



## Baltimore Capital Management

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July 8, 2009

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Dear «Dear»

For the first half of 2009 «M\_1\_in\_letter» has «gain\_loss» «PRF1» vs. the S&P 500 gain of 3% and the Dow Jones decline of 2%.

The second quarter of this year has been one of the best in many years. This is, of course, after a terrible 2008 and equally distressing first quarter of 2009. It seems clear now that the markets reached a bottom in mid-March. Although some investors had been expecting the markets to retest those lows, the magnitude of the upturn makes it look more like a new bull market. Given some recent signs that the economy is improving, it is entirely logical for the stock markets to anticipate that turn and begin moving up prior to the recovery. These historic patterns are very common when reviewed over long periods of economic history.

As we mentioned in a recent email (please let us know if you are not getting our emails), we actually expected a correction of sorts before the markets continue their upward movement. We now seem to be experiencing a general a correction in the overall market, and a larger one in specific sectors. We did marginally increase our cash levels in June. This in no way means we are pessimistic or having difficulty finding good investment ideas. Frankly, I am surprised by those who believe there are few opportunities at present, or that the stock market is fully valued. Considering that the S&P 500 is basically flat for the year and overall for the last ten years, it is absurd to contend that the markets are currently overvalued. If anything, I have seldom seen as many equities with attractive dividend yields in my career.

We have come a long way since last November, when people feared that banks were all failing and their savings were at risk. However, while the US government has done a good job stabilizing the financial markets, I have some longer-term concerns about its economic recovery plans and the deficit this is creating. At some point, we will have higher inflation and a weaker dollar, not to mention higher taxes that are already evident. All the above leads us to continue investing in foreign markets and gold, as we have been.

In the past few weeks, we have become particularly interested in natural gas and its historic price relationship with oil. The price of gas historically has been 1/9 the price of oil. It is now 1/20 the price of oil. In other words, natural gas is historically cheap vs. oil and at historic absolute lows. It is our expectation that natural gas, now at \$3.50 per one million cubic feet, will increase to \$7 within a year or less. While we have had exposure to this sector, it could be of even further interest.

During the past few months, some clients have asked about investing in bonds. Normally this would be a lousy time to invest in bonds because interest rates are near zero. One year Certificates of Deposit yield less than 1%, and five year CDs yield 2%. On a pre or after-tax basis, this is very unattractive. Note that US government bonds are similarly unattractive. Nevertheless, because of the credit meltdown, corporate and municipal bonds do have decent yields. We see similar patterns with preferred shares and even many common shares where the dividends seem secure. Good opportunities are out there - please see our newsletter for further thought on why just holding cash or cash-like investments may not be the best thing for your financial health.

In conclusion, we are relatively enthusiastic about the medium term and expect the second half of this year to provide positive returns. While volatility has diminished, it is unrealistic to assume that markets will not continue to have ups and downs. What is most important is that we seem to have the market lows behind us and that the economy is showing some signs of life.

Sincerely,

Alec Graham

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*Upon written request, we will deliver a copy of our Part II of the form ADV and a balance sheet.*