

Investment Perspective

Fourth Quarter 2010

“Progress always involves risk; you can’t steal second base and keep your foot on first base” - *Frederick Wilcox*

SFP Core Strategies*	Quarter 4	
	2010	One Year
US S&P 500	10.71%	15.00%
US Large Value	12.91%	20.17%
US Micro Cap	17.68%	31.29%
US Small Value	18.83%	30.90%
US Equity Real Estate	7.41%	28.67%
International Large Value	7.46%	10.57%
International Small Cap	12.54%	23.91%
International Small Value	18.83%	18.10%
International Real Estate	6.39%	18.09%
Emerging Markets	8.81%	21.82%
Emerg Mkts Small Cap	6.97%	30.18%
Emerging Mkts Value	8.37%	22.06%
Ultra Short Fixed Income	0.05%	1.16%
Shrt/Inter Global Fixed Inc	-1.69%	5.30%
Inflation Protected Sec	-0.97%	6.81%
Model Portfolios		
SFP Balanced Portfolio	6.26%	13.47%
Non SFP Std Balanced	4.80%	10.35%

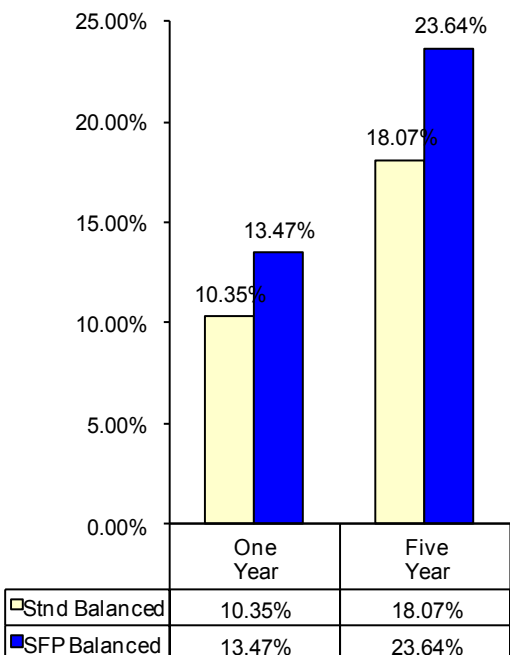
The past year unquestionably started with pessimism. Everyone, of course, was hoping for an economic recovery that brought jobs and prosperity, but fears of a double dip recession and concerns over U.S. debt levels were widespread. Many market professionals shared these concerns. One notable researcher who originally predicted the Great Recession of 2008 and 2009 was expecting “one of the biggest coordinated asset bust(s) ever.” Even the Economist magazine began the year with a cover story that warned of asset price bubbles and asserted that U.S. stocks were “nearly 50 percent overvalued.”

The headlines throughout the year provided even more reasons to keep money on the sidelines. Greece was teetering economically, the Gulf was awash in spilled oil, a flash crash sent the Dow down over one thousand points in just minutes and debt concerns swept through much of Europe with no clear solutions. In fact, eight months into the year, the S&P 500 Index was down 5.9 percent. But despite all that, 2010 finished as a great year to be a globally diversified investor.

The S&P 500 closed for the year up 15.06 percent, with 10.76 percent of the gain coming in the fourth quarter. Overseas stocks also did well, with 37 out of 45 countries tracked by MSCI registering positive returns. This drove our International Value strategy up 10.57 percent for the year and the Emerging Markets strategy up 21.82 percent. While large companies and large value stocks did well in 2010, small companies were up even more dramatically. Our U.S. Micro Cap and Small Value strategies were up about 30 percent for the year. Overseas, the same pattern existed with small outperforming large, but the effect was less pronounced. This size factor largely drove our relative performance. (*Please see the performance table.*)

The SFP Balanced Portfolio returned 6.26 percent for the quarter and ended the year 13.47 percent higher. This compares with 4.8 percent and 10.35 percent for the Non SFP Standard Balanced Portfolio, respectively. Over the five year period, our balanced portfolio was up 23.64 percent, versus the standard portfolio’s 18.07 percent. While we would obviously have liked higher five year returns, this leaves us questioning all the talk of a “Lost Decade” in the markets. How were these people investing? We didn’t lose a decade. We didn’t even lose five years.

