



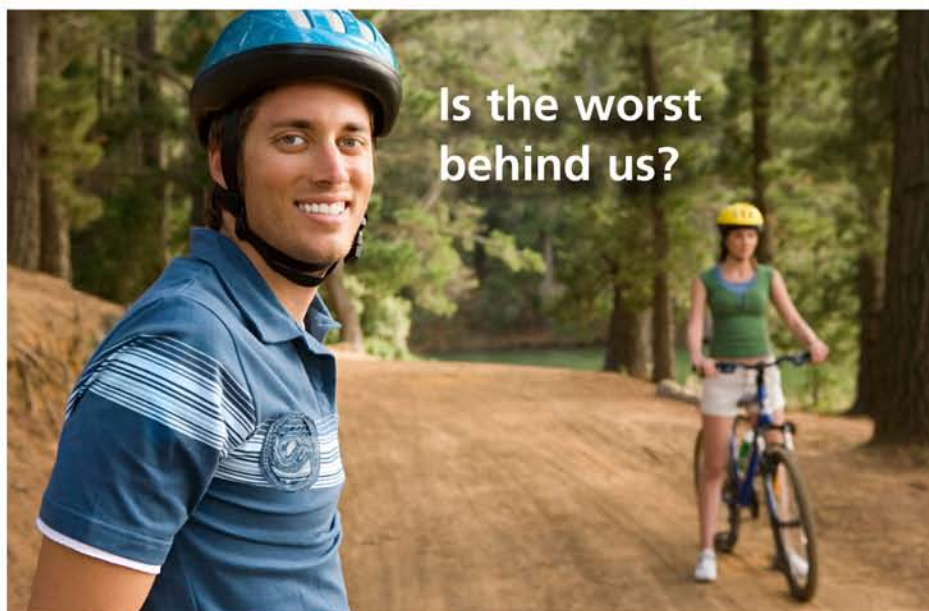
Sarah Wells

Start the new year right

This has been a disquieting time for investors. The economy seems to be coming around, but the recovery may have some unusual features. This issue of *QuarterNotes* reviews this terrain through a conversation with a Senior Investment Analyst from ING Advisors Network.

On page three you'll find "IRA Assessment." This is the time of year for review of this retirement planning resource, as well as for making contributions.

How has your portfolio weathered the financial storms? Please bring your investment questions to us—put our expertise to work for you.



One year ago investors faced great uncertainty, with financial market strains not seen in this country in generations. Given that bleakness, we are in better shape today than many people expected. Still, the economic news remains troubling, especially on the employment front.

For investors the news is not all bad. The recession apparently ended during the third quarter. Some stock prices recovered smartly after setting their lows in the first quarter of 2009. At this writing, stock indices look to finish in the black for the year, if still well below their historic highs.

What should investors be looking for in 2010, from the economy and the financial markets? *QuarterNotes* turned to Senior Investment Analyst Cameron Lavey of ING Advisors Network with questions about the future.

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Is the recession really over? If it is, is there a chance of a double-dip recession?

In our view the recession has ended, though it may not feel that way to some people. In terms of positive GDP growth and other traditional economic metrics, we believe the bottom has been reached. But more people care about the unemployment numbers than whether the end of the recession has been “officially” identified.

We expect unemployment to continue to grow during 2010. Unlike past recessions, we’re not expecting unemployment to decline quickly; it may still be at 8% in 2011. It will be at least until 2012 before we get back to normal employment numbers.

We don’t see the economy slipping back into recession, though growth will not be robust. With the amount of stimulus that the government has put into place, and with interest rates as low as they are, I don’t think we’ll see another recession.

You mentioned today’s low interest rate. Do you think that the Fed might raise rates in 2010?

The Fed has indicated that they plan to leave interest rates low for the near term, and I wouldn’t be surprised if the Fed leaves rates alone throughout 2010. They are focused on three things. Capacity utilization is only about 70%, and manufacturing utilization is just 67%, which are each ten percentage points below the averages for the past 30 years. There’s still a lot of slack in those numbers.

The CPI and inflation expectations are the other two key factors. We saw the latest CPI numbers were actually slightly negative, and inflation expectations remain low as well. With those three elements low, I don’t anticipate the Fed raising rates anytime soon.

You don’t expect inflation to make a comeback in 2010? Isn’t the current price of gold an inflation signal? Beh

A lingering cloud over housing



Do you think that the housing crisis is over? I would say no. Housing has been propped up by a lot of government policies, but we still have a lot of option ARMs to reset. The mortgage modification programs help initially, but the number of people who redefault keeps rising and rising. I think the housing market has a ways to go before we settle back to normal levels of supply and demand.

Is there a risk of a new wave of defaults? The government is working to keep people in their homes, and that’s important. But at the same time, those policies can artificially prop up the housing market; we don’t get to the real bottom. They may be good in the short term, but the long term can have adverse impacts.

No, we don’t see signs of near-term inflation, given the real lack of resource utilization, as well as the lack of employment growth limiting growth in consumer demand. Beyond 2010, yes, there is a potential for inflation if the Fed doesn’t handle things correctly.

The price of gold does suggest that someone is trying to hedge against inflation, but the more important element behind that price move is the decline in the value of the dollar. Gold is a momentum trade right now. It is a commodity that is in short sup-

ply, and there are not that many alternatives that have been doing well.

