



“THOSE WHO FORGET HISTORY  
ARE DOOMED TO REPEAT IT?”

The Dalbar Study has shown that the average mutual fund investor substantially underperforms the S&P 500 index. Why might that be? Emotion. When people are feeling nervous and fearful, there is a tendency to want to be invested in safe asset classes with low volatility. When they are feeling confident, and even greedy, there is a tendency to take on more risk. Unfortunately, confidence tends to peak at the top of markets and fear tends to peak at bottoms. As a consequence, investments based on emotions tend to lead to very poor investment results. To illustrate this point, the attached table shows returns based on a \$100 investment in each of 3 categories (Stocks, T-Bills, T-Bonds) in 1928. From 1928 through 2008, we noticed that there were three 10-year periods of outperformance by T-Bills and/or T-Bonds as compared to Stocks. These periods were 1928 to 1937, 1965 to 1974, and 1999 to 2008. In the two periods separated by these three 10-year spans (the first for 29 years and the second for 26 years), the outperformance by Stocks over T-Bills and/or T-Bonds was enormous. It is also interesting that, even with these three 10-year underperforming periods, the \$100 investment in Stocks in 1928 is \$112,968 in 2008, while T-Bills is \$1,964 and T-Bonds is \$6,013. No one knows what the future will bring, but IF history is to be a guide, it may be that the next few decades could be favorable to Stocks once again. It is also interesting that in the three 10-year periods, the first one encompassed the Crash of 1929 and the Great Depression, while the second one included The Cold War, a huge oil shock and double-digit interest rates, and the current one we all know only too well.

SHOULD WE BE BONDING?

Warren Buffet, often thought of as the world’s greatest investor, is predicting a “bubble” in U.S. Treasuries. He said U.S. Treasuries might be regarded in hindsight as “almost equally extraordinary” as the internet bubble of the late 1990s or the housing bubble earlier this decade. He further said that “clinging to cash equivalents or long-term government bonds at present yields is almost certainly a terrible policy if

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## CRITICAL MATH ADVISORS MARCH 2009 NEWSLETTER

continued for long.” He continued “that wonderful cash is earning close to nothing and will surely find its purchasing power eroding over time.” We view these comments as further support for our adaptive allocation strategy. If, as in the past, stock markets once again begin to outperform T-Bills and Treasuries, it will be essential to be nimble and able to take advantage of that circumstance. Many investors will stay in T-Bills and bonds for too long and miss some or even all of that stock market recovery. We believe that being adaptive and able to respond to ever-changing market conditions will be critical in the years ahead.

It is important to note that bonds, especially Treasuries, are interest sensitive vehicles. Total return on bonds does best in an environment where interest rates decline. Rising rates cause total return to suffer. It certainly seems that, in the near term, rates will have to stay low, but Federal Reserve Chairman Bernanke has stated numerous times that as the economy improves, monetary and fiscal stimulus will have to be withdrawn, and that would mean rising interest rates. That environment would not be favorable to bonds.

### THE LONG AND THE SHORT OF IT

Market sentiment is currently as low as we’ve ever seen it, with many sellers of stocks and relatively few buyers. Historically, this is the kind of sentiment that marks stock market bottoms. Will this time be different? No one knows. In the past, however, every seemingly disastrous economic environment has turned up, just, as I might add, every seemingly wonderful environment turns down. Has the cycle been broken? No one knows. If it has not, the next up cycle could be extremely interesting, if history is, in fact, an accurate guide.

Recently a well-known manager of a short fund, which had done very well in 2008 and thus far in 2009, said that people should not buy his short fund now. He predicted that “the S&P 500 index will surge to at least 1000 in 2009,” representing a gain of 40%.

### HOW NOW DOW JONES

During a recent conversation regarding the Dow Jones Industrial Average, it was suggested that in May 2007, those 30 stocks, listed below, would have represented, in his eyes, the bluest of blue chips with very good prospects for downside protection in terms of overall returns.

CRITICAL MATH ADVISORS  
MARCH 2009 NEWSLETTER

<b>3M</b>	<b>HOME DEPOT</b>
<b>ALCOA</b>	<b>INTEL</b>
<b>AMERICAN EXPRESS</b>	<b>IBM</b>
<b>AT&amp;T</b>	<b>JOHNSON &amp; JOHNSON</b>
<b>BANK OF AMERICA</b>	<b>JP MORGAN CHASE</b>
<b>BOEING</b>	<b>KRAFT FOODS</b>
<b>CATERPILLAR</b>	<b>MCDONALDS</b>
<b>CHEVRON</b>	<b>MERCK</b>
<b>CITIGROUP</b>	<b>MICROSOFT</b>
<b>COCA COLA</b>	<b>PFIZER</b>
<b>DU PONT</b>	<b>PROCTER &amp; GAMBLE</b>
<b>EXXON MOBIL</b>	<b>UNITED TECHNOLOGIES</b>
<b>GENERAL ELECTRIC</b>	<b>VERIZON</b>
<b>GENERAL MOTORS</b>	<b>WAL MART</b>
<b>HEWLETT PACKARD</b>	<b>WALT DISNEY</b>

It is hard to believe that from May 1, 2007 to February 27, 2009, these stocks, combined, lost over 40% of their value. Of course, we are looking in the rearview mirror, and I think everybody would agree that hindsight is 20/20.

