



* BLUE BELL *

PRIVATE WEALTH MANAGEMENT

2012: A Look Ahead

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You may remember my January 2011 newsletter in which I voiced my concern regarding the lack of fear in the equity markets. The most well known strategists were mostly bullish with only one market prognosticator calling for a slight decline in the S&P500. The average return from the sixteen strategists predicted a gain of 9.02% for the S&P500. We sailed through the first half of 2011 with hardly a worry, seeing market increases of almost 7% from the beginning of the year into July. As expected, S&P earnings were excellent - many companies increased their dividends and investors were calm. This quickly changed in late July as the S&P fell 16.56 % from July 22nd to August 10th. Fear returned quickly, volatility was back with the VIX (a widely used measure of market risk) moving an astonishing 201.89% from 15.95% July 8th to 48% on August 8th. My January 2011 comments stating “investors must be diligent to control their risk, control their emotions, and use some hedging strategies” once again became the mantra of many.

Using this as a backdrop, what can we expect in the coming year? The strategists have become more conservative with their estimates (see chart on page 2). While the strategists are cautiously optimistic, investors still NEED a place to invest. CDs (except for special situations) don't really work; U.S. interest rates are at record lows, presenting substantial principle risk in the future; real estate continues to be depressed; and foreign markets are uncertain. We have elections, the European debt crisis continues, growth appears to be slowing in India and China, with a recession in Europe a strong possibility, Treasury rates are offering less than “true inflation,” and inflation worries persist (the NJ Turnpike and Garden State Parkway just increased tolls 50%+). Increasing energy prices and stressed foreign relations, among other concerns, continue to be areas of uncertainty in 2012. With all of this in mind, it is my feeling that U.S. securities will have a volatile, difficult year but will continue to be the asset class which makes the most sense. My preferred strategies continue to be:

- Option writing (Barron's on 12/30/11 writes “buy/write is the right buy”),
- Investing in closed-end equity funds offering the best discount in the two years,
- Structured investments providing some downside protection and
- Purchasing exchange-traded funds

In summary, 2012 may offer slow but steady economic growth with the domestic equity markets volatile but positive by year end. This assumes of course, that we don't see a total financial collapse in Europe. As always, take a long-term but constantly monitored approach to your investments, and never make decisions on an emotional basis in the short-run.

Projections for the New Year

The following table contains estimates from strategists predicting where the S&P 500 will finish in 2012 and the implied percentage change from the 2011 year end value of 1,257.60

Firm	Strategist	Estimate	%Change
Bank of America	Savita Subramanian	1350	7.35%
Barclays	Barry Knapp	1330	5.76%
Bank of Montreal	Ben Joyce	1,325	5.36%
Citigroup	Tobias Levkovich	1375	9.34%
Credit Suisse	Andrew Garthwaite	1340	6.55%
HSBC	Garry Evans	1,190	-5.38%
Deutsche Bank	Binky Chadha	1500	19.27%
Goldman Sachs	David Kostin	1250	-0.60%
JPMorgan	Thomas Lee	1430	13.71%
Oppenheimer	Brian Belski	1400	11.32%
UBS	Jonathan Golub	1325	5.36%
Morgan Stanley	Adam Parker & Darst	1238	-1.56%
Nomura	Ian Scott	1400	11.32%
S&P Capital IQ	Sam Stovall	1400	11.32%
Wells Fargo	Gina Martin Adams	1360	8.14%
AVERAGE		1347.53	7.15%

Bank of America

- Combined profit by companies in the benchmark equity measure will be \$98.25 a share this year and \$104.50 next year, according to Subramanian, the head of equity and quantitative strategy, in her first equity forecasts since taking over the role from David Bianco in September. "While we expect uncertainty and volatility to remain high well into 2012, the avoidance of a U.S. recession and continued earnings growth could drive the S&P 500 toward the high end of its two-year trading range" of 1,100 to 1,365.

Deutsche Bank

- Binky Chadha, the chief U.S. equity strategist at Deutsche Bank AG, cut his 2012 year-end estimate for the Standard & Poor's 500 Index by 10 percent, saying sovereign debt concerns will rein in market gains.

Goldman Sachs

- "The U.S. economy remains in stagnation," Kostin said. "This fact will limit any significant rally or sustained P/E expansion in the S&P 500 in 2012. The high degree of political uncertainty coupled with downside policy tail risk drives our view that equity investors should focus on the underlying fundamentals and position portfolios for the worst while hoping for the best."

Morgan Stanley

- "Factors arguing in favor of equities include: (i) negative real interest rates and possible further monetary stimulus; (ii) robust S&P 500 profits (+18.9% y-o-y for 1Q2011; 12.1% y-o-y for 2Q2011; +17.9% y-o-y estimated for 3Q2011; and +10.0% y-o-y estimated for 4Q2011); (iii) continued GDP growth in emerging Asia and Latin America; and (iv) a likely soft landing in China (Morgan Stanley continues to estimate real GDP growth of 9.0% in 2011 and 8.4% in 2012)."

