

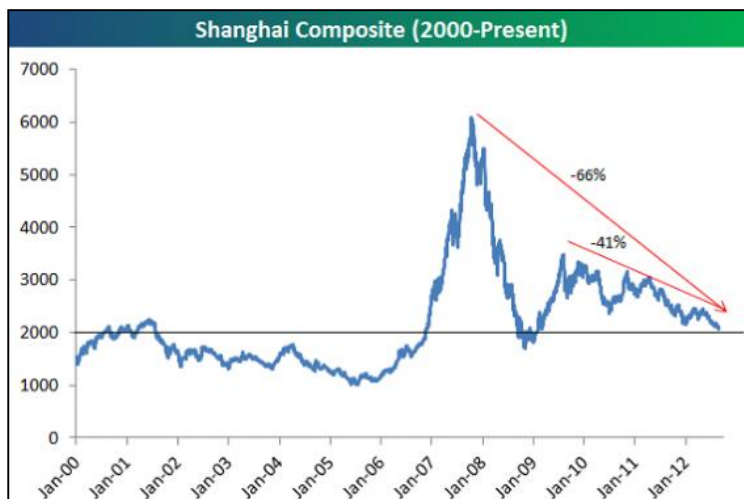
Investment Letter (September 4, 2012)

Market Headwinds

Supported by ongoing government intervention, market (S&P500) returns in 2012 have been solidly favorable, reaching 11.85% as of August 31st. As the summer progressed and the market moved higher, Ackerman Asset Management, LLC (AAM) took steps to protect gains. Positions in small cap, emerging markets and a partial position in the S&P500 were taken off the table (the latter two near range highs). Current equity exposure in the AAM Core Portfolio is approximately 43% (subject to change without notice), which is in addition to the 10% allocation in a multi-asset/alternative asset fund. Taking cautionary action in an investment portfolio may not necessarily lead to immediate outperformance. However, this is the prudent course of action, much like driving at reduced speeds in slippery/hazardous road conditions. Accidents (corrections and bear markets) happen routinely in the market; my goal is to provide you safe travel.

Let's review the major factors that lead to my current cautious positioning:

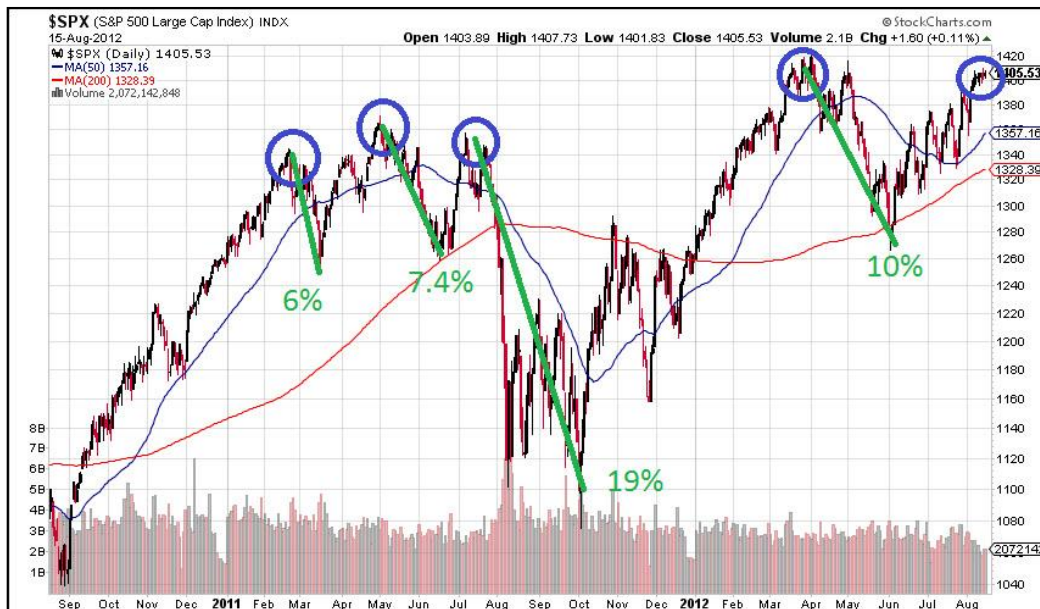
- **World economies are struggling** as highlighted by manufacturing activity reports in Europe and China, which indicate greater slowing than expected in August. Curiously, bad news such as this may actually further support upward movement in the stock market as it keeps alive hopes for fresh stimulus from major central banks. However, should stimulus not occur to the degree or on the timeline hoped for by investors, it could be a catalyst for negative market action. Providing further anecdotal evidence of global slowing are the mid-August comments from Caterpillar CEO Doug Oberhelman, who was quoted in the *Financial Times* saying, "The global economic outlook is more uncertain than at the start of the crisis in late 2008." He also said that it is harder to predict what would happen to the global economy over the coming year than at any other point of his near 40-year career.
- **China has led in the past; it could be leading the way down now.** The Shanghai Composite's sharp decline in October 2007 proved cautionary regarding ensuing global growth. The Shanghai Composite is dramatically underperforming the S&P500 this year and is nearly two-thirds lower than the late-2007 high and about 40% lower than the recovery high from August 2009. (Chart source: Bespoke Investments)



