



PERSPECTIVES

JANUARY 2011

NUMBER 50

First Quarter 2011

Connecting the dots; that is what investing is all about, especially this past year. In forecasting, a picture of the future is rarely clear. It is most often sketchy, fuzzy, fraught with contradictions and incomplete. However, experience allows us to pick out the important elements and infer what the rest looks like. As investors, we have to forecast and anticipate. By the time the picture is obvious, the early birds have already taken most of the worms.

Since March 2009, we have been saying that this economy was in the early phases of recovery. Although more extreme than anything we had seen before, the elements of decline and recovery looked like other patterns we had seen before. In fact, the pattern and psychology attendant with what was happening looked classical. This gave us confidence in our prediction. Along the way, evidence mounted that indeed the economy was recovering; the dots lined up.

This past year the economy continued to improve and the stock market reflected that improvement. Profits have been able to increase at a much faster pace than the

economy at large because of companies' improving efficiency and, in many cases, their participation in markets outside of the U.S. that are growing far faster than ours.

Nevertheless, the stock market did go through difficult phases. In the spring it was rocked by a crisis in European sovereign debt markets, as well as a flash crash of almost a 1000 Dow points that has never been fully explained. During the latter part of summer, investors worried about a return to recession - a double dip. However, the economy maintained its bearings, corporate profits continued to mount, the stock market recovered and in the end produced excellent gains (see the Indices section of this report).

Interest rates went to unbelievable lows as fearful investors sought safety. In fact, bond mutual funds received an enormous amount of new money to invest when rates were at their lowest. Riverplace Capital sounded the alarm that the bond market was overdone and likely to produce losses for the most recent investors. By the end of the year that is exactly what happened as interest rates began rising.

Forecast

Economy

Unevenly but persistently is how we believe this economy will continue to recover. We will have periods of both acceleration and deceleration. The underlying imbalances in our economy will take years to resolve, not months. There needs to be a shift to production from an over emphasis on consumption. The U.S. needs to earn its way in the world and provide as much value to the rest of the world as it takes.

That means that we need to become much more energy self-reliant. Our exports will need to better match our imports. These adjustments will take time, effort, and some sacrifice. These changes will happen either by design or as a result of market forces; probably some of both.

Riverplace Capital believes that economic growth is currently accelerating. We predicted this months ago, believing that once the election was out of the way, and

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Talk With Us

P/E ratios, there is a lot of mystery about this simple measurement. Not only does the prevailing level for the market average P/E change over time, there is at any given time a wide disparity from company to company.

A P/E is a simple ratio of the price of a stock divided by its earnings. The earnings number can be for the most recently completed earnings period or the estimate for the upcoming year. Most of the time it is forward looking; for the current or forward year.

P/E ratios are a benchmark for value. It is how much investors are willing to pay for the earnings a company produces. If interest rates are low, and fixed income (the alternative to equities) doesn't offer much of a return, investors are more inclined to invest in stocks, buying a future stream of earnings. Because there is competition for stocks, prices may be bid up and therefore P/Es are higher during low interest rate environments.

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Notice

Riverplace Capital offers our clients *free* financial planning. We believe strongly in the value of planning as it helps document goals and objectives, and provides a benchmark to measure progress. Planning helps us provide better, more targeted financial service to you. If you would like a financial plan, contact your portfolio manager at (800) 391-1212

MAJOR INDICES AS OF 12/31/2010

| | |
|----------------------------------|-------|
| Large Cap Stocks (S&P 500) | 12.8% |
| Dow Jones Industrial Average | 11.0% |
| Mid Cap Stocks (S&P 400) | 24.9% |
| NASDAQ Composite | 16.9% |
| Small Cap Stocks (Russell 2000) | 25.3% |
| MSCI EAFE | 4.9% |
| Barclay Aggregated Capital Index | 8.9% |
| Inflation | 0.8% |

(EQUITY INDICES ARE TWELVE-MONTH RETURNS EXCLUDING DIVIDENDS)



Forecast *(continued)*

when cooler weather and the holidays came around, consumers would return to the stores and the economy would get another lift. Once Christmas is over we would not be surprised by some consumer consolidation and a little slacking of demand; in other words – normal. For the entire year we expect growth to average a little higher than it did last year for reasons stated in the next section.

Equities

With stimulus from the Federal government continuing through the extension of current tax rates and additional cuts, as well as the Fed pumping almost another 600 billion dollars into the economy through quantitative easing, the economy and the stock market have a powerful wind to their backs. We expect stock prices to continue to recover and better reflect the improved profitability of so many public corporations. It will not be a straight line; it never is.

We expect periodic return of European debt concerns, rising interest rates, inflation worries, deflation worries, recovery doubts, terrorism, war, and others risks that we cannot foresee;

in other words, a normal year in the world we live in today.

Fixed Income

Higher, that is what we forecast for interest rates. Bond prices peaked and interest rates bottomed at precisely the time that the Fed announced its quantitative easing program (remember that as bond prices increase, yields decrease). Quantitative easing is a fancy term for the Fed buying bonds to hold in its own portfolio. It gets the money to buy them by creating currency; it prints dollars.

Printing more dollars could be construed as inflationary. However, if the overall money supply is contracting, which it has been, then the effect may not be inflationary, but merely an aid to getting the economy moving. Nevertheless, inflationary or not, we expect interest rates to rise. They have been too low and do not reflect the strength we are seeing in the economy.

Talk With Us cont'd

This ratio also may vary dramatically from company to company. A firm that is growing its earnings rapidly will usually command a much higher P/E ratio. That is because investors are willing to pay more today because the ratio will rapidly fall as the earnings quickly increase. By contrast, a company that is stagnating will not command a premium P/E, but may instead have a discounted one since investors see little incentive to own such a firm.

Today the market average P/E is below what has been historically the norm. It is especially low when compared to the low interest rates prevailing. This is not how the relationship of P/E's to interest rates is supposed to work; so what is going on? In a nutshell, investors either do not believe that current low interest rates will last very long and will go much higher, or earnings levels today cannot last and will soon fall.

If one or both of these does not happen, then the market has it wrong and P/E's may move higher. There is another reason that P/E ratios can be suppressed; it is fear. If there is a pervasive atmosphere of fear, then investors simply do not have confidence in any prediction and/or value. When confidence improves, there can be plenty of upside for stock prices. This is what we at Riverplace Capital believe is giving us such wonderful opportunities today;

Talk with Us.

Investment Strategy

Equities

We are following the growth and we are finding a lot of opportunities. Because of pervasive fear as a result of the recent financial crisis, the price of growth is as cheap as we have ever seen it. There is plenty of opportunity and cheap prices; what a country.

Our growth themes have been working; clean water, green energy, participation in faster growing foreign markets, internet services, and the mobile internet. These have not been the only areas where we have been looking. Agriculture and industrial renaissance have also become fertile ground for finding winners. Growth is the key, wherever we can find it at very favorable prices. When prices get out of hand, we have sold and/or looked elsewhere.

Fixed Income

Short and shorter; it is the only way to handle a rising rate environment. By keeping maturities near term, it avoids losing capital when prices are driven lower and provides regularly maturing bonds to reinvest in higher and higher rates. That is how we are postured at Riverplace Capital. That is how we intend to stay.

Wealth Management

We have made some adjustments. We have reduced bond exposure and increased domestic equity exposure. We see the U.S. stock market as having the most favorable potential over the coming year.

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