TRIVANT

CUSTOM PORTFOLIO GROUP, LLC

October 2011

Quarterly Insights

EXECUTIVE SUMMARY

Stocks Fall Hard In Third Quarter, Treasury Bonds Rise

In the Third Quarter, the domestic S&P 500 Index fell 13.87%. The grass was not greener on the other side of the fence. Foreign (MSCI EAFE Index) was down 18.95%. Emerging Markets sank 22.46%. The Russell 2000 (small cap) Index was down 22.15%. US blue chip stocks were the place to be on a relative performance basis. The leading causes of market concern continued to be the Greek debt crisis, the state of both the US and global economies, and employment. We view eroding investor confidence as a major market factor. US Treasurys fared well as investors fled to safety.

The Sentiment "Smile & Smirk": Embrace Low Confidence

When the Michigan Consumer Sentiment data is divided into ten deciles of sentiment (lowest to highest) and compared to S&P 500 Index stock returns, the graph forms a smile and smirk. The smile forms because market returns are highest when sentiment is extremely low or very high. The smirk forms when returns fall at sentiment bubbles.

Sentiment has reached its lowest level in 30 years. Low sentiment signals above-average potential returns. Stick to your investment strategy. And try to smile!

John Barber, CFA
Chief Investment Officer

Dan Laimon, MBA
Managing Member

Michael Harris, CFA
Vice President

Third Quarter 2011

In This Issue

www.trivant.com

1-866-4-TRIVANT

toll free

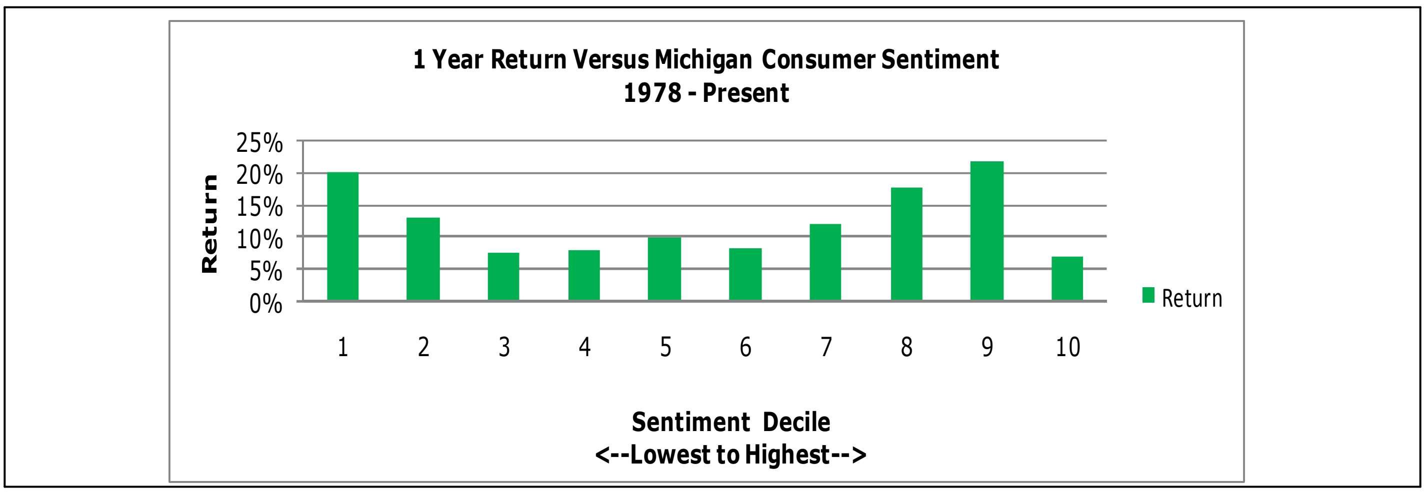
The Sentiment "Smile & Smirk"

