

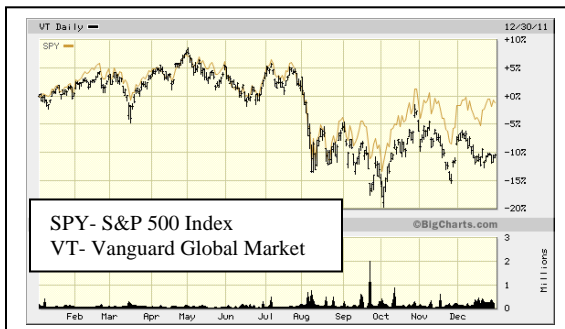
# SWM INVESTMENT REPORT JANUARY 2012



# STEWART WEALTH MANAGEMENT

## 2011 Review

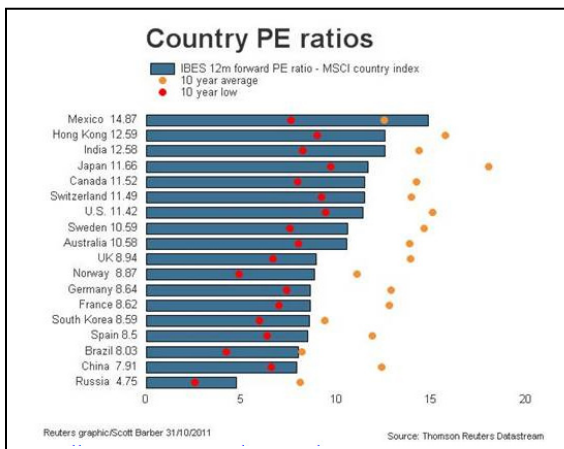
2011 was a very volatile ride for stocks. Treasury bonds were still a safe haven, despite meager yields, a huge deficit, and the historic S&P downgrade of the U.S. credit rating in August. In summary, there was a flight to safety and the Vanguard global stock market index (VT) plunged shortly after Quantitative Easing (QE2) ended on June 30<sup>th</sup>, 2011. In late summer, when the Eurozone debt crisis hit, volatility surged and has continued to do so with speculation of the possibility of a future breakup of the Euro. As you can see below, there was a nice rally in the 4<sup>th</sup> quarter of 2011 with European Central Bank bond purchases and a strong earnings season for stocks.



## 2012 Preview

After a year of muddling through, the US economy still isn't giving any clear signals on where it's headed in 2012. However, it's clear to me at this point, that the stock market does fairly well under the influence of stimulus packages and trends sideways to down when these programs end.

Currently, Europe has stabilized after the European Central Bank began a buying 500 billion dollar spree of Italian and Greek bonds that investors had shunned. There are also rumors surfacing of another US housing stimulus program. Maybe one of Obama's advisors told him he needs to fix housing if he wants a chance of re-election. There is also some evidence that China will continue monetary easing and perhaps put something together similar to its aggressive 2009 fiscal stimulus program. In summary, it is an election year and stimulus programs are the best remedy for an ailing economy, and these programs could boost economic data and stock market returns. Besides low valuations, this is indeed one of the best reasons to say invested through this tough cycle.



In our opinion, it is always important to focus on actual earnings and valuations. When assessing the US stock market earnings, SWM feels equities are slightly undervalued and emerging market equities are fairly cheap. In the attached diagram, you can see that the Price to Earnings ratio of stocks are well below their 10 year averages. (except Mexico & Brazil) The PE ratio of the US reached 32 in 1999 (bubble territory) and that was when everyone wanted a piece of the stock market. Well, it now trades at 11

times earnings. While nobody knows what the immediate future will bring, there is less risk buying cheap equities in an uncertain economic climate, than buying expensive equities when the market is trending up and nobody seems to care about valuations.

## **Top Fund Managers- 2012 Outlook**

### Morningstar- bullish on stocks

- **Economic outlook:** "When everyone has become uniformly cautious, it is just about the time that equity markets can provide an upside surprise. I might add that the U.S. economy is probably better positioned than most of the rest of the world economies, showing accelerating growth even as Europe falls into a recession and as growth in Asian economies slows to a more modest pace."

