

Investment Review & Outlook

December 31, 2011

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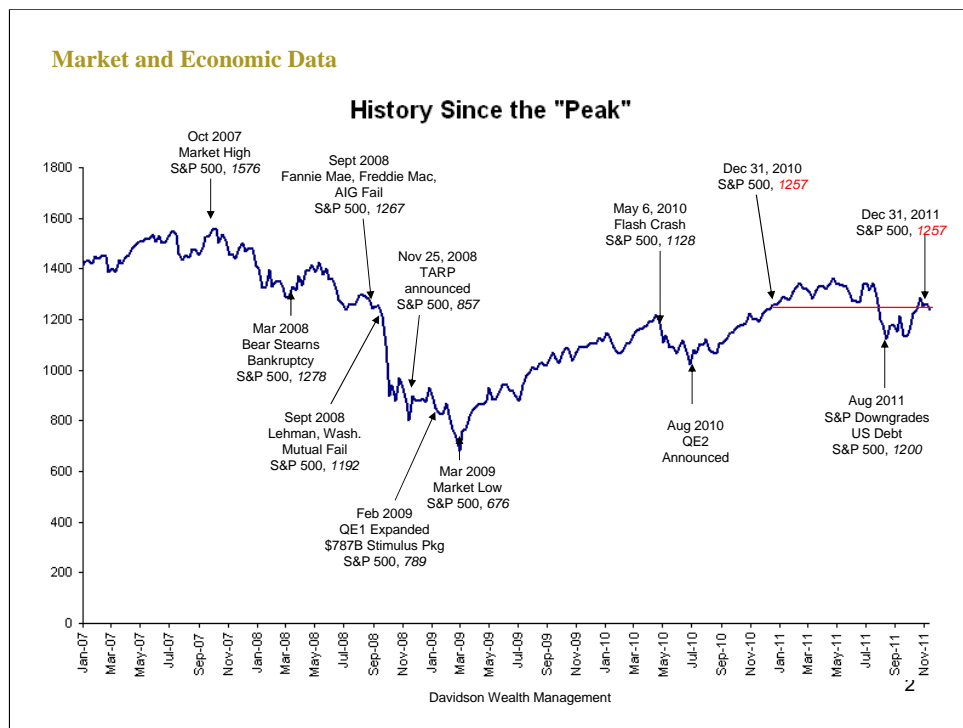
Investment Review and Outlook

We'd like to provide you with a perspective of the equity markets for the past year as well as common and uncommon themes for 2012. The charts in the package will help us make four points.

1. How political events have influenced the financial markets since the peak in October 2007.
2. That there has been a recent split in performance between domestic securities and international markets.
3. Why investors should keep the faith if they own international and emerging market assets.
4. Why investors should stay the course with diversification.

We will then explain secular markets and discuss what might lie ahead.

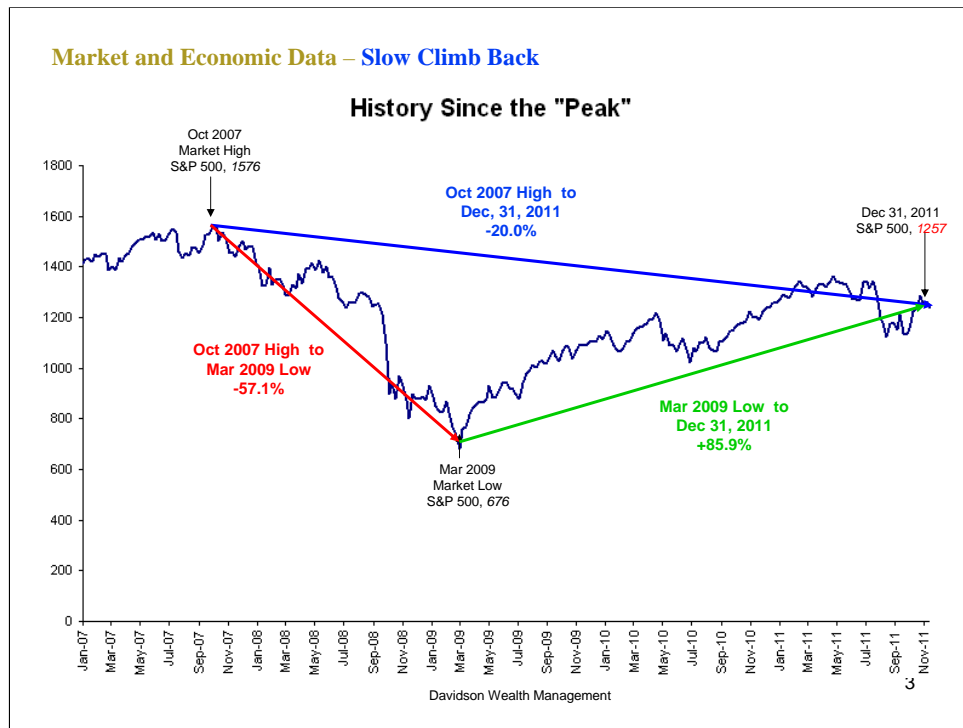
And lastly, looking toward 2012, we will share our research we call "Common Uncommon Themes for 2012".



