

4th Quarter 2011 Market Commentary and Outlook

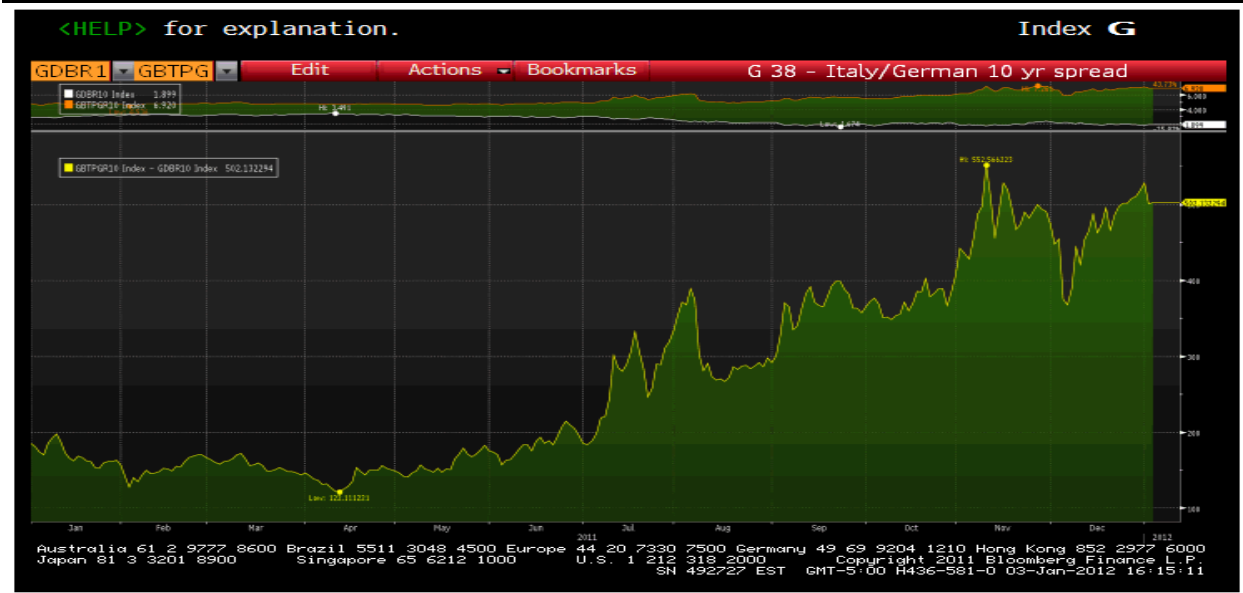
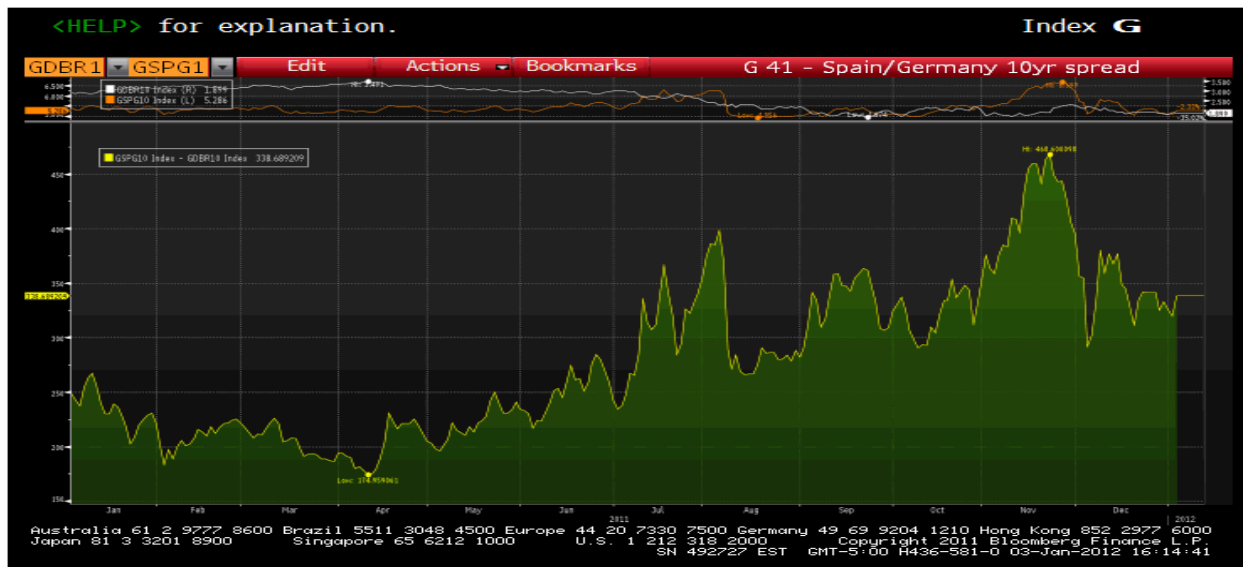
During the fourth quarter the S&P 500 rebounded 12% (see December Bloomberg chart below), a dramatic recovery from the third quarter double digit decline. This bounce helped the S&P 500 finish the year with a positive return of 2.1% (dividends included). The price of the S&P 500 was flat for the year, ironic for a year that ranked in the top 20% for volatility, dating back to 1928 (according to the Chart Store Inc). Essentially the entire return for the S&P 500 came from its 2.1% dividend yield. Volatility, high asset correlation and a continued short term focus best describe the action in global markets during the fourth quarter. Early in the fourth quarter economic fundamentals in the U.S. began to improve, however, that improvement was overshadowed by the ongoing negative headlines in Europe. Fear of a second financial meltdown based on European sovereign debt defaults, accompanied by concerns of an EU break-up and dismantling of the Euro, did not peak until late November. A slow motion liquidity crunch that started in the third quarter resulted in a second coordinated action by the world's central banks. In late November they united to ward off another Lehman Brothers-like meltdown. The coordinated action was announced in statements issued simultaneously by the U.S. Federal Reserve, the European Central Bank (ECB), the Bank of England, the Bank of Japan and the Swiss National Bank. Their statement indicated a united effort by the central banks to ease the strains in financial markets and "thereby mitigate the effects of such strains on the supply of credit to households and businesses and so foster economic activity". Politically, Greek, Italian and Spanish governments fell during the quarter and were quickly replaced with conservative, technocrat leadership inclined to implement austerity/ productivity mandates delivered via the ECB, France and Germany. Much like the third quarter, the fourth quarter had plenty of headline generating activities, resulting in many low to mid single digit percentage interday price swings. By mid December, markets seemed to have accepted that the immediate crisis had been averted as the EU executed a classic "kick the can down the road" refinancing/fiscal recommitment maneuver.



