ALL STAR QUARTERLY

FIRST QUARTER 2012 VOLUME 18 ISSUE 1

2012 – 1ST QUARTER REVIEW AND PREVIEW

BOB'S CORNER

How Do I Make Money The Next 30 Years?

Beware Of The Paradigm Shift!

During my first 30 years of managing assets, I have witnessed interest rates drop from 15.8% in September 1981 on government bonds, corporate bonds and bank certificates, to a low of 1.7% in the third quarter of 2011. For bonds, this has meant not just an average yield of approximately 6.8% but a total return of more than 900%. I will probably never see as great a total return on bonds ever again in my lifetime. This means that as rates climb from the 60 year lows of today, your total return will be more reliant on the capital appreciation of equities. Investors will also need to understand that the total returns for balanced asset allocation portfolios will be less as we enter a slower worldwide growth pattern. We believe the days of 8-12% growth in equity markets may be gone. That, along with bond yields and total returns shrinking, the average investor will need to have a greater percent of their assets invested in stocks in order to maintain their income potential in retirement. The Paradigm Shift will begin soon. It will be our job to keep you informed and educated on how to manage this shift. Please give me a call at your leisure to talk about this belief and how it affects you!

Thank you for your trust in the All Star Team!

Cautious Optimism Amid Slow but Steady Growth

MARKET OVERVIEW

Overview

The stock market enjoyed its best 1st quarter since 1998 as investors responded to stronger resolve from European leaders, the progress in job creation, improved consumer spending, and ongoing corporate profit gains.

As 2012 began, the European debt crisis dominated market headlines and loomed as a potential threat to global bond and stock markets. After months of negotiations European leaders finally approved a restructuring of Greek debt that keeps the European Monetary Union intact and provides needed debt relief to Greece. Debt reduction plans designed for implementation in the coming years were also approved for Italy, Portugal and Spain.

The European Central Bank stepped in by providing $1 trillion in long-term financing to European banks, giving them both the time and means to recapitalize while governments reduce their overall debt levels. Finally, during the closing week of the quarter, Euro Zone finance ministers agreed to boost funding to the European Stability Fund, providing additional support to the region's financially strapped governments. These actions raised hopes that the European debt crisis can be contained going forward.

In the U.S., the Federal Reserve promised to keep interest rates low until the economy is on sounder footing, encouraging investors to move out of the safety of low yielding bonds and into stocks and other long-term assets. Despite election year political gridlock that hamstrung fiscal policy, the Fed's aggressive monetary stance remains in place to support more employment, improved housing markets, and the overall flow of credit.

The economy demonstrated sufficient strength to chip away at the unemployment rate, with more than 730,000 new jobs created in the last three months. Glimmers of a housing recovery continue to prove fleeting, however, as home sales were flat and prices continued to decline, reaching their lowest levels since 2003.

Corporate profits continued to grow, but at a slower pace than we experienced coming out of the last recession in the early 2000s. Expect slower, single-digit profit growth in the coming year as companies have exhausted cost cutting gains of recent quarters.

The stock market's rapid ascent in the 1st quarter may be difficult to match. Slower corporate profit growth could result in more modest gains for the rest of the year. Though the European debt crisis appears contained for now, a European recession will slow global growth, and could impact economic fortunes in both the U.S. and China later in the year. Spikes in oil prices remain a risk due in large part to Iranian tensions, but recent hikes in Saudi oil production and domestic production gains should keep a lid on energy inflation over the long-term.

ECONOMY

THE 1ST QUARTER

The economy grew at a 3.0% clip during the 4th quarter of 2011 as increases in business inventories and improved consumer spending provided a year-end boost. Business spending and capital equipment investment led the economy by growing at a 9% pace during the 4th quarter. Consumers opened up their wallets as well, with overall spending improving by 4% in February. With monthly job gains of more than 200,000 for three consecutive months, consumer sentiment is also on the rise.

