

Schultz Financial Mgmt Corp - Investment Commentary

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Dear Investors,

When I wrote my last commentary on January 10th, I mentioned that the 6 week stock market rally was at risk. Sure enough, stocks continued to decline on the heels of Bank of America's financial woes. Last month proved to be the worst performing January on record with both the S&P 500 and Dow Jones Industrials down over 8.4% by month's end. Investors braced themselves for a retest of the November lows, but the market averages seemed to find solid support 7% above the November lows after government officials talked of a "bad bank" structure being created to move toxic loans off banks' ledgers.

In late December, the 30 year US treasury bond reached a record low yield of only 2.9%, as treasury bond values soared to all-time highs. Since then, long term treasury bond prices have been in a steady decline as yields have risen. However, both investment grade and high yield corporate bond values have held steady, even while stock markets declined. This narrowing of corporate bond spreads is a healthy sign for the credit markets.

Our Investment Styles:

Core - Dividend Income Stocks:

Our Dividend Income Stock strategy is a core basket of dividend paying value stocks and is managed with the intention of staying fully invested through market cycles. Because we have had less exposure to the volatile financial sector, we have experienced less volatility and have continued to outperformed our benchmark, the Dow Jones Industrial Average. However, consumer staples have been under performing as Kraft Foods, and Proctor and Gamble (which we own) have cut their earning projections as their sales have slowed considerably. We are currently overweight in health care, consumer staples, and industrial manufacturing (defense/aerospace sectors).

According to Valuengine.com, health care stocks, energy, and consumer staples are the most undervalued sectors.

Trend Following Stocks:

Our trend following stock strategies are intended to capture the upside potential of stocks, but preserve capital during severe market declines. I follow an intermediate term trend (i.e., 6 weeks) and quickly adapt to trend changes. Prior to last year, I would typically switch to a market neutral position (e.g., money market or hedged position) during brief down trends about twice a year. Since October of last year, market volatility has increased to twice that of typical bear market levels. As a result, we are taking a more gradual approach to adding stock positions when new up-trends begin, and often times, may exit our positions quickly.

Again, in early January, I moved to a market neutral position in stocks, while maintaining some high yield bond positions. I began adding stock positions again on January 28th and we are now about 60% invested in stocks, 35% in bond funds (mostly corporate high yield), and hold a small position in precious metal funds. As I mentioned last month, while our objective is to capture the upside potential of stock markets, we may hold upward trending bond funds as an alternative to money market.

South American and Asian stock markets (excluding Japan) are outperforming US markets, while European markets are lagging. Technology, health care, and energy stocks have been the strongest performing sectors. Our global strategy is invested accordingly.

Trend Following Bonds:

Our trend following bond strategy normally invests in high yield corporate bond mutual funds, but switches to cash (i.e., money market) during down trends in order to preserve capital. We shifted from cash into corporate bond funds (both investment grade and high yield) throughout the month of December and despite the stock market volatility, these funds have held steady and we continue to hold our positions, earning very attractive dividend yields ranging from 7-11%.

Our Current Outlook:

I continue to believe that high yield corporate bonds offer much more of a compelling value for investors than stocks, and will compete with stocks as cash comes out of treasuries and money markets funds back into riskier securities. Short term (1-3 year) investment grade corporate bonds are particularly attractive with many yielding 6%-9% or more.

Please give me a call if you have questions or comments about this investment commentary or if you would like to discuss your investment allocations.

Sincerely,

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