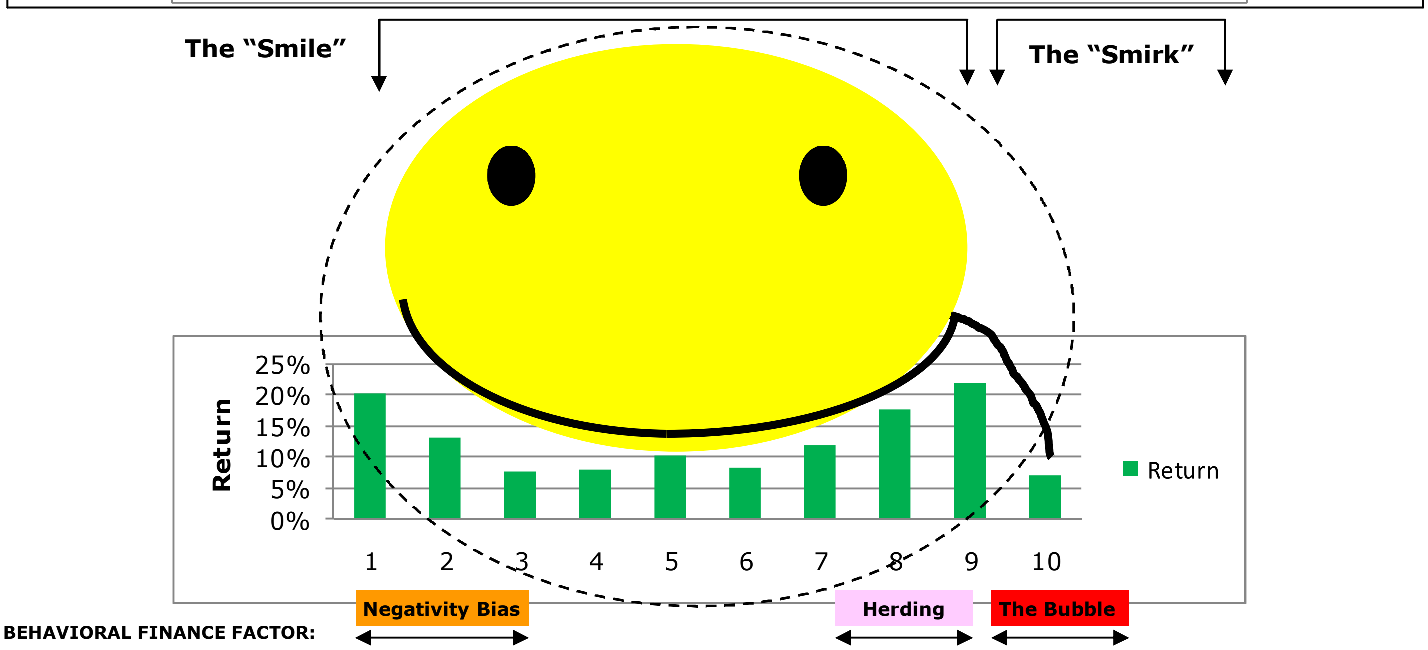
The Paradox Of Negative Sentiment

If you have been feeling on edge, you are not alone. The American public has been in a foul mood for some time. Contributing factors include a sluggish economy, weak employment, and European woes. The recent political stalemate surrounding the increase of the US debt ceiling brought down sentiment to its lowest levels in decades.

One of the older gauges of the country's mood, the Michigan Consumer Sentiment report, showed the lowest level of confidence in the past 30 years in July. Surprisingly, this should make you smile. Future one-year market returns are near their highest when sentiment is extremely low or very high.

The graph below splits the monthly Michigan Consumer Sentiment into ten deciles of sentiment, from lowest to highest. The S&P 500 Index stock returns are then calculated from that sentiment level for the following 12 months. Notice how the graph forms a smile and a smirk. The smile forms because market returns are highest when sentiment is extremely low or very high. However, at bubble levels of positive sentiment, returns fall to their lowest levels. This forms the smirk.





The Two Sides Of The Smile, And The Smirk

The Sentiment Smile & Smirk may seem counterintuitive but we believe the explanation can be found in behavioral finance. Extremes in pessimism have generally resulted in above average returns.

The Left Side Of The Smile: Negativity Bias

Originally derived from the Nobel Prize winning Prospect Theory of Tversky & Kahneman, Negativity Bias has been researched and extended by Baumeister and Bratslavsky. They have shown that bad events outweigh good events in forming investors' views. This causes beliefs to often be overly pessimistic. With the recent 30-year low in confidence, we believe investors are more bearish than is warranted. Negative bias is now in the first decile (lowest level) of sentiment. This provides an opportunity for above-average returns.

