

Client Conference Call Script October 2010

Good morning everyone, this is Ali Yousaf – Chris is booked in meetings this week, so Chad and I will be running today's call.

I'd like to begin by thanking all of you who have joined us today – this is our 3rd Quarter 2010 Market Update call. As usual, in order to keep to the time allotted, we will begin with commentary on the macro economic picture, and then Chad will lead in with an update on CIMCO portfolios. We are unable to comment on any client specifically, so please call us directly with any questions relating to your personal accounts.

September surprise? We'd say so...

After the double-dip worries that sent the market lower in August, investors have responded positively to the more encouraging economic reports that followed in various regions of the world. The market's September performance has bucked historical trends, and the choppy and corrective phase of the last two quarters appears to be giving way to a more sustainable advance.

With lackluster economic data, September seemed poised to maintain its status as the worst-performing month of the year – however, overly pessimistic sentiment, coupled with some better-than-expected data, led to the market posting solid positive returns.

The recent run in the market could be indicative of the general market direction during the coming months, although we expect pullbacks along the way if sentiment gets overly optimistic. During the most recent rally, stocks broke out of their latest trading range, providing more near-term momentum. Seasonal tendencies still suggest that stocks could face obstacles in October as this rally has taken place on low volume. Also, any number of developments could spark a sell-off – from renewed sovereign debt worries to currency concerns, to mid-term election uncertainties. Let's discuss these areas in more detail.

In the US, the potential restraining influences include: 1) the probability of a change in Congress (from Democratic to Republican or mixed), 2) likely tax increases, and most importantly, 3) the continuation of a secular bear market characterized by structural unemployment, deleveraging, and a retrenching consumer.

Businesses in general continue to cast a skeptical eye toward Washington – uncertainty regarding the regulatory environment, the costs of doing business, and whether tax rates will be increasing at the start of 2011, all have companies largely sitting on their hands. Though it will answer some of these uncertainties, the effect of the election on financial markets is often overblown, and most likely, has already been priced in. Historically, within the four year presidential cycle, the third year has tended to be the best for the

market, which Chad will discuss in more detail, but we are expecting more subdued performance this year over normal.

The Federal Reserve continues to fight an uphill battle trying to restore confidence to the business sector. Recent Fed comments, reiterated in the statement from the last FOMC meeting, indicate that the Fed clearly stands ready to implement another round of quantitative easing, to the extent economic conditions so justify.

The FOMC expressed concern that inflation wasn't high enough, and that they have a goal of actually raising the inflation rate. Clearly, the possibility of deflation remains a near-term concern, and the Fed stands ready with its finger on the trigger should the economy need another jolt of cash.

However, the quantity of money isn't the problem – it's the “velocity” of money, or getting money circulating in the economy, that is providing difficulty. Companies have plenty of cash on their balance sheets (not to mention interest rates remain historically low), but they remain reluctant to use it.

While the jobs report was decidedly lackluster, the household survey of employment indicated improving conditions. That doesn't mean that risk is off the table however. The unemployment rate remains stubbornly high – continuing to show readings between 9.5-10% as businesses remain disinclined to add to payrolls.

Recent housing data has been mixed. Existing home sales rose, but that was off from record lows, and with more foreclosures coming down the pipe and banks increasingly anxious to rid their balance sheets of homes on which they've already foreclosed, we believe that housing will continue to bounce along this bottom it seems to have found.

Globally, Europe still remains a source of anxiety, and China has been making headlines. The poor financial health of the PIIGS (Portugal, Ireland, Italy, Greece, and Spain), which have large deficits (shortfall on an annual basis), high debt (accumulated deficits), or a mixture of both, came into focus when Greece doubled the estimate of its 2009 deficit.

Concerns about debt led to the European bank stress tests, the goal of which was to enable investors to assess banks' foreign government debt exposure. However, banks' differing interpretations of the rules and disclosure caused investors to question the results, while the continued poor financial condition of many countries will continue to plague markets. The main question waiting in the wings?...When will the US have to start discussing the austerity measures that European countries already face?

The all-important Chinese markets are also likely to have an eye on the political situation as pressure from the United States is building for China to revalue its currency, and protectionist sentiment is building. At this point, it seems to be mainly a lot of tough talk, with little action taken by either side because the interdependence of the two countries warrants action to be undertaken with great caution.

