KIELY WEALTH ADVISORY GROUP, INC.

From Left To Right: Joe Kiely, Scott Below, Katie Burr, Brownie Cordell, and Kellie Kiely

BEHIND THE SCENES

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OPENING THOUGHTS

Happy New Year! We hope this newsletter finds you happy, healthy and looking forward to the New Year. As we turn the calendar on 2009, we look back at a year of extreme volatility that ended far better than it began. In late 2008 and into early 2009, equity markets across the globe experienced historic declines, unprecedented volatility, and many segments of the global credit markets simply stopped functioning for a period of time. As a result, 2008 was a year in which only one segment of the financial markets—Treasury bills—made money. The carnage and panic that began in 2008 continued into early 2009 and necessitated a series of aggressive, unconventional, and often controversial programs to help stabilize the national economy and the global financial system. These programs (as a whole) have laid the groundwork for a remarkable global economic recovery over the last year. To say the world economy is currently in a much better place than it was twelve months ago would be to vastly understate just how far we've come. However, this does not mean we are out of the woods. In fact, we believe we currently sit at a crossroads, with numerous economic, political, and environmental challenges still ahead. If we have the courage to meet these challenges head-on and are able to find reasonable solutions, we'll see positive growth in the global economy into the foreseeable future. On the other hand, failure to adequately deal with these issues could be costly, resulting in economic stagnation and sluggish financial markets. While we believe some of our best days are ahead of us, we do not come to this conclusion lightly. We fully recognize that there will be sizeable bumps in the road, but we also know the American economy has dealt with more serious situations in the past. In each case, we have emerged as a better country than we were before.

A SPECIAL THANKS

Before we delve into our year-end analysis, we would simply like to say… thank you! We recognize how difficult the six month period between September, 2008 and March, 2009 was. We know it tested your patience and your trust in the American financial system. Thank you for your continued confidence in our firm during such a difficult year. While the media (and probably some of your friends and acquaintances) routinely bombarded you with negative economic news, wild speculation, and baseless rumors, you remained stoic through adversity and maintained confidence in our "evidence-based" investing philosophy. When we provided hard evidence that the healing had

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IRA UPDATES

ROTH CONVERSION 2010:

PLEASE BE SURE TO CHECK WITH YOUR TAX ADVISOR FOR MORE INFORMATION ON HOW TO TAKE ADVANTAGE OF CONVERTING IRA MONEY INTO A ROTH FOR 2010!

RMD'S REINSTATED:

JUST A BRIEF REMINDER THAT REQUIRED MINIMUM DISTRIBUTIONS HAVE BEEN REINSTATED BY THE GOVERNMENT FOR 2010. IF YOU ARE REQUIRED TO TAKE THIS DISTRIBUTION, YOU WILL RECEIVE NOTIFICATION FROM TD AMERITRADE.

begun in December, 2008 and January, 2009, almost everyone listened and heeded our advice. We were frank when we wrote, *"…it's important to remember that these recoveries and bounce backs can take time and that the short run is vexingly unpredictable."* In addition, we wrote, *"…there are penalties for holding cash and abandoning well thought-out plans in markets like this—and those penalties are potentially huge. Every dark cloud has a silver lining, and the silver lining of this financial mess is that extreme pessimism and panic create excellent opportunities for rational, patient investors."* Thank goodness, you listened when we told you that, *"…we believe investors who maintain a long-term focus and avoid giving in to their emotions in this market will be handsomely rewarded."*

In January (2009), we outlined a comprehensive plan for capitalizing on some of the unique opportunities that typically exist during periods of extreme volatility. This multi -level approach incorporated asset reallocation, portfolio rebalancing, manager selection and tax harvesting. We felt confident that we had developed a comprehensive plan that would pay significant dividends through 2009 and beyond. You listened to our message and you believed in us. For that, we are extremely grateful. You see, everything we do at Kiely Wealth Advisory Group is done with the best interests of our clients at heart. Sometimes, this means we're forced to say or do things that may not be popular at the time. But we say and do them anyway, even if it means losing an account. We have always believed our clients were a special group, and through this economic crisis you have proven this over and over again. So while we are pleased that we were able to provide sound advice to you throughout the crisis, we're even more pleased with how you reacted and how you trusted us enough to stick it out through a very difficult period.

In sum, we want you to know we are always 100% committed to your financial wellbeing. And going forward, we guarantee that we will continue to provide the same sound, "evidence-based" advice that we've always provided, even if it's not always popular. So thank you once again for your business, your trust in us, and your commitment to our firm during a very difficult time. Your trust does not go unnoticed. Neither do your kind words of encouragement, constructive feedback, or considerate referrals.

