

## The Farm:

Just yesterday someone I have known for some time came in and brought me some farm fresh eggs! I took all nine of them home and my family ate them over the next two days. It reminded me of the simple things in life we all forget. I remember raising pigs, 4H, and many of the great times I had growing up in rural Indiana. (even baling hay in the hot summer days) Just as I said on the front article, these glimpses in time get us back to our core values and show us what we are made of. We remember when we were a bit more frugal with our dollars and did not chase the latest craze whether it is an "apple" or the latest shoes. This time the market has forced this reflection on many of us. We are a very strong nation of individuals. When we come together, anything can happen. I have said in my weekly blogs before that the energy crisis and now the financial crisis are going to make the USA more innovative. I believe the Farm operated by the USA will prove to be more productive and innovative than any of our farms in the past. We need to plant the seeds of greatness even if we have a few setbacks politically and economically.

*The opinions written within this publication are the opinions of Troy Patton and are not intended as investment advice or an offer or solicitation to buy or sell any securities. Investing may result in loss. If you would like to contact Troy Patton, he can be reached directly at 800-671-5872.*

**QUARTERLY GUIDE TO BUILDING AND MAINTAINING WEALTH**



## A Glimpse:

by Troy Patton, CPA

I hope you have seen the movie, *Family Man*. It stars Nicolas Cage and he is thrust into a different time to get a glimpse of what his life would have been like had he married his sweetheart. He lived the "perfect" life only to see what ruin his life may have been had he followed a different path and got married worked for her Father at Big Al's selling tires and raising two kids who are a challenge of their own. However, in the end it is not ruin, but it gives him a glimpse of a better life. One that he had not foreseen, but made him a better person as a result.

This market has done the same thing, it has given us all a glimpse of a different world where there is personal responsibility for one's actions. We have seen a glimpse of the other side and it is going to make us all better for seeing tough times. It may not be sitting well with the market down, but this too shall pass. However, I have learned some valuable lessons as I think we all have.

This most recent run in the market is also a glimpse of what is to come. The market has sprinted off the bottom and run back up to where the bottom maybe should be. However, this base will be tested over and over. It will head lower and then higher and trade within a range before the final sprint. This recent 20% run will look like child's play once the earnings return to Wall St. On the next couple of pages, I am going to

show what this means to the markets and your pocket book. Can you imagine the market moving higher than 60% to 80% off the bottom. It may happen. I am going to show you why and when in my estimate this will take place. It will give us a glimpse into the future. This does not mean we forget our new found frugality.

I also will show you why this market down the road will find some tougher footing in terms of inflation and how I plan to combat some of this.

Many of you are thinking things are looking bleak. There is a financial crisis, unemployment is soaring and heading higher, home prices have fallen, taxes are being increased, more government involvement in our lives, etc. Let me explain one thing and it is simple to understand.

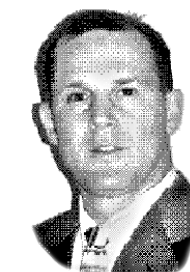
This market is UNDEFEATED in comebacks. That is right. The market has always come back. Whether it is the Great Depression, World Wars, or the inflation days of the 70's and early 80's, this market has always been able to shake it off and find some firmer footing, the economy has rebounded, housing prices have fallen, numerous crisis have risen and fallen. This time will be no different. The country we live in and the people who inhabit it are resilient even if we do not all agree all the time. -UNDEFEATED-

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### Troy C. Patton, CPA

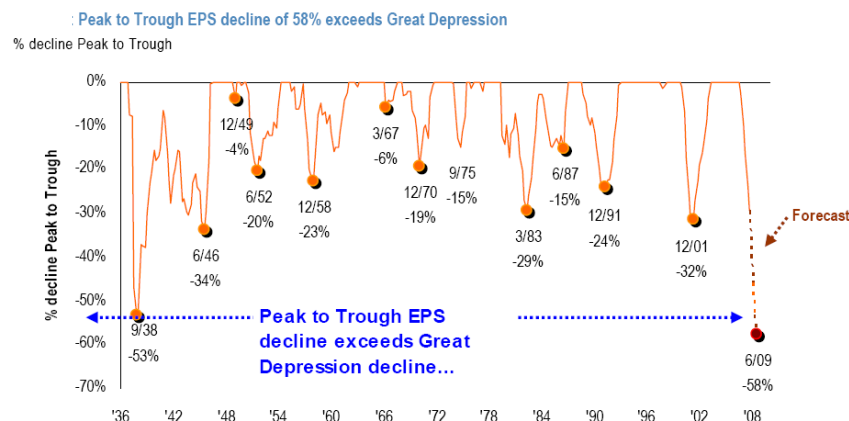
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### How do the Earnings Compare? By Troy Patton