Despite this market reviving maneuvering, BFP continues to maintain a cautious asset allocation as we believe the potential economic fallout from this fall's market uncertainty will have a fundamental impact in the first half of 2012. The following major questions remain: have European leaders acted quickly enough to not only prevent a financial meltdown but also blunt the depth of an anticipated first half 2012 European recession? Will the coming European recession be deep enough to derail the slow global economic recovery, specifically export-oriented emerging economies? While we continue to look for ways to protect client portfolios from ongoing uncertainty and volatility, we are also positioned to opportunistically take advantage of the markets emotional over reactions.

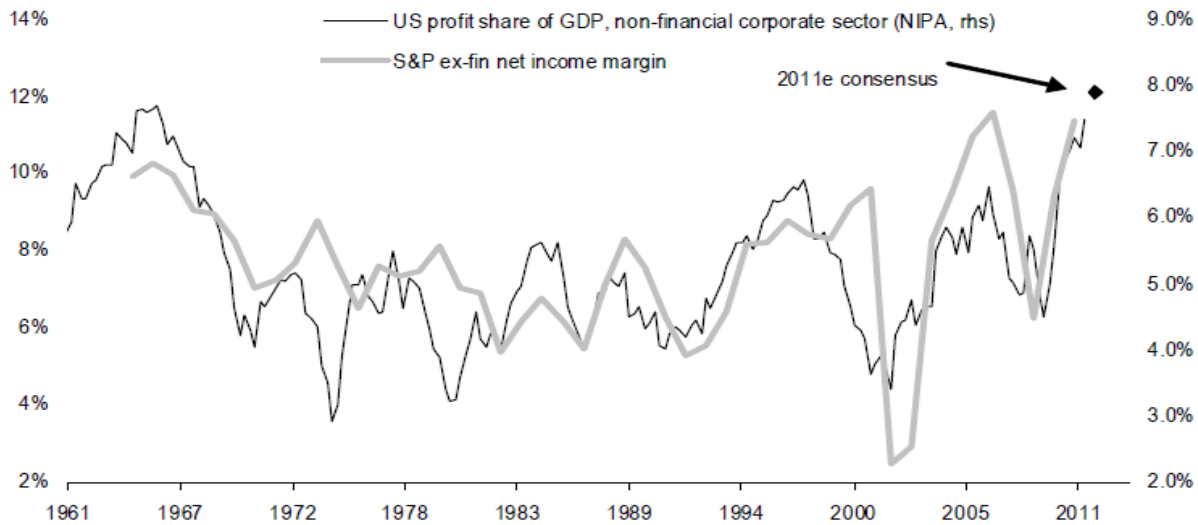
The Euro Rollercoaster Continues

During the fourth quarter, global markets wrestled with assessing the potential fall-out of a European sovereign debt default and an accompanying break-up of the European Union. As seen below, Bloomberg's December, Spain/Germany, Italy/Germany interest rate spread charts (local interest rates above the benchmark German 10 Year bond rate) spiked. Towards the end of the quarter, Spanish and Italian spreads dropped from peak levels as negotiations around changing the EU treaty to encompass better defined fiscal controls were accelerated. Greek debt spreads (not shown) remained at elevated levels reflecting the markets view that Greece has fallen into the non-salvageable category and may eventually be allowed to default.



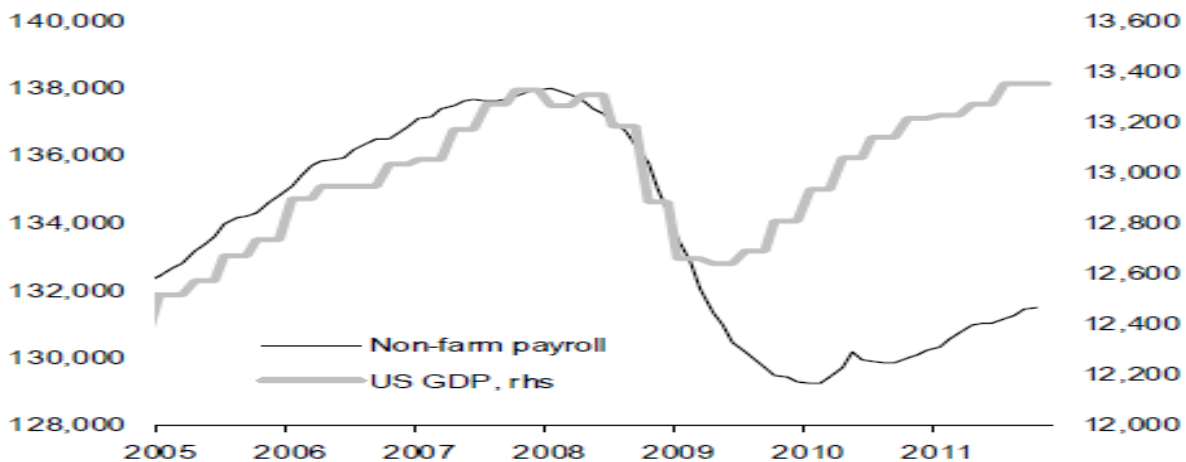
U.S. Corporate Profits, Balance Sheets and Cash - An Oasis or a Mirage?

After the 2008 financial crisis U.S. corporations have done an outstanding job increasing profits through aggressive restructuring and productivity improvements. Unfortunately this meant millions of U.S. workers lost their jobs and benefits in a very short time period. While the cost has been high for many individuals and society in general, there is no questioning that it was the right thing to do to restore corporate balance sheets. As one can see from the Credit Suisse chart below, non-financial corporate profits as a percentage of GDP (left axis) and as a % of sales (right axis) are at record levels.