We have all learned recently that if an investment promises double-digit returns every year, there is a strong possibility that a fraud is involved somewhere. As we have stated many times in the past, no investment strategy is perfect. Ours is designed to reduce risk in down markets and enhance returns in up markets. Bruce Greenwald, the Columbia Business School professor known as The Guru, was examining Warren Buffet's Berkshire Hathaway company. He said that, even though Berkshire Hathaway stock lost almost 50% of its value, the companies that Mr. Buffet invested in had performed extremely well, having been down "only" around 20%. It would seem as though we are in good company.

CRITICAL MATH ADVISORS  
MARCH 2009 NEWSLETTER

HOW & WHEN?

Most mutual funds, as well as many investors, do not have an exit strategy to cash, but for different reasons. Most mutual funds are required by prospectus to be “fully invested.” This guideline allows them to move up as the market moves up, but causes them to move down when markets move down. Investors, on the other hand, don’t know what indicators might call for a change in investment strategy. The bottom line.....the results of most mutual funds and investors tend to closely mirror or substantially underperform the markets in general. Our strategies enable us to respond to the current state of the markets, allowing us to be in large cap stocks or small, growth or value, foreign or domestic, or none at all, while not being locked in to any one position.

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Please remember that past performance may not be indicative of future results. Different types of investments involve varying degrees of risk, and there can be no assurance that the future performance of any specific investment, investment strategy, or product made reference to directly or indirectly in this newsletter, will be profitable, equal any corresponding indicated historical performance level(s), or be suitable for your portfolio. Due to various factors, including changing market conditions, the content may no longer be reflective of current opinions or positions. Moreover, you should not assume that any discussion or information contained in this newsletter serves as the receipt of, or as a substitute for, personalized investment advice from Critical Math Advisors LLC. To the extent that a reader has any questions regarding the applicability of any specific issue discussed above to his/her individual situation, he/she is encouraged to consult with the professional advisor of his/her choosing. A copy of our current written disclosure statement discussing our advisory services and fees is available for review upon request.

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The S&P 500 Index is an unmanaged composite of 500-large capitalization companies. This index is widely used by professional investors as a performance benchmark for large-cap stocks.

## Annual Returns on Stock, T.Bonds and T.Bills: 1928 - Current

The raw data for treasury bond and bill returns is obtained from the Federal Reserve database in St. Louis (FRED). The treasury bill rate is a 3-month rate and the treasury bond is the constant maturity 10-year bond, but the treasury bond return includes coupon and price appreciation. It will not match the treasury bond rate each period. For more details, download the excel spreadsheet that contains the same data.

Year	Compounded Value of \$ 100		
	Stocks	T.Bills	T.Bonds
1928	\$143.81	\$103.08	\$100.84
1929	\$131.88	\$106.34	\$105.07
1930	\$98.75	\$111.18	\$109.85
1931	\$55.46	\$113.74	\$107.03
1932	\$50.66	\$114.96	\$116.44
1933	\$75.99	\$116.06	\$118.60
1934	\$75.09	\$116.44	\$128.05
1935	\$110.18	\$116.64	\$133.78
1936	\$145.38	\$116.84	\$140.49
1937	\$94.00	\$117.19	\$142.43
<b>Return for the 10 Year Period (1928 thru 1937):</b>	<b>-34.64%</b>	<b>13.69%</b>	<b>41.24%</b>
1937	\$94.00	\$117.19	\$142.43
1938	\$121.53	\$117.29	\$148.43
1939	\$120.20	\$117.33	\$154.98
1940	\$107.37	\$117.36	\$163.35
1941	\$93.66	\$117.46	\$160.04
1942	\$111.61	\$117.85	\$163.72
1943	\$139.59	\$118.30	\$167.79
1944	\$166.15	\$118.75	\$172.12
1945	\$225.67	\$119.20	\$178.67
1946	\$206.65	\$119.65	\$184.26
1947	\$217.39	\$120.33	\$185.95
1948	\$229.79	\$121.56	\$189.58
1949	\$271.85	\$122.90	\$198.42
1950	\$355.60	\$124.34	\$199.27
1951	\$439.80	\$126.18	\$198.68
1952	\$519.62	\$128.29	\$203.19
1953	\$513.35	\$130.72	\$211.61
1954	\$783.18	\$131.98	\$218.57
1955	\$1,038.47	\$134.17	\$215.65
1956	\$1,115.73	\$137.60	\$210.79
1957	\$999.05	\$142.04	\$225.11
1958	\$1,435.84	\$144.57	\$220.39
1959	\$1,608.95	\$149.27	\$214.56
1960	\$1,614.37	\$153.82	\$239.53
1961	\$2,044.40	\$157.30	\$244.46
1962	\$1,864.26	\$161.67	\$258.38
1963	\$2,285.80	\$166.70	\$262.74
1964	\$2,661.02	\$172.54	\$272.53
1965	\$2,990.97	\$179.28	\$274.49
<b>Return for the 29 Year Period (1937 thru 1965):</b>	<b>3081.88%</b>	<b>52.98%</b>	<b>92.72%</b>

