CENTURION Asset Management
610 W. Germantown Pike, Suite 150
Plymouth Meeting, PA 19462

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In this month's Market Letter, we will review the May ending market and economic performance, explain why now may be a good time for Emerging Markets investing, and provide some interesting factoids.

Go away May

During the month of May the markets struggled mightily. The Dow Jones 30 declined 9.39%, and the S&P 500 was down 7.99%. The small stock based Russell 2000 index was down 7.59%, while the international markets as measured by the MSCI EAFE declined significantly by 12.06%.

Index Levels	12/31/2009	4/30/2010	5/31/2010
Dow Jones 30	10,428	11,008	10,137
S&P 500	1,115	1,186	1,089
Russell 2000	625	716	662
MSCI EAFE	1,580	1,551	1,363

Alternatively, we experienced fairly good economic data about jobs, durable goods orders, and home sales. Each was an improvement and led to positive consumer confidence readings. These positives were mostly the result of data gathering during the month of April, so it will be very telling if we see slowdowns in these figures in June, reflecting the sentiment in May during a sour month for the market.

In currencies, the dollar generally continued to strengthen, but interest rate movements were mixed. The short end of the curve continued to rise while long-term rates have trended flat thus far this year, as well as the past twelve months. Commodity prices were up for Gold, Crude Oil, and Gasoline.

The strongest domestic sectors for investors were in Consumer Staples, Technology, and Health Care, while the worst performers were Financials, Industrials, and Energy. As the market recovered from March of 2009 through the end of April 2010, the sectors that performed best subsequently performed the worst in May 2010.

Emerging Markets

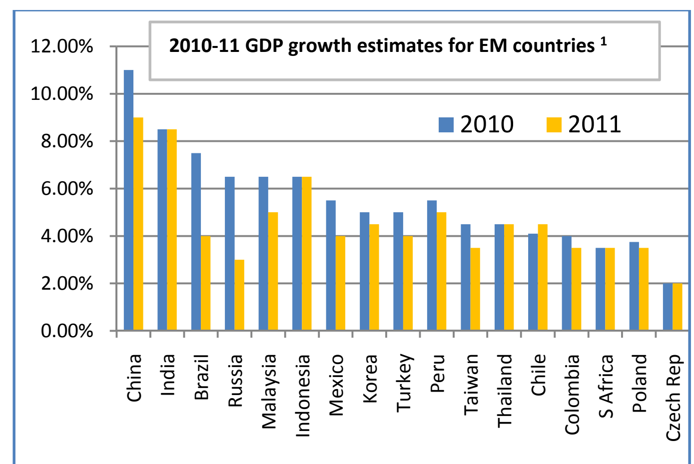
Some investors view a mutual fund or exchange traded fund (ETF) that represents the S&P 500 as a diversified investment. It appears that your money will be spread across a wide variety of companies, but when measured against the totality of international markets, the S&P 500 only scratches the surface with regard to global diversification. Yes the U.S. market is the biggest and most heavily capitalized market, but if an investor is to truly seek opportunity, they would be naive to not look for accretive investments overseas.

This adds to the conversation with the idea of tapping into Developed Markets (DM) or Emerging Markets (EM). The Great Recession and related crisis has caused some investors to feel cautious about investing overseas and only expose themselves to the developed markets. But as we have realized, the U.S. and the rest of the developed world actually had greater issues than emerging market countries. Much of the challenge that faces developed regions, such as high debt and poor capitalization, is not as great an issue for emerging areas. These markets tend to have high consumer savings rates which can create a boon for expansion.

Daniel Tubbs, Director and portfolio manager of the BlackRock Global Emerging Markets Fund, recently commented, "Though investing in emerging markets is not as 'foreign' a concept as it once was, these regions continue to be vastly underrepresented in investors' portfolios." From our vantage point as investment advisors and portfolio managers, we certainly see the same issue. Let us address what is attractive about EM.

Why EM Today

The EM asset class has been traditionally viewed as "risky" and "volatile" but with great opportunity. Our view is that the volatility has lessened a bit, but the opportunity remains – a great combination. All parts of the world were affected by the financial crisis, but due to having less exposure to leverage and showing strong valuations, today the EM market is positioned with perhaps the greatest growth potential.



As the above chart indicates, expectations for GDP growth in EM countries is far higher than for the DM countries. The U.S. is projected to grow by 3-4% this year, close to its 20 year average. Compare that to Brazil, Russia, India, and China (the BRIC countries) in the above chart, and you can clearly see that for an investor seeking *opportunity*, the U.S. is likely to lag.

We are seeing EM valuations that are comparatively strong, and similar levels in the past have resulted in positive returns. The current level of Price to Earnings (P/E), Price to Book (P/B), and equity risk premium (ERP) in emerging market countries is in line with periods that led to 6 month average market upside of 10%-33%[2]. Because of the recent correction in the month of May, oversold conditions may exist that will allow investors to begin to buy into EM with some comfort that they are not overpaying for their exposure.

Within our Global Allocation Portfolio utilizing domestic and international indexes, we are looking to overweight our Emerging Market exposure as the opportunity arises. We were able to remove ourselves from Spain prior to the European crisis of this spring, and reduced our DM exposure – a turnaround from our stance late last year – and have been in cash up to 18% recently. However, as you can tell from our encouragement to investors in this Market Letter, we feel the best risk reward opportunities may be outside of the U.S.

EM Final Word

Generally, our approach to investing is to seek opportunity and avoid peril. Understandably, international investing involves risks from foreign currency, limited liquidity, government regulation, and the potential for adverse political and economic influences. However, with proper diversification, and professional investment selection, the overall risk to an investor can be manageably reduced.

Factoids

• June is a tough month - The last time the month of June produced at least a gain of 2% on a total return basis for the S&P 500 was a decade ago when the stock index was up +2.5%. Over the last 20 years (1990-2019), June has averaged a 0.3% loss[3].

• May retreat – As of Friday April 23rd, the S&P 500 was up +9.8% YTD, its peak for the year. As of last Friday June 4th, the S&P 500 is down -3.7% for the year, a swing of over 13%[4].

• Volcker and Bernanke – The target range for the short-term fed funds rate is between 0% and 0.25% today. The range was between 19% and 20% in January 1981[5].

• 2010 tax windfall – The government projects that total tax receipts for fiscal year 2010 (12 months ending 9/30/2010) will be $2.165 trillion or 15% of the $14.6 trillion U.S. economy[6].

Considering the content of this month's Market Letter, you may have questions. If you are uncomfortable with your current investment plan, we encourage you to contact us to discuss your situation. Please call 610-629-0660, or email us at PaulL@centurionassetmgt.com , to discuss your feedback or questions.

Sincerely,

Paul G. Liebezeit, CFP®
Principal
Centurion Asset Management, LLC
www.centurionassetmgt.com

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[1] GDP growth estimates, source Morgan Stanley Research Investment Perspectives Emerging Markets, June 3, 2010.

[2] Source : IBES, Factset, DataStream, MS research

[3] Source : BRN Research

[4] Source : BTN Research

[5] Source : Federal Reserve

[6] Source : Treasury Department

Past performance is no guarantee of future results. Indexes are unmanaged, do not incur fees or expenses and cannot be invested in directly. Investing in sectors may involve a greater degree of risk than investments with broader diversification. International investments are subject to additional risks such as currency fluctuations, political instability and the potential for illiquid markets. Investing in emerging markets can accentuate these risks.

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