Identifying Opportunity.
Navigating Risk.

Newsletter – February 2010

Our Practice – An Update

Over the past several weeks, we have helped clients transfer their assets to our new platform. We understand that these recent changes may have caused inconvenience to you. It will be our responsibility to show you in the months and years ahead how these changes benefit you. Our hope is that this is the last major change of custody we will ask of our clients. Thank you for your patience, and please contact us to make sure your needs are being met or exceeded by our team.

We have several enhancements to our service offering that we will be implementing in the months to come. 1) We have expanded our dedicated service team with the addition of our new employee, Pamela Weldon, as a Client Service Administrator. Pam most recently worked for State Street Bank, Putnam Investments and Thomas Weisel private client group after graduating from Rogers Williams College, with a major in Financial Services. 2) In the next couple of months, we will be rolling out our new web portal for your accounts, Black Diamond Reporting, and 3) your quarterly performance report at the end of April. 4) Our new website should be completed soon, and we will also have 5) enhanced planning software to assist in evaluating your financial situation and implementing the appropriate strategies.

Planning Opportunity or Not? – The 2010 Roth Decision

Much has been written this year about the opportunity for high income earners who now have the ability to convert their traditional IRAs to Roths while spreading the tax owed over a two year period. For those of you who have heard of this, we are sure you have wondered if this is something for you to consider. We hate to skip to the end, but the 2010 Roth conversion option will not present a compelling opportunity for most of our clients. However, the only way to be sure if this is true for you individually, is to have your CPA run an analysis and to discuss your current financial situation and the results with us. Unfortunately, this is a cumbersome process to follow, but we believe it is the only way to determine the right course of action for each person individually. There is one group of clients for whom it clearly makes sense to pursue an analysis of a Roth Conversion: clients with very long time horizons whose primary interest is wealth transfer between generations. As always, we stand ready to assist you with this process if it interests you.

Investment Perspective – A Look Back at 2009

The early part of 2009 was a continuation of the financial crisis gripping worldwide financial markets and the concern that we were heading into a global depression like the 1930s. Investor fear increased. Bonds traded at historically wide spreads. Stocks were valued at depression levels at 9x trailing earnings, as if bankruptcy was the expectation for some major companies. The selling and shifting into cash climaxed on March 9th as the S&P 500 Index closed at a 14 year low!

By early spring, credit markets, the global economy, and markets started to stabilize. The markets' sudden reversal was astonishing as investor risk appetites went from avoiding risk to seeking risk-a nascent "junk" rally at that point. Stock markets worldwide rallied dramatically through the summer. The S&P 500 Index ended its worst bear market since the 1930s in March, and then made its best nine-month start to a bull market on record. By the end of 2009, markets had posted one of their biggest and most broad-based rallies in years. In fixed income markets, riskier high-yield corporate bonds had their best year ever. Financial market roller coaster rides have rarely, if ever, featured these types of highs and lows within one calendar year.

This table demonstrates the dramatic turnaround for various asset classes with one major exception, residential real estate, which not only was down for the first time in history in 2008 but also produced another down year in 2009; The negative psychological impact to investors, of what is likely their largest asset, haunts them to this day.

MARKET INDICES	2008	2009
DJIA	-32%	23%
S&P 500 Stock	-37%	27%
S&P 400 Stock	-37%	37%
Russell 2000	-34%	27%
EAFE INDEX	-43%	32%
Emerging Markets	-53%	79%
Long-Term Treasury	24%	-13%
Intermediate Treasury	11%	-1%
U.S. Credit Index	3%	8%
Barclays High Yield	-26%	58%
Municipal Bond	-3%	13%
Taxable Money Market	2.00%	0.20%
1 Year CD	2.4%	1.2%
Gold	4%	23%
Residential Real Estate	-8.2%	-3.8%

Sources: Total Returns from WSJ Market Data Group, Russell Investments, MSCI, Standard & Poor's, Barclays, Bankrate.com

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What will 2010 bring?

As we move into 2010, the market volatility has increased, both on the upside and downside. The wild ride of the last two years continues to play out so far this year with the early rally reversing quickly before showing signs of yet another reversal back upwards. Markets are focused on global fiscal issues with Greece's deficits-Portugal and Spain close behind-and the impact to European Union and to global markets. There is a collective mass psychology of primacy bias that what has just occurred, seems most likely to occur again. While not predictive, the likelihood of a 2008 repeat, thankfully, seems remote to us at Shorepoint Capital Partners.

