

MARKET COMMENTARY

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The Third Quarter was a bad quarter for investors. Fear about European Debt and a slowing in emerging market economies sparked real concerns of a Global Recession. As a result, the markets sold off steeply in the quarter. One of the fears investors have is that government policy will have a dramatic impact on the global economy. This causes uncertainty. It is difficult to predict what governments will do and even more importantly, a concern with whether it will work. I do not believe that the International Banking System will allow a financial lock up like 2008. Many of the problems are similar, including the huge amounts of debt. However, the difference this time is this is sovereign debt as opposed to private debt in 2008.

I have discussed the sovereign debt problems of PIIGS in previous Market Commentaries. I believe the markets have over corrected. The markets have dropped to a point that they are pricing in a belief that all of these countries are as bad off as Greece. Several of the other countries have already taken steps to correct their problems. Ireland has taken steps to implement reforms to recapitalize their banks. Spain is taking steps to correct its problems and Portugal is repairing its Government budget problems. The Italians are running a budget surplus, so they will be able to pay their bills.

The second problem that concerns investors is the slowing of the emerging markets. Oil, copper, coal, iron ore and other industrial metals sold off during the third quarter. Emerging market Central Banks raised interest rates to contain rising inflation. As the interest rate increase took hold, their economies slowed, bringing down inflation. Several of these countries have once again lowered interest rates and their economies are expanding again. Oil has risen from a low in the seventies per barrel (WTI) to the low nineties. Copper fell to a low of three dollars/pound and has risen back to the high threes. Late third quarter data show moderate but steady gains in Emerging markets. The US is expanding at a 1 1/2% to 2 1/2% rate. Europe is much slower and I believe this data indicates a growing world economy and one that will not slip back into a recession.

With the emerging markets expanding, the need for basic commodities and industrial products should continue to expand. Saudi Arabia has not been able to meet its 10MM bbl/day commitment, shipping around 9.5MM bbl/day. The International Energy Agency stated that the non OPEC producing countries will not be able to increase production in 2012. These items continue to convince me that Brent Oil Prices will average \$125/bbl over the rest of this year and move higher next year. Several investment ideas related to that continuing demand would be SeaDrill Ltd. (SDRL), the Norwegian deep water driller that has a current dividend rate of almost 10% and Knightsbridge Tankers (VLCCF) which transports oil and currently has a dividend yield in excess of 8% as well. In addition, I feel that the oil service companies are poised for significant gains in the last half of the year. Cameron International (CAM), Schlumberger Limited (SLB), and Helmerich & Payne (HP) are good plays. The huge oil finds in the BAKKEN and EAGLE FORD Shale plays will benefit the service companies.

We also believe that the worldwide recovery in industrial production should lead to an increase in demand for coal, iron ore, and liquefied natural gas (LNG). We are buying stocks that should benefit from this increased demand. We are increasing our positions in companies such as Caterpillar (CAT) and Joy Global (JOYG), which are both deeply involved in mining operations. We are also buying Teekay LNG Partners (TGP) which has a 6.6% dividend but should also benefit from the worldwide demand to reposition LNG products. We are recommending Peabody Energy Corp (BTU), Southern Copper (SCCO), Freeport McMoran (FCX) and Cliffs Natural Resources (CLF) because of the anticipated increases in shipments of coal, copper and iron ore to meet the higher demand. These companies all sold off in the most recent market pullback, giving investors a chance to buy very good companies that produce a large percentage of their income from expanding markets overseas.

Based on our views of the demand for all types of energy commodities, we are also recommending Penn Virginia Resources (PVR), Linn Energy (LINE), and Kinder Morgan Partners (KPM). Even if it takes a little longer for the higher equity values to be recognized, these investments are currently paying a dividend of between 7% and 9%.

The Manufacturing Sector for Industrial products has shown good earnings growth. The majority of industrial companies that have reported third quarter results have beaten forecast and many have raised guidance. We like Honeywell (HON), United Technology (UT), Emerson Electric (EMR), and Cummings Inc (CMI), as well as the aforementioned Caterpillar (CAT).

Investors should not let fear deter them from staying with producers that supply the developing world. We believe the recent panic was a good buying opportunity. I do not believe the International banking system will allow the European Sovereign debt to cause a general financial lock up. I believe we are in a secular growth period for both hard and soft commodities. However, market volatility could be high over the next few months. Developing economies are consuming large quantities of better food and materials for economic expansion. In the last ten years, two billion people worldwide have doubled their income. They seem to be steady in their demand for better housing, better food and a better life. These producing companies are able to prosper without the US economy expanding.

We look at longer term ideas at BSG&L Financial Services. Over the last year, it has served us well. Investors should try not to focus on the short term indicators which we feel will only confuse them and lead them to make incorrect decisions about their investment holdings. We believe we are on the right track by having a longer term perspective with our investment ideas.

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