Emily Drake: Hello everyone, this is Emily Drake, Partner & Senior Advisor at Fairport Asset Management. I want to welcome you, our clients and friends, to Fairport in Fifteen and wish you a very happy New Year! We hope your holidays were wonderful and that 2011 is already off to a great start.

We cannot begin this New Year without extending our sincere thanks for your business and your trust in our firm. Lasting relationship with valued clients like you have allowed Fairport to become a leading wealth management provider, not only in Northeast Ohio, but also nationally. We are proud to have been recognized recently by *Investment News* as one of the Top 30 Financial Planners in the country.*

We are also enthusiastic about our firm's upcoming tenth anniversary celebration. We hope you'll join us for this happy occasion as we reflect on our roots, dating back to 1963, and celebrate a decade of success under the Fairport Asset Management banner. We'll keep you posted on the activities and events as plans unfold.

So without further ado, let's kick off the New Year with Fairport in Fifteen. We hope this webinar clearly illustrates our outlook for the economy and the markets and more importantly, the steps we are taking to best position your portfolios. As always, the goal of this quarterly update is to identify a few of the specific trends that will most affect our clients and their investments and address changes and tactics that we are implementing to help manage risk and return. We appreciate your feedback and hope that you will keep letting us know how we can strengthen our communication.

Joining me today is John Silvis, Director of Investments, who manages the research of the investment team and oversees the implementation of the firm's Global and Large Cap model portfolios as well as Rick D'Amico, Manager of Investments, who oversees the implementation of the firm's fixed income models and is responsible for the review and oversight of Fairport's alternative investments and strategies. John and Rick conduct in-house research and monitor and analyze a tremendous amount of economic and investment data, so we're glad to have them here today to share their insight.

John, let's start with a brief overview of what happened in 2010.

John Silvis: After starting out the year in positive territory, the equity markets stalled at the end of April and proceeded to fall over 15% over the next two months as uncertainty over the strength of the economy, the direction of Fed policy and the outcome of the then upcoming elections were called into question. Eventually cooler heads prevailed and clarity over the pressing issues became apparent, leading the equity markets to rally in the second half of 2010 to finish the year with the wind to their backs. During the recently completed fourth quarter, the S&P 500 Index notched a total return of 10.8%, outpacing the international benchmark MSCI EAFE Index which captured a return of 6.7%. As you can see on the current chart, the S&P (represented by the green box) returned 15.1% for the year, while the MSCI EAFE Index (the brown box) lagged behind at 8.2%.

It is our belief that the equity markets still have the wind at their backs and the environment for stocks continues to improve as we look out towards the first half of 2011. Now should be the time to emancipate ourselves from the credit crisis of 2008 and take our focus off the rearview mirror and instead look to road ahead.

Emily Drake: Recent reports on the economy have been improving. What are your thoughts?

John Silvis: The domestic economy seems to be reaccelerating after hitting a “soft patch” in the middle of last year. Productivity continues to improve and the index of leading economic indicators continues to point to further economic expansion down the road. The Federal Reserve remains firmly accommodative after embarking on another wave of quantitative easing (outlining a commitment to buy $600 billion of intermediate government obligations through June) which will take us into the midpoint of this year. Weekly unemployment claims have broken to the downside as less new applicants apply for government aid. We believe that real job growth, as illustrated on the current chart, should start to materialize as we head into the year building off the 103,000 jobs created in the month of December. This has led many economists on Wall Street, including Goldman Sachs and JP Morgan, to raise their Gross Domestic Product (GDP) growth forecasts to a range of 3-3.5% from lower estimates of 2-2.5% to reflect the improving data.

Emily Drake: What are the big picture trends, or themes, for 2011?

John Silvis: As we ring the bell to welcome in the New Year, we believe that many of the themes that emerged during 2010 should spill over into the first half of 2011 as well. We continue to believe that the equity markets are poised for further gains over the coming months. It may be premature to call it a change in trend, but after almost two years money has stopped flowing into bonds and bond mutual funds, as measured by the ICI, and has started to work itself back towards stock funds. You can see this change illustrated on the current slide. The high level of ill will gauged by the retail investor may finally be waning and a new source of capital may just be starting to find its way back to the stock market. Equity markets have been highly correlated to the direction of earnings and estimates for the S&P 500 Index continue to rise with consensus at $93 for 2011. Valuations remain attractive and multiples should have room to expand as companies increase productivity and continue to manage costs effectively.

As seen in the current chart, equities should continue to outperform bonds on a relative basis as the Fed remains accommodative, heeding to the old adage of "Don't fight the Fed," leading us to be tactically overweight equities in 2011. Small and Mid Caps are poised to repeat their dominance on the capital curve as an improving economy and better credit climate reward investors willing to take on more risk, or beta, in their portfolios. We expect companies to continue to increase dividends, stock buybacks and mergers and acquisitions (M&A) activity throughout 2011 to leverage better growth going forward.

