

A Look Into 2011

Building on 2010

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General Thesis

- The economic recovery has become self-sustaining
- Corporations are lean and have the ability to grow earnings at 10%+ per year
- The consumer is in far better shape today
- Retail investors are yet to re-engage equities
- Equities remain reasonably valued
- We are positive on 2011



THE ECONOMY



Where We Were



Where We Are Today



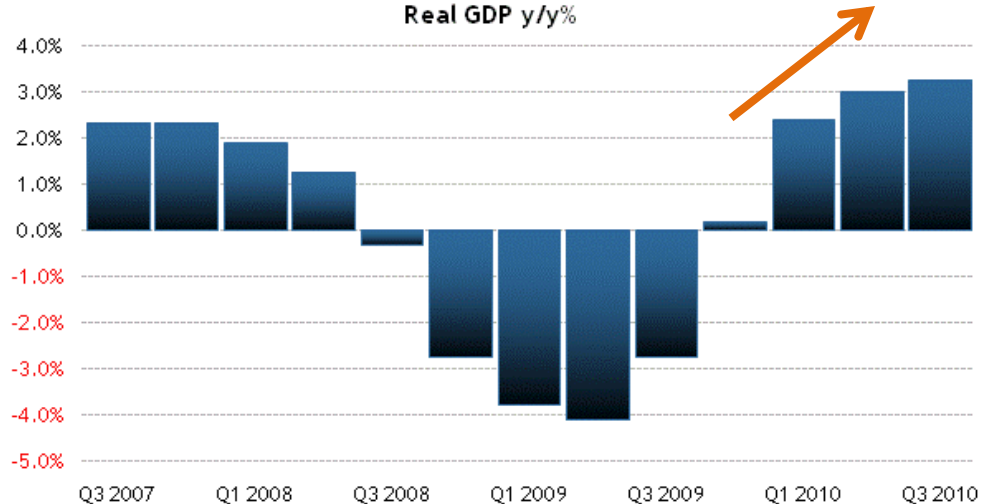
A0NDKC Alamy Images

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Double Dip?

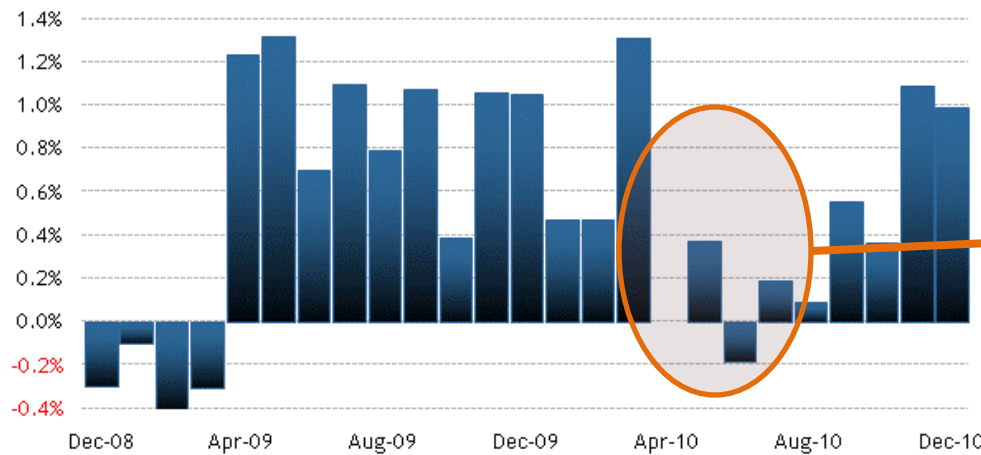
- Real GDP continues to improve
- “Double Dip” that everyone feared never materialized
- Leading indicators reaccelerating



Source: Bureau of Economic Analysis; updated 11/23/10

Briefing.com

Leading Indicators m/m%



Fears of “Double Dip” cause S&P 500 to decline ~16% from April –July 2010

Source: Conference Board; updated 01/20/11

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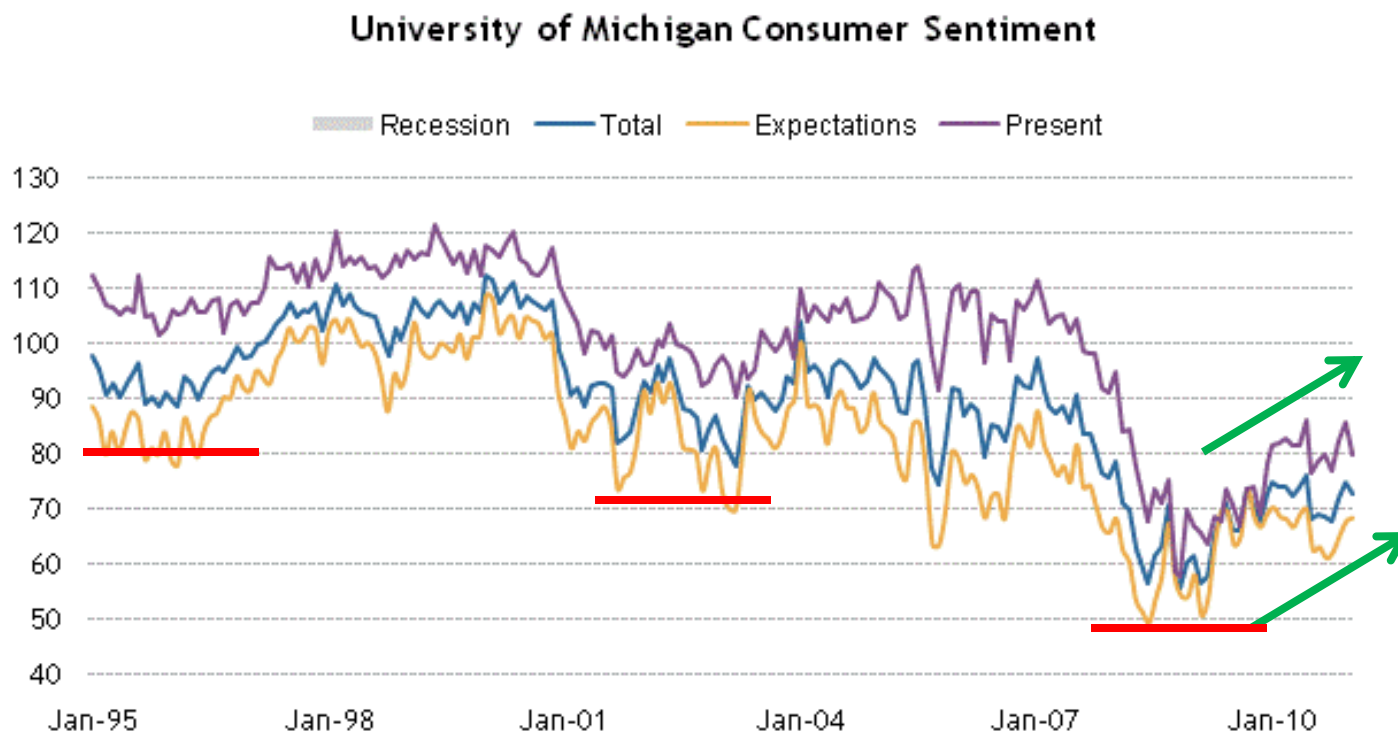
A Question For You

How many of you are MORE confident about the economy and your personal situations than you were a year ago?

How many of you are LESS confident about the economy and your personal situations than you were a year ago?



