Market Review and Outlook—December 5, 2011

Don't Look Now, But Things Are Getting Better! US companies are financially solid, profitable, and are hiring. Consumers have rebuilt their savings, helped by refinancing their mortgages at incredibly low rates, and are spending a less-anemic amount this holiday season. The gridlock in Congress has a silver lining—a divided Congress is unable to enact any sweeping, surprising legislation. 'No surprise' is good for stock markets.

Overseas storm clouds continue. The "first step to recovery," proposed by Alcoholics Anonymous, is admitting that you have a problem. The European Union is on the verge of this admission—after eighteen painful months of denial. While this is only the first step—it must come first, and we are witnessing it. There are still many possible paths ahead of Europe; however, they each point forward.

The developing countries, which had been growing quite well, are slowing down—up to a point, this is a good development. Unlike our central bank, developing countries' central banks still have plenty of ammunition left to exert some control over their economies. Long-term moderate growth is far better for everyone than a few years of red-hot growth, which inevitably is followed by a crash.

Investment Landscape—Bond investors have a double-edged sword. Bonds mature, and this places both a cap and a floor on their potential returns. Until maturity, bond investors receive interest, which when coupled with the price change between purchase and maturity provides the **total return**. Due to historically high demand, bonds pay miserably low levels of interest (2% for both ten-year Treasuries and ten-year municipal bonds, less than the S&P 500's dividend yield). Also due to this high demand, current prices for bonds are at large premiums. The technical term for this is 'double whammy,' as low current interest rates are coupled with flat, if not falling future prices for bonds.

Stocks on the other hand don't mature. This means that there is no ticking time bomb for stocks; patient investors are not limited in companies' rising fortunes, and the accompanying rising stock prices. Until these fortunes turn upward, stock investors are pocketing fairly secure dividends, often yielding more than bonds.

So Now What?—With the Firewall up (since late September), we recommend that investors hold onto their stocks, with added emphasis to US (especially large companies) and foreign (ex-Europe). Emerging markets have been pummeled; however, the long-term economics are very positive for emerging markets. We are also 'firewalling' clients' bonds, maintaining—but not boosting—clients' opportunity bonds (where we favor high yield), and for client's quality bonds, we continue to favor intermediate-term maturities. Balance is rewarded.

Category	3 Months	Past Year	3-Year Avg	5 Year Avg	10-Yr Avg
Fidelity Cash Reserves	+0.00%	+0.02%	+0.28%	+1.79%	+1.99%
Intermediate Term Bond	-0.08%	+3.80%	+10.03%	+5.28%	+5.03%
Intermediate Muni Bond	+0.83%	+5.46%	+7.18%	+4.10%	+4.18%
Large-Cap Blend Stock	+1.78%	+4.74%	+13.88%	-0.81%	+2.71%
Mid-Cap Blend	+1.15%	+3.06%	+19.08%	+0.56%	+6.11%
Small-Cap Blend	+1.85%	+3.03%	+18.73%	+0.20%	+6.52%
Foreign Large Blend Stock	-5.55%	-5.25%	+11.12%	-3.64%	+4.38%
Real Estate	-1.67%	+7.58%	+25.89%	-3.36%	+9.01%
Natural Resources	-3.40%	-1.25%	+17.58%	+2.40%	+13.84%
Technology	+1.53%	-0.08%	+24.40%	+3.06%	+2.74%
Moderate Allocation	+0.33%	+3.61%	+12.53%	+1.41%	+3.96%

The data in this table comes from Morningstar, and is as of November 30, 2011