The Barometer Investment Strategy

Barometer Capital LLC

Dynamic Portfolio Management
For Changing Economic and Market Conditions

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The purpose of this presentation is to discuss and explain the philosophy, approach and structure of Barometer Capital's investment strategy.

It encompasses the concept of dynamic asset allocation – wherein the asset-class allocation in our Model Portfolio is adjusted over the course of economic and market cycles to achieve superior returns with less risk.

We utilize econometric decision rules to objectively gauge the prospects for stocks versus bond – and incorporate the results into a dynamic portfolio management system that adjusts asset allocations systematically.

Those who find the strategy appealing can subscribe to our free monthly newsletter, the "Barometer Capital Report," which provides the information necessary to implement the strategy on an ongoing basis.

Representative Investment Vehicles

	Mutual Funds (used for Barometer performance metrics)	**Exchange Traded Index Funds (ETFs)**
Stocks	Vanguard 500 Index (VFINX)	SP500 Spydrs (SPY)
Long Term Bonds	Vanguard Long-Term U.S. Treasury (VUSTX)	iShares Lehman 20+ Year Treasury Bond (TLT)

References will be made to the generic asset classes: stocks and long-term bonds. While the analyses contained in this presentation could have been based on publicly available indexes, investors can not invest in indexes directly. For that reason, we have chosen to base our findings on the results of publicly available index funds. Listed above are representative examples of index funds.*

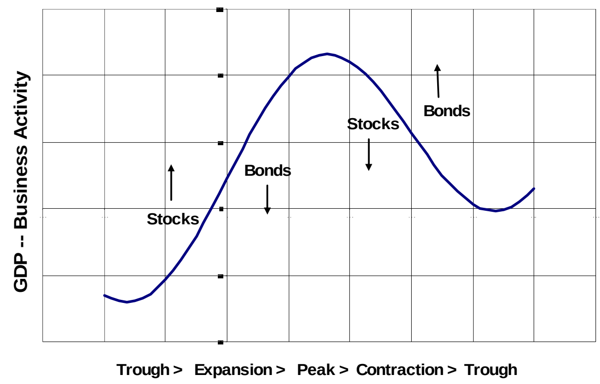
With regard to traditional mutual funds, the two Vanguard funds shown above are well respected examples with no front-end loads and low annual expense rates; however, many other no-load mutual funds are available as well. Of note, the historical and current results for these funds are used in calculating the performance statistics in this presentation and in our monthly newsletter.

Exchange Traded Funds also offer index funds focused on specific asset classes. Two representative examples are shown in the third column, however again investors should note that other ETFs are available as well. Many investors find ETFs to be advantageous relative to traditional mutual funds, because they have no minimums, trade during the market day like stocks, and do not declare capital gains distributions at the end of the year. Barometer Capital does not recommend one over the other.

It is up to each investor to select the index funds they think are most appropriate to their situation, including considerations as to what funds are available through their broker or 401K plan.

*Investors should note that the above-named mutual funds have been picked by Barometer Capital solely for illustrative purposes and should not be deemed recommendations for investments.

U.S. Economic Cycle
Prospects for Stocks and Bonds



Fundamental economic theory argues that the outlook for stocks and bonds follow the business cycle in predictable ways:

1. The prospects for stocks are most favorable during the expansion phase, when interest rates are low, business activity is rising, and companies are reporting strong increases in sales and profits.
2. The unfavorable times for stocks occur during the contraction phase, caused by a recession, when the same factors are reversed.
3. The unfavorable times for bonds are when the expansion is in full swing. As the demand for credit goes up, so do interest rates. Simultaneously, the Federal Reserve begins raising interest rates to cool down the economy and avoid fueling inflation. Higher interest rates cause bond prices to fall.
4. The prospects for bonds are most favorable in the contraction phase, when the Federal Reserve is working to stimulate the economy by lowering interest rates.

So, why would you want to be invested in bonds during the expansion? And why would you want to be in stocks during a contraction? Alternatively, why would you want to deploy a fixed asset allocation over the full course of the cycle, when you know that at certain times the prospects for a given class are clearly unfavorable.

It is only logical that portfolio returns could be increased by properly adjusting the allocation to specific asset classes over the course of the economic cycle. This is the fundamental concept behind the Barometer Investment Strategy.

