



During 2011, the performance of individual stocks was not primarily based on the potential of the underlying companies, but on the large up and down swings of the market based on unpredictable “macro” factors. The major macro factor that negatively affected the market over the past year was the inability of the European Union to satisfactorily deal with the faltering debt of Greece and Italy, the near stalemate in the US government, and the tsunami/nuclear event in Japan. These events caused a market variation of roughly twenty five percent (from peak to trough) during the year. Fortunately, a strong and independent Federal Reserve System in the US was able to keep its finger in the dyke, and the market closed just slightly negative for the year.

During the fourth quarter of 2011, the average of all Westport Resources portfolios appreciated by 11.6 percent (after commissions). Over the same period, the S&P 500 index increased by 11.2 percent and the Value Line Geometric index increased by 11.1 percent . We achieved the above performance while we increased our cash position to roughly 14 percent. During the fourth quarter, we limited call writing to at most one position. Thus, for the year, the portfolios declined by 3.2 percent (after commissions), while the S&P 500 index increased by 0.1 percent. The broader Value Line Geometric index declined by 11.5 percent for the year.

Over the past two years, Westport Resources portfolios have increased by 16.5 percent (after commissions), while the S&P 500 and Value Line indices have increased by 12.8 percent and 8.2 percent, respectively.

TIMING MODEL

The Timing Model improved during the fourth quarter. It moved up by five points to a bullish reading of 60%. Thus, it predicts a 60% chance of market appreciation and a 40% chance of market decline over the next 3 – 6 months.

2012 OUTLOOK

The economic outlook in the US continued to gradually improve in 2011. We were able to avoid a double dip recession, but growth did slow to about 2 percent for the year. Since this was below the expectation of 3 - 3.5 percent growth, it was a disappointment to the market. The consensus estimate for US GDP growth for 2012 is a more conservative 2.0 – 3.0 percent. During 2011, the economies of China, India, and Brazil slowed, and Europe is expected to be in recession during the first half of 2012. Thus, it is possible that in 2012, the US will resume its old role of being the engine of world growth.

The Federal Reserve Board has continued its stimulative monetary policy. Our Federal government has been essentially stalemated in its budgetary policy and is therefore roughly neutral in its effect on the economy. The Fed has signaled, however, that it will maintain its present low interest rate policy indefinitely into the future (i.e. until at least 2014).

Commodity prices have moderated due to slower world growth. A significant new positive factor is that US oil consumption has declined by roughly six percent during 2011. In addition, large new sources of oil and natural gas have been found in the US. This is a big positive for the US economy.

The housing market has bottomed. While housing prices are not expected to increase significantly over the coming year, the mortgage default rate is slowing. Existing home sales, and new home starts have been increasing. As the housing market continues to improve in 2012, it should provide a positive influence to corporate profits and the stock market.

Corporate earnings grew by roughly ten percent during 2011. All of that earnings gain went to reduce the price-to-earnings ratio rather than to increase the price of stocks. Thus, the price-to-earnings ratio of stocks has come down to roughly 13.5 over the course of the year. That means that the market is now cheap by historic standards.

Finally, unemployment as defined by the Labor Department, has reached 8.5% percent in December, down from a seasonally adjusted 8.7% in November). This has led to improved consumer confidence and better retail sales. I expect that roughly one and a half million new jobs will be created during 2012, and that the unemployment rate will fall to roughly 7.5 – 8 percent. Thus, consumer sentiment and retail sales should continue to improve over the coming year.

In summary, the economic outlook for the US is moderately good and improving. Since the market is undervalued, I expect the US Bull Market to continue during 2012. The fly in the ointment is the threat of a European bond default. The default of a major country (i.e. Italy or Spain) would be as bad as the 2008 Lehman bankruptcy. That's why the likelihood of such an event is extremely low (i.e. below 5%). Everyone, including the US Fed and China, will intervene to try to prevent that kind of a financial failure. If Europe can significantly reduce the risk of a sovereign bond default, the US market could have a big up year (i.e. 20+%). Otherwise, it is reasonable to expect a normal improvement (i.e. 8 – 12%) in the market.

I wish you all a healthy and prosperous New Year, and thank you for your continued confidence.