THE NUMBERS IN 2009

Despite a rough start, 2009 turned out to be a very good year for stock investors. For the year, the S&P 500 (large company stocks) increased 23.5%, while the Russell 2000 (small company stocks) grew 25.2%. From the early March lows (reached on March 9, 2009) through end of the year, the Russell 2000 climbed a staggering 84.5%, while the S&P 500 gained 67.8%. This amazing performance in stock prices was driven largely by three factors. First, we experienced the inevitable bounce-back from the panic induced sell-offs. Second, companies rapidly reacted to the economic situation by cutting costs (and jobs) in order to maintain profit margins. Finally, the federal government and central bank infused capital and cut interest rates to zero. Spurred by these factors, corporate earnings began to increase and the economy began growing once again - even exceeding most expectations. None of this should come as a surprise, however, since it's all pretty typical of post-recession economies. Unfortunately, many advisors, clients and poorly educated market pundits missed the rebound. Had they had bothered to look back and examine the previous nineteen economic recoveries, they would have seen that our current recovery is little different from those we've experienced in the past. If this trend continues, it bodes well for patient, levelheaded investors.

Our Economy Today: Why Investors are Confused

We watch the nightly financial news, just like everyone else. But we've always believed it is critical to do so with the recognition that journalism is not in the "truth" business, but rather the "advertising" business. This is an important distinction. Look at the daily national headlines: High unemployment, ballooning budget deficits, declining housing values, consumer deleveraging, a weakening dollar, greater financial regulations, high taxes and health care reform. All of these wonderful topics clog the airways day after day. It's no wonder people are scared! We get it. We see the incessant nonsense journalists report every day. Just remember, the ultimate goal of financial journalism isn't to help you become financial secure. It's to get you to buy **more financial journalism**, by tuning in every day. Frankly, investing is fairly straight forward, if you focus on the right items and follow some simple rules again and again over time. However, providing this advice would be suicide for financial journalism, as it would lead you to stop listening to their nonsense each and every day. The truth is our economy (for the most part) is doing just fine. In fact, when we examine past recoveries, we find we are actually ahead of pace of a typical recovery. We are certain this observation surprises you, but we're not in the "advertising" business, we're in the "truth" business. And the truth is…things are improving. Don't believe us? Well, many people didn't believe us last January either.

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The Economy Today: The Real Story

Please allow us the opportunity to repeat our comments in our opening paragraph. ***"To say the world economy is in a much better place than it was twelve months ago would be to vastly understate just how far we've come."*** And that's the unvarnished truth. Today, our banking system is much better capitalized and is lending again. The housing market is stabilizing and in many areas around the country home prices are rising. And every major economy in the world is projected to grow over the coming few quarters. Contrast that with where we were last year at this time, when our financial system was on the verge of collapse. Our credit markets were frozen, the housing market was in a freefall, and the world was in the midst of the worst recession many of us had seen in our lifetime. In addition, consumers had simply stopped spending. What a difference a year can make!

To provide a more comprehensive view of where our economy is at, we've detailed the status of twelve major economic indicators in the table below. Viewed collectively, it is obvious an economic recovery is well underway. However, this does not mean we're out of the woods yet. We fully expect to see some additional volatility, just as we typically do in "year two" of an economic recovery. However, after reviewing the economic data, we think it will be clear why we remain optimistic about the economy and the equity markets. Remember, opportunities do not come gift-wrapped, they usually come in the midst of storms.

TWELVE ECONOMIC INDICATORS	
Inflation	At this point, a few emerging economies may be facing inflation, while deflation still haunts Japan. However, prices are stable in the U.S. and most developing economies. Over the previous nineteen economic recoveries, inflation has remained at bay for nearly four years (on average) and is typically 40% lower than average during that period of time. Over the past year, CPI (or inflation) in this country is down 0.2%.
Corporate Earnings	Earnings estimates continue to improve every quarter, reflecting improved demand and remarkable productivity improvements. We believe earnings will continue to surprise on the upside, given the generally pessimistic outlook of investors. Restrained leverage and deferred internal investment will likely moderate future earnings growth, while mergers and acquisition activity will enhance it.
Global Growth	With the exception of Japan, most developed economies appear to have moved beyond the trough of their recessions. This quarter every major economy in the world is poised to grow. Emerging markets appear to be on a sustainable path. Growth will likely remain muted for a while (given excessive leverage) but will also likely be higher than most believe. Again, pervasive pessimism works in our favor.
Manufacturing	Pent-up consumer demand, enormous business inventory demand and a weak dollar have all boosted U.S. competitiveness and will stimulate moderate growth in manufacturing. The manufacturing index has risen for five straight months and is at its highest reading since 1996.
The Dollar	A weaker dollar has helped our economy in the short term. Since a large part of our corporate earnings come from overseas, more competitive exports have translated into higher earnings in the U.S. Greater earnings will eventually translate into more jobs. We believe much of the pessimism surrounding a weak dollar is unfounded. We would also not be at all surprised to see the dollar strengthen in the coming year, as the "carry trade" is unwound.
Housing	Housing prices have clearly stabilized across the country, particularly on the low end of the price spectrum. The Case-Schiller home price index has increased for six consecutive months. As prices have stabilized and begun to climb, unsold inventories are approaching long term averages. So while housing may not be helping economic growth, at least it's not hurting it at this point.

