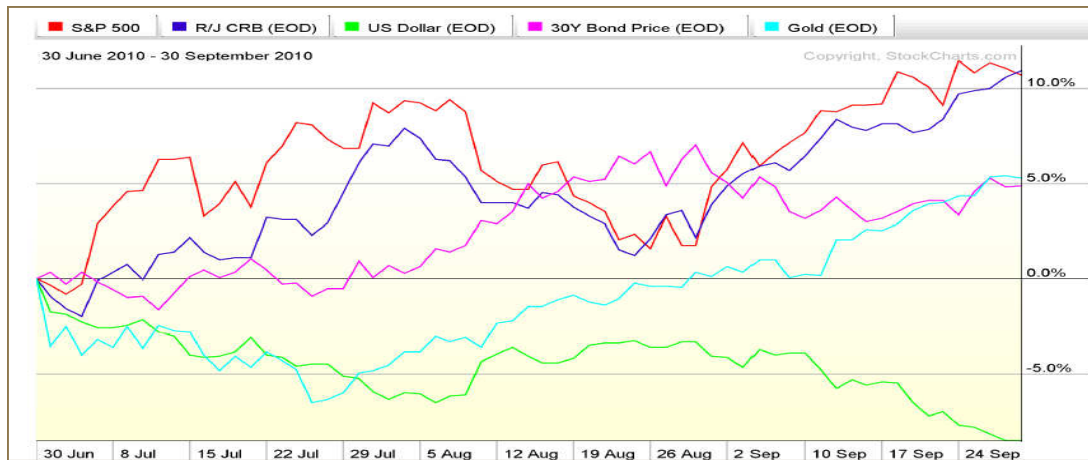


## Is This Market A Bull? Or, is there a canary in the coalmine?

No jobs, no credit, foreign currency crisis, political instability. Forget it. That is what the stock market did over the last quarter. This is starting to remind us of the end of 2004 when stocks rallied nearly 10% in December. We won't get too carried away in case that canary stops singing, but we do not want to miss out on a Santa Claus rally either.



Composite / Index	Q2 %	YTD %	5 Years % Annualized
Regan Macro Absolute Return*	+ 2.67	+ 2.82	+ 6.71
HFRX Absolute Return Index	+ 1.23	- 0.79	- 0.98
HFRX Macro Index	- 0.56	- 2.89	+ 1.12
Dow Jones Industrial Average	+ 10.37	+ 3.45	+ 0.41
S&P 500	+ 10.72	+ 2.34	- 1.47
NASDAQ	+ 12.20	+ 4.38	+ 1.94
Balanced Composite (60% Stocks & 40% Bonds)	+ 8.12	+ 6.67	+ 3.50
Gold	+ 5.06	+ 20.18	+ 22.53
Dow Jones/UBS Commodity Index	+ 13.01	+ 6.27	+ 8.84
Vanguard Prime Money Market	+ .03	+ 0.07	+ 2.85
Oil	+ 5.74	+ 0.77	+ 3.84

Performance numbers for the Regan Macro Absolute Return composite are back tested with best efforts internally by Regan Investments and not audited by outside parties. This newsletter contains general information that is not suitable to everyone. The information contained herein should not be construed as personal investment advice. Past performance is no guarantee of future results. There is no guarantee that the views expressed in this newsletter will come to pass. Investing in the stock market as well as all financial markets involves gains and losses and may not be suitable for all investors. Information presented herein is subject to change without notice and should not be considered as a solicitation to buy or sell any security. Regan Investments Inc. is a registered investment advisor with its principal place of business in the state of Minnesota. All other performance numbers for listed indices, managers, and stocks are used for comparative purposes only in this report are not verified by Regan Investments. They are taken from public sources and Regan Investments does not claim any responsibility for their accuracy. For a complete list of our sources, or a detailed explanation on how we calculate our internal numbers please contact Regan Investments directly.

## MARKETS

**W**e do not see much change in the economy since last quarter. Jobs are scarce, credit is tight, and debt is still at unsustainable levels. What seems to have changed is that the average American has followed through on threats to “Throw the bums out” in Washington. This is not as much a right or left statement, as incumbents from both sides appear to be getting kicked to the curb for a fresh start. The natives are indeed restless!

