TRIVANT

CUSTOM PORTFOLIO GROUP, LLC

October 2012

Quarterly Insights

EXECUTIVE SUMMARY

Stocks And Bonds Rise In The Third Quarter

In the Third Quarter, the domestic S&P 500 Index rose 6.35% and is up 16.44% year to date. The market rallied in advance of the U.S. election. Fiscal cliff uncertainty was not enough to slow the momentum. Positive trends included signs of improvement in the housing market and rising consumer confidence. The Barclay's Aggregate Bond Composite Index rose 1.59% and is up 3.82% year to date.

Election Outcomes And Market Returns

The Presidential election is around the corner. There is tremendous media posturing regarding how each candidate would impact the market should he win. We are most concerned about the President's agenda as it pertains to the fiscal cliff, tax policies, and sector effects. We are less concerned as to whether there is a controlled Congress.

History favors the incumbent. Therefore we have positioned your portfolio for the moment toward an Obama victory. This can change soon. A Romney victory would likely result in higher spending cuts, lower tax rates, the removal of Obamacare, and eased financial regulations. All of this would influence our future portfolio strategy.

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Third Quarter 2012

In This Issue

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Election Outcomes And Market Returns

You May Have Presidential Election Anxiety, But We Don't

The Presidential election is around the corner. You may be a Republican who fears another four years of President Obama. You may be a Democrat who dreads the prospect of seeing Mitt Romney in the Oval Office. The country is politically divided. So are our clients. There is tremendous media posturing, bordering on fear-mongering, regarding how each candidate would impact the market should he win.

As your portfolio manager, we ignore the noise! We must remain unemotional and unbiased regarding the upcoming election. Our goal is effective portfolio risk control. This has everything to do with assessing probability and statistics. Let's break down these two areas as they pertain to your portfolio and the election.

History Favors The Incumbent

There are reasonable probabilities that either candidate can win. The probabilities shift daily and will do so right up to the election. We cannot predict the winner with certainty. However, we are cognizant that history shows it is tough to defeat an incumbent. Post WWII, the incumbent President has won seven out of nine elections. Therefore, we give a higher probability to an Obama victory and have positioned your portfolio toward an Obama political agenda. This will change if we deem a major shift in the probability of a Romney victory. We will soon deal with certainty (versus probability) regarding who is President and how to react.

Markets Favor The Incumbent

Let's look at hard statistics as they pertain to Presidential elections. Post-election two-year stock market returns since 1945 are much more attractive when the incumbent wins. This is no guarantee of future performance. But the trend is comforting if you fear the incumbent.

Presidential Election Outcomes: Subsequent Two-Year S&P 500 Index Returns Since 1945

INCUMBENT VERSUS CHALLENGER	Subsequent 2-Year Market Return
Incumbent Wins	**22.6%**
Incumbent Loses	4.9%
STRONG VERSUS WEAK PRESIDENT	
President Controls Congress (Strong)	23.8%
President Does Not Control Congress (Weak)	23.1%

Control Of Congress Is Insignificant

You may find it surprising to learn that whether the President is "strong" (he controls Congress) or weak" (he does not control Congress) has had no statistical bias on two-year market returns subsequent to a Presidential election. In fact, the returns are virtually identical under either scenario.

So what does all of this mean? It means that from a portfolio strategy standpoint, we are more concerned about the President's agenda and not as much concerned regarding whether or not he controls Congress.

What We Are Watching For In The Election From A Portfolio Strategy Standpoint

Whoever is elected President will impact our portfolio strategy going forward. We will pay close attention to the President's agenda pertaining to areas such as the fiscal cliff, taxes, health care, and financial regulations.

KEY PORTFOLIO CONSIDERATIONS

The President's Agenda

Fiscal Cliff	Tax Policies	Sector Effects
Will the President have a controlled or divided Congress in early 2013 regarding a solution to spending cuts and tax policies? The election results will give us greater clarity regarding government initiatives and their potential effects on the economy.	Will the highest income bracket be 39.6% (Obama proposal) or 28% (Romney proposal)? Will capital gains and dividend taxes be 20% (Obama proposal) or 15% (Romney proposal)?	How will the Health Care sector fare with Obamacare (Obama agenda) or no Obamacare (Romney agenda)? How will the Financials sector fare with heightened regulations (Obama) or lowered regulations (Romney)?

1. Fiscal Cliff

The fiscal cliff is a combination of measures to reduce debt - $7 trillion in tax hikes and spending cuts over the next decade - that will begin in January unless Congress intervenes. We anticipate some compromise in early 2013. However, the degree and ease of the compromise is unclear and will be dictated by the election results.

