



Historical Performance: 2000-2010

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Longtime clients will remember that we had an outside auditor determine 5 year investment performance for the period 2000-2004 for those clients who had managed portfolios during that time.

We have updated our investment performance for the period 2005-2010 on an unaudited basis and show performance data for both periods and the combined 11 year period in the table below.

The client makeup for the 2005-2010 period includes all managed accounts, excluding those which had dedicated fixed income portfolios.

While there are differences in the makeup of the various portfolios in terms of risk level, asset allocation, etc., we believe that the data shown below are a reasonable reflection of our overall investment performance.

While the last 10 years have been difficult for equity investors, we are pleased that our performance meaningfully outperformed the S&P 500 Index.

Our defensive posture in bear markets was the single most important reason for our performance. We expect to continue with this approach in the current market environment.



Tom Koehler
Partner

	<u>2000-2004</u>			<u>Compounded Annual Growth Rates</u>		
	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>01/01/2000</u> <u>12/31/2004</u>	<u>01/01/2005</u> <u>12/31/2010</u>	<u>11 year</u> <u>Cumulative</u>
Grant Koehler & Levin Managed Accounts	12.4%	23.2%	(24.7)%	6.4%	4.2%	5.2%
S&P 500 Index	12.8%	25.5%	(37.0)%	(2.3)%	2.2%	0.1%

- ◆ 2000-2004: The audit begins with the first full calendar year for which the investment style was implemented by the advisor. Audit report available upon request. Information shown includes performance while Chris Grant was employed with another investment advisor through March of 2003. Mr. Grant was primarily responsible for the performance generated through this date, and the investment style used to manage the advisor's accounts was substantially the same throughout the five year period.
- ◆ 2005-2010: Data shown is unaudited. Results are for all GKL clients, except those who had a dedicated fixed income portfolio.
- ◆ Performance is shown net of fees paid by the clients. Reinvestment of income and dividends is assumed. Past performance is no guarantee of future results, and investing in securities may result in a loss of principal.

Don't buy bonds - yet



Ted Levin
Partner

Election Day 2010 was a watershed event, as U.S. voters sent a clear message to Washington. It was also the beginning of the recent rise in the interest rate on the closely watched ten year U.S. Treasury bond.

From 2.59% on Tuesday, Nov. 2 the rate escalated to 3.30% by year-end. Pessimists declared victory, arguing that buyers of U.S. debt demanded higher interest rates to lend money to a government facing trillion-dollar deficits and politicians unwilling to offend their constituents by advocating for cuts in entitlement programs.

The glass half full crowd rationalized the run-up as a sign that the U.S. economy was gaining sustainable traction. As a result, investor expectations regarding interest rates are that they will be going up, as the Federal Reserve releases the patient from intensive care and things get back to normal.

As interest rates rise, investors who already own bonds will notice that the value (price) of those bonds has declined. This inverse relationship between interest rates and price is perhaps less of a concern for those investors who plan to hold

the bonds to maturity. For other bond owners it is a concern just as significant as watching a stock's price go down.

For those investors who have been patient and prudent by avoiding bonds, the recent decline in price is still not enough to entice us to recommend them.

We arrive at this conclusion by applying the same approach as we do in evaluating stocks. We start by trying to determine the underlying or "real" (in our opinion) value for bonds and then comparing that price to the market price.

To determine our best estimate of the value of the ten year U.S. Treasury we look at several forward-looking factors, including inflation expectations, economic growth and the U.S. government's ability to repay its bills. In each instance we conclude the market is still stuck in crisis mode, although to a lesser extent than in 2008, and therefore believe that interest rates in general will continue to increase.

Inflation Expectations

While the government's reported statistics on inflation remain tame, it's hard to believe that the massive

stimulus spending, quantitative easing, and run-up in commodity prices won't lead to higher inflation. Moreover, at some point investors will realize that real inflation is higher than what the government reports. It's hard to believe that inflation is running less than 3%, as health care, tuition, energy, food and property taxes are increasing at a significantly faster rate.

