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THE TEMPO VANTAGE

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The Bull is Alive!

After two very profitable quarters (The S&P 500 gained more than 10% in Q4, 2011 and in Q1, 2012) it is not surprising that the market took a breather in the second quarter of 2012. This is especially true if you believe, as I do, that we are in the third stage of the economic recovery which is characterized by periodic advances and declines resulting in higher highs and higher lows. As I've written extensively about this pattern over the past few years I won't belabor it here. Suffice it to say that the market movement in Q2, 2012 is well within the range of expectations.

Thanks to a positive June the S&P 500 lost only -3.3% for the quarter. Mid Cap U.S. equities (-5%), small cap U.S. equities (-3.6%), and international equities (-6.9%) didn't fare as well.

The newspapers, magazines, and TV personalities tell us that the reasons for the decline were concerns over fears of a double dip recession and worries over the Eurozone. And they might be right.

But for them it is not about being right or wrong. It is about being sensational to grab viewers' attention. How boring would it be if they said that the market was simply following the normal cyclical pattern that occurs in economic recoveries? Even I wouldn't watch!

The peak decline of -9.7% (March 26 to June 1) on the S&P 500 doesn't even qualify as a correction (defined as a -10% drop) let alone a bear market (defined as a -20% drop). The fact that the quarter resulted in a decline of only -3.3% makes me think that this is a normal pause in the midst of a continuing bull market.

I don't want to minimize concerns about Greece and the economy. These fears are real and legitimate. But they are not new stories. We've been talking about them for the better part of three years now. If market participants were really worried about Greece and a double dip recession the market would have fallen more.

The stories that will dominate the news (and markets) between now and the end of the year are just beginning to surface: the presidential election and the expiring Bush era tax cuts.

Right or wrong (perhaps a good subject for a future Vantage) the market perceives Republicans as better for the economy and the stock market. As we get closer to November the shifting winds of the election will surely sway the markets.

But even more significant will be the fate of the Bush era tax cuts. If the government does nothing these tax cuts are scheduled to expire at the end of the year. In that case taxes would rise on income, dividends, capital gains, and estates. This is exactly the wrong time to raise taxes and would heighten fears for the fragile economic recovery. Believe it or not the government raised taxes twice in the midst of the Great Depression and that did not work out very well. "Those who cannot remember the past are condemned to repeat it." (George Santayana)

My best guess is that the government will do what it does best and kick the can down the road by preserving (most of) the current tax structure for another year or two.

But if you think that the cuts will expire and taxes will rise you would certainly consider taking some tax savings actions by the end of the year. These would include realization of long term capital gains, accelerated income recognition, and increased gifting.

Tempo Financial Advisors' Investment Performance

The ultimate coup as an investor is when you make money when the rest of the world is losing money. It doesn't happen very often. But that was exactly the situation for both the **Tempo Dynamic Income** and **Tempo Dynamic Growth** programs in the second quarter.

The Dynamic Income Program gained 3.2% and the Dynamic Growth Program gained 1.1%. Our models correctly invested accounts conservatively with over-weight positions in a variety of bonds and minimal equity exposure. And the equity that we did own (utilities, healthcare, and The Gateway Fund) all out-performed the overall market by either breaking even or earning slightly positive returns.

If you only look at your accounts quarterly (which is perfectly fine by the way), you sometimes miss the Dynamic Programs at their best. At the beginning of June when the market was at the low point and the world seemed a scary place the Dynamic Programs were pillars of stability, both hovering around break-even. Maybe I need some more excitement in my life but I found that exhilarating.

By contrast it was not as exhilarating watching **Tempo Lifestyle** accounts at the beginning of June. As long term investments these accounts are more prone to ebb and flow along with the markets. In the end though, the positive June did a lot to make the quarter much less painful.

Relative performance for Lifestyle accounts followed financial theory with conservative accounts falling a bit less than the market (as measured by the S&P 500) and aggressive accounts falling a bit more than the market. As has been the case on and off recently, the leadership in the market was in large cap U.S. equities. That means that our diversifying positions in mid cap equities, small cap equities, and international equities hindered performance.

Our tactical over-weights also had varying degrees of success or lack thereof. On the plus side our real estate position bucked the overall market direction and generated a gain for the quarter. Less successful were our technology holdings, which underperformed the market. The bad news/good news story belongs to our financial services positions. The bad news is that the average financial fund under-performed the overall market. The good news is that our specific financial funds were better than average, either performing in line with or better than the market.

Company News

June 20th, 2008. A date I'll never forget. That is the day Tempo opened its doors. Hard to believe that is over four years ago! Thanks to all of you who helped make this the best business decision I ever made!

As always, please contact us if there has been a change in your financial circumstances that would warrant a fresh perspective on your portfolio.

Daniel J. Traub