Investment Update

April 2012

MIDDLETON & COMPANY, INC.

2012 First Quarter Update

Review:

Equity markets responded strongly to the resolution of the latest installment of the ongoing Greek debt crisis and positive economic data from the US, rallying 12.6% in the quarter. With this gain, the market ended at the highest level since June of 2008, just prior to the financial crisis. Bonds had a weak quarter. The Barclays Aggregate U. S. Bond Index was up marginally, 0.3% in the quarter.

Quarters	***1Q12***	***4Q11***	***3Q11***	***2Q11***	***1Q11***
S&P 500	***12.6%***	***11.9%***	***-13.9%***	***0.1%***	***5.9%***
Barclays U.S. Aggregate Bond	***0.3%***	***1.1%***	***3.8%***	***2.3%***	***0.4%***

Domestic Economy:

Aided by an unusually mild winter, the economy continued on an upward path. Weekly unemployment claims are now consistently in the 350,000 range, down from more than 400,000 a year ago. Job creation has also improved. In the first two months, 470,000 new jobs were created, compared to 228,000 in the same period last year. Consumers are clearly feeling more confident as demonstrated by the figures: retail sales were up 6% in the first two months of the year and auto sales were up 12% compared to the same period a year ago.

Business surveys continue to find companies expanding. Corporate profits ended 2011 at an all-time high. Businesses are in excellent financial shape and able to fund growth plans.

International Economies:

The international economic picture is more benign than three months ago, as the Greek debt crisis has been averted for now. We expect Europe to experience a shallow recession, ending in the second half of this year. The growth expectations for emerging economies have been marginally reduced as exports to Europe have slowed and monetary policy has been tightened to wring out speculative excesses in China. On the other hand, wages in China have increased rapidly, leading to more consumer spending, offsetting slower exports.

While the prospects are good, there are several concerns:

- **Energy prices**: The mild winter and low natural gas prices have helped consumers. In contrast, gasoline is up 24% since the beginning of the year, pushed by speculation and concerns about the Middle East. Higher prices would clearly hurt consumer spending. However, the chance of disruption by Iran has diminished somewhat and inventories are high. Therefore, we believe that energy prices are near their highs for the year and will settle back by late summer.
- **Europe**: The European debt crisis has pushed the Eurozone into recession, which could have spillover effects on us. At present, it appears the recession will be mild. The two largest economies, Germany and France, seem to be weathering the problems well. In Germany, unemployment is at a ten-year low based on strong exports. Spain and Italy still face difficult adjustments to reduce debt, and the Greek crisis is still not completely resolved. Nevertheless, the potential for future shocks has been significantly reduced by the recent EU action to increase the backup funds to 900 billion euros.
- **Fiscal drag**: Unless Congress acts, the expiration of the Bush-era tax cuts, the 2% reduction in Social Security taxes, and added spending cuts agreed to in the debt ceiling bill will subtract almost 3% from GDP growth next year. Nothing will happen until after the election. However, depending on the outcome of the election, we expect Congress to either moderate or eliminate the tax increases. Spending cuts (especially Defense) are likely to be adjusted. The net result will likely mitigate the drag to a manageable 1.0-1.5%.

Strategy:

In our view, the U.S. stock market is attractive based on better than expected economic growth and a reasonable valuation. We are emphasizing domestic, economically sensitive stocks that can benefit from the broadening recovery of the U.S. economy. Accordingly we have significant weightings in consumer discretionary, industrials and technology stocks.

The U.S. has the best prospects among developed economies. Emerging economies appear to be downshifting to a lower, but still healthy pace of growth. We are, therefore, becoming more selective with our emerging economy investments.

Bonds appear over-valued. Even with current moderate inflation, ten-year or less government bonds have a negative real return. As the economic expansion continues and the Fed begins to remove liquidity, we believe that bond prices will decline, making bonds less attractive than stocks. Our bond portfolios remain defensively positioned.