Weather Barometer

Inches of Mercury	Forecast	Probability of Rain
31.0		
-	*Very Dry*	0%
-		
-	*Fair*	10%
30.0		
-		
-	*Change*	30%
-		
29.0		
-	*Rain*	70%
-		
-	*Stormy*	90%
28.0		

We adopted the trademark "Barometer", because our decision models have been engineered to produce outputs ("readings") that are analogous to the way a weather barometer is used to gauge the outlook for the weather – forecasting both the nature of the weather and the probability of rain.

As a quick review, a weather barometer measures atmospheric pressure in terms of inches of mercury. These readings have been statistically correlated to the prospects for the weather in the next 12 to 24 hours:

- When the pressure is very high, the upcoming weather tends to be clear and fair, with little chance of rain.
- When the pressure is very low, storms are anticipated with a high chance of rain.

If you are a fisherman in Maine, using this information is pretty straightforward. When the pressure is 30.5, that's the time to go to the outer banks to try for a big haul. When the pressure is 28.5, that's the time to keep your boat in the harbor and mend your nets.

If you had similar barometers for your investments, using this information would also be straightforward. When the forecast is favorable, you would be fully invested. When the probability of rain (losses) is high, you would take your money off the table.

Successfully developing such barometers for stocks and bonds has been the key breakthrough for the Barometer Investment Strategy.

Econometric Stock Barometer

For Period from 1980 to 2009

Stock Baromenter Reading			Average S&P 500 Return Over Next 12 Months	% of Periods with a Loss
90	to	100	25.9%	0%
80	to	90	21.3%	12%
70	to	80	19.8%	9%
60	to	70	21.7%	3%
50	to	60	20.7%	3%
40	to	50	16.5%	0%
30	to	40	5.9%	14%
20	to	30	6.0%	34%
10	to	20	-2.5%	54%
0	to	10	-13.9%	91%
Overall Average			12.1%	22%

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This exhibit introduces our proprietary Stock Barometer and reviews its historical performance relative to the S&P 500 index* over the 30-year span of our database, which embraces a total of 348 holding periods of 12 months each.

The body of the table displays the 12-month forward returns for the S&P 500 as a function of the Stock Barometer reading at the beginning of the period, where the readings (ranging from 0 to 100) are grouped into 10 percentile brackets.

- When the Stock Barometer reading was between 90 and 100 (the top bracket), the market delivered an average return of 25.9% over the following 12 months, without a single period experiencing a loss.
- When the Stock Barometer reading was very low (0-10), the market produced an average 12-month return of –13.9%, experiencing losses in 91% of the periods.
- Readings in between the high and low percentile brackets delivered results on a generally sliding scale between the two extremes (though not perfectly so).

The bottom line displays the average 12-month performance of the S&P 500 index during this period: It delivered an overall return of 12.1% per year. In doing so, it experienced losses in 22% of the years (roughly 1 out of 5).

Over the last 30 years, it was much more profitable to be in the stock market when the Stock Barometer reading was high than when it was low. And, the econometric relationships underlying the Stock Barometer have been validated as statistically significant.

*Note: Investments can not be made directly in an index, such as the S&P 500. The returns shown are from the Vanguard 500 Index Fund (VFINX) and are gross of all transaction fees/costs and taxes typically associated with mutual funds investments.

Econometric Stock Barometer (1980-2009)

Very Favorable vs. Favorable vs. Unfavorable

	Stock Barometer Reading			Average S&P 500 Return Over Next 12 Months	% of Periods with a Loss
Very Favorable	90	to	100	25.9%	0%
	80	to	90	21.3%	12%
	70	to	80	19.8%	9%
	Category Average			22.3%	7%
Favorable	60	to	70	21.7%	3%
	50	to	60	20.7%	3%
	40	to	50	16.5%	0%
	30	to	40	5.9%	14%
	Category Average			16.2%	5%
Unfavorable	20	to	30	6.0%	34%
	10	to	20	-2.8%	54%
	0	to	10	-13.9%	91%
	Category Average			-3.6%	60%
	Overall Average			12.1%	22%

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As shown by this chart, the Stock Barometer provides a systematic and objective decision-rule for determining the general prospects for stocks over the next 12 months. This information can then be used in determining appropriate asset allocation in an investment portfolio to achieve superior returns.

When the Stock Barometer reading is below 30, the prospects for stocks are unfavorable. Historically, readings in this range have preceded 12-month holding periods with an average return of -3.6%, with losses experienced in 60% of the cases.

Between 30 and 70, the Stock Barometer reading is considered favorable, with average returns of 16.2% and losses experienced only 5 % of the time.

Above 70, the readings are considered very favorable, as annual returns have historically averaged 22.3%.