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TWELVE ECONOMIC INDICATORS

Employment	Unemployment remains at a 17 year high. However, layoffs are declining, average work hours are increasing, personal income is going up and temporary work is at an all time high. Remember, employment is the last thing to recover after a recession. That said, job growth will be muted for some time. Fortunately, unemployment rates are not a predictor of future corporate earnings as the two are unrelated in the short term. We expect job growth to begin at some point in 2010.
Credit	Interest rates are at all time lows, which has been a major boost for first-time home buyers and those businesses and households with strong balance sheets. However, some lenders are still hoarding capital, which should come as no surprise. Congress has finally recognized the important role "shadow banks" play and has introduced legislation to help that market recover.
Personal Income	Hours worked, average income and payrolls have all been consistently increasing over the past six months. Many believe the economy cannot grow without employment growth but this belief is a fallacy. Personal income is the key, and if personal income grows, personal consumption will follow. In fact, over the past six months personal consumption has increased a bit more then personal income.
Productivity	The rise in productivity has caught even the most optimistic observers by surprise. New technology has increased productivity across a wide range of industries. Health care, energy, and manufacturing are just a few of the industries that are dramatically improving productivity through technological advances.
Interest Rates	At some point, interest rates are going to increase. Today, the Federal Reserve remains accommodative, but when the Federal Reserve begins to tighten, interest rates will increase. This will put pressure on bond prices, corporate expansion and budget deficits.
Budget Deficits	A growing federal deficit, potentially worsened by state and local governments, threatens to push tax rates and interest rates higher. Deficits will be the biggest issue facing our government over the coming years. Everyone agrees – we simply cannot continue to spend at the current pace. However, as the economy grows so will tax revenues, but this is only a first step.

*If you'd like access to reliable economic and financial data, we recommend either the **usatoday.com (money page)** by scrolling down to the "Money Essentials" charts - or - the **wsj.com (markets page)** by pulling up the "market data page" which allows you to examine the Economic Indicators archive. These are resources we use every day and they will allow you to form your own objective opinions about economy and the markets.

Overall, if you objectively analyze each of the economic indicators above, it's difficult to be pessimistic about our economy. Clearly we still have some major hurdles to negotiate (like the impending issues in commercial real estate and large government deficits). However, we are pointed in the right direction. Just remember, the sensationalism and hyperbole news you hear every day is designed to capture audience share and is not always indicative of reality… particularly when it comes to our economy.

Regardless of what you read in the paper or hear on TV, this economic recovery - even when you factor in the high unemployment rate - is following in the footsteps of previous recoveries. The underlying economic issues may be somewhat different, but the roles of fear, greed, and pessimism never change. Many investors look for a magic indicator that will signal it's time to invest in the stock market, ***but that indicator does not exist.*** Remember, the stock market is forward looking and current stock prices already reflect the market's collective "expectations" about future earnings. If earnings wind up being better than expected, the market will increase, just as it did last year. So from an investor's perspective, pervasive pessimism is actually a good thing, as it makes positive earnings surprises more likely, thereby increasing the upside potential of stocks. Unfortunately, last year many investors let their emotions and a sensationalistic media convince them to stay away from the stock market. It was a costly mistake.

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THE STOCK MARKET: LOW EXPECTATIONS?

Last year, as we wrote our year-end update we knew the biggest challenge we faced was "psychological". Consumer confidence was approaching an all-time low and investor confidence had been largely replaced by fear and panic. During these periods we knew the typical investor reaction is to avoid stocks like the plague. But we also knew that historically, periods like this were the absolute best times to ***own*** stocks. Fear and panic unfortunately trigger a natural flight response, and even the most experienced investors are not immune. Driven by panic selling, such periods invariably result in stock prices being driven down to absurdly low levels. To illustrate this, we looked back at stock performance data for the periods following the five previous times consumer confidence had reached similar levels and we shared the results at our client dinners last January. If you recall, we found that returns on the S&P 500 averaged roughly 25% in the year following a major consumer confidence trough. So should it then come as no surprise that last year the S&P 500 was up 23%? Hmmm.

Rearview Investing

The second reason we knew we'd run into investor resistance was based on the simple fact that people make investment decisions by looking into a rearview mirror. We knew the previous years return would provide a second psychological hurdle. Investors routinely extrapolate the most recent market and economic data into the future. Since the economy and financial markets were both down significantly from their all time highs, the natural assumption was that bad things would continue to get worse as we moved forward. This exacerbates the flight response. However, like driving a car, we make much better (and safer) decisions if we pay attention to where we're going, rather than looking back at where we've been. Of course, many of you wonder what's in store for the markets as we move forward through year two of this economic recovery.

Year Two of the Recovery

From an investor's perspective, the second year of an economic recovery is generally little different than the first. This is because pessimism is still pervasive and many people still expect the worst. Every time we speak we ask people to raise their hands if they think things will get "worse" before they get "better"? As you might imagine, almost every hand goes up. Unfortunately, investors act on these thoughts at the absolute worst time. In 2009, we saw net cash "outflows" from stock mutual funds in every single month of the year! Of course, financial analysts and market guru's continue to tell people the market is overvalued and likely to retest the lows. This news validates their poor decision. It may seem counter intuitive, but pessimism bodes well for stocks. Frankly, it's best to be a buyer when expectations are low and pessimism is high because there is a greater likelihood of surprises on the upside. If you go back and examine the five worst market declines going back to 1926, you will find that the second year following a significant market decline was always positive and in most cases it was better than the first.

