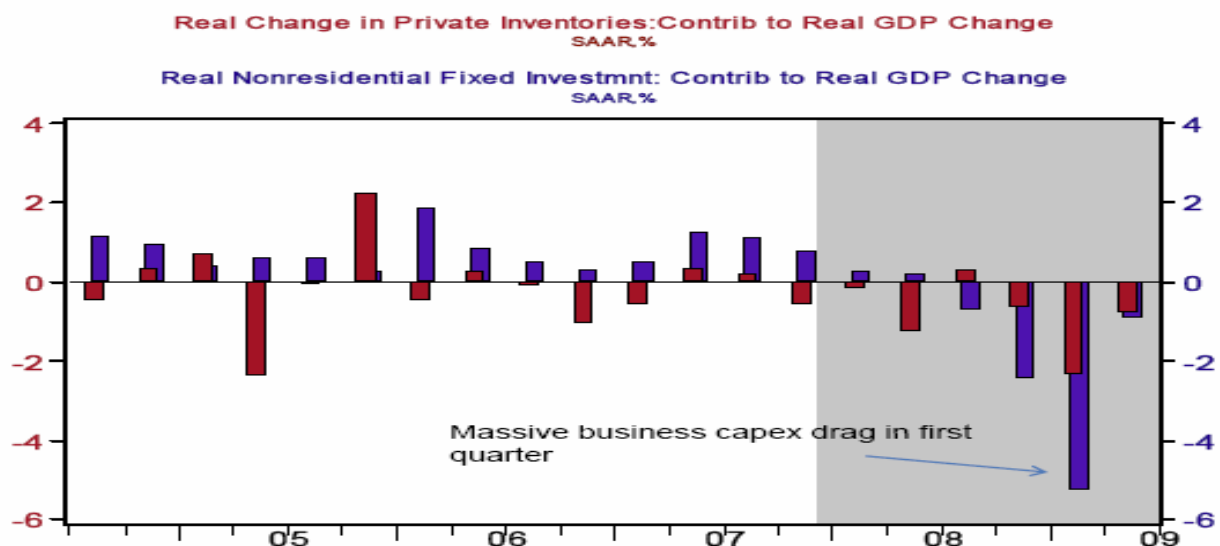


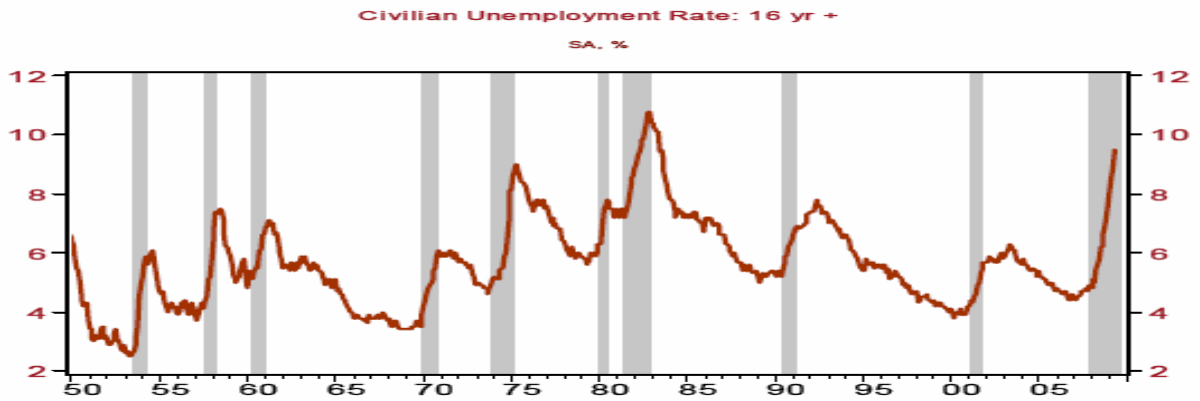
3rd Quarter 2009 Market Commentary and Outlook