INSIDE…1ST QUARTER REVIEW AND PREVIEW CONTINUED…PERFORMANCE SUMMARY

Even though spending by consumers and businesses increased and energy prices spiked, inflation remains under control, up at a modest 2.9% annual rate. Interest rates remained low as well, though the 10-year Treasury yield increased 25 basis points during the quarter. The 10-year Treasury yield still ended the quarter with a very low yield of 2.22%. The Federal Reserve repeated its pledge to keep interest rates low for now, attempting to restore the flow of credit to businesses and consumers.

Both the Manufacturing and Service Sector Indexes were in expansion mode during the 1st quarter, with growth especially strong in the larger Service Sector. Manufacturing growth has waned in recent months, evidenced by a 1.2% decline in factory orders and modest 2.2% growth in durable goods orders. This is due in part to slowing export orders from Europe, where economic weakness could slow the rate of manufacturing job gains domestically in coming months.

The weak housing market and muted government spending remain the most significant drags on the economy. The most recent S&P Case/Shiller Home Price Index showed housing prices declined another 7% last quarter and 4% annually. Recent data on home purchasing indicates that a housing rebound is years off. Government spending fell 1.2% and will continue to decline as the U.S. joins other developed nations in attempting to reduce ballooning deficits and debt levels.

LOOKING AHEAD

Economic activity broadly improved during the 1st quarter, but these gains could be difficult to maintain. Business spending and investment is expected to slow down for the remainder of the year, with an anticipated decline from 9% to the 6% range. Corporate earnings are expected to moderate as well. Much will depend on whether the economy can sustain job creation at levels seen in recent months.

The low interest rate and low inflation environment remains favorable for business, so many economists expect the unemployment rate to continue declining through the remainder of the year, perhaps falling below 8% by year-end. A more severe recession in Europe, slower than expected growth in China, or an unexpected rise in inflation remain potential risks to the economy going forward. The Conference Board Index of Leading Indicators and the ECRI Weekly Leading Indicators both point toward modest economic growth ahead, with both indicators rising for the last five weeks of the quarter. Yet investors should be prepared for slower economic growth in the coming months.

BOND MARKET

THE 1ST QUARTER

Aggressive monetary policy by the Federal Reserve, the European Central Bank, and other global central banks led to solid performance in bond and credit markets during the 1st quarter. Corporations took advantage of low interest rates by issuing a record $400 billion in bonds during the quarter, providing fuel for future investment, hiring, and acquisitions.

The shift into risk assets benefited credit related sectors of the bond market, including Emerging Market, High Yield, and Corporate bonds. Emerging Market bonds led the way gaining 7% during the quarter, and High Yield bonds were not far behind, returning 5%. Corporate and Multi-Sector bond funds also had a solid quarter, both gaining 4%. Global bonds, Municipal bonds, and Inflation-Protected bonds saw more modest gains of 1% to 2%.

Those investors seeking the safety of U.S. Treasuries had a disappointing quarter, as broad U.S. Government bonds lost 1% and longer-term Government bonds declined 3-6% due to a significant jump in yields on U.S. Treasury securities.

LOOKING AHEAD

As long as global central banks maintain their stance of monetary easing, we expect to see continued gains in Corporate, High Yield, Emerging Market, and other credit-related bond sectors. Bond strategists see narrowing yield spreads between these bonds and Treasuries in the months to come as well.

We remain watchful for increases in inflation and additional jumps in Treasury bond yields. Further down the road as credit-related bond sectors return to normal yield levels and spread levels narrow, we expect to see inflation protected bonds and floating rate bank loans become attractive as ways to insulate bond investors from both rising inflation and rising interest rates.

DOMESTIC STOCK MARKET

THE 1ST QUARTER

The rally in risk assets extended to stock markets during the 1st quarter, with the Russell 3000, a measure of broad U.S. stock market performance, gaining 12.9%. The wealth was shared across the board as Large Caps and Small Caps, Growth and Value, and all industry sectors except Utilities displayed significant gains.

Large Cap and Mid Cap stocks gained 12.9% during the 1st quarter, and Small Caps were not far behind, returning 12.4%. Growth style stocks led the market, gaining 14.6%, while Value style stocks rose 11.2%.

Financial and Technology stocks were the best performing industry sectors, both gaining 21% during the period. Other cyclical sectors such as Consumer Discretionary, Materials, and Industrials also generated double-digit gains.