This slide shows the market, utilizing the S&P 500, since the peak in October 2007. You'll note on the vertical axis, the price of Standard and Poor's 500 starts near 1400. You'll note the horizontal axis carries us from January 2007 to November 2011. That market decline from October 2007 to March 2009 was the worst since the Great Depression where a credit shock occurred, resulting from 25 years of debt buildup. Only in hindsight, we can see widespread over accumulation of debt. Homeowner's aspirations of larger and larger homes, investors seeking higher and higher yields, financial institutions that facilitated and obscured the risk are all to blame.

Note the subsequent recovery that began with an economic stimulus, since referred to as Quantitative Easing, followed by QE 2. Note on the far right hand side, the August 2011 time period that included debt ceiling negotiations, a downgrade of the U.S. debt, acknowledgment by Ben Bernanke of a slowing economy and his announcement that interest rates would stay low until June 2013. This also coincided with the beginnings of the European debt crisis recognition. Whew!

The straight red line on the right side, illustrates that a calendar year is an arbitrary data point. You can choose any one year period and get a different slope! This reminds us that stocks are longer term investments than for just one year.



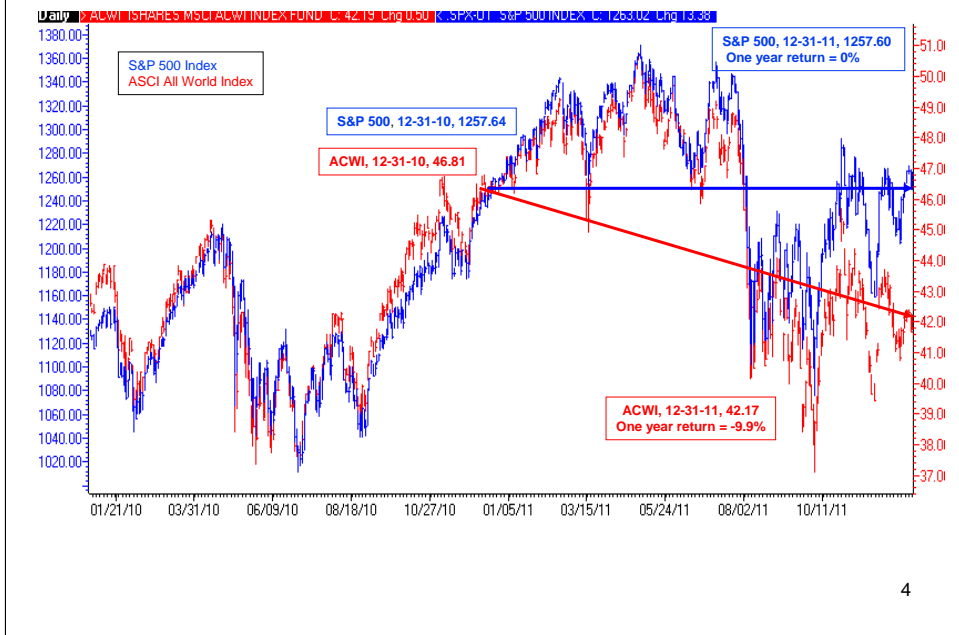
This is the same chart with a different insight. The blue line at the top shows that over three and a half years the market has still not recovered. The red line illustrates a drop of 57.1%

The green line shows a stock market recovery of 85.9% from the bottom, but that it still does not overcome a drop of 57.1%. This illustrates one of the puzzles of mathematics that requires a much larger recovery off the bottom to break even. For example, if you had a \$100 investment in ABC Co. and the stock value dropped 50%, you would have an investment worth \$50. If the stock were to subsequently rise 50%, your investment would be worth \$75. You would need a 100% increase in value from the initial 50% drop to \$50, to get you back to "break even" or to a \$100 value.

