



Tarpley & Underwood

Financial Advisors, LLC

October 22, 2009

Mr. and Mrs. John Smith-Sample Client
ABC Company, Inc.
123 Peachtree Street, NE
Atlanta, GA 30303

Dear John and Nancy,

Please find enclosed your reports for the third quarter of 2009.

Quarterly Commentary

Stocks continued to climb in September, bringing the third-quarter gain for the large-cap Vanguard 500 Index Fund (which replicates the S&P 500) to 16%. For the year-to-date, that benchmark is now up 19.3%. In terms of market cap, the small-cap iShares Russell 2000 gained 19.2% in the quarter, and is now up 22.4% for the first nine months of 2009. Mid-caps outperformed both larger- and smaller-caps, gaining almost 21% for the quarter and more than 32% for the year-to-date. Foreign stocks continued to outpace their U.S. counterparts, with Vanguard Total International Stock Index Fund gaining almost 20% in the third quarter and 32.5% for the year to date. Emerging-markets equities (based on Vanguard Emerging Market Stock Index Fund) continued its sharp rally, with a near double-digit gain in September bringing their third-quarter return above 21% and its year-to-date return just north of 62%.

Turning to fixed income, the intermediate-term, investment-grade Vanguard Total Bond Market Index Fund was up 3.7% for the quarter and is now up 5.9% for the year. High-yield bonds, as measured by the Merrill Lynch U.S. High Yield index, nearly matched the gains of domestic equities in the third quarter.

Current Outlook

While we will see more bank failures, as real estate-related loan losses (residential and commercial) continue, we are confident that the government *has taken the financial-system meltdown risk off the table*. The economy is probably already growing again. But the important question of how strong the recovery will be remains. It is also unclear whether it will be sustained or whether there will be another leg down for the economy and the markets (which is commonly described as a W-shaped recession).

With drops in household net worth erasing years of gains; debt levels far too high; access to credit more limited than it has been in years; and labor markets feeble, the consumer is in a weakened state. We continue to believe it is highly probable that households will want and

REGISTERED INVESTMENT ADVISORS

THREE RAVINIA DRIVE • SUITE 1500 • ATLANTA, GA 30346

telephone (770)730.5010 • facsimile (770)730.5050 • WWW.TUFA.COM

need to rebuild their balance sheets, especially the 78 million baby boomers depending on their net worth to help fund retirement. The end of the home equity ATM, and generally less available credit as financial institutions repair their balance sheets, will reinforce this trend. The consumer is 70% of the economy, so clearly consumption growth is of critical importance to economic growth. It is the expectation of slow consumer spending growth coupled with increasing regulation and likely reduced risk taking on the part of businesses and investors (relative to much of the past 20 years) that suggests to us that any near-term burst of economic activity is unlikely to be sustained at a robust level.

Opportunities and Risks

We are always assessing opportunities and risks. Do asset-class fundamentals and valuations justify significant risk taking, risk aversion, or something in between? Our weighing of risk versus opportunity is driven by scenario analysis that combines fundamental and valuation analysis. Valuations have certainly been affected by the recovery in financial markets we have witnessed and participated in this year. Stocks are no longer undervalued unless one believes that earnings growth will be very strong over the next few years. We believe that is unlikely. Both fundamentals (such as the weakened consumer) and valuations are pushing us toward a more tempered view.

As we look ahead, we will continue to weigh our “new normal” subpar-growth scenarios more heavily than our optimistic return to “old normal” scenario. This is a critical debate among today’s investors. If we believed the recovery from this recession to be in the range of all the other post-WWII recoveries, then we would expect much more upside from stocks. But if the housing and debt bust triggered a transition to an economic re-set at a lower level, then economic history clearly suggests a period of subpar growth and lower returns.