Economic Growth

With the threat of a double dip recession all but off the table, we expect modest economic growth in 2011. Sustainable economic growth, however modest, will cause an upward bias in interest rates.

Budget Deficits

The flight to safety (U.S. treasuries) during the financial crisis, combined with the Fed's resultant monetary policy decisions, drove interest rates down to extreme levels.

The government's emergency fiscal measures created a trillion dollar plus deficit. At the state and local levels, deficits are also major issues, as declining tax revenues cannot offset the growth in generous benefits afforded government employees. At some point the (cont'd page 4)

Market Commentary

Recently I had a lengthy discussion with a client regarding whether he would feel worse if he did not perform as well as the market in a bull market versus not protecting his portfolio in a bear market. In other words, is he willing to take major losses from time to time in order to fully participate in a strong market, or is he more concerned with playing a bit of defense in order to protect himself in a down market.

There is no “correct” answer to this question, but each investor should have a clear understanding as to how they answer the question and ensure that their overall investment portfolio is congruent with their answer. Some additional comments follow:

The arithmetic

We fully agree with one of the core rules of successful investing...”Avoid losses, the gains will take care of themselves.” The deeper the hole, the harder it is to climb out.

The GKL historical performance shown on page 1 was driven by significant outperformance in the two bear markets of the past decade, 2000-2002 and 2008, not by outperformance in bull markets.

Current environment

The optimist in us is comforted that there appears to be an emerging consensus among Wall Street strategists that 2011 should be a good year for investors.

The realist in us is terrified of that consensus. At best, consensus estimates are built into current prices and at worst (usually the case) they are flat out wrong.

Yes, the economy appears to be improving, albeit at a glacial pace. Less encouraging are the increasing signs of emerging global inflation, e.g., food, commodity and energy prices. In addition, the negative dynamics of unemployment, housing and government debt remain far from resolved.

Our concern with Federal Reserve monetary policy centers around its attempt to manipulate asset prices (e.g., housing, stocks) in hopes of resolving some of the underlying economic problems, as opposed to letting the various markets reach an equilibrium price. We admit that there are reasonable arguments on both sides. Our bias is toward less manipulated markets, not more.

Financial Theory

We believe in efficient capital markets.....most of the

time. Outlier events (black swans) occur, perhaps a bit more frequently than we would like. When an outlier event faces a consensus opinion that is in conflict with the event, guess who wins? The most recent example of this, of course, was the unfolding housing crisis in 2006-2008 that was the epicenter of the 2008-2009 global recession.

Summary

1. Avoid losses.
2. The economy is improving.... slowly.
3. The consensus Wall Street opinion is bullish.
4. The Fed’s attempt to manipulate asset prices is dangerous, in our opinion.
5. Black swans occur.

Conclusion

We respect the improvement in the economy and want to participate.

The underlying arithmetic, our concerns with several aspects of the economic situation & Fed policy, and the inherent danger of consensus thinking all suggest a conservative strategy, not aggressive.

We will continue with this approach in managing client portfolios.



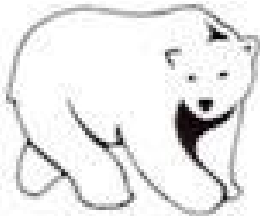
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Don't buy bonds (cont'd)



Polar Investment Counsel Inc.
 Securities and Future's transactions
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buyers of U.S. debt will demand real action to reduce our deficits. If they don't see it soon, they can be expected to demand higher interest rates. Unfortunately, we don't think Washington will act until it's too late.

For those fixed income investors fretting over the low current interest rate environment, we continue to recommend restraint. With relatively safe utility stocks offer-

ing 4%-5% dividend yields, we encourage investors to revisit this sector.

One of the positives that came out of the financial crisis is that it identified those companies strong enough to maintain/raise their dividends those that had to cut.

If a company was able to survive this "tsunami", there is a good chance it can withstand whatever the mar-

ket throws its way. Regulated utilities, blue chip consumer non-durable companies and selected energy companies all have solid balance sheets, reasonably stable cash flows and attractive dividend yields, providing some peace of mind in an otherwise tough fixed income environment.

