

Can The Bull Skate?

There's an old proverb about ice skating on a frozen pond. "1 inch stay away, 2 inches one may, three inches small groups, 4 inches all may." There's another little saying "If you're going to dance on thin ice, you might as well do the polka!" So how thick is the market's ice? It's surely thick enough for a little swing, and may even support a rousing polka....but ice has been known to crack suddenly. What percentage of our portfolios should still be held in cash, and what is the optimal balance of stocks and bonds? How much confidence should we have in the U.S. recovery, and is it time to invest with confidence in the emerging markets?

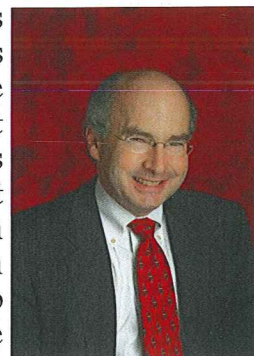
What about those recent headlines that announced the third anniversary of the Bull Market? What Bull Market? For the last three years we've been crawling across the most dangerous ice since the Great Depression, panic stricken, and grinding our finger nails to the quick as the European Credit Crisis has tried to drag us back into the frigid black waters of 2008. How about waiting until the Dow and the S&P are nearing their levels of October, 2007 before anyone starts talking bull?I (compliance requires me to state that the Dow and S&P are not securities and that past performance is not a guarantee of future return) If the global economies continue to recover throughout the spring and summer, and if the Dow gains another 6% or 7%, we will have regained our pre-debacle high of 14,000. (October, 2007) May we then breathe a sigh of relief for having recaptured what is legitimately ours, and watch the bull charge across green pastures? Or, should we view a 14,000 Dow as a lucky score and prepare for another market correction as we watch the bull skid spraddle-legged across thin ice?

This is my personal opinion, so please

remember that talk is cheap and anything is possible. I believe we dodged a deadly bullet in 2008, and as bad as the market was, it could have been worse. I agree with those economists who suggest that we were very close to going

over the cliff and into a worldwide depression. I believe that both political parties were at fault for creating an irrational and fraudulent mortgage environment, that there was an alternating imbalance between government and private enterprise, and that a bubble may have been building for longer than we first thought. With that being said, it appears that Uncle Sam is coming out of his economic stupor and may soon begin flexing his muscles again.

The world is no longer freaked-out about the European Credit Crisis, and even if Greece eventually leaves the European Union, there may be sufficient financial safeguards in place to protect against another 2008. Global stability will always be challenged by tensions in the Middle East, the fluctuating cost of oil, and the unpredictable behaviors of such rogue nations as North Korea and Iran. Old clichés about capitalism vs. communism are probably invalid as China's state owned corporations install bridges in Oakland, and as Starbucks, Apple, KFC, and Cadillac invade China. Meanwhile, Walmart continues to expand into Russia, Russia's Evratz Steel owns Oregon Steel, and 4.3 Billion people in Asia are continuing their push for greater prosperity and political freedoms. With the usual caution flags flying, I believe the global economies are moving towards a new growth cycle, and that our own market's ice is 4 inches thick....except for that spot in the middle.



Van Mason, CFP™, CLU, MBA

An Honored Guest in May

In our January 2012 Quarterly Profit, I discussed our many events for 2012. On May 16th, we are pleased to host a very special speaker at our Friends and Family dinner.

Jeffrey Kleintop, LPL Financial's Executive Vice President and Chief Market Strategist will share LPL's 2012 outlook as well as his updated economic forecast.

Jeffrey Kleintop serves as Executive Vice President and Chief Market Strategist of LPL Financial, where he establishes market forecasts, helps define the tactical allocation used to help manage \$77 billion in assets, and authors several flagship research publications, including weekly market reports and white papers on investment decision making.



As a nationally recognized strategist, Mr. Kleintop is regularly sought after to speak to the national media—including Bloomberg, CNBC, and Fox Business—as well as at financial advisor and financial services industry events. He was featured in the *Wall Street Journal* article "Wall Street's Best and Brightest" and was called "One of Wall Street's best long-term thinkers" by the *New York Times*. Mr. Kleintop is the author of the popular investment book *Market Evolution: How to Profit in Today's Changing Financial Markets*, which was published in 2006.

Prior to joining LPL Financial in 2007, Mr. Kleintop served as chief investment strategist at PNC Financial Services Group for seven years. At PNC, he helped define the asset allocation and portfolio strategy for over \$50 billion in assets under management, served as vice chairman of the investment policy committee, and was co-portfolio manager for \$10 billion advantage portfolios of large-cap growth, value, and core U.S. stocks. Prior to PNC, Mr. Kleintop served as senior investment analyst at Aris Corp of America, where

he was instrumental in founding the registered investment advisor program that grew, within five years, from a small local firm with \$300 million in assets into a regional asset manager with nearly \$2 billion under management.



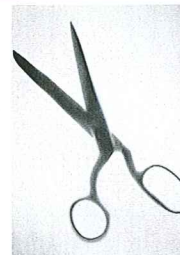
Mr. Kleintop has a Bachelor of Science in business administration and finance from the University of Delaware and an MBA in finance from Pennsylvania State University. He is a Chartered Financial Analyst and is Series 7, 65, 86, and 87 registered.

An invitation with the final details will be mailed as we get closer to the event, but we wanted to make sure you marked your calendars. We would love the opportunity to meet your Friends and Family. Stoneridge is very excited to host this special event and honor our relationships with our clients. Please be our guests...

Amy Treat, Chief Operating Officer/Partner

Rock, Paper, Scissors

Valuations | Technicals | Fundamentals



Making Tactical Asset Allocation Decisions

The optimal way to make investment decisions is to follow a structure that offers the rigidity of a process but the flexibility to identify which factors are the most significant in each unique investment opportunity.

