



SPINNAKER

SPINNAKER TRUST QUARTERLY NEWSLETTER

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Forget Your Troubles Come on Get Happy...

It certainly seems as though stock markets around the globe in 2009 did just that - forgot their troubles, at least for a while. After the lows of early March, markets have been on a steady ride up. Few would have predicted a year ago that the S&P 500 would end the year up 26.5% with the technology (59%) and basic materials (45%) sectors leading the way. Mid- and small-cap indices had strong years and international markets, especially emerging markets, also had significant gains. Some emerging markets, particularly Brazil and India, had triple digit gains!

While equity markets went up, interest rates remained at historic lows. Three-month Treasuries are paying about 0.03%, 6-month issues now pay 0.17% and 12-month T-bonds are yielding 0.35%, all of which are well below the inflation rate. Every rise in the CPI* means the value of money in these low yielding bonds is going down--which is something we aren't reading much about in the headlines. Right in line, money market fund yields are at record lows, many yielding near zero percent.

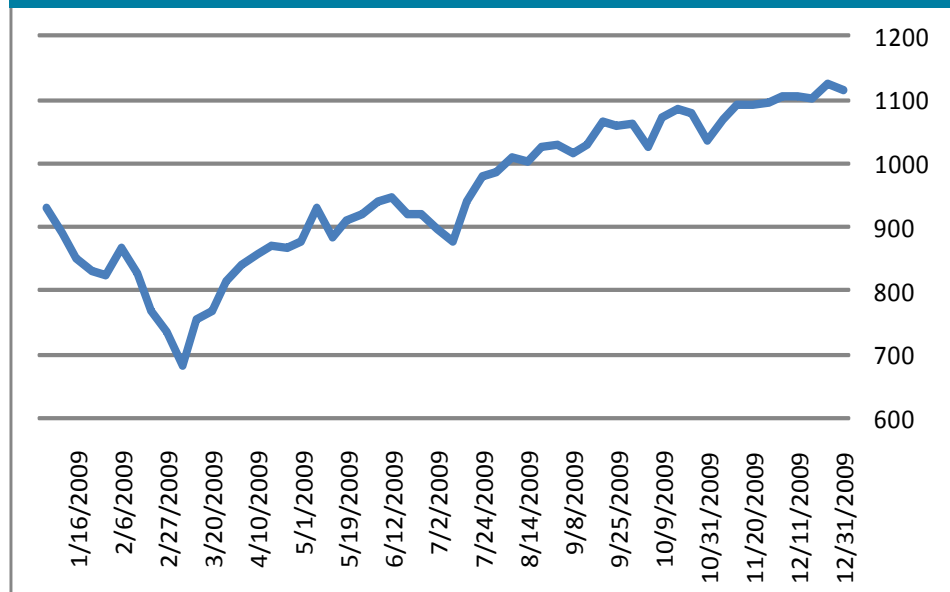
When will the Federal Reserve Bank begin to increase the rates it charges banks for money?

Most economists agree it will be sometime in the second half of 2010. If the Fed acts in the first half of the year it would surprise many. That would likely create a hiccup for the stock market initially because low interest rates are part of the reason the market has done so well. Large corporations can borrow money at very favorable rates helping businesses grow cheaply. But when the Fed increases rates, it means that it sees a stronger economy and rising earnings and that it believes the economy is improving.

No one knows when the Fed will act but, if it is sooner rather than later, those actions will be taken only because the economy is strong and the market will bounce back.

"Forget your troubles come on get happy (Get Happy)" was recorded originally in 1930 – and made famous by Judy Garland in the 1950s. If you continue on in those lyrics, you are getting 'ready for judgment day.' While we do not foresee a 'judgment day' in 2010, the markets will be forced to face the reality of high unemployment, continuing home foreclosures in many parts of the country and mounting government debt.

BULL: Since the low close on March 9, 2009, the S&P 500 is up 67.8%



Source: Bloomberg

Expanding Economy with Increased Savings

In November, Federal Reserve officials projected that the U.S. economy would expand at a slow rate in 2010. Not surprisingly, not everyone agrees with that. In fact, many see stronger growth. Whether slowly or not-so-slowly, most investors are looking for some economic expansion in the U.S. and in other developed nations. Government stimulus programs worldwide have helped to calm fears and boost confidence and, in some countries, expansion is already underway. The true test will come in 2010 as these stimulus programs come to an end and economies must stand on their own.

As we noted in the third quarter newsletter, the holiday shopping season might tell us a little bit about what to expect in 2010. It turns out that there was a Christmas and consumers spent about 3.6% more than in 2008. So folks are out there spending, but not much, and nowhere near 2007 levels. Maybe that is not a bad thing. The U.S. savings rate is higher than it has been all decade. The chart below shows the last 50 years

of U.S. savings rates. The average over that time period has been almost exactly 7%. Over the past 10 years the average has been about 2.8% and in 2009 it approached 5%. We believe it is a good and healthy trend that hopefully will hold, though Americans tend to have short memories and may go back to old spending habits.

