THE PLANNING GROUP

A Wealth Management Firm

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The Markets

Former Federal Reserve Chairman Paul Volker was back in the news last week as he warned that the financial system needs broad reform or else we run the risk of another financial crisis.

You may remember Volker as the cigar-chomping Fed Chairman from 1979 to 1987 who raised interest rates dramatically to try and break the back of inflation in the early 1980s. He succeeded, but the price for success was a major recession.

During his speech last week to the Economic Club of New York, Volker argued that the Federal Reserve should be a key player in overseeing the financial system and that they, "should have the power to dismantle big banks that pose a systemic risk to the economy," according to CNNMoney.com.

Volker worries that as the economy continues to heal, the urgency for reform will fade and that will set the stage for the next crisis. While we will likely get some type of financial reform in coming months, we hope that it will preserve the principles that have made our country so great.

Ironically, on the day Volker spoke, the S&P 500 index hit a fresh 52-week high, according to Briefing.com.

Data as of 1/15/10	1-Week	Y-T-D	1-Year	3-Year	5-Year	10-Year
Standard & Poor's 500 (Domestic Stocks)	-0.8%	1.9%	33.6%	-7.4%	-1.0%	-2.5%
DJ Global ex US (Foreign Stocks)	0.3	3.0	55.9	-5.0	4.4	0.9
10-year Treasury Note (Yield Only)	3.7	N/A	2.2	4.8	4.2	6.8
Gold (per ounce)	0.1	2.2	39.3	21.6	21.7	14.7
DJ-UBS Commodity Index	-3.0	-0.8	24.0	-4.5	-1.1	3.7
DJ Equity All REIT TR Index	-0.1	-0.2	49.5	-13.4	1.5	10.6

Notes: S&P 500, DJ Global ex US, Gold, DJ-UBS Commodity Index returns exclude reinvested dividends (gold does not pay a dividend) and the three-, five-, and 10-year returns are annualized; the DJ Equity All REIT TR Index does include reinvested dividends and the three-, five-, and 10-year returns are annualized; and the 10-year Treasury Note is simply the yield at the close of the day on each of the historical time periods.
Sources: Yahoo! Finance, Barron's, djindexes.com, London Bullion Market Association.
Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested into directly. N/A means not applicable or not available.

BACK IN EARLY MARCH 2009, there was palpable fear in the markets. Our banking system was on the verge of collapse, unemployment was skyrocketing, and the stock market was touching 12-year lows. But on March 10, the collective psychology changed, the market turned around, and since then we've witnessed one of the greatest short-term bull markets in history.

What do we do for an encore in 2010?

Before we figure out 2010, we need to understand what drove the 2009 bull market. While it may be a little early to write the history of 2009, we can make some observations that provide a framework and context for the great reflation.

With the benefit of hindsight, here are some reasonable conclusions on what drove the 2009 bull market:

1. The Federal Reserve flooded the economy with easy money. This money had to go somewhere and some of it found its way to the financial markets.
2. With short-term savings rates near zero, investors had to move out on the risk spectrum (e.g., stocks, commodities, high-yield bonds) in order to have a chance at higher returns.
3. China implemented a massive stimulus program that kept their economic engine running and that helped goose other countries' economies.
4. There was a one-time re-pricing of risk as investors realized the world was not coming to an end, so they snapped up stocks that were perceived as "generational" bargains.

One of the tenets of investing is that there is "no free lunch." In this case, it means the government cannot endlessly flood the economy with stimulus. If they try, there may be repercussions such as unacceptable inflation, a crashing currency, and soaring deficits.

Here's the key question as 2010 unfolds: Can the economy get on a self-sustaining growth path without further government stimulus?

If we are over the hump and the economy is self-sustaining, that may bode well for the markets in 2010. Conversely, if the economy still needs substantial government help, investors may get nervous again. The tug-of-war between investors who believe the former versus the latter may be the defining dynamic in the 2010 market. Regardless of which comes to fruition, we'll continue to do our best to help you meet your long-term goals.

On The Economy[7]

Followers of the so-called "January effect" will be hoping that the month turns out on the plus side. They believe that the first month of the year gives a forecast of how the rest of the year will turn out. Evidence is mixed, and I wouldn't put too much store by it, but we'd all be happy if the year got off to a good start. I'd rather see strong 4Q earnings reports come in over the next few weeks.

Long-term Treasury rates and mortgage rates fell as the Consumer Price Index (CPI) and the "core" CPI (which excludes food and energy prices) advanced a meager +0.1% in December. That's evidence that inflation is not much of a concern at this time. Jobs and unemployment are what's on the radar these days.

The US dollar strengthened a bit against the Euro. That might seem surprising given the bulging trade deficit, but it reflects a growing confidence that increased world trade will be beneficial in the long run.

Oil prices dropped despite the cold weather chilling much of the country. Crude oil doesn't seem to be able to hold above $80 per barrel. If that continues, it should keep a lid on gasoline prices until we hit the summer driving season.

Tidbits[8]

The Last Decade – the "Big Zero" - We've seen lots of suggestions of names for the decade we just exited, but economist Paul Krugman is suggesting "The Big Zero". Why? "It was a decade with basically zero job creation, zero economic gains for the typical family, zero gains for homeowners, and zero gains for stocks, even without taking inflation into account."