The “**Great Recession**” as it is now being described, has been the longest and deepest economic slowdown in the post -WWII period. Real Gross Domestic Product (GDP) has fallen 3.7% from the peak versus an average decline of 1.7% in past recessions. Assuming a June trough, the recession will have lasted 18 months, versus an average of 10 months in the past. From the peak of Q4 2007, the declines in consumer spending, business spending, residential investment, and exports have been larger than in any other recession post -WWII. While the recession technically began in December 2007, the chaotic phase did not begin until September 2008 (one year ago) with the failure of Lehman Brothers. It did appear at that point, that the global financial system stood on the abyss and was only weeks away from a complete meltdown that could have plunged the global economy into a 1930’s style depression. Unlike the March 2008 forced takeover of Bear Stearns by JPMorgan, the decision to allow Lehman to fail proved to be the turning point. Lehman’s failure led directly to the need to immediately rescue AIG (\$85B) due to its exposure to the Collateralized Debt Securities (CDS) market, then came the (\$700B) TARP rescue package, FDIC debt guarantees, massive quantitative easing (printing money) and near zero percent interest rates. What began as a U.S.housing and consumer spending recession quickly morphed into a synchronized global downturn. Unemployment has quickly jumped to a 26 year high. This high unemployment, combined with the potential for “stagflation” (higher prices combined with limited growth last seen in the 1970’s), dramatically limits the longer term strength of this recovery.

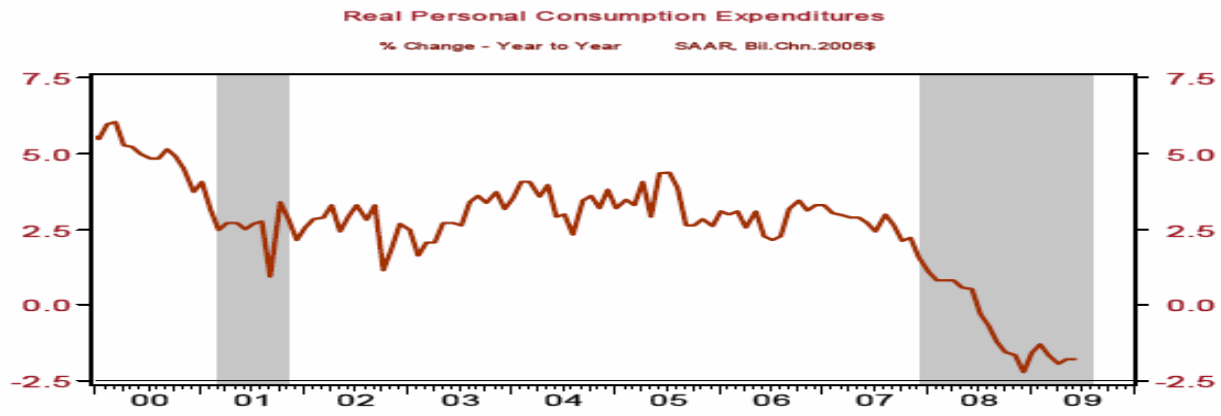
Business Dramatically Cut Inventory and Investment



Business Also Slashed Their Largest Variable Cost – People



The Pain Translated Quickly to a Highly Leveraged Consumer Who Stopped Spending



“HAPPY DAYS ARE HERE AGAIN”

Despite the harsh reality of the economic fundamentals referenced above, the market has rallied dramatically (58%) off its March lows. This was also true back in the Fall of 1929 when the song “Happy Days are Here Again” topped the play list. In the face of this rally, Beaumont Financial Partners has maintained a conservative asset allocation. We fear there may be near term volatility due to some real long-term concerns. First, however, we will review recent catalysts and highlight what we believe are the temporary nature of some of these market drivers.