The Right Side Of The Smile: Herding

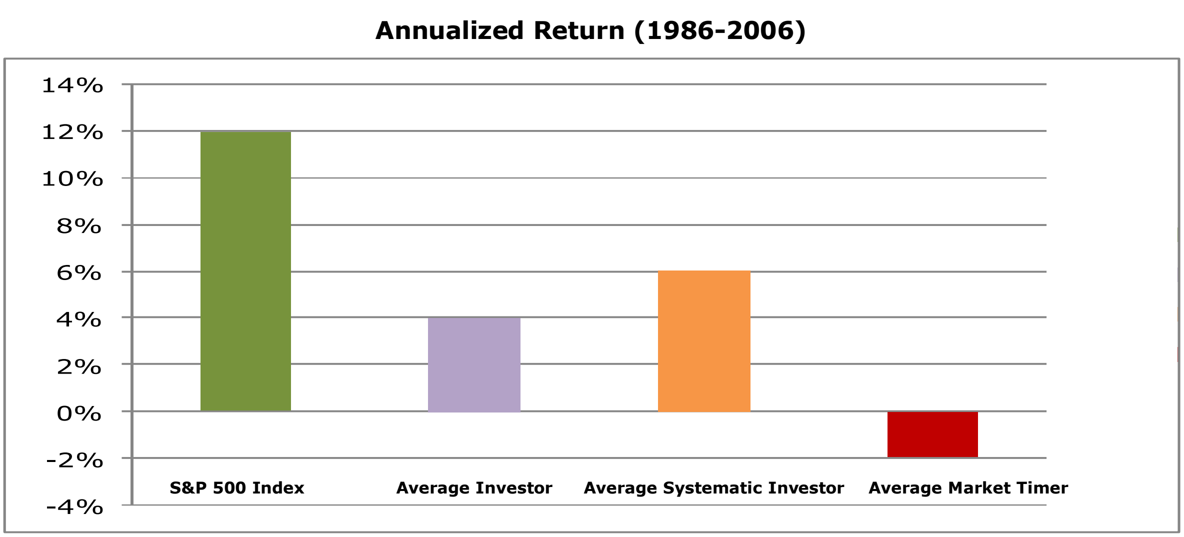
Returns fall as sentiment rises from the lowest levels. At slightly above average sentiment, returns start to increase. These higher returns foster further increased sentiment. Herding is a behavioral term that describes how others' views tend to affect your views.

The Smirk: Overconfidence And The Bubble

Very good sentiment is followed by good returns, but great sentiment is not. As investors become over-confident, they tend to dismiss risk and are therefore more vulnerable to it. Ironically, the worst returns are when sentiment is at its strongest. Bubbles end poorly. An example of a past bubble was Internet stocks (2001).

Don't Let Your Emotions Get The Best Of You

There is a natural tendency to try and avoid the stock market when your sentiment is low and enter the stock market when your sentiment is high. According to a study that measured the flow into and out of equity mutual funds among three investor categories, timing market entry and exit failed miserably from 1986-2006. Low sentiment signals above-average potential returns. Stick to your investment strategy. And try to smile!