Pessimism is Our Friend

We'll admit that pessimistic people aren't that much fun to be around, but when investors remain pessimistic in a rising market (as they are now) it's a strong indicator that stocks remain underpriced. Pessimism acts as a counterbalance to optimism (and greed). So when one dominates the other, stock prices generally become unbalanced and disconnected from their fundamental value. When pessimism dominates, expectations about the economy and corporate earnings tend to be low. This, in turn, makes economic and corporate performance more likely to surprise on the upside and is obviously positive for stocks. As a long term investors, the best time to purchase stocks is when expectations are low and stocks are undervalued. And if you won't believe us, perhaps you'll believe Warren Buffett, who once wrote, *"The most common cause of low prices is pessimism—sometimes pervasive, sometimes specific to a company or industry. We* ***want*** *to do business in such an environment, not because we like pessimism but because we like the prices it produces. It's optimism that is the enemy of the rational buyer."*

Stocks for the Long Run

Every so often it's important to reiterate that stocks are a long-term investment and we build our client portfolios with the expectation that the money invested in stocks is money that won't be needed in the immediate future. Generally, every dollar committed to stock investments should have a minimum time horizon of five years…and longer. While we think most indicators point to 2010 being a positive year for stocks, we're under no illusions that the short run can (and often does) bring with it some interesting surprises. That's just the nature of stock investing and why stocks are ill-suited for investors with short time horizons. Given where stock valuations are currently, we're confident that five or ten years from now stock investors will be very pleased with their returns. But short-run market moves are unpredictable and those who

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attempt to predict them usually find themselves following the herd, which is more often wrong than right. Short-term market moves are often driven more by emotion than by company fundamentals. And as we know, emotions can drive asset prices to unreasonable levels. Eventually, the market comes to its senses and realizes valuations are unreasonable. Unfortunately, it's impossible to predict when that will happen and how far away from reality prices will get before this happens. In other words, the market occasionally falls prey to the madness of crowds, just as we saw last March. When that happens the most important thing an investor can do is ***not*** to get caught up in what's happening in the short-run by following the herd. As the legendary Benjamin Graham put it, *"The intelligent investor is likely to need considerable will power to keep from following the crowd."*

What about Asset Bubbles?

Asset bubbles have seemingly become more common as financial market innovations have made moving money from one asset class to another asset class both easier and less expensive. Right now, we have concerns about excessive market valuations in both China and Russia. On the commodity side, we believe both gold and oil are trading well above their fundamental valuations. That said, bubbles are notoriously hard to predict and prices can continue climbing long after the fundamental valuations of the assets in question have been surpassed. As long as there are sufficient numbers of people who believe gold is worth more than $1,100 an ounce it will continue to climb in value. We would not be surprised to see gold prices climb another 40% to 50% from their current levels. It's the nature of bubbles. However, don't forget, gold wiped out scores of investors in the 1980's and 1990's. In early 1980 the spot price of gold hit more than $850, but by the late 1990's it was trading down near $250, or roughly 70% below the peak of the bubble twenty years earlier. Ouch…

Beyond potential bubbles in foreign markets and some commodities, our biggest concern at present is bond prices. There is no question that at some point in the future, interest rates will rise. And given the liquidity that has been pumped into the global economy, and the growth of the deficits across most of the developed world, these rate increases could be significant. Since we all know that bond prices decline as interest rates rise, the impact on the portfolios of bond investors could be equally significant. Many of our clients have substantial exposure to bond holdings in their portfolios and most have at least some exposure to bonds. Thus, it probably comes as no surprise that we currently view rising interest rates as one of the more important issues we face.

The Bond Market and Fixed Income: Rising Interest Rates?

In late 2008 and through much of 2009 we saw a "flight to quality" in the fixed-income markets. Investors flocked to CDs, T-bills and money market funds even though the interest rates on these instruments were essentially zero. The money rushing into these "safe" assets, of course, had to come from somewhere and in most cases the hapless victims were corporate bonds or common stocks. This created a bubble in Treasuries and government-backed assets and an unbelievable opportunity in corporate bonds and stocks. In fact, the prices of corporate bonds had fallen so low by late 2008 that we felt their returns going forward were likely to be comparable to the returns on common stocks, but with far less downside risk. As a result, in early 2009 we moved a portion of almost all our client's portfolios into bond funds such as the Loomis-Sayles Strategic Income (NEFZX) and/or the Calamos Convertible Fund (CCVIX). It was our feeling that these managers stood the greatest chance of capitalizing on the extreme under-pricing we saw in most sectors of the bond market. At the same time, we removed Vanguard GNMA fund (VFIIX) from most of our client portfolios, believing that the GNMA bonds were either fully priced or overpriced. In retrospect, these decisions paid off, as NEFZX returned 39.3% in 2009, while CCVIX earned 34.0%. The Vanguard GNMA fund, on the other hand, returned just 5.3% on the year.