According to Ned Davis Research (NDR), rarely has a market seen a six month rally like the one that just occurred. This rally is one of just six of this magnitude in the last 100 years. All previous rallies of this magnitude took place in the 1930’s and one occurred in the 1970’s. Those also were periods of great economic and market turbulence. Unfortunately, none of these gains were sustained and, in the case of the 48% rally of 1929 -1930, it turned out to be a trap for many as it was followed by an 86% plunge. According to Tim Hayes of NDR, one problem with these rallies is that they tend to lack follow through. In addition, more than half of the gain tends to come in the first six months. As a result, if you do not time your buys perfectly, you can miss most of the gain and potentially risk buying as the market subsequently rolls over.

Current Rally is Unlikely to be a Repeat of August 1982

Only one short term rally (which began in August of 1982 when the Dow rose 40% in a six month period) sparked a new “bull market”. That rally marked the end to a 16 year period of market disappointment and started a new 18 year bull cycle that ran until 2000. One reason to be skeptical that the current market rally could be analogous is that the following 18 year “bull run” was credited to the actions of then-Federal Reserve Chairman Paul Volcker. Volcker’s Fed was truly independent and had the will to squeeze inflation out of the economy by gradually raising interest rates to 20% in 1981. Unfortunately current U.S. fiscal and monetary policy is hurtling in the wrong direction towards a potential currency crisis. With the financial crisis still looming in the rear view mirror, there is no talk of taking the foot off the accelerator. The question then becomes, “will there be the necessary political will to withdraw the stimulus when needed?” One recent indication says the answer to that question is “no”. Paul Volker recently testified before Congress that the Obama Administration’s plan to create a council of regulatory agencies to be headed by the Treasury Department was akin to the Government sanctioning reckless behavior. Volcker noted that such a move might signal that the government is prepared to ensure that no major bank will be allowed to fail. Volcker’s comments were clearly driven by his concern that any council or over-arching regulatory agency would threaten the independence and power of the Federal Reserve to act free from the political arena.

TEMPORARY FORCES DRIVING THE MARKETS

A market consensus has developed that June 2009 was the recession trough. This perspective was recently supported by comments made by Federal Reserve Chairman Ben Bernanke in his September 15th speech at the Brookings Institute, *“from a technical perspective, the recession is very likely over at this point...It’s still going to feel like a very weak economy for some time because many people will still find that their job security and their employment status is not what they wish it was.”* Why is the recession perceived to be ending? According to RDQ Economics, “in part it is burnout of some of the factors forcing the economy down and the math of easy comparisons”. In addition, we see the effects of heavy handed government intervention (e.g. the \$8K first time home buyers credit and the “Cash for Clunkers” programs). These programs have resulted in direct government intervention into both the auto and housing market to pull demand forward and attempt to jump start the economy.

Housing Stabilizing with Subsidized Rates and an \$8K 1st Time Home Buyer Tax Credit

