Inside Views From an Investment Management Leader

UPDATE

October 2011

About our Company

Company Profile:

Concord Investment Counsel is a private, boutique investment firm who has helped our clients grow and protect their wealth since 1991.

Key Offerings:

- *Personal wealth management*
- *Proactive investment strategies*
- *Proprietary research*
- *A professional team*
- *Fee-only services*

Distinguishing Values:

- *Passion for excellence*
- *Strategic focus*
- *A disciplined process*
- *Prudent risk management*
- *Comprehensive client care*
- *Superior long-term performance*
- *Sound judgment*
- *Objective Analysis*

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Economic & Financial Market Review & Outlook

Volatility in Markets & Economic Data

Mitch Pletcher
President
Chief Investment Officer

Quick and easy methods to change investment portfolios combined with turbulence in the global economy have produced near record volatility in financial asset prices. Stocks had their worst quarter since 2009, finishing down over 13% after a volatile quarter of optimism and pessimism (figure 1 below), as well as changing trends in economic data. Treasuries found another leg higher as weak economic data points helped a highly valued market move to extreme levels. Ten-year notes dropped to sub 2% levels and 30-yr paper fell to yields below 3.0%. Gold finally stumbled after a very long period of steady gains(figure 1 below). The gold selloff was likely tied to the Fed's decision to not pursue a new program of quantitative easing but instead announced Operation Twist which will redirect existing investments into longer maturities.

Distressed debt had a good quarter relative to equities, with modest losses of principal offset by high yields. The increasing level of volatility has created a lot of concern for investors. Many of us are wondering what's behind the rising tide of volatility. Is it tied to the problems in our financial markets or is it just the result of investors having the ability to change their portfolios with little effort or cost? While nothing is certain it would seem that the latter is the cause.

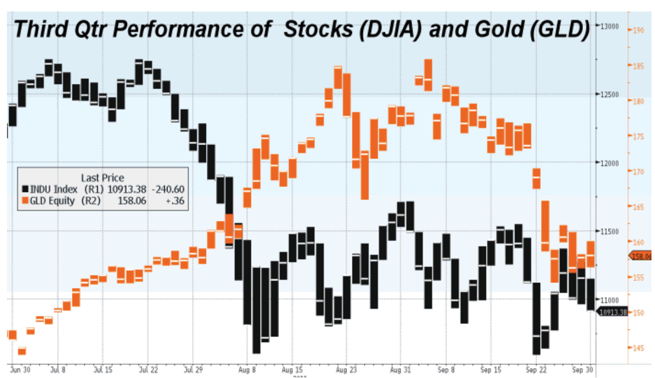


Figure 1 - Source: Bloomberg Financial

The stumbling global economy is difficult for investors to discount into current market values. Recent data shows the US economy has noticeably softened (ISM charts page 5). The strong revival in consumer spending has slowed after 14 months of steady gains. Personal Consumption (fig 5 pg 4)however has continued to rise despite low confidence. Employment gains were never that good (200K/month), but now job creation has fallen flat. Generally, economic trends in the US are soft and concerning. Trends elsewhere are both good and bad. The good is mostly in the BRIC (Brazil, Russia, India, & China), while the bad is centered in Western Europe. Western Europe's problems are tied to their socialistic ways and lack of quick action to reduce costs during this difficult period. Debt has been used to stimulate and carry on consumption in most parts of the Eurozone. Countries whose economies are tied heavily to tourism, like Italy and Greece, have seen little improvement in their growth picture. Germany, the UK, and France have done much better as stimulation there has had some success on these more industrial based economies, and it appears these economies are on a path of growth. The weak players in the Eurozone cannot use debt any longer as markets will not loan them money, given their debt to GDP ratios of 1 or more. The problems in Greece are not significant in themselves as Greece is a very small country, accounting for only 1.8% of the GDP of the Eurozone. Their government debt is very small in relative terms (330 billion Euros) and is spread broadly across many investors. The real concern about the PIG (Portugal, Ireland & Greece) amongst investors is whether the PIG is a model of similar problems around the globe.

Outside of Europe, the economic picture is a bit better. In the US the actions of consumers are much better than confidence surveys indicate, with consumption data pausing but at all time highs. The industrial sector likewise has experienced a strong recovery but seems reliant on the continued strength in the BRIC which has slowed but is still strong in relative terms. These economies are now big enough today to make meaningful consumption for US global players.

