

# LORING WARD QUARTERLY MARKET COMMENTARY

As of December 31, 2011

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Loring Ward's *Structured Investing* portfolios are strategically invested with a focus on long-term performance objectives. Portfolio allocations and investments are not adjusted in response to market news or economic events; however, we evaluate and report on market and economic conditions to provide our investors with perspective and to put portfolio performance in proper context.

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## U.S. Economic Review

The fourth quarter of 2011 continued to see massive headline risk. There was a shift, however, from concerns over domestic deficits and political issues to European ones. The European Central Bank spent the quarter fighting fires, moving from crisis to crisis as fears shifted from one country to another.

After a dismal third quarter there were few signs of optimism in the market as of October 1st. Many analysts saw continued losses going into the end of the year. Yet market sentiment was quick to change, as investors decided stocks were under-valued and we saw the third best October return since 1926. Volatility remained high, but the 10.9% return for the month brought market indexes back into the positive for the year.

On Halloween we found out that MF Global had done a less-than-stellar job at managing their exposure to European debt and subsequently filed for bankruptcy. About a month later we heard of another large bankruptcy when American Airlines filed chapter 11 on November 29th.

The markets swooned in mid November, but signs of a zealous consumer emerged following Thanksgiving and brought the markets back. Holiday sales at retail stores were up 4.5% over the previous year as stores went to great lengths to make sure they were open as often as possible. Online sales increased 16% this year for the week leading up to Christmas.

Economic data started to improve noticeably in the fourth quarter, as we received final Q3 real GDP growth of 1.8%, which while not a fast rate itself, helped put to rest the double dip recession fears from the summer. Unemployment also showed positive signs with the November number coming down to 8.7%, and December falling to 8.5%, a number we haven't seen since early 2009. The four week moving average unemployment claims set a 44 month low in December.

With energy costs falling for most of the quarter, inflation numbers were subdued, most recently the November reading showed a 0.0% change month over month. On an annual rate inflation decelerated from 3.6% to 3.4%, with core inflation down to 2.1%.

## Financial Markets Review

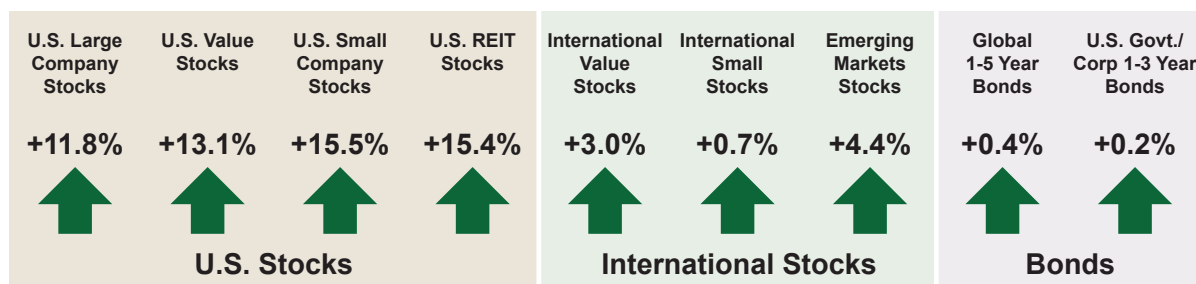
The fourth quarter was historically good for domestic equities, where we saw across the board gains of double digits. International markets also saw gains, but at a much more muted level. Bond yields were relatively flat for the quarter.

## Fixed Income

After a drastic fall on the 10 Year Treasury yield in Q3, this quarter saw some ups and downs but ended the year down just 3 basis points at 1.89%.

**U.S. and International Market Indexes**

October 1, 2011 through December 31, 2011



Source: Morningstar Jan 2012. Market segment (Index representation) as follows: U.S. Large Company Stocks (S&P 500 Index); U.S. Small Company Stocks (Russell 2000 Index), U.S. Value Stocks (Russell 1000 Value Index). U.S. Real Estate Market (Dow Jones U.S. Select REIT Index), International Developed (MSCI EAFE Index (net div.)), Emerging Markets (MSCI Emerging Markets Index (gross div.)), Global Bonds (Citi WGBI 1-5 Yr Hdg U.S.D), U.S. Bonds (BofA ML Corp&Govt 1-3 Yr TR). Source: Morningstar Direct. Indexes are unmanaged baskets of securities that are not available for direct investment by investors. Index performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results. All investments involve risk, including loss of principal. Foreign securities involve additional risks, including foreign currency changes, political risks, foreign taxes, and different methods of accounting and financial reporting.

**Domestic Equity**

Investors with the patience to stay invested through a very rough third quarter were quickly rewarded with large gains in October. For the quarter there were positive premiums for the equity, small cap and value risk factors, and REITs also performed well.

- Broad U.S. equity market, as measured by the Russell 3000 Index, gained 12.1%.
- U.S. large value equities, as measured by the Russell 1000 Value Index, rose 15.5%.
- U.S. small cap equities rocketed 15.5% for the quarter, as measured by the Russell 2000 Index.
- U.S. REITs, as measured by the Dow Jones U.S. Select REIT Index gained 15.4% for the quarter.

For the year, returns were relatively flat domestically with the broad stock market returning 1.0%. The value premium was nearly flat in 2011, with large cap value rising 0.4%. The small cap premium was not rewarded in 2011, with small cap falling 4.2%.

**International Equity**

International equities continued their trend for the year and underperformed their domestic equivalents significantly, as heightened concerns within the Euro and slowing growth rates across many developed and emerging economies put downward pressure on international equities.

Sovereign debt worries have continued in Greece, with investors questioning the future of Greek involvement in the Euro. The path out of crisis remains cloudy, as reduced government spending is being offset by a sharply contracting economy, making it increasingly difficult for Greece to reduce its debt to GDP ratio without resorting to some sort of default. The contagion fear that had plagued Euro headlines for over a year came to fruition as funding rates on Spanish and Italian government debt rose significantly over the quarter.

- International value equities, as measured by the MSCI World Ex. U.S. Value Index (net), rose 3.0% in U.S. dollar terms.
- International small equities, as measured by the MSCI World Ex. U.S. Small Cap Index (net), inched up 0.7% in U.S. dollar terms.
- Emerging Markets, as measured by the MSCI Emerging Markets Index (net), gained 4.4% for the quarter.

For the year, returns were down for international equities with International Large Value falling 11.7%. The small cap premium also lost internationally in 2011, losing 15.8%. Emerging Markets declined the most, falling 18.4% for the year.

Source: Morningstar Direct Jan 2012. Market segment (Index representation) as follows: U.S. Large Company Stocks (S&P 500 Index); U.S. Small Company Stocks (Russell 2000 Index), U.S. Value Stocks (Russell 1000 Value Index). U.S. Real Estate Market (Dow Jones U.S. Select REIT Index), International Developed (MSCI EAFE Index (net div.)), Emerging Markets (MSCI Emerging Markets Index (gross div.)), Global Bonds (Citi WGBI 1-5 Yr Hdg USD), U.S. Bonds (BofA ML Corp&Govt 1-3 Yr TR). Source: Morningstar Direct. Indexes are unmanaged baskets of securities that are not available for direct investment by investors. Index performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results. All investments involve risk, including loss of principal. Foreign securities involve additional risks, including foreign currency changes, political risks, foreign taxes, and different methods of accounting and financial reporting.