

February 20, 2012

*“Good investors gather information, put that information into current and historical context, then make sound decisions.”*

**One of the risks of not getting to a party early is that it may heat up quick.** This is not usually the case, so generally it is not a strong priority to be one of the first through the door. On occasion, however, the party favors will come out quick. That is how 2012 is kicking off and so far we are partying like the Prince song, ‘1999.’ Hopefully, the rally will develop the legs to carry us through the year.

**The numbers thus far are pretty impressive.** Emerging markets are leading the charge, with the MSCI Emerging Markets Index up +16.05% for the year as of last Friday’s close. The technology sector is not far behind, up +14.85% YTD, with the S&P Latin America 40 Index close behind, up +13.99% YTD. Those returns annualize at over 100%, so we know how overheated these sectors currently are. Domestic indexes are also bursting through the door, with the Russell 2000 Small Cap Index up 11.97%, the Russell MidCap Index up +11.05%, and the S&P 500 Index up +8.56% YTD. These returns annualize at 60-80%. Only seven weeks into the year and with no market pullbacks thus far, we expect some drama in the form of a nice correction at some juncture.

**This strong push was more than adequate to provide positive confirmations for the January Barometers.** The First Five Days January Barometer saw the S&P 500 up +1.8%, and there was no slowing down through the end of the month. For the month of January, the S&P 500 was up +4.48%, its best return for January since 1997. Since 1950, when January is a gainer, the full year has been a gainer 88% of the time. These are impressive odds looking into the remainder of 2012, and have bolstered investors’ confidence in the early on. It also makes a pretty good argument for buying equities on dips, as well as looking for sectors which have not participated as fully in the current rally.

**Bond markets have also been enjoying a good start to the year, with the exception of longer term U.S. Treasury bonds.** On the positive side, the Barclays Capital Emerging Markets Bond Index is up +7.37% and the iBoxx \$ Liquid High Yield Index is up +3.83% YTD. The S&P National Municipal Bond Index is up +2.54%, the Barclays Capital TIPS Index is up +1.45%, and the Barclays Capital U.S. Aggregate Bond Index is up +0.48%. The only bond indexes in negative territory are U.S. government bond indexes after their very strong 2011. The Barclays Capital U.S. 20+ Year Treasury Bond Index is down -3.96% and the 10-20 Year Treasury Bond Index is down -1.48% YTD.

**While it is a target-rich environment on the buy-side, the early push has moved several equity sectors into quite expensive territory.** These include domestic small and mid cap equities, in addition to emerging markets. These sectors would be far more attractive at lower prices. It is still quite early in the year and we will continue to monitor the opportunities as they develop. There are other sectors which have been able to defeat downtrends with all of the positive energy seen thus far, and have not yet become so over-bought. These include developed international equities, basic materials, and energy sectors.

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**Our ‘risk off’ trade in late December positioned SELECTOR® models into decidedly conservative allocations.** As a result, we have not been participating fully in this early ‘rush’ market. On the other hand, we are most certainly well positioned for a market correction and the opportunities to move into equities at better than current prices. With a more positive longer-term forecast for the year, our confidence has increased and we look forward to taking advantage of the generally improved environment for equities.

**SELECTOR® Aggressive Growth and Growth models are currently 40% domestic equities, with the balance in high quality bonds and money markets. SELECTOR® Conservative Growth and Balanced Growth models are now 20% domestic equities with 80% high quality bonds and money markets. SELECTOR® Income & Growth and Income models are 100% invested in high quality bonds and money markets.** We are currently reallocating portfolios and preparing for future reallocations, in response to the positive opening moves of the year.

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