Investors should also note you can draw a fairly steep line from the bottom illustrating a strong V-shaped recovery off the bottom, then a breather in the market, and then another steep upward line, about the time of QE2.

Now we're experiencing another breather. We think this chart will set the stage later for a 2012 outlook that offers some encouragement going forward.

Market and Economic Data – Global investing was not rewarded in 2011



Global Investing *Was Not Rewarded* in 2011. This colorful slide illustrates the recent separation of the US and international markets. On the vertical axis, in blue, is the price scale for the Standard & Poor's 500, and the vertical axis on the right represents the MSCI All-World Index. The MSCI All-World Index represents the entire world's stock market, including both US and all other countries' markets.

What is interesting to note is that from the time period starting from the bottom left-hand axis, January 2010, both markets traded in lock-step with one-another until August of 2011. While the US market recovered, the international markets pulled down the All-World Index. Global investors temporarily lost money in 2011.

It is important to note that during the last part of the year, the value of the dollar increased relative to other currencies, which in effect, gave a boost to the US market, allowing it to “breakeven”. You'll note on this chart the blue line that is horizontal, based only on price, offering a one year (price only) return of the Standard & Poor's 500 of zero. You'll notice the declining red line for the All-World Index illustrating a one year return of -9.9%. These do not reflect the actual returns of the respective indexes as they only illustrate price, but are illustrations to tell a bigger story; that investors were not rewarded in the past year for global investing. You might be thinking, “Why not just keep my investment dollars here at home?”

Market and Economic Data

Ebbs and flows of international investing Rotating market leadership

Russell Global xUS Index vs. the Russell 3000® Index
Rolling Twelve Month Excess Return



- Global equity leadership changes frequently
- Reversals can occur quickly and dramatically
- International equity returns have been higher than U.S. returns with higher volatility since 1970
- Diversifying across markets to potentially capitalize on market swings

Excess Rolling Returns

- Useful for understanding the behavior of returns over multiple time periods. For example, 1 year rolling time periods calculated monthly over a decade allows us to view 121 observations as opposed to looking at a single end date.
- Demonstrates patterns or longer term trends in the return data.
- This rolling excess return stream is comparing the twelve month period return of non-US equity relative to U.S. equity. For each rolling twelve month period the comparison ROLLS forward by adding the next month to the one-year window while dropping off the first month. The charts covers rolling periods including January 2000 through September 2011.

Source: Russell Investment Group
Indexes are unmanaged and cannot be invested in directly. Returns represent past performance, are not a guarantee of future performance and are not indicative of any specific investment.

Russell Investments

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The following two charts were provided to us by Russell Investments. This first chart refers to the ebbs and flows of international investing and rotating market leadership. The chart shows rolling 12-month excess returns, explained on the bottom. The time period, as shown in the bottom left-hand corner, runs from April 1, 2000 to February 1, 2011 illustrating that international stocks have had periods of both out-performing and under-performing the US markets.

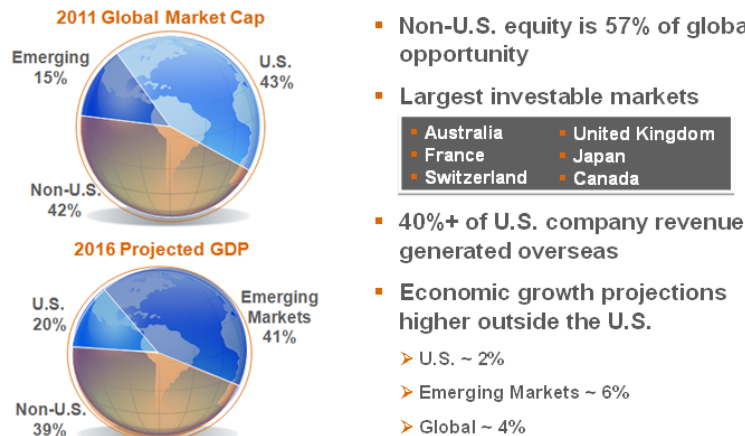
Note the bullet points on the right; *global equity leadership changes frequently, reversals can occur quickly and dramatically, international equity returns have been higher than U.S. returns with higher volatility since 1970, and lastly, diversifying across markets can potentially capitalize on market swings.*

In short, using strategic asset allocation, investors should consider re-balancing annually which means putting additional dollars into the underperforming category of the past year - international markets - in spite of the short-term news that we're reading about Europe.

