

NAIL JELLY TO A WALL

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President Theodore Roosevelt faced considerable political opposition to building the Panama Canal in the early 1900's. It was considered the greatest engineering feat of the age, ushering the start of faster global trade. President Roosevelt likened the intense political opposition for the canal to "trying to nail jelly to a wall." But over time and with much political wrangling the canal came to reality.

Today, the political challenges seem enormously daunting – involving the ongoing solvency of the Euro (and its banks) and the financial position of the US. For citizens and investors it seems painfully unstable - like a forest fire is near; or like bungee cord jumping (the up/down markets); watching for the paint to dry; or as impossible as nailing jelly to a wall. Bond market vigilantes are active in Europe; stock market vigilantes are active in the US. And it appears a sharp market reaction to the downside may be the only catalyst for political leaders (Europe or US) to come together putting aside present political ideologies.

November is historically a good month; though not so true in 2011. The month managed to conclude with a slight negative return including the worst Thanksgiving week performance since the 1930's. Focus centered on Italy and the US Super Committee of 12 failing in its mission to find federal budget cuts/savings. Client portfolios experienced similar slight negative returns (of course this follows a fantastic rebound in October). All year foreign exposure is negatively impacting the portfolio performance experience. Yet foreign exposure is critical to tactical strategy success in a multi-speed world. The US may be in a temporary growth patch as we conclude 2011, while Europe may be starting a recession; while foreign countries with low/no debt will provide faster economic growth to the world as a whole. In general those with heavy debt loads will be burdened to grow. Reducing debt is a very slow, multi-year process where slow economic growth is the dominant by-product.

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Style	November	YTD
Small Value	-0.1%	-6.0%
S&P 500	-0.3%	+0.6%
Mid Value	-0.4%	-4.8%
Small Growth	-0.5%	-2.8%
Mid Growth	-0.7%	-2.3%
Large Value	-0.7%	-3.7%
Large Growth	-1.0%	-0.6%
Foreign	-2.8%	-11.3%

Client Objectives (Stocks/Bonds)	November	YTD
20/80	-0.5%	-0.2%
35/65	-0.4%	-0.9%
50/50	-0.5%	-1.6%
65/35	-0.8%	-3.6%
80/20	-0.9%	-6.1%
95/5	-0.7%	-7.0%

As we put a wrap on 2011, this commentary is our final before preparing the year-end client newsletter in January 2012. By all accounts, 2011 was an exceedingly difficult year for investing using active (versus passive index) portfolio managers. Performance data indicates only about 23% of active stock managers (mutual funds and hedge funds included) are beating the S&P 500 through November 30. The "average" stock underperformed significantly since July when spiking market volatility jumped again. During heightened market volatility, many investors resort to market timing - which is an elusive trait that no one can master.

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NAIL JELLY TO A WALL -CONTINUED-

At present, all investments on earth feel lashed together with a single bungee cord that is yanking them up and down together. In times of great turmoil and uncertainty, this similar movement by different assets makes diversification feel pointless; all asset movements seem linked, or different asset correlations move to 1.0. In times of less stress, many assets move up and down at different rates and/or directions; correlations are 0.7 or lower; diversification offers benefit. Recently, the correlation among emerging market stocks is drifting away from developed stocks price movements. While US stocks are moving in tandem to other developed countries, emerging market stocks correlation (diversification benefits) is declining (improving). That's because the US and much of Europe must solve many of the same issues – rising debt and deficits. But, those stocks growing faster (due to less debt) and growing their dividends are trending better than the market.

Our client portfolios own no-load funds invested in bonds and stocks with an emphasis on financially strong companies – often displaying faster growth than the economy and also growing their dividend payouts. We are excited by this recent market development and prospect for alpha performance. It suggests active-managed funds should begin to offer increased performance advantage to passive index strategies. Retail investor confidence may then improve to permit the brave to try stocks again (heretofore all but abandoned). We believe our tactical portfolio strategy is out-front of the market, and will aid long-term investors with a real return hedge for inflation in a low interest rate environment (financial repression). Our portfolio focus still endorses stock funds and (not or) cash, and blended with a variety of other asset categories, designed to reduce risk.

We expect 2012 will still share its challenges relating to various political issues which will keep market investors on edge. But hopefully the tide is turning, and improving investment returns will be forthcoming. Please, in the meantime, avoid trying to “nail jelly to a wall”, but instead enjoy your favorite flavor on a peanut butter sandwich, stuffed in a donut, or on your morning toast.

We wish you a joyous Merry Christmas and Happy New Year!



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