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**Sandpiper Capital**

# Gleanings

## "But, what should I do now?"

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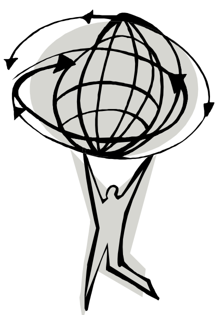


*"There is a solid relationship between the price of gold and the quantity of central bank reserves. Reserves are growing and will continue to grow at a rapid pace."*

That's the typical response from friends of mine who've read "Gleanings" and found it maybe a little too "conceptual". There *has* been a conspicuous absence of formal buy/sell advice in these missives. Having read thousands of market letters over the course of my career has been, I have to admit, a corrupting influence on my client communication skills. Market letters have a couple of big handicaps that the writer needs to consciously attempt to overcome. One is the regulatory liability that accompanies any specific public investment letter recommendations. (see the new disclaimers that follow). The other is the writer's fear of providing a documentable record of predictions about the future. The constantly shifting dynamics that shape financial markets challenge any investment strategy that is not distinctly flexible. That being said, there are a few things that we *can* know, (regardless of the fact that there are many more that we can't). So… In answer to the question, "What should I do now?" ; here is some specific advice for 2012 about those things I believe I *do* know.

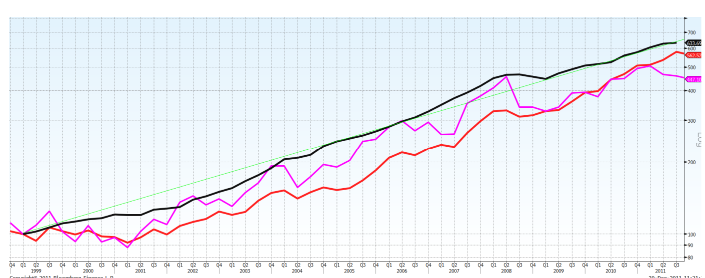
### Market Returns through 12/31/2011

| Index | 2009 | 2010 | 2011 | 5 Yrs |
|---|---|---|---|---|
| **S&P 500** | 26.5 | 15.1 | 2.1 | **1%** |
| **ML 1-10 yr Govt/Corp** | 5.7 | 6.0 | 5.9 | **5.9%** |
| **EAFE (Dev Fgn Mkts)** | 31.8 | 7.8 | -12.2 | **-1.2%** |
| **Emerging Markets** | 78.4 | 19.0 | -18.4 | **2.5%** |

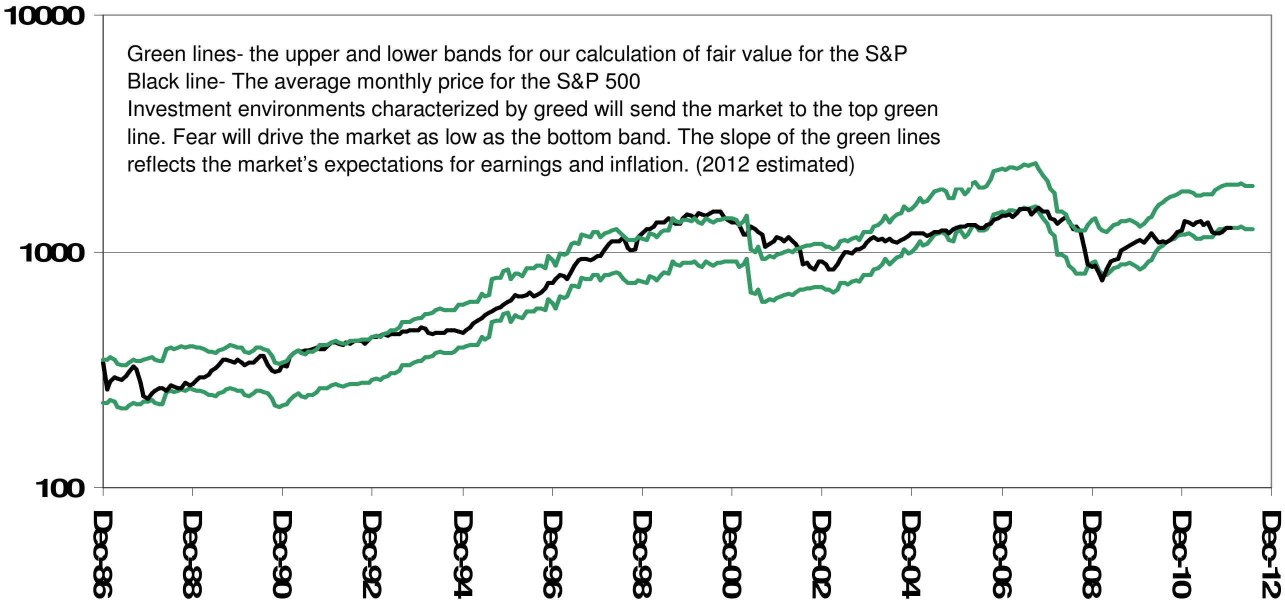
**Bonds** Rampant increases in global manufacturing capacity means there are too many goods chasing too few dollars. (New money creation is not keeping up with the wealth destruction from defaulting debt.) With central banks targeting low rates because of the deflation risk, short term rates will stay low and the US ten year rate will reflect that. Any resolution of the Euro crisis will bring the dollar down, lifting rates and should provide a buying opportunity. Buy six to ten year AA or AAA taxable muni's at 4% or better and hold to maturity.

