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ABOUT LEGACY

Legacy Asset Management, Inc. is an independent Registered Investment Advisory firm, committed to providing the best solutions for our clients' success.

We offer professional money management and sound objective advice throughout a full range of investment and Qualified Retirement Plan consulting services for the institutional and high net worth client.

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ROAM

LOOKING FOR CATALYSTS

The U.S. economy continues to be stuck in low gear. The inventory rebuild cycle has just about run its course from depressed levels in 2008 and 2009. The effect of the stimulus is wearing off and unemployment remains stubbornly high. In September, consumer confidence fell to its lowest level since January due to less favorable business conditions and a declining outlook. Furthermore, state and local governments find themselves facing massive budget deficits and a low tax base from which to draw from. Clearly, there are major obstacles that must be negotiated before the economy can get back on its feet. In the meantime, where should investors turn for return opportunities?

Last quarter, I used Don Henly's hit "Dirty Laundry" as an analogy to point out the inadequacy of CNBC's hosts, probing their guests. This quarter, the lyrics from the song "Roam" by the rock band The B-52s, comes to mind as a descriptive solution for seeking investment opportunities.

"Fly the great big sky, See the great big sea
Kick through continents, Busting boundaries..."

From "Roam" The B-52s

MONEY FLOWS EFFICIENTLY

In an efficient global economy, capital will flow to its highest and best use. In other words, investors will deploy money to those geographic areas that have the ability to generate greater returns for a certain level of risk. With the world leading economy in a state of flux, investors are turning toward international markets and unfamiliar regions for earnings growth and price appreciation.

Last quarter, I asked the rhetorical question, "where will growth come from?" It's becoming apparent that certain international regions and countries are further along the recovery path than the U.S. and might provide a more appealing investment environment. For example, at the end of September, the IMF (International Monetary Fund) indicated that an economic recovery is underway in the UK as unemployment has stabilized, the financial sector's health has improved and their multi-year fiscal deficit reduction plan should ensure fiscal health. In Germany, (Europe's largest economy) consumer confidence is increasing as improvements in employment materialize. The Asian Development Bank raised its forecast for the region's economic growth for 2010 and 2011. Southeast Asia is experiencing a bump-up in economic activity as the IMF is projecting the average GDP growth of Taiwan, Indonesia, Vietnam, Singapore, Thailand and Malaysia to be about 5.5%.

When economic activity begins to improve in developed countries like England and Germany, demand for basic necessities returns before spending on discretionary or luxury goods. Once the economy begins to stabilize, consumers usually feel more confident about spending on big ticket items. Emerging markets, like the countries

of Southeast Asia, benefit from the expectation of global growth as their manufacturing base expands. As production ramps up, demand jumps rapidly for raw material inputs, commodities and basic consumer products. This escalation in demand helps stimulate revenue growth for multinational companies selling products throughout the world.

U.S. investors can gain exposure and capitalize on international growth by investing in U.S. multinational companies that garner a large portion of their revenue stream from foreign markets. Although Legacy manages a “large cap” equity portfolio of stocks domiciled in the U.S., the companies themselves conduct a significant portion of business overseas. Currently, 90% of client equity portfolio holdings generate some portion of their sales from international markets. Furthermore, 45% of the stocks in the portfolio generate more than half of their total net revenues from abroad. Chip giant Intel is a perfect example of an equity holding that is levered to overseas growth. The company generates 30% of its revenue from Taiwan, 17% from China, 15% from Europe, 8%, Asia Pacific and 5% from Other Americas. Having exposure to some of the highest growing countries of the globe helps insulate the

company from total reliance on the prospects of U.S. economic growth.

Multinational companies carry foreign exchange risk. The weak U.S. economy, generous monetary policy and uncertain political environment have caused the U.S. dollar to weaken relative to other competing currencies. A weak dollar helps U.S. companies sell products abroad. As the dollar falls, our exports become cheaper as it costs our foreign trading partners fewer dollars to purchase U.S. exports. In a price sensitive environment, cheaper products have a higher sell through enabling U.S. multinational’s to acquire global market share and report greater than expected revenue growth.

While owning a portfolio of multinational companies does not eliminate the need to have exposure to international stocks or mutual funds, it does however, provide diversification to an otherwise all domestic portfolio with a high correlation to the slow or stagnating U.S. economy. As a Large Cap U.S. equity manager, it is incumbent upon me to look out on the investment landscape to find assets that will not only provide value overtime but also, buffer investors from correlation risk.

3RD QUARTER REVIEW

What a difference a quarter makes! All of the major indices roared back into the black for the year and recorded double digit gains; the best third quarter results in over seven decades. In spite of the robust returns, these same markets continue to be stuck in a 13 month trading range within a band of 16%. Looking for positive returns continues to be challenging as stock market volatility whipsaws investors from one side of the range to the other.