Confidence Returning



Source: University of Michigan; updated 01/14/11

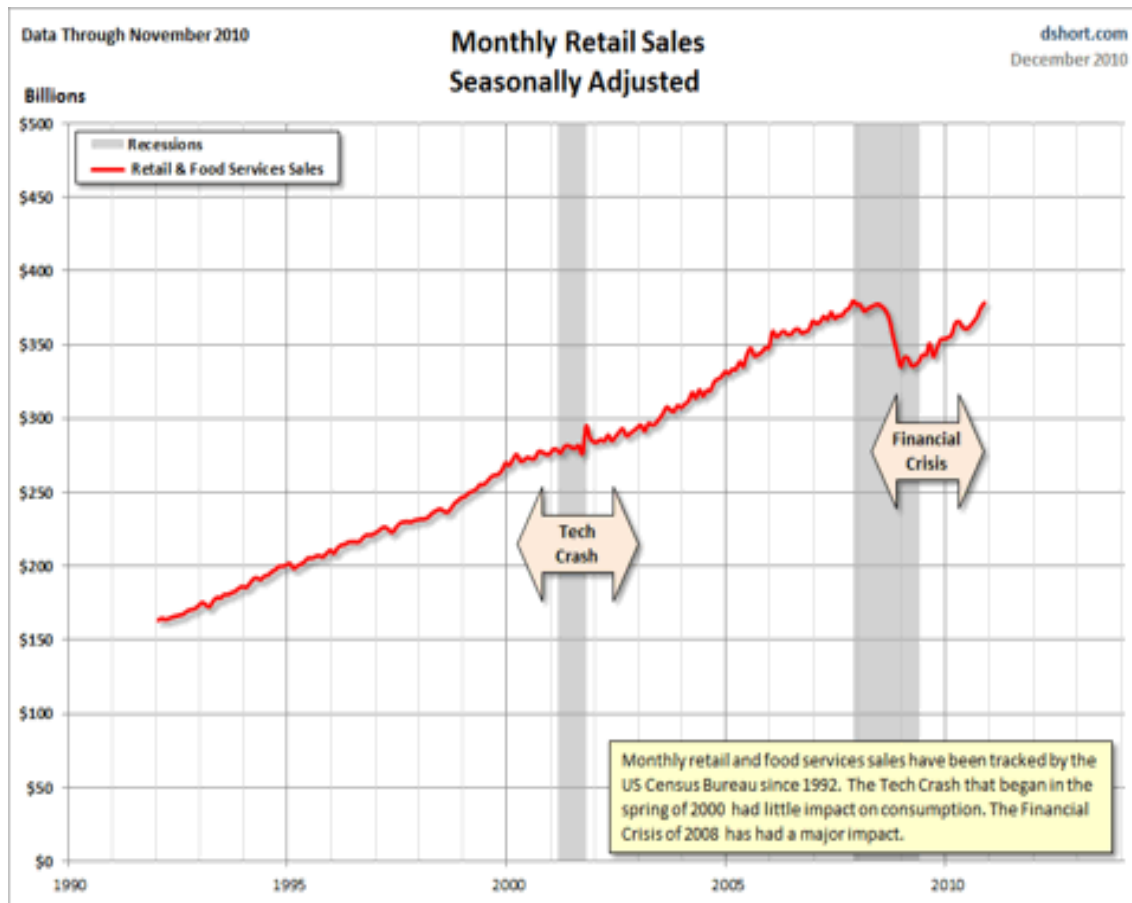
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Much bigger decline than '95 and '01 recessions!

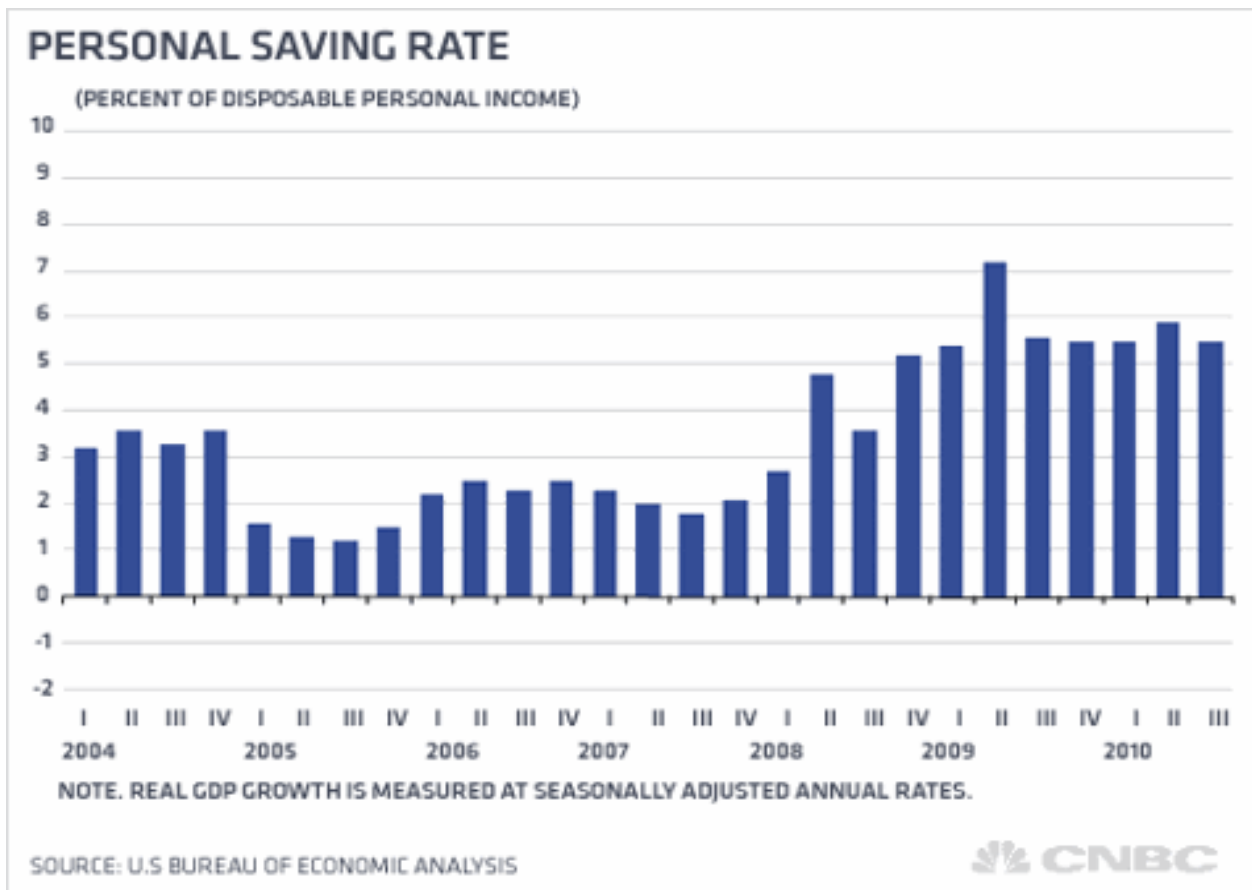
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Getting Back To What We Do Best

