



## INVESTMENT MANAGEMENT UPDATE

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### MARKET UPDATE & INVESTING OBSERVATIONS

<u>Market Index Returns</u>	<u>2<sup>nd</sup> Qtr</u>	<u>1-Year</u>	<u>5-Year</u>
S&P 500 Index	15.9%	-26.2%	-2.2%
Russell 2000 Small Cap	20.7%	-25.0%	-1.7%
Foreign Stock Index	27.4%	-30.3%	4.2%
Taxable Bond Index	5.1%	2.1%	3.3%
Municipal Bond Index	1.6%	3.3%	3.0%

The 2<sup>nd</sup> Quarter of 2009 provided strong rallies in nearly all equity and fixed income securities markets. This bounce-back, following 15 months of declines, reconfirms several fundamental investing lessons for both investors and advisors:

- It is impossible to predict the direction of such markets.
- Despite lots of bad news within the economy, valuations often move well in advance of an economic turnaround.
- Investors need to honestly assess their long-term capacity and tolerance for risk, and then establish an asset allocation suitable for that risk capacity and tolerance.
- Finally, they must stick with that asset allocation, both in good markets and bad markets. Plus, neither investors nor advisors know whether it's a good or bad market until they have that unreachable vantage point of hindsight.
- Rebalancing works! We rebalanced our model portfolios and most client accounts on March 3, April 17, May 22 and June 22. That enabled us to buy stock funds at cheap prices, harvest gains in stronger-performing funds and ensure consistent allocations in our selected asset classes.
- Diversification works! However, this principle has been tested recently and we've had to reassess how we define diversification. But clearly, the most important step in the diversification process is still an investor's allocation across the broad asset classes: stocks, bonds & cash. In this recent downturn, correlations among virtually all equity markets were very close. For example, large-cap value stocks performed about the same as small cap growth stocks. Also, global markets generally followed domestic markets. But stocks still performed much differently than both bonds and cash.

The other benefit of diversification is at the individual security & industry levels. Avoiding over-concentrations in particular stocks, bonds and industries has been critical in avoiding devastating losses, such as those from various banks & brokers, AIG and the autos. We've also learned that no investment should be considered "bullet-proof."

- Finally, live on your income! This gives investors "staying power" by not having to sell assets at low prices or dip into principal to fund their retirement income.

### BOND MARKET UPDATE

Individual corporate and municipal bonds have continued to be a great market for clients seeking less volatility than equities. They have also provided steady streams of cash to fund retirement incomes for many clients. However, with the run-up in prices since late last year, it has gotten tougher to find really cheap values.

Our exposure to **General Motors** bonds has ended poorly, at least so far. The negotiated bankruptcy of **GM** gave the bondholders a 10% stake in the "**New GM**;" however, we expected that stake to be about 30%. We haven't received the new shares yet, so we don't know the precise valuation. But even though we bought many of the bonds at big discounts and clients received sizable interest payments over the years, we expect the long-term total returns to be negative. We'll keep you posted.

### MUTUAL FUND & MODEL PORTFOLIO UPDATE

- We added two short-term bond funds to our model portfolios, based on the tax status of the accounts:

- **Vanguard Short-Term Investment Grade Fund**
- **Vanguard Limited-Term Tax-Exempt Fund**

These funds were added to protect against rising interest rates, add income over low-interest money markets and take advantage of attractive valuations in the (non-U.S. Treasury) corporate and municipal bond markets. These funds feature current dividend payouts of 4.6% and 3.1%, respectively. Not bad given money market rates are now at 0.5% and a 5-year U.S. Treasury Note pays only 2.3%.

We added these funds to the model portfolios by reducing our money market allocations and high yield bond funds, which have recovered nicely since the first of the year.

- We also eliminated the rest of our position in **Ariel Appreciation Fund**. The fund has underperformed the past few years, but had rallied nicely this year. Still, it's been inconsistent and we disliked its higher expense ratio.
- We are also researching funds with exposure to some "alternative markets" for growth-oriented clients. While these have been devastated the past year, we believe they're now cheap and offer some diversification, particularly in a high-inflation environment. In particular, we like the concept of a "satellite" strategy fund that has the flexibility to move among diverse markets, such as commodities, real estate, precious metals, currencies, emerging markets and international fixed income. This one-fund approach is also appealing since we have limited expertise at The Trust Company in navigating these alternative markets. Again, we'll keep you posted!