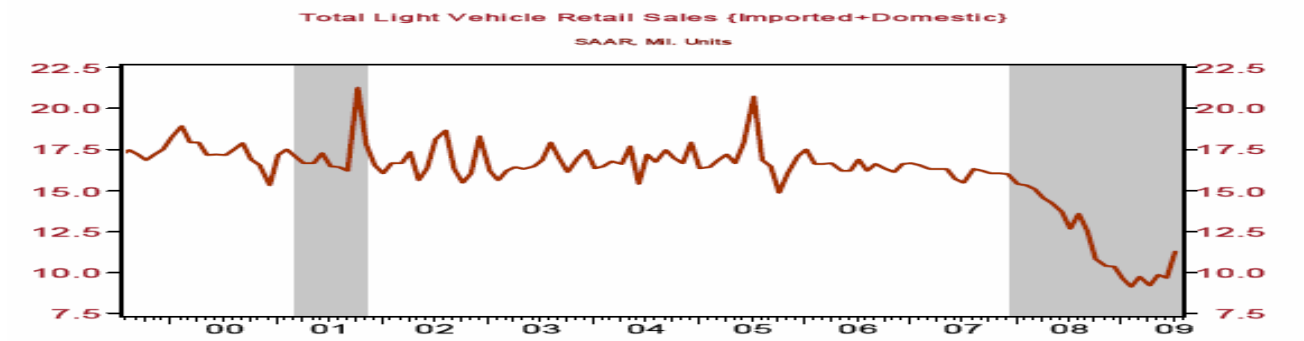
In the case of housing, the Government is now essentially funding 80% of all new mortgages and has made a dramatic pledge to buy a total of \$1.25 trillion in agency mortgage backed securities (MBS) and up to \$200 billion of government agency debt. The Fed recently commented that they will slow their purchases of MBS and stretch the program to the end of the first quarter, rather than end the program at year end as originally planned. Absent the Fed, the national fixed mortgage rate might be closer to 6% according to mortgage data tracker HSH Associates. Mortgage rates above 5% are seen as a major hurdle for household affordability and a roadblock to a recovery in the housing market that is trying to find a bottom (see RDQ chart below). In addition, the low end of the housing market has been supported by an \$8K first-time home buyer tax credit which is set to expire in November. Though the credit has helped stabilize the housing market nationally, it goes only to first-time buyers who make less than \$75,000 for singles and \$150,000 for couples, limiting its impact in high-priced areas. Even with all this support, existing home sales dropped 2.7% in August

to a seasonally adjusted annual rate of 5.10 million homes. This was the first decline in five months, according to the National Association of Realtors and may indicate that the artificial support provided by these policies may not be enough to do anything more than stabilize the housing market at a very depressed level.



“Cash for Clunkers” – Pulling Demand Forward

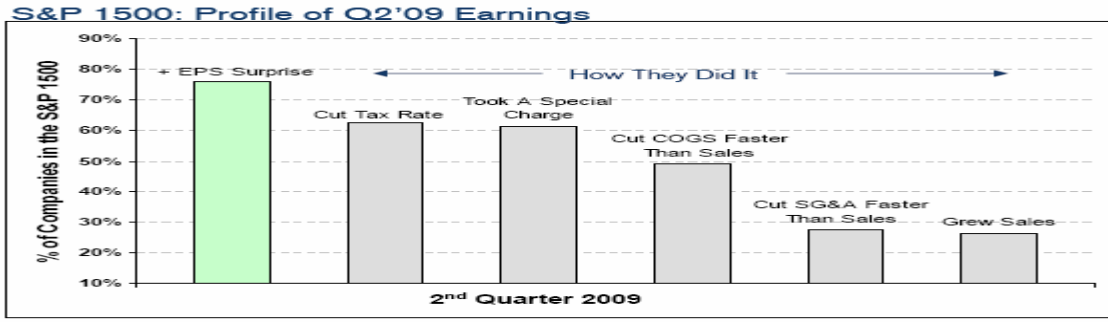
The Cash for Clunkers program, officially known as the Car Allowance Rebate System (CARS) ended Monday, August 24th. The program was signed into law on June 24, 2009 with a goal of encouraging consumers to trade in older, less fuel-efficient vehicles for new vehicles that get better fuel economy by providing a credit of either \$3,500 or \$4,500. It was modeled after several programs that have already been successful in Europe. As a result of this program, retail sales for August were up 2.7%, which was well above the 1.9% expectation. A major driver of this surprise was auto sales, which were up 10.6% in dollar terms with unit sales up 25.4%, an artificial bounce that cannot be sustained. To wit, September auto sales declined 23%.