...Continued on page 3

Unrealized Gain and Loss Statement Does Not Always Tell the Whole Story

Analyzing the unrealized and realized gain loss statement is rarely an appropriate method to determine performance of an investment or an account. I can't think of an asset class that this proves more true for than Closed-End Funds (CEFs). The reason CEF returns are poorly reflected on unrealized/realized gain loss reports is because of the outsized distributions many CEFs pay.

Take for example the Blackrock Enhanced Capital and Income Fund (CII). If an investor had purchased CII on January 2nd 2009 (the first trading day of the year) at the opening price, they would have paid \$11.31 per share. On December 30th 2011, CII closed at \$12.30 per share an increase in share price of 8.75%. A \$100,000 investment would show an unrealized gain of approximately \$8,753 on the statement. During that same period, if you had purchased SPY, the ETF for the S&P500, you would have paid \$90.44. The closing value on December 30th was \$125.50 or a gain of 38.77%, reflecting a statement gain of approximately \$38,776 on a \$100,000 initial investment. For an investor relying on the unrealized gain/loss statement to determine CII returns, they would assume that SPY performed considerably better than CII; after all a \$38,776 gain is much larger than a \$8,753 gain. While this assumption appears correct it would be wrong. The unrealized gain/loss report does not reflect distributions.

The investor that purchased CII would have received \$5.445 per share in distributions or 48% of the initial price during the holding period. An investor in SPY received \$6.539 per share in distributions or about 7.2% of the initial price. Including distributions the \$100,000 investment in CII would have gained \$56,898.27 through December 30th, vs. \$46,008.49 for SPY, a \$10,889 difference. Not only did CII not under perform SPY as one may have assumed, it actually performed considerably better. We believe poor reflections of CEFs on statements is a contributing factor of inefficient trading/pricing in the CEF market. These are the type of inefficiencies we try to take advantage of. Of the \$56,898.27 of gains from CII, \$48,144.69 were from distributions and would not be reflected on a gain/loss statement.

On the unrealized gain/loss statement it would appear as if CII returned **\$30,022.78** less than SPY

	Initial Investment	01/02/2009 Open	Shares	12/30/2011 Close	12/30/2011 Value	Unrealized Gain/loss	% Gain
CII	100,003.02	11.31	8,842	\$12.30	\$108,756.60	\$8,753.58	8.75%
SPY	100,026.64	90.44	1,106	\$125.50	\$138,803.00	\$38,776.36	38.77%

In reality when total return is used adding back distributions CII actually gained **\$10,889.78** more than SPY

	Initial Investment	Dividends per share	12/30/2011 Value	Unrealized Gain	Distributions	Total Return	% Gain
CII	\$100,003.02	\$5.445	\$108,756.60	\$8,753.58	\$48,144.69	\$56,898.27	56.90%
SPY	\$100,026.64	\$6.539	\$138,803.00	\$38,776.36	\$7,232.13	\$46,008.49	46.00%

Projections for the New Year Continued...

Citigroup

- “The 1,400 projection for the S&P 500 laid out last December appears too optimistic at this juncture,” Levkovich wrote. “While the S&P 500’s potential gains still look quite attractive over the next six and 12 months on our metrics, the investment community may not be as willing to bump up share prices that vigorously.”

Barclays

- Barry Knapp, the New York-based head of U.S. equity strategy, raised his earnings projection for companies in the S&P 500 by \$1 to \$97 a share this year and \$103 a share next year. Stocks will remain in a range for the first half of 2012, with the S&P 500 at 1,150 as of June 30, as investor concern about a recession in Europe weighs on equity valuations.

S&P Capital IQ

- The recommended asset allocation for a moderate investor would be 45% U.S. equities/15% foreign equities/25% bonds and 15% cash. The suggested allocation to bonds is below S&P’s standard 30% exposure, while the cash allocation is up from its normal 10% recommendation.

BBPWM in the News

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“Recent volatility has some trading at a larger discount than usual or a larger discount than is warranted.”

-**Scott Miller, Jr.**, *Wall Street Journal: December 12, 2011*, speaking about the closed-end fund market.

“Why buy structured products instead of options? We do use options and do them ourselves, there are advantages to both structure products and options, many times market conditions dictate what is more advantageous at the time.”

-**Scott Miller, Sr.**, *Bloomberg Brief interview; December 15, 2011*

“Most of my clients would feel that the more money you give to the politicians, the more money they will spend. With that in mind, I think in the short run, people will react negatively to eliminating the deduction.”

- **Scott Miller, Sr.**, *Investment News: October 26, 2011*, speaking about the possible elimination of the mortgage interest deduction on second homes.

REMINDERS

- For 2011, the maximum contribution allowed for both Traditional and Roth IRAs remains at \$5,000 if you are under age 50, or \$6,000 if you are age 50 or older. You have until April 17th, 2012 to make your 2011 contribution. Talk to your children about the benefits of starting an IRA.
- If you mail a check to us, please make the check payable to “Charles Schwab & Co, Inc.” with your IRA account number written on the check along with the year in which the contribution is intended.
- Please contact Scott Jr. or Justin to schedule your account review, 610.825.3540

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