Market driving events that occurred during the quarter included the Federal Reserve's approval of dividend payments for major U.S. banks and the announcement by Apple, Inc. that it would begin paying investors a dividend from its $100 billion cash pile. These events gave an extra lift to Financial and Technology stocks.

Performance Update

Market Index	*1st Qtr*	*1 Year*	*3 Years*	*5 Years*
DJ Industrial Average	12.91	7.67	24.31	2.47
S&P 500	12.59	8.54	23.42	2.01
Russell 2000	12.44	-0.18	26.90	2.13
S&P Mid Cap 400	13.50	1.98	28.55	4.78
Russell 3000	**12.87**	**7.18**	**24.26**	**2.18**
S&P Global BMI	**12.34**	**-0.92**	**22.44**	**0.58**
MSCI EAFE	10.86	-5.77	17.13	-3.51
MSCI Emerging Mkts	14.08	-8.80	25.07	4.67
NASDAQ Composite	18.96	12.31	27.68	5.96
Barclays US High Yield Bond	5.34	6.45	23.87	8.10
Barclays US Aggregate Bond	0.30	7.71	6.83	6.25
Barclays Global Aggregate Bond	0.87	5.26	7.52	6.38
JPM Emerging Local Mkt Bond	4.86	12.60	16.47	8.60
Barclays US Government Bond	-1.12	7.89	3.96	6.02
Barclays US Credit Bond	2.04	9.58	12.32	6.91

Valuations for stocks remain below historical averages, interest rates linger near historical lows and corporate cash levels are topping historical highs. All were fundamental underpinnings of the rally in stocks during the 1st quarter.

LOOKING AHEAD

Despite recent gains in stocks, the outlook is more cautious. Profit margins are beginning to level off for many companies. This could result in a modest stock market pullback again, much like we experienced last year.

The outlook for Technology and Financial stocks remains favorable and we expect they will be among the most attractive industry sectors going forward. Small Cap stocks also look attractive compared to the broader market and we expect they will resume market leadership later in the year. Dividend stocks lagged the market during the 1st quarter but we expect they will again become increasingly important if stock market returns moderate.

INTERNATIONAL MARKETS

THE 1ST QUARTER

With much of the headline risk originating overseas, foreign markets lagged domestic U.S. stock markets in the 1st quarter. The primary contributor to this weakness was, not surprisingly, Japan. The natural disaster and nuclear crisis led to sharp sell-offs in Japanese stocks, though they have now begun to recover. By quarter's end, Japanese equity markets were down 4.9%. Despite its sovereign debt issues, European markets were the best performers, gaining 6.5%. Solid economic growth and falling unemployment rates boosted both France and Germany, as they returned 10.6% and 7.5% respectively.

Emerging Market stocks got off to a strong start during the quarter, reversing their 2011 performance. Even though returns leveled off towards the end of the quarter, Emerging Market stocks still led global stock markets with a 15% gain during the period. International stock market gains were broad-based as well. Most nations experienced double-digit returns, with export giants Germany and India leading with 20% gains.

Broad European markets gained 12%, matching returns in U.S. domestic markets. Some investors saw European stocks as bargains despite the region's economic struggles. Stocks in debt-stressed nations such as Spain and Portugal were essentially flat. Japanese stocks gained 11%, participating in the global rally despite slowing export sales.

LOOKING AHEAD

Although the European debt crisis may be contained, Europe is still facing a recession during the remainder of 2012. The key unknown for global markets is whether its recession will be mild or if government budget cuts will make it more severe and its impact be felt in markets worldwide.

China, the world's second largest economy is also undergoing a transition from a largely export driven economy to one with more domestic demand for its products and services. The government is also undergoing a transition in political leadership and this is expected to slow economic growth to the 7-8% range during 2012, still healthy and far from the "hard landing" that some economists fear. As long as global economic growth is sustained, we expect Emerging Market stocks and Asian stocks to be well positioned.

SUMMARY

Two quarters of strong stock market gains could create an environment for market corrections in the coming months. As long as the U.S. economy continues to show improvement and Europe avoids a "severe" recession, these pullbacks should prove to be only temporary. They could represent an opportunity for long-term investors who have been out of the stock market to "get back in the game."