Q2 Earnings Stronger Than Expected; “Quality and Sustainability” the Question

As identified by Credit Suisse (see chart below), 76% of firms in the S&P 500 reported a positive earnings surprise in the 2nd Quarter of 2009. The composition of “How They Did It” can be seen below. We question the quality and sustainability of these results when only 26% of the companies beat expectations due to positive revenue growth. According to Goldman Sachs, sales among companies within the S&P 500 experienced an accelerating year over year sales decline of 16% in the second quarter, following a 14% decline in the first quarter. In the short term, consensus anticipates that earnings prospects remain favorable. Aggressive expense control and a modest inventory restocking could boost Q3 results leading to further positive surprises. The fourth quarter will have easy comparisons versus an awful Q4 2008 that will give the appearance of healthy profit increases. However, soon the market will turn its attention to 2010 and the ability of stocks to sustain or extend their advances will have to

come from a revival in top line growth. That will be very tough in a challenging economic environment. Over the past six months, investors have been comfortable knowing that at least the decline in profits has ceased. At some point that knowledge may not provide enough incentive to continue to drive this market.

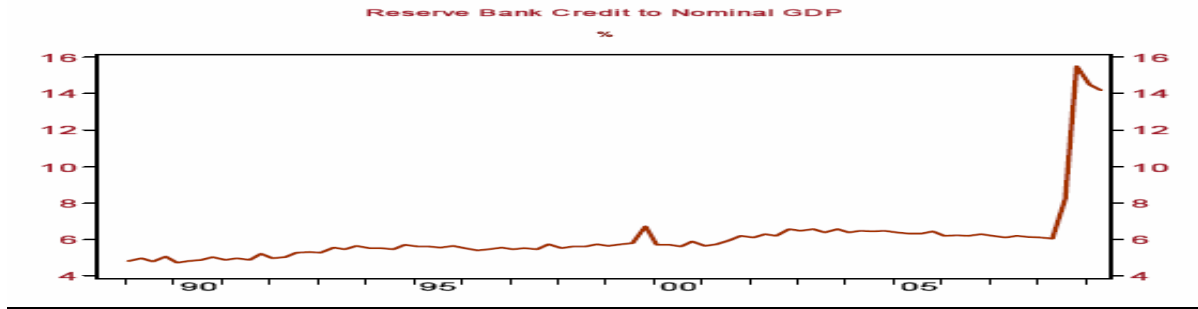


Liquidity Driven Market

As can be seen from the chart below, the Federal Reserve has injected an unprecedented amount of liquidity into the financial system. Thankfully the Federal Reserve and several other Central Banks did execute on their role as “lender of last resort” throughout this financial crisis, averting an even larger financial disaster. Obviously this wall of liquidity has had the intended effect of driving interest rates dramatically lower and insuring that those who needed credit could obtain it.

An unintended consequence of this policy has been to drive bond and other low risk assets yields so low that insurance companies, pension funds, mutual funds, and even individual investors cannot get adequate income in a safe way. As a result, they are forced to stretch for yield and take more risk. While money market assets are still at very high levels, they have come down dramatically as capital has been forced into equity markets or into higher risk investments. With hindsight, we all know that the desire to leverage up and stretch for yield is how we got into trouble in the first place. If the Bernanke Federal Reserve makes the same mistake that the Greenspan Federal Reserve made (leaving rates too low for too long), the financial system will gorge on risky assets again to the point where we are vulnerable to another financial crisis. If this occurs, the Fed’s balance sheet (no longer pristine and underleveraged) will not be able to adequately defend against a crisis. In response, consensus at recent global financial forums (Jackson Hole & G20 Meetings) has encouraged the rapid development of global financial regulation to deal with the excesses in the financial system. With the need to get financial regulation established and in place so urgent, the potential for a policy misstep is made even greater. If Congress does get effective regulation in place, the worry will be that tighter regulation combined with higher interest rates will constrain business activity. The question then becomes, “when these constraints kick in, do they

negatively affect markets?” In short, if the Fed does not take their foot off the accelerator, inflation is likely; if they hit the brakes too hard, the recovery may be derailed!