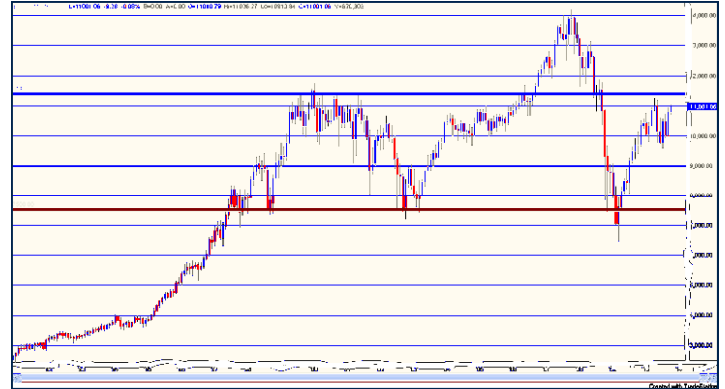
### BULLISH ON STOCKS?

In late 2004, we were bearish on the stock market. Most of our accounts were up about 3% while the S&P 500 was down 5%. Our accounts were hedged for market downside which we thought could be an additional 5-10%. At the time, we were geniuses. Then, George W. Bush won reelection and the stock market ended the year up over 10%. Our accounts remained up 3% and just like that...we were fools.

There is strong potential for a rally in the stock market as the elections near. The big question is whether it has already occurred. Technically speaking, there is significant resistance at about 11400 on the Dow (*Chart One-blue line*). The closer we get, the more likely we would be to hedge our stock positions. On the flipside, if the Dow were to break this level, we may look to remove some of our hedges in case the market continues to advance.

***“We'd love to be bulls...but that would be helped if stocks were priced appropriately and if there was not a large anvil suspended on a fraying string overhead.”***

***John Hussman***



**Chart One**

The Federal Reserve and its counterparts around the globe are doing everything they can to devalue their currencies in order to support asset prices and add inflation to the system. We think this will ultimately be a losing game. For the moment however, the re-flation trade appears to be on again. This concentrated effort by all central banks, while bullish for most assets, would most likely be short lived.

### BEARISH ON STOCKS?

Dismal trading volume on the exchanges sets up the potential for stocks to move violently in either direction as high frequency trading firms cause significant market distortions. It is easy to push a market up on low volume, but, if the market declines, there will be very few buyers, and a crash is possible. Any hint of bad news or unsuspected election results could have traders heading for the exits.

The first level of support on the long term chart is about 9950 on the Dow, while the longer term level of support is about 7450 (*Chart One - red line*). The large head and shoulders pattern would suggest a potential test of the stock market lows sometime between 2012 and 2013.

We think the stock market could easily advance another 5% during the last quarter of 2010. If the market turns bearish, we believe the downside is about 10%. The potential for a 30% selloff exists, but we do not see that as likely...yet.

## RECESSIONARY TALES

If you think this is an ordinary recession, please see *Chart Two* below. Luckily, the National Bureau of Economic Research has declared that this recession officially ended in June 2010. Maybe one of the many GDP revisions down the road will show that the recession did not actually end in June. Or, it ended and another one started. But does it truly matter?

In a 70% consumer driven economy that still has double digit unemployment, historic debt imbalances, and a ratio of 1/381 homes that have received foreclosure notices, calling an end to the recession is folly. The real question is, *How will it affect these unfortunate people's ability to spend money?*

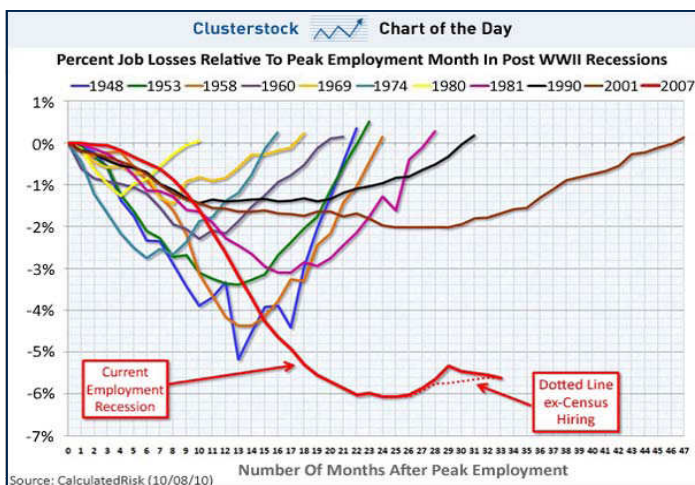


Chart Two

It is easy for us to take aim at the political process because we are not part of that process. We have listed a few ideas that we think might help address certain issues within our economy. While some are easier done than others, at the very least, they seem fair.

