



After two tumultuous years, it appears that we as a nation are now emerging from what many are calling the "Great Recession". Many of us remember our parents or grandparents relating stories of how they survived the Great Depression. The Great Recession, though certainly less severe, has impacted all of us in a profound and lasting way. Where we are now and where we are likely to go from here are addressed in this newsletter.

Capital Markets

2009 will be recorded as the year of recovery in the capital markets. The following chart demonstrates the dramatic swings that we experienced over the past two years:

DataBank		
Major Stock Market Indices	2008	2009
Dow Jones Industrial	-39.6%	26.1%
S&P 500 Index	-37.0%	26.5%
NASDAQ Index	-40.5%	43.9%
MSCI EAFE (U.S. Currency)	-45.1%	27.8%
Major Bond Market Indices		
Barcap Long Term Treasury	24.0%	-12.9%
Barcap High Yield Corp Bd	-26.2%	58.2%
Other Asset Class Indices		
Dow Jones U.S. Real Estate	-40.1%	30.8%
Dow Jones UBS Commodity	-35.7%	18.9%

Data is derived from sources believed to be reliable.

As you can see, the rebound in the markets was broad-based. The riskiest of corporate bonds, high yield, made a remarkable turnaround as the flight-to-safety appeal of the long Treasury Bond waned. Non-US equities, U.S. REITs and OTC stocks showed dramatic increases in 2009, after harrowing drops in 2008. And large cap U.S. equities rebounded nicely, though less dramatically than other asset classes.

Despite this perceived "healing" in capital markets, most asset classes have yet to

recover to even 2007 levels. This is based on a simple mathematical fact: a decline followed by an advance of the same percentage does not return an investor to even. In fact, 2008's decline was so severe that the bellweather index of U.S. stock market performance, the S&P 500, was actually lower in value at year-end 2009 than it was at year-end 1999 – resulting in one of the worst 10 year returns in U.S. stock market history.

As we witness the early stages of a recovery, we temper our expectations with the knowledge that the capital markets remain volatile. The lessons learned over the past decade have sharpened our investment focus and portfolio strategies going forward.

Your Portfolio

As you know, your investment portfolio incorporates a broad mix of non-correlated asset classes (i.e., investments that do not necessarily move in concert with each other) and at least one class designed specifically to be negatively correlated with the stock market (short equity). Combined with the selection of top-performing money managers to drive alpha in our portfolios, our goal is to have you own both offensive and defensive positions to deliver competitive returns in both rising and falling markets.

Last year provided a real life test for our approach to asset management: your portfolio held up very well as global markets tumbled through March 9th and yet was able to capture substantial upside once the market turned positive. Your 2009 monthly statements reflect these results.

In general, all of our portfolios were very competitive in 2009 with most finishing either close to or above the performance of their respective benchmarks. We view this as validation of our investment philosophy. Not content to rest on our

achievements, however, we have since conducted an in-depth review of all of our clients' investment portfolios and will be recommending some minor adjustments for 2010.

The Economy

For the first time in nearly two years, Gross Domestic Product grew in the third quarter of 2009 at an annualized rate of 2.2% (*FactSet 11/30/09*). This substantial upward movement, following four consecutive quarters of contraction, was the first indication that the recession may be coming to a close.



Largely responsible for the turnaround in GDP, the Federal Reserve's stimulative monetary policy (begun in late 2008) remains in place. At year-end, the Discount Rate (.50%), the Fed Funds Rate (.11%), and the Prime Lending Rate (3.25%) are all at 15-year lows. In the past, a monetary push of this magnitude has stimulated private and public investment in capital, the lifeblood of our economy. And with the Fed still focused on recession vs. recovery, we anticipate that this aggressive monetary approach will continue through much, if not all, of 2010.

Much of the more recent economic data has been positive, albeit in small increments. Though unemployment remains high at 10.0%, ongoing job losses have begun to slow; and consumer confidence levels have begun to rise from their trough of early 2009. And for the first time in over two years, the year-over-year percentage change in retail sales recorded a positive .28% (*FactSet 11/30/09*). Now while it is still too early to tell whether American consumers will contribute to the growth of the economy in 2010, we are optimistic.



Strategic Thinking

Given our current assessment of the capital markets and the global economy, we join the consensus of strategists that believe the markets will be generally positive over 2010 and beyond. However, we also believe that market volatility will remain with us, i.e., returns will never be predictable or linear.

In December, we reviewed our current allocations and investment positions. We stress-tested our assumptions across a wealth of economic and market data. We applied time-tested metrics to measure the performance of our money managers through both bull and bear markets. Finally, we back-tested our allocations over each year of the past decade. The end result is that we are recommending some minor adjustments to your portfolio going forward. In fact, we plan to add a couple of asset classes and to replace a few managers as we rebalance your portfolio. We believe that rebalancing will permit us to manage risk in your portfolio more effectively and ideally, deliver even more competitive returns going forward. Of course, since past performance is no guarantee of future results, we cannot guarantee that any of our recommended adjustments will be effective.

Nonetheless, we remain convinced that a balanced approach to investing, i.e., mixing a sound defense with a solid offense, remains the most prudent way to mitigate risk and produce solid returns for our clients. The results of 2009 provided empirical evidence that we can indeed design portfolios that offer both downside hedging and upside potential.

Investor Psychology

In recent months, we have begun to see our clients' perspectives on the markets improve. Much of this change is a result of perceptions in their own world. Friends and family seem to have weathered the economic storm. The fear of a loss of

income has waned. People are generally more confident and less pessimistic than say, a year ago.

Nevertheless, the Great Recession has had a sobering effect on investors. Many investors will not soon forget the horror of plummeting asset values; and this has led to two decidedly different perspectives.

The first perspective is the "I have to get it back now" investor. His "emotional meter" has swung away from fear and toward greed. This investor wants to take more risk in an attempt to makeup ground. Prudent risk management is viewed as being detrimental to this goal; he has forgotten the lessons of the recent past.

The second perspective is the "just don't lose any more" investor. This investor is paralyzed by fear and the prospect of another downturn. Any reduction in asset value is viewed as being permanent. The overwhelming focus is on risk reduction, even if expected returns approach zero. This investor has forgotten the lessons learned over decades of history.

We know that the bulk of our clients fall in the middle of these two mindsets, and we are thankful for that. Our clients tend to recognize that rebounds in asset values are gained incrementally over time. They also recognize that to eliminate market risk at any cost is, in-fact, a huge risk to long-term financial success. In short, most of our clients are now taking a rational approach to investing; one where reason trumps emotion and ultimately leads to long-term success.

Impact on You

Once again, we have taken great care to design your portfolio to take advantage of strategic and tactical opportunities. Please do not hesitate to call your financial advisor or any member of our team to discuss your perspectives and ask questions. As said before, we have strong convictions about the advice we

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offer, but ultimately you must decide if our approach is suitable to your wants and needs as an investor. Lastly, we appreciate the trust and confidence you have placed in us. We hope to continue to reinforce your faith in our work and we look forward to building a growing relationship for years to come.

Upcoming Events!

Our next **Client Update Session** is planned for late April 2010. This presentation will provide deeper insights into our thinking and will include a question & answer period. Look for your invitation as the date draws nearer.

We are also in the process of planning our annual **Baseball Outing**. This is a great opportunity for our clients and their families to enjoy a ballgame and some good summer fun. We are currently planning the event for late-May or early June and will keep you updated as the date draws nearer. Remember, winter won't last forever!

