Fagan Financial Report

Registered Investment Advisors

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TO OUR CLIENTS

By any measure, the first calendar quarter concluded with robust equity returns as well as positive results for fixed income investors as the U.S. Economy continued to push forward at a relatively modest pace. For those that follow the regular commentary we post on our website at faganasset.com you read on March 29th our belief that "after the spectacular first quarter investors in the U.S. stock market have experienced, we would expect a bit of profit taking at the beginning of the second quarter as investors will begin to worry about a slowing corporate earnings outlook as well as the upcoming Payroll Report…. However, at this time we believe that any selloff will be shallow (five percent or less) and therefore buyable. Regarding fixed income, keep your average maturities less than ten years and look for opportunities in corporates, government agencies and high yielding corporates. It is late in the game in the bond bull market and thus, caution is the better part of valor."

As noted above, if history is any guide, the recovery that the United States is currently experiencing has been modest at best. As a rule of thumb, the deeper and longer a recession, the more robust and lengthier will be the ensuing recovery – and make no mistake about it, the last recession was deep as compared to historical standards as well as quite lengthy. In fact, during the recovery there are usually several quarters of annualized economic growth in excess of six percent. However, since the U.S. Economy officially exited the recession after the third quarter of 2009, over the following six quarters growth has not once exceeded six percent. For that matter, the fastest rate of growth for that time period has been only 3.9% which occurred during Q2-2010.

In our opinion, the prime culprits for the middling economic growth are the build-up of credit between calendar years 1993-2008; weak recoveries in the housing and labor markets and over-regulation of the financial services industry.

Despite the above, there is reason to be somewhat optimistic. Americans have begun to work down their overhang of debt, specifically credit cards as well as other revolving loans thereby boosting their purchasing power. In addition, the housing market and labor markets, although not robust by any stretch of the imagination, have at least stabilized. And finally, corporations have begun to deal with the myriad of this new, onerous regulatory environment.

Regarding those issues negatively impacting the recovery noted above, three individuals, Chairman of the Federal Reserve, Ben Bernanke; Vice-chair of the Federal Reserve, Janet L. Yellen and the President and Chief Executive Office of the Federal Reserve Bank of New York, William C. Dudley, recently delivered pertinent speeches.

Describing the current status of the labor market as well her outlook for it, Vice-Chair Yellen noted that "there have been encouraging signs of improvement in recent months. The unemployment rate had hovered around 9 percent for much of last year but moved down in the fall and averaged 8¼ percent in the first three months of this year, about 1¾ percentage points lower than its peak during the recession."

One day after Vice-Chair Janet Yellen made somewhat positive comments concerning the direction of the labor market, President Dudley outlined the case for a relatively buoyant consumer, stating that "the incoming data on the U.S. economy generally has been a bit more upbeat over the past few months, suggesting that the recovery may be finally establishing a somewhat firmer footing. Real GDP expanded at a 3.0 percent annual rate in the fourth quarter of 2011, the fastest growth since the first half of 2010."

Although we may be hitting something of an economic soft patch resulting in some profit-taking in the stock market. At this time, we believe it will be relatively shallow and provide an attractive entry point for long-term investors.

TEN STEP PROGRAM TO NAVIGATE THESE TURBULTEN INVESTMENT WATERS

Just as it pays to establish an escape route from your home in case of a fire, it pays to establish a disciplined plan of action pertaining to your investments, all the while keeping in mind that panic is not a strategy. It is with this in mind that we thought it was timely to provide a ten step program that might help you navigate these turbulent investment waters.

Step number one. Assess your current financial situation. Items to include - your income, perceived job security, details of your pension plan, projected Social Security benefits, insurances (life, health, disability, property and casualty), real estate values, mortgage information and other debt.

Step number two. Get an historical perspective on this period in history. Is it really different this time or are we in a phase in our history that will pass? Keep in mind that the stock market generally moves up over a twelve to twenty year period with mini bulls and bears contained within and then moves sideways over the next period with mini bulls and bears in between. We believe that until further notice, we are obviously in a sideways moving period and have been so since early 2000.

Step number three. Given the above, begin to determine your appropriate asset allocation. Some rules of thumb include the older you are, the more fixed income (bonds) you should include in your portfolio. The more guaranteed your pension plan, the closer you are to realizing the benefits of that plan, and to what extent that pension plan along with Social Security will meet your income needs during retirement, the more equities (stocks) one should include in their portfolio. The more prone you are to making emotional investment decisions, the more you should include fixed income investments. Keep in mind that the opposites of the above also hold true and that we are speaking in generalizations only.

Step number four. Sell the peripheral holdings. Get out of investments you don't understand or investments that contain volatility that exceeds your temperament. These may include but are not limited to emerging market funds, aggressive growth funds, non-investment grade (junk) bonds, and small cap stocks. Sell so that you can sleep at night.

Step number five. Hold some cash. Depending upon your situation, we believe that anywhere from zero to twenty-five percent of your account is appropriate. Too little and you may sell in panic. Too much and you are not moving toward your long-term goals.

