Dear Client: January 4, 2012

2011 Year End Review

On New Year's Eve we raised our glass with excitement and optimism for the arrival of 2012.

The past year has been filled with extreme market volatility and global economic and political uncertainty. These events coupled with the harsh natural disasters experienced around the world makes it easy for us all to say farewell to 2011! An iconic song from one of the classic movies of our time, *The Sound of Music,* comes to mind as we gesticulate to 2011,"So long, farewell, auf wiedersehen, adieu… I leave and heave a sigh and say goodbye -- Goodbye!"

After a dismal Q3, the market rebounded in Q4, and while still volatile, it demonstrated resilience to the stress in Europe and evidence that the US economy is improving. Both the S&P and Dow returns were in excess of 11%, while the international returns were lower but still positive (see below chart).

However, U.S. equity markets had the last laugh of 2011 when they slid on the last day of trading. The Dow remained in positive territory for the year ending up a respectable 5.5%. The S&P 500, conversely, which is a broader market indicator, relinquished its slight gain in the final moments of trading of 2011 and ended the year essentially flat. The flat-line result masked the much talked about volatility. The S&P was up as much as 8.4% in April and down nearly 13% at is nadir in early October. International markets, were not as fortunate, posting losses for the year well into the double digits amid the debt crisis.

The silver lining continued to be commodities and the Bond market. Low Treasury yields were reflective of investors seeking the safe harbor of US Treasuries (despite the August downgrade of the US from AAA to AA+). Yields on the 10 year bond finished the year at 1.9%, and the Barclays Aggregate returned over 4%. Global uncertainty fueled a continued rally for Gold, which hit its peak in August at $1,888, but fell back at year end to $1,565, resulting in a 10% gain on the year.

Index	Index Close	Q4 Total Returns (%)	2011 Total Return (%)
S&P 500	1,257.60	11.15	0.00
DJIA	12,217.56	11.95	5.53
NASDAQ	2,605.15	7.86	-1.80
MSCI EAFE	49.53	3.66	-14.93
MSCI Emerging Markets	37.94	8.09	-20.36
Barclays Bond Aggr.	110.25	0.13	4.26

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Although economic deleveraging and political paralysis across the US and Europe will provide markets with little wiggle room in 2012; the US domestic outlook appears somewhat promising. Economic indicators are trending positive and the majority of economists are forecasting positive equity returns and flat bond yields in 2012. Beginning signs of the return of manufacturing to the US is one area that economists are referencing as evidence of improvement.

The major concern that continues to persist is Europe.

As we have stated in previous correspondence, Europe is not a single entity, politically or economically and any potential solution brings its own set of unique implications. Adding to the complexity of the situation, fiscal and monetary efforts (austerity and deleveraging) could be hampered by a shrinking economy in the euro area, which would crimp tax revenues and fuel unemployment. The economy of the 17-nation area will shrink by about 0.7 percent in 2012 according to Howard Archer, an economist at IHS Global Insight in London.

"The road to overcoming this won't be without setbacks, but at the end of this path Europe will emerge stronger from the crisis than before," German Chancellor Angela Merkel said in a New Year's speech broadcast Dec. 31. Merkel reiterated that her government will do "everything" to bring the euro out of the slump.

"We expect euro-zone recession to occur in late-2011 and the first half of 2012 in the face of the ongoing euro-zone sovereign debt crisis," Howard Archer wrote in a Dec. 30 note. "It is vital that euro-zone policy makers get a real grip on matters quickly."

The cloud in Europe is overshadowing the generally more optimistic view in the emerging markets. The consensus is that Europe is critical to emerging markets and their success hinges on Europe resolving its issues.

Magnifying the uncertainty for the coming year will be presidential elections in the US and France.

We look forward to speaking with you soon. Please don't hesitate to contact us should you have any questions or require any additional information.

Sincerely,

Locust Capital Management, LLC

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