Other than rebalancing, what rationale is there to invest abroad?

Market and Economic Data

U.S. centric investing is a thing of the past



Sources: Russell Investments Group's Global Equity Index, Aug 2011, The International Monetary Fund's World Economic Outlook, Sep 2011, Standard and Poor's Global Sales Report, July 2011. International securities can involve risks relating to political and economic instability or regulatory considerations and currency fluctuations. Investments in emerging or developing markets involve exposure to economic structures that are generally less diverse and mature, and to political systems which have less stability than those of more developed countries.

Russell Investments

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Rationale can be found in the fundamentals. This page offers the perspective, that in spite of the current news coming out of Europe, Russell Investments suggests that US centric investing is a thing of the past.

In terms of Global Market Cap, the United States currently only makes up 43% of all investable equities in the world, 15% is in the emerging markets. As noted, 40% of US company revenues are generated overseas and that there are higher economic growth projections outside of the United States.

Russell Investments projects that in 5 years, 2016, gross domestic product will be dramatically skewed towards the emerging market nations often recognized as China, Brazil and Latin America, India, Indonesia, and South East Asia.

If your time horizon exceeds 5 years, then as an investor you are forced to consider the argument of a broadly diversified strategy that includes international and emerging market securities. Just because investors were not rewarded for doing so in 2011 does not change the argument, in our opinion.

As wealth managers engaged in asset allocation, you often hear us speaking of a "bucket approach". We often hold cash buckets, invest in buckets of income securities and in growth strategy buckets. This particular discussion speaks to the growth bucket. Growth strategies accept short-term volatility and short-term disappointments.

Market and Economic Data

2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	4Q11	10-yr '02-'11
REITs 19.9%	DJ UBS Cmnty 23.9%	MSCI EME 56.3%	REITs 31.6%	MSCI EME 34.5%	REITs 35.1%	MSCI EME 39.8%	Barclays Agg 5.2%	MSCI EAFE 79.0%	REITs 28.0%	REITs 8.3%	Russell 2000 15.5%	MSCI EME 277.2%
Market Neutral 9.3%	Barclays Agg 10.3%	Russell 2000 47.3%	MSCI EAFE 26.0%	DJ UBS Cmnty 17.6%	MSCI EME 32.6%	MSCI EAFE 11.6%	Market Neutral 1.1%	MSCI EAFE 32.5%	Russell 2000 26.3%	Barclays Agg 7.8%	REITs 11.8%	REITs 54.2%
Barclays Agg 8.4%	Market Neutral 7.4%	MSCI EAFE 39.2%	MSCI EAFE 20.7%	MSCI EAFE 14.0%	MSCI EAFE 26.9%	DJ UBS Cmnty 11.1%	Asset Alloc. 23.8%	REITs 28.0%	MSCI EME 10.2%	Market Neutral 5.0%	S&P 500 11.8%	Barclays Agg 75.4%
Russell 2000 2.5%	REITs 3.8%	REITs 37.1%	Russell 2000 18.3%	REITs 12.2%	Russell 2000 16.4%	Market Neutral 9.3%	Russell 2000 -33.8%	Russell 2000 27.2%	DJ UBS Cmnty 16.7%	S&P 500 2.1%	Asset Alloc. 6.5%	Asset Alloc. 73.5%
MSCI EME -2.4%	Asset Alloc. -5.4%	S&P 500 28.7%	Asset Alloc. 12.5%	Asset Alloc. 8.0%	S&P 500 15.8%	Asset Alloc. 7.3%	DJ UBS Cmnty -36.6%	S&P 500 26.5%	S&P 500 15.1%	Asset Alloc. -0.2%	MSCI EME 4.5%	Russell 2000 72.8%
Asset Alloc. -3.4%	MSCI EME -6.0%	Asset Alloc. 25.2%	S&P 500 10.9%	Market Neutral 6.1%	Asset Alloc. 14.9%	Barclays Agg 7.0%	S&P 500 -37.0%	Asset Alloc. 22.5%	Asset Alloc. 12.7%	Russell 2000 -4.2%	MSCI EAFE 3.4%	Market Neutral 72.7%
S&P 500 -11.9%	MSCI EAFE -15.7%	DJ UBS Cmnty 22.7%	DJ UBS Cmnty 7.6%	S&P 500 4.9%	Market Neutral 11.2%	S&P 500 5.5%	REITs -37.7%	DJ UBS Cmnty 10.7%	MSCI EAFE 8.2%	MSCI EAFE -11.7%	Market Neutral 2.9%	MSCI EAFE 64.8%
MSCI EAFE -21.2%	Russell 2000 -20.5%	Market Neutral 7.1%	Market Neutral 6.5%	Russell 2000 4.6%	Barclays Agg 4.3%	Russell 2000 -1.6%	MSCI EAFE -43.1%	Barclays Agg 5.9%	DJ UBS Cmnty -13.4%	Barclays Agg 1.1%	DJ UBS Cmnty 58.0%	DJ UBS Cmnty 58.0%
DJ UBS Cmnty -22.3%	S&P 500 4.1%	Barclays Agg 4.3%	Barclays Agg 2.4%	DJ UBS Cmnty 2.4%	REITs -2.7%	MSCI EME -53.2%	Market Neutral 4.1%	Market Neutral -2.5%	MSCI EME -18.2%	DJ UBS Cmnty 0.3%	S&P 500 33.4%	S&P 500 33.4%

