



2012 Themes and Outlook

by Jude Bedell & Mike Frazier

A strong finish to the turbulence of 2011 demonstrates that both U.S. Markets and the American consumer are strikingly resilient. With all the negativity circulating around the world, it's remarkable that the Dow Jones Average ended in the green whilst most foreign markets declined over 10%. The greatest irony of 2011 was the downgrade of U.S. credit by Standard & Poor's. This action drove hoards of global cash into American markets and the U.S. dollar. Seeking safety, the world came to American shores for refuge once more recognizing our financial supremacy. In 2012, American stocks and bonds continue to be the ones to own.

Bull Markets historically last about four-and-a-half years. This current run began in March of 2009, so the survey says we have another year-and-a-half of wind at our backs. It's naïve to think we can proceed the old fashioned way of buying low and selling high. We have to act quicker and be more nimble. Markets move faster than ever and so do we. Ultimately, we believe that investors need to embrace longer-term themes to reduce the short-term gyrations. But for the time-being, we plan to continue to buy like investors ... but sell like traders.

WHAT WE KNOW

Europe's problems will not be solved quickly nor easily. Europe will remain a thorn in the side of the global economy in 2012 and beyond, with resolution far from clear and more pain likely.

There will be a Presidential election in the U.S. in 2012. Election years are historically positive for investors. It is way too early to tell who will represent the Republicans, but it is clear that both parties are gearing up for a street fight. The election will no doubt have an impact on the Markets. The problem is that Washington has been in election mode since last summer, and the prospects of getting meaningful legislation before 2013 is slim to none. This gridlock frustrates investors and voters alike.

WHAT WE SEE

Contrary to popular belief, the U.S. economy actually continues to grow. We are not in a recession. We repeat, we are not in a recession. Job creation is at hand. The

unemployment rate has come down, currently sitting at the lowest level in two-and-a-half years. It's still high by historic standards, but it's moving in the right direction. Recent polls suggest companies are planning to hire more in the new year. Spending creates jobs and new jobs create more spending. And so the economy grows.

2012 INCOME THEME: MANUFACTURING CASH

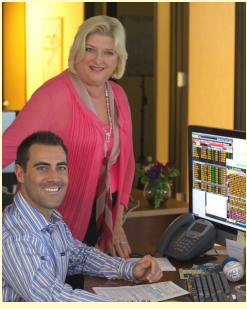
The 2012 Income component of your portfolio will "manufacture" cash in three ways: collecting dividends (think stocks!), depositing interest payments (think bonds!) and accumulating cash premiums up front (think options!).

2012 GROWTH THEMES: TECH, ENERGY AND THE CONSUMER

Innovation has not been hampered by the problems in Europe nor the bickering in Washington. Demand for Smartphones and other web-enabled devices is only getting stronger, and they're not just for "techie" anymore.

We are in the midst of an energy renaissance in the U.S., with vast reserves of oil and natural gas secured. The result could be lower energy costs, a reduction of CO₂ emissions, more stable supplies, removing dependence on foreign energy, and a source of new and higher-paying jobs. Technology has made this renaissance possible.

The American consumer is back with a vengeance. Retail sales jumped a whopping 4.7% this holiday season. We continue to be impressed by the consumer's toughness and see this trend continuing into 2012.



Income Themes for 2012

by Jude Bedell & Mike Harris

The Income component of your portfolio “manufactures” cash in three ways: Collecting dividends – think stocks! Depositing interest payments – think bonds! Accumulating cash premiums up front – think options!

DIVIDENDS

Collecting dividends is not new, but its importance is growing due to the volatility of world markets. While stocks provide portfolio growth, their dividends and derivatives add cash-flow. In other words, stocks rise in price, but so can their dividends. Dividends are increased over long periods of time by blue-chip companies like Coca-Cola and McDonald’s. This reliable source of cash, when added to the appreciation of the shares, secures your income. 2011 was a fantastic year for high-dividend stocks as they outperformed many high-growth dividend-less companies. We expect 2012 to continue this trend as investors favor cash-producing investments.

