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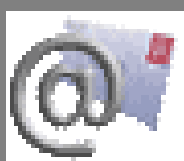
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THE MARKETS

Several encouraging U.S. economic reports pointed to improvements in the job market, housing market, and overall outlook, helping to keep the quiet holiday trading week on the bright side. U.S. consumers are reportedly more confident, jobless claims trended downward in December, and retailers had stronger sales this Christmas season than a year earlier.

Overnight borrowing from the European Central Bank spiked Thursday, to its highest point since February, as euro zone banks sought to keep cash flowing and meet year-end capital requirements. Meanwhile, private lending in the euro zone is tightening as cautious bankers are less reluctant to take on risk. In a sign of a slight gain in bond buyers' confidence, yields dropped on Italy's government bonds from a month earlier. However, 10-year Italian bond yields remained stubbornly high. Overall, the markets had a mild and quiet week on light trading and minimal volatility.

Returns through 12/30/11	1 Week	YTD	1-Year	3-Year	5-Year
Dow Jones Industrials	- 0.60	8.38	8.38	14.89	2.37
NASDAQ Composite	- 0.52	- 1.80	- 1.80	18.21	1.52
Russell 2000	- 0.88	- 4.18	- 4.18	15.63	0.15
S & P 500	- 0.58	2.11	2.11	14.11	- 0.25
MSCI EAFE NR USD	0.81	- 12.14	- 12.14	7.65	- 4.72

Source: Morningstar.com. * Past performance is no guarantee of future results. Indexes are unmanaged and cannot be invested into directly. Three and five-year returns are annualized. The S&P, excluding "1 Week" returns, is a reflection of return to an investor, by reinvesting dividends after the deduction of withholding tax.

No bank failures last week – According to information available on the FDIC website, no bank failures were reported last week. 90 banks failed in 2011. The FDIC website listed 157 bank failures in 2010, 140 in 2009, 26 in 2008, 3 in 2007, zero in 2006 and 2005.

U.S. consumer confidence rises – Confidence among U.S. consumers hit an eight-month high in December, reflecting an improving job market. The Conference Board's index rose to 64.5, up from 55.2 in November. The Bloomberg Consumer Comfort Index also improved, rising to -45 in the week ended December 18, from -49.9 a week earlier, its biggest weekly gain since January.

U.S. pending home sales hit 19-month high – More Americans agreed to buy an existing home in November than in any month since April 2010. The National Association of Realtors' seasonally adjusted index for pending sales of existing homes rose 7.3% to 100.1. However, the Standard & Poor's/Case-Shiller Home Price Indices in 20 cities fell 3.4% from October 2010 to October 2011 as foreclosures continued to weigh on the U.S. housing market.

Christmas season was merry for U.S. retailers – U.S. retail sales are headed for a 3.8% rise in November and December from a year ago, according to the International Council of Shopping Centers. Retailers started the Christmas season with a surge of sales over Thanksgiving weekend, and they benefited from a last-minute surge of shoppers lured by extended hours and large discounts.

Weekly jobless claims rise; four-week average drops – Although initial claims for U.S. unemployment benefits rose 15,000 to a seasonally adjusted 381,000 for the week ended December 18, the four-week average eased 5,750 to 375,000, its lowest level since June 2008.

Sears to close 100+ stores – Sears Holdings expects to close 100 or more underperforming stores to cut costs as the company continues to struggle with sales declines. Sears reported that same-store sales slid 5.2% so far this quarter. The company, which has close to 2,200 Kmart and Sears stores, could generate \$140 million to \$170 million in cash from inventory sales and subleased or sold real estate.

Fitch cuts Sears credit rating, S&P to review it – Fitch Ratings cut the credit ratings for Sears Holdings three notches — to CCC from B — citing the large retailer's declining sales and profits and its inability to resolve these issues. Standard & Poor's Ratings Services also is reviewing Sears' credit rating for a possible downgrade based on Sears' disappointing quarterly performance.

Lowe's buys online retailer – Home improvement retailer Lowe's is buying ATG Stores, an online home improvement retailer, in order to expand its Web presence and product offerings. ATG Stores will be an independent, wholly owned unit of Lowe's. The companies plan to maintain separate branding and say that no jobs will be lost.

ECB overnight loans jump – European Central Bank overnight loans to euro zone banks spiked Thursday to more than €17.3 billion, up sharply from €4.3 billion a day earlier. Two factors appeared prominent — the need for liquidity amid a strain in private sector lending as well as the need to meet certain end-of-year capital requirements.

Eurozone private lending tightens – Private sector lending in the euro zone fell in November to its lowest level in more than a year, signaling tightening monetary conditions. The European Central Bank reported that private sector lending fell 0.1% from October to November. Fears of a euro zone credit crunch are growing as banks become increasingly cautious.



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Italy's bond yields ease, as confidence rises – Yields on some Italian government bonds fell substantially this week from elevated yield levels in late November. Comparing yields with those issued one month earlier, six-month bills yielded 3.251%, down from 6.504%, and three-year bonds sold for 5.62% down from 7.56%. However, 10-year bonds were priced at 6.98%, lower than November's 7.56%, but still very elevated.

