Dorchester Advisors
Money Worked Harder

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January 15, 2013

U.S. stocks had a good year in 2012; the S&P 500 Index was up 16 percent. Overseas stock markets also performed well as did Bonds. Generally, riskier areas were more profitable.

There are bullish factors that could drive stocks to high returns over the next five years, but in our view it is more likely that we see slow-growth with a continued aversion to risk. Our expectation of slow economic growth has been the case in the recent past. Though there has been progress with deleveraging, the process is not complete and the risk of another crisis still exists. And we do know that there will be higher taxes on investment profits.

A key risk going forward is growing public sector debt. The developed world faces significant debt-related challenges and the solutions are neither easy nor quick. Last-minute compromise buys politicians a little time to address important long-term fiscal issues, but does little to resolve them. Developing countries are generally less indebted and growing faster, but growth has slowed there as well.

Given continued risks and modest return expectations for most asset classes, our portfolios are positioned conservatively but not excessively cautiously. We also hold some assets that may perform well and continue to look for more opportunities. But, this strategy requires patience; fortunately, 2012 was an example of it working.

ANNUAL MARKET REVIEW 2012

Resilience in the face of adversity seemed to be the theme for 2012. Hurricanes that shuttered Wall Street for two days and cut oil production, the threat of a "Grexit" from the euro, Europe's record unemployment and second recession in four years, Chinese growth that hit a three-year low, and uncertainty about elections here and abroad--such formidable obstacles slowed the progress of the global economy but didn't bring it to its knees.

Debt-related news out of Europe continued to play a major role in global bond and equities markets. Despite cracks in the French/German alliance, the eurozone finally appeared more willing to take joint action to enforce fiscal discipline. In exchange for fresh austerity explosive to merely robust, China chose new leaders for the next decade who are considered to favor existing policies. In the United States, strong U.S. corporate earnings had begun by year's end to show the toll taken by a slowing global economy. Solid if not robust economic growth, an improving housing market, lower unemployment, and low inflation all had to contend with concerns worldwide about the fiscal cliff.

However, that resilience could be tested in 2013. Though a last-minute bargain averted a full-scale plunge off the fiscal cliff, headwinds could pick up if Washington can't reach an agreement (again) on the debt ceiling and spending cuts still scheduled to begin in 2013.

Market/Index	**2011 Close**	**As of 9/28**	**As of 12/31**	**Q4 Change***	**2012 Change***
DJIA	12217.56	13437.13	13104.14	-2.48%	7.26%
NASDAQ	2605.15	3116.23	3019.51	-3.10%	15.91%
S&P 500	1257.60	1440.67	1426.19	-1.01%	13.41%
Russell 2000	740.92	837.45	849.35	1.42%	14.63%
Global Dow	1801.60	1921.70	1995.96	3.86%	10.78%
Fed. Funds	.25%	.25%	.25%	0 bps	0 bps
10-year Treasuries	1.89%	1.65%	1.78%	13 bps	-11 bps

*Equities figures reflect price changes, not total return.

Snapshot 2012

The Markets

- Equities: Though equities certainly experienced some volatility during the year, the stomach-churning declines of 2011 gave way to 2012's more moderate fluctuations and dramatically improved performance. Optimism about the prospects for an economic recovery powered equities to year-to-date highs in the fall that lost ground in the fourth quarter as the path to a detour around the fiscal cliff seemed rockier. Helped (and eventually hampered) by some key tech bellwethers, the Nasdaq's Q1 gain of almost 19% helped it set the pace for the domestic indices for much of the year and generally remain above its 2007 high. The Russell also powered back from 2011's loss, while the Dow--the strongest of the five indices in 2011--took a back seat last year. It was even outperformed by the Global Dow, which benefitted in the year's second half as Europe managed to avoid disaster. And the S&P 500's 13.4% gain for the year was a definite improvement over the 0.0% of the year before.