Central bank policy has been the solution to economic problems for the last thirty years in America. Today economists believe we are in a different environment in that the problems we have now are largely due to the past policies of central banks (using liquidity to stimulate and

(Continued on bottom of Page 2)

Table 1: Stock & Bond Market Returns — 9/30/11

	Quarterly Change	Trailing 12 Mos		Quarterly Change	Trailing 12 Mos
Large Cap Growth (IWF)	-13.1%	3.7%	Small Cap Value (IWN)	-21.5%	-6.2%
Large Cap Value (IWD)	-16.2%	-2.0%	Small Cap Growth (IWO)	-22.3%	-1.0%
Europe Asia Far East (EFA)	-20.6%	-10.5%	Emerging Markets (EEM)	-26.3%	-20.2%
Invest Grade Bonds (LQD)	3.1%	4.0%	High Yield Bonds (HYG)	-7.6%	-0.3%
Interm Treasuries (IEF)	10.4%	9.3%	Mortgage Bonds (MBB)	2.3%	5.1%

Source: Bloomberg, Barclay's Global Investors ETFs. Actual performance including dividends.

Table 2: Real Estate & Commodity Returns — 9/30/11

	Quarterly Change	Trailing 12 Mos		Quarterly Change	Trailing 12 Mos
DJ US Real Estate (IYR)	-15.2%	-0.6%	DJ Commodity Index (DJP)	-11.6%	-1.3%
NAREIT Industrial/Ofc (FNIO)	-19.6%	-4.4%	Goldman Commodity (GSG)	-11.5%	0.6%
NAREIT Residential (REZ)	-9.0%	7.2%	Gold (GLD)	8.3%	23.6%

Source: Bloomberg, Barclay's Global Investors ETFs. Actual performance including dividends.

Table 3: Case-Shiller Home Price Index — 7/31/95 - 7/31/11

Last 90 Days (4/30/11 - 7/31/11)	2.9%	Last 12 months (7/31/10 - 7/31/11)	-3.7%

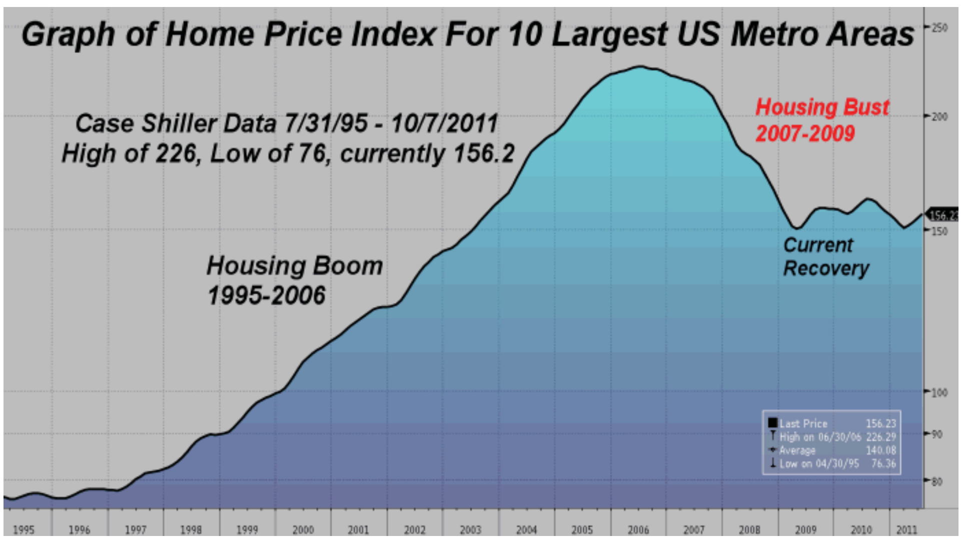


Figure 6 - Source: Bloomberg Financial

Economic and Financial Market Update

From Page 1

never tightening liquidity once growth was sustainable) for the last three decades. Most central banks around the globe can no longer stimulate as debt to GDP is too high. The US is an exception, but we have a limit to what the Fed can reasonably do. The likely solution to our problems is austerity and slow growth as we and the developed world deleverage ourselves. The emerging world will help us through the difficult period ahead of us with steady consumption from their now large and growing economies that are mostly debt free. The financial markets will eventually become satisfied with the reality of the growth picture and valuations in risk assets, which are quite compelling on a relative basis to non-risk assets and will be bought again. Volatility will ultimately decline as well.

