Leigh Baldwin & Co.
Investment Brokerage

What are the odds?

The most famous American bookie (and football analyst) "Jimmie the Greek" first made his name when he wagered $10,000 in 1948 on the presidential election. Getting 17-1 odds, The Greek bet that Harry S. Truman would beat Thomas Dewey based primarily on the fact that Dewey had a mustache, and "American women didn't trust men with a mustache." The rest is history.

The year in stocks for 2011, as measured by the S&P 500 (500 largest companies) ended the year at mathematically the exact same place that it started 52 weeks earlier. Amazing, when you consider that market historian John Harris has looked back to 1928 and there has only been 9 times where the market has been between -5% or +5% of where it began and in 2011 we hit it square on, the Mendoza line. This lack of change is particularly shocking when you consider what the headlines were this year, US debt downgraded, European debt imploding, and US unemployment over 10%, Middle East conflict, etc. What does this tell us for 2012 and beyond?

The volatility of 2011 reminds us that what was true last year and for the past 200 years is that stock prices follow earnings. It is true that headlines and world events move markets and all stocks along with them, and it is hard to find a time period when there wasn't some type of crisis or concern to deal with. Great companies, companies that have strong balance sheets, recurring revenue, dividend growth, premier brands, etc will perform ultimately based on those factors. That is why IBM and McDonalds traded to all-time highs in 2011 and helped lift the Dow to a 7% gain including dividends. 2012 may bring more of the same.

Heading into 2012, I believe that stock valuations are relatively cheap at a projected PE of around 12. Analysts and economists are predicting a 7-10% growth in profits (although those numbers have fallen in the past 3 months) and if we get something close to resembling that number, US stocks should remain a major part of your portfolio. Mix in some international and emerging markets exposure for the growth that is happening overseas and returns may follow. In the bond market arena, interest rates will most likely remain low for another year, but substantial gains (like the +8% seen in treasuries) is most likely a long-shot.

The markets in 2012 could be treacherous based on the structural problems with debt in many countries including our own. There will be an election that will cause some uncertainty that markets do not like. I believe though that after 12 years (since the Dow first hit current levels) great companies are as profitable as ever, are buying back stock at a significant pace and are in a great position to weather what could very well be a "slow motion" financial debt crisis in Europe as opposed to what we lived through in 2007-2008. Finally, when considering headline risk, take a moment to imagine (think Truman vs. Dewey) what happens if the headline is that Europe and the world have dealt positively with their issues. The horses would be off to the races and Jimmy the Greek would smile down as our markets finally hit stride. Thanks to everyone for your continued business and to the lock pick that 2012 is the best year ever!

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