INTEREST PAYMENTS

Interest payments from your bonds are paramount to creating cash. This cash flow provides stability

and predictability to your portfolio income. 2011 was a stellar year for bonds. Municipal bonds impressed and Corporate bonds were a close second, returning solid cash-flow combined with capital appreciation. All of this was made possible by historically low interest rates and a flight to safety by income-reliant investors.

With interest rates expected to remain low for a few more years, bonds should continue to be a great source of income. With interest rates staying low, we hesitate to forecast the dynamic capital appreciation we enjoyed in 2011, but we nonetheless expect the cash-flows to continue to remain healthy and predictable in 2012.

CASH PREMIUMS

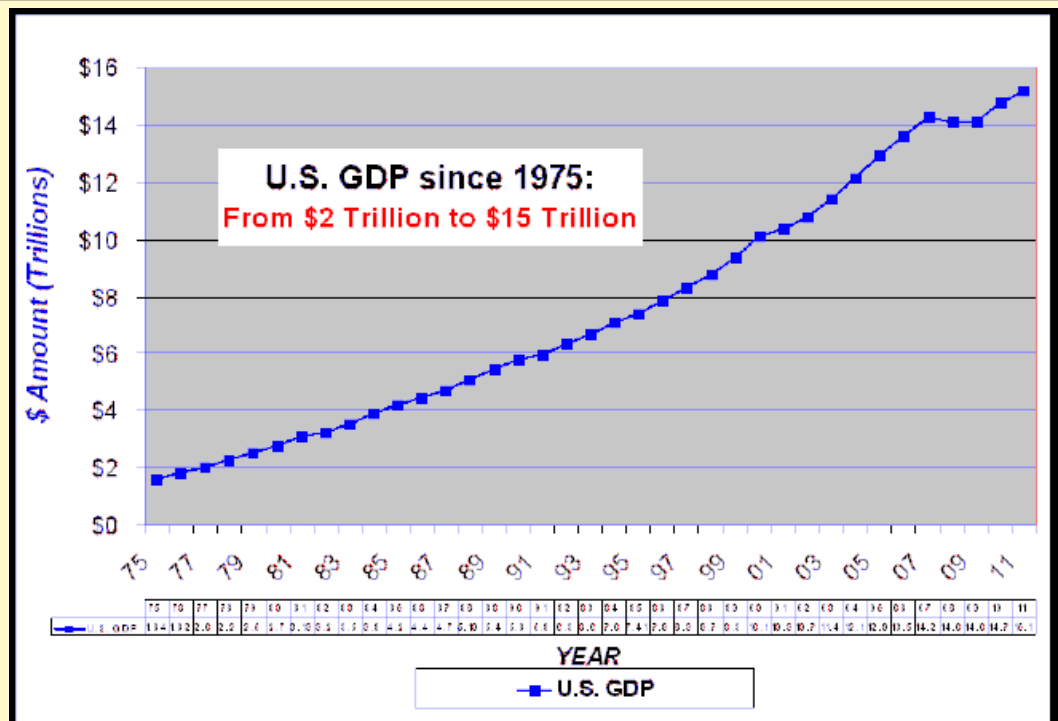
Since more is better when it comes to your income, we produce more cash flow by using options. These options are strategically targeted to “double the dividend” every year while safeguarding your profits year after year. We expect volatility to remain elevated well into 2012, which is a boon for options programs.

Since volatility makes up an important component of how options price (higher volatility in turn makes option prices higher), our covered call options strategy will continue to play a key role in the total income component of your portfolio.

U.S. GDP: OVER \$15 TRILLION

America continues to grow despite worldwide crises. The chart to the right illustrates our country’s GDP growth for the past 36 years.

The GDP represents all goods and services Americans produce in a given year. In 2011, the GDP surpassed \$15 trillion for the first time in history. GDP growth for 2011 should come in at over 3% once all the beans are counted. If the U.S. was a growth stock, one might say that since we founded our company in 1975, America has grown at an average annual rate of 6.5%. It’s important to see this chart as a long-term trend which has every chance of continuing.





