NOESIS CAPITAL MANAGEMENT

A REGISTERED INVESTMENT ADVISOR

January 15, 2012

Dear Client:

2011 turned out to be a difficult year for equity investors worldwide. The S&P 500 was volatile but ended essentially unchanged, making the U.S. one of the best-performing stock markets of the year. Other markets did not fare as well with most other equity indexes posting declines, many of which were significant. Formerly popular emerging markets were hit especially hard as investors questioned the sustainability of their growth. During this turbulent period the U.S. defended its status as a safe harbor.

Sources of Uncertainty

The Eurozone's sovereign debt crisis continues to be a main topic of concern. In order to improve liquidity, the European Central Bank (ECB) lent €489 billion worth of three-year loans to over 500 banks on December 20th. This is reassuring as it shows that the ECB is willing to provide unusually high support to avoid a potential credit crunch. Unfortunately, these same banks returned almost one half of this capital to the ECB the very next day in the form of new deposits, showing that credit markets are still stressed and that European banks are still in the process of deleveraging. The Eurozone's resolve will be tested in the first quarter as €300 billion of public and €250 billion of bank debt become due. Replacing this amount under current market conditions could prove to be difficult without coordinated support.

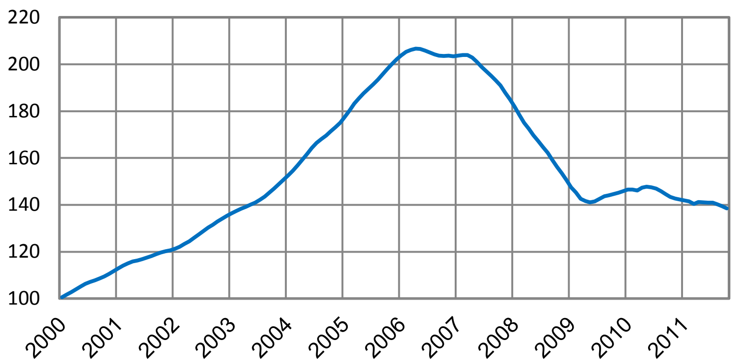
Country	Index	2011
US	S&P 500	0.0%
UK	FTSE 100	-5.6%
Korea	KOSPI Comp	-11.0%
Spain	IBEX 35	-13.1%
Germany	DAX	-14.7%
Australia	All Ordinaries	-15.2%
France	CAC 40	-17.0%
Singapore	Straits Times	-17.0%
Japan	Nikkei 225	-17.3%
Brazil	Bovespa	-18.1%
H.K.	Hang Seng	-20.0%
Taiwan	TAIEX	-21.2%
China	Shanghai Comp	-21.6%
Russia	RTS	-21.9%
India	SENSEX	-24.6%
Italy	FTSE MIB	-25.2%

The economic picture in the U.S. remains murky as well. Government debt levels are approaching 100% of GDP and could continue to rise for several more years. The housing market has been weak for over five years now and prices are not yet showing signs of recovery (Chart 1).

Another key concern is the labor market. During the latest recession, we lost more than 8.8 million jobs in the private sector. So far, we have re-employed only 3.2 million people. The scarcity of jobs is reflected in both the elevated unemployment rate and in the number of weeks it takes for a person to return to the labor market after they have become unemployed (Chart 2).

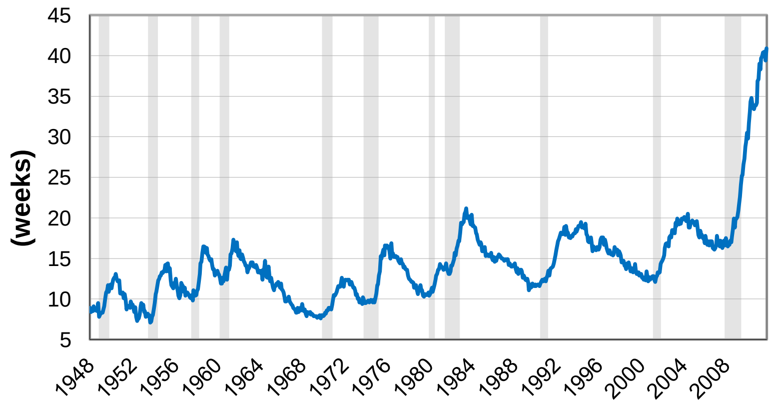
1801 Clint Moore Road, Suite 100, Boca Raton, Florida 33487
561-999-9888 • Fax 561-994-2893 • E-Mail: info@noesis-capital.com
www.noesis-capital.com

Chart 1: S&P/Case Shiller 20-City Home Price Index



Source: Standard and Poor's

Chart 2: Average Duration of Unemployment



Source: The U.S. Department of Labor

Emerging markets are negatively impacted by economic weakness in the U.S. and Europe too. Most of their economic growth still depends on exporting products to the west. Without western buyers, their growth engines are losing steam. These economies have been growing unsustainably fast during the past decade or two, and thus caused high inflation and possibly stretched valuations in certain asset classes like real estate.