A controlled Congress (either party) will result in a quick compromise. A Romney-controlled Congress will stress lower taxes and higher spending cuts. An Obama-controlled Congress will stress higher taxes and lower spending cuts. A divided Congress (Romney or Obama) will likely entail tremendous political grand-standing before a solution is reached, making it tough to predict the degree of the tax / spending trade-off.

2. Tax Policies

The higher the income tax rate, the higher our clients will be taxed in areas such as bond payments, social security payments, and IRA distributions. The higher the future capital gains rate, the lower the future after-tax value of stocks with unrealized capital gains and the greater the impetus for taking gains before year-end. The greater the differential between income and dividend tax rates, the greater the potential motivation to hold dividend-paying stocks versus bonds. All of these considerations can impact asset allocation decisions.

3. Sector Effects

We have the portfolio positioned for an Obama agenda. A Romney victory, especially if he has a controlled Congress, would motivate us to adjust sector weights - especially Health Care and Financials.

Romney intends to repeal the Patient Protection and Affordable Health Care Act ("Obamacare"). With or without a Republican Congress, he could do it. If he wins, we would examine Health Care exposure in areas such as pharmaceuticals, hospitals, insurance, and life sciences. Romney also intends to lower regulations in the financial industry. We would dramatically raise Financials exposure with a Romney-controlled Congress.

Stock Market Spotlight

The U.S. Market Rallied In The Third Quarter

In the Third Quarter, the domestic S&P 500 Index rose 6.35% and is up 16.44% year to date. The market rallied in advance of the U.S. election. Fiscal cliff uncertainty was not enough to slow the momentum. Positive trends included signs of improvement in the housing market and rising consumer confidence.

In an effort to calm investors and support economic growth, European Central Bank (ECB) President Mario Draghi initiated a significant bond buying program to keep European interest rates low. This effectively guarantees successful European sovereign debt auctions. With the threat of a failed auction alleviated, the European market rose 10.03% in the Third Quarter, but lags the U.S. market by roughly 5% year-to-date.

We Maintain Our Portfolio Strategy Going Into The Election

Your portfolio was hardly adjusted in the Third Quarter. We continue to favor "high quality companies" over "low quality companies" (see Quarterly Insights, July 2012, Stock Market Spotlight, page 5). These are the companies that have considerable financial strength, well-established market niches, and greater agility to react to market conditions. Buoyed with strong cash positions, many "high quality" companies have been buying back their stock. Stock buybacks have been double the rate of equity fund redemptions, creating a high level of stock price support. We viewed the European out-performance as a temporary versus long-term trend, and did not raise foreign exposure.

Apple: An Interesting Dilemma In Our Portfolio Decision Process

Apple Inc. (symbol: AAPL) has been in the news - a lot. The company recently broke through a $700 share price (it started the year at $411) and a $650 billion market cap. It is now nearly 5% of the S&P 500 Index, a 50% higher weight than the second-largest company (Exxon Mobil). The eagerly-anticipated iPhone 5 has just been released. Can the Apple juggernaut continue? Is the company invincible?

The Evolution Of Apple Over The Last Five Years Is Staggering

We began purchasing Apple during the economic crisis (November, 2008) when the share price was $106. Our rationale was that Apple was financially strong, offered excellent products, and had a market niche that could grow in any economy. In the crisis, we sought the same types of "high quality" companies that we currently emphasize in your portfolio. We did not expect (but certainly welcome) a seven-fold price increase.

Apple remains "high quality", but its focus and stature have completely changed. In 2008, 72% of its business was desktops, laptops, and the iPod. Today, 72% of its business is the iPhone and the iPad. From 2008 to 2012, revenues rose five-fold ($32 billion to $148 billion) and profits rose ten-fold ($6 billion to $53 billion).