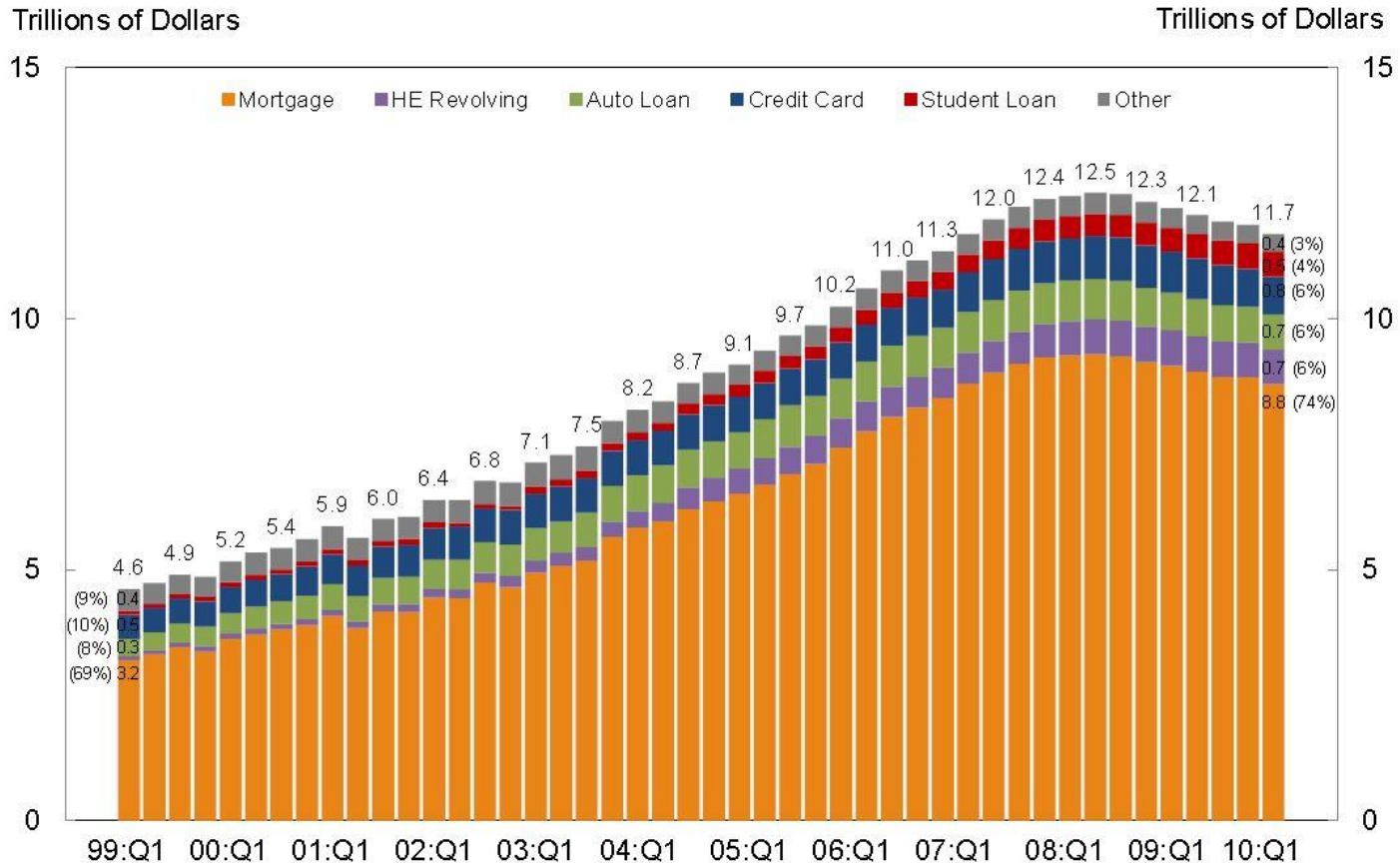


While Saving More



And Paying Down Debt

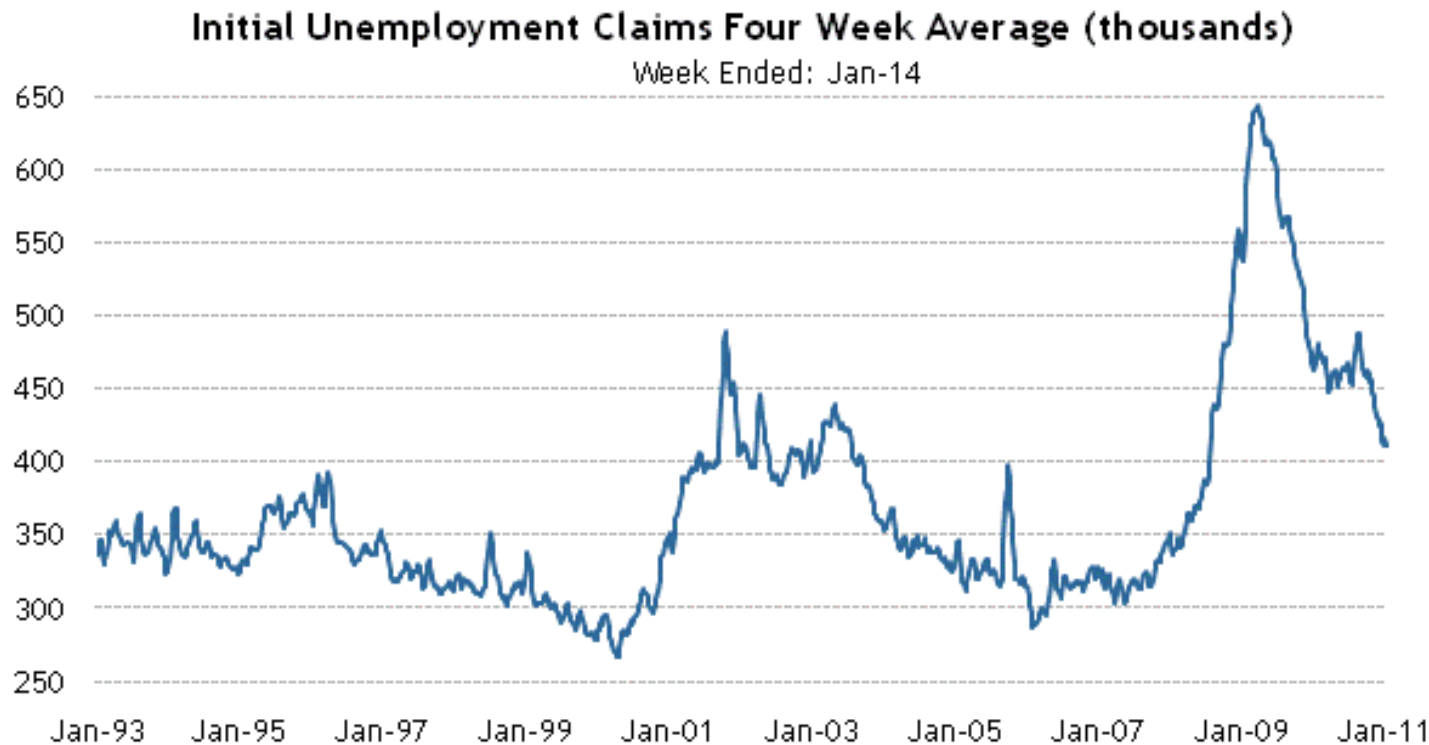
Total Debt Balance and its Composition



Source: FRBNY Consumer Credit Panel



Companies Showing Confidence



Source: Department of Labor; updated 01/20/11

Briefing.com

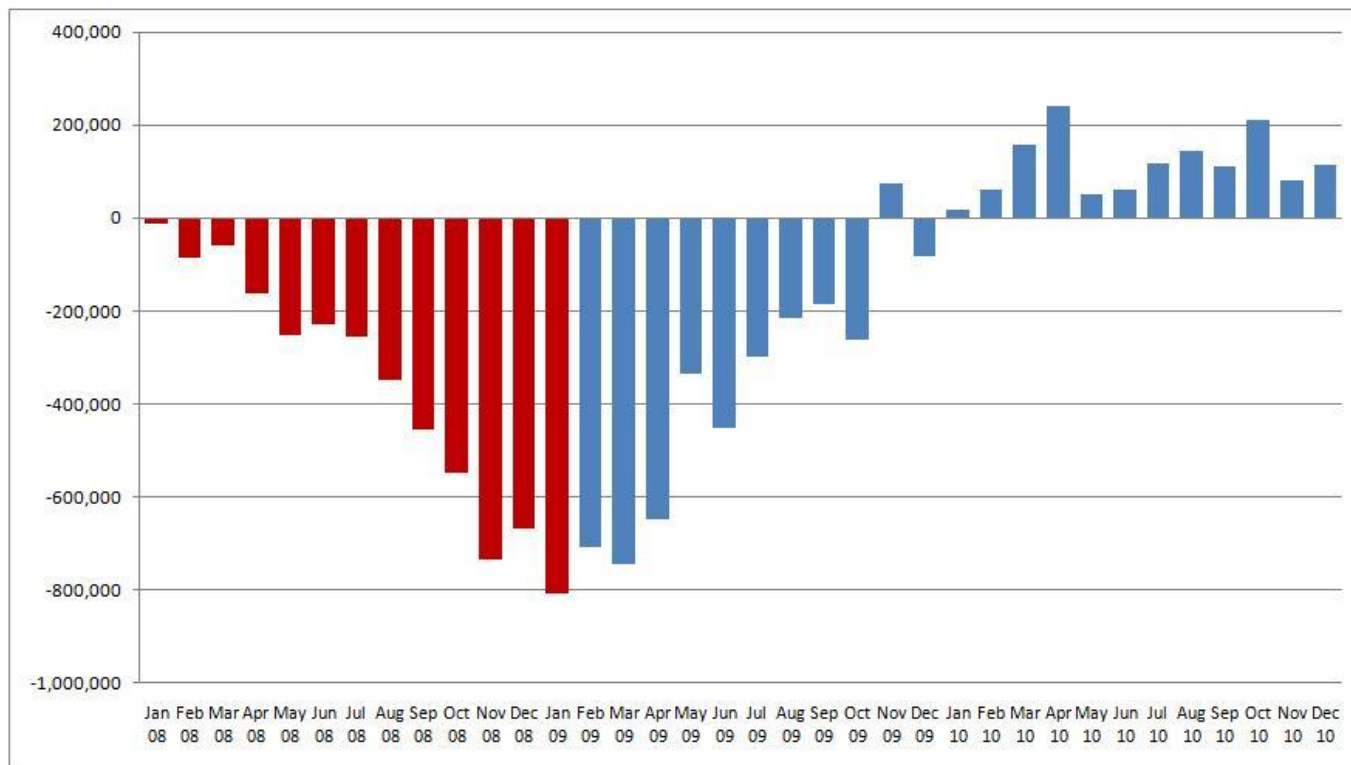
- We have to look at improvement in terms of how far we've come
- Massive trauma to the employment mechanism
- Companies cut bone to ensure survival
- Fewer people collecting unemployment

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The Sleeping Giant At Least Stirs