Our market view is to be cautiously optimistic based on the mix of positive and negative factors on the horizon:

POSITIVES

1. Accelerated job gains of 200,000-plus in the last three months
2. Improved economic indicators
3. Stability in European debt markets
4. A favorable business environment with low interest rate and low inflation
5. Record profits and increasing dividends
6. Equities under-represented in portfolios

NEGATIVES

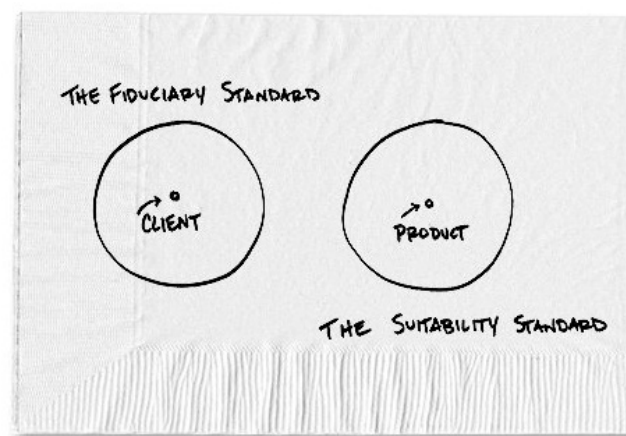
1. Frequent downward revisions to government economic data
2. Questions on impact of "mild winter" on economic strength
3. Spain, Portugal and Italy still facing debt issues
4. Business spending and investment slowing
5. Slower earnings growth for 2Q/3Q
6. Historical trend of low volatility often preceding market pullbacks

A Conversation about the 'F' Word

While some content in our newsletter is best suited for adults, the 'F' word referred to in the title is not of the four-letter variety. This page focuses on the word **fiduciary** and why it is important for all investors to understand the difference between a fiduciary advisor and a more traditional broker. All Star Financial has operated as a fee-only, independent, fiduciary adviser since 1990 and we built our business by putting clients' best interests first. There are an increasing number of reputable wealth managers that serve in a fiduciary capacity, but disappointingly there remain a large number of brokers who try to position themselves as advisors. The table below details some of the important distinctions between an independent, fiduciary investment advisor and a broker.

Fiduciary Standard (RIAs)	Suitability Standard (Brokers)
Legally bound to act in the best interests of clients	Choose investments that suit a risk tolerance standard, but are not specifically geared to the clients' best interests
Required to obtain client consent for any unavoidable conflicts of interest	Required to disclose conflicts of interest, but not necessarily to avoid them
Provide disclosure on advisory fee in an up-front and transparent manner	Can receive soft dollars and revenues that are not necessarily consistent with the clients' best interests
Not involved in underwriting or investment banking	Firm may provide underwriting and/or investment banking services, often in conflict with the clients' interests
Cannot trade with their clients as principal dealer	Can earn significant undisclosed profits by trading as a principal with clients

There is another 'F' word that is also gaining more steam in the financial press today and that word is **fees**. All Star Financial continues to be fee-only, which states that we are compensated solely by our clients through either an asset management fee and/or an hourly/fixed-rate fee. We do not receive commissions, rebates, awards, bonuses or other forms of compensation from third parties as a result of clients' implementation of our recommendations. **Less than 2% of all financial advisors are truly fee-only.** Our fee structure genuinely distinguishes us from most of our competitors when it comes to providing objective guidance.



Sketch provided by Carl Richards

In the first three months of 2012, many articles in the financial and mainstream press touched on the fiduciary standard. Most notable was the criticism leveled by a disheartened ex-Goldman Sachs employee about how his former Wall Street firm struggled to put clients first. There have also been numerous opinion pieces on the expansion of the fiduciary standard to cover brokers and not just independent advisers like All Star Financial. The expansion of the fiduciary standard would be beneficial to investors that are not currently using a fiduciary advisor, though many highly compensated Wall Street lobbyists are determined to see that this proposal does not pass. **All Star Financial will continue to operate with the client's best interest as our top priority and we know that in the long run this philosophy will work to the benefit of both our clients and ourselves.**

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