Growth Themes for 2012

by Mike Frazier & Meredith Rosen

TECH AND THE MOVE TO MOBILITY

We wrote a year ago that we were in the early stages of a massive migration to mobility. People want to stay connected no matter where they go. They need it to work. They need it to play. They need it to simply exist in these modern times. iPhones, Android phones, iPads and Kindles are all must-have devices. Tech will inspire long-term growth for years to come.

There are over 80 million Smartphones in circulation in the United States. One out of every three Americans over 13 years old own one. This number is expected to double in three years. There are over five billion mobile phones in circulation around the world today. That's an astounding three-quarters of the global population.

The Smartphone adoption rate is staggering, and most of it takes place overseas. We plan to continue to invest in companies that provide smart mobile devices and content providers in the cloud.

ENERGY RENAISSANCE

2012 is setting up for a big year for energy. Recent discoveries in North American shale are proving energy independence is actually within reach again for centuries to come.

Demand for all energy sources is on the rise around the globe and the U.S. has the capability to provide traditional as well as renewable sources in size.

We see an energy renaissance in the U.S., which will increase stable supplies, reduce costs and kick-start new, higher paying jobs. American manufacturing is making a comeback because of these low energy costs. To capitalize on this theme, we will focus investments on traditional U.S. energy companies as well as renewable innovators.

The large U.S. integrated energy companies are well-exposed to the oil and gas reserves in North America, as well as around the world. They are

run by seasoned and disciplined management teams who are long-term thinkers and shareholder-friendly. They pay healthy dividends and raise them every year. They remain excellent investments.

Smaller, "growthier" energy explorers have been under great demand for acquisition as larger companies are finding immense value in the U.S. shale. China, India and France, among others, have made substantial investment in the U.S., and we see this theme accelerating in 2012. Mergers and acquisitions validate this lucrative new but long-term investment theme.

AMERICA IS CONSUMING

The American consumer is back to her spending ways. We are happy to see this, since consumer spending represents approximately two-thirds of the U.S. economy. Retail sales jumped a whopping 4.7% this holiday season, thanks to a surge in online shopping, increased gift card sales and successful in-store promotions.

Consumer confidence is on the rise again – so we see this trend of increased consumer spending to continue. People are feeling better about their financial situation and are becoming comfortable spending again.

Unemployment is easing and is currently at the lowest level in two-and-a-half years.

We anticipate continued improvement on the employment front in 2012. Hiring begets more spending; hence the consumer will be one of the cornerstones of our 2012 investment plan.

Housing has been a major drag for Americans, but this too is looking brighter. U.S. pending home sales in November hit their highest levels in 19 months. This is another positive for the consumer.

A FOCUS ON CONSUMER STAPLES

In 2012 we will focus on consumer staples that remain in high demand as well as stand-out retailers who understand that to be successful in today's retail landscape you must have good merchandise, fair prices and be consumer-friendly both online and in-store.