It is relatively easy to present a "Bear Case" with major investor concerns being:

•Debt levels for both private and public sector remain stratospheric with public sector leveraging and private sector just beginning to deleverage
•Big move by stocks suggests corrective phase and valuation stretched relative to 3/09 levels
•Fed beginning its exit strategy and threat of future tightening
•Budget deficit (federal, state and local) outlook horrendous
•Some anti-growth government initiatives (rising taxes, protectionism)
•Commercial real estate losses
•Inflation in China and India/China Tightening credit
•Unemployment rate remains elevated
•Long-term rates rising (affecting mortgage rates)

However, the "Bull Case" is very compelling and outside of the consensus:

•Strong market resiliency considering bad news such as potential Greece default and weak US employment growth
•Unprecedented global stimulus
•Coiled springs for inventories, production and employment
•Pent-up demand building (consumer & business) and housing bottoming
•Foreign economies recovering sharply-global industrial production surging
•Credit markets back to pre-Lehman levels
•Steep yield curve portends expansion
•Booming corporate profits and productivity leading to upward earnings revisions for 2010
•Household net worth now rising
•Inflation remains tame
•Negative investor sentiment is significant, which is positive as a contrarian indicator

We are cautiously optimistic for 2010 and beyond. First, we are contrarian by nature and the prevalent negative sentiment is reassuring to us. Do we have concerns? Yes, but in our 40 years of combined investment experience, we have learned that markets normally do not top when investor sentiment is so negative. To make money in the market, one has to go against the grain. Yes, the U.S. economy is facing many issues (higher taxes, high unemployment, political unrest and fiscal budget challenges) that may result in a slower recovery and subpar domestic economic growth in the near term. However, growth in Emerging Markets—the story of the next 20 years along with energy, water, and other natural resources-can result in positive returns for US global companies which may not be factored into stock valuations**.**

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•We are contrarian by nature…

•Cash flow into bonds is a concern…

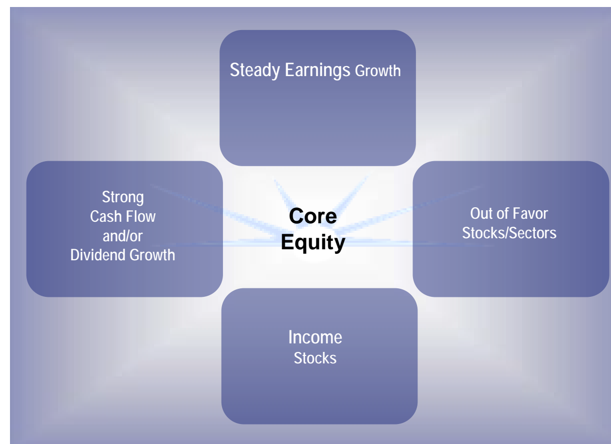
•Ideal time to re-evaluate portfolios and your needs…

•Gradual increase to equities driven by prevailing negative sentiment…

Second, cash flow into fixed income (individual bonds and mutual funds) continues unabated which concerns us. We believe investors were too aggressively positioned, not enough bonds, entering 2008 and did not understand their risk tolerance. If nothing else, 2008 made each of us reevaluate our own risk tolerance. However, the extent of cash flow into bonds is worrisome as investors seem to be chasing yield (money markets yield close to zero) and believe bonds are "safe". The "easy money" in bonds was made in 2009 and some of the major issues highlighted earlier such as the Federal Reserve raising interest rates and the huge budget deficits make bonds less attractive and could result in principal losses. We are not advocating eliminating bonds but investing with caution, shortening maturities and focusing on higher quality bonds. This is an ideal time for us to review and discuss your allocation, make modifications if appropriate, and to develop a plan to implement these changes.

Third, we are gradually increasing the allocation to equities in accounts with our focus on well established global companies with strong earnings potential and the opportunity for dividend growth. When purchased at a reasonable price, we believe these companies will provide superior returns over the long term. The blend of our complementary investment experience uses a:

- Thematic Macroeconomic Approach combined with fundamental analysis
- GARP- expected future growth at a reasonable price
- Focus on high quality global companies with durable competitive advantages whose business models and capital allocation process we understand
- Historically, dividends comprise 40% of total equity returns and help mitigate risk during downturns. Therefore, we generally devote a sizeable portion of the portfolio to companies with above average dividend yields.



In addition, we expect to take advantage of tactical opportunities that present themselves in the current elevated volatility environment in other asset classes such as inflation protected securities, dollar hedged securities, commodities, real estate, etc.

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