Strategy Snapshot
Fourth Quarter 2011

"You Can Go Home Again"

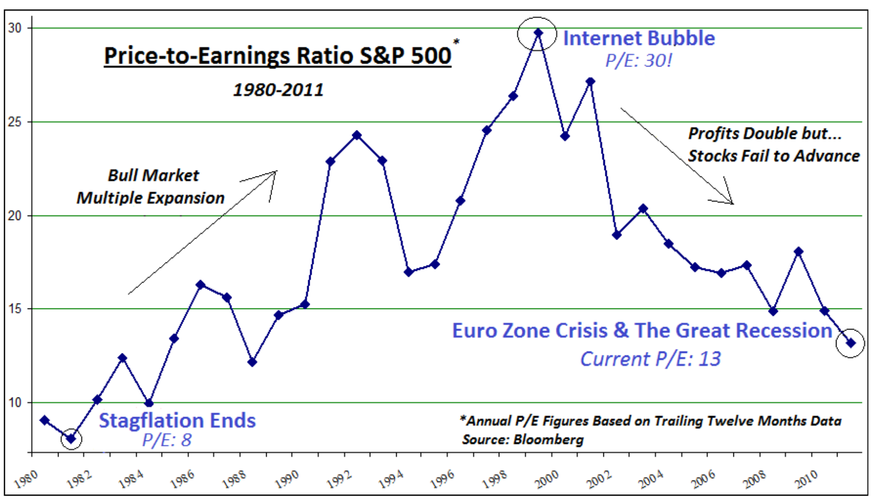
In previous editions of the *Strategy Snapshot,* we ventured abroad to discuss the role of developing economies and the emerging consumer within the global capital market system. As the New Year approaches, we return home to find value, opportunity and even a degree of comfort in what remains an uncertain world.

The psychology of the market swings like a pendulum across market cycles. Optimism and fear engage in a perpetual struggle to capture the hearts and minds of stock market participants. On occasion, a clear winner emerges and share prices move to extremes. Successful investors approach these moments with a skeptical eye, a contrarian attitude and a willingness to endure short-term bouts of volatility in pursuit of longer-term goals.

The "New Economy" of the 1990s brought with it the myth of a new paradigm in the global markets, a golden age of productivity that would all but ensure perpetual growth unfettered by pesky historical norms like economic cycles, inflation or unemployment. The stock market was assigned an unreasonable and ultimately unsustainable valuation as the exuberance of the era infected investor psyche. The pendulum now has swung towards the other extreme as the volatility and anemic returns of the recent past have shaken the confidence of equity investors.

To be sure, serious global issues confront stock market participants. The euro zone is struggling to solve difficult fiscal challenges, as is the United States for that matter. Social unrest is percolating with government leadership fragmented, while the global economy, including China, is slowing. With memories of the 2008 crisis fresh in their minds, investors are understandably wary of risk and are shunning stocks in favor of assets they believe are safer. Aided by a media complex that sells fear and sensationalism, investors have become conditioned to look around the corner for the next crisis. For an investor to be successful in uncertain times, however, the problems of the day must be taken within the context of the market moment with an eye on longer-term goals. Specifically, to what extent have current stock prices properly discounted an uncertain future?

The U.S. stock market has spent the better part of the past thirteen years paying for the technology inspired greed of the late 1990s and a decades-long global borrowing binge that is just beginning to unwind. Over this period, corporate earnings have more than doubled, but the stock market has failed to advance. Investors, scarred by unpredictable market swings, have stubbornly refused to pay a premium, or even a fair value in some cases, for the strong performance of American companies. And who could blame them? The result has been a market that has gotten much less expensive in recent years as seen in the price-to-earnings graph for the S&P 500.