- Bonds: Rock-bottom Treasury yields somehow managed to drop even further as the 10-year bond briefly hit a record low of roughly 1.43% in July. Treasuries, corporates, munis, junk, internationals--bonds benefitted across the board from investor demand and the Fed's stepped-up quantitative easing efforts. Investors who continued to pull money out of stock funds put much of it into bonds, reassured that higher interest rates were at least a couple of years away from affecting bond prices.
- Oil: After starting 2012 at roughly $103 a barrel and remaining above $100 through the first four months, oil prices reversed the previous year's upward trajectory. Despite a slight bump in August/September, mounting concerns about a slowing global economy took oil to $85 a barrel before a year-end rally nudged it back up to end the year at roughly $93 a barrel.
- Currencies: After a spring surge pushed the U.S. dollar to the year's high against a basket of six currencies in June, the greenback lost 7.5% over the next three months before rebounding to end 2012 only slightly lower than where it started. Despite a couple of dips, the euro strengthened against the dollar, gaining roughly 2% over the year to end at roughly $1.32.
- Gold/silver: After plummeting almost 14% between late February and mid-May, gold spent the summer bouncing along on either side of $1,600 an ounce. By mid-July, a rebound had sent the price to the year's high of just under $1,800 before fading to end 2012 at $1,676. And after spiking more than 60% to a high of $48 an ounce in April, silver prices settled down, ranging between $26 and $37 for the rest of 2012 and ending at $30.

The Economy

- Unemployment: The unemployment rate continued to meander downward, ending the year at 7.7%. Though the pace of improvement was frustratingly slow--the jobless rate didn't fall below 8% until September--the employment picture was still better than December 2011's 8.5%. However, the Fed has forecast only minimal improvement in that figure during 2013, and has promised to keep interest rates low until unemployment hits 6.5%.
- GDP: Despite a little spring slump, by the third quarter the U.S. economy was growing at an annualized 3.1%--more than double Q2's 1.3% and the fastest growth of 2012--and Q3 corporate after-tax profits were 3.2% ahead of the same time a year earlier. However, there were signs that growth had begun to taper off in the fourth quarter as anxiety about elections and the fiscal cliff mounted.
- Inflation: Modest improvements in the economy had little impact on prices at either the consumer or wholesale level. By November, annual consumer inflation was only 1.8%--well within the level the Fed considers acceptable and lower than 2011's 3%. The 1.5% increase in wholesale costs was slightly better, and was far more moderate than 2011's 4.7% wholesale price jump. Consumer spending and retail sales both showed gains for the year, though holiday shopping was reportedly slower than anticipated.
- Housing: While not completely healed, the housing market showed signs that a sustainable recovery was under way. By year's end, sales of new homes had hit their highest level since

April 2012 and were 15.3% higher than a year ago, while home resales had their ninth straight month of gains. Home prices were up an average of 4.3% from a year earlier, while housing starts, construction spending, and building permits all had strung together several consecutive months of improvement.

Data sources: Includes data provided by Brounes & Associates. Economic: Based on data from U.S. Bureau of Labor Statistics (unemployment, inflation); U.S. Dept. of Commerce (GDP, corporate profits, retail sales, housing); S&P/Case-Shiller 20-City Composite Index (home prices); Institute for Supply Management (manufacturing/services). Performance: Based on data reported in WSJ Market Data Center (indexes); U.S. Treasury (Treasury yields); U.S. Energy Information Administration/Bloomberg.com Market Data (oil spot price, WTI Cushing, OK); www.goldprices.org (spot gold/silver); Oanda/FX Street (currency exchange rates). All information is based on sources deemed reliable, but no warranty or guarantee is made as to its accuracy or completeness. Neither the information nor any opinion expressed herein constitutes a solicitation for the purchase or sale of any securities, and should not be relied on as financial advice. Past performance is no guarantee of future results. The Dow Jones Industrial Average (DJIA) is a price-weighted index composed of 30 widely traded blue-chip U.S. common stocks. The S&P 500 is a market-cap weighted index composed of the common stocks of 500 leading companies in leading industries of the U.S. economy. The NASDAQ Composite Index is a market-value weighted index of all common stocks listed on the NASDAQ stock exchange. The Russell 2000 is a market-cap weighted index composed of 2000 U.S. small-cap common stocks. The Global Dow is an equally weighted index of 150 widely traded blue-chip common stocks worldwide. The U.S. Dollar Index is a geometrically weighted index of the value of the U.S. dollar relative to six foreign currencies. Market indexes listed are unmanaged and are not available for direct investment.

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