Thus, by investing in stocks only when the Stock Barometer exceeds 30, we can achieve superior results by avoiding periods when fundamental economic and market conditions are unfavorable to stocks.

Econometric Bond Barometer (1980-2009)
Favorable vs. Favorable vs. Unfavorable

	Bond Baromenter Reading	Average S&P 500 Return Over Next 12 Months	% of Periods with a Loss
Very Favorable	90 to 100	24.4%	0%
	80 to 90	14.7%	9%
	70 to 80	12.1%	12%
	Category Average	17.1%	7%
Favorable	60 to 70	13.2%	0%
	50 to 60	14.2%	3%
	40 to 50	9.8%	3%
	30 to 40	7.7%	12%
	Category Average	11.2%	4%
Unfavorable	20 to 30	3.0%	36%
	10 to 20	2.2%	40%
	0 to 10	4.8%	23%
	Category Average	3.3%	33%
	Overall Average	10.6%	14%

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Our second proprietary indicator, the Bond Barometer, shows similar capabilities relative to the returns on long-term Treasury bonds.* Investing in bonds was far more lucrative, with a lower chance of experiencing losses, when the Bond Barometer reading was high than when it was low. These relationships, as well, have been validated statistically.

With the combination of the Stock and Bond Barometers, we now have objective, metric gauges that can tell us which asset class has the best prospects at a given time in the economic cycle. Just as importantly, changes in the Barometers provide the information needed to transition from one to the other in a timely manner as new economic dynamics unfold.

We therefore now have the requisite tools for constructing a dynamic asset allocation system that can provide the asset-class tilt that we desire.

*As measured by the performance of the Vanguard Long-Term U.S. Treasury Fund (VUSTX) before transaction fees/costs and taxes.

Dynamic Portfolio Management System

Using a Proprietary Asset Allocation Algorithm

- Changes implemented once a month based on the readings of the stock and bond barometers
- Each monthly adjustment is less than 10%.
- Asset mix changes systematically over time to overweight the asset class with the most favorable prospects.
- Cash is an alternative when prospects for both stocks and bonds are unfavorable.
- Mix can move from 100% stocks to 100% bonds.

Because this is an investment strategy, not a trading strategy, we do not have to monitor the economy and markets daily. Nor do we have to make frequent allocations adjustments. More specifically, we recalculate our Stock and Bond Barometers once a month based on the most current economic and market data available. Constant monitoring is not required.

Appropriate adjustments to the portfolio mix are, therefore, also made only once a month – with the magnitude of any adjustment limited to under 10% of the portfolio value. No gut-wrenching decisions affecting large portions of the portfolio.

Accordingly, the asset mix changes systematically over time, overweighting the asset class that has prospects for the highest returns and the lowest chance of losses. Indeed, if the prospects for both stocks and bonds are unfavorable, the allocation system moves money into cash.

Over the course of the economic cycle, the portfolio can move from a 100% allocation in stocks to a 100% allocation in bonds and vice versa. The strategy does not require a minimum level of investment in either asset class.

That said, some investors may find this range of outcomes to be too aggressive for their particular requirements or risk tolerance. For example, a more conservative investor may not want the allocation to stocks to drop below 30%, nor the allocation to bonds to drop below 20%. In this case, the Barometer Strategy could be used to determine the allocation in the remaining 50% of the portfolio – the portion set aside for dynamic asset allocation.

Barometer Strategy Performance[1]

Back-Tested Historical Returns ending Dec 31, 2009

	Barometer Strategy	Fixed 60/40	Stocks
10 Years: Annual Return[2]	8.8%	3.7%	1.1%
Years with a Loss	1	3	4
Cumulative 10-Year Gain	102%	38%	-10%

[1] Prior to January 2004, the performance returns in this chart are hypothetical, based on back-testing the Barometer Strategy. After January 2004, they are based on published recommendations in the monthly Barometer Capital Report.

[2] Equals the arithmetic average of the respective 12-month returns.

Shown here are some performance statistics for the Barometer Strategy over the last 10 years ending December 31, 2009.

Comparison statistics are presented for two fixed allocation strategies. “Fixed 60/40” refers to a portfolio consisting of 60% stocks and 40% long-term bonds. This represents a particularly good benchmark for gauging the performance of the Barometer Strategy, because it is diversified across both stocks and bonds, the two asset classes incorporated in our dynamic asset allocation strategy. It is also generally representative of the allocation strategy adopted by many pension funds and, therefore, reflective of the results achieved by professional investment managers.

