Investment Update

October 2011

MIDDLETON & COMPANY, INC.

## 2011 Third Quarter Update

### Review:

During the quarter, stocks exhibited unusual volatility as the debt ceiling debate in Congress and potential default by Greece weighed on investor confidence. The S&P 500 finished down sharply, losing nearly 14%. Bonds, especially Treasuries, rallied strongly as investors sought safe havens. The Barclays Aggregate Bond Index was up 4.7% for the quarter.

| ***Quarters*** | ***3Q11*** | ***2Q11*** | ***1Q11*** | ***4Q10*** | ***3Q10*** |
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| ***S&P 500*** | ***-13.8%*** | ***0.1%*** | ***5.9%*** | ***10.8%*** | ***11.3%*** |
| ***Barclays U.S. Aggregate Bond*** | ***4.7%*** | ***2.3%*** | ***0.4%*** | ***-1.3%*** | ***2.5%*** |

### Domestic Economy:

The economy has exhibited a remarkable resilience in the face of the on-going conflict over budgets and the deficit in Washington and the negative news regarding the European sovereign debt crisis. The economy is certainly not booming, but neither is it sliding into a recession, as many analysts predicted. Consumer spending has continued to increase modestly. Auto sales are running 8% ahead of last year, despite some continued shortages of Japanese cars due to the earthquake. Capital investment by businesses was up 10% in the most recent report. Exports are exceeding pre-recession levels.

We believe there are several reasons for the resilience of the economy. There seems to be “headline fatigue”. Consumers are not changing their spending plans based on the news. There are sectors of the economy that are experiencing strength. Agriculture in the Midwest is booming, as global demand for food remains robust. The energy-producing states are benefiting from high energy prices.

Many businesses are reporting a continued gradual recovery in activity. Corporations have been very disciplined about adding costs and are producing good profits. They are benefiting from strong export business.

In summary, we expect GDP growth to be a very modest 1.5-2.0% in 2011.

## International Economies:

International economies are mixed, with the major developed economies nearly flat. Europe will experience little growth as it deals with the sovereign debt crisis. Japan will be flat or down slightly as they struggle to recover from the earthquake and tsunami. Emerging economies are expected to grow at healthy rates, although somewhat slower than in the past year.

## Financial Markets:

Markets around the world have experienced a period of high volatility, reacting to the Eurozone debt crisis and the political stalemate in Washington. Stock markets fell, while government bonds rose as investors fled to safe havens. The factors are in place to reverse the trend in the months ahead: Legislators in Washington have passed funding resolutions for the fiscal year that began on October 1st with less rancor than was displayed during the debt ceiling negotiations in August. The Eurozone shows signs of dealing decisively with the sovereign debt problem with a plan analogous to the bank bailout plan employed by the US in 2008-9. Stock market valuations are attractive based on modest growth assumptions. The S&P 500 is trading at less than 12x the 2012 earnings estimate. Notably, at 2.4%, the dividend yield on the S&P 500 exceeds the 2.0% yield on a ten-year US Treasury bond.

## Strategy:

We think economic growth will continue in the fourth quarter of the year. The latest estimates for the S&P 500 are for 12% growth in earnings this year, with a further 8-9% growth expected in 2012, providing a favorable environment for stocks. U.S. bond rates are at thirty-year lows, making fixed income unattractive. Stocks should provide significantly better returns than bonds or cash. We favor economically sensitive stocks, such as industrials and technology which should continue to benefit from efforts to improve productivity and participate in the growth of emerging economies.