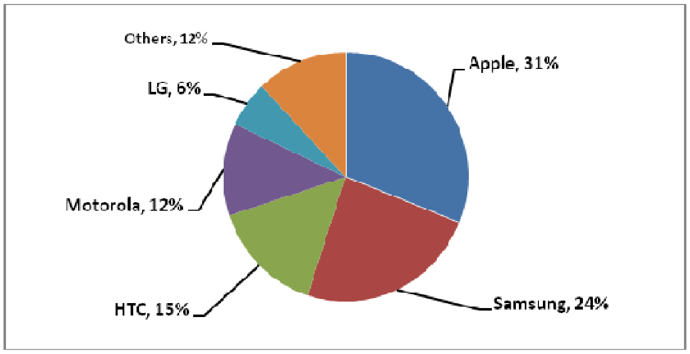
The Evolution of Apple Over The Last Five Years

Product or Service	% Revenue - 2008	% Revenue - 2012
Desktops	**17%**	4%
Laptops	**27%**	10%
iPod	**28%**	3%
iTunes (Music Products)	10%	6%
iPhone	6%	**46%**
iPad (did not exist until 2010)	N/A	**26%**

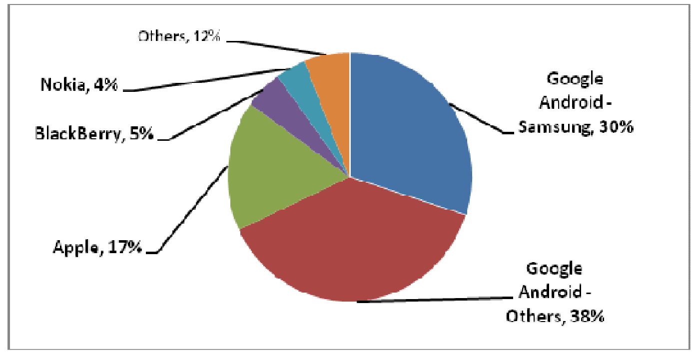
Smartphone Competition Is Intense

Competition is intense in the smartphone market. Apple dominates the U.S. (31% market share), followed closely by Samsung (24%) and others. However, Apple does not dominate the global market: the Google Android is by far the leading platform with a 68% market share, followed by the Apple iOS (operating system) with a 17% market share. The iPhone is higher-end and higher-priced in relation to its competitors.

U.S. Smartphone Market Share



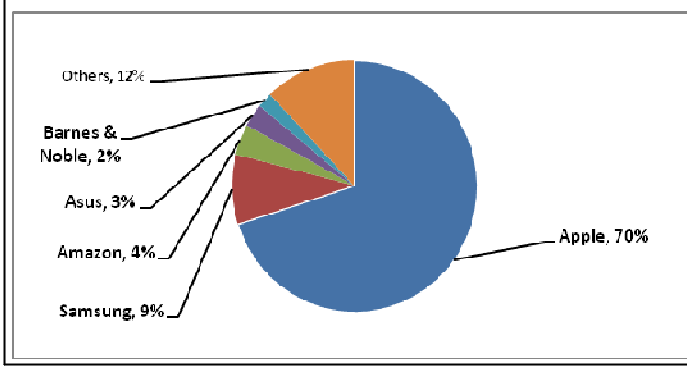
Global Smartphone Market Share



Apple Dominates The Tablet Market Right Now

Two years after creating the market with its iPad, Apple has a 70% market share of the global tablet market. During the Second Quarter, Apple sold 17 million iPads, up a stunning 44% from 12 million in the First Quarter. This translated into a market share gain of 12%. Apple provides a higher-end iPad as well as a lower-priced alternative (iPad 2). There will be two new market entrants: Google (Nexus 7) and Microsoft (Surface Products).

Global Tablet Market Share



Source: International Data Corporation (IDC)

Apple Risk Factors Have Risen Along With Its Stock Price

Apple is now a two-pony show. Half the company rides on its smartphone and another quarter of the company rides on its tablet. What is the ultimate size of the smartphone and tablet markets? Will these products and Apple's market share in these products exist five years from now? They didn't five years ago. Will the iPhone be able to further penetrate global markets with its higher price point? Will formidable competition such as Google and Microsoft erode its tablet market share? Complacency and failed innovation are large potential risks to Apple in an industry where market leaders can change in the space of a couple of years. Blackberry went from a 45% market share in 2008 down to its current 5% and is battling for survival.

Our Apple Dilemma: Risk Control Versus Taxes

Apple may appear to be invincible but it is not. No company is. We believe in limiting any one company's exposure to 5% of your portfolio. Apple is currently a 7% portfolio weight even though we previously pared it back twice. We want to pare it back again to at least its S&P 500 Index weighting of 5%, but ideally after the anticipated strong holiday sales for the iPhone and iPad. Selling Apple in a tax-deferred IRA account is no issue from a tax standpoint. Selling Apple in a taxable account is problematic given its large unrealized gains and 2013 capital gains rate uncertainty. We will assess what to do for each client based on their account type, tax bracket, age, and Apple weight. Apple still has a wonderful future and we intend to own a part of it.

