



## Fourth Quarter 2009 Review and Outlook

*Tim Clift*

*Lead Portfolio Manager*

Equity and bond markets had a strong finish to 2009, capping off an impressive rally that started in the first quarter of the year. For many indices it was their best calendar year performance since 2003. Helped in large part by government spending and guarantees, investors regained confidence and moved back into the markets. The Dow Jones Industrial Average finished the year up 18.8% while the S&P 500 Index rose 23.5% for the period. The more technology weighted NASDAQ Index ended the year up an impressive 43.9% (78.9% from its March low point).

The economy also appears to be on the slow road to recovery from what is being called “The Great Recession.” While the stock and bond markets rose quickly and rapidly, economic recovery has been more uneven as some segments of the economy are still struggling, even with massive government stimuli. The housing market has stabilized but has seen little improvement despite being propped up by the Federal Reserve’s efforts to purchase mortgage securities to keep mortgage rates low. The unemployment rate surpassed 10% in the 4<sup>th</sup> quarter and may not improve anytime soon as few companies are indicating any major hiring initiatives.

Although stock prices for many companies rose dramatically in 2009, it has not been from earnings growth. Earnings numbers have been “less bad” rather than “improved.” Most of the earnings improvements have come from cost cutting measures rather than top line revenue growth. Further progress will need to come from revenue growth, as cost cutting is only a short term solution. Another factor driving up stock prices has been the search for yield. Now that many money markets instruments are yielding essentially 0%, many investors with assets sitting on the

sidelines have started searching for higher potential returns in the stock and bond markets.

Most sectors of the bond market benefited from the increase in liquidity from government spending, creating favorable market conditions and pushing prices up. Bond prices have been driven by the tightening of credit spreads as credit markets have thawed. Low-quality corporate bonds such as high yield led the bond markets with equity-like returns for the year while more conservative Treasury bonds lagged far behind. The Barclays Capital Aggregate Bond Index, which is a mix of corporate and government bonds, returned 5.9% for the year.

While the Fed acknowledges there have been improvements in some sectors of the economy, concerns about sustainability of the improvements continue. This has led the Fed to declare that interest rates will remain low for an extended period of time (between 0% and 0.25%), which are at exceptionally low levels. A major unknown is how the markets will react when the Fed begins to unwind some of its support. The Fed’s level of success in withdrawing market support will be closely watched and scrutinized. Pulling back support too abruptly could cause the markets to panic again. If it is done too slowly, growth may occur too rapidly and drive up inflation.

International markets also benefited from government intervention and the easy money policies of central banks. A generally weaker dollar boosted returns for US investors holding international assets as well. The MSCI EAFE Index returned 27.8% for the year.

## Outlook

As we transition into 2010, there are many outstanding issues that will impact the direction of the markets. One of the biggest questions now is whether the US economy is strong enough to thrive on its own, without massive government spending, or whether further government intervention will be required. Corporate earnings will also be under the microscope. Last quarter's earnings were better than expected based on cost cutting measures. At some point cost cutting is no longer an option for companies and earnings have to be driven by top line sales growth.

Most likely, we are entering into an extended low-growth and low-interest rate environment. The risks of a double-dip recession or another sharp market pullback are real, but the economy has made some progress over the last year. Predicting the direction of the markets over the short-term is extremely difficult as unexpected events will always occur. The most prudent way to invest is by diversifying your portfolio. A portfolio with exposure to many areas of the market is key to weathering volatility and being positioned for growth in the future.

*An individual investor's situation can vary; therefore the information presented above should be relied upon only when coordinated with individual advice.*

*Index performance is presented for illustrative purposes only and does not represent the performance of any specific investment product or portfolio. An investment cannot be made directly into an index. **Past performance is not a guarantee of future results.** ActivePassive Fund performance can be obtained at [www.activepassivefunds.com](http://www.activepassivefunds.com). Diversification does not assure a profit or protect against loss in a declining market. Sector allocations are subject to change and are not recommendations to buy or sell any security.*

*Current and future portfolio holdings are subject to risk.*

The Dow Jones Industrial Average is a price weighted index of 30 of the largest, most widely held stocks traded on the New York Stock Exchange. The S&P 500 Index is an unmanaged index comprised of 500 widely held securities considered to be representative of the US stock market in general. The NASDAQ Composite Index measures all domestic and international based common type stocks listed on the NASDAQ stock market. The Morgan Stanley EAFE Index represents 21 developed markets outside North America. The Barclays Capital U.S. Aggregate Bond Index covers the USD-denominated, investment-grade, fixed-rate, taxable bond market of SEC registered securities. The index includes bonds from the Treasury, Government-Related, Corporate, MBS (agency fixed-rate and hybrid ARM passthroughs), ABS, and CMBS sectors. U.S. Agency Hybrid Adjustable Rate Mortgage (ARM) securities were added to the U.S. Aggregate Index on April 1, 2007.

*The ActivePassive Funds investment objectives, risks, charges and expenses must be considered carefully before investing. The prospectus contains this and other important information about the investment company, and it may be obtained by calling 1-877-273-8635, or visiting [www.activepassivefunds.com](http://www.activepassivefunds.com). Read it carefully before investing.*

**Mutual fund investing involves risk. Principal loss is possible. Investment in the ActivePassive Funds may include risks associated with non-diversification, foreign securities, emerging markets, small and mid cap companies, ETF's, REITs, debt securities, high yield securities, and mortgage backed securities. The fund will bear its share of the fees and expenses of the underlying funds. Shareholders will pay higher expenses than would be the case if making direct investments in the underlying ETFs. Please refer to the prospectus for the risks specific to each fund.**

The ActivePassive funds are distributed by Quasar Distributors, LLC.

---

**Tim Clift** is FundQuest's Chief Investment Officer and is the lead portfolio manager of all of the ActivePassive Funds. He joined FundQuest in 1994. Tim has overall responsibility for the Firm's investment management programs for separately managed accounts, mutual funds, alternative investments, ETFs and annuities. As Chairman of the Investment Committee, Tim leads a team of analysts and portfolio managers that produce the research and portfolio recommendations for all client programs. He has over 18 years of industry and investment management experience. Tim earned his BA in Economics from Allegheny College and his MBA from Boston University.