It is tempting to ring the bell and say that stocks are on sale. They are not. We will repeat this point as it is critical. **The market is not cheap.** Yes, prices relative to earnings are well below the historical average, but the macroeconomic headwinds outlined earlier lead our team to the conclusion that stocks are fairly valued at today's levels. As we saw during recent rallies, however, valuation is beginning to provide a margin of safety that instills confidence in would-be buyers as they step in during periods of market weakness. This type of price action based on company fundamentals may be the start of a healing phase that allows investors to return to stocks with more conviction over time. A foundation is being built for a sustainable move higher in the years ahead. And, while the timing of meaningful market reversals is notoriously difficult to predict, the long-term message is clear. In the words of Warren Buffet, "Be fearful when others are greedy and greedy when others are fearful."

STRATEGIC
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Portfolio Strategy: *Income and Sustainable Growth*

The deleveraging cycle in the developed markets will be with us for the foreseeable future. There is simply too much global debt, and we will spend years getting our collective balance sheets back in order. Nevertheless, persistent investors can capitalize on the opportunities offered by this period of unusual uncertainty and potential value, as long as they maintain the proper respect for risk within a well-diversified portfolio.

The single most important determinant of a stock's long-term performance is share price in relation to a company's intrinsic value. It is under this axiom that Strategic is finding opportunity in selected segments of the market. A repeatable, disciplined process focused on fundamentals and mindful of the big picture will lead investors to high-quality stocks that can thrive in an uncertain environment. At Strategic, we prefer attractively valued companies, led by solid management, that can extend sustainable competitive advantages over the long-term while returning cash to shareholders now. Defendable business models, pricing power, balance sheet strength, stable or growing earnings, and ample free cash flow are among the metrics that we consider for our individual stock strategies.

Company Spotlight I: *Colgate-Palmolive*

We added to a core position in Colgate-Palmolive (CL). A familiar name to Strategic investors, Colgate is a leading consumer products company with dominant market positions in four global businesses: oral care, personal care, home care and pet nutrition. For readers interested in a "stock tip", Colgate is admittedly a bit mundane. However, in a world where consistency and reliability are in short supply, the investment of client capital in a firm that demonstrates a superior growth profile, attractive emerging market exposure, earnings visibility and a healthy dividend is a prudent decision in our opinion.

Company Spotlight II: *Oracle*

ORACLE

Oracle's (ORCL) share price has come under pressure recently due to a lack of visibility in corporate spending plans. We view the sell-off as an opportunity to build a long-term position in a leading worldwide provider of business software and hardware systems. Operating in over 145 countries and in partnership with over 380,000 customers, Oracle's integrated portfolio of solutions is the industry standard. We see numerous catalysts for growth in the coming years, including the move to a cloud based delivery system and an applications upgrade cycle. A $17 billion net cash balance supports an accelerating share buyback program, a modest dividend, a robust research & development program and strategic acquisitions.

Firm Update: *New Team Members*

We are pleased to have welcomed several exceptional professionals to the Strategic investment team in 2011.

Aaron Evans returned home to Upstate NY from Boston, MA to join Strategic as an equity research analyst and financial planning associate. Prior to Strategic, Aaron was an engineer for Lockheed Martin where he designed defense solutions for the United States Armed Forces. He holds an MBA in Finance and a BS in Electrical and Computer Engineering, both degrees from the University of Rochester. Currently, Aaron is studying for Level II of the CFA program.

Other recent additions to the team include David Lemire, CFA and Robert Hanft. Dave, the former president of the Investment Advisory Division at Adirondack Financial Services, joined the firm in September as a managing director and senior market strategist. Bob, the former chief operating officer of the Global Equities Group at JP Morgan in Manhattan, joined Strategic in October as a company adviser and member of the investment committee.

As always, please contact any of us here at Strategic with comments or if we can be of service to you.

Thank you and Happy New Year!

Alan

Alan R. Leist, III, CFA

Strategic Financial Services, founded in 1979, is an independent investment firm currently managing and advising clients on assets in excess of $750 million. Strategic has offices in Syracuse NY, Utica NY and West Palm Beach FL.

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