Market Commentary

1ST QUARTER 2012

Economic Summary

U.S. stocks staged their strongest start to a year in more than a decade in the first quarter of 2012, as investors responded to signs of Europe's debt troubles easing and a strengthening global economy. Even the weather cooperated with the buoyant mood. For the quarter ended March 31, 2012, the S&P 500® Index was up 12.6% (CHART 1). The first quarter saw a continuation of steady but slow growth in the U.S. economy. For the most part, consumer confidence remains resilient despite the rise in gasoline prices (CHART 2). The rising consumer sentiment can be attributed to a falling unemployment rate, which in turn helps to explain a willingness to purchase big-ticket items, such as automobiles.

From a corporate standpoint, many American companies have emerged from the economic crisis leaner, more productive, and more profitable. While reluctant to add new employees, corporate optimism has been evidenced by a strong rebound in capital spending on new plants and equipment. The recovery is favoring larger companies over smaller companies that more often struggle to stay competitive or have a more difficult time obtaining financing. The larger companies also benefit from having a larger global reach, which helped many cushion the impact of the recession.

Very recently, corporate profit growth has slowed, as companies are running out of ways to cut costs further and boost productivity. Profit margins are at very high levels, as evidenced by the fact that over the past three years, earnings grew 95%, while sales rose only 1%.

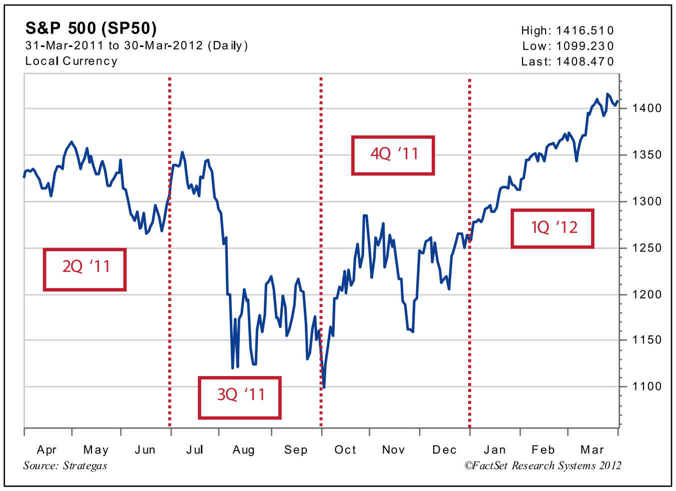


Chart 1

SOURCE: STRATEGAS RESEARCH PARTNERS
"QUARTERLY REVIEW IN CHARTS", APRIL 2, 2012

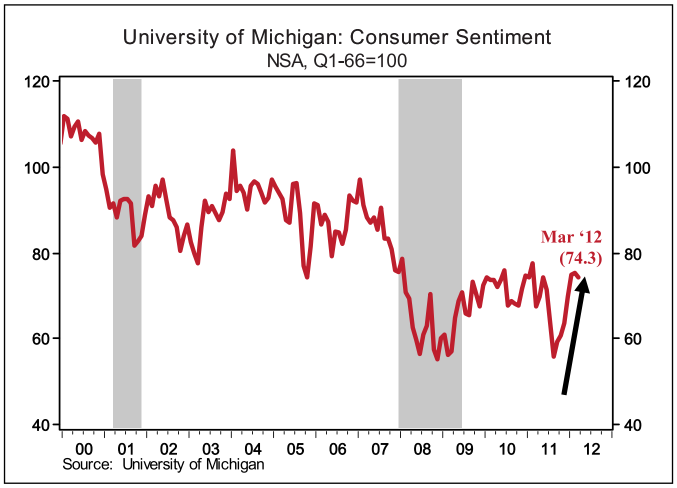


Chart 2

SOURCE: STRATEGAS RESEARCH PARTNERS
"ECONOMICS BALANCE SHEETS", MARCH 19, 2012

Past performance does not guarantee future results.

Economic Summary (CONTINUED)

For the balance of 2012, there are plenty of potential headwinds facing the U.S. economy – mostly from abroad. Europe is likely in a recession. The finances of Portugal, Spain and Italy are still in dire shape due mostly to overspending by their governments (SOUND FAMILIAR?). Emerging markets, notably China, are seeing slower growth, probably 8% real GDP growth this year, versus 10-11% in recent years. The underpinnings of the U.S. economy are probably solid enough to withstand these global developments and our economy will grow at a 2.5% to 3.0% rate for 2012.

Sharing the media spotlight with the economy is, of course, the fall election. As it gets closer, we will discuss the investment implications. Currently, President Obama is conducting a media blitz on high gasoline prices caused by the evil oil corporations. He apparently understands the negative impact high gasoline prices could have on voters' attitudes toward his leadership (CHART 3).