2010 is a New and Different Decade

Over the past decade, the environment for bond investors has been one of the best in history, with bond funds generally outpacing stocks funds. Much of the performance of bonds over this period was boosted substantially by a favorable interest rate environment (i.e. sharply falling interest rates). Going forward, fixed income (bond) investors are likely to face the headwinds of a rising interest rate environment, meaning that generating returns sufficient to keep pace with inflation will be a significant challenge. In fact, if interest rates rise rapidly, some bond investors could face significant losses in their portfolios. Fortunately, not all bonds are created equally, which means some will be affected less than others. However, assessing the riskiness of a bond or bond portfolio requires that you first understand the specifics of bond pricing, so before going further we first need to examine which bonds are most susceptible to rising interest rates.

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Which Bonds Are Sensitive to Rate Increases?

One of the most important tenets of bond pricing is that, all else equal, the longer the maturity of the bond, the greater the price fluctuation. In addition, bonds with lower coupon interest rates (also known as a bonds "stated rate" of interest) will fluctuate more than bonds with higher coupon rates when interest rates change. Together then, it's pretty easy to deduce that the bonds you'd least like to own as interest rates rise are bonds with both long maturities and low coupon rates. Hmmm…has anyone looked at the coupon rates on long maturity Treasury bonds lately? As of this writing, 20-year Treasuries are yielding just 4.1% annually, while 30-year Treasuries are yielding just 4.7%. And if you follow the bond market you know those longer term rates are as low as we've seen in the past 50 years or so! To make matters worse, many investors are currently flocking to these low-rate, long maturity Treasury bonds because the rates on short-term instruments like CDs and T-bills are essentially zero. Yes, 4.7% annually is a lot better than zero, but what happens to the long term, low coupon bonds when interest rates begin to rise?

How Much Can Bonds Lose if Interest Rates Rise?

Bond investors are currently caught in an interesting dilemma. They know interest rates will eventually have to go up, so they would prefer to hold short-term bonds so they can have their funds available when rates increase. Unfortunately, current short-term interest rates are close to zero and thus unlikely to keep pace with any inflation. So, many bond investors are choosing longer maturity bonds in order to receive the higher interest rates they offer. And they are doing this in spite of the fact that current interest rates are as low as they've been in half a century. They are engaging in a process called "chasing yield". Unfortunately, many investors don't realize just how much risk they're taking on.

The Price Risk of Bonds

As we pointed out previously, long maturity, low coupon bonds stand to lose the most in value as interest rates rise. But how much money are we actually talking about? To find out, let's assume we recently purchased one 20-yr. Treasury bond and one 30-yr. Treasury bond at their face values of $1,000 each. Let's also assume their coupon rates are equivalent to the current market interest rates for these maturities (4.1% for the 20-yr. bond and 4.7% for the 30-yr. bond). The tables below illustrate what would happen to the prices of these bonds if interest rates were to suddenly rise. As long as rates remain unchanged, our bonds will continue to trade at their face value of $1,000 each. However, as soon as rates start to rise, the values of the bonds start to fall…and the potential losses are significant.

PRICE RISK ON A 30-YEAR, 4.71% COUPON U.S. TREASURY BOND		
Interest Rate Increase	**New Bond Price**	**Percentage Change in Price**
0%	$1,000	0.00%
1%	$857.06	-14.29%
2%	$742.83	-25.72%
3%	$650.78	-34.92%

PRICE RISK ON A 20-YEAR, 4.1% COUPON U.S. TREASURY BOND		
Interest Rate Increase	**New Bond Price**	**Percentage Change in Price**
0%	$1,000	0.00%
1%	$950.21	-4.98%
2%	$839.50	-16.05%
3%	$745.71	-25.43%

These tables illustrate a concept called "interest rate risk." Even though most investors know that bond prices fall when interest rates rise, most don't know the extent to which their bond portfolios are exposed to rate increases. Before seeing this example, could you have imagined that a 30-year Treasury bond would lose roughly 35% of its value if interest rates rise by just three percentage points? Or that the price of a similar 20-year Treasury would fall by more than 25%? Even if you answered "yes" to this question, we're certain most investors currently engaged in "yield chasing" have no idea the risks they are exposing themselves to today. That's unfortunate because risks are substantial and interest rates can't stay at historic lows forever.

Can We Avoid Interest Rate Risk at KWAG?