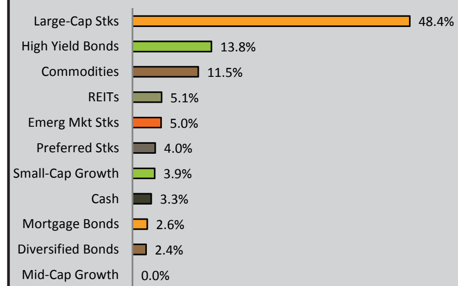
The current outlook for the growth, inflation, and interest rates is never easy to forecast. In the past the bond market has been a good indicator. The treasury market seems to be telling us that a long period of slow growth or no growth is ahead. Today ten year treasuries are yielding 1.8% and thirty-year paper is at 2.8%. This would normally be seen during a bad recession or a period of no growth. However, rates are not likely at these levels because of what investors are doing. It seems more likely that rates are where they are because of the $2 trillion the Fed has printed and used to purchase treasuries. Further confirmation of this is the rate of current inflation which is about 3%. This inflation rate gives treasuries a negative real return if this inflation persists. We conclude that the bond market today is not a good indicator of expectations for growth, given how the Fed is currently manipulating it. The majority of Economists surveyed by the WSJ still believe we are in a recovery that has only slowed a bit.

CIC Managed Accounts

Growth Portfolios

Dynamic Growth

A dynamic blend of stocks, bonds, commodities, REITs, and cash for growth investors with a bias toward timely asset classes.

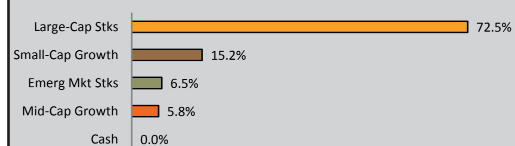


Growth

A portfolio of large- and mid-cap US stocks that are industry leaders with strong brands and timely products.

Diversified Equity

A global, all-cap equity portfolio following economic trends across capitalization and geographic ranges.



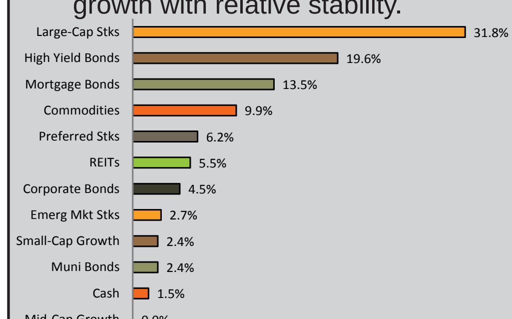
Focused REIT

A portfolio of companies whose primary business is owning and leasing real properties.

Balanced Portfolios

Asset Allocation for Income

A portfolio of stocks, bonds, and cash for moderately-conservative investors seeking income and growth with relative stability.



Equity Markets: Consumption Drives Growth

Earnings growth drives leadership in the stock market, while consumption generally drives earnings. Every market cycle has consumption themes which are either secular or cyclical in nature. Here's what is active in this market cycle.

Secular Consumption Themes:

- **Theme:** Global demand for wireless devices, digital media and cloud computing power. Demand growth is a product of industry's ability to innovate. Sector: Technology
- **Theme:** Global demand from wealthier and growing emerging market populations for meat and poultry to support more "western-like" eating habits, as well as growing demand for technologies that provide greater agricultural yields.

  Sector: Materials
- **Theme:** Global demand for energy as population grows as well as increasing demand for the technologies that make it viable to extract natural resources from the farthest reaches of the earth. Sector: Energy
- **Theme:** Increasing demand for healthcare as population ages, as well as growing demand for new and better products provided by innovation in the development of life-saving drugs, devices, and services. Sector: Healthcare

Cyclical Consumption Themes:

- **Theme:** The return of mild consumer discretionary spending balanced against purchasing decisions based on need instead of want. Sector: Consumer Discretionary/Staples
- **Theme:** Pent-up demand within the enterprise upgrade cycle. Sector: Technology
- **Theme:** The re-surfacing of emerging market infrastructure spending. Sector: Industrials
- **Theme:** Credit market stabilization and a return of demand for investment banking products and services. Sector: Financials
- **Theme:** The return of demand for manufactured products.

  Sector: Industrials, Energy

Commentary: Energy, Staples, Healthcare, and industrial Equipment

The slow growing US economy is demanding more defensive items like healthcare, staples, energy, and food. Cyclical rebounds in apparel and leisure are also occurring, but durable items have not rebounded to post recession levels. The demand for technology has also occurred but is not as strong as many had predicted and has been overshadowed by growing global demand for raw materials, industrial equipment and agriculture. Financial services have also underperformed expectations as global financial service demand has been weak but recovering.