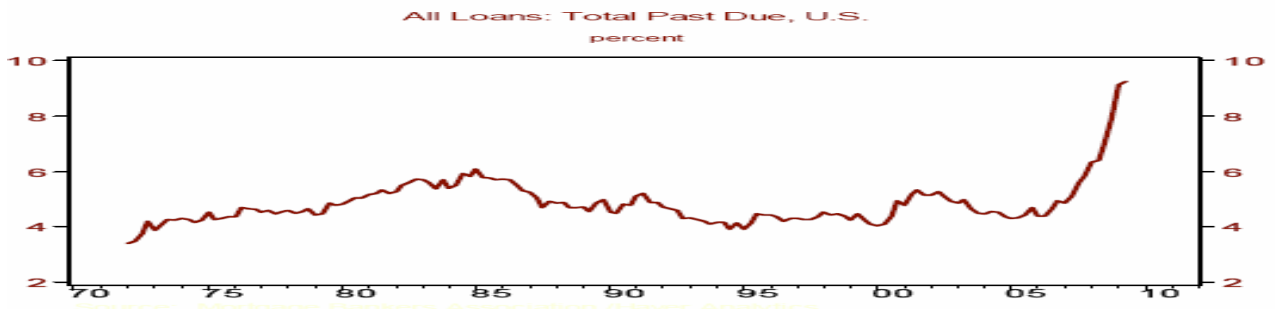


REAL CONCERNS – WHY THE CONSERVATIVE ASSET ALLOCATION

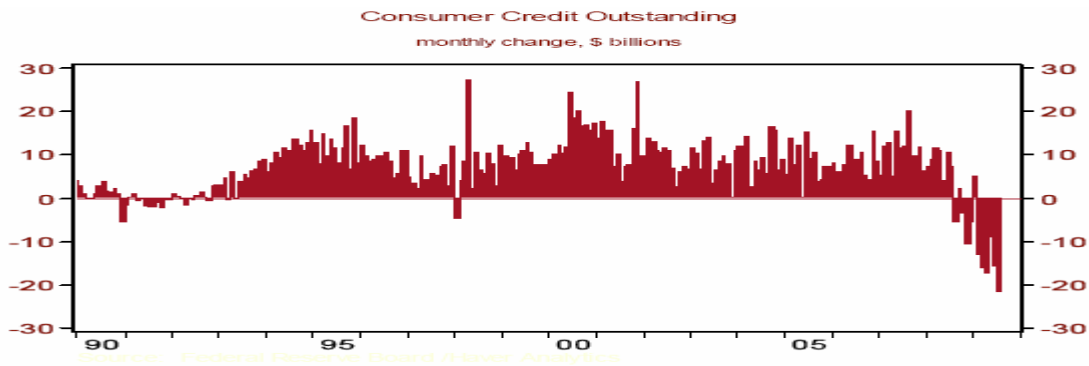
While Beaumont Financial Partners has stayed in equities, we continue to maintain a conservative asset allocation. For many clients, we have tactically shifted up to 15% of (higher risk) equity exposure into (lower risk) cash/short duration fixed income assets. While we can see the potential in the near term for a continuation of this trading rally, based upon the “coiled spring” concept and high cash balances, we have some real concerns in the mid to long term which we will walk you through.

U.S. Consumer (~70% of U.S. GDP) Remains in Serious Trouble

Total past due mortgage loans rose to 9.2% in the second quarter from 9.1% in the first quarter, reaching levels not seen at any point in the past 40 years. (see RDQ chart below). In addition, according to Reuters, consumer bankruptcies soared 41% in September to a year to date total of 1.05 million households. With unemployment staying stubbornly high and continuing to grow, past due numbers will continue to increase. This trend will continue to force the banking industry to raise capital to cover extensive credit losses well into 2010.