Source: Morningstar Estimates

### PIMCO-bullish on bonds, cautious on stocks

- **Economic outlook:** "The year ahead will likely be very challenging for the global economy. Growth faces several hurdles that we believe collectively will impose a sense of greater uncertainty and increased volatility on financial markets. These hurdles include the need for accelerated balance sheet deleveraging, slowly creeping but surely rising risks of financial and economic de-globalization and the constant drum beat of re-regulation, particularly in developed-country banking systems."
- **Investment outlook:** "Investors should recognize the Euroland's problems are global and secular in nature, reflecting worldwide delivering and growth dynamics that began in 2008. It will be years before Euroland, the United States, Japan, and developed nations can constructively escape from the straitjacket of high debt and low growth. If so, then global growth will remain stunted, interest rates artificially low, and the investor class continually disenchanted with returns that fail to match expectations."  
—Bill Gross, founder, Managing Director, co-CIO

### Goldman Sachs-bullish on emerging market & China stocks

- **Global economic outlook:** "Our outlook for the global economy in 2012 and 2013 is slower growth than the last couple of years— about 3% global GDP growth in 2012 with quite a bit of differentiation between the strongest performers and the weakest performers. The strongest performers should be emerging markets, including China."  
—Jan Hatzius, Chief Strategist

### Blackrock-bullish on dividend paying stocks

- **2012 investment outlook:** "We continue to operate in a post-credit bust world, a chief consequence of which is ongoing deleveraging. As a result, economic growth will be slow in 2012. Slow growth should be partially offset by the forces of accommodative monetary policy in much of the world, designed to provide the liquidity necessary for solvency and debt repayment. This combination of slow growth and debt repayment/deleveraging is likely to be a difficult one, fraught with occasional accidents and subject to low tolerance for policy errors."

—Bob Doll, Chief Equity Strategist for Fundamental Equities

### Fidelity Investments-Expect more volatility

- **Market outlook:** "But make no mistake about it, this has been a macro all-in or all-out environment, and as long as these structural imbalances persist, I

suspect that it will stay that way. That suggests more time compression, high correlations, and large market swings. So, if there is one thing I feel comfortable predicting with confidence for 2012, it is to expect more volatility."

—Jurrien Timmer, Co-Manager of Fidelity Global Strategies Fund

### Roubini Global Economics –Bearish as Usual

- **Economic outlook:** "The outlook for the global economy in 2012 is clear, but it isn't pretty: recession in Europe, anemic growth in the United States, and a sharp slowdown in China and most emerging-market economies. "Restoring robust growth is difficult enough without the ever-present specter of deleveraging and a severe shortage of policy ammunition. But that is the challenge that a fragile and unbalanced global economy faces in 2012. To paraphrase Bette Davis in *All About Eve*, "Fasten your seatbelts, it's going to be a bumpy ride."

—Nouriel Roubini, Chairman

### T. Rowe Price- Global Recession

- **Economic commentary:** "As of this writing, our base-case scenario envisions the economy expanding by 2% in 2012. Nevertheless, we acknowledge several downside risks to our outlook, including a worsening of the eurozone crisis, deepening fiscal austerity in the U.S. (whether intended or not), and a hard landing for the Chinese economy. On the positive side, however, stronger export performance and lower commodity prices may lead the economy to exceed our expectations in the coming year."

A. Levinson, T. Rowe Price

### Richard Bernstein Advisors-US outperforms in times of uncertainty

- **2012 investment outlook:** "If fundamentals rule, then we think 2012 will be another year of U.S. asset outperformance. Investors still consistently flock to the highest-quality asset in the world, U.S. Treasuries, when market volatility increases. "Some of our favorite investment themes include overweight of the U.S. equity market, and underweight of emerging markets; overweight of smaller U.S. stocks, with an eye for smaller, domestically oriented financials; underweight commodities and gold for U.S. dollar investors; positions in Treasuries to maintain portfolio diversification; increasingly avoid alternative assets."

—Richard Bernstein, CEO



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