Standard Balanced vs. SFP Balanced

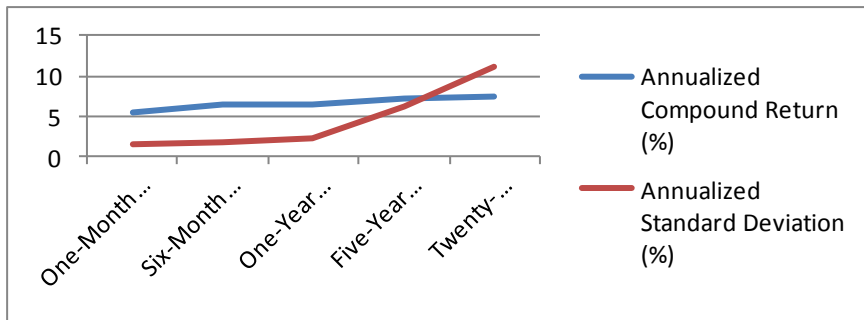


Fixed Income investments also had a good year, but the fourth quarter did see some weakness. Our intermediate bond strategy lost 1.69 percent during the quarter and our Inflation Protected Securities strategy's lost 0.97 percent. This downside in bonds resulted from a rise in longer term interest rates. Those who had locked in lower rates for longer periods of time saw the value of their investments decline as newer, more attractive rates became available. This effect can clearly be seen in the performance of the Vanguard Long-Term Treasury fund. It was down 8.24 percent in the fourth quarter. This is a pretty huge move for a fund that is only yielding about 4 percent.

In fact, most investor concerns we have heard over the last quarter concerned bond investments. We think the situation was summed up nicely by bond guru Bill Gross when he said that investors are left with the choice of "zero percent interest rates if you stay in cash, or probable principal losses if you take durational risk by buying 5 and 10 year maturities." For some time, we have favored the earlier approach by holding funds with shorter maturities and allowing more cash to build in money markets.

This worked to our favor during the fourth quarter when our ultra short strategy moved up 0.05 percent for the quarter, Vanguard's GNMA fund went up 0.39 percent and DFA's Selectively Hedged Global nosed up 1.61 percent. These are the three areas we have been focusing investor bond money. Moving money from the slightly longer termed intermediate strategy toward shorter term issues may sound suspiciously close to market timing or interest rate forecasting, but it is more of a near term expression of our long term fixed income philosophy.

We believe that when you build globally diversified portfolios, it is best to take most risk on the stock side where the upside potential is the greatest, and to use Fixed Income for diversification and safety. We do take some currency risk with a portion of the holdings that are not denominated in dollars, but we are not lured by higher yields into taking credit risk—the risk that you won't get your money back as bonds mature - or extending maturities. The following chart illustrates the issue when it comes to term risk. This chart shows the volatility and performance of various Treasury securities from 1964 through 2009.



As can be seen by the red line, volatility moves up gradually when moving from One-Month Bills to One-Year Notes. From that point, longer maturing bonds come with rapidly increasing volatility. Since we primarily want to take risk on the stock side where upside is unlimited, we choose to stay on the shorter, less volatile side.

US Treasury Securities	One-Month Bills	Six-Month Bills	One-Year Notes	Five-Year Notes	Twenty-Year Bonds
Annualized Compound Return (%)	5.57	6.33	6.53	7.27	7.31
Annualized Standard Deviation (%)	1.38	1.74	2.33	6.24	11.2

The investment outlook from many market forecasters has shifted from clearly pessimistic to cautiously optimistic. Had they got it right in 2009 and 2010, they would have been shouting from the rooftops how great the next couple years in the market would be. Of course, they did not. We still see plenty of good ingredients for market growth, and are hoping for a third straight year of solid returns.

Wishing you good health and happiness in the New Year!

Brian J. Skaggs, CFP

The information in this newsletter should not be construed as investment advice. Investment advice is only given in the context of individualized interactions that ideally result in the development of a continually evolving financial plan. *Total returns as measured by the performance of associated DFA funds - advisor fees not included in strategy performance. Advisor fees are subtracted from model portfolio performance at 8.3 basis points per month. This information is believed to be reliable, but we do not guarantee the accuracy of the information. **Past performance is not an indication or guarantee of future performance.**