Over the 10-year period, Barometer’s return of 8.8% was more than double the 3.7% return produced by the Fixed 60/40. Furthermore, the Barometer Model Portfolio experienced a loss in only one year, as opposed to three years for the Fixed 60/40. As a result, the cumulative gain in the Barometer Portfolio (with dividends reinvested) was 102% (before taxes). That’s over 2.5 times the 38% cumulative gain of the Fixed 60/40 Portfolio.

Meanwhile, over the same 10 years, the Barometer Strategy even more dramatically outperformed the stock market (8.8% versus 1.1%) while experiencing only one loss year versus four for stocks.

Barometer Strategy Performance

Previous 10 Years by Year

	Barometer Strategy	Fixed 60/40 Allocation Portfolio	S&P 500 Index
2000	18.8%	2.5%	-9.1%
2001	3.4%	-5.5%	-12.0%
2002	13.5%	-6.6%	-22.2%
2003	27.3%	17.2%	27.9%
2004	10.9%	8.9%	10.9%
2005	4.8%	5.3%	4.8%
2006	15.6%	10.1%	15.6%
2007	5.8%	7.8%	5.8%
2008	-35.2%	-13.9%	-37.0%
2009	23.4%	11.0%	26.5%
Average 10-Year Gain	8.8%	3.7%	1.1%
Cumulative 10-Year Gain	102%	38%	-10%

This exhibit displays the most recent 10-year perfomance on a year-by-year basis.

Of particular note is the manner in which the Barometer Model Portfolio successfully sidestepped the 2000-2002 bear market. By being largely in bonds during this period, our portfolio would have recorded gains during all three years of the downdraft – instead of the cumulative loss of 38% that was experienced by the S&P 500.

Unfortunately, our strategy was not able to similarly sidestep the bear market of 2008. The primary reason was that the stock market collapse was triggered by a financial crisis, not by weakening economic fundamentals due to an evolving business cycle. Therefore, the underlying econometric relationships of our Stock Barometer did not anticipate the dramatic loss of confidence that led to the stock market crash. That said, our models have since been revised to include new monetary policy variables that would have significantly reduced our losses had they been incorporated in our Stock Barometer at the time.

Also of note, when compared to the benchmark Fixed 60/40 Portfolio, the Barometer Strategy delivered superior returns in seven out of the ten years.

Barometer Strategy Summary

- Investment decisions based on objective and statistically validated econometric models.
- Dynamically adjusts portfolio to changing economic conditions -- toward most attractive asset class.
- Easy to implement. Small monthly adjustments without the need for frequent monitoring or gut-wrenching decisions.
- Achieves superior risk-adjusted returns.

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In summary, the Barometer Investment Strategy offers an effective alternative for investors striving to achieve their goals in an ever-changing economy:

1. It bases investment decisions on the results of objective econometric decision rules that have been rigorously validated over a 30-year span of economic and market data – not on intuition, subjective judgments, or speculative economic theories.
2. It dynamically adjusts the composition of the portfolio in favor of the asset class most favored by today's economic conditions – to deliver more attractive returns than a fixed allocation strategy with fewer years of losses.
3. It is easy to implement, requiring only one decision per month impacting a small percentage of one's portfolio. It avoids the frequent monitoring and hand-wringing decisions that are common for market-timing strategies.
4. In doing so, it achieves superior returns on both an absolute and risk-adjusted basis.

The Barometer Strategy is the right alternative for investors seeking attractive returns at a comfortable level of risk using an easy-to-implement process. It allows our investors to eat well *and* sleep well through the turmoil and uncertainty of the economic cycle.

Disclosures

- The information herein is assembled from sources that are believed reliable, but the accuracy of the data or conclusions cannot be guaranteed.
- Indicated performance metrics are illustrative, reflecting a back-testing of the strategy over history, not the results of actual investments.
- Past performance does not guarantee future results. There is always risk in using past experience to project future performance.

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The Barometer Economic Model and the performance of its recommendations are grounded in a 30-year historical database of key variables related to the U.S. economy and financial markets, dating from January 1980 to December 2009.

We believe that the data sources, analyses, and resulting conclusions are reliable, but their accuracy cannot be guaranteed.

Performance metrics that are presented reflect a back-testing of the strategy. They do not reflect the results of actual investments.

The findings in this presentation reflect the behavior of the economy and the markets over several economic cycles; however, there is always risk that underlying dynamics will change over time. Past performance does not guarantee future results. The burden rests on the investor to choose his/her own basis for making investment decisions relative to the future.