CAPITAL MANAGEMENT GROUP, INC.

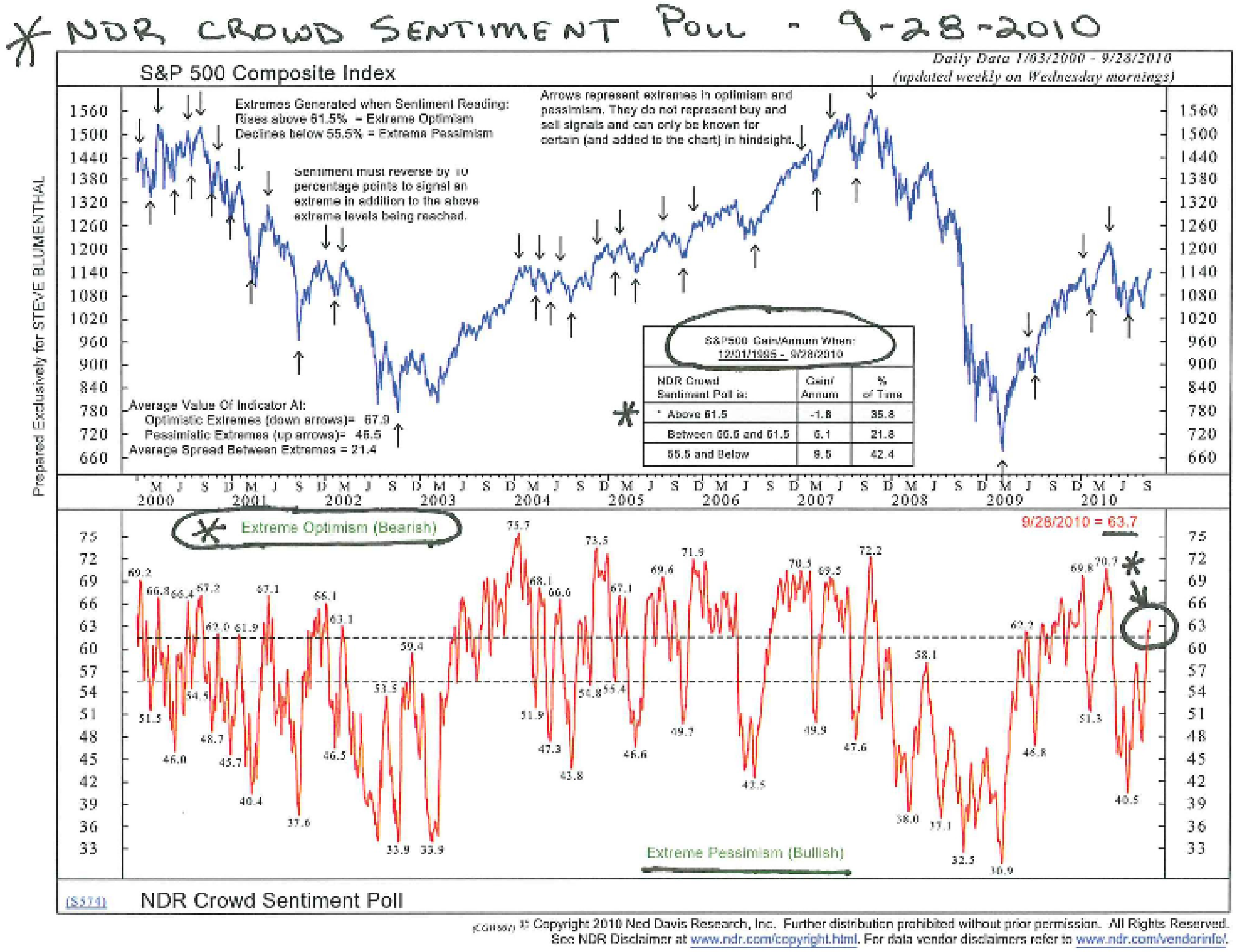
Alternative Investment Strategies

October 7, 2010 Market Update:
Investor Sentiment Update - Extreme Optimistic (Bearish) Zone

Below I take a quick look at the most recent Investor Sentiment data and share my response to a recent investor email.