We'll pause here, and hand it over to Chad to delve a bit deeper into the portfolio performance and investment outlook.

Thanks Ali, and thanks again to all of you that are joining us this morning.

As Ali was saying, the equity markets have posted some notable gains since the beginning September, and it seems that risk appetite is back on the table. I will assess this shortly, but first I'll start by briefly commenting on the market activity last quarter along with the main changes to our models. I will then take a minute and discuss what our expectations are for the fourth quarter, and what this will mean to our strategies.

Just like in Q2, third quarter of 2010 was dominated by heightened volatility, although this time it was more on a month-by-month basis. After a number of whipsaws during June, Q2 ended with another notable correction, as the S&P dropped more than 8% during the last half of the month. This reversed in July, giving the third quarter a kick-start with gains around 7% for both the S&P 500 and the Dow Jones Industrial Average. Although July was a bullish month and equities went up in a fairly straight line, volatility, as measured by the VIX, did not come down much, and eventually investors became risk averse again. After another round of weak economic data, along with investors digesting Ben Bernanke's assessment that the economic landscape is "unusually uncertain", another small correction hit the markets in August, bringing the S&P500 and the Dow down between 4 and 5%.

September has historically been the worst month of the year for equities. This year however, significant improvements in European and emerging equity markets, along with the Fed starting to discuss the potential for another round of quantitative easing, was a significant boost to investors as the month posted the highest September gains in over seven decades. The S&P 500 and the Dow added between 7 and 9% to end the quarter in the positive for the year. Although this was a great month for the equity markets, it is worth noting that the rally happened on the back of a devalued dollar. According to David Rosenberg, in euro terms the S&P500 was only up 1.5% for the month. However, this move definitely led to improvements in the markets, and it has made us more bullish than we were since we last spoke.

As far as our models go, the high volatility in Q2 and the beginning of Q3 lead us to keep our hedges on for most of the quarter. We did, however, start the process of reducing these as we saw improved conditions during September, and currently we do not have any short exposure in any of our models. Our 5050 and Momentum 1 models are currently fully invested, and we are gradually moving the Momentum 2 model up to full allocation. Our seasonality models are active again, and we had a really good trade in this strategy at the beginning of October.

From a technical viewpoint, all major indices have now moved well above both their short- and long-term moving averages; the Dow broke 11,000 for the first time since early May, and we are seeing higher highs and lower lows for most major indices, which

is a positive sign for the market. Economic data is still mixed, however, and although the National Bureau of Economic Research officially announced that the recession ended in June 2009, it certainly does not feel that way for the 40% of unemployed that have been looking for work for over 6 months. Regardless, equities are rallying, and, in our opinion, there are two factors that are currently driving the markets.

Number one is the November mid-term election. Typically what happens at mid-term election is that the incumbent party in the White House loses materially within the lower house of Congress, and this has historically been very positive for equities. We think investors believe this will happen again, and that they are anticipating this as we move closer to election date. According to the Stock Traders Almanac, mid-term election Q4-Q1 returns have averaged 15% for the S&P500, 14.4% for the Dow Jones Industrial Average, and 24% for the Nasdaq, so we could be entering a better period for equities.

The second factor currently driving equity markets are expectations around Quantitative Easing 2. Investors seem to have determined that another round of QE is good for the economy, and any indication that this will happen is considered good news. However, the Fed has stated that it is getting ready to make this move, but only if there are indications that the economy is not improving as much as desired. Because of this, unchanged or even poor economic data can be considered good news for the market, as this will increase the probability of QE2. Although we are concerned that QE2 might not have the impact investors are expecting, we are cautiously optimistic about the fourth quarter, and we hope that this will give us opportunities to gain some ground in our models.

With that, I will conclude this call by mentioning that the few major themes we have seen impact the majority of this year are still in play. Economic data has been stabilizing, though risks remain. Political and monetary tensions are being monitored closely. As always, we are keeping a close eye on the many factors, and are grateful for the opportunity to serve our clients and their portfolios. Thank you for your continued trust in our firm.

Have a great fall!