Source: Russell, MSCI, Dow Jones, Standard and Poor's, Credit Suisse, Barclays Capital, NAREIT, FactSet, J.P. Morgan Asset Management.
The "Asset Allocation" portfolio assumes the following weights: 25% in the S&P 500, 10% in the Russell 2000, 15% in the MSCI EAFE, 5% in the MSCI EMI, 30% in the Barclays Capital Aggregate, 5% in the CS/Tremont Equity Market Neutral Index, 5% in the DJ UBS Commodity Index and 5% in the NAREIT Equity REIT Index. Balanced portfolio assumes annual rebalancing. All data except commodities represent total return for stated period. Past performance is not indicative of future results. Data are as of 12/31/11, except for the CS/Tremont Equity Market Neutral Index, which reflects data through 11/30/11. "10-yr" returns represent cumulative total return and are not annualized. These returns reflect the period from 1/1/02 - 12/31/11. Please see disclosure page at end for index definitions. "Market Neutral" returns include estimates found in disclosures. Data are as of 12/31/11.

J.P.Morgan
Asset Management

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Why diversification? You may have seen this "quilt" before. Asset classes are "stacked" in order of performance each year beginning in 2001, beginning on the left of the chart.

Take your pen and start at the top left corner in the red box which is Real Estate investments which happened to be the best performing asset class in 2001. From the left side of the chart connect the red boxes year by year. You will see how Real Estate has been the best performer and the worst performer over the last 10 years.

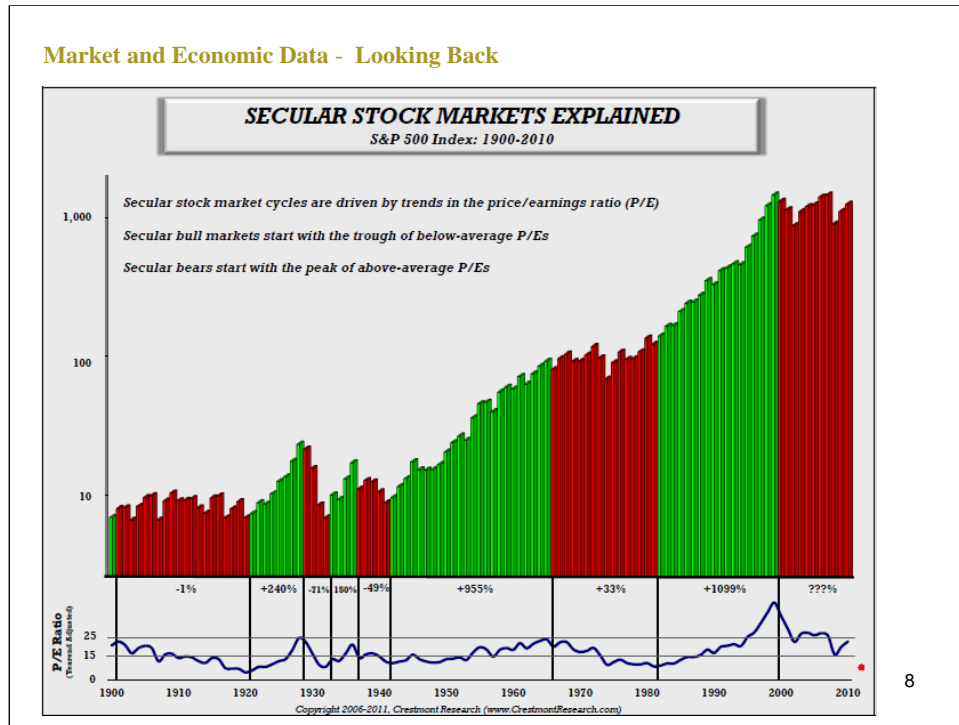
Now begin at the bottom of the page and do the same thing by connecting the gray blocks, Commodities, which happened to be the worst performing asset class in 2001. You will note commodities have neither been consistently at the top or the bottom.