The financial markets began to ascend right after the long 4th of July weekend and the really crummy employment report for the month of June. In spite of weak employment, the aggregate economic data for July was somewhat better than expected; led by durable goods orders, industrial production and a slight bump in capacity utilization. As a result, economists and investors became more optimistic that the economy would avoid slipping back into a recession. In August, weakness abroad gave way to a strengthening dollar which pressured the financial markets. The major indices gave back almost half of the gains reported in June. As the calendar flipped to September, the Federal Reserve added its rhetoric to the mix by suggesting that they would continue to support the economy through “quantitative easing”. The Fed engages in “quantitative easing” by expanding its balance sheet through purchasing mortgages, treasury securities and corporate bonds from banks

and other financial institutions in order to create excess bank reserves and increase the money supply. Overtime, this action can be seen as inflationary causing commodity and stock prices to rise.

During the 3rd quarter, the Dow Jones, S&P 500 and NASDAQ jumped 10.85%, 11.29% and 12.30%, respectively. All 10 sectors of the economy were up for the period. Unfortunately, the two smallest sectors registered the greatest pop as Telecom Services (3% of the composite) and Materials (4% of the index) jumped 19% and 17%, respectively. The two largest sectors, Information technology (18% of the index) and Financials (16% of the index) rose 12% and 4%, respectively. For the year, the two most cyclical sectors, Consumer Discretionary and Industrials performed best, with returns of 12% and 11%, respectively. On the flip side, the Energy and Healthcare sectors are still down for the year, with losses of approximately -2% each.

Growth stocks did much better than value stocks across all market caps in the quarter. However, the extent of the relative out performance was uneven and expanded with the size of the market-cap. According to the Russell indices, the largest stocks had the greatest variance in performance. Growth did better than value by a whopping 34%. In the Mid-Cap and

Small-Cap space, growth outpaced value by 21% and 15%, respectively. This deviation validates the sector performance as traditional growth sectors (consumer discretionary, information technology and telecommunications services) lead the market in the quarter. As hope builds that the economic environment will not deteriorate further, investors are more willing to purchase stocks with growth characteristics in an effort to capture above market rates of return.

INVESTMENT STRATEGY

With the equity markets near the top of the trading range, investors are wondering what their next move should be. Like a game of chess, where players have to plan their strategy several moves in advance, so too must investors when faced with the numerous factors that could alter the direction of the financial markets.

Our long-term outlook has not changed since last December. We are still looking for modest GDP growth over the next several quarters as the country works through a dormant job cycle, excessive housing inventory and uncertainty related to regulation, taxes and national debt. Since last December, we have been preaching that equities would fall and slowly recover (like the Nike Swoosh) as signs of economic improvement materialize. So far, we have been more or less right on as the markets have waffled within the current range.

Although equity prices rebounded last quarter on broad based belief that the economy would not fall back into a recession, we don't expect near-term economic news to drive market prices higher. We believe the catalyst for future stock price appreciation will come from Washington and "Main Street". The new congress and the President will have to address taxes, healthcare and the budget deficit. Should they agree to support business with tax cuts and incentives for capital investment, earnings growth and valuations should gain momentum.

In the short-term, we will be looking for opportunities to sell our cost basis in securities that have jumped in the recent market rally and reinvest resources into unloved or ignored dividend paying value stocks. Selling the cost basis of a security reduces exposure and volatility of a specific stock that may have recently enjoyed significant price appreciation. It can also facilitate the re-deployment of capital into other securities. For example, if an investor had bought 100 shares of IBM at \$75 per share, the total cost (excluding trading costs) would be \$7,500. If IBM increases in price to \$125, the value of the 100 share position would jump to \$12,500. Selling 60 shares would completely recuperate the original investment of \$7,500 and thus constitute "selling the cost basis. The remaining 40 shares or \$5,000 would represent the profit off the investment in IBM. If the stock continues to rise, the profit would grow. Conversely, if the price falls, the total profit on the investment would decline. Bottom line, as long as the stock doesn't go to \$0, the investor will always have a profit.

Catalysts for a rising stock market would include (1) attractive absolute and relative valuations in certain sectors, (2) the 10-year treasury bond with a yield under 2.5%, (3) better than expected earning season with positive commentary on future quarters and (4) over \$3.5T in money sitting on the sidelines in money market funds that could be allocated to equities.

We will be putting excess cash and proceeds from the sale of cost basis in sectors and stocks that characteristically have high dividends. With the 10-year Treasury yielding a paltry 2.4%, it is not hard to find good quality companies with a solid balance sheet and strong cash flow to support a dividend payout that exceeds the Treasury yield. While rates remain low, stocks provide a greater long-term rate of return over Treasury bonds. Sectors that traditionally pay higher than market average dividends include utilities, integrated oil, pharmaceutical, and telecommunications companies. Recently, mature technology companies are getting in on the act and paying out a portion of their earnings in dividends as way to compensate investors for lackluster earnings growth.