Our current bond fund managers understand the hazards posed by rising interest rates and they are managing their portfolios accordingly. There are a variety of strategies bond managers can use to help mitigate interest rate risk and these vary depending on the makeup of the bond portfolio they manage. For example, our bond managers are all currently shortening the maturities of their portfolios, which we learned previously is one way

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to reduce interest rate risk. In addition, they are also diversifying their portfolios into areas they believe will be less sensitive to interest rate increases. In some cases this means diversifying internationally, and in other cases it means diversifying away from Treasury bonds and into corporate bonds. Each of our managers has been through rising rate environments many times before, and their track records over such periods are exceptional. That's the reason we hired them in the first place. We feel very good about how our bond portfolios are currently positioned with respect to the interest rate environment. In addition, we are also considering a couple of alternative investments that we believe could help diversify our fixed-income holdings even further. We have yet to add any of the new alternatives to our list of approved funds, so we it's probably not appropriate to cover them here. However, we will share our thoughts on them with you at our upcoming client dinners and we'll keep you updated on our decision processes in our monthly email updates—as always.

10 Questions With Dr. Joe

This quarter, we are going to alter the 10 questions in a way that we think will improve this section. Usually, we select the most common 10 questions that seem to come up routinely over the quarter. This quarter, we selected the same type of questions and provided them to one of our peers in the industry. Then we asked her to put together an interview which incorporated those 10 questions. The result is the following interview which happened just after the end of the 2009 calendar year.

Q1. Joe, I've known you for over 10 years, first as a speaker at TD Ameritrade conventions, then as a fellow board member at TDA and now as member of the 20 elite advisors who share "best practices" with one another. I've always admired the fact that you have a Ph.D. in finance, but don't ever attempt to pick individual stocks or bonds. Instead you prefer to use professional money managers to build portfolios. Why?

A1. Well, as you know, picking stocks is extremely difficult. In fact, most people fail to realize that even the best stock pickers can't pick winners more often than 60% of the time. Basically, this means four out of every ten stocks picked by a professional manager underperforms the market averages. These managers think about how companies work all day long. If they can't pick six out of ten correctly, I believe it's highly unlikely that the average person living outside of New York City could pick five.

Q2: So, you and your team at KWAG like to use professional money managers exclusively?

A2. We do. Simply put, the average person does not have access to the same information as a professional money manager would, so we're at a disadvantage to begin with. For example, professional managers meet with the top executives of the each firm and communicate with them frequently; they know who sits on the board of directors of each firm; they have a team of Ivy League educated MBA's that they send out to meet the middle managers and "kick the tires"; they have expert financial analysts who know how to tear apart financial statements; and they have a steadfast discipline to buy a company at one price and exit it at another. When we meet with and interview money managers, it's clear they have a significant "informational" advantage over most of us when it comes to picking stocks or bonds.

Q3: So how many managers do you like? And how do you fit them together in a portfolio?

A3: There are almost 16,000 mutual fund managers and thousands upon thousands of others who claim to be good stock pickers. We only look at professional managers if they have successful track records that are validated by unbiased third party data providers like Morningstar and Lipper. Overall, we like about 30 equity (or stock) managers and 8 fixed income or bond managers out of more than 16,000. That's it. In other words, we're very selective about the managers we use and there are very few we feel have earned the right to manage our clients' money.

In terms of portfolio building, we build well diversified stock portfolios with roughly equal commitments to large, medium and small cap stocks, which are in turn diversified equally across growth and value stocks. I have yet to meet anyone who commits as much capital to small and mid caps as we do. But the research clearly supports this strategy. On the bond side, we follow the same approach when it comes to manager selection, but we also we let interest rates and unique situations (like the credit crisis) drive our decision making. Of course, we rebalance regularly to take advantage of tax losses and/or market dips. And we rotate out of overpriced areas when we think it's warranted.

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Q4: I'd like to follow up on both your stock and bond strategies, because I agree…they are both different than the average financial advisor. And in both cases, these strategies have worked over long periods of time. Let's start with stocks. Why do you commit so much to small and mid caps?

A4: There are a number of reasons. First, the research shows that throughout history, small and mid cap stocks (particularly on the value side) have outperformed their large cap counterparts. These are the hard numbers and they're indisputable. Remember, all of these companies still trade on the national exchanges, so they're not really small companies like most people might think of them. They're just "small" relative to a huge GE or Wal-Mart. Second, we believe the blue chip companies in the 21st century are currently residing in the small and mid cap universe. These companies embrace change. They embrace new technology. And if you think about the blue chips your parents always talked about…they were probably the same size as small and mid-cap companies today. Third, small and mid-caps have outperformed large caps eight out of the last ten years…including last year. This isn't a fluke. It's the norm! Finally, there is tons of research substantiating the premiums provided by "small-cap" and "value" stocks, which both tend to be underweighted in most people's portfolios. Over the long run, we know that well-diversified portfolios have easily beaten large cap dominated portfolios…and they have done so with less risk.

Q5: I'm also interested in your bond strategies - particularly last year. How did your firm develop a strategy of buying discounted corporate and convertible bonds when the rest of America was buying T-bills and CD's?

