OUTLOOK 2012

A REPORT FOR INVESTORS BY RINCON PACIFIC MANAGEMENT

JANUARY 2012

2011 was not all that bad a year for investors in the U.S. equity market. Large cap stocks, particularly dividend paying stocks, were the best place to be in 2012. The S&P500 out-performed most other indexes and about three-quarters of professional U.S. equity managers. Investors with large positions in international equity markets did not fair well. The MSCI World Index, minus the U.S., lost almost 15% for 2011.

Yes, the market was volatile but isn't it always that way? From top to bottom in 2011, the market measured by the S&P500 dropped 18% between May and September. But consider that the average intra-year drop for all years beginning in 1946 is 14.1% and once every three years or twenty-one times there have been declines of 15% or more.

The S&P500 registered a year-to-date gain of 8% in early May 2011 before falling to a 14% loss in October, yet this volatile market finished virtually unchanged for 2011'

So how will the market perform in 2012? On the positive side the Federal Reserve is targeting higher stock prices and doing everything possible to make cash and fixed income securities unattractive. Their stated policy is that they will hold interest rates down at least through 2013. On a short-term basis, this strategy seems to be working. Money seeks a return. Since the intermediate market bottom in early October 2011, investors have begun to shift money back into equities after favoring bonds for three years.

On the negative side, there are a number of issues. No one can predict how the European financial crises will play out in 2012. Even though the U. S. economy seems to be improving, it is difficult to identify powerful sources of economic growth in 2012. Europe is moving toward fiscal restraint. Here at home, political wars threaten to undermine a struggling economy, and taxes are rising. In short, investors face short-term market conditions that are positive but artificial, primarily due to unsustainable government policies.

Analysis of stock market price trends support the view that we will continue to experience volatility within a long-term sideways market. This range-bound market is now in its eleventh year. In the near term, we believe that seasonal patterns will hold in 2012. Historically equity markets have appreciated from November to May and then produced almost no investment return during the period May to November. The current market advance began in October 2011 and still appears to have potential for further gains. We believe the market will head higher in the early part of 2012 based upon a continuing flood of liquidity. The Federal Reserve is holding interest rates down and forcing investors into risk assets. Corporate earnings continue to rise although earnings pre-announcements appear to reflect a weakening economic backdrop. If we have a rally in stock prices in the first half of 2012, it will likely give most of the gains back sometime after mid-year. The news backdrop then will be the uncertainty of the national election outcome and the possibility that unserviceable debt structures in Europe may lead to some defaults.

The S&P 500 is advancing toward a double top in the 1400-1500 range. It appears to us that the range bound market will persist another 2-3 years.

Currently our managed portfolios are 60% to 80% invested in equities, concentrated in U.S. based companies that pay dividends. In managed portfolios, we are utilizing short-term bond funds, both tax-free and taxable, as a substitute for low yielding money market funds.

SUMMARY

On December 7, 2011, we wrote to you that increased equity positions were warranted. Our indicators suggested that the stock market correction and volatility of last summer was over and would be followed by a rally in stock prices. In a range-bound market, our strategy is to buy on weakness and sell on strength. Our indicators suggest that this rally in stock prices has further to run and we feel that a diversified equity investment position is appropriate.

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President

RINCON PACIFIC
MANAGEMENT

For more information about our services, please visit our website, www.rinconpacific.com, or contact us at (949) 369-0393, or via email: mspoo@rinconpacific.com

Rincon Pacific Management is a Registered Investment Advisor offering managed programs with a disciplined approach to creating wealth. The concept is simple and straightforward: our programs provide an organized method for earning superior returns in rising markets and preserving capital in declining markets.

With investment services designed for serious investors, Rincon Pacific Management combines the benefit of traditional investing with proper investment timing. Our methodology seeks to identify the best opportunities available, based on each client's individual objectives and risk tolerance.

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