We know that no one has a crystal ball and there are experienced and very savvy investors on both sides of the argument. We periodically examine the evidence for a more aggressive growth scenario as we attempt to understand what could make us wrong. Nevertheless, our view is that the weight of the evidence continues to be heavily skewed towards subpar economic and earnings growth over our five-year horizon even though, as noted above, there are factors that could fuel a better outcome. As we continue to process all the factors we’ve discussed here (as well as others), it will impact the degree of risk we take and the opportunities we pursue in the portfolios we manage.

Thoughts

As we look ahead, there are a few thoughts we’d like to leave you with.

First, we believe the last year underscores the appeal of tactical asset allocation. As we’ve stated before, great tactical opportunities come along only occasionally, but when they do, they can provide an opportunity for a performance advantage over the long run. During the last 12-18 months, our tactical changes led us to move out of non-investment grade bonds and commodities into higher quality bonds. We also underweighted equities and



overweighted cash. While certainly not a complete defense against the volatility experienced, these tactical moves provided some mitigation against the negative market movement. Additionally, the active tactical tax management trades we initiated, made during the worst of the market slide, will, in many taxable accounts, allow for minimal taxes to be incurred as both strategic and tactical rebalances are made in future periods.

Most recently we have made tactical allocations which have reduced investment grade bond allocations and increased foreign bond and high yield bond allocations. We believe these are appropriate moves in the high budget deficit and weakened dollar environment we find ourselves in.

Second, our approach to tactical allocation requires a multi-year time horizon. We will not always be rewarded quickly so patience is required—a critically important investment trait that is lacking among many investors.

Finally, when making tactical moves, we are by definition investing our portfolios differently than their benchmarks because we believe it makes investment sense to do so. Therefore, this requires a willingness among investors to accept results that are different from the benchmark. Over time, if we can continue to apply our discipline, this different performance will mean periods of outperformance will more than offset periods of underperformance, resulting in overall long-term outperformance. But shorter term, we will enjoy and suffer through both types of periods.

It is important to note that we are currently postured differently from our benchmarks, with emerging-markets bond and equity exposure, high-yield bond exposure, and below-benchmark U.S. equity and Treasury bond exposure. Thus, if the markets continue their momentum it is less likely that we will continue to outperform in the near term. In particular, if stock returns are very strong we will probably underperform. This could be the case for a number of months but we think it is unlikely to be sustainable. On the other hand, we believe our portfolios are likely to outperform in a downturn, though they would still suffer in a significant market decline. Overall, we believe that our positioning makes sense in the environment we consider most likely in the years ahead, and reflects prudence in our weighting of risk versus potential return.

Client View

We would like to highlight the addition of a new valuable client service. You can now have online access to your most important documents and account information with Tarpley & Underwood Financial Advisors. You can log into your secure webpage via our company website, www.tufa.com, to view:

- Your portfolio of assets
- Your important family documents (such as your estate planning documents, insurance, and other legal documents)
- Your Quarterly Performance Reports
- Customized reports and financial data



Many of our clients have expressed an interest in storing their most important financial documents on this webpage. Your private webpage is designed with your needs in mind: security, anytime access, and easy-to-navigate functionality.

We have introduced this new capability to a number of our clients and have received great feedback. If you are interested in obtaining online access to your accounts with us, please contact Jorja Davenport at jdavenport@t-u.com or at (770) 730-5012 to obtain your login username and password.

We are excited to offer this great new service to our clients in an effort to provide greater convenience, security, and accessibility to help simplify your financial life. We welcome you to explore more about Tarpley & Underwood Financial Advisors, LLC at www.tufa.com today.

We would also like to remind you of our client communications resource hub at www.tufaviews.com. This site is another valuable resource for providing you with timely information on financial topics of interest. Please check it out.

While we as a country, a global economy, and as investors continue to work our way out of the current recession, we appreciate the opportunity to continue working with you to achieve your financial goals. Please continue to let us know how we can assist with this objective.

Best Regards,

Tarpley & Underwood Financial Advisors, LLC

Certain material in this work is proprietary to and copyrighted by Litman/Gregory Analytics and is used by Tarpley & Underwood Financial Advisors, LLC with permission. Reproduction or distribution of this material is prohibited and all rights are reserved.

