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CONSUMER HEALTH
IMPROVING

Despite an indecisive government, the corporate sector is generating record profits, and the consumer is healing.

The most recent evidence can be seen in rising retail sales figures, driven by a combination of pent up demand, aggressive retail pricing, and an improved consumer balance sheet (mortgage and credit card pay downs have been impressive).

For the Thanksgiving weekend:

- There were 226 million shoppers (up 6.6% from '10)
- Total spending was \$52.4B (up 16.4% from '10)
- The average shopper spent \$398.62 (up 9.1% from '10).

The results show a powerful combination of more shoppers, who on average also spent more.

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Has Vertigo Set In?

Market Overview & Commentary

After a major decline in Q3, global equity markets staged an impressive rally during October. The rebound was fueled in part by an improving economic picture in the US, but more importantly due to a belief that Europe was beginning to solve their debt crisis. Major compromise deals between European debtor and creditor nations were widely reported, and investors were encouraged that the worst was behind them.

The rally was short-lived, however, as improving US economic news was overpowered by renewed crisis in Europe, when tangible actions failed to materialize from prior promises made. Sovereign bond yields widened to unprecedented margins not only in Greece, but also in large countries such as Spain, Italy, and even France. These large rate rises threatened national defaults, major bank failures, and potentially even the unraveling of the entire European Union. Consequently, markets turned back down during early November and have only recently begun recovering on more coordinated action amongst EU leaders, and global central banks.

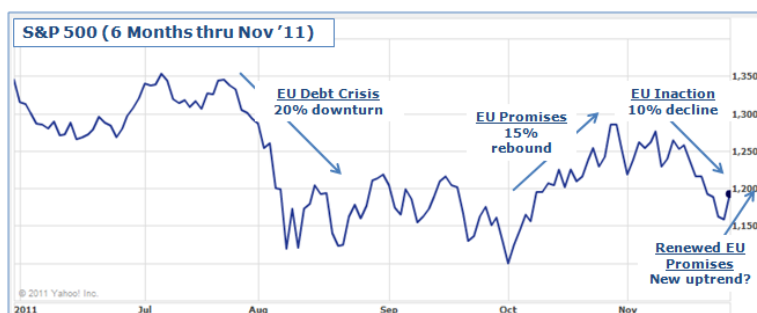


Chart I – S&P 500 Throughout Recent Debt Crisis (June – Nov 2011)

As one might expect, volatility has been high for a number of months now, albeit lower than the most recent peak in August. In our view, volatility is being caused by three main factors: (1) a lack of clarity, (2) high-frequency computerized trading, and (3) a thinly traded market:

- Lack of Clarity: While longer term expectations are driven by traditional indicators such as equity valuations, short-term moves are currently being driven by factors out of one's control. For example, it is impossible to know whether EU countries will announce a course of action to work towards resolving their debt issues, or whether they



will play hardball and be uncooperative. Markets have moved 2-3% daily, both up and down, on random announcements that are impossible to predict in advance.

- High-Frequency Computerized Trading: Estimates place the number of algorithmic computerized trades at 60-70% of daily volume. These computers “surf” the trend by identifying a directional move and rapidly taking positions in the same direction. As a result, movements in the market end up being exaggerated in the short term.
- Low Volume / Thin Markets: Fear and volatility cause investors to move cash to the sidelines. Consequently, trade volumes and diversified trading strategies are reduced. This in turn causes larger market moves as the remaining players tend to be trend surfers (see previous point).

When all these factors act in concert, the net result is higher volatility. Vertigo has set in, and investors are dizzy trying to figure out where the market will go next.

The good news is that equities can become incredibly undervalued in periods of high volatility, and this price dislocation tends to last no longer than 6-12 months (we are 4 months into the current surge). While it is unknown exactly how long such a period will last, or if markets will go lower in the near-term, high volatility and depressed pricing offers investors an attractive entry point for outsized long-term returns. Consequently, we are nearly fully invested for our most aggressive clients, and at or slightly above risk benchmarks for our more conservative clients.

As has been the case in the last couple quarters, it can be trying on the nerves to deal with high volatility in the short-term, but we believe there will be outsized long-term rewards for those who are fully invested or who are adding to their investments. If you are on an automatic savings plan, fantastic! If you have extra cash on the sidelines, now is the time to put those long-term funds to work.

As always, we encourage you to pursue life’s dreams as we help achieve your financial goals through active management, growth, and protection of your assets.

Warm Regards,

Raphael A. Martorello

QUESTIONS

We are available to discuss any questions you have regarding progress towards your financial & investment objectives.

INTRODUCTIONS

We offer a complimentary 2nd opinion service to family members, friends and colleagues of our clients. Please reach out to us if you know of someone who may need the help.

We are accepting new clients through our sister company LotusGroup: www.LGAdvisors.com

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