2012: 'Risk On, Risk Off – Repeat Often'

This present day investment phrase will be in vogue throughout 2012, again, as investment markets will vacillate between euphoria and despair or basically a manic-depressive psychological state of mind. Remember when fundamental analysis counted for something? It will again, sometime, but not today.Remember when domestic and international markets were negatively correlated? That was then, today is a whole new paradigm or in plain English, this time it's different. Now that we live in one, big happy world, systemically interconnected everywhere, simply connect the dots and when one market coughs. all markets cough. Case in point, Europe. Finally, remember when politics was a side show? It is now center stage and most often, creates extreme angst for us minions as we try to navigate the challenging economic and investment marketplaces. So, as 2012 unfolds, what should one be aware and beware of..?

Here is my list of hot buttons:

1) Europe

Decades of social and populist government programs are coming home to roost via massive deficits and the elixir to health is too painful for most to stomach. Fiscal austerity is a given, but economic growth is elusive because most Europeans feel entitled to everything under the moon. Go down the list, Ireland, Greece, Malta, Portugal, Spain, Italy, France, Hungary, et. al., know what they must do, but can't bring the message to the masses, for fear of public revolt. The only country that can save Europe and the Euro is Germany. Deutschland Uber Alles. Their painful memories of 1930's-style depression (wheelbarrow of DeutscheMarks for a loaf of bread) is seared into it's collective memory. Thus, Angela Merkel holds all the cards for Euro survival. The EU will survive, but I have my doubts about the common currency. Time will tell, starting with a March deadline for Greek debt. Then Italy, then Portugal… You get the drift.

2) Wisconsin

People Look East, the time is near- The Badger State, our neighbors to the East holds the biggest referendum on the Obama agenda, namely the recall effort against Governor Scott Walker. Why is this happening? Because unions went into a tizzy after the 2010 elections gave Republicans a mandate to improve State finances, due to a gaping budget deficit, courtesy of former Governor Jim Doyle and years of Democratic control. Solutions were proposed, Democrat legislators fled to Illinois (extreme cowardice) to hold up landmark legislation that required a nominal contribution by public union workers for their health insurance and pension, up from ZERO and the result was eliminating the budget deficit, without any accounting gimmicks. Governor Walker should be hailed, not pilloried for leading the march on fiscal sanity. If he is triumphant in not being recalled, look for this to be the template other states will use in closing their budget shortfalls. If he loses, the United States will follow Europe into full blown Socialism, since no one has the guts to implement the financial solutions needed to keep our country great…and solvent.

3) Corporate

Earnings continued to advance solidly and I will posit that many large cap behemoths are beginning to act as their own banks and not get caught up in loan covenants or anything that will impair their ability to change course on a moments notice. Makes sense to me, given the uncertainty in domestic and international markets, increasing regulation and unease about venturing outside each corporations core competencies. Bottom line upside is increased dividends greater liquidity that bonds and many corporations more creditworthy than the US Government. Cash flows matter. To everyone.

4) Supreme Court

Simply put, their decision on Obamacare will weigh supremely on what happens with the elections in November. If upheld, Obama will get re-elected and explode the deficit; If partially rebuked, taxes go higher and Obama gets re-elected; If struck down in total, the deficit is given a temporary reprieve and it's game on for November. Considering the Congressional Budget Office recently scored 9 years of expenses and 10 years of revenues, resulting in a deficit of $ 1.7 trillion, it doesn't take rocket science to figure out what will happen if upheld.

5) Congress

A non-event in this election year. Posturing will be done leading up to November, then the real activity will take place in the last 60 days of the year. Debt ceiling debate re-ignites, revisiting the partial payroll tax forbearance (which accelerates the insolvency of Social Secuirty) ensues and the pleading for higher taxes on the wealthy gains fervor. Maybe a starting point for everybody should be the basic money management concept of only spending what you take in. Get your fiscal house in order first, then come back with plans to spend what you don't have or the adhere to the agreed upon concept of "Paygo". Seems everyone has amnesia when it comes to that tenet.

Heaven knows there are more issues than these four, but these are my major keys. Other notables include Iran, Public Sector Pensions and Public-Sector Budgets (They go hand in hand), the Federal Reserve and Low Interest Rates (They go hand in hand), Housing, Subsidizing Fannie and Freddie (Eliminate) and my sleeper concern, Deflation. Why else would the Fed declare interest rates will stay low through 2014, even in the face of slowly improving economic fundamentals? And improving housing sales? Better unemployment statistics? Japan. The Rising Sun has been setting since the early 1980's and the Fed does not want a repeat here, so they are throwing everything, including the kitchen sink, at our economic problems. Trouble is, most consumers standard of living is decreasing, average housing resale prices are still declining and we have a systemic problem with employment. Just my thoughts but stay tuned…

Crystal ball analysis over, what does it all mean? Equities will grind higher, especially in developed markets (US, specifically) as earnings support the short term, economic euphoria. Read dividend-paying stocks. How long does this last? A majority of 2012, but if earnings slow (margin compression) and debt problems rear their ugly head again, all bets are substantially muted. Stocks should perform better than bonds, simply due to dividends, providing a boost to total return calculations. Real estate, as a hedge against inflation, will do well, especially the residential rental market, as more foreclosures continue. Below grade corporate or junk bonds will do well as investors search for yield and balance sheets can support interest payments. Finally, select preferred stocks (mainly financials) and short-intermediate, general obligation municipal bonds will provide above average and/or tax-free investment income.

Truth be told, the investment process has become more challenging, particularly in a low interest rate environment. The ability to provide above average returns with below average risk (Our goal) is more difficult, but prudent asset allocation and attention to fundamentals will win the race in a very dynamic financial landscape.

All The Best…