Quarterly Market Update

SEPTEMBER 30, 2010

The "Summer of Recovery" turned out to be an apt description of capital markets, propelled in large measure by the best equity index investment results for the month of September since 1939. It nearly reversed the double digit decline recorded by virtually all equity indices during the 2nd quarter of 2010. In fixed income markets, the 10 year Treasury continued its decline in yield, closing at 2.51%, down 45 basis points from the June 30 level.

Whereas the macroeconomic concerns of the second quarter, surrounding European sovereign debt, seemed allayed or at least reduced, third quarter ebullience seemed centered on merger and acquisition activity. Even with interest rates at the lowest levels since the Post World War II accommodation between the Federal Reserve and the Treasury, there was very little activity related to taking public firms private via a leveraged buyout. There were, however, a significant number of large companies utilizing substantial cash resources to acquire smaller companies.

Concurrently, there has been a continuing net outflow of funds from equity oriented mutual funds towards fixed income oriented mutual funds. This was caused by the combination of sluggish growth in the economy, persistently high unemployment rates, and lowered consumer confidence. Gold continues to hit new highs. The Exchange Traded Fund (GLD) that emulates the price of gold has experienced huge increases in size and may well be the investment of choice for risk averse investors.

With the benefit of hindsight, many market commentators have indicated that the best performing stocks in the Dow Jones Industrials have above average dividend yields. Of course, the best way to participate in that outperformance is to have made that judgment before the year began. Fortunately for us, that is one of the criteria we use in evaluating individual equities for clients. During the 3rd quarter our composite rose by roughly 200 basis points more than the S&P 500, bringing our cumulative outperformance this year to about 700 basis points.

We continue to believe that fixed income securities are extraordinarily risky and should be minimized in portfolios. Our expectation is that equity markets will continue to provide positive returns from current levels through the end of 2011.

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