Source: Thomson Reuters, Credit Suisse research

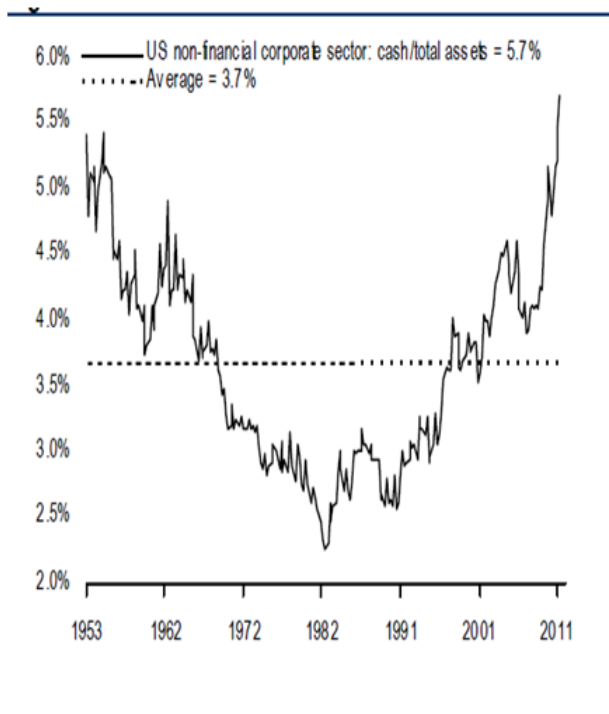
In addition U.S. productivity has dramatically improved as GDP has returned to pre-crash levels (see Credit Suisse chart below) as the economy is producing at these levels (right axis) despite employing 6.5 million fewer workers (left axis).



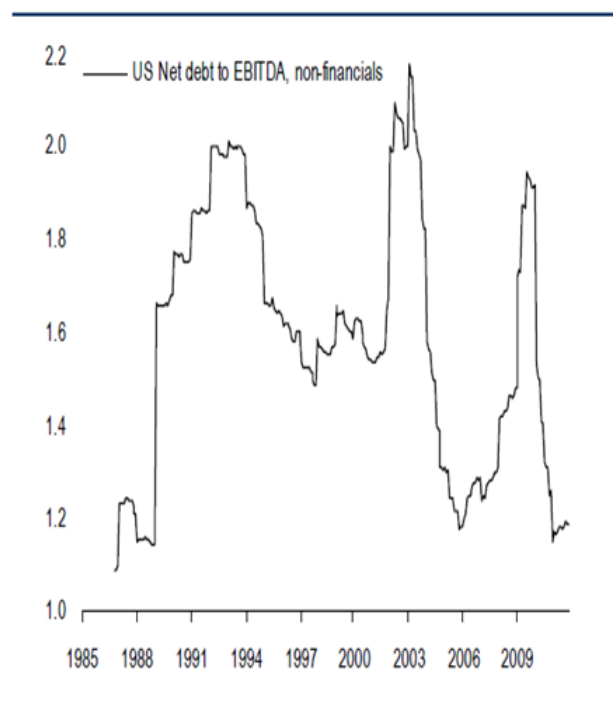
Source: Thomson Reuters, Credit Suisse research

The sustainability of the initial 2009 profit recovery was questioned as it was based upon “cutting your way to prosperity”. Fortunately, during 2010 and into 2011 top line revenue growth came in better than expected. This impressive double digit top line growth combined with tight operating expense controls, resulted in significant operating leverage and profits. Eight quarters of continued earnings improvements and the resulting significant free cash flow (FCF) has created what we at BFP are calling an “embarrassment of riches” or large amounts of cash on corporate balance sheets. The good news is that these riches are finding their way back to the shareholders via share buy backs and dividend increases.

As you can see from the Credit Suisse charts below, cash as a percentage of total assets is at record high levels (5.7%) and non-financial debt to earnings is near record low levels. In a world plagued by excess leverage in which individuals and governments are faced with limited options due to stressed balance sheets, we see corporate balance sheets as a unique oasis. The flexibility that this provides company managements to manage earnings and hence equity price volatility will be a major asset class advantage as we move forward throughout this near stall-speed economy. No other economic segment (consumer or government) has retained this shock absorber feature. This is a key reason we feel so strong about the *relative* positive outlook for U.S. corporate bonds and equities. Historically, the “risk free” asset class has always been government bonds. This time around, the corporate sector may replace the government sector as the lowest risk asset class since governments have taken on record levels of debt.



