

SECOND QUARTER FINANCIAL MARKET COMMENTARY  
"NINETY DAYS IN NINETY SECONDS"  
JUNE 30, 2012

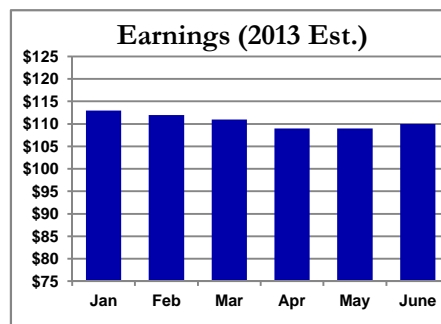
OVEREMPHASIZED AND OVER REPORTED

- ◆ We live in a world with numerous unresolved economic issues. Greece and the other southern European countries are dealing with recessionary economies and debt crises. Domestically, we have a dysfunctional political environment in Washington, stubbornly high unemployment and the approaching "fiscal cliff" of tax hikes. China and several other emerging market countries have seen a slowing in their growth rates. These issues are not "new news", yet they continue to dominate the headlines and create financial market volatility.
- ◆ Our view is that the risks associated with these issues are largely factored into current stock market valuations. The average price/earnings ratio over the past twenty years is 20x. Stocks are currently valued at a P/E ratio of less than 13x 2012 earnings. At these depressed valuations, stocks offer investors significant long term upside in exchange for the near term price volatility that surrounds the global macroeconomic uncertainty.

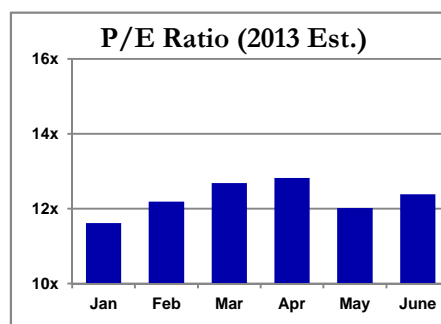
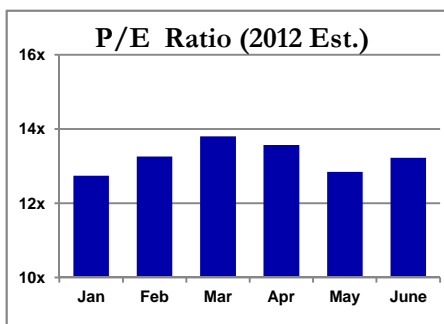
EARNINGS AND VALUATIONS

- ◆ Earnings estimates fell during the second quarter. Declines were experienced across seven out of ten economic sectors. However, the magnitude of the decline was an insignificant one half of one percent. Since stock prices fell by about three percent, valuations actually dropped during the quarter, making stocks more attractively priced.

S&P 500 Earnings Estimates

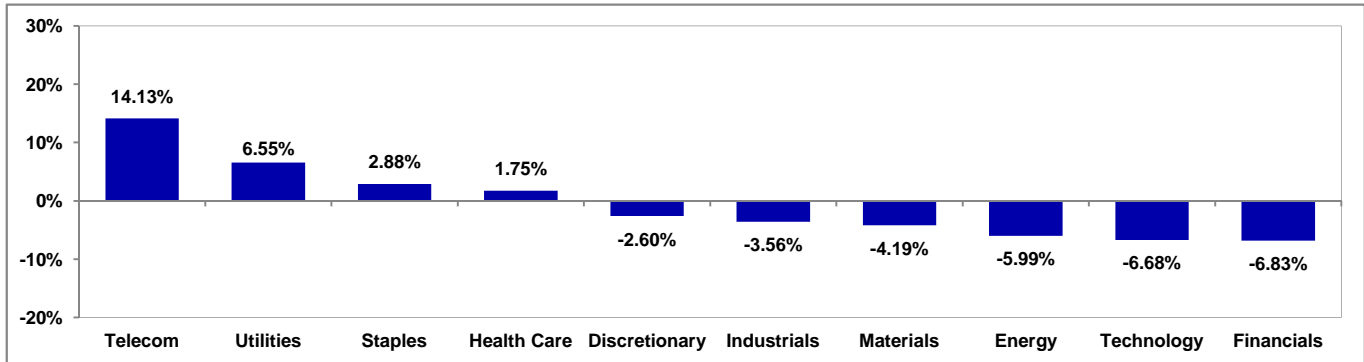


S&P 500 P/E Ratios

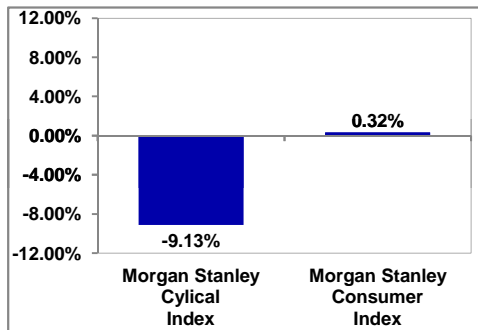


Second Quarter Investment Performance (including income)