Spain's projected budget deficit grows – The Spanish government says its budget deficit will be much larger than earlier forecast, growing to close to 8% of the country's gross domestic product, up from 6% of GDP. As a result, Spain is introducing a €8.9 billion austerity package, including tax increases and the freezing of civil servants' salaries.

Japanese industrial production falls – Industrial production in Japan fell 2.6% in November, largely as a result of flooding in Thailand, a key production center for Japanese manufacturers. Other factors included the global economic slowdown and the yen's rise. However, forecasts for December and January are strong. Japan's Ministry of Economy, Trade and Industry forecasts a 4.8% increase in output in December and a 3.4% rise in January.

The week ahead

- Amgen and Monsanto announce quarterly earnings Thursday, January 5.
- ADP monthly employment report released Thursday, January 5.
- U.S. weekly unemployment claims released Thursday, January 5.
- Bloomberg Consumer Comfort Index published Thursday, January 5.
- Monthly U.S. employment situation report published Friday, January 6

WEEKLY FOCUS

It's a bittersweet way for investors to begin 2012. On the one hand, economic news in the U.S. has been getting steadily better. The recent holiday shopping season is shaping up to be the best since the beginning of the Great Recession; the housing market is starting to show some signs of life and even the job market's showing slight improvement.

Consumers are spending, but not a lot. Employers are hiring, but not a lot. There are constraints and headwinds that prevent us from having the typical bounce-back recovery that you'd like to see after a recession. Most economists believe that the U.S. is not heading into another recession. The recent numbers are encouraging, but we can't expect too much. If the economy grows from 2.5 percent to 3 percent that would be great news. But, we can't expect the next stop to be 4 percent. It's important for the U.S. is to maintain respectable growth.

Housing continues to be the big drag on the economy. According to the Case-Shiller index, the cataclysmic decline in home prices has long ended and prices bottomed out in May 2009. But we've only continued to bounce along the bottom. Banks are unwilling to make mortgage loans and many existing loans remain higher in value than the homes. That's kept the real estate recovery very slow. New construction is taking place at half the pace of population growth. At some point these things will have to balance out.

U.S. corporate profits don't equate to U.S. growth anymore. U.S. consumption only accounts for 28 percent of the S&P 500 profits. Only 55 percent of the largest companies' revenue comes from the U.S. Globally, China and India seem to be slowing down. Even with continued slowing, China and India will count for about half of global GDP growth in 2012. So those are critical economies. If the authorities can beat runaway inflation in those two countries, and Europe doesn't fall off a cliff, their economies will have a soft landing. And that's critical.

But then, there's Europe. The region's leaders have failed once again to convince investors that they will be able to prevent a breakup of their 17-nation currency union. Greece could still default on its debt, causing huge losses for banks in France and elsewhere that hold Greek bonds. Investors fear that could cause a financial panic to spread around the world, similar to what happened in 2008 after Lehman Brothers collapsed. The probability of a solution to Europe's issues remains low. Nobody knows what it will be, or what the solution might look like. The European authorities' attitude to dealing with their problem has been to close their eyes, hold their noses and hope it might go away. Continuing to stumble along is the most likely path going forward.

The alternative is even more troublesome. If there's immense pressure on politicians, there can be an accident that takes the form of a bankruptcy, or nationalizing of some banks, the collapse of the euro, or that a country exits the European Union. Muddling through is the best option. Europe could then face a mild recession and economic contagions would be limited. But the darker scenario could lead to a financial contagion which would be drag the global economy down.

The European Central Bank has many different masters to serve. There's Germany looking over its shoulder and is aware that it will have to help the troubled countries, but doesn't want to help them too fast. They want to see fiscal austerity before bailing out anyone. But how do you enforce fiscal austerity?

It's like the stories coming out of Greece where people get higher taxes tacked on to their utility bills and they say they won't pay them because they can't. It's an illustration of the principle that they want to do the right thing, but how can they get it done if nobody will pay the bill.

The U.S. economy is not yet strong enough to withstand any financial contagion that spreads from Europe. The uncertainty will continue to dominate the financial market news in 2012. However, it does appear that the economy is on the mend and things will improve ever so slightly in 2012.

Sources: The Wall Street Journal; The Associated Press Newswire, The Wall Street Journal Online; Bloomberg News; Financial Times, Investor's Business Daily. This material does not constitute tax, legal or accounting advice and neither Pinnacor Financial Group, Inc. nor Cambridge offers such specific tax advice. The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general. The Dow Jones Industrial Average is a price-weighted index of 30 actively traded blue-chip stocks. NASDAQ Composite Index is an unmanaged, market-weighted index of all over-the-counter common stocks traded on the National Association of Securities Dealers Automated Quotation System. The Morgan Stanley Capital International Europe, Australia and Far East Index (MSCI EAFE Index) is a widely recognized benchmark of non-U.S. stock markets. It is an unmanaged index composed of a sample of companies representative of the market structure of 20 European and Pacific Basin countries and includes reinvestment of all dividends. Diversification does not guarantee against market declines or portfolio losses. You cannot invest directly in an index.

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