Source: Thomson Reuters, Credit Suisse research



Source: Thomson Reuters, Credit Suisse research

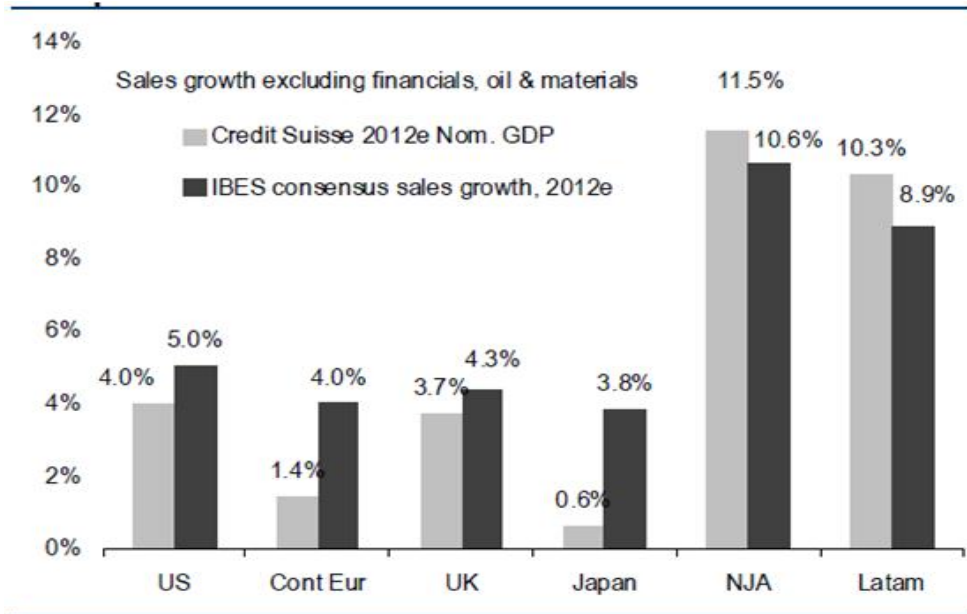
Can The Powerful U.S. Corporate Profit Picture Persist?

While U.S. corporate profits are at historic levels and have dramatically recovered from their 2008 fourth quarter bottom, tough year over year comparisons have and will reduce the growth rate of corporate earnings going forward. However, many key profitability variables remain in corporate hands as we head into 2012. A review of some of those key variables follows. Employment cost, a key driver of corporate profits remains well under control. Historically profit margins have not peaked until labor has pricing power. We are a long way from full employment which, historically, has been the point when labor’s pricing power returns. As noted earlier, the U.S economy has recovered to pre-recession levels utilizing over 6 million fewer workers. Hopefully we are seeing a bottoming in unemployment; however, we do not expect a rapid recovery in this aspect of the economy. This is due to secular shifts and the availability of cheap capital which makes low cost emerging market employment more attractive. Commodity or input costs have been a major headwind (ex: copper prices up over 200%) for corporate gross margins. These costs have moderated recently based upon the fears of a recession in Europe and may become much less of a headwind with further global economic moderation. Significantly lower interest rates and reduced leverage resulting from the corporate cash generation outlined above have dramatically reduced interest expense. In addition, the

powerful corporate FCF likely will continue to be used to fund significant share buy backs and/or acquisitions, which may provide further earnings per share growth going forward.

2012 Revenue and Earnings Expectations

A key factor used in assessing the outlook for U.S. equity markets is next year's earnings expectations. This far into a profit recovery, we need to see continued positive earnings surprises (historically 70% of all companies reporting) to support a positive market psychology. As can be seen from the December Credit Suisse chart below, the Institutional Brokers Estimate System (IBES) sales expectations for 2012 are in line with Credit Suisse's nominal GDP expectations. A 5% U.S. sales growth expectation seems reasonable under a 3-5% nominal GDP growth scenario (2% real and 2-3% inflation). This kind of top line assumption combined



