



HANLON
INVESTMENT MANAGEMENT, INC.

Market Commentary



Sean Hanlon, CFP®
Chief Executive Officer and
Chief Investment Officer

Why Hanlon Investment Management Continues to Like High Yield Corporate Bonds in This Economic Environment

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In the last week of 2008 Hanlon Investment Management began to purchase high yield corporate bonds in our client accounts, where available. Prior to that, we had been 100% in money markets for all our client accounts for months and months. In our December 24, 2008 IA Alert we described the reasons for that new found enthusiasm for high yield corporate bonds. The reasons were as follows:

- ✓ The average current yield on high yield corporate bonds had hit an all-time high greater than 20% in November / December 2008.
- ✓ The yield spreads had contracted for the first time in months. In this case the yield spread is the difference in interest rates between what “risk free” US Treasury’s are paying and what high yield corporate bonds are paying.
- ✓ By November 2008 the Merrill Lynch High Yield Corporate Bond Index had suffered its greatest six month decline ever, which we thought was overdone. It bottomed in mid-November, appreciated some, then dropped again to about the November lows, re-tested those lows, and then appreciated past the prior short term highs.

Last week Hanlon increased client account investments in high yield corporate bonds by another 25%, in all allocations. All of our client accounts are now invested in 75% high yield corporate bond funds, where available (products that use Rydex and Profunds are still 100% in money market – please see our latest weekly update for all product weightings by clicking on this [link](#)).

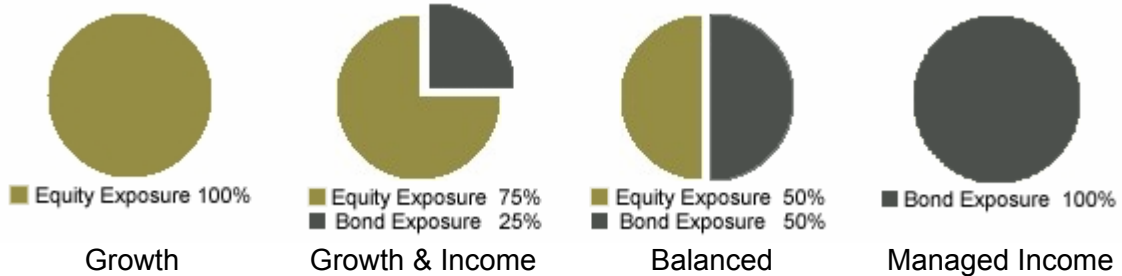
The remainder of this Market Commentary will explain why our client accounts are only in high yield corporate bonds at this time, even for the components of three of our allocations which would normally be invested in equity funds. We have not changed our standard, long-term approach to portfolio allocations at all; just now this portfolio allocation is best.

One of the attributes that is common to Hanlon account management is that we attempt to have an acute awareness of risk. We believe that the equity and bond markets are far more risky than most individual and professional investors realize. Our money management strategies are geared toward attempting to reduce risk and generate market beating returns, without any guarantees of course. To that end, after the client completes our standard Investor Profile Questionnaire (IPQ), the result is a recommendation for their account to be managed in one of our Allocations.



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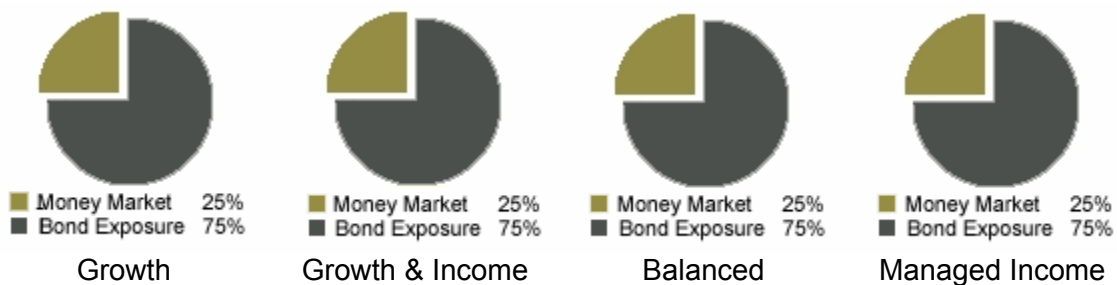
These Allocations, each with a successively declining risk profile, are normally as follows when fully invested, i.e. when we are most comfortable with the market risk.



The above is an approximate allocation “maximum” that we would dedicate to the equity and bond asset classes under normal conditions. We would manage these asset class “pools” separately and would not decline – meaning if we did not like equities, that portion of the above Allocations would be in money markets. The same is true for the bond portion.

However, in keeping with our desire for the best risk adjusted returns for our client accounts, we will, in certain economic and market conditions, increase the bond exposure beyond the above limits. Of course this is all to the extent that we think it will benefit our client accounts. Note that we will not typically exceed the equity maximums listed above, but that we will at times exceed the bond maximums. Now is one of those times. Although rare, we have experienced this type of market condition before, as it occasionally occurs.

Currently our Allocations are as follows:



We believe that high yield corporate bonds present a far superior risk-reward opportunity than equities. Think about it. High yield corporate bonds have current yields on the order of approximately 13%+, basically 1%+ per month. So if the high yield corporate bonds go sideways in price for the next year (not a prediction, just example) we will gross 13% from these investments. If these high yield corporate bonds appreciate in value some, then that is additional total return that we will benefit from. Of course they could depreciate and we would



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likely sell them in that case. These are not projections or guarantees of returns or future portfolio transactions and results, just examples. Client accounts can lose value.

Stocks, on the other hand, have been very choppy and down in price, with no discernible positive trend to the upside as of yet. The earnings prospects for the S&P Index companies are as bleak as I have ever seen them. The probabilities, currently, for stocks to turn in a good performance in the foreseeable future is quite low. But high yield corporate bonds pay us while we wait, in form of interest. Or research is uncovering that at this time, with this environment, bonds present a far more compelling opportunity than equities. Of course, rest assured that should equities begin to demonstrate an improved enough risk-reward relationship, then we will modify the client portfolios accordingly.

These are not normal times. We are proud and comfortable that our money management techniques provide you and your portfolio with this flexibility, all geared towards an attempt at a successful outcome.

Thank you,

Sean Hanlon, CFP®
CEO and CIO

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