BEACON POINTE

ADVISORS

BEACON'S POINT: SLIPPERY WHEN WET

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CONFIDENTIAL – PROPRIETARY

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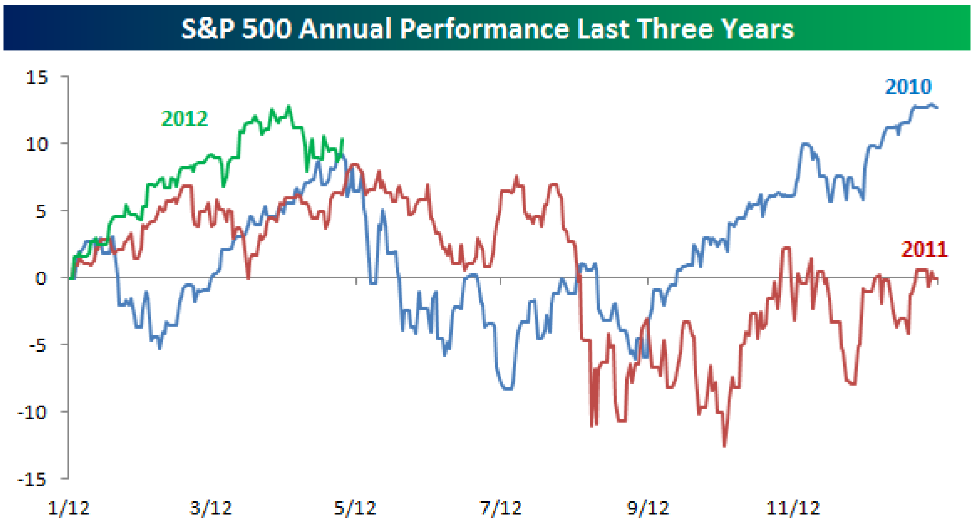
Slippery When Wet

After a thrilling start to the year, April brought about a cooling of sentiment and renewed concerns over the sustainability of global growth, the ultimate resolution to the EuroZone crisis, and geopolitical uncertainty around the world. During the January-March quarter, U.S. equities, represented by the S&P 500 Index, gained over 12%, reaching new post-financial-crisis highs; non-U.S. equities and other risk assets were also strong. Since then, however, financial markets have adopted a decidedly more cautious tone, resulting in a flat-to-slightly down April returns for most major indices. Naturally, investors are wondering if 2012 will play out in a fashion similar to either 2010 or 2011. As shown in the graph below, both years started off with rallies, which were followed by mid-year slowdowns.



In 2010, the S&P 500 was up 9.2% when it reached its first half peak on April 23rd. From there, the index dropped sharply and was down as much as 10% YTD before rallying when the Fed stepped in with QE2. In 2011, we saw a similar pattern. When the S&P 500 reached its first half peak on April 29th, the index was up 8.4% on the year. From there, it was a downward slide as the index fell roughly 20% through October. Then late in the year, the market once again rallied when the summer ended and the Fed stepped in with Operation Twist.

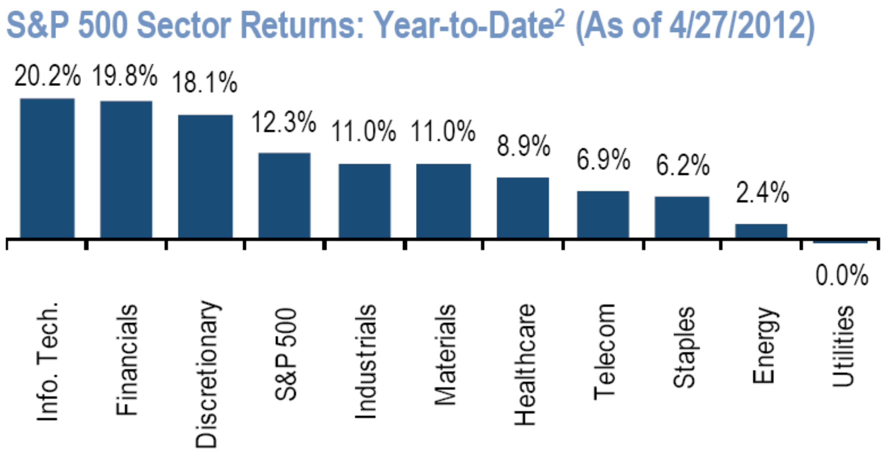
Source: Bespoke Investment Group

Compared to the past two calendar years, present fundamentals have improved in certain areas (global central banks are more accommodative, corporate profits have continued to advance, the impact of the Japanese disasters is now in the past), but many key issues remain unresolved and new obstacles have emerged. On the political front, these include a new socialist President in France, upcoming elections in the U.S., and China's pending power transfer. On the economic front, multiple signs point to deteriorating growth and employment in the EuroZone, with more austerity measures still to come. In addition, debate is underway about what should be done to offset the impact of the "fiscal cliff" facing the domestic economy at the start of 2013. Analyzing the current environment is as challenging as ever. In discussing the U.S. economy, for example, one prognosticator stated that there are multiple, and often divergent, forces at work and concluded that:

> "Our current expansion contains a mixture of a cyclical recovery and structural issues that are yet to be resolved and are not addressed by economic growth alone. **Hard realities require hard decisions ahead**."

