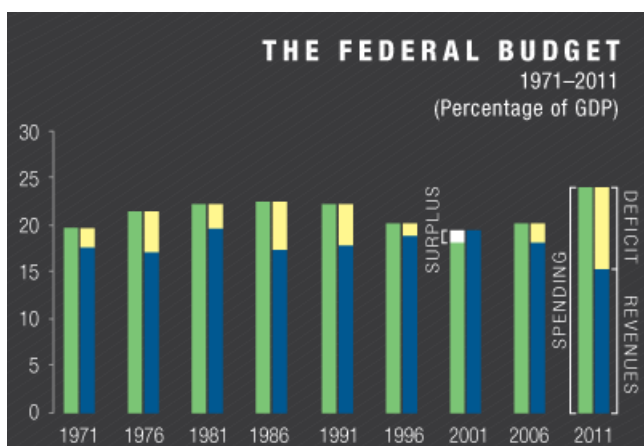


Observations

- ❑ After being bailed-out by the government (read US taxpayers), the banks continue to put the screws to consumers. The big four, JPMorgan Chase, Bank of America, Citigroup, and Wells Fargo, have been especially shameless. Both news reports and our client experiences confirm the dysfunctional state of the banks. Their transgressions range from excessive fees to denying credit-worthy borrowers (including rejecting applications to refinance mortgages or lowering interest rates of credit-worthy borrowers). And while government regulation is partially to blame, the actions of the banks show that they are no longer too big to fail, but too big to succeed.
- ❑ Three cheers for federal judge Jed Rakoff for rejecting a settlement between the Securities and Exchange Commission and Citigroup concerning an investment in which investors lost \$700 million. Judge Rakoff rejected the \$285 million settlement as “pocket change” for Citigroup and wondering what the SEC received “other than a quick headline”. In short, investors get fleeced by Citi, who when caught agreed to give back some of the profit. The judge recognizing the cozy relationship between Wall Street and the regulators did the right thing. Follow this one as it travels the path of judicial appeals. Fingers crossed that truth, justice, and the American way prevail.

Facts & Figures of Importance

Economic



While a picture is often worth 1,000 words, the above chart from the CBO can be simplified into spending exceeded revenue by \$1.3 trillion last fiscal year. The federal government has a huge spending problem that is rapidly becoming everyone's problem.

Economic Outlook

- North America – treading water while reshuffling debt.
- Europe – political fiddling while economies are burning.
- Middle East – greater instability in Iran and Syria move to the front-burner in 2012.
- Asia – growing, but slowing growth rates are a concern.
- Emerging Markets – overdue for a crisis.

Financial

	Treasury Yields		Equity Markets		
	5 Year	10 Year	MSCI EAFE	S&P 500	DJ Wilshire 5000
2007	3.45%	4.04%	2,253	1,468	14,819
2008	1.94%	2.96%	1,237	896	9,087
2009	2.69%	3.85%	1,581	1,115	11,562
2010	2.06%	3.38%	1,658	1,258	13,360
12/31/11	0.83%	1.89%	1,413	1,258	13,190
YTD Return			-14.82%	2.11%	-1.27%

Elsewhere in the World

A new equity index has been added to the overview to provide perspective on global equity markets. The MSCI EAFE Index (Europe, Australasia, Far East) is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US & Canada. The MSCI EAFE Index consists of the following 22 developed market country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Greece, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom

Investment Outlook

- Ignore the cheerleading by the media and those pushing product. Fundamentals will prevail in the end. Watch for sustainable earnings and revenue growth.
- Equity markets tend to begin the year on an optimistic note. Whether it holds or not is another story.
- While not “cheap” long term investors know that small cap equities can handsomely reward the diligent and patient.

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Insightful Thoughts of Others

...the U.S. in particular has rapidly acquired relative deficiencies over the last 20 years that will hamper the effective functioning and growth of its economy. Relative to other developed countries, and an increasing number of developing countries, we are sliding in some key areas that threaten loss of competitiveness:

- Notably depleted infrastructure
- Marked fall-off in the effectiveness of education and training
- Much decreased effectiveness of government, particularly in its ability or even willingness to concern itself with long-term issues.

--Jeremy Grantham

The bottom line is that 2011 was a year in which our political elite obsessed over short-term deficits that aren't actually a problem and, in the process, made the real problem — a depressed economy and mass unemployment — worse.

--Paul Krugman



A Few More Things

- A person caught shoplifting is immediately arrested and booked. So why aren't top executives and directors from MF Global in jail awaiting trial? Many MF customers still do not have access to their money as MF cannot account for their funds. Given the level of sophistication of accounting systems and back-up systems it should be a crime for customers not to be able to access their deposits within one business day. If the executives of MF were given 48 hours to find the money or be placed in a real prison with hardened criminals, those execs would be singing like canaries.
- Another supreme regulatory failure comes to light in the wake of MF Global. Why are not the regulators at least suspended without pay, fired, or under investigation? You may find it curious that after being out of the securities business for ten years, Jon Corzine received a pass from FINRA with respect to taking exams that are required for anyone actively involved in a firm's investment banking or securities business. FINRA guidelines require a person more than two years removed from the business to re-take exams. After the Madoff fraud and fiasco, every regulatory agency has had three years to get its act together. Is there any reason the lead regulators involved with supervising MF should continue to draw a salary from taxpayers until answers are obtained as to how this collapse happened?
- Let's say you are in a senior executive role at a publicly traded company. When a stock price is depressed, executives usually receive more stock options and other equity compensation as incentive to boost their share price. A stock price that remains too low for too long has cost many a CEO their job. There are political pressures for the economy and stock market to grow in 2012. Your earnings outlook is satisfactory however there is uncertainty. Do you bow to the pressure to attempt to juice earnings in anticipation of a political reward or to simply avoid any potential political repercussions? Do you ignore political considerations and let the chips fall where they may risking political blow-back?
- A quick tour of the world does not inspire confidence that better days are right around the corner. Asia appears to be slowing, led by China. Political unrest in North Korea and Pakistan along with the Afghanistan "conflict" will keep the world on edge. Think the fix is in for the Russian elections later this year? The Middle East seems to always be close to chaos, especially with Syrian unrest and the Iranian government up to hijinks. The economic woes of Europe are well known. In the US, all you need to know is that it is a presidential election year.
- Happy New Year!** Please ignore the Mayan calendar and other nonsensical forecasts. Have a wonderful 2012.

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