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January 2, 2013

2012: The Year in Review and a Look Ahead

Dear Client,

There is a common expression on Wall Street that, in order to notch gains, stocks must first climb a "wall of worry." This phenomenon was on display again in 2012 as stocks—despite numerous real or feared obstacles—delivered double-digit gains (the S&P 500 Index[1] gained 13%). Whether it was tepid economic growth in the U.S., concerns about the euro zone's government debt crisis, or the impact of an economic slowdown in China, there was no shortage of things to worry about in 2012.

Over the past few weeks, the financial media have been fanning the flames of fear over the potential damage the U.S. and global economy would sustain if we were to fall over the so-called "fiscal cliff." If you somehow escaped the round-the-clock media coverage of this issue, the fiscal cliff refers to a combination of automatic government spending cuts and higher tax rates that would be triggered if Congress failed to reach a deal to reduce the federal budget deficit by year-end. These triggers were enacted back in August 2011 during the negotiations to raise the nation's debt ceiling. Unfortunately for our nation's economy, our Congressional leaders have a tendency to procrastinate as long as possible before finally getting down to business.

The primary fear over the fiscal cliff has been that, should Congress fail to reach a deal, the impact of higher taxes, reduced government spending, and uncertainty over future fiscal policies would trigger a recession in 2013. Such a development would likely hurt corporate profits and potentially trigger a stock market sell-off. I'm happy to report that, as of this writing, it appears that Congress will reach a partial agreement that buys time to design a more broad-based plan to deal with our nation's burgeoning budget deficits.

It's also possible that Congress will strike some type of "grand bargain" that removes much of the uncertainty that has plagued the economy in recent years. This could give business leaders the confidence they need to invest more aggressively in their businesses and thereby spur stronger economic growth. Consumer confidence, which has ticked down in recent weeks due to all the fuss about the fiscal cliff, might then rebound and trigger a rise in consumer spending. Of course, if the budget talks bog down amid partisan bickering, then all bets are off.

Depending on whether you are pessimistic or optimistic, you may be wondering whether now is the time to raise cash or load up on stocks. In such an uncertain environment, I believe a cautious, diversified approach is prudent. While diversification does not protect against losses, it helps reduce overall portfolio volatility. This keeps you invested and can help ensure you don't panic and sell your holdings at a market low.

Looking ahead to 2013, there is no doubt we will once again face economic challenges and market volatility. But as 2012 demonstrated, it pays to keep some skin in the game and maintain a balanced approach, no matter how uncertain the future looks.

Thank you for your trust. I wish you and your family a healthy, happy, and prosperous New Year.

Sincerely,

Mike

Mike Ovshak
CFP®

[1] All indices are unmanaged and investors cannot invest directly into an index. Past performance is not indicative of future results. The S&P 500 Index is a broad-based measurement of changes in stock market conditions based on the average performance of 500 widely held common stocks. Diversification does not assure a profit or protect against a loss in declining markets.