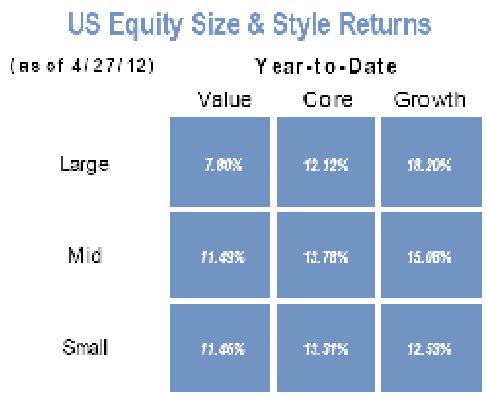
Source: Wells Fargo Economics Group

Despite the April pause, most economic sectors are still holding onto healthy year-to-date gains, as shown in the bar chart below. The leadership, however, has been rather narrow. Only three sectors in the S&P 500 -- Information Technology, Financials, and Consumer Discretionary -- outperformed the total index. The remaining seven economic sectors trailed the index, with one of them -- Utilities -- falling into negative territory. The difference between the best and worst performing sector is over 2,000 basis points. Defensive areas of the market, which had held up significantly better in 2011's correction, have so far trailed their more cyclical counterparts, although this trend reversed again in the month of April.



Source: Goldman Sachs Asset Management

In addition to the large differences between sector returns, year-to-date results also show a noteworthy outperformance of Growth stocks over Value stocks, especially in the large cap space. While Large Cap Growth increased over 18% through April 27th, Large Cap Value in aggregate advanced less than 8%.



US Equity Size & Style Returns

(as of 4/27/12)	Year-to-Date		
	Value	Core	Growth
Large	7.80%	12.12%	18.20%
Mid	11.49%	13.78%	15.06%
Small	11.46%	13.31%	12.53%

Source: Goldman Sachs Asset Management

A major driver behind the strength of the Information Technology sector, the Growth style benchmarks, and even the broader S&P 500 Index has been the performance of one stock, Apple. Now the largest company in the world by market capitalization, it represents 4.4% of the S&P 500 Index, 7.6% of the Russell 1000 Growth Index, and an even larger percentage of the tech-heavy NASDAQ Index. As of April 30th, 2012, Apple's stock has gained 40% in the year-to-date period, 61% in the trailing 1-year period, 344% in the trailing 3-year period, and 461% in the trailing 5-year period, which incidentally included the severe 2008-2009 bear market. Within the Russell 1000 Growth Index, Apple accounts for a fifth of the large growth benchmark's 1Q2012 return, a third of its trailing one-year return, and a significant portion of its trailing 3- and 5-year returns. According to Morningstar, ***"Apple has been among the biggest factors explaining the difference between top- and bottom-performing large blend and large growth funds for the year-to-date, as well as the trailing 12-month and trailing three-year periods."*** In both categories, the funds with the highest returns had, on average, significantly more exposure to Apple that the funds with the lowest returns. The Morningstar data supporting this conclusion is summarized in the following table:

Bobbing for Apples: Apple explains much of the difference between top- and bottom-performing large-cap funds

	Top Quartile YTD	Bottom Quartile YTD	Top Quartile 1 yr	Bottom Quartile 1 yr	Top Quartile 3 yr	Bottom Quartile 3 yr
Large Growth						
% Assets in Apple	7.8	2.8	6.9	4.3	7.2	4.2
Large Blend						
% Assets in Apple	3.2	0.84	3.1	0.98	2.9	1.6

*Data as of 4/23/12

Source: Morningstar Analysts

Of course, the future direction of Apple's stock price is uncertain. Some of Beacon Pointe's recommended managers own shares in the company and others do not, because of either an investment criteria mismatch or insufficiently attractive valuation. The impact of Apple's performance on recent broad market returns, however, is not lost on either group. It is an interesting phenomenon and we will keep an eye on it.

Mohamed El-Erian, PIMCO's CEO and co-Chief Investment Officer, recently spoke at the Altegris/Mauldin Strategic Investment Conference in front of 500 industry professionals. One of his concluding recommendations was to acknowledge the present state of the world and the need to think differently. He stated that it is dangerous to anchor one's expectations in the performance of benchmarks, because they are backward-looking. Instead, investors need to take an active approach with a forward-looking frame of mind. Restrictive guidelines only limit the ability to protect capital and/or take advantage of opportunities. Finally, he reminded the audience that for every risk, there is an opportunity.

Beacon Pointe shares Mr. El-Erian's views and believes that opportunities are present in both equity and fixed income markets. However, we also recognize that we live in "unusually uncertain times", to borrow a phrase from Fed Chairman Ben Bernanke. Because the road ahead gets slippery when wet, we continue to believe that diversification and careful manager selection are of paramount importance. Diversification has been aptly compared to a seat belt: its benefits only become obvious in case of an accident, yet one must wear it all the time. When guiding our clients in devising an investment plan, we recommend diversification among asset classes (i.e. equities, fixed income, and – where appropriate – alternatives) as well as investment styles (i.e. value vs. growth, large cap vs. small cap, domestic vs. international) to create the most attractive risk/return profile for the aggregate portfolio. And finally, the investment managers we recommend to our clients share a focus on strong fundamental research, a margin-of-safety valuation discipline, and a long-term investment horizon with an emphasis on capital preservation. We strongly believe that these are the cornerstones of successful investing and that they will serve Beacon Pointe's clients well in today's increasingly complex market environment.

Please feel free to call Beacon Pointe at 949-718-1600 should you need additional information or have any questions.