Source: Bureau of Labor Statistics, DALBAR QAIB 2007, Charles Schwab

Stock Market Spotlight

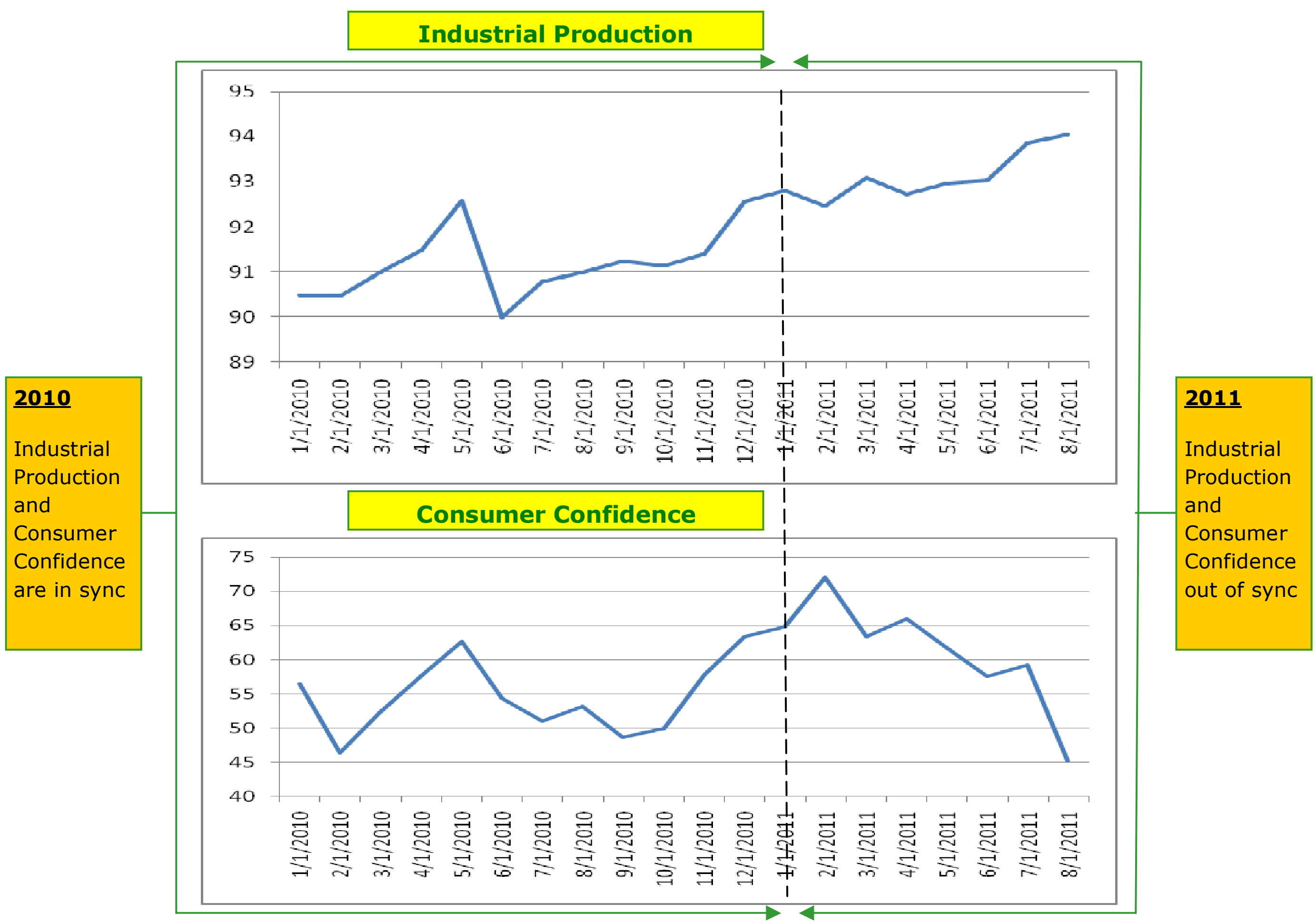
The Third Quarter Was Rough

In the Third Quarter, the domestic S&P 500 Index fell 13.87%. The grass was not greener on the other side of the fence. Foreign (MSCI EAFE Index) was down 18.95%. Emerging Markets sank 22.46%, led by China (-25.19%) and Brazil (-26.93%). The Russell 2000 Index, which gauges US small cap performance, was down 22.15%. US blue chip stocks were the place to be on a relative performance basis.

The leading causes of market concern continued to be the Greek debt crisis, the state of both the domestic and global economies, and employment. While we appreciate the reality and rationale of these concerns, we do not view them as dire as currently perceived. We expect Greece to default, but do not anticipate the event to be catastrophic. Economic growth is tepid, not spiraling downward. Employment is concerning yet stable: private sector job gains are outpacing public sector (government) job losses.

We Have A Confidence Crisis, Not An Economic Crisis

Industrial Production, a hard measure of the actual goods being produced in the United States, has been steadily rising since late-2010. Consumer Confidence, a soft measure of individual attitudes towards the economy, rose in sync with Industrial Production in 2010, but has diverged in 2011. There is a perception that the economy is in much worse shape than it really is. We have a confidence crisis, not an economic crisis.



Improved Confidence Should Catapult The Market

For quite a while, we have communicated to you that we believe companies are in good shape. They have attractive valuations, strong balance sheets and improving profits. Our view has not changed. We assess the recent market pullback as much more to do with investor emotion than hard data. Looking ahead, we think it is likely that hard data will trump investor emotion and the market will progress. What we need to catapult the market is improved confidence. And we think it is closer than most people think.

