

June 2011 Newsletter

Quick Update

Currently the stock market is rightly focused on the many risks emanating from the macro environment. The European debt crisis is once again flaring up, there is inflation and social unrest in emerging markets, especially China, and domestically our economy has slowed dramatically while unemployment remains elevated. Most of these conditions were peccating well before the stock market started its decline in early May. **We took advantage of that period to reduce risk in our portfolios by selling some stocks, especially the more cyclically oriented companies. As a result our portfolios are holding up better than their benchmarks in the current correction.**

Despite our macro concerns it is important not to panic and lose sight of many attractive opportunities in the stock market. High quality stocks are outperforming: Since the beginning of the year, the large-cap Russell 1000 is up 1.95% while the small-cap Russell 2000 is up 0.23%. Health care has been the S&P 500's best sector. During the decline, while every sector is down, the narrowest losses have been in consumer staples and health care while financials and industrial have seen the widest losses.

We are in a unique period of time where an investor can own very high-quality stocks and **generate a sustainable and growing income stream** well above money markets and even on par with medium term U.S. Treasury securities. Our current portfolio of stocks (for this discussion we are not including the ETFs) **is yielding just over 3%** despite having over 20% of the companies with no or very low yields. Valuations are extremely attractive with the average Price to Earnings ratio of only 12x. Best of all, we are not taking balance sheet risk to achieve this yield as our companies sport very high credit ratings.

High-quality stocks have been largely ignored by investors who have chased the momentum in small capitalization stocks over the past decade. We believe this asset class is underrepresented in institutional portfolios and will benefit as this group rediscovers the value in this area.

As we end the quarter it is a good time to review your risk expectations relative to your allocation to stocks and fixed income. We make "risk" adjustments in portfolios relative to our outlook for stocks. We are able to be nimble but investors should review their exposure to stocks and evaluate their suitability relative to the market and their specific needs. We would be happy to discuss your situation especially if you have a change in lifestyle or income needs.

James G. Tillar, CFA, Steve Wenstrup