Now, take a look at the white blocks which is an equally weighted blend of all the asset classes. Note that by blending strategies you will never be at the top and you will never be at the bottom.

How does diversification help?

It reduces portfolio risk, forces sell disciplines and keeps you invested in assets you might normally not have an affinity towards. By being well diversified, you experience a much smoother ride in your investment portfolio than by investing in one or two asset classes.

Market and Economic Data - Looking Back



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We would like to introduce the terms “secular” and “cyclical”. A secular market is one that lasts 5 to 20 years. A cyclical market might last 1 to 5 years. There's no magic around the number. Secular is long-term, cyclical is short term.

With this chart, Ed Easterling of CrestmontResearch.com takes much of the mystery out of bull and bear markets. On the upper section of the chart the vertical scale is a measure of wealth and the horizontal scale is time from 1900 to 2010. Note that the red sections represent years that the stock market did not make material progress, i.e. secular bear markets. The green sections are periods of time that the stock market made significant progress, i.e. secular bull markets.

Looking at the bottom left-hand corner of the chart, the vertical axis is price to earnings ratio (P/E), i.e. the price that is paid for every one dollar of earnings of the stock market of the last year. The horizontal axis is time.

Note a secular bear market starts when the P/E is high and ends when it's low. For the period from 1900 to 1920, you can see that the P/E started high and ended low – a secular bear market. The implication is when the price is high, relative to the earnings per share, investors are more optimistic about the future and conversely, when the price is low, more pessimistic about the future.

Now focus on the period from 1980 to 2000. In 1980, the P/E was around 8; a very pessimistic period of high inflation. In 2000, investor optimism drove the P/E to 40. Today, analysts tell us the P/E is now closer to 12 or 13 (see the red dot in the lower right-hand corner). Corporate earnings are up since 2000, but stocks are lower than 2000, because the price paid for each \$1 of earnings is less.

We think the chart makes two suggestions:

1. On a historic basis, the market is cheap, perhaps due to justified pessimism.
2. We are unable to identify the catalyst for optimism, but the chart illustrates the current course is unsustainable forever.

2012 Common and Uncommon Themes:

- **Government problems worldwide attract media attention and drive asset price volatility near term.**
- **Corporate and consumer fundamentals continue to improve, unnoticed by media.** (Our "Fork in the Road" theme.)
- **Investors are likely to experience anxiety and fatigue, yet make financial progress.**

Common conclusions by economists and strategists

- Volatility remains high all year, driven early by "policy-centric" uncertainty of all governments, especially Italy.
- Strong U.S. Dollar whenever there is a "back against the wall" European scare.
- European recession, but no economic Armageddon, as the Euro survives as a currency.
- No U.S. recession. Repeat, no "double dip".
- Low U.S. GDP growth and low interest rates stimulate interest in dividend paying stocks.
- WILD CARDS: **Bad** - Euro does collapse. **Good** - unexpected additional quantitative easing and policy agreements on both continents. Referred to as the "Paranormal", replacing the "new normal" economy.

We ask ourselves, "How long can these or any theme be sustained?"

Davidson Wealth Management themes and principles for 2012

- Global government deleveraging will continue for years to come. Get used to it.
- Reacting to politics has proven pointless. Resist the urge to trade reactively in 2012.
- Avoid "high frequency viewing" of economic data points and news. Most of today's current worries will be replaced by tomorrow's solutions and of course, new worries.
- Hold a little more cash than normal, not because the fundamental risks are so great, but because the human condition has become more reactionary and less thoughtful.
- We find investors with investment plans, driven by deep seeded values and a purposeful vision of the future, are the most hopeful.

Our planning in 2012 will ask one question in short supply, "What could go right?"

Davidson Wealth Management of Wells Fargo Advisors, LLC

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- Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater share price volatility. These risks are heightened in emerging markets.