- **The number of stocks recording 52-week highs have declined** suggesting an increasingly narrow market. As the market has advanced during the last two months, a noticeable divergence has emerged; the number of stocks within the S&P500, as well as other major indices, that have claimed new 52-week price highs, has declined. This occurrence signals a potential decay in the strength of the advance. On July 2nd, with the S&P500 at 1374, the number of new 52-week highs within this index peaked at 62. On August 17th, when the index reached 1422, the number of new highs reached only 42 and has since fallen off to 8 as of Friday, or an average of 11 for the week. A strong, healthy advance theoretically should generate an expanding number of stocks that achieve yearly highs. The current situation indicates that fewer stocks are participating in or driving the advance of the index.
- **Major resistance.** The S&P500 finds itself struggling for the last month in the same vicinity as the April 2012 highs, which coincided with the May 2008 highs (circled below). However, a confirmed push above this resistance line would be bullish and may lead to more substantial market gains.



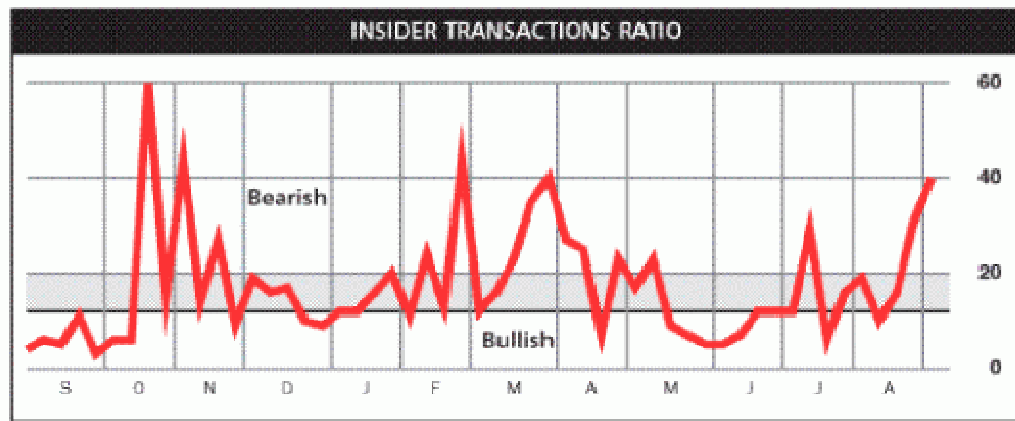
- Volatility Index (VIX).** The VIX, an index which measures implied volatility of the market, is currently in the region of a multi-year low (<15). Typically, heightened VIX values (>30) are associated with investor fear or uncertainty, while values below 20 generally indicate a sense of investor complacency. As can be seen in the two charts below and denoted by the blue circles, a sub-20 VIX reading presented prior to downturns of 6%, 7.4%, 19%, and 10% since the beginning of 2011. A low VIX environment does not necessarily precipitate an immediate market down turn, as investor complacency can persist for extended time periods. Nonetheless, this is a cautionary factor.