### 1. Tax Change

Now is the time to overhaul the tax system. A national sales tax instead of double taxation of dividends and income seems logical as it taxes consumption rather than investment. In addition, a flat tax seems like an idea whose time has come.

### 2. Suspension of Gifting Limits

95-year old David Rockefeller has a net worth over \$3 Billion and is only able to gift his children, grandchildren, and great grandchildren, \$13K per year. In an economy looking for velocity on money, it makes sense to get some of this dead money into the hands of younger generations to spur economic activity.

### 3. Go Grassroots on Social Security

Let people remove themselves and loved ones from the social security pool by making contributions into an IRA. Contributions would be based on the present value of the person's future benefits and could be made in one lump sum or periodic payments. This should not only remove future claims on social security, but it should also remove current social security taxes on the beneficiary and may allow for less in estate taxes for the contributor. Best of all, beneficiaries could potentially earn a return on their money.

### 4. IRA/401K Financed Mortgage Relief

Saving for a rainy day is a good thing; but for many, it's already a downpour. Allowing people to place retirement assets in trust for the purpose of protecting their residence or buying a home might help. Funds used as collateral could be used to buy government bonds. This creates additional demand in case China stops buying our bonds, creates more buyers in the housing market, and puts the responsibility back on the homeowner rather than the taxpayer.

In addition, abolishing minimum required IRA distributions would be a nice gesture too.

### 5. Repatriation of Offshore Funds

Tying significant tax benefits to the investment of capital for corporations that repatriate funds could directly target the unemployed. While it is not going to solve our job woes, creative maneuvering of capital can go a long way.

**ENDOWMENT INVESTING**

We use the Harvard Endowment fund as a proxy for “Smart Money.” The Harvard fund has outperformed the average investor by a wide margin over just about any time period.

As you can see from *Table One* below, over the last five years, the Harvard endowment fund has done very well. The Regan Macro Absolute Return composite (gross return) has done even better with less than half of the volatility (Stdev). The key in our performance, as well as Harvard, has been the ability to avoid down markets.

Harvard’s endowment is very different than the average mutual fund or money manager in that they invest in sweetheart private equity deals and the best hedge fund managers. In addition, they have a consistent inflow of donations, perpetual time horizon, and favorable expense leverage. While we will never get the elite opportunities that await Harvard, we are confident in our abilities to keep pace.

According to Harvard’s most recent annual report, the single largest allocation is in absolute return with a 16% weighting. Harvard’s stock weighting is comprised of Domestic equities (11%), Foreign Equities (11%), and Emerging Equities (11%). Fixed income is weighted at 13% of the portfolio.

	1 Yr Return	3 Yr Return	5 Yr Return	Stdev (Annual)	Growth of \$1M
S&P 500	+12.1%	-31.5%	-14.1%	19.5	\$858,812
Balanced 60/40 Stocks/Bonds	+10.8%	-14.6%	-2.8%	12.0	\$972,515
Harvard	+11.0%	-12.4%	+25.8%	19.6	\$1,257,949
<b>REGAN</b>	<b>+9.48%</b>	<b>+10.11%</b>	<b>+47.95%</b>	<b>7.9</b>	<b>\$1,392,246</b>

**Table One**

**IS JAPAN OUR FUTURE?**

As Jim Rogers noted on CNBC this week, The Japanese stock market is still 75% below where it was twenty years ago (*Chart Three*). This is a sobering reminder that anything is possible when it comes to the financial markets.

Experts are trying to figure out how we can learn from Japan’s last twenty years of deflationary struggles in order to avoid a similar fate. Richard Koo’s book, “Balance Sheet Recession” is a good primer for those interested.



**Chart Three**

When an economy is strapped with debt, a downturn is almost certain. In most cases, the values of assets (houses, stocks, etc.) will deflate, but the high debt levels associated with those assets remain. This will lead to default or what Koo calls a “Balance Sheet Recession.” As Koo notes,

*Individuals and businesses repay debt by drawing down deposits, but if the entire private sector behaves this way, the money supply will decline. The Great Depression was the classic example of a balance sheet recession. The US money supply shrank by 30% as businesses and households moved collectively to pay down debt.*

This would explain our current situation. However, Koo’s answer is that the government needs to step in and take on the spending role of the individual. A common Keynesian principle, government deficit spending opens the door for continued bubbles. It also avoids the logical solution to a world of amplified debt...a complete washout that allows for order and structure to be restored to the system.