Step number six. Buy some dividend paying stocks. Do you realize that the ten-year U.S. Treasury Note yields only 2.10% and that Proctor and Gamble stock yields over 3.40%? Moreover, interest rates are at or near a fifty year low and P&G has not only paid, but increased its dividend every year for the past fifty-three years. With this in mind and assuming that P&G does NOT increase or decrease their dividend over the next ten years, should the stock decline thirty percent over this time frame you will still make a little money. A pool of these stocks sounds like a better alternative for long-term investors than money sitting at zero percent in a bank account.

Step number seven. Recognize that too many investors have their fingers on the sell trigger and too many investors have guns in the form of their computers. Try to determine if perhaps you are one of those individuals that does not have the temperament or time to invest on your own. There is an old adage that says, "just because you can afford the ticket doesn't mean you can fly the plane." Simply put, yes, it is your money, but perhaps your time, talent and temperament are better spent elsewhere.

Step number eight. Be disciplined. Don't chase the stock market on up days thinking that you have missed the boat. There will be many more boats to come around. The volatility will continue. Be patient and let the stock market come to you. What a novel idea, buying on the down days.

Step number nine. Gain some perspective. We're both around fifty. If statistics hold true, that means we have only about thirty more Summers to enjoy. All that you can do is do your best and work toward reaching your goals. It is kind of like dieting and exercising, it is your best shot, but doesn't promise anything.

Step number ten. Become an investor, not a day trader. The media wants you to act, act, act, by always yelling fire in a crowded room. Think of the preceding nine steps to gain perspective. Buy low, sell high. Sounds easy but is rarely accomplished by the retail crowd because they are often scared out of their investments at the wrong time. If history is any guide whatsoever, this is truly what will prevent you from reaching your goals.

23 Years Serving the Investors of the Capital Region

FACEBOOK – IT'S ALL ABOUT VALUATION

Ever since word spread that Facebook was filing to become a publicly traded company, we have been receiving many requests soliciting our opinion. Given the fact that it will be three to four months prior to Facebook trading, it would be premature to weigh in with an opinion. Many questions still remain. However, there are some known facts that we will weigh in on. They include.

According to the Registration Statement (Form S-1) filed with the Securities and Exchange Commission, Facebook had 845 million Monthly Active Users (MAU) as of December 31, 2011 as compared to 608 million MAU one year prior for an increase of 39%.

Facebook had 483 million Daily Active Users (DAU) as of December 31, 2011 as compared to 327 million DAU one year prior for an increase of 48%.

Facebook had more than 425 million MAU who used mobile devices as of December 2011 an area of their business that is one of the fastest growing.

Facebook users generated an average of 2.7 billion Likes and Comments per day during the three months ended December 31, 2011 and uploaded more than 250 million photos per day.

Revenue at Facebook increased by 88% to $3.711 billion during calendar year 2011 from $1.974 billion one year prior and by 2,325% from $153 billion during calendar year 2007.

Expenses at Facebook increased by 98% to $2.711 billion during calendar year 2011 from $1.368 billion one year prior and by 831% from $291 billion during calendar year 2007.

facebook

The net result when comparing revenue increases at Facebook relative to increases in expenses is a profit margin of approximately 27%, slowing from prior years but nonetheless healthy by most standards.

Approximately 12% of the revenue Facebook generated during calendar year 2011 was from its' relationship with gamemaker Zynga (ZNGA). This revenue is from direct advertisements purchased by Zynga as well as sales of their virtual games.

Facebook shares currently trade in a private market for approximately $30 per share, which would imply a market capitalization of approximately $75 billion, more than the Walt Disney Company, General Motors and Nike.

Should Facebook come public at a market capitalization of $75 billion, it will therefore be trading at nearly 19 times revenue, this as compared to Apple and Google, which trade at approximately five times revenue.

When Facebook becomes public, co-founder Mark Zuckerberg will maintain his iron grip on the company with a 28.4% outright ownership and 57.0% of the voting rights.

Rather than bore you to death with more data, let's just take a wait-and-see attitude regarding our opinion on whether or not the shares are worth purchasing. It has yet to be determined how many shares Facebook will ultimately issue and at what the issue price will be. Keep in mind that if this Initial Public Offering is like the vast majority of others, nearly 90% of the shares will be taken by large institutions and insiders with the general public getting the balance. Demand will certainly exceed supply so the first trade will most likely be WAY above the initial public offering price.

We will keep an eye on this popular Initial Public Offering as its trading debut nears.

CORPORATE EARNINGS SEASON ABOUT TO KICK OFF

As we prepare to enter first quarter earnings season, we have assembled some strategies for dealing with the volatility which is sure to accompany these corporate reports.

You either have faith in the benefits of investing or you do not. Changes in the value of your portfolio should not alter that faith. It is not ironic that market downturns challenge this assumption. The news media jumps on stories of lost wealth and investors tend to get caught up in those stories. However, keep in mind that despite the horrific bear market experienced during 2008, the stock market is within ten percent of its all-time high. You either believe in the fairness and longer-term opportunities of investing or you do not. If you think the playing field is stacked against you, get out now as stocks have doubled over the past three years.

