DREAMWORKS
CAPITAL MANAGEMENT, LLC

When Planning and Hard Work Payoff Q3 2012

The biggest news of the quarter, besides the equity markets impressive double digits return through the end of Q3, had to be the announcement by the US Federal Reserve to launch what we are calling "QE Unlimited".

The Fed is set to start buying back $40B worth of mortgage backed securities each month until it sees a turnaround in the economy and more specifically the unemployment rate. Maintaining artificially low interest rates isn't doing much to stimulate the economy in any meaningful way. One consequence of the Fed's low interest policy, has been to hurt the savers of this country. Lower interest rates basically force people into higher risk assets in order to achieve the possible returns that they are looking for in order to produce income or achieve their financial goals.

Whether you are receiving any interest or not, having a consistent and dedicated savings plan is still the prudent approach to take in order to accomplish financial and lifestyle goals. As we stressed in this quarter's lecture, *Balancing Your Changing Investment Needs*, emergency planning which should be your first priority within the wealth management planning process. Having and maintaining an emergency fund is more than just having some money sitting in a liquid savings account. This type of planning helps to protect your assets and can get you through life's volatile storms, which is the basis for our case study this quarter.

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Case Study

Client:

Married Couple, mid 40's, two children (college & high school) – The Harwells (name has been changed for confidentiality)*

Client Situation:

Everything was going smoothly for the Harwells until a sudden and surprising corporate restructuring left Mr. Harwell, the breadwinner of the family unemployed. The Harwells had never worked with an investment advisor previously, but had attended one of DWCM's quarterly lectures and knew DWCM worked with people of all asset levels. They were people who had done systematic planning, developing a budgeting process and working hard to execute it. The Harwells had saved a sizable amount of cash in a liquid savings account over the years. In addition, Mrs. Harwell was able to work extra hours in her part-time career. The Harwells were looking for reassurance that they would be okay.

DWCM Objective:

Our goal was to design a strategy that would allow the Harwells to weather this financial storm and to find peace of mind. With an emergency fund already established, we went through the couple's financials, and based upon the numbers, concluded that they had a year's worth of living expense covered in their emergency fund account. Using our "SMART" principles, we helped The Harwells determine that they really needed to focus on their retirement assets. We rolled both of the couple's 401k and 403b plans into Traditional IRA's which would give them flexibility and allow DWCM to invest the assets according to the couple's risk/reward profile. We also provided Mr. Harwell with contacts that could help him with his new career search.

Client Outcome:

By saving early and consistently throughout the years, the Harwells had enough in liquid savings to weather this life changing event. The couple now had even greater flexibility when it came to investing their retirement assets towards the new goals they had established using our "SMART" principles. Within the first few weeks of October, Mr. Harwell was able to secure new employment. The couple is now looking forward to replenishing assets used in their emergency fund and contributing additional funds to their new Traditional IRA accounts. Through planning and hard work, the Harwells found their peace of mind.

Economic & Market Viewpoint

We have discussed at great lengths this quarter with clients and DWCM website readers the growing disconnect between the equity markets and the economy. The equity markets, which have had their ups and downs this year, have managed to post impressive double digit returns through the end of Q3 this year. The economy here in the US continues to deal with subpar economic and job growth, while the world economy is dealing with a recession in most of the European Union and a slowdown in China. As many people have put it, the US looks to be the best house in a bad neighborhood when it comes to investing.

The US Federal Reserve has certainly done its job this quarter in trying to pump up the economy by announcing "QE Unlimited", a series of monthly mortgage backed security repurchases with the goal of stimulating demand and decreasing stubbornly high unemployment. The Fed is now identifying the unemployment rate as one of its biggest challenges to get under control with a target rate of around 7.3%.

We do not believe that the Fed will be able to accomplish this target with monetary policy alone. While the stock markets may like this addiction to easy money, we see it as completely bad for the future of the economy and the country.

As we move into the Q4 this year, we face what has become known as the "wall of worry". The "wall of worry" consists of the following three points (in no particular order):

1. US Presidential Election
    a. Although the election appears to be coming down to the wire, we are not certain that any major changes will occur within the economy or markets if either nominee is elected. However, this does not mean that there couldn't be shot-term volatility caused by a tight election. Think back to the 2000 Presidential race between Bush and Gore.
    b. It is our view, no matter who the President is, they usually receive too much credit for a positive economy and too much blame for a bad economy. Again, this does not mean that the markets do not react in the short-term.
2. The Fiscal Cliff
    a. The fiscal cliff which results in the combination of mandatory spending cuts (largely in the defense budget) and the expiration of the Bush tax cuts, goes into effect at the end of the year. This is a result of the so called compromise which occurred on Capitol Hill during the debt extension negotiations.
    b. It is widely speculated that if we do go off the Fiscal Cliff, the US will likely enter into a recession. How bad that recession could be is anyone's guess. The question then becomes, does congress work to extend the deadline before the end of the year, or are actions taken right away to limit its

effect? This congress gives us no reason to believe that it can come together in order to do the right thing. We believe that the US is headed for a possible recession.

3. Slowing Earnings Growth
   a. With corporate profits at all time highs but demand waning at best, earnings growth could go negative over the next few quarters which could create a major correction in the equity markets. With a recession already in progress in the European Union and China slowing, we don't believe that the US will be able to withstand these global economic pressures. The world economy is just too integrated for big economic powers to have a cold and the US not to catch it.

DWCM Performance

The US equity markets had a powerful performance to the upside during Q3. All four major stock indices finished up between 6.6% and 9.4%. However, it was the DWCM Fund that finished higher than any of those indices.