Emily Drake: In light of your comments on equities, what are your thoughts about bonds and the direction of rates in the coming months?

John Silvis: In all likelihood, the thirty year bull market in bonds is coming to an end, as illustrated on the current slide. The backup in rates over the last few months has been the result of an economy shifting from fears of a double dip to the realization of a more robust trend. Rates on the 10 Year Treasury should settle into a slightly higher range over the next few months with resistance at around 4%, helped by the Federal Reserve looking to keep a lid on the high end of the yield curve.

Emily Drake: John with all of this data supporting an improving backdrop, is there risk of the economy "overheating" or moving too fast?

John Silvis: If there is a risk as it relates to the economy, it could be to the upside. Although we acknowledge there have been false starts over the last couple years, job creation may finally be taking hold as the economy has started to re-accelerate at the end of 2010. Small business hiring has surged in the past few months and large corporations may finally be at the point where future sales are at risk. As the economy grinds higher, further GDP growth revisions to the upside should be expected as we move into 2011. As seen in the current chart, Global GDP should accelerate at an even stronger rate than the domestic economy as China becomes the new global engine for growth. The Emerging Markets now represent over 50% of global GDP growth creating a new leadership paradigm. Europe could be the exception as they struggle with the fiscal decay of several of their secondary members.

Emily Drake: What are your thoughts about other global model asset classes such as Commodities?

John Silvis: Commodities should continue to climb higher over the coming months as the capital markets worldwide recalibrate for higher growth and increased demand. Technical trends for gold, oil and copper all point to higher prices while agriculture commodities continue their steady climb as well. If inflation is to be a threat at all during the year, it's likely to start in the Emerging Markets where consumers struggle with the scarcity and rising costs of food while producers are dealing with the climbing costs of raw materials. Driven by strong growth and increasing demand, Emerging Markets should again lead the equity markets and outperform the Developed world, building on their return of 16.4% from last year. Overall, we would favor the producers of raw materials over the consumers leading us to favor markets like Canada and Australia in the Developed world and Brazil as it relates to the Emerging Markets.

Emily Drake: What sectors will benefit from the current expanding economy?

John Silvis: As the economy reaffirms the current expansion, we expect leadership from the cyclical sectors to reemerge during the first half of 2011. Materials, Industrials, and Energy are tied closest to an expanding economy and should build off current momentum. Technology should also show promise during the New Year as balance sheets are strong and revenues are projected to increase with corporations enacting long overdue product replacements. Defensive sectors like Utilities and Telecom should post gains but underperform the overall market as investors look to capture more systemic risk in the form of beta. Dividends will again play an important role as payout ratios are under historic averages and should increase as companies look to reward patient investors.

Emily Drake: John, before we turn to Rick to discuss fixed income, what's the final word on equities?

John Silvis: As we look towards the coming year with renewed optimism, some risks still remain and could derail what should be a good year in equities. The debt crisis in Europe, while contained to a few peripheral members, could spread to others within the union causing the dollar to strengthen. This could cause a disruption to earnings of many multinational corporations that benefit from sales overseas. China could overreach in their attempt to orchestrate a soft landing for their overheating economy causing the global expansion to lose steam or to be derailed. Commodities, which we believe will move higher throughout the year, could see a surge in prices causing supply shortages and price spikes. Finally, housing remains the biggest wildcard as prices remain soft, falling 1% over the last 12 months. Any increase in the rate of decline could give investors further pause in the coming months lowering confidence.

With tax cuts remaining in place, an additional $120 billion in stimulus in the form of lower payroll tax and loose monetary policy, the macro environment has been set for investors to take on more risk within their portfolios. Seasonally, being the third and strongest year in the four year presidential cycle, the wind is at our back. Fundamentals remain strong and technicals remain positive, shaping 2011 to be a positive year in the equity markets.

Emily Drake: Rick, what are your thoughts about inflation in 2011?

Rick D'Amico: We don't see inflation, as it relates to the published Consumer Price Index (CPI), as much of a threat for 2011 for several reasons. Historically, inflation takes hold after we have had several quarters of GDP growth above the historical trend (which is around 2.8% annually). We have not seen that yet as the third quarter GDP growth for 2010 was recently revised to 2.6% meaning there is still "slack" in the system. Ned Davis Research, one of our primary research resources, calculates that the economy is 6.1% below potential GDP. The Federal Reserve is still accommodative as it relates to monetary policy with their focus on deflation and job creation. And the breakeven inflation rate, the inferred inflation rate on the 5 year TIPS, is only 1.8% – well below the long term average inflation rates of 2.5-3.0%.

Emily Drake: Discuss some of the reasons behind the recent sell-off in the municipal bond market.