Going about our daily business of financial planning and managing money, we are quite often asked the question "how often should I review my account." To that we respond, "how often should you shovel your driveway in the winter or water your lawn during the summer." More specifically, the answer is whenever it needs it. When you have a change in your life, be it marriage, a new baby, a change in jobs, retirement or the death of a spouse, review your financial situation. When the stock market is volatile, has lost more than ten percent or for that matter gained more than ten percent, review your financial situation.

Investing is not a static environment. You shouldn't review your portfolio merely on a quarterly basis. The stock market does not experience volatility merely because it is the end of a quarter. Review your portfolio as the values change or as noted above, as you experience changes in your life.

Have a plan to deal with the potential for a negative short-term outcome in a specific investment you have made or perhaps a downdraft in the overall stock market. By nature people are optimistic. We like to think good things will happen to all of our investments. However, as you know, that is not always the case. So have a plan for dealing with a negative outcome. Panic is not a strategy. Assess your situation and develop a sell discipline.

Don't fight the last battle or the ghosts of 2008. Investors have a tendency to miss opportunities because they remain afraid of a similar bear market like the one a few years ago. Allocate your investments according to your objectives and then as noted above closely monitor that allocation. That is your best chance of success. Otherwise, you'll be getting 0% to 1% in the bank which also puts your retirement plan and/or retirement income at risk.

There is not problem holding some cash. If you are a bit skittish, a bit conservative or need a level of comfort, keep ten to twenty-five percent of your investment portfolio (this excludes your vacation, rainy day, short-term money) in cash. You'll sleep better at night and who knows, you might be able to put this cash to work at lower market levels.

Establish a well-designed financial and investment plan. Then, monitor, evaluate and, as necessary, make changes to that plan along the way. This seems logical and simple. However, when fear of monetary loss and emotions get in the way, watch out. That is a certain recipe for buying high and selling low! Avoid this by sticking to your plan and being disciplined.

FIVE FINANCIAL TENETS TO LIVE BY

1. Dollar Cost Averaging Into Your 401(k) Works, It's Just Not Exciting
2. Don't swing for the fences. Solid portfolios are built on a couple of solid hits not a blast. Over the years we have seen a lot of money destroyed with speculative shots.
3. Be consistent. – If you aren't a risk taker, don't begin after big market rallies and if you are an aggressive investor, don't become a wallflower during times like last August.
4. Zigging and "sagging." There is this romantic picture of daytrading.
5. Emotional investing is losing investing.

Largest Holdings Regardless of Asset Class Ranked by Market Value as of March 31st, 2012.					
Percent of Total Assets Managed	*Company Name*	*Symbol*	*As of Mar 31st, 2012*	*As of Feb 29th, 2012*	*As of Jan 31st, 2012*
11.69%	Cash & Equivalents		1	1	1
5.72%	Payden GNMA Fund	PYGNX	2	2	2
3.96%	Apple Computer	AAPL	3	3	4
2.96%	SPDR Dividend ETF	SDY	4	4	3
2.71%	Loomis Sayles Bond Fund	LSBRX	5	5	5
1.95%	Conoco Phillips	COP	6	6	8
1.91%	Nike, Inc.	NKE	7	7	7
1.80%	PIMCO Total Return	PTTDX	8	8	6
1.73%	MasterCard, Inc.	MA	9	9	11
1.60%	MetWest Tot Ret Bond Fund	MWTRX	10	10	10
1.57%	General Electric	GE	11	13	14
1.55%	iShares Barclays TIP Bond	TIP	12	11	9
1.55%	DoubleLineTotal Return	DLTNX	13	12	12
1.45%	Intel Corporation	INTC	14	14	15
1.31%	McDonald's Corp.	MCD	15	15	13
1.27%	Altria Group, Inc.	MO	16	16	16
1.21%	Visa, Inc.	V	17	17	20
1.16%	Celgene Corporation	CELG	18	18	17
1.16%	JP Morgan Chase	JPM	19	22	21
1.10%	Ford Motor Company	F	20	20	18
1.06%	Exxon Mobil	XOM	21	19	19
1.05%	EMC Corporation	EMC	22	23	23
1.03%	Las Vegas Sands	LVS	23	21	28
0.97%	Schwab 1000 Fund	SNXFX	24	24	22
0.92%	Permanent Portfolio	PRPFX	25	25	24
0.92%	Ridgeworth High Income	STHTX	27	26	25

Portfolio Concentration: Top 25 holdings represent 54.39% of the Assets Managed at Fagan Associates as of March 31st, 2012.

Largest Mutual Fund Holdings as of March 31st, 2012.		
Domestic Equity Funds	***International Equity Funds***	***Hybrid/Fixed Income/ Muni Fund/ETF***
Schwab 1000 Fund	William Blair International Growth	Payden GNMA Fund
Baron Asset Fund	Harbor International Fund	Loomis Sayles Bond Fund
Parnassus Equity Income Fund	Tweedy Browne Global Value	PIMCO Total Return
Dow Jones Broad Market Index	Vanguard International Growth	MetWest Total Return Fund
Oakmark Fund	Harding Loevner Emerging Markets	iShares Lehman Bros TIPS

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