



*“Always do right. This will gratify some people, and astonish the rest.”*

Mark Twain

Third Quarter 2009

**In this issue:**

Review	1
Opportunities	1
Threats	2
Fiduciary Corner	2

Volume 3, Issue 3

# The Capstone Review

## REVIEW OF THE 2<sup>ND</sup> QUARTER 2009

The second quarter saw the equity rebound that began in early March continue with a vengeance through April and May. The quarter saw the S&P 500 Index gain 15.9%, though that was almost all from the surge that took place in April and May. With that terrific quarter, the S&P 500 was up a very modest amount for the year to date. While penning this report, the index has fallen back to negative territory for the year to date. The price to earnings ratio of the index closed the quarter at 21.3 based on

trailing earnings. This is an above average reading and is likely linked to the market's more recent stagnation. At Capstone, we enjoyed a good quarter that has left us with above market returns on a year to date basis. That performance has been driven by our increased exposure to corporate bonds. Bonds have done very well year to date, outpacing stocks while having significant dividend yields at the same time.

## OPPORTUNITIES GOING FORWARD

We began the year with a strong preference for bonds over stocks, so we increased our portfolio weightings for bonds. While that has been an excellent concept year to date, we believe things will be a bit tougher from here. Prices have risen in stocks, bonds, and closed end funds to where we still see some potential, but no real “fat pitches” (easy to hit home runs in the investing world). So, we believe most of the opportunities going forward will need a somewhat tactical approach. We still like emerging markets, some commodities,

and corporate bonds as the most likely winners in coming years. However, in both those areas and all others, we believe we need to carefully manage risk and look for opportunities as we go forward. We will still focus on trying to capture total return, limiting risk and grabbing returns when we can. So, you may see us buying when others are selling and selling when others are buying. In short, we expect a bumpy market that will necessitate skill to capture gains.



**CAPSTONE**  
investment financial group, inc

5555 DTC Parkway, Suite D2002

Greenwood Village, CO 80111

(720) 842-1249

Toll Free: 1-888-571-3713 [www.capstoneinvest.com](http://www.capstoneinvest.com)

615 North Nevada Ave.

Colorado Springs, CO 80903

(719) 447-9883

[info@capstoneinvest.com](mailto:info@capstoneinvest.com)

## ***Crafted Portfolios for the Thoughtful Investor***

### **THREATS GOING FORWARD**

The two primary threats going forward are caused by investor sentiment and the huge amounts of debt that has been incurred. Investor sentiment has been all over the board this year. Going into early March, we had panic selling and a rapidly declining environment for almost all assets. Then, we had a huge rally in which investors seemed to be saying that our problems were behind us. Now, we seem to have sentiment returning to neutral with a somewhat negative bias. The threat is that investors will return to panic mode and asset prices will plummet again. We would likely return to being a buyer in this circumstance, as we don't think investor sentiment has been based in reality this year. Remember, the twin towers of investor mistakes, fear and greed, have driven investors to do the exactly wrong maneuvers all year. At the moment of maximum opportunity in early March, they were selling and going to cash.

By the end of the rally in late May, they were busy moving from cash back to other assets.

The huge debt, on the other hand, is a threat we will live with for many years. It will cause what Bill Gross and Mohammed El-Erian have labeled the "new normal". The new normal includes slower economic growth, higher unemployment, and the emerging world becoming the primary source of economic growth. The new sobriety (i.e. we can't all have everything we desire right away) is not a bad circumstance, in our opinion. Opportunities for growth will appear and the U.S. will be able to prosper if it negotiates its challenges well. It is, however, a different circumstance. The road we will travel will be somewhat difficult and we need to make new decisions in order to get to our goals safely.

### **FIDUCIARY CORNER**

Our review of managers and positions has not led to any immediate portfolio changes this quarter. The managers we are currently using are performing up to expectations. As we look forward, we may take steps during the quarter to remove a bit more risk from the table, possibly increasing our shorter term bond holdings.

As an aside, there are currently SEC proposals to make all advisors fiduciaries (i.e. people who must put client's interests

first). There is organized opposition to this notion from the financial services industry. We applaud the SEC's idea here at Capstone. Client's interests are of paramount importance to us and we would like to see the industry shed those who put their interests or those of their firms before the client's. Any advisor unwilling to take on the mantle of fiduciary should in our opinion have zero clients at the end of the day.

Registered Representative—Securities offered through Cambridge Investment Research, Inc., a Broker/Dealer, Member FINRA/SIPC.

Investment Advisor Representative—Cambridge Investment Research Advisors, Inc., a registered investment advisor

Cambridge and Capstone are not affiliated.