Sector Performance Review *9/30/11*

	Quarterly Change	Trailing 12-Months
Utilities	0.3%	11.7%
Consumer Staples	-4.4%	10.6%
Telecom	-9.0%	3.7%
Technology	-9.1%	3.4%
Healthcare	-11.0%	6.1%
Consumer Discretionary	-14.3%	5.4%
Energy	-21.2%	6.3%
Industrials	-21.9%	-4.9%
Financials	-22.1%	-15.4%
Materials	-24.8%	-6.8%

Data based upon Russell 1000 Index and GICS sectors. Source: Bloomberg Financial

Asset Class Review

By Kyle Aron

Divergence in the Bond Market

Fixed income in general has outperformed equities, commodities, and real estate over the last 5 months of turmoil in the markets. The best returns, however, came in the area that seemed the most overvalued before the recent market crisis began – long-term Treasuries. This trend has been going on since the financial crisis began in 2008 and a significant performance rift has developed between risk assets and perceived non risk assets. High yielding, lower credit quality fixed income and low yielding high credit quality Treasuries and investment grade bonds are the assets we have seen diverge in price and yield. Continued participation by the Federal Reserve in the Treasury market has helped Treasuries reach record prices and historically low yields. Market turbulence has also induced investors to flee lower quality debt instruments. We are wary that there may be little upside left in high quality fixed income and believe considerable selling pressures are looming on the horizon. The Fed's presence in the Treasury market will diminish once the economy gets through this current period of weakness. Given these reasonable forecasts, we find better risk/reward in the higher yielding segments of the fixed income market.

Lower quality, high yield debt has unfortunately fallen victim of late to the stubborn economic throes that have plagued the world economy and markets throughout the second half of 2011. As concern has risen about the ability for global economies to continue to recover, fear of the default by distressed debtors has resulted in a marked selloff of lower quality debt worldwide. However, we remain of the opinion that such economic ebbs and flows are merely part of the bumpy road to recovery. Strong corporate earnings are reassuring that lower quality corporate debt is perhaps undeservedly being sold-off and is of good relative value under current circumstances. As the global economy and markets settle, high yield debt will likely see high total returns and will outperform high quality debt.

Preferred stocks are generally considered a fixed income asset and have done well through the downturn, but they have poor relative performance to treasuries. This is due in large part to their issue mainly from the financial sector. As banks continue to struggle though the aftermath of the recession, investors have had little confidence in their strength even though it is highly unlikely that the Fed will let another major bank go down. It is our view that there will continue to be dark clouds above this segment. Downtrodden as they may be, preferred stocks have good relative value because of their high yields.

Emerging market government debt is another high yielding area we feel has a desirable risk/reward outlook. Emerging markets are typically export-based economies with low government debt-to-GDP ratios. Given their strength through the recession and manageable government debt levels, we expect emerging economies to continue to do well in the current environment and accelerate to the upside as the developed world strengthens. With credit ratings slightly better on average than high-yield US corporate debt, emerging market government debt provides high yield with better credit quality. Further, the ability to purchase US Dollar-denominated emerging market debt provides a hedge against foreign currency inflation.

A Word from Our Advisory Team

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What about market timing?

Economic uncertainty. Volatile markets. Abundant index funds. Ease of trading. Taken together, these elements offer investors the ability to indulge a long-standing tendency – market timing. In an era when crazy financial markets almost feel normal, the past quarter netted a 12-14% decline in major US indices, with weekly swings of 4-7%. This summer, attention bounced between America to Europe and moods shifted from hopeful to dreary to encouraged to dismal. Such a setting may be the new normal for the time being. In the grip of it all, armed with keyboards and touchscreens, what are investors to do? It seems many trade index funds, buying when they sense a bargain and selling when they're scared.

The 21st Century has given us access to markets and ways to trade them that never existed before, imparting the basic tools to build wealth across the masses. But if people can trade markets more easily than ever, are they successful in practice? The answer appears to be "no." The latest annual DALBAR study from April 2011 shows investor returns lagged the market itself. Their research illustrates that over a 20-year period, equity investors earned 3.8% compared to the S&P 500 return of 9.1%. Average equity investor retention or holding time was just 3.3 years. It seems people have the tools to invest wisely but are too flighty to stick it out. Add trading costs to buying high and selling low and the result is wealth erosion.

John Bogle can say he told us so. In his book "Don't Count on It!" the father of the index fund says, "The simple broad market index fund of yore, which I believe is the greatest medium for long-term investing ever designed by the mind of man, has now been engineered for use in short-term speculation." He says even if you're right about the market some of the time, you won't be all of the time, and you'll get into trouble.

But what good is a static, buy-and-hold approach when you have a lost decade in stocks like the last one? Your wealth management team at Concord believes the answer is neither risky market timing nor plodding buy-and-hold. In fact, a hallmark of our firm is to invest in what's timely, so we employ research for active management based on economic trends. Since market moves can be deceiving, we gauge ongoing portfolio adjustments on established economic data. This makes our management dynamic and offers protection from market head-fakes.