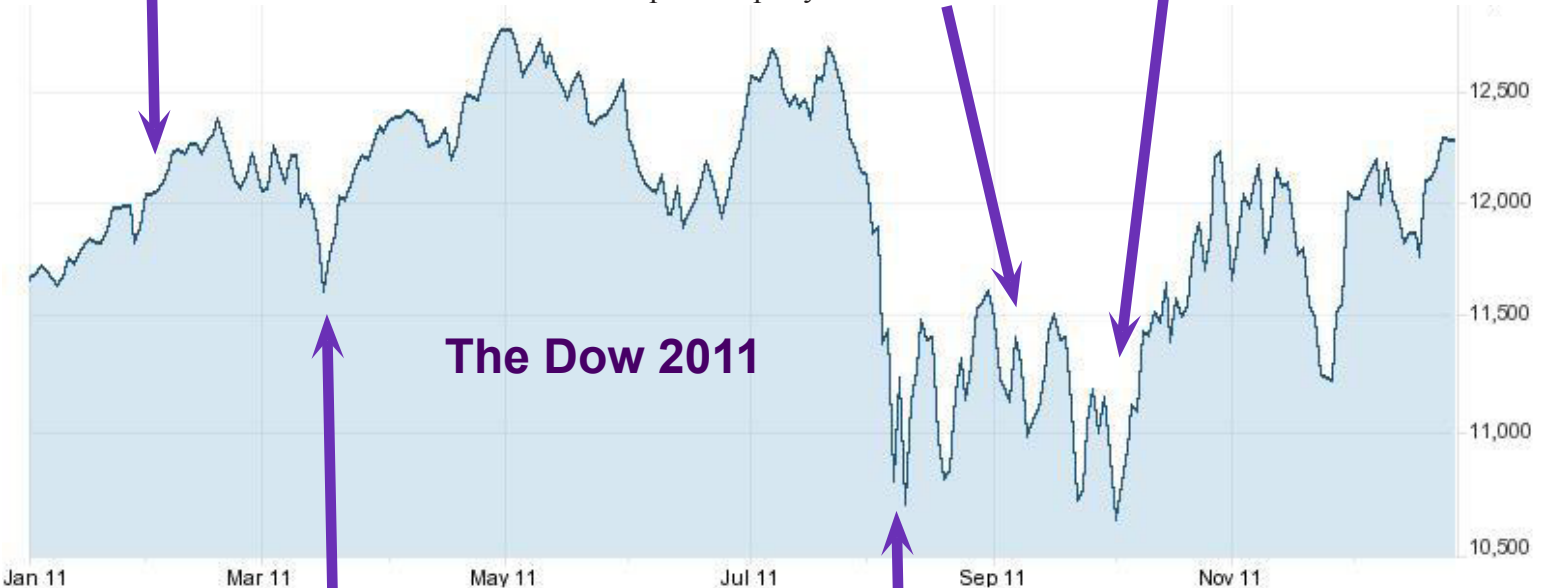
Retailers who continue to evolve with consumers will thrive and those who do not will be left behind.

2011: The Year In Review

February 11: Egyptian President Mubarak resigns, continuing the so-called “Arab Awakening” that began in December 2010. Revolutions took place in Tunisia and Egypt. A civil war in Libya and civil uprisings in Bahrian, Syria and Yemen led to protests in eleven other Arab nations.

October 5: Steve Jobs, cultural visionary, dies. He inspired us to think different.

September 17: Occupy Wall Street began a protest movement that spread rapidly across the U.S.



March 11: Most powerful known earthquake ever hits Japan. Estimated cost of US\$235 billion makes it the most expensive natural disaster in world history.

August 6: Thanks to a political battle that took the country to the brink of default, the U.S. loses the prized AAA credit rating from S&P.

The top business story of 2011: The government-debt crunch rattled Europe’s financial system and weighed on the global economy. Greece, Ireland and Portugal required a bailout as borrowing costs soared and investors worried that Spain and Italy would also need help.



Death & Taxes in 2012

By Nancy Tredwell

Many favorable tax changes persist in 2012:

- **Investors** continue to enjoy a break for qualified dividends and long-term capital gains. These are taxed at a maximum rate of 15% through 2012.
- **Tax brackets** remain the same, ranging from 10% to 35%.
- **Itemized deductions** and personal exemptions are not capped for high-income earners for one more year.
- **Estate tax changes** are threatening, but for 2012 the Federal estate tax exclusion receives an inflation adjustment up to \$5.12 million, from \$5 million in 2011. The annual gift tax exclusion remains at \$13,000.



2012 Time Capsule

By Doc Brown

My pal Marty McFly had a perfect market prediction record last year with five out of five. He didn’t do so well with the cultural predictions, however. Now it’s my turn predicting 2012:

- Gold hits \$2,000
- The U.S. economy sees 3% growth
- The Dow rises above 13,000
- Oil reaches \$120
- The San Francisco 49ers are back!
- Gadgets of the year: iPhone 5 and The Apple TV Set
- And the Oscar goes to ... Midnight in Paris