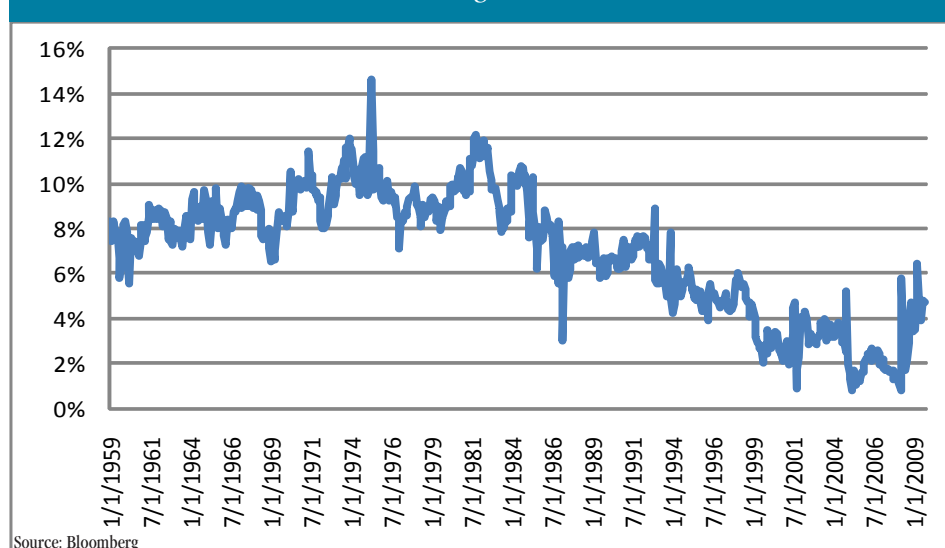
Prediction Addiction

We are constantly asked what we think will happen in the markets, next month, next quarter and next year. And the bottom line in this business is we really do not know what will happen – in the short run. It seems as human beings, believing that we know what is going to happen next, even if it is unknowable, brings us comfort. Like it or not, we venture forth every day, control what we can control (allocation, investment costs, gains and losses), and strive to make more money in the upturns than we lose in the downturns. While we cannot predict the short-term market, we do believe we know what will happen over the course of many years. A well diversified portfolio will grow over time and will

do better, and have less volatility, than a portfolio with one or two asset classes. Spinnaker Trust builds portfolios with exposure to many asset classes including domestic stocks (large, mid and small-cap), international stocks, emerging markets, fixed income, real estate and cash.

We also carefully look at the various sectors of the economy and allocate portfolios according to our thoughts on what sectors may prosper in the current conditions. In 2009 we were over-weight (compared to the S&P 500) in the basic materials and technology sectors, both of which had very good years. We are heading into 2010 with over-weightings in basic materials (we still believe emerging markets will need these raw materials to grow), health care and energy. The health care sector has been under pressure from all the uncertainty in the political arena. This ought to be lifted as the bill is finalized in early 2010. The energy sector underperformed the market in 2009 as economies slowed down, but we believe the basic supply and demand issues remain and, as economies begin to grow again, energy stocks will again do well. We remain significantly under-weight in the financial sector as we still see some difficulty for banks going forward.

U.S. Personal Savings Rate (50 Years)



Source: Bloomberg

*CPI: Consumer Price Index is a measure estimating the average price of consumer goods and services purchased by households. The index does NOT include food and energy.

Selected Post-Recession Recoveries

Troughs	Crash (Relative to 12 months before trough)	9 months after trough	3 months after first 9 months	6 months after first 9 months	1 year after first 9 months	2 years after first 9 months
Feb 2003	-25%	27%	8%	4%	9%	14%
July 1920	-27%	13%	-1%	4%	36%	47%
Oct 1907	-36%	37%	3%	9%	23%	2%
Oct 1857	-41%	42%	3%	10%	-1%	43%
Feb 2009	-43%	49%				
Sept 1974	-48%	49%	-13%	-8%	7%	5%
March 1938	-48%	58%	-2%	1%	13%	18%
Mean	-38%	38%	-2%	1%	13%	18%

Source: Credit Suisse

Crash, Recovery... then?

After equity market panics, the first part of a recovery typically records sharp gains such as we have seen the past nine months. After that, a new phase of recovery begins in which returns are typically much lower but still positive. Perhaps there is something natural to this, with the second year of recovery marking a return to normality. Or perhaps it is driven by

an inevitable normalization (realization) of financial conditions, including higher interest rates, that weigh on market performance and limit gains even if the economy continues to recover. In any case, the exhibit above, prepared by Credit Suisse, shows a clear pattern: a panic, then a sharp recovery, and then a milder period of slowing gains.