**Gold** There is a solid relationship between the price of gold and the quantity of central bank reserves. (See the chart below). Reserves are growing and will continue to grow at a rapid pace (15 to 20% annually) as central banks try to offset loan losses. Gold miners, while more volatile than gold, are cheap currently. Buy three or four of the largest, as well as the bullion (GLD) and hold.

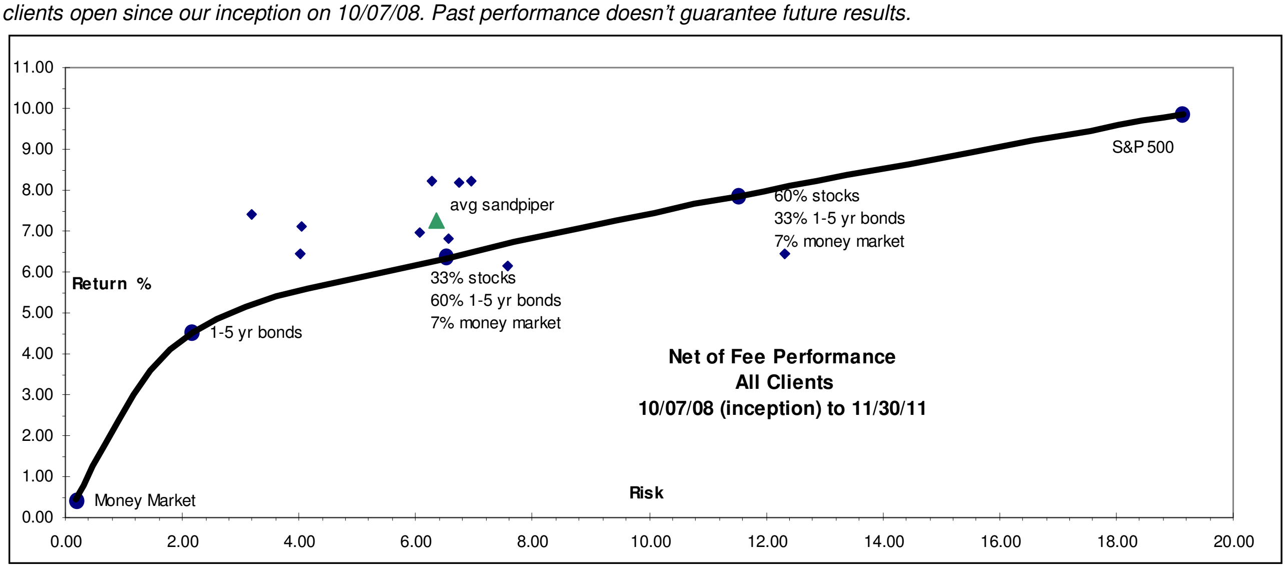
Black line- Total Global Monetary Reserves
Purple line- American Barrick (ABX) and Goldcorp (GG) equal weighted
Red line- Gold price
Green line- 16% trendline



**Stocks** We are in a secular (the long term trend) bear market as valuations suffer from monetary inflation. The more money printed, the less the market will pay for a dollar of earnings. Profits are also at peaks as compared to sales, GDP and wages suggesting some retrenchment is possible. A 1250 S&P index (13x's earnings) accurately reflects those issues, however low cost money will continue to generate record volatility with risky assets all trading the same direction. For the coming year, I'd expect a range of 1100 to 1400 with lots of trips in between.




*Disclaimer- While these ideas reflect the long term macro-economic factors that drive my investment process, there are risks that they will not play out as forecast.* ***For bonds****, buy and hold for six to ten years means that entirely new factors may come to the fore buy then. If rates are higher on similar maturity securities, the market value will be decreased. Holding to maturity also means giving up the opportunity to use this money for other things. Should you decide to proceed anyways, compare the offering yields from your broker to traded prices at [http://emma.msrb.org/](http://emma.msrb.org/), you know, just to make sure. You'll also get a feel there for the bid/asked spread, that is; what you lose if you turn around and immediately sell, bigger issues get tighter spreads.* ***For gold****, the main risk is that the market continues to treat all risky assets the same. Traders now sell any security that has volatility whenever they decide that they might profit from market fear. Good/bad, foreign/domestic, stock/commodity/currency, all get sold when traders want a "risk off" trade and bought just as indiscriminately when growing optimism tells them to reverse course. Crazy, noisy, meaningless volatility is the price of cheap leverage.* ***For stocks****, the risk to the 1150 minimum S&P is that politicians get in the way of central bankers bailing out the system. Trillions of dollars of potentially defaulting debt needs trillions of dollars of replaced bank capital. Central bankers know that, let's hope governments do too.* ***And generally****, history says that, if you're the typical investor, the principal risk to your portfolio is you. Have a plan. Stick to it. Never make an emotional trading decision. People cannot process information well in an emotional context. Wait for cooler moments or call me if you're unsure, I don't mind. Then document your risk and returns (you should be above the market line as illustrated below) and periodically compare them to that from professional managers. The diamonds here are all SC clients open since our inception on 10/07/08. Past performance doesn't guarantee future results.*




*Tom Lukic*