The DWCM Fund was up double digits, returning 10.3% for the quarter. For the year the Fund is up 27.5% almost doubling the performance of the DJIA, S&P 500, and the Russell 2000.

What were the key drivers that led to this performance? We hit on all but one of our strategies that we have been discussing throughout the year which include the following:

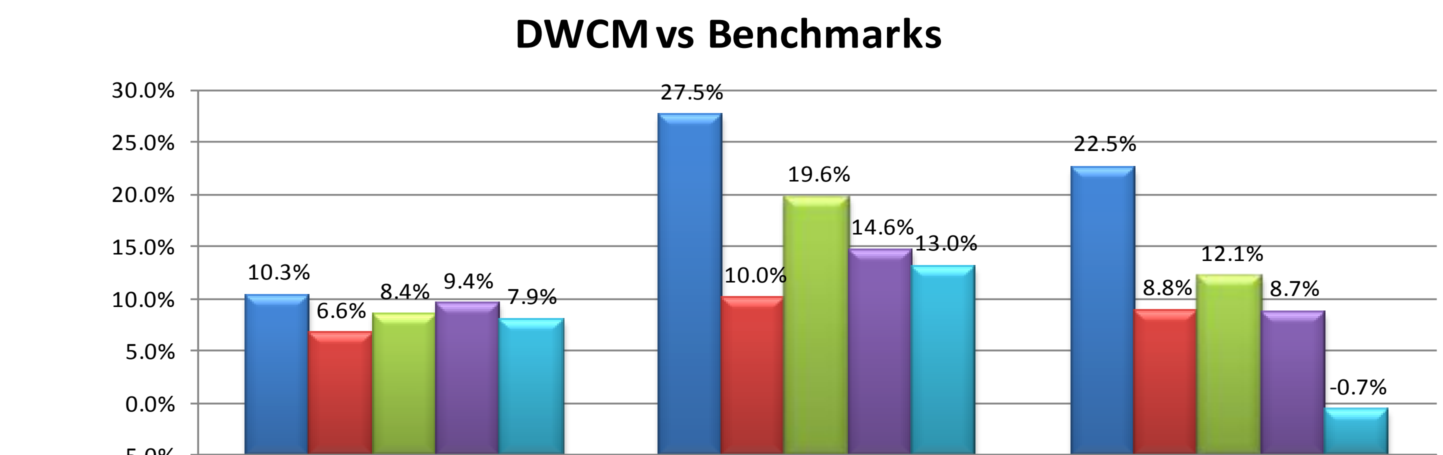
- **Agriculture companies**, feeding a growing and diverse global population. Here companies and farmers are trying to get more output with the same amount of acreage. The severe drought was also a driving force behind some of the price movement up.
- **Dividend paying companies**, but not just any dividend paying company. Those that have a strong balance sheet with little to no debt and produce extreme amounts of cash did the best. Here we diversified ourselves away from just telecoms and into health care, real estate, and energy.
- **The Best Technology companies**, Apple and Google. These two companies are the best at what they do and both turned in phenomenal quarters. It's no surprise that these companies are the largest two holdings within the DWCM Fund.

Top 5 Holdings

1. Apple
2. Google
3. Mosaic
4. Potash
5. Gold (GLD)

Our losses this quarter were basically contained to our short position in a group of 6 home builders. Our belief was that with a weak economic recovery that was not producing enough growth in both jobs and income, people were not going to be able to afford new homes. We also took into consideration what is known as the "shadow inventory" issue where banks are sitting on an undisclosed amount of foreclosed houses because they are not ready to take the losses yet. From a technical analysis perspective, these home builder stocks already had such a huge run up (in some cases near 100%) that a pullback was likely in the cards. Well no such pullback has occurred and the home builders have produced decent returns which have made their stock prices climb even higher.

With plenty of uncertainty abound, what investment strategies will be able to climb this potential “wall of worry”? We are encouraging clients to stay with the game plan we have utilized all year long which is to stay balanced and conservative. Balanced meaning having your core positions in the places we described above which include agricultural companies, solid dividend paying companies, and the a few technology names for growth and speculation purposes, while maintaining a conservative cash position between 30% and 50%.



	2012 Q2	2012 YTD	Since Inception (3/31/11)
DWCM	10.3%	27.5%	22.5%
DJIA	6.6%	10.0%	8.8%
NASDAQ	8.4%	19.6%	12.1%
S&P 500	9.4%	14.6%	8.7%
Russell 2000	7.9%	13.0%	-0.7%

DWCM Quarterly Lecture Update

I want to thank everyone who attended our quarterly finance lecture, *Balancing Your Changing Investment Needs* on September 18th at The Community House in Birmingham, MI. We had a very interactive group and we appreciate everyone's support. We plan to give another lecture in March, 2013

If you are currently trying to develop your own investment plan or are seeking the help of a professional investment advisor we urge you to give us the opportunity to show you what DWCM can do for you. No matter what stage in life you are currently at, DWCM can help you plan for your ever changing needs.

DWCM can you help you with any of the steps in your wealth management journey including:

- Addressing emergency fund needs
- Developing a retirement plan
- Sending a child to college
- Exploring various investment options
- Determining how to involve philanthropic passions as part of your planning process

With our "SMART" principles, we can help you develop your own unique goals and create a focused customized plan to achieve your financial and lifestyle goals.

Paul Fenner is president and founder of DreamWorks Capital Management, LLC (DWCM). DWCM is a Registered Investment Advisor (RIA) servicing individuals, families, and small- and medium-sized businesses.

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