Bond Market Spotlight

Bond Prices Rise Modestly In The Third Quarter

The Barclay's Capital Aggregate Bond Composite Index, a broad-based representation of bond performance, was up 1.59% in the Third Quarter. For the year, the index is up 3.82%. Government Treasury rates were flat. In contrast, Treasury Inflation-Protected Securities (TIPS) rallied sharply. There are reasons why the U.S. bond demand continues despite mediocre 2012 performance. Investors embrace the safety of U.S. bonds. The Fed is supporting the bond market through quantitative easing (QE3) .

The Fed Has A Dual Mandate: Full Employment And Inflation Control

The Fed mandate is full employment (widely considered to be a 5% unemployment rate) and inflation control (3% or lower). With currently low inflation (the CPI is 1.70%), the Fed is meeting one of its goals. However, the unemployment rate is still at 7.8%. Through its third round of quantitative easing (QE3), the Fed is buying bonds to stimulate the economy (by keeping interest rates low) and promote job creation.

The Federal Reserve bond buying spree continues to push Treasury and mortgage yields to record lows. To further fuel the fire, the Fed is also buying $40 billion per month of mortgage backed securities (MBS) until it sees further improvement in the labor market. Monetary policy has been somewhat effective, as evidenced by record low interest rates and surging mortgage refinancing.

Is Higher Inflation Around The Corner?

When the Fed injects money, the threat of inflation looms. Expected inflation is the yield differential between a Treasury bond and its same-maturity TIPS counterpart. Inflation expectations jumped sharply in the Third Quarter. This is why your TIPS fared well. TIPS appreciate when inflation expectations rise.

Inflation Expectations Rise In The Third Quarter (source: Federal Reserve)

Description	June 30	September 30	Change
5-Year Treasury Yield	0.71%	0.67%	(0.04%)
5-Year TIPS Yield	(1.05%)	(1.47%)	(0.42%)
5-Year Inflation Expectation	1.76%	2.14%	0.38%
10-Year Treasury Yield	1.62%	1.72%	0.10%
10-Year TIPS Yield	(0.50%)	(0.71%)	(0.21%)
10-Year Inflation Expectation	2.12%	2.43%	0.31%

Higher Inflation Could Halt Monetary Stimulus

Higher inflation is a big risk factor for the Fed bond buying spree. U.S. GDP growth of +2.3% (source: The Economist) is now roughly identical to inflation expectations. If inflation were to grow faster than the economy, the Fed dilemma will be how to balance its mandate of full employment and inflation control. Quantitative easing and other monetary stimulus geared towards economic and employment growth could halt in order to control inflation. If this happens, the economy and the market will feel the effects.

Bonds Remain Critical For Your Disciplined Asset Allocation Strategy

The bond market remains "yield challenged". We hold bonds where warranted as part of a disciplined asset allocation strategy (risk control) even though 2012 bond returns have lagged stocks. We continue to advocate corporate bonds and shorter-term (low duration) Treasury Inflation Protected Securities (TIPS).

Your Portfolio

The stock market rallied more in the Third Quarter than it had pulled back in the previous quarter. Year-to-date, the S&P 500 Index is up in exactly the range we initially forecast for 2012. Hopefully the index will continue its positive trajectory in the Fourth Quarter and our 2012 prediction of +15% will prove understated. The bond market has been much more subdued. This is exactly what we anticipated in January.

Our portfolio trading activity was limited in the Third Quarter. We sold a small Phillips 66 position in many accounts. This is a spinoff oil refinery company from ConocoPhillips. We never wanted oil refinery exposure in the first place. The industry is extremely capital intensive and only profits from an oil price spread that is beyond its control. We viewed a Third Quarter Phillips 66 price run-up as the perfect time to exit the stock.

The Fourth Quarter is when we assess tax-loss selling in taxable (non-IRA) accounts. This year, we have few unrealized gains to harvest. Most portfolios have realized and unrealized gains, some very significant. We will contact you shortly to discuss your account regarding potential measures for tax efficiency (if applicable).

Our bond portfolio was hardly adjusted in the Third Quarter and we do not anticipate changes in the near term. The portfolio has a short duration to ensure that it is less susceptible to rising interest rates.

As the election results become known and we enter 2013, we anticipate several adjustments to the stock component of your portfolio. Stay tuned for updates.

We will continue to closely monitor the market and adjust your portfolio as needed. Please feel free to contact us anytime to discuss questions or comments you may have. We will keep you informed of portfolio progress.

Respectfully submitted,

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CUSTOM PORTFOLIO GROUP, LLC

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