

	Market Returns			Market Returns			
	YTD	February	2009		YTD	February	2009
DJIA	-1.0%	+2.6%	18.8%	MSCI EAFE	-5.3%	-0.9%	27.8%
S&P 500	-1.0%	+2.8%	23.5%	MSCI Emerg Markets	-5.4%	+0.3%	74.5%

February This year US markets have led foreign markets, reversing last year's trend. The MSCI EAFE (Europe, Australasia and the Far East) Index was held back because European nations are dealing with Greece's economic woes. The European Monetary Union markets have declined 10.3% year-to-date and 3.7% last month alone. Emerging markets performed better, eking out a small gain in February. MCSI Emerging Market's Index was held back in part by its Asian members, as investors fear that China's "tapping of the brakes" on their economy may be a sign of a bubble brewing.

S&P 500's LOST DECADE S&P 500 companies reported average fourth quarter earnings that beat consensus analyst estimates by 12%, yet the S&P 500 has lost 1.0% year-to-date. Robert Barbera, chief economist at independent research firm, Investment Technologies Group, estimates that the level of corporate profits in the National Income and Product Accounts, a measure of general economic activity kept by the Department of Commerce, was nearly 85% higher in 2009's fourth quarter than in Q-4 1998. Meanwhile, the S&P 500 was about 7% lower at the end of 2009 than in 1998. This indicates the market, which went on to add another 19% in 1999, was either terribly overpriced at the end of 1998, or seriously undervalued at the end of 2009. We think the truth is somewhere in between.

NORMAL VOLATILITY Citigroup Global Markets reports: "Since 1928, the S&P 500 has returned an average of 9% per year. In doing so, it has also averaged 3.5 price corrections per year of 5% or more, reflecting the normal ups and downs of volatility. Pullbacks of 10% or more occur roughly once a year... Pullbacks of 20% or more generally are considered 'bear markets,' and occur about once every three years." Market volatility is not new. These numbers underscore market timing's futility, where one must guess right on multiple short-term oscillations to make any money. It also shows January's market correction was a normal, albeit unpredictable, occurrence. We don't believe it will get much worse. The last two Market Commentaries presented our bullish case (well below average 10-year return on the S&P 500, mutual fund flows into fixed income funds far exceeding flows to stock funds, and ultra-low interest rates). Citigroup goes on to say the usual suspects that cause a bear market; tight monetary policy forcing a recession, overly bullish investor sentiment, problematic inflation, and inflated stock market valuations, which are most certainly not in evidence today.

Purchasing Power of \$1.00				
Annual Inflation Rate	After 1 year	After 5 years	After 10 years	After 20 years
1%	\$ 0.99	\$ 0.95	\$ 0.90	\$ 0.82
2%	\$ 0.98	\$ 0.90	\$ 0.82	\$ 0.67
3%	\$ 0.97	\$ 0.86	\$ 0.74	\$ 0.54
4%	\$ 0.96	\$ 0.82	\$ 0.66	\$ 0.44
5%	\$ 0.95	\$ 0.77	\$ 0.60	\$ 0.36
6%	\$ 0.94	\$ 0.73	\$ 0.54	\$ 0.29
7%	\$ 0.93	\$ 0.70	\$ 0.48	\$ 0.23
8%	\$ 0.92	\$ 0.66	\$ 0.43	\$ 0.19
9%	\$ 0.91	\$ 0.62	\$ 0.39	\$ 0.15
10%	\$ 0.90	\$ 0.59	\$ 0.35	\$ 0.12
12%	\$ 0.88	\$ 0.53	\$ 0.28	\$ 0.08
15%	\$ 0.85	\$ 0.44	\$ 0.20	\$ 0.04

FIDUCIARY RESPONSIBILITY & STOCKS Given their volatility, investing client funds in equities may seem in conflict with a fiduciary's responsibility to protect client assets. However, as a hedge against the ravaging effects of inflation, having a portion of one's portfolio in stocks is prudent. Fixed income investors are most vulnerable to the effects of inflation, as their investment pays only income with generally no appreciation. A little inflation is good for both bankers and the Fed, as it protects the value of assets serving as collateral. In a perfect world, a 1% annual rate would suffice, but in an uncertain world, 2.5% is safer and closer to the Federal Reserve's target. At that modest rate, a dollar's purchasing power in 10 years shrinks to \$0.78, and to \$0.60 in 20 years. As a rule of thumb, we recommend a minimum 30% equity allocation to keep up with inflation.

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Norwalk and Sandusky • 888.645.4121 • www.CitizensWM.com
Dublin and Urbana • 800.604.9368 • www.CWealthManagement.com

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