Tax Planning in Quicksand

It is difficult to believe, but 2009 came and went, and we still have no permanent federal estate tax reform. Since 2001, clients and practitioners have been forced to plan their estates under federal estate and gift tax rules that have resembled quicksand.

Most experts in this area never thought it would get this far. Surely, before the clock struck midnight on January 1, 2010, Congress would pass a permanent estate tax, and taxpayers and their advisors would have some certainty. But here we sit, with more uncertainty than ever before. Max Baucus, among others, has vowed

to reinstate the federal estate tax retroactively to January 1, 2010. The 35% gift tax rate potentially could be increased retroactively as well.

From 2001 to 2009, the estate tax exemption increased from \$675,000 to \$3.5 million per person. For those who die in 2010, there is currently no federal estate tax (meaning an unlimited exemption). This created a macabre situation at the end of 2009 where the terminally ill and their families were being forced to consider tax consequences while making medical decisions.

The tax rates have also shifted dramatically since 2001. The top estate and gift tax rate in

2001 was 55%, which dropped to 45% in 2009. For 2010, the gift tax rate is set to mirror the top federal income tax rate, or 35%. This reprieve is only temporary, however, as the estate tax is scheduled to reappear in 2011 with a \$1 million exemption and the old 55% rate will be reinstated for both the estate and gift tax.

Getting less press these days, but of equal importance, are the carry-over basis provisions that went into effect in 2010. While currently the estates of those who die in 2010 will not owe a federal estate tax, the beneficiaries of such estates will take assets with a carry-over basis, subject to limited exemption amounts. The federal government tried instituting carry-over basis requirements in the 1970s, and it was such a disaster that they were forced to repeal it.

We had hoped that this quarter's column would be devoted to an overview of the new, permanent federal estate tax. Instead, we will continue to monitor the situation throughout the year and update you accordingly. If you have questions about the estate or gift tax, we encourage you to contact your estate planning lawyer, accountant or us at any time.

We want to wish all our clients and friends a Happy New Year. We look forward to serving you in 2010.

MARKET DATA: 2009, 2008, 2007

<i>Index</i>		<i>12/31/09</i>	<i>2008</i>	<i>2007</i>
S&P 500	<i>U.S. Large-Capitalization Stocks</i>	26.5%	-37.0%	5.5%
S&P 400	<i>U.S. Mid-Cap Stocks</i>	37.4%	-36.2%	8.0%
S&P 600	<i>U.S. Small-Cap Stocks</i>	25.6%	-31.1%	-0.3%
Russell 1000	<i>U.S. Large- and Mid-Cap</i>	28.5%	-37.6%	5.8%
Russell 1000 Growth	<i>Growth Stocks broken out</i>	37.2%	-38.4%	11.8%
Russell 1000 Value	<i>Value Stocks broken out</i>	19.7%	-36.8%	-0.2%
MSCI EAFE Index	<i>Established International Markets</i>	32.2%	-45.1%	8.6%
MSCI Emerging Markets	<i>Developing International Markets</i>	78.5%	-54.4%	36.9%
		<i>12/31/09</i>	<i>12/31/08</i>	<i>12/31/07</i>
90 day T-Bill	<i>Short-Term Interest Rate</i>	0.08%	0.08%	3.25%
10 Year US Treasury Rate	<i>Longer-Term Interest Rate</i>	3.82%	2.21%	3.91%
VIX Index	<i>Risk Measurement</i>	22	40	23
Corporate Bond Spread	<i>Risk Measurement</i>	122 bps	570 bps	197 bps
TIPS Spread	<i>Inflation expectations</i>	241 bps	17 bps	233 bps

Three little letters... IRS

The tax system is constantly changing. What we do not hear about as frequently are the changes the IRS is making to try to improve services and cut costs. (It is true, the IRS is trying.) Some of the changes the IRS makes directly affect us as taxpayers.

If you prepare your own tax returns, please note that the IRS is consolidating its processing centers and the address to which you must send

your paper tax return may have changed. Please look for that in April. Also, depending upon where you live, the IRS changed some filing addresses for payers of quarterly estimated tax.

If you use a tax return preparer to prepare your income tax returns, he or she will provide you with correct addresses for filing your tax return and mailing estimated tax payments. Also, you will find additional information about these and other IRS changes at www.irs.gov.

Spinnaker Trust works closely with tax return preparers to serve our common clients. If you would like Spinnaker to pay your tax balance due, file your paper income tax return, and pay quarterly estimates for you from your Spinnaker Trust account, please let us know. We will ask you or your tax preparer to provide us with your tax return(s) and vouchers. You will see all payments we make on your behalf on your periodic statement and online.