1965	\$2,990.97	\$179.28	\$274.49
1966	\$2,692.74	\$187.95	\$282.47
1967	\$3,333.69	\$196.10	\$278.01
1968	\$3,694.23	\$206.41	\$287.11
1969	\$3,389.77	\$219.96	\$272.71
1970	\$3,510.49	\$234.66	\$318.41
1971	\$4,009.72	\$245.32	\$349.57
1972	\$4,761.76	\$255.01	\$359.42
1973	\$4,080.44	\$272.16	\$372.57
1974	\$3,023.54	\$293.33	\$379.98
<b>Return for the 10 Year Period (1965 thru 1974):</b>	<b>1.09%</b>	<b>63.62%</b>	<b>38.43%</b>
1974	\$3,023.54	\$293.33	\$379.98
1975	\$4,142.10	\$310.90	\$393.68
1976	\$5,129.20	\$326.35	\$456.61
1977	\$4,771.20	\$343.09	\$462.50
1978	\$5,081.77	\$366.87	\$458.90
1979	\$6,022.89	\$403.33	\$461.98
1980	\$7,934.26	\$448.58	\$448.17
1981	\$7,561.16	\$512.73	\$484.91
1982	\$9,105.08	\$569.18	\$644.04
1983	\$11,138.90	\$617.26	\$664.65
1984	\$11,823.51	\$676.60	\$755.92
1985	\$15,516.60	\$727.26	\$950.29
1986	\$18,386.33	\$771.15	\$1,181.06
1987	\$19,455.08	\$815.27	\$1,122.47
1988	\$22,672.40	\$867.86	\$1,214.78
1989	\$29,808.58	\$938.24	\$1,429.72
1990	\$28,895.11	\$1,009.08	\$1,518.87
1991	\$37,631.51	\$1,065.69	\$1,746.77
1992	\$40,451.51	\$1,101.98	\$1,910.30
1993	\$44,483.33	\$1,134.84	\$2,181.77
1994	\$45,073.14	\$1,180.07	\$2,006.43
1995	\$61,838.19	\$1,245.15	\$2,477.55
1996	\$76,566.48	\$1,307.68	\$2,512.94
1997	\$100,958.71	\$1,373.76	\$2,762.71
1998	\$129,568.35	\$1,438.70	\$3,174.95
1999	\$156,629.15	\$1,503.58	\$2,912.88
<b>Return for the 26 Year Period (1974 thru 1999):</b>	<b>5080.32%</b>	<b>412.59%</b>	<b>666.59%</b>
1999	\$156,629.15	\$1,503.58	\$2,912.88
2000	\$142,482.69	\$1,590.23	\$3,398.03
2001	\$125,598.83	\$1,648.63	\$3,587.37
2002	\$98,009.73	\$1,675.96	\$4,129.65
2003	\$125,801.18	\$1,693.22	\$4,145.15
2004	\$139,315.72	\$1,714.00	\$4,331.30
2005	\$146,050.90	\$1,765.59	\$4,455.50
2006	\$168,853.19	\$1,848.18	\$4,542.87
2007	\$178,114.34	\$1,933.98	\$5,006.69
2008	\$112,968.13	\$1,964.64	\$6,013.10
<b>Return for the 10 Year Period (1999 thru 2008):</b>	<b>-27.88%</b>	<b>30.66%</b>	<b>106.43%</b>

**SOURCE:** [http://pages.stern.nyu.edu/~adamodar/New\\_Home\\_Page/datafile/histretSP.html](http://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/histretSP.html)

**Please remember that past performance may not be indicative of future results.**