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The Federal Reserve Minutes of 2006

Early in 2012, the minutes of the 2006 Federal Open Market Committee were released. Great praise was heaped upon retiring Fed Chairman Alan Greenspan for his alleged brilliance and magnificent stewardship from 1987 through 2006. The president of the San Francisco Federal Reserve Bank applauded Greenspan as he handed his chairmanship to Ben Bernanke, saying that he was handing over an economic situation similar to a tennis racket with an enlarged sweet spot! At the time, Timothy Geithner was president of the Federal Reserve Bank of New York, and believed that Greenspan's legacy would continue to grow. Then along came 2008. Greenspan's tennis racket turned out to be a caveman's club, and it literally beat the financial stuffing's out of the global economy.

The world has been asking why these financial experts didn't see the 2008 debacle coming. After all, they were immersed in the most extensive and accurate reporting available, and shared the privilege and confidence of the power elite. According to Robert J. Samuelson, writing for the Washington Post, no one saw the crisis coming because there had never been a financial crisis of this magnitude since the Great Depression, and it was literally outside the collective experiences of our financial leaders.

Samuelson suggests that since the early 1960's, U.S. economists have tried to smooth the irregularities of business cycles. By manipulating the cost and flow of money, the Federal Reserve prolonged those periods of relative prosperity, reducing the number of recessions that might otherwise have occurred, and reducing the overall sense of market risk as well. As short term risk was reduced, greater long term risks were taken by the public and private sectors alike. It was generally assumed that a true financial crisis was almost impossible as increasingly complex and highly leveraged programs were thought to insulate the markets from devastating loss. The 2008 debacle was a perfect storm that had been building for several decades. Whether or

not the globe's power brokers will learn from the experience is the trillion dollar question. We should never forget that pirates are genetically inclined to pillage and plunder.

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Monthly Market Monitor

As of March 31, 2012

Employment:

- March saw 120,000 jobs being added; the lower number was mainly a result of a large decline in private-sector retail jobs and the continued contraction of the public sector.
- Both February and January job numbers were revised to 240,000 and 275,000, respectively.
- The unemployment rate fell to 8.2%.

Manufacturing:

- Manufacturing data in February remained mixed but still showed an improvement from January, at least in terms of durable-goods orders.

Housing:

- Real estate data continued to be relatively inconclusive as abnormal weather wreaked havoc on the data, causing most real estate numbers to show better results on a year-over-year basis than on a month-to-month basis.
- The Case-Shiller Home Price Index (seasonally adjusted) for the three months ending in January was flat compared with December, while the year-over-year numbers showed some improvement.
- Month-to-month pending contracts for February were down 0.5% and have now declined for two of the last three months, while year-to-year pending contracts were up a stunning 9.2%.

Retail:

- The International Council of Shopping Centers reported 4.1% year-over-year same-store sales growth in March, matching the gains in February. Warm weather and an earlier Easter helped boost the numbers, with both apparel and department stores showing an improved growth rate.

Reference: RS FUNDS

Rock, Paper, Scissors (continued)

LPL Financial Research believes that fundamental, valuation, and technical factors form the basis of a sound investment decision-making process. However, how they combine and which takes precedence when making an optimal investment decision changes depending on the scenario. The reason is that successful investing does not always follow a basic "rule's based" decision-making framework. Rather, the optimal way to make investment decisions is to follow a structure that offers the rigidity of a process but the flexibility to identify which factors are the most significant in each unique investment opportunity.

In short, a successful investment strategy is a multi-factor, multi-scenario process. In other words, depending on the scenario, factors such as fundamental, valuation, and technicals can either be a significant, insignificant or negative determinant to success. But understanding which combination of factors work in concert under which scenarios requires a sophisticated decision-making structure.

While there are many instances in science, nature, physics, evolution and mathematics of multi-factor, multi-scenario models, perhaps the best known is the game of Rochambeau; otherwise called Rock, Paper,

Scissors ("RPS"). Nearly every one is familiar with the children's game of Rock, Paper, Scissors. The premise of this game is that at the same time, players reveal one of the three hand symbols. Rock trumps (crushes) scissors, scissors trumps (cuts) paper, and paper trumps (covers) rock.

While few think of RPS as a sophisticated framework, the interdependencies of the three factors and the multiple scenario outcomes lead to a complex model for making decisions. For example, compare RPS to a simple version of a "rule's based" framework, such as cards. In cards, the King is always greater than the Queen, regardless of the scenario. It is simply a rule. But in RPS, it is much more sophisticated. Each of the factors can either be a winner, a loser or a non-event, depending on the scenario. For example, a rock wins against scissors, loses to paper, but is insignificant to another rock. There is no one choice that is always optimal. The right answer just depends on the scenario. The same is true in investing. Fundamental, valuation, and technical analysis are all important factors to consider when making portfolio decisions; depending on the scenario, each can be relatively more or less important. This multi-factor,

multi-scenario decision-making framework is highly complex and allows for LPL Financial Research to build optimal strategies by evaluating which combination of factors under which scenarios may offer the best risk/reward tradeoff.

Multi-Factor Decision-Making Process

If RPS is a key element in the disciplines of science, math, and nature, then why not an investment process?

Valuations = Rock
Technicals = Paper
Fundamentals = Scissors

Valuation

Valuation (rock) trumps Fundamentals (scissors) but is trumped by Technicals (paper).

Conclusion: Market participants compete with one another in an environment of imperfect information. No single approach to investing has proven to always be superior. We believe the discipline of Rock Paper Scissors (Valuations, Technicals, and Fundamentals) is the optimal model to maximize the reward/ risk relationship by utilizing a multi-factor, multi-scenario framework.

This research material has been prepared by LPL Financial.



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