We will also continue to play the inflation trade. This strategy consists of accumulating and/or holding stocks or ETF's (Exchange Traded Funds) of commodity based securities. This would include oil, gas, copper, gold and other metals. Oil and gold are dollar denominated assets. Their value is inversely related to fluctuations in the dollar. The thesis behind this investment strategy is to capitalize on our prevailing belief that the dollar will continue to decline on a relative basis to other major currencies. As the dollar declines the commodities become more expensive as demand rises on the world market. Indeed, in 2010, gold has jumped over 30%.

We continue to be somewhat ambivalent toward financials. While we continue to like the long-term fundamentals of JP Morgan and the strategic turnaround at Citigroup, we are less enthusiastic about the long-term growth prospects of many regional banks. With the implementation of Basel III, rising tier I capital requirements and the scrutiny of regulator looking over management's shoulder, the fear that regional banks could become nothing more than utilities like securities – earning only a regulated maximum return – is not unlikely. Time will tell how these institutions will react and morph into their new business environment.

QUARTERLY ACTIVITY

LEGACY INITIATED POSITIONS IN THE FOLLOWING COMPANIES:

Hewlett - Packard (HPQ) – Hewlett-Packard is the world's largest technology company based on \$114B in revenue generated in 2009. HPQ's largest segment, technology solutions, was acquired through the 2008 acquisition of EDS (Electronic Data Systems) and represents 42% of total revenue. The company's imaging, printing and personal systems groups generates 55% of total company net sales. Hewlett-Packard has over \$3B in net cash that management plans to utilize for acquisitions and other growth opportunities. The company generates strong cash flow to support its growth initiatives. From a value perspective, HPQ is undervalued as it is selling at a P/E multiple of 8, which is a 37% discount to its 10-year median. It is also selling at a 15% discount to its peer group. A large part of the valuation is attributed to the resignation of its CEO, Mark Hurd and the ridiculously high acquisition price it ended up paying for utility storage and cloud computing firm 3Par. Unfortunately, all of this activity occurred after we purchased the stock. However, subsequent to reading and learning about the new CEO and analyzing the 3Par acquisition, I believe HPQ does have value and is worth keeping in the portfolio. It is our opinion that the market has over-reacted to the hiring of Leo Apotheker as CEO and the purchasing of 3Par will boost HPQ's presence in the market for virtual data center and cloud computing. We will be monitoring the progress of both the integration of 3Par and the implementation of Mr. Apotheker's business strategy.

JPMorgan Chase (JPM) – JPMorgan Chase is a global financial services institution with total deposits of almost \$900B, net loans outstanding of over \$600 billion and total assets in excess of \$2T. JPM has operations in more than 60 countries and provides services in Retail Banking (30% of Revenue), Investment Banking (25% of revenues), Credit Card Services (16% of Revenues), Asset Management (9% of Revenue), Private Equity (8% of Revenue) Commercial Banking and Treasury Management (6% of Revenue each). We added JPM to the portfolio based on its value characteristics. The bank is selling at a 10% discount to both its book and tangible book value. JPM's forward P/E was at a 10% discount to its peer group while its credit quality continues to improve. In the second quarter of 2010, the bank reported that loan loss reserve declined by \$2B and both non-performing assets and net charge-offs declined meaningfully. Return on Assets (ROA) and Return on equity improved 40% and 43%, respectively on a sequential basis.

LEGACY LIQUIDATED POSITIONS IN THE FOLLOWING COMPANIES:

Hudson City Bancshares (HCBK) – We sold our position in HCBK over concerns of deteriorating credit quality associated with the challenging housing market in metro New York and its reliance on Jumbo mortgages. Basically, the bank's liberal lending model is coming back to haunt itself as we are increasingly concerned that HCBK's inadequate loan loss reserve and high loan-to-deposit ratio will increase the likelihood that management will have to sell securities to meet capital requirements. While the bank's attractive 5% dividend will be missed, the downside risk is considerably greater.

IBM (IBM) – We sold positions in IBM in early July as concerns over the economy and market cannibalization from competitors like Oracle. Indeed, revenues in the second quarter earning announcement came up a little shy of analyst's expectations while service signings disappointed as well. Interestingly, the biggest area of strength was in the U.S Federal sector which might not continue due to budget contraction. Margins in some of the company's key business units such as software are peaking near 90% which will make further growth difficult. While company fundamentals continue to be attractive and the product cycle favorable, we are concerned about sustainable growth in the face of continued domestic and global economic weakness and intense competition in many business lines. We will continue to monitor IBM and their earnings announcements for evidence of a stabilizing environment.

Visa Corp (V) – While Visa's valuation remains somewhat attractive, the underlying business environment for the credit card industry has been negatively impacted by a tsunami of economic weakness and strict regulations imposed through FINREG. The new financial regulatory reform act will limit or cap the amount of fees credit card companies can charge. While this new law may not directly hurt revenue, it will certainly compress earning and profit margin. There is significant uncertainty within the industry and we have a tendency to sit on the sidelines until management figures out how to operate within the new environment.