundtable has a mean prediction of 1,360 for the S&P500 (up 8.2% from 1,257, where we start the year). On the bright side, corporate earnings are remarkably good, and their balance sheets are strong with lots of cash. Valuations are somewhat low so this should add some protection to any downside potential. So overall the consensus is that 2012 will be a decent year, but extreme outcomes can’t be completely discounted either. What is safe to bet on is that 2012 will unlikely be a year of steady 1% per month gains with low volatility. Instead, we’re likely to see a 20% or more total range during the year, with months of up as well as down. As for Bonds and interest rates, interest rates are at near-record low levels. While continued demand for safety and certainty will likely keep rates low, there is more chance that rates creep a bit higher than go much lower. As a result, it’s probably the wrong time for investors to “chicken out” and go to All-Cash or All-Bonds; that would be chasing last year’s performance and is often the wrong thing to do.

Investing in 2012

Our strategy for 2012 is to be globally diversified including asset classes like US Bonds, Int’l Bonds, US & Int’l Stocks, Commodities, and REITs. We’re focusing more on dividend paying and interest bearing asset classes to provide cash flow during the slow periods. And most importantly, we continue our trend-following discipline to keep us fully invested in each asset class that is up-trending and trimmed back any asset class that is down-trending. By doing this, we’ll collect dividends and interest throughout the year, participate in any available growth, and protect from significant loss if needed. As we start 2012, nearly every asset class is up-trending and we’ve positioned portfolios for growth. It always feels good to start the new year making money - but we stand ready to raise cash if the tides turn. Here’s to a healthy and prosperous 2012 to us all. Cheers.