## Portfolio Shift Commentary: January 27, 2012

With most of the economic data in for December, it is almost time to close the books on 2011. In a nutshell, there were more positives than negatives during the closing months of the year, leaving the economic glass slightly more than half full. Admittedly this is a modest accomplishment. At this stage of a cycle, more than two years into a recovery, the economy would ordinarily be expected to follow a much stronger growth path. Instead, we are left wondering if more obstacles loom ahead, which could impede the modest progress that seems to be underway.

The most visible and immediate threat is the intractable European debt crisis that continues to defy a solution. So far, the U.S. economy has not been deeply affected, although exports are already starting to suffer as a result of the sharp slowdown among our European trading partners. No doubt, exports, along with capital spending, have been a few of the bright spots in our recovery.

We feel the U.S. will have to rely more on internal sources to drive growth in 2012 than was the case over the past two years. Not only is Europe on the cusp of a recession, but most emerging market nations, who are the fastest growing export destination for U.S. products, are also experiencing weaker growth. China, the third largest export market for U.S goods, has cooled down considerably, growth in Brazil has stagnated, and other developing Latin American countries are suffering from falling commodity prices. What's more, the sovereign debt struggles of the weaker euro zone members have sent the region's currency on a deep slide, with the euro recently hitting a 16-month low. That's because uncertainty over how the debt woes will play out has caused investors to flee the currency and place their funds in safer havens, particularly dollar-denominated assets. As a result, the dollar has strengthened, which makes U.S. goods more expensive on the global market place, reinforcing the drag on exports.

The question is whether the U.S. can find enough strength among domestic sources to drive the recovery on to a faster growth track. Most economists expect that growth will speed up from the tepid 1.7% GDP growth in 2011. There are still too many headwinds that are visible and some that remain under the radar, including the risk of a "credit event" should the euro debt crisis spread to the U.S. financial system.

There are bright spots in the economy which we continue to watch. By all accounts, the job market is improving, and even the housing meltdown has seen a modest revival underway. We feel that along with a slight increase in economic growth, the markets should also see modest growth in 2012. But, with so much uncertainly still looming, we continue to run the portfolios with a conservative bias. We continue to favor higher yielding market segments with strong dividends and we still feel higher than normal cash positions will help dampen market risk. Our most recent rebalance included the acquisition of a low volatility equity position, which we feel will help in our efforts to lower portfolio volatility.

As always, we thank you for your continued support.

Sincerely,

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