



Q4 2011 Market Commentary

Unprecedented levels of market volatility throughout 2011 reminded investors of being on a roller coaster ride at their favorite amusement park. One moment would be a feeling of sheer elation as the S&P 500 appeared to be on track to climb skyward, then the next moment would deteriorate into extreme nausea as the ride turned into a steep plunge downward. It was simply a crazy year where stocks would catch fire one minute, and then suddenly collapse to near bear-market lows the next. In the end, when the roller coaster pulled back into the station, the market ended the tumultuous year right where it started. The broad market as measured by the S&P 500 posted its smallest year-over-year move, either up or down, in the history of the index finishing down 0.04 points or 0.003%. In the meantime, the DJIA averaged daily intraday swings of 270 points between August and November, more than 2X as wide as during the same period in 2010.

Negative headlines that had been prevalent since the start of 2011 simply continued to dominate the news and would not go away. The possibility of the European debt crisis finally spiraling out of control, uncertainty here at home over prospects for the 2012 election, the possibility of the global economy slipping into a recession, and the inability of our own government to quell their fiscal squabbling all led to violent ups and downs in the market. Yet despite the constant barrage of negative news, the markets managed to pivot in the fourth quarter and finish essentially flat for the year.

In short, 2011 experienced a great fourth quarter, but overall a very frustrating year for stocks. The S&P 500 posted an 11% gain for the fourth quarter but finished flat for the year. The DJIA comprised of 30 large stocks rose 12% during the fourth quarter to end the year +5.5%. Notably, the gain of 1344 points during Q4 was the largest point gain in the index's history. The tech-laden NASDAQ advanced nearly 9% for the quarter to finish 2011 with a return of -1.8%. Cambridge portfolios trailed the markets in Q4 finishing up 5.3% for the quarter. For the year, portfolios were down 9.7%. A combination of momentum stocks getting whipsawed in the third quarter as well as a defensive posture established at the outset of Q4 contributed significantly to relative underperformance in 2011. A majority of the ten technical indicators which Cambridge utilizes to assess market risk turned negative at the conclusion of September resulting in one third of the portfolios being liquidated and invested in cash. These market indicators will continue to be assessed on a monthly basis. For the time being and until the majority of indicators are again graded as positive, however, portfolios will be postured with two thirds invested in equities with the remaining one third invested in risk-free cash equivalents.

As we proceed into 2012, we do so with great caution. Acknowledging that much of the extreme domestic market volatility seen in 2011 was caused by extraneous factors such as the earthquake and tsunami in Japan, continued Middle East unrest, Europe's ongoing debt crisis, and political gridlock in a dysfunctional Washington, to name just a few, many problems remain unresolved and have therefore carried over into 2012. Until there is some clarity to these issues and sustainable long term market trends reemerge causing our technical market indicators to once again shift into positive territory, our investment posture will remain less than fully invested. As we move forward into these very uncertain times, Cambridge Financial Group believes that erring on the side of caution is prudent and recommended at this time.

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