

## Nauset Market Commentary Fourth Quarter 2010

### Market Performance Recap: **Stocks Strongly Higher, Bonds Dip**

Stocks closed the year with a flourish, up +11.6% for Q4, and +16.9% for 2010 as measured by the Dow Jones Total Market Index. Riskier small and mid cap stocks paced results as investors were buoyed by improved economic reports. International results lagged as the MSCI EAFE Index posted +4.9% gains for 2010. Bonds suffered Q4 losses as Treasuries sold off amid deficit concerns. However, Barclays Intermediate Gov/Credit Index was up +5.9% on the year.

### Economic & Market Discussion: **Will the Beat Go On?**

In our annual outlook, we examine the three factors that we believe determine the general direction of US stock prices - interest rates, corporate profits and valuation levels.

- Interest Rates – We expect interest rates to rise from their low base, continuing the Q4 trend in government bond interest rates. This is a slight negative for stocks.
- Corporate Profits – We see overall profits in a moderate range, close to historic averages of 10%; a plus for stocks.
- Market Valuation – We believe that the market is fairly valued, which is a neutral for the market. However, as at the beginning of 2010, we like the risk-reward profile of stocks as compared to those of cash and fixed income.

In summary, we are positive, though cautious, on stocks given the economy's slow forward momentum. Gains are likely to be muted by housing and unemployment headwinds, and possible negative effects of the Fed's money policies. Additionally, any of these factors could lead to a market correction in coming months after the +20% six-month rally.

Our current investment strategy emphasizes: high dividend stocks, growth areas like tech and emerging markets, energy and commodities, hedged equity investments, and defensive bonds investments in a rising rate environment – floating rate and inflation-protected bonds, and hedged fixed income.

Market Performance Index	% Change for Periods Ended 12/31/2010			
	Fourth Quarter	2010	3-Year Annualized	5-Year Annualized
Dow Jones US Total Mkt.	11.59	16.93	-2.01	2.74
S&P 500	10.76	15.06	-2.86	2.29
MSCI EAFE – Non-US	6.23	4.90	-9.72	-0.26
BarCap Intermediate Gov't/Credit Bond	-1.44	5.89	5.40	5.53
BarCap Municipal Bond	-4.17	2.38	4.08	4.09
3-Month T-Bill	0.04	0.13	0.69	2.30