A5: This is one area where I believe our firm really stands out. We have two PhDs on the staff and an experienced management team who have the ability to separate fact from fiction. There is so much irrational nonsense coming from the financial press—in ways that seem plausible—that it's virtually impossible for the average investor to understand the difference between good and bad information. Frankly, if you don't have a strong educational background in economics and finance, I'm not sure how you could tell the difference between good and bad information. We've been doing this for over 20 years now, so we have both the educational training and the experience, and it's still not easy. Regarding our specific bond strategies, we have been following the research of Dan Fuss at Loomis Sayles for years. In January, when we had our first investment committee meeting of 2009, it was obvious to both Scott and I that Loomis Sayles was onto something regarding severe under-pricing of certain classes of bonds. Then it just became a matter of developing a strategy and executing it. The truth is, Brownie, Scott and I live, eat, drink and breathe finance. We all read voraciously. And we challenge one another all of the time to make sure we have left no stone unturned.

Q6: So there is a real team aspect to your firm?

A6: Well, everyone on our management team has been around for at least ten years. We all sit in on each other's committee meetings and we all share each other's duties when someone is out sick or travelling. It's like a small family, but without the usual dysfunctional aspects many families have to deal with. We all have pretty calm personalities and we love what we do, which means we can focus on the task at hand without some of the political nonsense that can bog some firms down.

Q7: So, let's change the topic a bit. Given your academic background in Economics, I'm always interested in your thoughts on the economy. How do you feel about the economy as a whole and what worries you going into 2010?

A7: I guess nobody gave you our most recent newsletter? In our opinion, the economy is recovering as expected. In fact, it's even ahead of where most expected it would be at this point. We hate the fact that so many people are out work. But, we also believe in the resiliency of this country, which means we believe in the resiliency of this country's people. This is the greatest country on Earth and no one else is even close. We have the most dynamic and productive workforce in the world. We know that there are problems in our educational system, health care and government. However, we also like to focus on what's right with our country…and if you look around and dig below the surface just a little bit, it's hard not to get excited. We have a ton of great things going on in every industry across this great nation. I know people and companies who are thriving in every industry and they have never been more excited about their future prospects. They could care less about the negative news that's seems so prevalent…they're too busy creating new products or services. I also know people in the finest educational institutions across the U.S. and they tell me that we have some of the best students they have ever seen. Finally, let's not discount the amazing work being done by the Federal Reserve and Treasury.

So, we know we have problems…but I firmly believe we can handle them. Our country has always risen to the

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challenge in the past…I'm not sure why anybody would think this time would be any different? Of course, I'm not blinded by politics, so it makes it much easier to see all that is good right now.

Q8: Okay fair enough…I always feel so positive after we talk. So, tell me what really worries you?

A8: Okay, what really worries me are the things we don't know about. For example, in 2008, we knew that there were "unregulated" companies trading "unregulated" derivatives. However, since they were unregulated we had absolutely no idea the extent to which these companies were exposed to harmful mortgage derivative products. Why? Because we had no way of knowing what was happening behind closed doors. As it turns out, they were playing with a "financial" time bomb and it went off while they were holding it in their hands. Then, and only then, did the rest of the world find out about it.

Today, we don't have those same types of problems, because all of the unregulated products, players and institutions are now being regulated. We now know exactly what's happening in every one of our financial markets.

Frankly, I find it very interesting how people get so worked up about one economic variable or another. And then they use that variable to construct a story about why the markets will increase or decrease in some manner. Frankly, if we know what the economic issue is and we spend countless hours discussing it on national TV, I assure you that's not the issue that will take our economy down. That information has already been priced into the market. Information is the great equalizer. That's what's so great about our country and its system of checks and balances.

So, I have no doubt we'll get through the issues we are aware of…that's the easiest part. It's the issues like 1) Unregulated trading; 2) 9/11; 3) a nuclear war or 4) a dirty bomb - the things we don't know about. These are the real issues that can really hurt our economy. That's what really worries me - the unknown.

Q9: I never thought about it that way, but it makes sense! Tell me a little bit about your client base. Is there a specific client you like and try to find?

A9: We don't look for a particular type of client, although we do like clients who want to be educated. We try to be as educationally oriented as we can in our practice. Our clients come from all walks of life and they all interest me. In fact, most of our closest friends have been developed through a professional relationship through our firm. I'd like to think that says something about our firm. In my mind, there's nothing like meeting a client, going over their account and the economy, and then enjoying a cold glass of beer.

Q10: I've looked over your web-page and noticed you have a whole section on giving. That seems to be a core element in your practice. Can you provide some background on that?

A10: Our firm's mission is based on one my favorite sayings, which I happily take from my father who used to routinely say **"give first – and you'll get back a million times"**. We've tried to build our firm and live by that motto. In our "Pay it Forward" programs we try to expand upon that. We have three primary goals when we get involved in a project. First, every dollar must go to the end user. Second, the program must have a "pay it forward" component, so the investment grows over time. Finally, we think it's important to be personally involved through some sort of "hands on" involvement. The "hands on" experience feeds on itself…as you always want to push to do more for those in need.

Q11: I'm supposed to stop at ten questions, and I went over. Sorry! So let me finish with a question about your newsletters and monthly updates. I don't know any advisors who write as much as you do each and every month. We all communicate with our clients but why do you think so many updates are useful to your practice?