Private Sector Job Creation

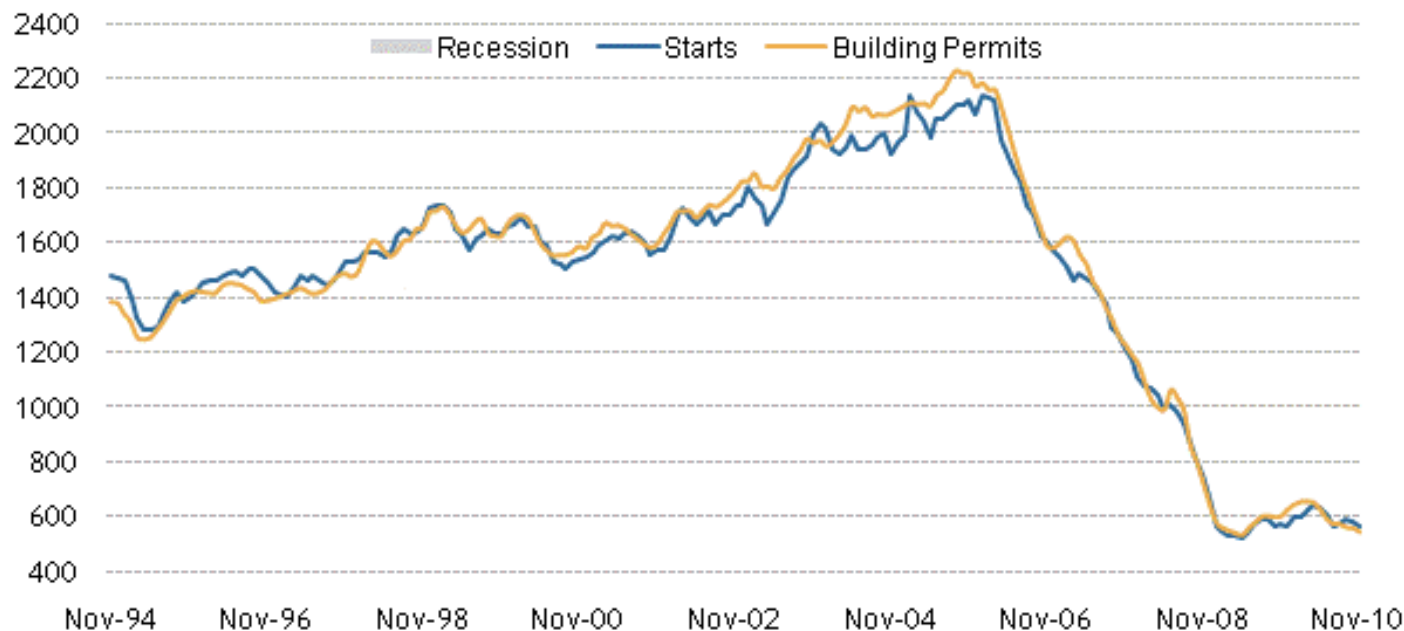


- December 2010 marked the 12th straight month of private sector job creation
- The private sector created 1.25m jobs in 2010 = 100k/mo average



When Is Bad Good?

Housing Starts and Building Permits 3-Month Moving Average
(thousands, SAAR)