Twenty years of solid results in helping our clients achieve their goals is evidence enough that our strategy works, but a study by NYU Stern School of Business offers further validation. According to David Hoffman in InvestmentNews on 11/10/2009, "The fund managers who invest based on macroeconomic trends – and are willing to adjust their portfolios as those trends change – are the managers most likely to add value for investors." One finance professor at NYU says, "Our work suggests that individuals should be looking for a different type of investment manager, one that invests based on macro information."

This newsletter is a good resource for knowing what we think is timely – but please give us a call if you'd like a closer look.

Economic Charts

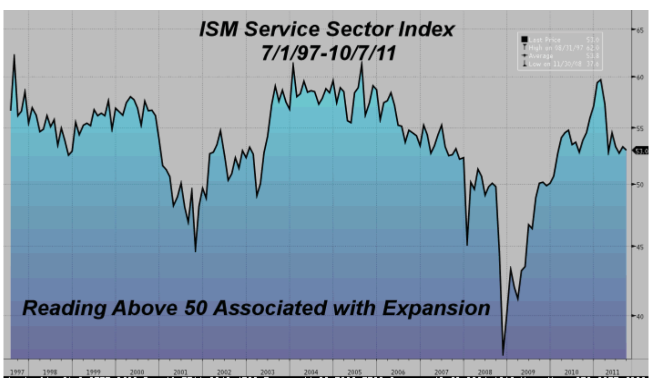

Figure 2 - Source: Bloomberg Financial

Purchasing managers survey of service sector showing sharp recovery and than some weakness.

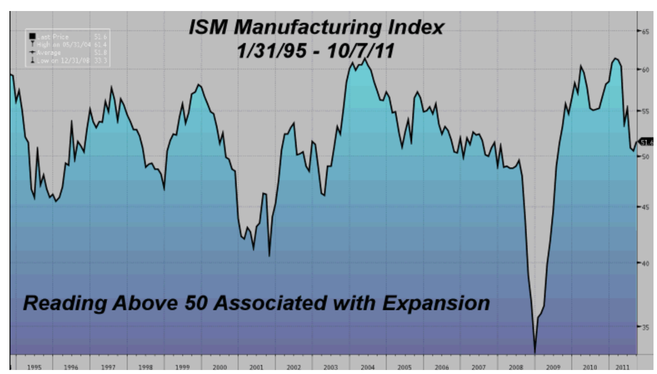

Figure 3 - Source: Bloomberg Financial

Purchasing managers survey of manufacturing sector showing sharp recovery and than some weakness.

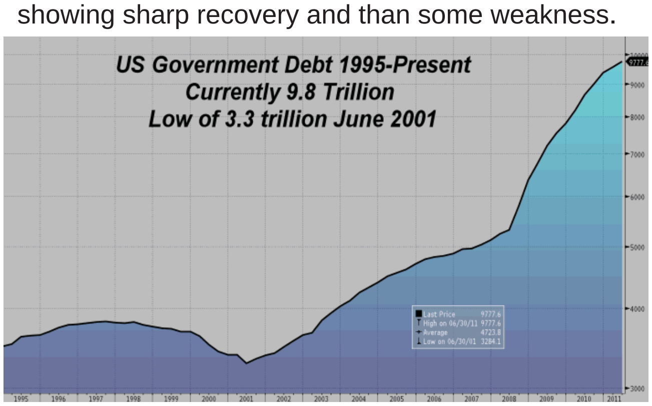

Figure 4 - Source: Bloomberg Financial

Us Government debt buildup over the last 5 years.

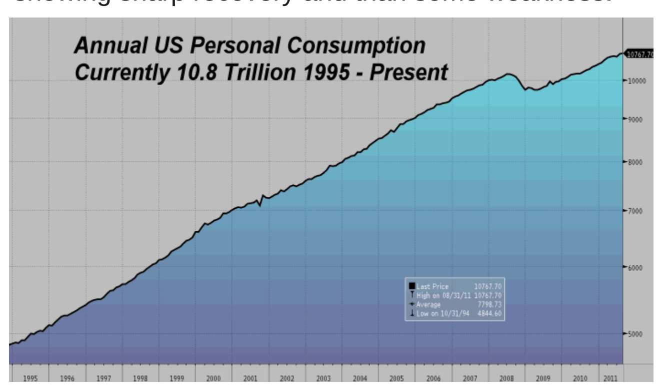

Figure 5 - Source: Bloomberg Financial

Personal Consumption Index showing steady improvement from first major setback in 2008.