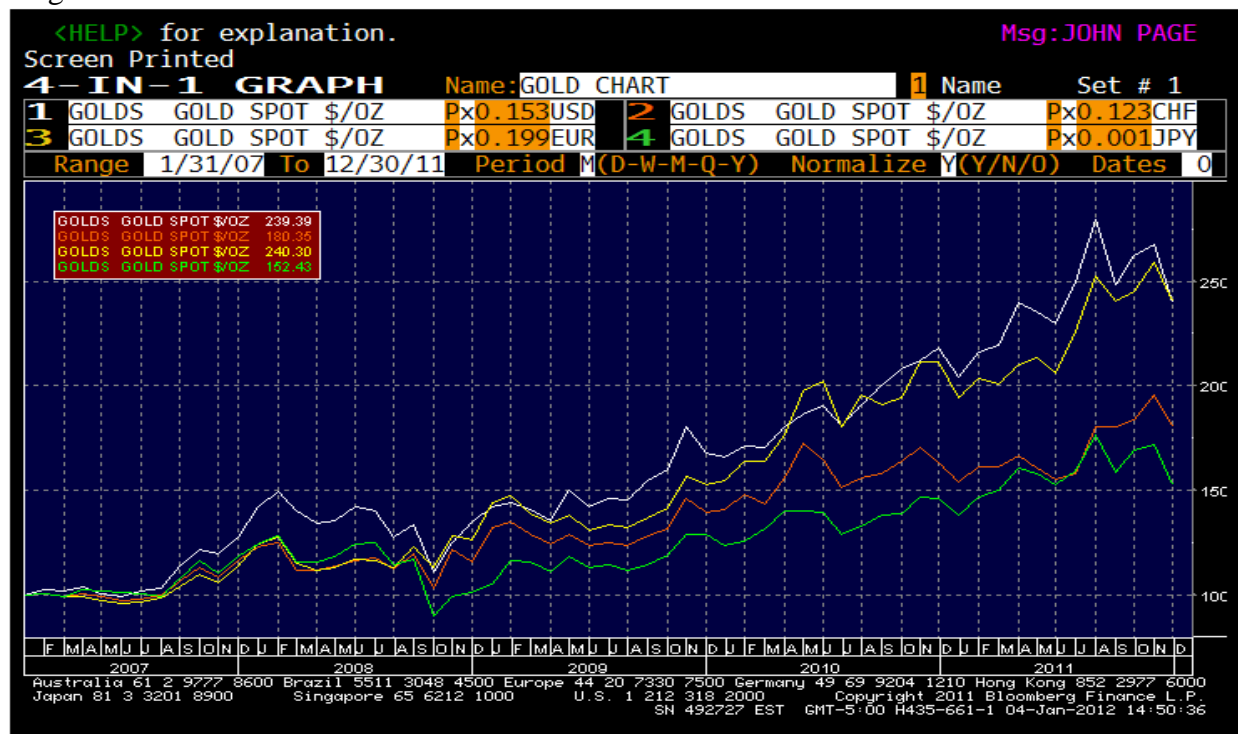
Source: Thomson Reuters, Credit Suisse estimates

with corporate income statements that are set to benefit from continued operating leverage and positive cash flow, makes the 6% earnings growth expectations (see lower right on the Thomson Reuters Table below) seem like a reasonable target for 2012.

S&P 500		12/05/11					
(SPX)		1257.08					
Earnings Per Share - % change							
Latest Qtr (Sep 11)up 14 %							
%Q	Earnings Per Share						
	%'s Based on Yr to Yr Comparisons						
	89						13
	2006	2007	2008	2009	2010	2011	2012
Mar	14 %	10 %	-17 %	-31 %	52 %	35 %	-5 %
Jun	17 %	9 %	-21 %	-13 %	29 %	18 %	0 %
Sep	21 %	-4 %	-17 %	-5 %	32 %	14 %	1 %
Dec	11 %	-23 %	-28 %	47 %	24 %	8 %	7 %
Yr.	16 %	-2 %	-20 %	-5 %	33 %	12 %	6 %
Yr. to Yr.		-2 %	-20 %	-5 %	33 %	12 %	6 %
Estimates	Mean Estimates: First Call					House	

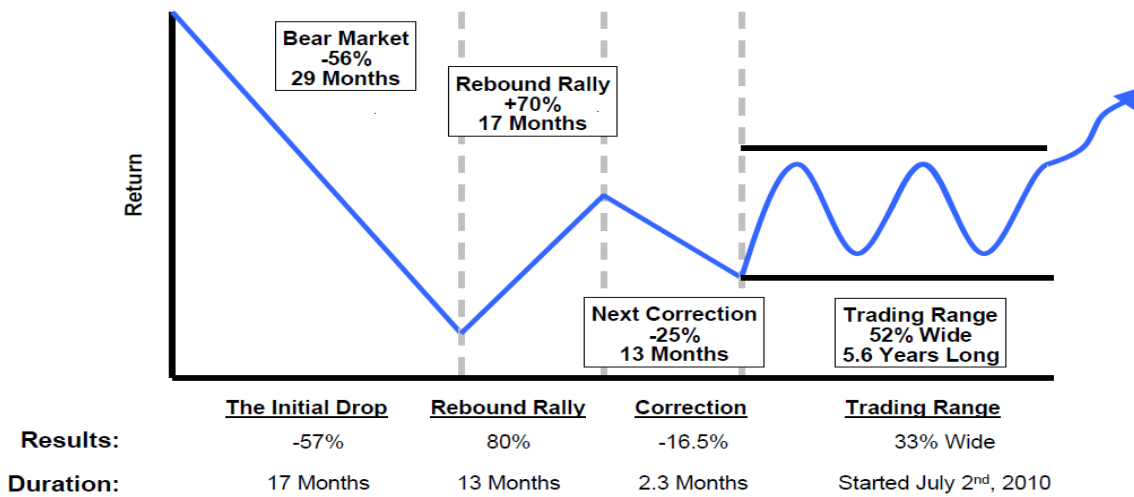
Gold – Multi Currency Wealth Protection Over Time