Trust Company Mutual Fund Model Performance					Market Index & Sector Performance				
Returns to June 30, 2009	2nd Qtr	1-Year	3-Year	5-Year	Stock Market	2nd Qtr	1-Year	3-Year	5-Year
Aggressive Growth	18.1%	-22.7%	-7.1%	-0.7%	S&P 500 Index	15.9%	-26.2%	-8.2%	-2.2%
Aggressive Growth / Tax-Ltd	17.4%	-22.7%	N/A	N/A	Dow Jones Indus. Avg	12.0%	-23.0%	N/A	-1.7%
Growth	16.5%	-18.3%	-5.0%	0.2%	Russell 2000 Small Cap	20.7%	-25.0%	N/A	-1.7%
Growth / Tax-Limited	15.0%	-18.1%	-5.2%	0.0%	Foreign Stock Index	27.4%	-30.3%	N/A	4.2%
Balanced Growth	15.1%	-14.9%	-3.4%	0.8%	Science & Tech Funds	19.5%	-21.9%	N/A	-1.7%
Balanced Growth / Tax-Ltd	13.0%	-15.3%	-4.0%	0.3%	<b>Bond Market</b>				
Balanced Income	12.5%	-9.2%	-0.7%	1.9%	Govt / Corp 5-Year	5.1%	2.1%	3.9%	3.3%
Balanced Income / Tax-Ltd	9.9%	-9.8%	-1.7%	1.2%	Mortgage Bond Index	1.6%	5.0%	5.1%	4.0%
Conservative Income	10.6%	-4.9%	1.2%	2.6%	5-Year Muni Index	1.6%	3.3%	3.3%	3.0%
Conservative Income / Tax-Ltd	7.8%	-6.1%	N/A	N/A	T-Bill Index	0.1%	0.6%	3.0%	3.1%

**Trust Company Fund Performance & Comparative Rankings (A = Best; E = Worst)**

STOCK FUNDS	2nd Qtr	1-Year	3-Year	5-Year	10-Year	Expense Ratio
<b><u>LARGE-CAP VALUE FUNDS</u></b>						
Dodge & Cox Stock Fund	23.1%	-29.4% - D	-12.7% - E	-2.8% - C	3.2%	0.5%
Goldman-Sachs Structured Large Value - Inst'l	13.8%	-32.5% - E	-14.3% - E	-4.1% - E	N/A	0.6%
Mutual Beacon Fund - Z	16.3%	-25.3% - C	-9.4% - C	-0.8% - B	3.3%	0.8%
Vanguard Value Index- Inst'l	16.8%	-26.7% - C	-10.3% - C	-1.8% - B	-0.8%	0.1%
<b><u>LARGE-CAP BLEND FUNDS</u></b>						
Davis New York Venture	21.1%	-27.5% - D	-9.0% - D	-1.4% - B	0.7%	0.6%
Mairs & Power Growth	17.7%	-18.2% - A	-6.7% - B	-1.4% - C	4.6%	0.7%
<b><u>LARGE-CAP GROWTH FUNDS</u></b>						
Growth Fund of America - F-2	16.8%	-26.8% - B	-6.4% - B	0.6% - B	2.5%	0.6%
Vanguard Growth Index - Signal	15.6%	-25.8% - C	-5.4% - B	-1.7% - B	-3.3%	0.2%
<b><u>SMALL &amp; MID-CAP FUNDS</u></b>						
Fidelity Low-Priced Stock	21.6%	-22.0% - A	-6.2% - B	1.5% - A	8.4%	1.0%
Buffalo Small Cap	20.6%	-0.5% - A	-2.4% - A	1.8% - A	11.4%	1.0%
<b><u>FOREIGN &amp; GLOBAL FUNDS</u></b>						
Capital World Growth & Income - F-2	19.6%	-26.7% - B	-3.8% - A	4.7% - A	6.4%	0.8%
Templeton Institutional Foreign Equity	5.2%	-26.5% - A	-3.9% - A	5.0% - A	4.3%	0.8%
BOND FUNDS	2nd Qtr	1-Year	3-Year	5-Year	10-Year	Expense Ratio
<b><u>TAXABLE FUNDS</u></b>						
PIMCO High Yield - Institutional	17.1%	-8.7% - D	0.1% - C	3.2% - B	4.3%	0.6%
PIMCO Total Return - Institutional	4.7%	9.3% - A	8.4% - A	6.4% - A	7.0%	0.5%
Vanguard GNMA Fund - Admiral Shares	0.5%	8.5% - A	7.5% - A	5.7% - A	6.2%	0.1%
Vanguard Short-Term Inv Grade Admiral	6.1%	2.1% - C	4.3% - B	3.7% - B	4.7%	0.1%
<b><u>TAX-FREE FUNDS</u></b>						
Vanguard Ltd Term Tax Exempt-ADM	1.0%	4.5% - B	4.3% - A	3.4% - A	3.9%	0.1%
Vanguard Intermediate Tax-Exempt - Admiral	1.7%	4.3% - B	4.2% - B	3.8% - A	4.6%	0.1%
Vanguard High-Yield Tax-Exempt - Admiral	5.2%	-0.3% - D	1.9% - C	3.2% - B	4.3%	0.1%

**Explanatory Notes:** This chart reports independent, comparative performance data and rankings assembled by the Investment Staff of The Trust Company of Manhattan. Sources for this information include: Morningstar, Lipper and the Wall Street Journal. The fund performance figures are provided by Morningstar and Lipper. The letter rankings or "grades" for 1-Year and 5-Year Performance are assigned by the Wall Street Journal. These rankings are based on the WSJ-assigned sector for the fund, which may not necessarily correspond to the fund's objective as defined by its own prospectus, or the sector to which we have assigned the fund within The Trust Company's Model Portfolios. However, we believe this format provides the fairest and most effective method of displaying fund performance comparisons.