First a look at the most recent NDR Crowd Sentiment Poll (my favorite sentiment chart). Note that it is again back in the Extreme Optimistic (Bearish) Zone. Given the current Long-Term Secular Bear market environment, if you can do so, I recommend putting some sort of portfolio protection back in place on the long equity portion of your investment portfolio. I'm expecting a hard sell-off that I believe will set up an attractive buying opportunity. If you have 33% in Equities, 33% in Fixed Income and 34% in Alternatives - Absolute Returns (active management), I'd look to protect the Equity bucket at this time (call this "fat tail" downside risk management). Raise some cash, look at inverse ETF's, buy put options if suitable for you. No need to protect the Active bucket as those managers have the ability to trade the markets both up and down and/or move to cash. The S&P 500 Index is at 1150 today, September 30, 2010. The seasonally troubling October month is ahead. I advise caution on long-equity exposure. I believe a buying opportunity will soon present itself at lower levels tied to an Extreme Pessimism (Bullish) reading. I'll send the next sentiment update out when we get back into that "buy" zone" tied to Extreme Pessimism.

Sentiment Chart:



Investor Behavior matters:

I believe investor behavior is a key to long-term investment success. We can read all of the books that teach us about the markets and follow the research from the brightest minds (gurus) in the business; yet if we can't honestly understand our own emotional behavior patterns, I believe we are destined to underachieve. I recently received an email from a former client. It said, "Dear Steve, I like your positive reports; but when I was invested with your company, I lost 10% of my funds." Following is my response. I touch on Investor Psychology, Sir John Templeton and the DALBAR study, which shows just how much the average investor underperforms.

Dear Investor,

Appreciate your email.

I've been in this game a long time. There were many times over a 12 to 18 month period that we have been in a draw down yet our returns over time have been pretty good. I've been called both hero and goat – sometimes on the same day (depending on which client and the date that client started with us). I'm neither. If your time frame is short-term, then you should be invested in CD's or Tax Frees (but don't extend those maturities too far out due to risk of rising rates 2-5 years from now). The Scotia S&P Plus allocation was the driver for your underperformance during the period you were with us. The strategy has never had a losing year, there were several other periods when he was down over 12 months, did very well in 2008 when the world crashed, and he averaged over 25% net of fees per year since 2004. I believe he has a solid process with probable edge. I wouldn't sell out of exposure to that strategy, I'd add more or rebalance to have a targeted exposure. Investing is a tough thing to do. I believe it is more about human psychology. Most investors buy and sell at the wrong time. DALBAR did a study that reflects this incorrect behavior clearly. Over the last 20 years, the S&P 500 Index gained 8.35% yet the average equity investor gained 1.87%. Interestingly, the Barclay's Bond Index gained 7.43% yet the average bond investor gained just 0.77% (data from Investment Company Institute, Morningstar and DALBAR, Jan. 1989 to 2009). The reason is that investors are always buying and selling at the wrong time. I can send you the research if you'd like to see it. In the past, I have written about Sir John Templeton: "Buy when everyone else is selling and sell when everyone else is buying". It is not an easy thing to do. Most people simply can't do this and it is why most people fail to make money investing (re: DALBAR study). I wish we always produced positive returns but that isn't real life. I advise clients to give a strategy time to work through a full cycle (call it three plus years). Of course, no investments' past performance can guarantee future returns. Nor can ours. I know that is hard to hear because all of Wall Street says just hang in there. Most of Wall Street sells you the next great thing just after that great thing had a great move (they know investor psychology). It is hard to invest just after an underperforming period. Ultimately, it is a question of portfolio balance and the shape of your portfolio allocation depends on things that are important to you (your risk tolerance, needs, investment time horizon, etc.). It has also been my experience that most people do not have a game plan. I'd encourage you to set a plan in place and be prepared to execute that game plan (that includes buying when you are most scared and selling when you see that everyone else is excessively over optimistic). It means following your investment game plan. An allocation to Actively Managed Strategies (like CMG) is just a part of an overall portfolio structure. Every strategy will hit a rough spot. It is how you handle that rough spot that I believe defines your long-term success. I'm really sorry we lost your business, I truly wish you the very best, and of course we would love to have you back as one of our valued clients.

With kind regards,
Steve

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