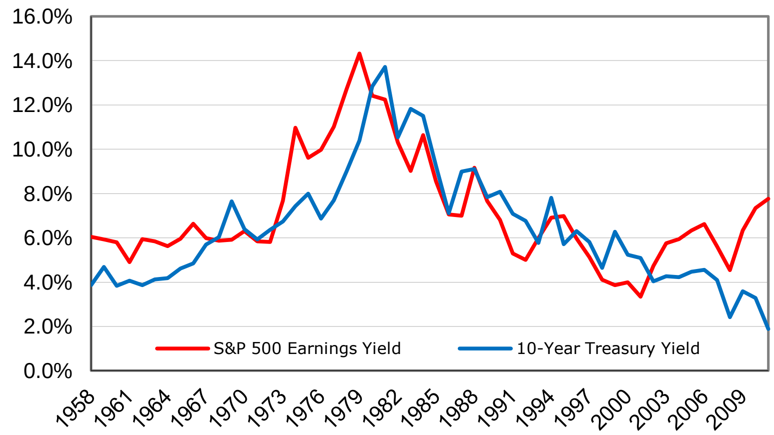
In summary, the global economic picture looks imbalanced and blurry. We believe that developed economies need to work hard on deleveraging, which may take years. On the other hand, inflation in emerging markets is acute but cyclical, which could be a short-term event.

Looking Ahead

Since investment risk is so high, what should we do? Normally, investors would seek the safety of bonds in these conditions; however, as we have argued before, bond markets are unattractive at this point in time. In fact, bond yields remain at all time lows while their prices are at all time highs. Bond investors face two headwinds: low yields, many of which are below inflation, and potential principal loss when markets begin to anticipate higher interest rates. Fixed-income investors specifically need to adjust their strategies and find a balance between reasonable yields without increasing risk too much.

Stocks appear to be valued attractively to bonds based on a comparison of the S&P 500's earnings yield to the yield of the 10 year US Treasury. These spreads have widened and are close to all time highs (Chart 3). This provides some evidence that stock market prices are attractive. Improving valuations also makes intuitive sense as the earnings per share of the S&P 500 grew by approximately 12% last year while the index itself remained flat.

Chart 3: The Fed Model



Source: Standard and Poor's, Federal Reserve Bank

Although the economic uncertainty ahead is quite high, our focus on companies that can generate strong cash flows consistently should protect our portfolios in difficult times. On the offensive side, we prefer companies with strong exposure to emerging markets thus providing them with better growth opportunities.

For example, Wal-Mart's mission states "*We save people money so they can live better*." In our opinion, the company's ability to deliver on this statement makes them valuable no matter when an eventual economic recovery occurs. Wal-Mart also seems well positioned to expand their business to cost conscious consumers outside the U.S. At 26%, the company's current international exposure remains small, but their strategic position in emerging markets is quite strong, which offers a great growth opportunity.

Similarly, Google's mission is to organize the world's information and make it universally accessible and useful. As the Internet becomes dominant in our daily activities, Google becomes a must-use tool. While the company makes information freely available to anyone with an Internet connection, it generates revenue by delivering online advertising on its main and partner websites. The more we use the web, the more Google benefits as it functions like a toll booth to the Internet. The company generates approximately 55% of its revenues from international sources and continues to expand rapidly.

UPS also benefits from the global shift to the Internet. As consumers are more willing to shop online, companies rely on UPS's timely delivery. Furthermore, globalization increases the need for international trade and shipping. The demand for reliable package delivery seems likely to increase in years to come, especially in light of a possible downsizing of the U.S. post office.

In conclusion, we continue to believe that investing in these and other high quality companies with strong cash flows, low leverage and high earnings visibility at reasonable valuations is the best path to long-term success. When viewed with this in mind, short-term volatility could be useful to long-term investors as it creates opportunities to buy the world's best companies at attractive prices.

RECENT PURCHASES

Walt Disney Company (DIS)

We are adding more shares of Disney to our portfolios this quarter. Fourth quarter reports showed that Disney is gaining momentum and is less sensitive to the economy than investors originally feared. The company's immense library of high quality content, ESPN's dominant position in sports broadcasting and its parks and resorts are admired by children and adults worldwide. Importantly, its leading position is hard to challenge.

Cisco Systems-Linked Reverse Convertible Note

This security offers a monthly coupon based on a 10.45% annualized yield with a 30% downside protection. As Cisco's fundamentals are improving and the stock's downside risk is reduced, we are using this security to provide income in the short-term.

Starting this year we switch our calculation methodology from internal rate of return (IRR) to time-weighted rate of return (TWR). The latter excludes capital flows like contributions and withdrawals as their timing and size is typically beyond the control of the portfolio manager. With this change we are following industry practice recommended by the CFA Institute.

Richard M. Brown

On a personal note, I want to inform you about a loss in the Noesis family. Our highly appreciated mentor, colleague and above all friend, Richard Brown, passed away at the age of 86. Upon his retirement as a Vice President and Supervisory Research Analyst at Goldman Sachs, we were very fortunate to have him join us in 1990. In the early years of Noesis he was instrumental in shaping our investment philosophy and always made himself available to coach our research team. He shared his astute investment knowledge and experience with us. Dick retired from Noesis in 2009, moving back to Massachusetts to be close to his family. All of us at Noesis send our thoughts and wishes to his beloved wife Nancy and all their children and grandchildren. We will all miss him.

Sincerely,

Joseph Lai, CFA
Chief Investment Officer

Our most recent Form ADV, Part II is available upon request