The Three Factors We Believe Will Improve Confidence

1. Improved Outlook Regarding The European Debt Crisis

The European debt crisis was the major contributing factor to the Third Quarter market pullback. We believe that a resolution (or even a partial resolution) would ease investor fears and spur the market. There are already signs of such a resolution.

The Spanish government recently announced that they are taking over three Spanish banks that had not been able to adequately recapitalize over the last few years. We view further potential nationalization of vulnerable European banks as positive. On October 9, Germany and France announced a concrete pledge to solve the debt crisis. The plan, which will include recapitalizing European banks, will be presented to world leaders at the G20 meeting in Cannes November 3 and 4.

"We are determined to do what's necessary to ensure the recapitalization of Europe's banks".
German Chancellor Angela Merkel (October 9, 2011)

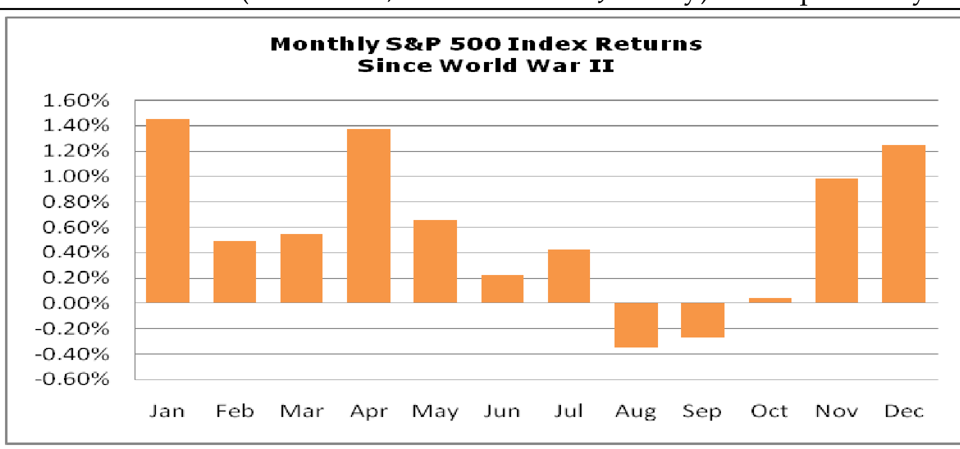
"The economy needs secure financing to ensure growth. There is no prospering economy without stable banks."
French President Nicolas Sarkozy (October 9, 2011)

2. Continued Economic Stability

We do not anticipate a major US economic expansion in the short-term. However, we believe continued economic stability will ease investor concerns. We are looking for stable or slightly improving data for Industrial Production, GDP and employment. And we believe the signs are there for this to happen.

3. Upward Market Momentum

A market upturn as we approach the end of the year would coax many investors from the sidelines. Historically the worst months in the market are August, September and October. We are heading into the historical best months in the market (November, December and January). Perhaps history will repeat itself.



Bond Market Spotlight

Opposing Market Forces: Investor Flight To Safety Versus S&P's US Downgrade

The Barclay's Capital U.S. Government / Credit Bond Index, a broad-based representation of bond performance, returned 4.74% in the Third Quarter and is up 7.46% for the year. This has occurred despite the Standard & Poor's recent downgrade of US sovereign debt to one notch below AAA.

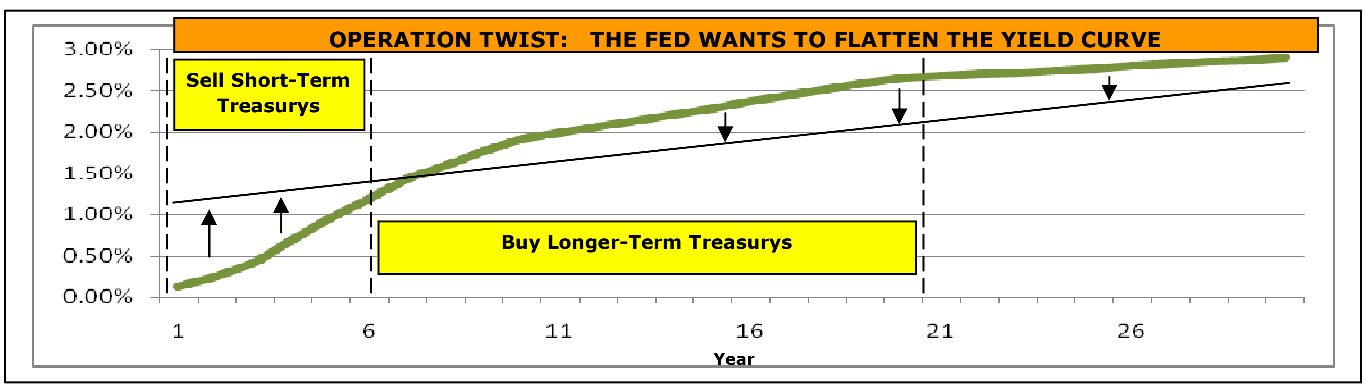
Clearly, the market is not worried in the least about the possibility of a US default, as evidenced by the yield on Treasurys. The 10 year US Treasury was yielding 2.58% yield to maturity on August 5, the day of the downgrade. Currently, the yield is 1.92%. A downgrade should have had the effect of driving up interest rates (and lowering the bond price) due to the higher bond risk. This did not happen.