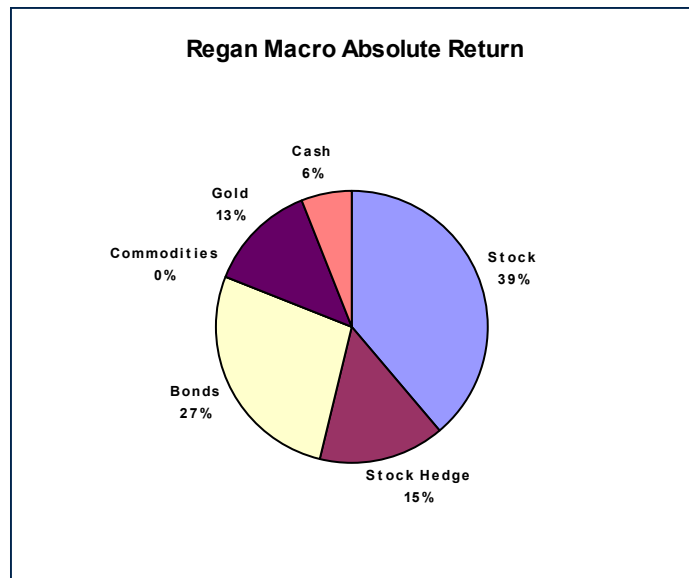
# PORTFOLIO

The Macro Absolute Return Portfolio is still defensive. Our net stock position is roughly 24% (Stock - Stock Hedge). In addition, our stocks are more conservative in nature. We still have various names that provide us growth opportunity (Apple, Celgene, etc.) but the majority of our holdings are blue chip companies that sell at a value (Microsoft, Medtronic) or provide higher dividend income (Xcel Energy, Waste Management ).

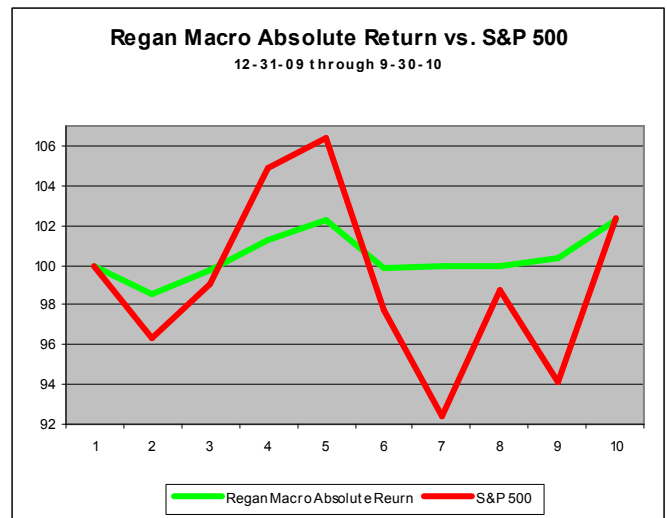
We still hold a decent position in gold (6.5%) and gold mining stocks (6.5%) but our overall weighting in other more industrial commodities is non existent. We do not like the risk/reward of holding commodity related investments (apart from gold) in a deflationary environment. We tend to like the depressed commodities as a long term investment but inflationary concerns would change our view drastically.

Our major moves over the quarter included increasing our positions in Apple, Medtronic, and Xcel Energy. We also benefitted from Southwest Airlines purchasing Airtran which resulted in a *one day gain of over 60%*. Our top ten stocks in the Macro Absolute Return Composite are listed below:

Top Ten Stocks	Weighting
Apple	4.5%
Celgene	3.5%
Microsoft	3.5%
McDonalds	3.5%
Xcel Energy	3.0%
Medtronic	3.0%
General Mills	2.5%
Walmart	2.5%
Waste Management	2.0%



Our Macro Absolute Return portfolio equaled the S&P in performance, but with much less volatility. We continue to view this market as dangerous and we will invest accordingly.



We have a healthy position in bonds (27%) that were purchased at tremendous yields. We will look to replace some of these with similar bonds, albeit, at less favorable yields as they mature. We still believe that select short term corporate bonds currently offer an attractive alternative to longer dated bonds and offer much more yield than cash.

*Thank you again for your faith and support!*  
**Robert, Robert Jr, Erle, and Cynthia**

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*Please feel free to share this newsletter with anyone interested in learning more about Regan Investments or needing financial expertise.*

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