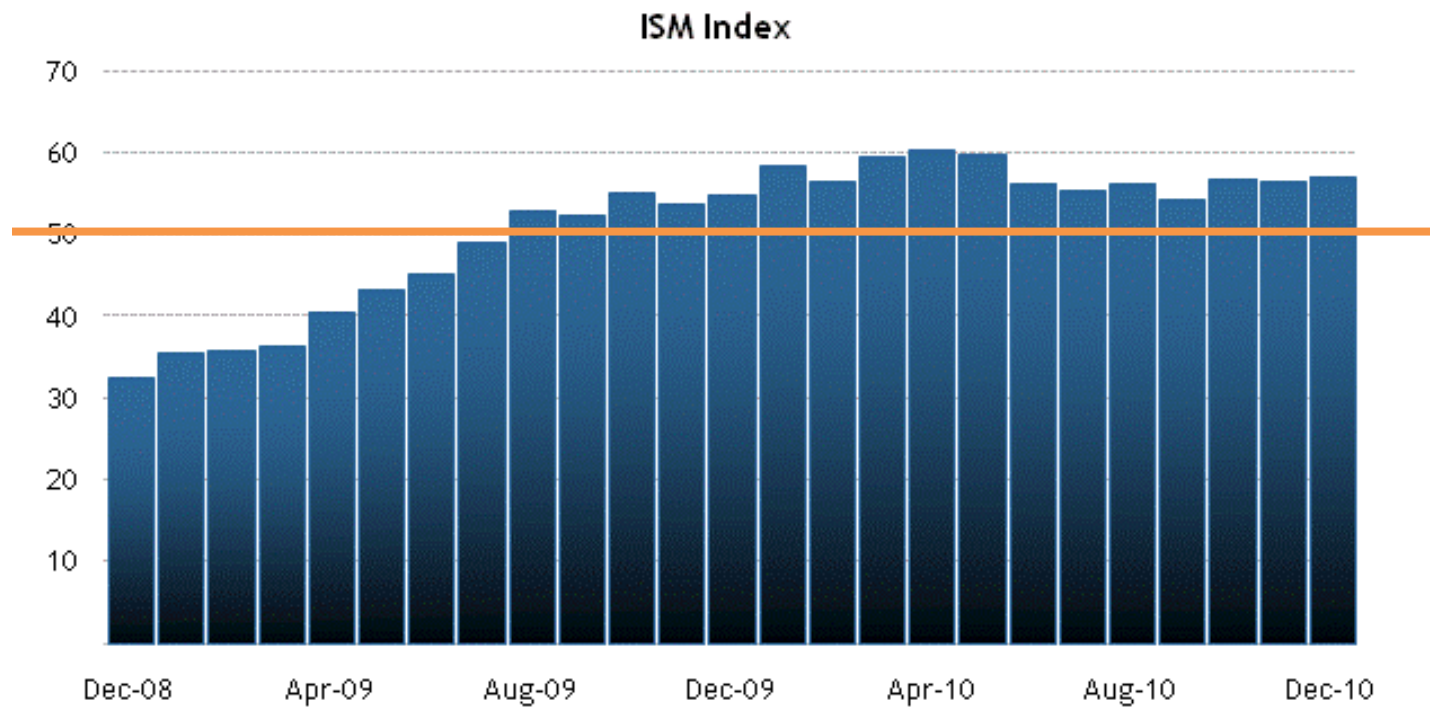
Source: Census Bureau; updated 12/16/10

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Other Economic Data

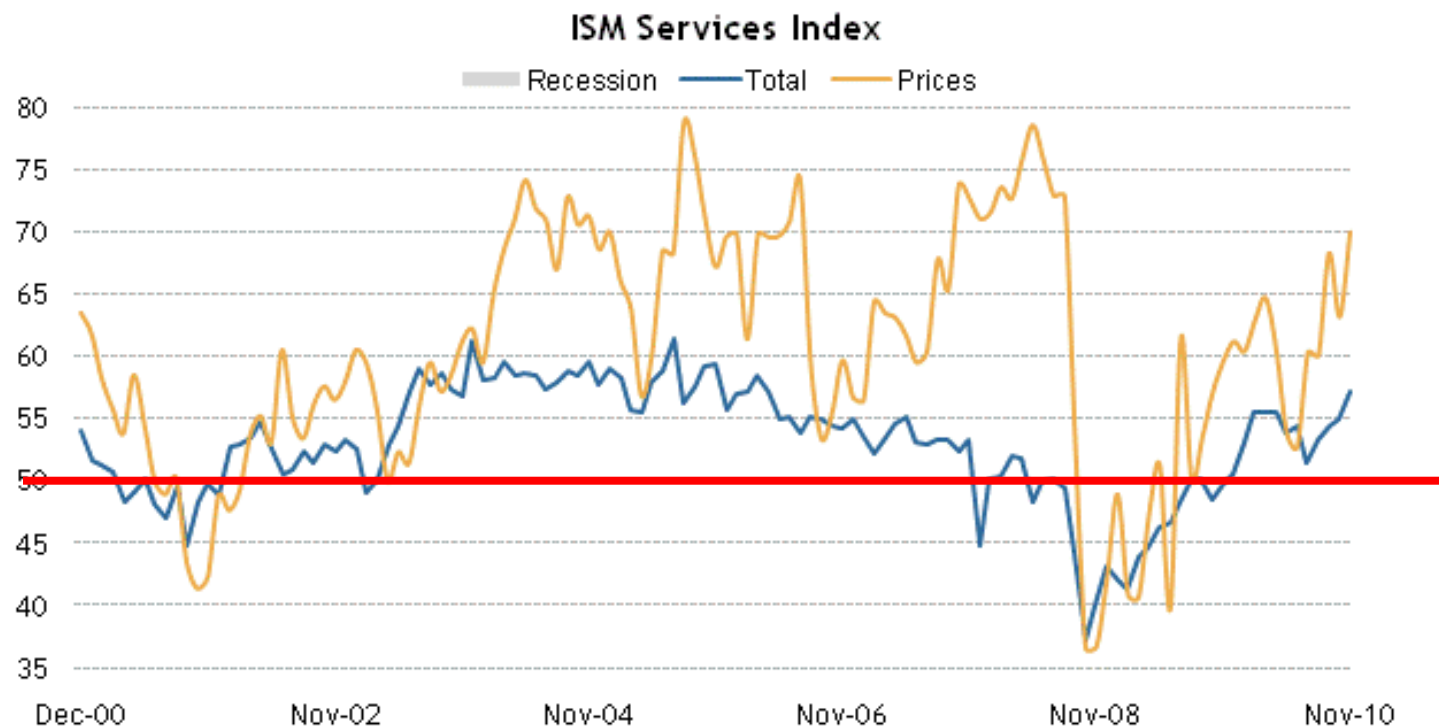


Source: Institute for Supply Management; updated 01/03/11

Briefing.com



Other Economic Data



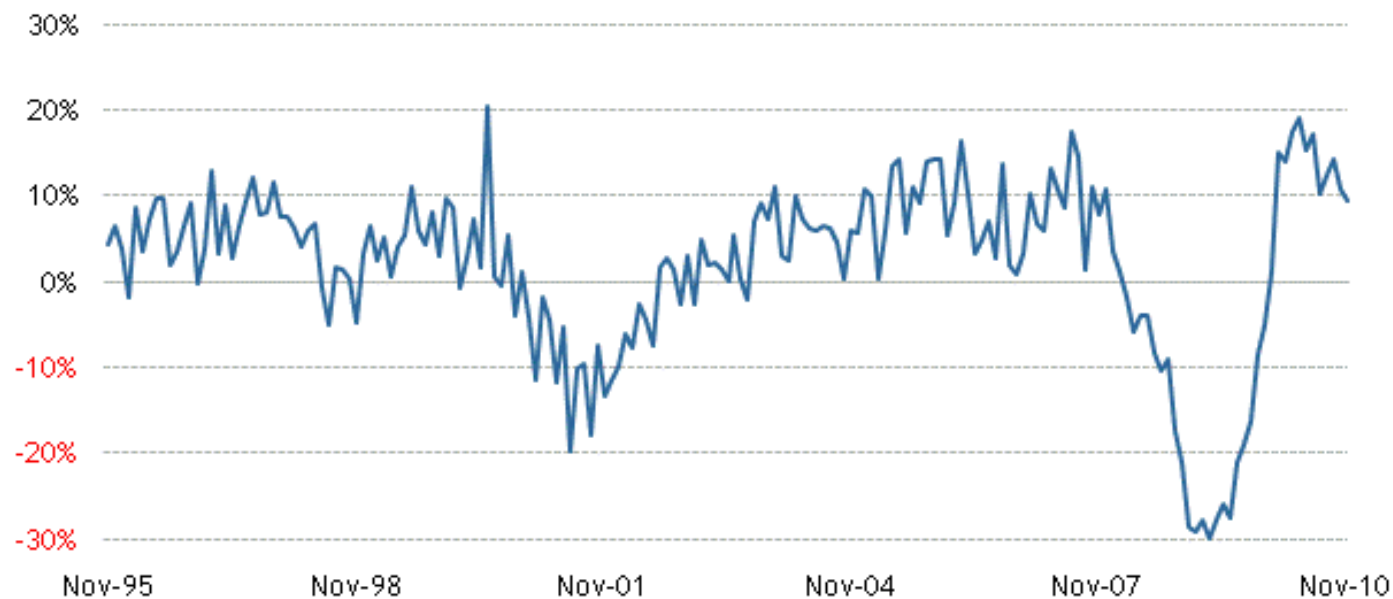
Source: Institute for Supply Management; updated 01/05/11

Briefing.com



Other Economic Data

Durable Goods Orders y/y%



Source: Census Bureau; updated 01/04/11

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Economic Takeaways

- Confidence is returning
- The economy is growing
- The Private Sector is creating jobs
- The consumer is reducing debt and saving more
- The recovery has become self-sustaining



THE MARKETS



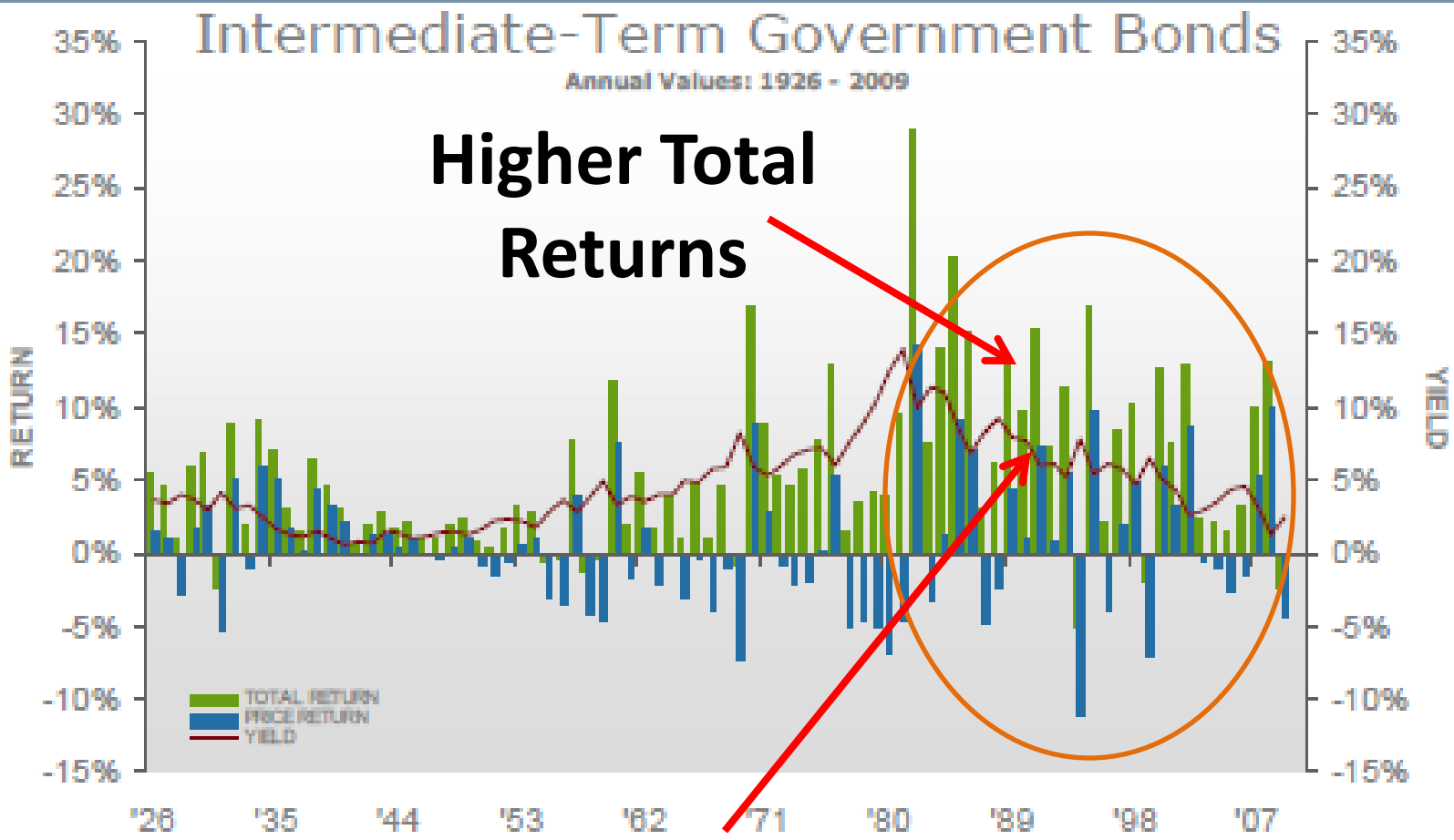
Return On Investment?

S&P 500 Earnings Yield	Money Market	10-Yr. Treasury	Investment Grade Corporate Bond	High Yield Bonds
7.55%	0.01%	3.50%	4.91%	8.28%

- S&P 500 earnings yield found using 2011 consensus earnings of \$95 and 12/31/10 closing price of 1257.88
- Money Market rates from Schwab on 12/31/10
- 10-yr Treasury yield as of 12/31/10 from www.treasury.gov
- Investment Grade Corp yield from iShares LQD ETF as of 12/31/10
- High Yield Bond from iShares HYG ETF as of 12/31/10



Rush To Safety?