Instead, the European markets have faced increasing uncertainty as they deal with the very real possibility of a Greek default. Germany and France are the best hope at saving Europe and stabilizing the Greek fiscal mess, yet they are both facing political pressures at home to avoid helping other members of the European Union. These issues have reaffirmed America's status as a reserve currency of choice. The investor flight to US safety is driving down the yields of US Treasuries to record lows.

Operation Twist

The Fed holds over $1 trillion in bonds from Quantitative Easing. They have decided that instead of increasing this amount, they will sell shorter-term Treasurys (downward bond price pressure and higher short-term yields) and buy longer-term Treasurys (lower long-term yields) to flatten the yield curve. The idea is that more loans such as mortgages are tied to the 10 year Treasury and lower interest rates on this part of the yield curve will be beneficial for borrowers. In turn, this should help stimulate the economy.

While this idea has some merit, studies suggest the Fed action can only lower interest rates about 0.15%. Additionally, we believe that bank underwriting issues are blunting the effect of lower interest rates. Mortgage loans, consumer loans and small business credit lines are now very tough to get. People want to borrow at low interest rates, but gun-shy banks do not want to lend. According to Richard Fisher, Dallas Fed President and dissenter, "this (Operation Twist) will represent nothing but pushing on a string."



Although the broad bond market returned 4.74% in the Third Quarter, it was a tale of two markets. US Treasurys did very well due to investor flight to safety, but riskier high yield corporate bonds fell considerably. We sold longer term government bonds and the large position of high yield corporate bonds. Our timing was good. Cash was raised before these bonds declined. We still own short-term high quality corporate bonds and short-term US Inflation Indexed Treasurys.

Your Portfolio

The stock market was unusually volatile in the Third Quarter. We were proactive regarding your portfolio positioning. In fact, we made more trades this past quarter than any other quarter since we have been in business. It was not our intent to incur so much trading activity, but it is the way things worked out.

In July, we went defensive by raising cash in the range of 10%-15% (all stock portfolios) and 20%-25% (mixed allocation portfolios). We pared back various stock positions and sold both the high yield corporate bond fund and longer term TIPS (Treasury Inflation Protected Securities) to raise the cash.

Stocks sold were Medco, Allstate, Borg Warner, Credit Suisse, Chico's and First Solar. Later in the quarter, we deployed excess cash. Stocks purchased were Proctor & Gamble, St. Judes, Berkshire Hathaway, General Mills, and Praxair. These adjustments were consistent with our migration toward US blue chip companies. We added short-term high quality corporate bonds to our mixed allocation portfolios.

All in all, the numerous portfolio adjustments were beneficial. Cash was a good place to be when the market went down. On a relative basis, US blue chip stocks performed best over the quarter.

Over the next few months, we anticipate further adjustments to both the stock and bond components of your portfolio as we anticipate rising investor confidence and a market upturn. Stay tuned for updates.

We will continue to closely monitor the market and adjust your portfolio as needed. Please feel free to contact us anytime to discuss questions or comments you may have. We will keep you informed of portfolio progress.

Respectfully submitted,

TRIVANT

CUSTOM PORTFOLIO GROUP, LLC

John Barber, CFA
Chief Investment Officer

Dan Laimon, MBA
Managing Member

Michael C. Harris, CFA
Vice President