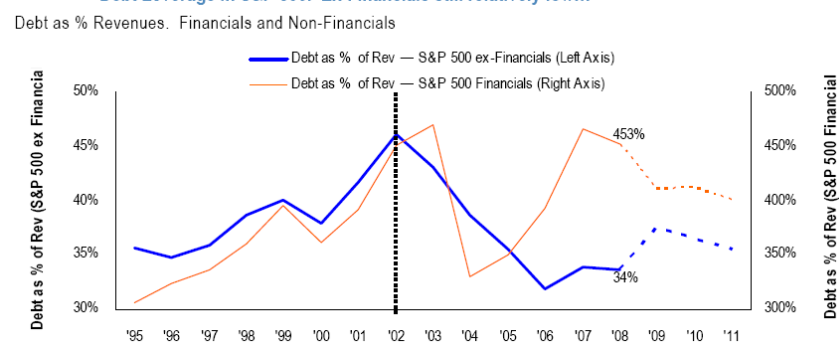
Earnings are bad. How do they compare to other downturns in the market. Can we use them to predict where the market is headed? Let's take a look at the first chart. The most recent earnings downturn is very comparable in percentages of declines to the Great Depression. This is based on what the estimated earnings are to be ending with June 2009 estimates. In fact, the earnings percentage will fall more than those of the Great Depression. We need to understand is earnings are not calculated the same way today as the 1930's. We now have mark to market accounting and other accounting changes that would greatly influence these earnings. My estimate is the earnings would have declined about 35%. The majority of this is from the banking sector. The second quarter of 2009 is estimated to be the bottom of the earnings crisis.



ings crisis. At this point, we are expected to move quite higher. On the next page, I will show how the earnings have progressed.

The chart at the bottom clearly shows how the financials were clearly irresponsible in leveraging their debt to levels that were astronomical. All the while the rest of the companies in the S&P 500 were deleveraging their balance sheets as seen by the blue line.

Debt Leverage in S&P 500. Ex-Financials still relatively low...



The reason I have shown both of these charts on one page is because the vast majority of this downturn has been caused by the irresponsibility of the large and small financial institutions with the backing of a government that wants to give a house to everyone. Now we know, not everyone will get an A in school and some will not pay their bills even if you give them the lowest rate on earth.

### Spring is Here!

Old Man Winter, has left the building. My yard is green, the grass is growing and new leaves are starting to bud after a long-cold bleak winter where the market was about as bleak as the gray skies. Spring is always more fun as the kids can get out of the house run around the yard and see new growth. This market is showing some signs of its own spring. Giving us a taste of summer or a hopeful longer period of growth and warmth is what we are all longing for.

Don't be lulled to sleep. Spring sometimes brings with it violent storms and some cold weather and hard rains. These always feel like setbacks, but we know that better weather will arrive, we have to be patient.

### Earnings and the Markets, Where do we Go? .... By Troy Patton

Earnings are what drive the markets. It really is this easy. What if I told you the S&P 500 will have hit 950 by the end of this year. Then in 2010 it will extend its gains to a level near 1250. This is a 56% gain from where we are as I write this newsletter, even after a 20% run up in the markets. You may be asking how is this possible? Let me explain using some hard cold facts as well as some estimates. You can take the estimates of the companies in the S&P 500 and use their weight towards that index and come up with the earnings that are expected to be reported as well as the past earnings, as seen below.