In July consumer credit outstanding plunged \$21.5 billion (RDQ chart below), the largest outright monthly decline on record (how much of this is due to defaults and bankruptcies is unknown). Consumer credit has fallen for six straight months as consumers have stopped using their credit cards and banks have pulled outstanding lines to limit their exposure. Despite this decline in consumer credit, recent trends in consumer spending levels appear to have stabilized. Our concern is that as the tail on this recession extends and we experience a jobless recovery, the consumer will continue to slide. In this scenario, the consumer will be unable to assume its traditional role as the engine powering global consumption.



How Quickly Will the Dollar Lose its Status as the Global Reserve Currency?

The dollar has started to slide again relative to other currencies as its status as the global reserve currency has been called into question. The dollar is used by other countries across the world to back up their own respective currencies. According to Eric Sprott of Sprott Asset Management, “in some cases, it is as simple as a country stockpiling US dollars in their central bank vaults. It is quite obvious how tenuous it is to back up one’s currency with a pile of paper issued by another country, but this is exactly how the world of international currency has worked for decades,” states Sprott. The real issue facing the dollar is the legitimacy of the U.S. government. Specifically, is it making promises it won’t be able to keep? Michael Goldstein of Empirical Research Partners points out that this year’s tax revenues are running at 15.5% of GDP, the lowest since 1950, while expenditures are 27.5% of GDP, the highest since World War II. As a result, the country is running a deficit of around \$1.7 trillion or 12% of GDP per Goldstein. He further adds, “to put these numbers into context, to eliminate the deficit, personal income taxes would have to go up 66% to cover the gap”.

Government debt held by the public is currently around 55% of GDP and may be headed much higher depending on the policies pursued by the Fed and Treasury. Because the US government is printing dollars to fund their liabilities (i.e. buying treasury and agency bonds with their own newly created dollars), it is highly unlikely that we will ever see a failed U.S. bond auction similar to that seen recently in Poland. However, we are more likely to see foreign buyers reduce their Treasury and agency bond purchases in the future and shift these monies into assets that no government can print (real assets) as a protest to the aforementioned dilution of the US dollar. The question over the near to long term then becomes “will the exit from the dollar be orderly?” If not orderly, the government will be forced to defend the currency by raising taxes, raising interest rates and/or reducing government expenditures. Any of these actions would be perceived as negative for the U.S. equity markets and possibly result in a dramatic sell-off. Taxes were boosted in 1937 after the Great Depression and again in Japan in 1997, both with disastrous consequences.

The Dollar Has Resumed Its Decline



Watching Gold – How Orderly Will the Exit From the Dollar Be?



SUMMARY

As outlined above, we continue to maintain a conservative asset allocation due to our significant concerns regarding continued weakness for the U.S consumer and the possibility of policy missteps. However, we are not in the dire camp of prognosticators like Gerald Celente of Trend Alert who recently commented ***“we are anything but confident...what is ballyhooed as recovery is nothing more than cover-up; papering over historically unprecedented financial losses with historically unprecedented trillions of dollars spun out of thin air, backed by nothing, and producing practically nothing.”*** Opinions like these may seem extreme, however they are what create the potential for significant volatility. We continue to believe that this is a trading market fed by less bad news, heavy handed government intervention and significant cash balances. We will continue to look for opportunities to participate in equities where values are attractive. Entering the third quarter reporting period, the market faces a critical transition. As is the case in many years, this period is normally the annual transition period for the market psyche to shift from current year to next year. Many market corrections take place approaching the fourth quarter because of this phenomenon. Positive earnings surprises will be helpful, however, investors will need to hear managements transition from Q2 buzz words like “stabilizing” and “cost management” to comments about top line growth and end demand.

In summary, with this view we will continue to be cautious and carefully monitor client equity exposure. While we know that significant challenges lie ahead, we at Beaumont look forward to guiding you through the balance of this year and into 2010. As always, we thank you for your trust and confidence. Please contact your relationship manager if you have any questions or concerns regarding your accounts and risk profile.

If you have any questions or comments, please contact us at 781-237-7170 or e-mail me at mstack@bfparkers.com.

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