A11: We believe the updates are necessary in today's new environment. Like many of our peers, we spend countless hours sifting through industry newsletters, mutual fund updates and an array of advisor perspectives. Our rationale behind our quarterly newsletter, our monthly updates and our daily conversations is simple. We want to provide our insight into the various viewpoints that exist out there. We believe it's our job to look at as many viewpoints as we can, so that we can be sure we have factored in all relevant information and all possible outcomes into our analysis. This is not easy. You have to have a thirst for knowledge and a passion for analysis. Furthermore, you have to recognize that you don't know everything – other advisors can provide great insights to our industries problems. To be successful, we believe you have to be willing to dig a little deeper than the next advisor. You can never be satisfied with your current base of knowledge. And you have to love what you do. Last year, we believe we hit the nail on the head when we identified specific corporate and

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convertible bonds for our clients and friends. We found a great "liquid asset" that decreased our portfolios' risk exposures and increased their returns. However, last year is over. It was a great year, but it means nothing as we look forward. You can't invest using a rearview mirror. **You have to follow the process**. And you have to do it with the same consistent passion year in and year out.

So, given all of the conflicting advice, we think it's important that our clients and friends know they have a consistent source that they can go to get common sense advice – at any time. If you've read about a topic in the financial press, odds are we've covered it in our regular meetings. In sum, we like to communicate the following general messages in these updates.

1. We care. Clearly, our clients are the most important asset to our firm.
2. We understand individual needs. We know people want to maintain their standard of living throughout their lifetime.
3. We know what the issues are. Government debt, Roth conversions, new estate laws, and the economy. We are on top of it.
4. We have a proven process that works, and we're committed to it each and every day.
5. We're not going anywhere. We're going to be here for a long, long time.

A FINAL NOTE

As usual, we want to thank each of you for your continued confidence in our services. Our overall philosophy, which combines the best managers (and mutual funds) with research-driven asset allocation strategies, has provided excellent returns to all of us. As we go forward, we remain committed to continuing to refine and improve these proactive strategies. As always, our goal is to provide each of clients with the best possible mix of assets given their particular situation.

If you need anything or your goals or time horizons have changed, please do not hesitate to call or drop an email to set up an appointment. We are here to serve your financial needs, whatever they may be. We thank you for your kind comments, your kind referrals and your feedback regarding this newsletter.

We hope you enjoy the New Year,

~ Joe and The Gang at KWAG

OUR 2010 CLIENT APPRECIATION DINNERS

Monday, January 25, 2010 | Sunset Beach, NC – Sea Trail Conf. Ctr. | 6 PM to 8:30 PM

Tuesday, January 26, 2010 | Greenville, NC- Brook Valley CC | 6:30 PM to 8:30 PM

Thursday, January 28, 2010 | Asheville, NC – Asheville CC | 6 PM to 8:30 PM

RSVP to our main office in Greenville today at 877-366-5623 or email Katie at katie@thekielygroup.com

You are invited to attend one of our client appreciation dinners listed above. During these dinners we will discuss our core strategies; examine the state of the economy; and identify potential economic pitfalls that could occur over the next few years. We will also examine our managers, both new and old, and take a look at their views on the economy. Finally, we will discuss a few strategies to take advantage of, the near certain "bubbles and busts" that will occur over the coming years ahead and why we continue to believe our best years are ahead of us. Please feel free to bring along any friends or relatives who may be interested in hearing what we have to say.

TAX & Required Minimum Distribution Note

A Personal Note from KWAG's Operations Director and Chief Compliance Officer

This note is a reminder of a few important Tax and IRS issues to come. First, KWAG will be mailing out your 2009 Realized Gains and Losses Reports (Cost Basis) by January 31st, 2010. This mailing will go out within a few days of receiving this packet. That said, not all clients will receive this tax mailing. For example, those clients who have money invested in IRA's will not receive a KWAG mailing. If you do not receive one by the middle of February, and feel you should, please contact me or your advisor for more information.

In addition to our Tax mailing, TD Ameritrade will also mail your 1099 reports by the same requirement date. These reports will also be available via your TD Ameritrade online site.

Finally, for clients required to take Minimum Distributions (RMD's) from their IRA accounts, these distributions have been **reinstated** by the government for 2010. TD Ameritrade will mail these RMD amounts to you within a week or so of receiving this newsletter. These distributions can be taken anytime during the 2010 calendar year. To do so, please contact me or your advisor and we will send you the proper documents to withdrawal your RMD. If we have not heard from you by October, we will send a reminder to you to take the RMD prior to the end of the year. These RMD's only pertain to clients 70 ½ or older and invested in a retirement account.

If you have any questions or concerns about your 2009 KWAG Tax Reports of RMD's, please contact me or your advisor for more information.

Best Regards,
Katie Burr
katie@thekielygroup.com

The Gang at Kiely Wealth Advisory Group

Left to Right: Brownie Cordell; Katie Burr; Joe Kiely; Kellie Kiely; and Scott Below

THE KIELY GROUP'S 2009 YEAR END PAST RECOMMENDATION NUMBERS

PLEASE REMEMBER: While we update the performance of these funds quarterly, the list of mutual funds only changes annually.

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