The next decade – the "Terrible Teens" - What should we call the new decade? Investment News nominates "The Terrible Teens" ..."expect the 'new abnormal', with prolonged joblessness, wage stagnation, and a continued hollowing-out of the middle class."

Banks Biggest Risk - A review by U.S. bank examiners indicates the biggest risk to U.S. banks in 2010 is the potential losses on commercial real estate loans. The review found that such loans will likely affect smaller lenders, but will not pose a major threat to the financial system as a whole. One study suggests we should not be surprised to see 300 to 500 banks get taken over this year (compared to 150 in 2009).

Never Having To Say You're Sorry - The first public hearing of the Financial Crisis Inquiry Commission opened with testimony from the "barons of Wall Street," who acknowledged taking on too much risk and "choking on their own cooking," but stopped short of offering any type of apology for their role in the worst recession in decades. There was also a defense made of Wall Street pay practices. Whether they're correct or not, the political deafness of these presumably smart people is stunning.

Fannie, Freddie Lose $400 Billion – American Enterprise Institute (AEI) reports that taxpayer losses from Fannie Mae and Freddie Mac will top $400 billion. The AEI believes, "It turns out it was impossible to regulate them. They were too powerful and no one knows how much will be needed to keep the companies solvent."

Tax And Cut – The Committee on the Fiscal Future of the United States says the U.S. must soon raise taxes or cut government spending to curb its debt, and failure to act will risk a crippling dollar crisis. Despite promises to the contrary, many expect taxes to hit the middle class hardest.

Expired Tax Cuts - Congressional inaction caused 50 individual and business tax breaks to expire at the end of 2009. While most of them will probably be reauthorized retroactively, it does create inconvenience for some taxpayers. The "biggie," however, is the estate tax...

The Perfect Year To Die? - 2010 may be the year for wealthy people to die. As things currently stand, there is no estate tax (replaced with a substituted capital gains tax), with the estate tax will be reinstated in 2011 with a top 55% tax rate. While it seems likely that Congress will reinstate the estate tax for 2009, when and will it be retroactive (which appears quite likely)? What happens if an estate has already been settled before Congress reinstates the estate tax, with a group of Senate Republicans and moderate Democrats wishing to raise the $3.5 million exemption to $5 million.

Investors Pessimistic - According to Eaton Vance's 11th annual survey of Americans, most investors are pessimistic about the economy, with 82% saying the economy is either in recession or stagnant.

Silver lining? The Federal Reserve announced recently that it had made record earnings on its investments last year. The gains came from its efforts to rescue the country from the so-called Great Recession. The Fed earned a record windfall of $52.1 billion. Of that total, a record of $46.1 billion is turned over to the US Treasury Department.

Government Cover-ups, How High And How Low Can It Go? - Apparently AIG withheld important information about its dealings with financial counterparties in the lead-up to its collapse and bailout by the Federal Reserve. That is a given, but the most troubling aspect of this episode is that it was officials at the Fed (not AIG) who seem to have orchestrated the secretive and potentially illegal activities. This was uncovered only through an investigation conducted on behalf of the House Oversight and Government Reform Committee. The New York Fed, led by our present Treasury Secretary Timothy Geithner, apparently told AIG to withhold details from the public about credit default swap payments it made to Goldman Sachs and Deutsche Bank.

Weekly Focus – Think About It

Our thoughts and prayers are with the people of Haiti and the relief workers who are trying to help them.

Best regards,

The Planning Group Investment Team

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[7] The source for the information for On The Economy was derived from Bob LeClair's Finance & Markets Newsletter.

[8] The source for the information for Tidbits was derived from The Virtual Advisor.

* The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general.

* The DJ Global ex US is an unmanaged group of non-U.S. securities designed to reflect the performance of the global equity securities that have readily available prices.

* The 10-year Treasury Note represents debt owed by the United States Treasury to the public. Since the U.S. Government is seen as a risk-free borrower, investors use the 10-year Treasury Note as a benchmark for the long-term bond market.

* Gold represents the London afternoon gold price fix as reported by the London Bullion Market Association.

* The DJ Commodity Index is designed to be a highly liquid and diversified benchmark for the commodity futures market. The Index is composed of futures contracts on 19 physical commodities and was launched on July 14, 1998.

* The DJ Equity All REIT TR Index measures the total return performance of the equity subcategory of the Real Estate Investment Trust (REIT) industry as calculated by Dow Jones.

* Yahoo! Finance is the source for any reference to the performance of an index between two specific periods.

* Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance.

* Consult your financial professional before making any investment decision.

* You cannot invest directly in an index.

* Past performance does not guarantee future results.

* This newsletter was partly prepared by PEAK, various commentaries, and our office.

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Scottsdale Office - 8800 N. Gainey Center Drive - Suite 176 - Scottsdale - Arizona - 85258-2122
Sun City West Office - 13912 W. Stardust Blvd. - Suite 119 - Sun City West - Arizona - 85375
Telephone (480) 596-1580 - (888) 596-1580 - Fax (480) 596-2165 - e-mail - kris@theplanninggroup.com