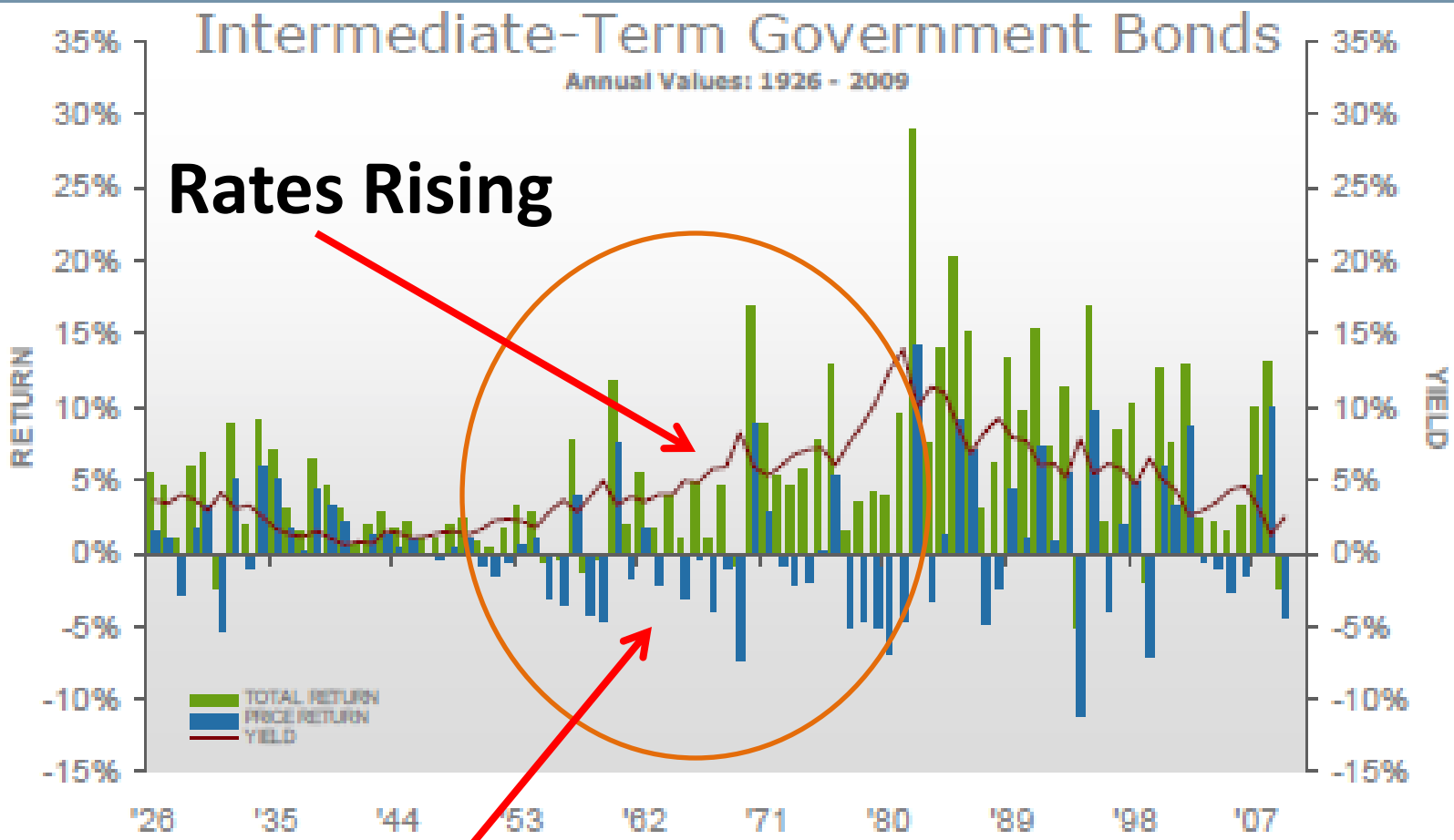
Higher Total Returns

Rates Declining

Source: Morningstar, 12/31/09



Rush To Safety?



Source: Morningstar, 12/31/09

Prices Falling



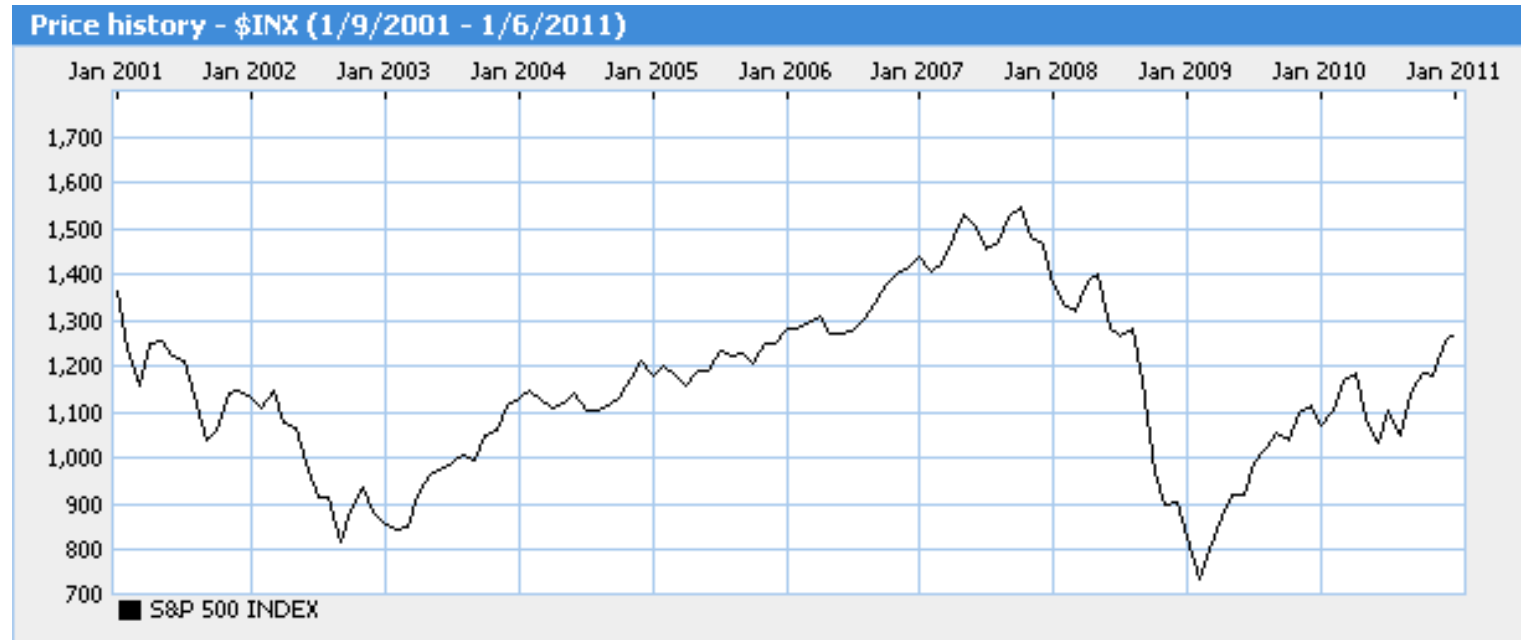
Stocks Have Rallied Too Much...



The S&P 500 has rallied 90% from the March 09 low



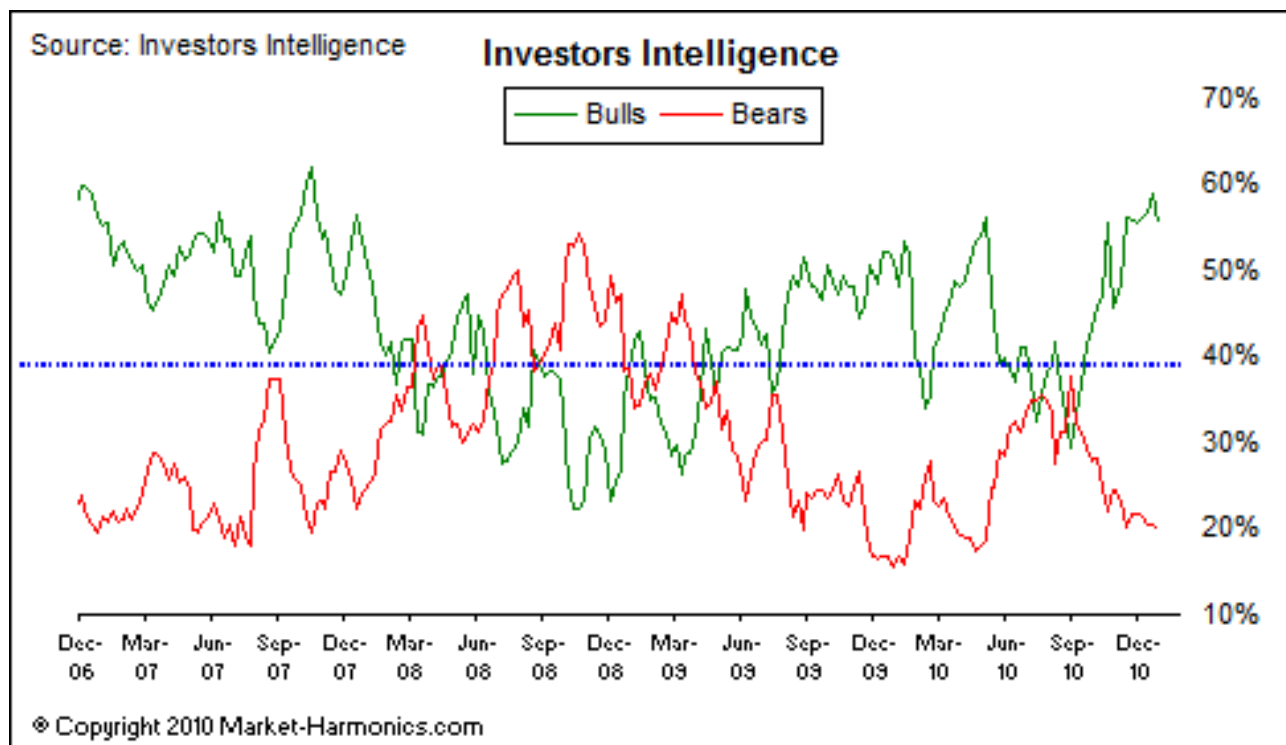
Or Have They?