Gold and commodity volatility will likely continue in 2012 as markets attempt to assess the opposing inflation/deflation scenarios that could occur in this liquidity-charged, muted global economic recovery. As can be seen from the December Bloomberg chart below, the price of gold, denominated in all major currencies (Dollar, Euro, Swiss Franc and Japanese Yen) is up in a range from 150%-240% over the last five years. Essentially what you are looking at is across the board purchasing power protection against competitive devaluation strategies (quantitative easing or printing of money) that central banks have implemented to help inflate their way out of the global debt bubble.



What Kind of Market Should We Expect?

As depicted in the Morgan Stanley chart below, we believe that we are in the “Trading Range” or distribution phase of this composite sketch. The graph below, sourced as “The Aftermath of Secular Bear Markets”, represents the composite of 19 bear markets experienced globally since 1929. While history never repeats exactly, we agree with this model’s expectation for a continuation of the volatile sideways pattern that started midway through 2010 and can swing in a band that is over 30% wide into the near to mid-term.



Source: “The Aftermath of Secular Bear Markets” - Morgan Stanley European Strategy, 8/10/2009
 (Study of 19 secular bear markets globally since 1929 - defined as a 40% fall in equity prices persisting for at least one year.)

SUMMARY

We will continue to emphasize a conservative asset allocation into the first half of 2012 due to potential economic and political fallout in the Euro zone. We will look for opportunities to take advantage of market fears and over reactions that may result as these headlines emerge. We believe that central banks will provide the liquidity necessary to keep the global economy moving forward. Specifically, we will look to buy relatively low volatility, well managed, multi-national equities with favorable cash flows on pullbacks. Our bond holdings continue to emphasize high quality and, in many cases, inflation protected securities. In the face of near term volatility, our long term commitment to real asset exposure continues as we feel that central banks will continue to inflate (print money) and try to grow their way out of the global debt bubble confronting all developed economies. Therefore, we remain very enthusiastic about the prospects for appreciation within our precious metal holdings. While our near term bias is toward asset preservation, we are cautiously optimistic that governments globally are positioning to provide answers (if only temporary) to allow markets to improve in 2012.

As always, we look forward to guiding you through these challenging times and thank you for your trust and confidence. If you have not done so recently, please review your portfolios with your relationship manager. In the meantime, if you have any questions or comments please feel free to contact us at 781-237-7170 or email me at mstack@bfpartners.com.

Michael P. Stack, CFA

Disclosures:

This material is provided for informational purposes only and does not in any sense constitute a solicitation or offer for the purchase or sale of securities nor does it constitute investment advice for any person. Individual securities may or may not be held in any or all client accounts.

The material may contain forward or backward-looking statements regarding intent, beliefs regarding current or past expectations. The views expressed are also subject to change based on market and other conditions.

The information presented in this reports is based on data obtained from third party sources. Although it is believed to be accurate, no representation or warranty is made as to its accuracy or completeness.

Diversification does not ensure a profit or guarantee against loss. An investment cannot be made directly in an index.

Sector investments concentrate in a particular industry and the investments' performance could depend heavily on the performance of that industry and be more volatile than the performance of less concentrated investment options and the market as a whole.

Foreign markets, particularly emerging markets, can be more volatile than U.S. markets due to increased political, regulatory, social or economic uncertainties.

ETFs may trade at a discount to their NAV and are subject to the market fluctuations of their underlying investments. ETFs are subject to management fees and other expenses.

Past performance is no guarantee of future results

Please Contact Michael Stack or your Relationship Manager for more information or to address any questions that you may have.

Definitions:

S&P 500 - An index of 500 stocks chosen for market size, liquidity and industry grouping, among other factors. The S&P 500 is designed to be a leading indicator of U.S. equities and is meant to reflect the risk/return characteristics of the large cap universe.

Read more: <http://www.investopedia.com/terms/s/sp500.asp#ixzz1amicOZgd>