Rick D'Amico: In our opinion, the -4.2% return in the fourth quarter for the municipal sector, noted on the current slide, can be attributed to higher treasury yields, supply/demand imbalances and psychological factors, rather than changing credit trends. The market was flooded with a very heavy supply of new bonds, totaling more post-labor day supply and more fourth quarter supply than in any other year in U.S. history. The sharp increase in supply can be partly attributed to the expiration of the Build America Bond program, as issuers rushed to the market before year-end, hoping to lower borrowing costs by capturing the 35% federal interest subsidy received over the life of these bonds. As shown on the current slide, there was also a sharp decline in bond fund flows, with outflows averaging $2.5 billion a week – the most rapid pace of outflows since Lipper started keeping track in the early 1990s. As the equity markets improved, the momentum of leaving fixed income behind for equities continued to build. Additionally, we saw substantial pressure on longer term Treasury rates as the 10 Year Treasury yield climbed over 120 bps from a low of 2.3% on October 8th to a high of 3.6% on December 15th. And finally, negative headlines continued as evidenced by a *60 Minutes* segment on December 19th, which suggested massive local government defaults in the very near term.

It is clear that municipalities are facing a genuine budget crisis and pension obligations will continue to be a real consideration going forward. Budget gaps for states going into Fiscal Year 2011 are substantial, and for some, unprecedented, due to revenue shortfalls in sales, income and property taxes. State and local finances historically lag the national recovery, taking 18 to 24 months to recover after a national economic rebound has been confirmed, meaning municipalities could continue to face headwinds well into 2012.

That being said, in our opinion, widespread municipal defaults are not imminent and highly unlikely in the case of state General Obligation (GO) credits.

Emily Drake: What are some of the characteristics inherent in municipal bonds which have made them historically less likely to default when compared to corporate and sovereign credits?

Rick D'Amico:

1) Debt-servicing costs represent an exceptionally small part of state budgets. Debt service costs as a percent of annual spending range between 4% and 8%.
2) Debt repayment is also a high priority for state and local issuers. Principal and interest payments for General Obligation debt are senior to almost every other type of expenditure. For instance, according to the state constitution, the only obligation senior to debt service in California is education.
3) At the state level, the amount of primary government debt outstanding is considered small when compared to European sovereigns. Total primary government debt outstanding as a percentage of GDP for Local GOs and State GOs is 9.1%, and 3.8%, respectively. In comparison, Italy and Greece easily exceed 100% by the same measure.
4) Unlike a sovereign, states do not roll over their debt. Debt is retired (and amortized) using organic revenues, not new borrowing.
5) Flexibility to meet obligations through state taxing authority, expense reductions, alternate sources of funding (such as asset sales and revenue stream securitizations), as well as rainy day reserve funds.

Emily Drake: What specific steps have we taken in Fairport portfolios to manage some of the risks you've identified?

Rick D'Amico: Our focus will continue to be on high quality general obligation bonds, as well as essential purpose revenue bonds such as water, sewer and electric. Essential purpose revenue issuers tend to be monopolistic in nature and typically generate stable revenue streams, as even troubled households will strive to stay current on their water, sewer and electric bills.

We are targeting a weighted average portfolio duration in the intermediate range, between 5 and 6 years. The municipal yield curve depicted on the current chart continues to remain very steep, and significant yield pick-up can be achieved by targeting issues in the 7 to 10 year part of the curve.

Emily Drake: Rick and John, thanks for that overview. As always, we have been working diligently on behalf of our clients. We appreciate the Investment Team's efforts to help minimize volatility and protect downside risk while striving to benefit from continued strong fundamentals and positive technicals. Clients and friends, thank you for your time and interest. We appreciate being your partner who can give objective and unbiased financial advice.

Finally, we're delighted to announce a special client event with Liz Ann Sonders, Charles Schwab's Chief Investment Strategist on Wednesday, April 6th. Liz Ann is a nationally respected and dynamic speaker and we're so happy to be able to bring her to Cleveland for this evening event. Mark your calendar and watch the mail for your "save the date" postcard with more information.

Please feel free to give us feedback on our webinar and importantly, let us know if we did not answer any specific concerns or questions. If you have a friend or family member who needs a trusted financial advisor, please call a member of the Fairport team.

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**Investment News published in its December 2010 issue a listing of the Top 30 Financial Planners conducted by RIA Database, a Charlotte NC based company that focuses on providing accurate, relevant data for sales professionals on registered investment advisors. The national ranking is based on discretionary assets under management as of September 30, 2010. RIA Database qualified and ranked investment advisers based on the following criteria: 1) They must have a significant number of financial planning clients 2) Greater than 50% of their business must serve the individual investor marketplace 3) They must not be doing business as a broker-dealer or a bank 4) A dominant portion of their business must not be invested in proprietary products or managing proprietary products.*