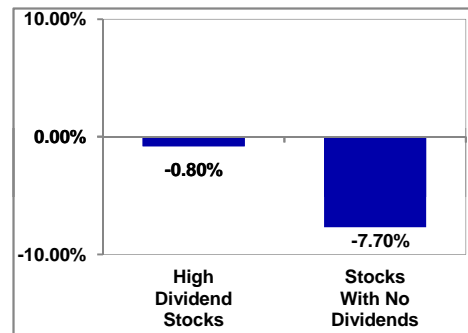
By Economic Sector



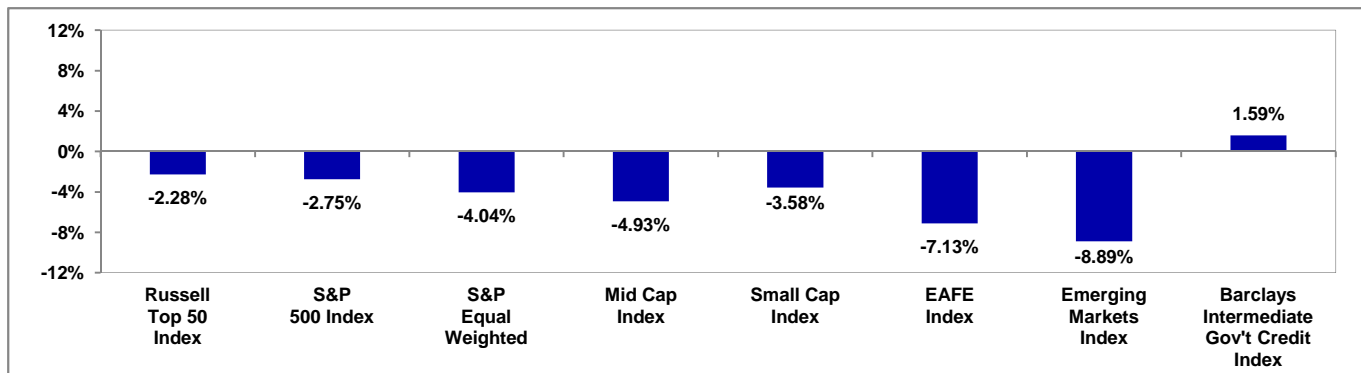
By Economic Sensitivity



By Dividend Yield



By Market Capitalization, Geography and Asset Class



- ◆ After a six month period of leadership from the more economically sectors, the pendulum of "risk on, risk off" swung back to a more defensive mode during the second quarter. At the sector level traditionally defensive groups all managed to achieve gains, while more cyclical sectors all declined. The same trends can be observed across factors as diverse as economic sensitivity, dividend yield and market capitalization.

### MY TWO CENTS ON EUROPE

- ♦ Europe's economic issues are long term problems that will require long term solutions. The recent decision to create a single euro-zone bank regulator is an important step in the long run viability of the euro. A second key issue to be resolved involves sovereign debt, liquidity and budget deficits. This will require sovereign austerity measures combined with private sector stimulus and will necessitate financial support from Germany. Such a combination will be difficult to achieve, but ultimately the Germans will see that it is in their best interest to hold the euro together. Lastly, significant trade imbalances exist between Germany and most of the remainder of Europe. To think about the issue of trade in a slightly different way, southern Europeans unfortunately expect a standard of living that their productivity cannot support. Dealing with these three issues and resolving the crisis conditions in Europe will be a long and tortuous road, but the proposal to create a single bank regulatory body is a necessary first step.

### GOOD NEWS ABOUT HOUSING AND AUTOS

- ♦ Two areas of consumer capital spending are showing signs of robust growth. Domestic auto sales have been strong for several consecutive months and new home sales hit a two year high in May. Home prices showed year-over-year increases in half of the twenty major markets in the Case-Shiller Index. Record low mortgage rates and an improvement in home buyer sentiment are allowing the residential real estate market to shake off global fears and continue to rebound.

### WHAT ELSE COULD GO RIGHT?

- ♦ In an environment of gloom and doom, it is important not to lose sight of what could go right. At some point in the future, politicians in Washington will have to display the qualities of statesmanship and leadership on crucial issues surrounding budget and tax policy. The pace of merger and acquisition activity is likely to accelerate as large cash balances, low interest rates, and low valuations spur strategic acquisitions. As dividends continue to rise, the income-oriented investor is likely to return to the equity market and begin to liquidate their low yielding bond investments.

### CONCLUSION

- ♦ The current environment may seem to be unique and therefore require a unique portfolio solution. However, the classic tenets of diversification, quality and dividends remain just as relevant in today's market as they have been in past time periods. Valuations are low, dividends are rising and diversification is an investor's friend. Long term investors should be rewarded by equity investments at current levels.