

Nauset Market Commentary Third Quarter 2010

Market Performance Recap: Stocks Rise on “Less Worse” Economy

A sharp rally in September reversed August weakness in the stock market and pushed returns to positive territory for the year. Evidence of a stabilizing US economy and promises of more help from the Federal Reserve encouraged investors. U.S. stocks shot up over +11% across most indices, including international stocks. Bonds also benefitted, especially high yield securities, as the Barclays Intermediate Gov./Credit Bond Index rose +2.8%. See table for details.

Economic & Market Discussion: Following the Fed

Investors are bullish on the Fed’s plan to stimulate the economy through quantitative easing. Let’s examine the implications of the plan for the economy and markets.

The role of the Fed is to maximize employment and stabilize prices. Through quantitative easing – asset purchases to increase money supply – the Fed is really battling deflation. By reflating the US economy, the Fed hopes to promote a manageable level of inflation that can benefit corporations and boost employment. Our view is that the Fed is trying to create a fight it feels it can win – one of inflation. We would rather that the Fed and its political supporters focus on creating more certainty around business costs and demand growth.

Regardless of one’s view, the Fed’s plan will likely reflate prices in the short term, which can benefit riskier assets like stocks over Treasuries. However, we could see a market correction if the Plan does not work or creates unintended negative consequences, such as a much weaker US dollar.

Therefore, we are wary of market volatility and are focusing on investments in the following areas: High quality stocks with strong earnings, income-producing stocks, emerging markets securities, and alternative investments like commodities. We will actively manage your portfolio to favor these opportunities while monitoring and managing overall risk.

Market Performance Index	% Change for Periods Ended 9/30/2010				
	Third Quarter	2010 Year-to-Date	1-Year	3-Year Annualized	5-Year Annualized
Dow Jones US Total Mkt.	11.53	4.78	10.96	-6.59	0.92
S&P 500	11.29	3.89	10.16	-7.16	0.64
MSCI EAFE – Non-US	15.79	-1.25	0.53	-12.12	-0.72
BarCap Intermediate Gov’t/Credit Bond	2.76	7.44	7.77	6.93	5.95
BarCap Municipal Bond	3.40	6.83	5.81	6.04	5.13
3-Month T-Bill	0.04	0.09	0.12	1.01	2.48