What sectors should investors give close attention to in 2010?

Given the severity of the recession, the speed of the recovery in 2009 probably caught a lot of people off guard, so unfortunately all the easy money has already been made. 2010 will be a much more challenging year to find decent returns.

We’ve been telling clients to look for value in emerging markets that are growing well, such as China, India and Brazil. We favor both equities and bonds in those areas. We are also favoring the “go anywhere” managers who are able to rotate in and out of different types of assets in different countries, who are not benchmark specific. These managers can go large cap, or small cap, or international, or stay within the U.S. whenever they see attractive opportunities. They have similar flexibility in the bond markets. Without constraints such managers can act more quickly in today’s fast-moving markets.

But how does that mesh with asset allocation planning? Should the investor just give up on that?

That is a challenge. Investors may lose some strict adherence to an asset allocation plan, but our experience over the last year is that these managers have outperformed. In a low-growth, low-yield environment, it is better to put the professionals in charge of portfolio management, and let them handle the asset allocation.

What role should dividend-paying stocks play in portfolio planning for 2010?

Strong dividend payers can be a good way to get more yield from a portfolio. I am a bit concerned about valuations of the dividend-paying stocks right now, because the stock market has risen so fast. Yields are down to 2% to 3% for many stocks. One segment we

find attractive is utilities, not a sexy sector but one with higher yields than others.

With equities, you are taking on more risk, but equity-income products can be a good way to play the slow-growth environment.

What about retirement portfolios, given these low interest rates and dividend yields?

The only way to increase yield and income is to take on more risk. For example, one can move to corporate

bonds, where yields may be closer to 5% to 6%.

Retirees may have to spend less, or think about dipping into principal.

What is the main take-away for the coming year?

Our main messages are to become accustomed to slower growth, and to prepare for higher taxes in the near term. Even though higher taxes may retard economic growth, all this government spending has to be paid for at some point. We may have to sacrifice future growth for stabilization today.

The “rich” don’t have enough money to pay for all the spending we’ve seen.

That may mean, for example, more muni bonds for some investors, and paying attention to tax efficiency for others.

The views are those of Cameron Lavey, Senior Investment Analyst, ING Advisors Network, and should not be considered as investment advice. All information is believed to be from reliable sources. However, we make no representation as to its completeness or accuracy.



The earlier that you make your IRA contributions, the longer they will grow. So, under that theory, you should have made your IRA contributions for tax year 2009 12 months ago! But if you didn’t, it’s still not too late.

This also may be a good time for an assessment of all the IRAs that you’ve established over the years. IRAs are easy to take for granted, but they should not be placed into the “invest and forget” basket.

Tax diversification

The tax deduction for the traditional IRA contribution is welcome; it makes funding the IRA easier, especially when times are tight. But eventually the music has to be faced, and taxes must be paid.

The alternative is to have some money in Roth IRAs, where the income tax has been prepaid. Roth IRAs are exempt from required minimum distributions during the owner’s life, and earnings are potentially tax free.

For a comprehensive review of your personal situation, always consult with your tax advisors. Neither PrimeVest nor any of its representatives may give tax advice.

Beginning this year, everyone with a traditional IRA has the option of converting it to a Roth IRA—the old income limits on conversions have been eliminated. If you do convert this year, you have the option of reporting the income in the 2010 tax year, or splitting it over 2011 and 2012. Taxpayers generally prefer to defer payment as long as possible, though if you know that you will be in a higher tax bracket later, such an approach may not be right for you.

Multiple minor accounts

Have you set up several IRAs over the years at different financial institutions? Are you swamped by statements for the many accounts?

Consolidation of your IRAs in a single account will simplify your financial life. You’ll have just one statement to contend with, and one account to review for investment decisions. Maintenance fees may be reduced as well.

The consolidation process need not be complicated. We’ll be happy to help if you wish to take this step.

Investment incoherence

Your IRA investments should be reviewed in the context of all your investments, including 401(k) accounts and taxable savings. You want to have one asset allocation plan for all of your holdings, not a separate plan for every account. Having multiple accounts does not provide you with investment diversification if all the accounts are invested in the same way.

If you are unsure of the best investments for your IRA, seek professional guidance. Doing nothing, taking the IRA investments for granted, is not a good solution.

JUST ASK US

I understand that the first-time homebuyer credit has been extended into next year? And more people can qualify now?

Yes, a credit for 10% of the purchase price, up to \$8,000, is permitted for a first-time homebuyer. For “long-time residents” a \$6,500 credit is now allowed as well, which could draw more buyers into the pool.

What’s more, the income limits have been raised. Singles with modified adjusted gross income of \$125,000 or less, or married couples with \$225,000 or less, qualify for the full credit.

When does the credit expire now?

In general, there must be a binding sales contract by April 30, 2010, and the sale must close by June 30, 2010. However, members of the military and certain federal employees stationed outside the U.S. get a full one-year extension on those dates.

Any new restrictions?

Yes, Congress added three stipulations to curb perceived “abuses” of this tax credit.

- Homes valued at more than \$800,000 do not qualify.
- The purchaser must be at least 18 years old.
- Dependents may not claim the credit.

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