

Nauset Market Commentary Third Quarter 2011

Market Performance Recap: Major Stock Sell-Off Amid European Debt Fears

Stocks were slammed in the third quarter by the euro-zone debt crisis and fears that European weakness could tip the US into recession. Dow Jones Total Market Index fell -15.3% in the quarter, its worst performance since Q4 2008. International stocks were hit even harder, down -19.6% in the MSCI EAFE Index. In fixed income, corporate bond prices were slightly lower, while Treasuries soared, pushing the Barclays Intermed. Gov/Credit Index up +2.4% for the quarter.

Economic & Market Discussion: Inevitable Greek Default: Messy or Orderly?

The US financial markets are currently held captive by the macro events of the euro-zone debt crisis. As we discussed last quarter, this is a crisis of high government debt levels in Greece and other European countries. Despite improving US economic data, investors fear that the consequences of the euro-zone debt issues will spill onto our shores.

We believe that Greece will eventually default on its debt. How that happens will determine much of the impact on the US. While Europe is already very close to recession, the US may avoid that fate if euro-zone policy makers construct an orderly path for Greek debt restructuring. That would restore investor confidence, stabilize European economies and provide a map for other euro-zone countries, such as Spain and Portugal, to possibly restructure as well.

An orderly debt restructuring process must include a recapitalization of the European banking system. The alternative is a messy, chaotic default that would cripple the euro-zone banks, seize up economic activity in Europe and definitely hurt the US. We hope for the best, but are preparing for the worst as this crisis plays out in the coming months.

Given the uncertain environment, we have hedged most portfolios with cash and focused our equity strategy on high quality, defensive dividend stocks. Our fixed income stance is diversified, including use of multi-sector bond investments.

Index	Market Performance			
	% Change for Periods Ended 9/30/2011			
	Third Quarter	2011 Year-to-Date	3-Year Annualized	5-Year Annualized
Dow Jones US Total Mkt.	-15.32	-10.23	0.31	1.75
S&P 500	-13.87	-8.68	1.14	1.23
MSCI EAFE – Non-US	-19.60	-17.18	-12.02	-4.02
BarCap Intermediate Gov't/Credit Bond	2.39	4.92	3.40	7.02
BarCap Municipal Bond	3.81	8.40	3.88	8.08
3-Month T-Bill	0.01	0.07	0.11	0.20