Composition of S&P 500 Operating EPS by Sector

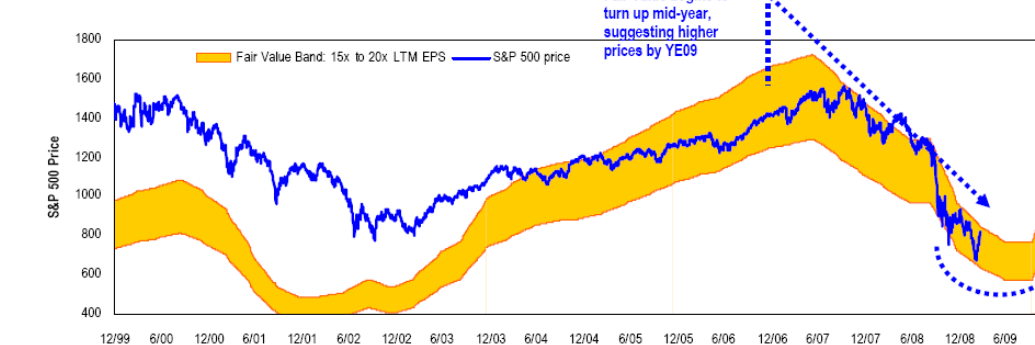
2002 to 2010E	2002	2003	2004	2005	2006	2007	2008	2009	2010
Resources									
Energy	\$1.40	\$4.84	\$7.18	\$11.50	\$13.42	\$14.32	\$16.17	\$9.27	\$11.89
Materials	\$0.38	\$0.97	\$1.90	\$2.32	\$3.00	\$3.00	\$1.52	\$1.58	\$1.84
Exporters									
Industrials	\$4.33	\$5.12	\$5.99	\$7.63	\$9.13	\$10.16	\$9.98	\$5.59	\$7.76
Technology	(\$1.89)	\$3.90	\$6.70	\$7.97	\$9.07	\$10.39	\$9.56	\$8.40	\$8.67
Defensives									
Staples	\$4.65	\$5.49	\$6.40	\$6.50	\$6.98	\$7.82	\$8.81	\$8.82	\$10.16
Health Care	\$5.57	\$4.81	\$6.20	\$7.45	\$8.94	\$10.04	\$10.54	\$11.80	\$13.03
Telecom Services	(\$1.48)	\$1.79	\$1.10	\$2.29	\$2.58	\$2.64	\$2.56	\$2.55	\$2.67
Utilities	\$0.72	\$1.30	\$2.28	\$2.38	\$3.05	\$3.01	\$3.03	\$3.25	\$3.12
Other									
Consumer Discretionary	\$0.42	\$5.13	\$4.58	\$4.43	\$7.81	\$6.51	\$2.45	\$3.42	\$5.22
Financials	\$12.56	\$16.06	\$17.13	\$19.02	\$23.75	\$14.66	(\$14.48)	\$1.99	\$11.37
<b>Total S&amp;P 500 EPS Operating</b>	<b>\$26.49</b>	<b>\$49.38</b>	<b>\$59.05</b>	<b>\$71.27</b>	<b>\$83.07</b>	<b>\$68.05</b>	<b>\$49.49</b>	<b>\$66.65</b>	<b>\$75.73</b>

We can clearly see in 2007 the decline in earnings of the financials after starting to deleverage in 2007. Financials have not only lost all their earnings, but have slipped to negative territory due to mark to market accounting as well as some being leveraged 30 to 1 and not having any hedges in place in case things went wrong. I say good riddens to

them. What I am more interested in is the expected earnings as some of these banks start to come back. You can see the change from 2008 to 2009 for the financials even while the Energy companies decline due to the downturn in oil prices. The recession has taken its toll on many of the Sectors above except for Health Care which continues to post gains. Even more telling is the expected earnings in 2010.

The chart below then shows how the market has generally traded within 14-20 times earnings. Some of this will depend on how inflation responds to the 90%+ increase in monetary supply. Basically the government is printing money to pay for all the programs as well as buying all the US

Why we see a bottom around mid-2009



Treasuries and asset backed mortgages. This is sure to cause inflation which will move the trading band lower. Even with this, the market should move much higher, then pause before heading even higher.

I am confident that there will be other ways to make money before inflation shows its ugly head. We have those plans at our disposal and plan to implement them over the next quarter or two to hedge against inflation. As such, after a 50% run in the market from these levels, we should generally see a sideways move before ultimately moving higher. It will take time, but we are going to get there.