Source: Doug Kass, Seabreeze Partners



- **Insider selling is at heightened levels.** As depicted in the chart below (presented in *Barron's*), insider selling has reached its highest level since late March, which coincided with a multi-year high in the S&P500.



Ratio of Insiders Sales to Buys. Readings under 12:1 are Bullish. Those over 20:1 are Bearish.

Source: Thomson Reuters

- **Other factors**
 - **Fiscal Cliff.** According to the Congressional Budget Office, the U.S. economy will slide into a "significant recession" in 2013 if Congress does not avert tax increases and spending cuts set to begin in January. I suspect this major issue is not factored into current market action, but will move to the forefront once the November election has occurred.
 - **Israel/Iran.** The saber-rattling is intense, but market action suggests that investors do not expect preemptive military action by the Israelis in addressing the Iran nuclear situation. Israeli Prime Minister Netanyahu has indicated that Israel needs to take military action prior to the November U.S. election, while the U.S. and other world leaders have stressed a diplomatic approach.
 - **U.S. Election.** Anticipation of the Presidential election will increasingly impact the market as we approach November, particularly if one candidate takes a decisive lead. A Romney win has the potential to be viewed more favorably by investors and would support a stronger market, at least in the short-term. The balance of power in Congress should also play a key role in market behavior surrounding the election. It should be noted however, that the stock market has gained appreciably during President Obama's term, thus the association of a positive market climate strictly with Republicans is somewhat of a fallacy.
 - **Europe.** Hope for a favorable rate decision and/or other monetary action by the European Central Bank (ECB) continues to support markets. On September 3, 2012, Moody's downgraded the outlook of the EU's AAA long-term issuer rating to negative from stable, citing negative outlooks to the AAA sovereign ratings of Germany, France,

the UK and the Netherlands, which combined account for about 45% of the EU's budget revenue.

○ **September Events.**

- September 6th: ECB meeting
- September 7th: U.S. Aug nonfarm payrolls
- September 12th: Federal Open Market Committee (FOMC) meeting
- September 12th: Germany court ruling on bailout fund
- September 12th: Dutch general election

Summary.

The issues identified in this report are provided to elucidate the risks in the market. However, no market is without risks and climbing a ðWall of Worryö is a common market occurrence. The challenge, as always, is to identify the preferable risk/return opportunities and to prudently deploy capital. Although the market, by my assessment, shows some vulnerability at the present time, the longer-term upward trend is currently intact and suggesting higher levels over the next 12 months. As such, I expect to increase the equity allocation in the AAM Core Portfolio upon a pullback or a favorable outcome of certain factors identified in this report. As always, my primary priorities are to: 1) protect client assets, 2) achieve favorable/market competitive returns over the course of a typical 5-7 year market cycle, and 3) manage portfolio volatility.

Thank you for your continued confidence in Ackerman Asset Management. Please feel to call me with any questions or to request a meeting in person.

Kind regards,

Jim Ackerman
09/04/12

** The AAM Core Portfolio is the equity-focused center piece to client portfolios. An individual client's total portfolio may differ from the AAM Core Portfolio due to customization related to legacy positions, fixed income requirements, risk tolerance, size of portfolio, and other client specific reasons.*

*This investment evaluation is directed only to the client for whom the evaluation was performed. The underlying data has been obtained from sources considered to be reliable but its accuracy and completeness cannot be assured. This evaluation is for informational purposes only and is not intended to be an offer, solicitation, or recommendation with respect to the purchase or sale of any security or a recommendation of the services supplied by any money management organization. **Past performance is not a guarantee of future results.***