



Dear Friend:

December 10, 2012

Home Stretch

The Holiday Season is here and 2012 is racing to a close after having been bumped and bruised in a variety of perspectives.

The markets in 2012 have been very much influenced by geopolitical events primarily out of Europe. The European Union (EU) has made significant progress with their commitment to the Euro. The EU has empowered the European Central Bank with oversight powers and provided financial support to struggling member nations. The Euro zone, however, will struggle for the foreseeable future and the risk remains whether the vision of the 1992 Maastricht treaty and its architects will ultimately be achieved.

The year to date return of the S&P is up over 12.0%, but that does not tell the complete story. After getting off to a roaring start in 2012, the equities markets have given us a ride that would give indigestion to the most experienced NASCAR professional. Daily and weekly swings brought investors major stress. In Q1, returns were a robust 12%, only to contract 3.2% in Q2. The S&P had been down significantly in Q2 (-10%) but thanks to a late rally in June, what would have been a tragic quarter for equity returns, was somewhat muted. Global events quieted down over the summer and the markets responded with a 5.7% advance in Q3. However, post-election concerns have provided new stress and with it renewed volatility as we traverse through Q4!

The Bond market participants experienced a similar ride in 2012. Treasuries (10yr note yield) started the year at 1.87%. During Q1 rates rose to 2.22%, then due to the global stress and a flight to quality in Q2, Treasuries dropped dramatically to 1.62%. While rates continue to be volatile due to market forces, Treasuries are generally hovering around the 1.6% range.

As autumn arrived and market volatility became the norm, Locust Capital responded with recommendations to our clients to revise investment policies and increase alternative exposure (to address volatility). At the time, the U.S. also became inundated with pre-election debates and “mudslinging” advertisements. The Presidential race was much closer than President Obama had predicted and there were rumblings of a sea change in Congress.

All the election chaos took a back seat when Super Storm Sandy brought some of the worst destruction ever experienced on the East Coast. We are now thankfully past the worst of Super Storm Sandy, and communities are beginning to rebuild. Many of the costs to the insurance industry and the Federal and local government will take months to determine. We learned firsthand how fragile our existence is and we have counted our blessings!

Fortunately, Sandy did not prolong the exhaustive election season. It is thankfully behind us, but unfortunately, not much has changed in Washington!



The focus for December, and likely the first half of 2013, will be the ability of Washington to address the expiration of the Bush era tax cuts and “The Fiscal Cliff!” The status quo of our inept Congress does not promote confidence that the issues will be easily resolved. We were recently reminded that this same body of politicians fumbled the much needed reform of the US Postal Office. Irrespective of their many blunders, we can confidently say that both political parties stand to lose if nothing is accomplished.

The Fiscal cliff has and will continue to dictate the behavior of the global markets between now and year end. Our September Newsletter, “Rising Tax Environment”, which is on our website (www.locustcap.com), provides a summary of potential tax impacts along with possible strategies to consider.

In addition to the situation in Washington, we are concerned with the heightened tension in the Middle East with Israel, Iran and the Syria. While the US people are clearly exhausted from our past military participation, there are scenarios where we will have no other option but to intervene. Our involvement will stress our citizens, our military, our fiscal situation, and the global markets.

As your trusted advisor, we are paying close attention to these issues and are ready to react on your behalf, if warranted.

Happy Holidays,

Locust Capital Management, LLC