Still have not returned to 2001 levels even though earnings are 115% higher!

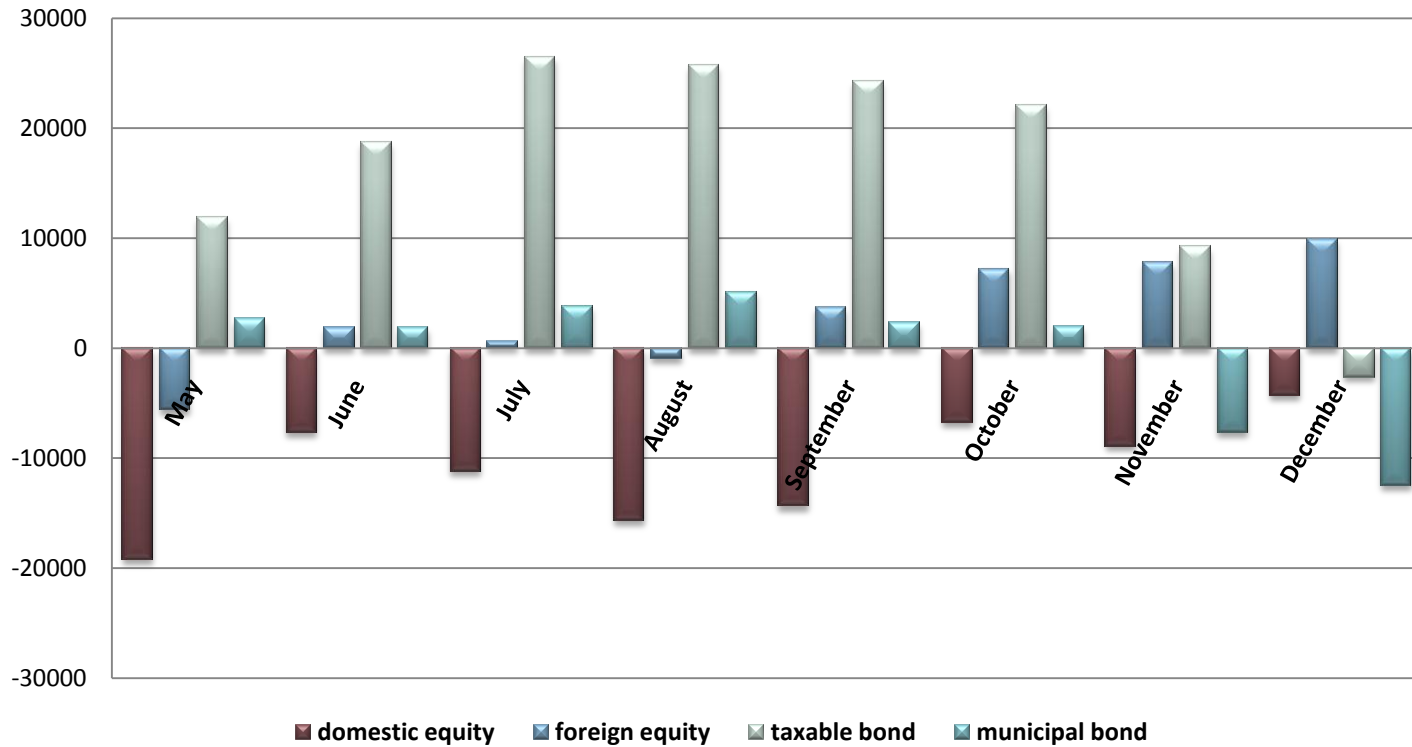


Sentiment Is Getting Too Positive...



Or Is It?

Equity & Bond Fund Flows May - Dec. 2010



Source: Investment Company Institute



The West Isn't Strong Enough...

	2008	2009	2010	2011
USA	0.4	-2.4	3.3	2.9
Europe	0.6	-4.1	1.0	1.3

Source: International Monetary Fund

- **Below trend growth for Western economies**
- **High sovereign debt levels**
- **Austerity rather than expansion**



Emerging Markets Provide Fuel

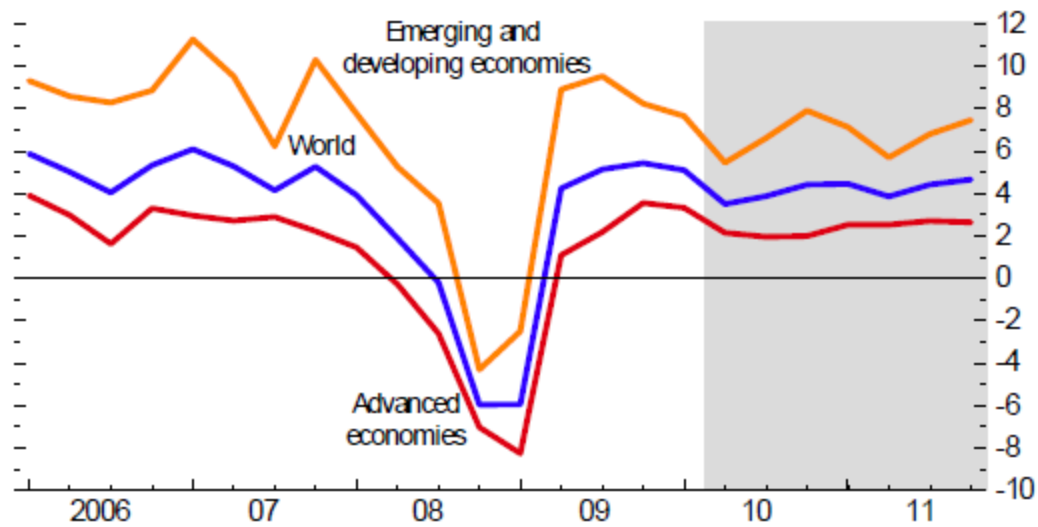
Represent 34% of total GDP of the top 15 economies

Annual GDP Growth

	2008	2009	2010	2011
China	9.6	9.1	10.5	9.6
Brazil	5.1	-0.2	7.1	4.2
India	6.4	5.7	9.4	8.4
Russia	5.6	-7.9	4.3	4.1

Source: International Monetary Fund

Global GDP Growth



Source: International Monetary Fund



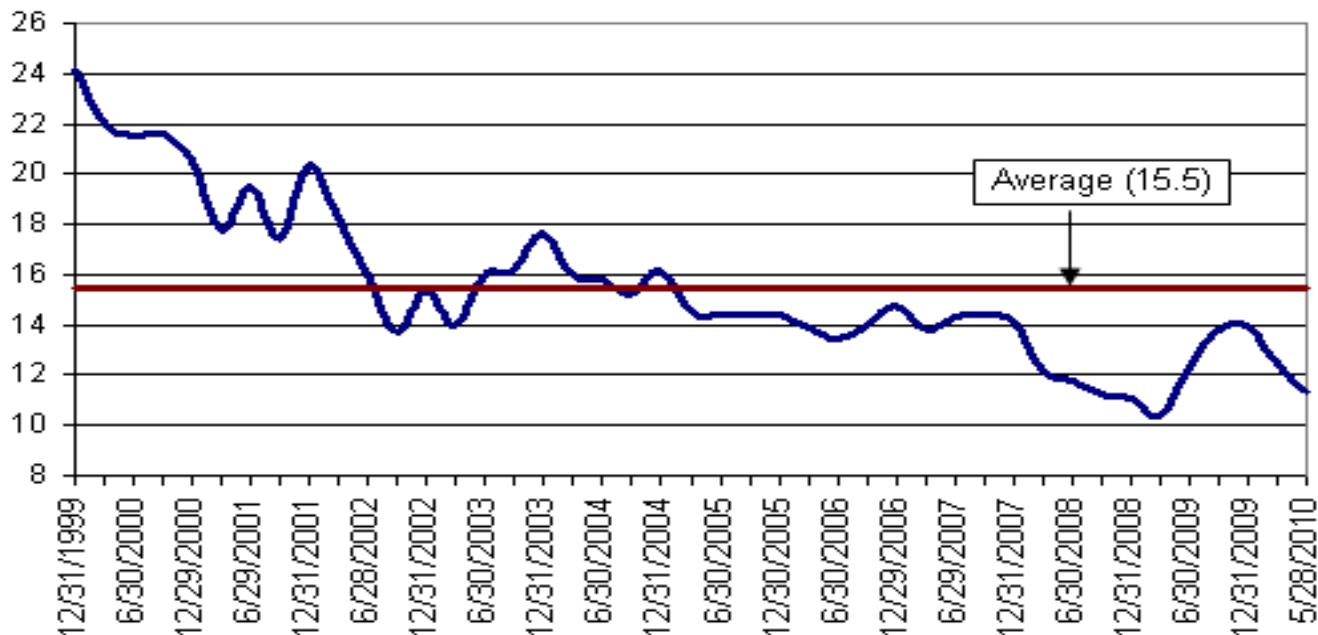
Stocks Are Overvalued...

