

# Investment Policy Committee Notes

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## Economic and Stock/Fixed Income Market Outlooks

### Economic Outlook

#### Recent Reports

- Payrolls dropped in 34 U.S. states in September, led by California and New York, showing job losses were dispersed throughout the country. The labor market has been slow to improve as state and local governments cut staff to repair budget shortfalls and companies await increased sales.
- Retail sales in the U.S. climbed more than forecast in September, easing concern that unemployment stuck near a 26-year high will bring the recovery to a halt. Other reports showed inflation cooled and manufacturing in the New York region accelerated.
- Production in the U.S. unexpectedly dropped in September for the first time in more than a year, showing the industry that led the economy out of the recession is cooling. Inventory rebuilding, a component of the rebound last year, will probably cool following eight consecutive gains.

#### Upcoming Reports

- (10/25) Existing Home Sales (4.3m vs. 4.1m, +4.1%) & (10/27) New Home Sales (300k vs. 288k, +4.2%)
- (10/27) Durable Goods Orders (2.0% vs. -1.5%) & Durables Ex-Transportation (0.5% vs. 1.7%).
- (10/29) 3Q Advance GDP (2.1% vs. 1.7%) & Personal Consumption (2.4% vs. 2.2%). Also, GDP Price (1.9%) & Core PCE (1.0%).

#### Longer-Term Outlook

- The multi-decade tailwind of declining interest rates for bonds is likely over, so returns from traditional bond indexes will be low. Equity index prospective returns also look subpar relative to their long-term historical averages. With lower returns likely, it is a good time for investors to revisit their financial independence or retirement plan and make adjustments accordingly.
- In light of the above, we believe this is an environment that favors tactical asset allocation approach and opportunistic investments in asset classes and strategies outside of the standard stock and bond indexes.

### Market Outlook

#### Equity Outlook

- While we believe the odds are tilted towards a subpar return outcome for the stock market over the next five years, if some version of our Goldilocks scenario plays out then equities are likely to perform well and have less downside risk after the fact than we are assuming ex ante.
- Based on our analysis and assessment we remain underweighted to risk assets (equities) in our balanced portfolios. While this means our portfolios should hold up relatively well in a subpar or more negative scenario, they will likely lag if a bullish scenario plays out in the near term.

#### Fixed Income Outlook

- Money continues to flow out of U.S. equity mutual funds and flood into bond funds. While some (maybe much) of this activity is due to a rational reassessment by investors of their risk tolerance as a result of their experience during the market crash, we can't help but believe that some portion reflects investors' age-old and ill-timed habit of investing through the rear-view mirror rather than based on a disciplined forward-looking assessment.
- There is only so much return that can be squeezed out when the starting yield on the index is under 3%. Unlike equities, our five-year potential return range for the Barclays Aggregate Bond index is relatively narrow, ranging from a low of around 1% to a high of 2% across our scenarios.

## S&P 500 GICS Sector Performance and Recommended Sector Weightings

S&P 500 Sector	% Total Return			Forward P/E Ratio	Actual Sector % Weightings	Forward Looking
	MTD	YTD	2008			CB&T Sector Emphasis
Consumer Discretionary	3.3	17.2	41.3	15.4	10.4	Underweight
Consumer Staples	2.5	10.2	14.9	14.9	11.1	Marketweight
Energy	5.3	4.4	13.9	12.9	11.2	Marketweight
Financials	1.9	2.5	17.2	13.9	15.5	Underweight
Health Care	2.1	1.3	19.7	11.7	11.5	Marketweight
Industrials	2.8	16.5	20.9	16.0	10.7	Marketweight
Information Technology	4.9	4.8	61.7	13.8	19.1	Overweight
Materials	5.8	8.6	48.6	16.8	3.6	Underweight
Telecommunication	1.5	12.4	8.9	16.6	3.1	Marketweight
Utilities	2.7	7.1	11.9	12.8	3.6	Marketweight
S&P Composite 1500	3.3	8.1	27.3	14.5		
S&P 500	3.3	7.3	26.5	14.0		
S&P MidCap 400	2.3	14.2	37.4	18.2		
S&P SmallCap 600	4.1	13.1	25.6	20.6		

Sector recommendations are market-cap weighted, influenced by economic, fundamental, and technical consideration.

The above information is provided by outside data vendors; CB&T cannot guarantee the accuracy of the data provided.

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