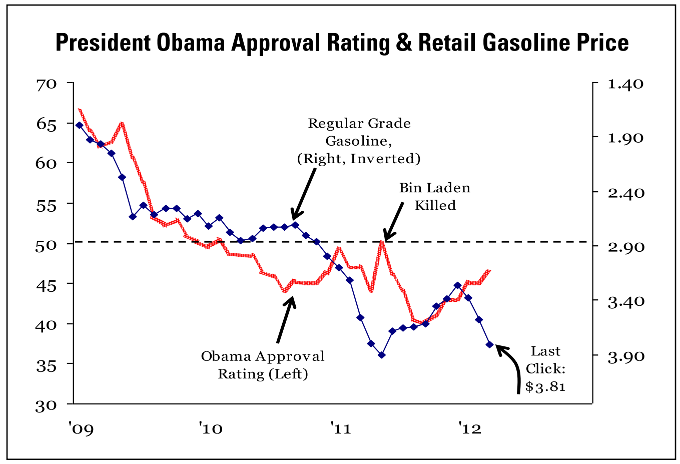
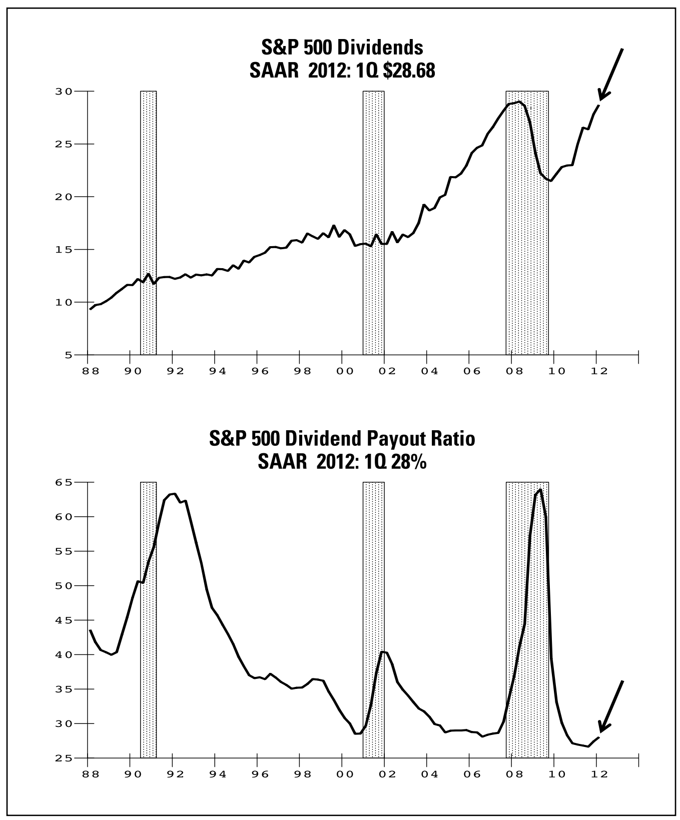


Chart 3

SOURCE: STRATEGAS RESEARCH PARTNERS
"QUARTERLY REVIEW IN CHARTS", APRIL 2, 2012

Equity Market

Our equity strategy continues to seek out large-cap, high-quality stocks. These are often referred to as "wide moat" companies, meaning they have especially strong competitive advantages that help insulate them from the damaging effects of recessions, inflation and competition. In our view, these companies have solid balance sheets, strong cash flows, and histories of increasing dividends. This last point on dividends is very important in this period of near 0% interest rates. CHARTS 4 AND 5 show that S&P dividends rose 14.9% in the first quarter year over year, and though this was close to a record high, the payout ratio in the first quarter was basically at a record low, meaning there is plenty of room for increases.



Charts 4 and 5

SOURCE: ISI – WEEKLY ECONOMIC REPORT
APRIL 2, 2012

Past performance does not guarantee future results. It is not possible to invest in an index.
Seasonally Adjusted at an Annual Rate (SAAR) is a rate adjustment that attempts to remove the seasonal variations in data.

Fixed Income Market

Our bond strategy remains unchanged. We think inflationary pressures will increase, pushing up interest rates. We have been early with this interest-rate forecast, but in our opinion, you can throw out the monetary policy textbooks, because we are in uncharted territory with Fed funds rates at 0% and the Fed's balance sheet with debt up $2 trillion. The conservative approach seems more prudent now than ever. We think inflation is coming, and maybe soon. Stay tuned! To best protect principal, we have invested our portfolio in what we consider to be top-quality, short- and intermediate-maturity issues.

Conclusion

On this topic of Fed policy, we'll close with part of a letter to the Wall Street Journal written by Charles Schwab, which we feel really hits the nail on the head.

Charles Schwab letter to the Wall Street Journal

This is what investors, business people and everyday Americans should hope to hear from Mr. Bernanke after the next Federal Open Market Committee meeting:

'The Federal Reserve used its emergency powers effectively and appropriately when the financial crisis began, but it is very clear that the economy is on the mend and that the benefit of inserting massive liquidity into the economy has passed. We will let interest rates move where natural markets take them. Our experiment with market manipulation will stop beginning today. Effective immediately, we will begin to move Fed rate policy toward its natural longer-term equilibrium. With the extremes of the financial crisis of 2008 and 2009 long behind us, free markets are the best means to create stable growth. Our objective is now to let the system work on its own. It is now healthy enough to do just that. We hope today's announcement does two things immediately: first, that it highlights our confidence – supported by the data-that the U.S. economy is out of its emergency state and in the process of mending, and second, that it reflects our belief that the Federal Reserve's role in economic policy is limited.'

There is a saying in finance: 'Don't fight the Fed.' It's now time for the Fed to step out of the fight. It did its job. Let's allow the free-market system to do its job. Doing so will restore business confidence and spur much needed new investment."

Past performance does not guarantee future results.

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