S&P 500 Historic P/E Ratio



Not If You're Looking Ahead

Forward S&P 500 Price/Earnings Multiple



Data Source: Quarterly data from Factset
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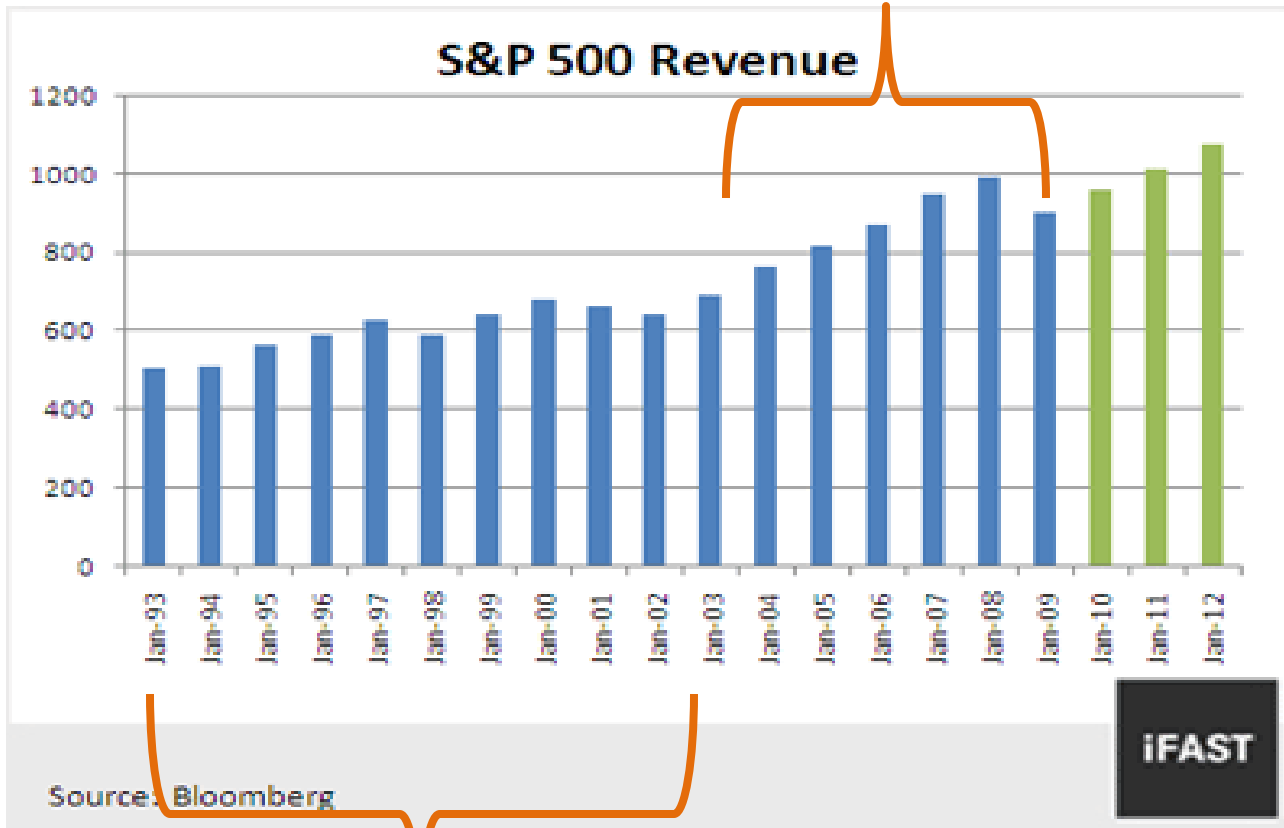
Posted: 06/18/2010

S&P 500 Trading at 13.6x as of 1/25/11



Companies Are Getting Stronger...

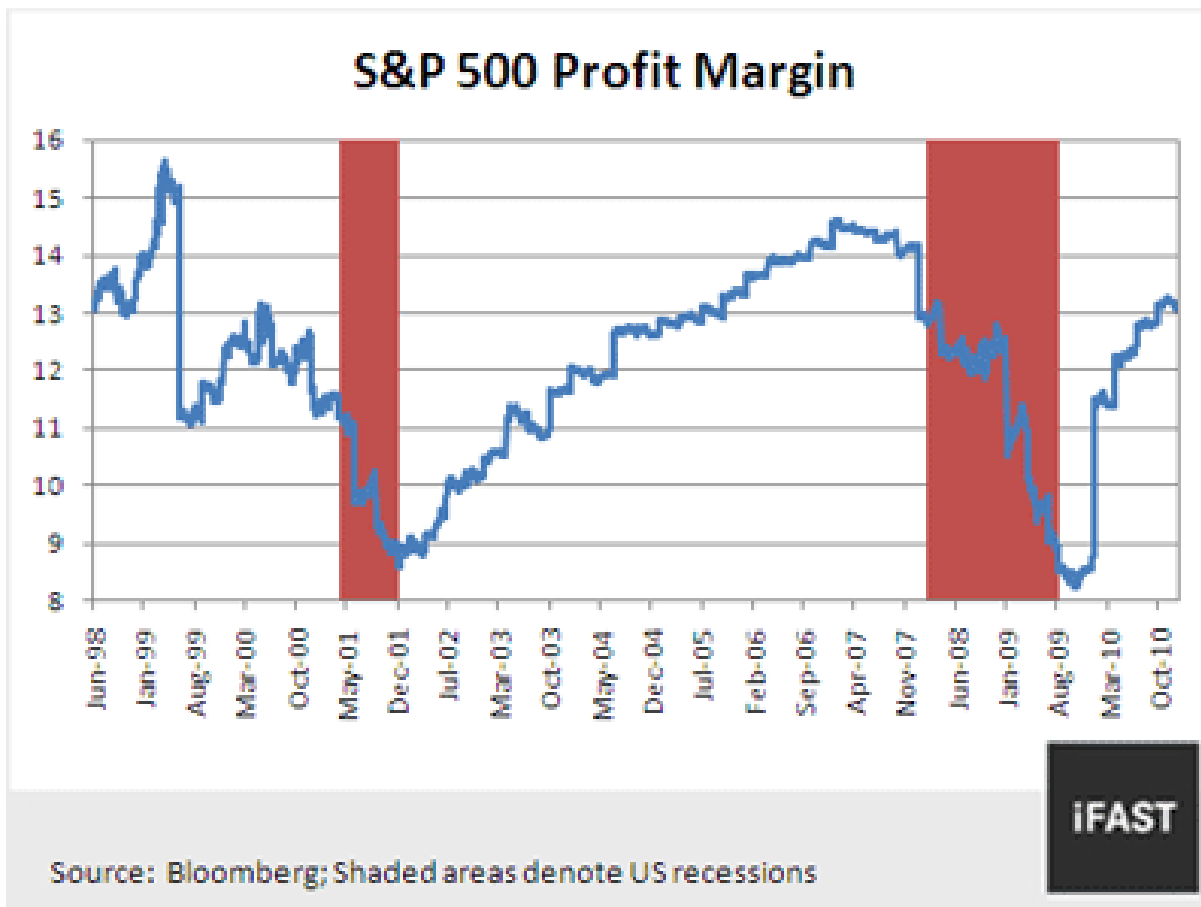
Western Economies & Emerging Markets = 7.4% CAGR



Western Economies Only = 4.3% CAGR



There's No Denying It



Market Takeaways

- Stocks are yet to recover to 2001 levels, even though earnings are 115% higher
- Retail investors still don't like stocks
- Emerging markets have helped revenue growth
- Companies are stronger now
- Looking forward, stocks are cheap



Out On A Limb

2011 PREDICTIONS



The Crystal Ball

- Oil prices rise above \$100/barrel causing gas prices in the US to rise above \$4/gallon.
- Capital exits bond funds and flows back into equities.
- Private sector hiring accelerates and the unemployment rate in the US falls to 8.5% by the end of 2011.
- Financial stocks, namely banks, regain their leadership role and are one of the best performing sectors during the year.
- Republicans in Congress successfully block funding of The President's health care plan enabling health care stocks to rally.



The Crystal Ball

- Money will continue to flow into hard assets (oil, metals, timber, coal) causing raw material prices to increase.
- S&P 500 companies post \$100+ in operating earnings for 2011.
- European stocks post good returns despite various debt crises.
- The Fed raises rates for the first time by the 4th quarter of 2011.
- 2011 sees no major municipal debt defaults.



Thank You

