

KWAG February E-mail Update

Good afternoon. We would like to thank each of you for attending our Client Appreciation Dinners across the state during the last week of January. It was good to see everyone, as we truly appreciate your continued confidence in our firm. We really enjoy the dinners because they provide us with an opportunity to reinforce our long term investment strategies - and – the dinners give us a chance to say “Thank You.” Unfortunately, we had to cancel our Asheville dinner as we were expecting ice and snow that evening. The Asheville dinner has now been rescheduled for Wednesday, April 6th at 6PM at the Country Club of Asheville. In March, we will send out invitations as a reminder. For those of you who don't live in or around Asheville, you are invited to attend as well. This will give you a great reason to visit Asheville during the spring, when it is absolutely spectacular.

A Recap of the Evening

Based on your feedback, each of the dinners were informative, educational and fun. The tone of the evening was set by presenting tables which examined the excellent growth in our portfolios over 2009 and 2010. The last two years have been good for all of our clients, and we expect that this trend will continue well into 2011 and 2012. In fact, the first five weeks of 2011 have been nothing short of excellent. Simply put, the economy is pointed in the right direction and it continues to surprise even the most optimistic economists on the upside. Of course, we also expect a few of the normal "bumps in the road" as we move forward. We have a number of challenges that will no doubt result in greater short term volatility and the usual short term decreases. This is normal, so please remain patient as our economy emerges from this past recession.

During our dinner, both Scott and I provided a birds-eye view of the economy and our portfolio's. These “State of the Union” presentations focused on a number of well known issues that you are no doubt seeing and hearing in the news. Our goal was to provide some perspective on which of these issues are really important to long term investors. A short synopsis follows.

Joe's Message

As usual, my message was fairly "upbeat" about what's taking place in the financial markets today. We believe the global economy will improve at a significant pace, given the low cost of labor and capital. In addition, with the incredible advances in technology and increased flow of goods and services across borders, we see this global expansion

continuing for quite some time. However, not everything is all “rosy”. We discussed a number of the potential headwinds, which include rising interest rates, potential inflation, our deficit, government spending, continuing low unemployment, the balance of trade, and other potential unknowns. The headwinds offer some very complex and difficult decisions that will have to be addressed by our leaders. However, given the direction of the economy and the new tenor in Washington, we believe a number of these issues will be dealt with in a positive way. Overall, we remain very positive about the long term view for our markets, our economy, global growth and most importantly our portfolios.

Scott's Message

Scott's presentation dealt with the issues taking place in the fixed income and bond markets over the next few years. There is no question that interest rates will start going up again. And, over time, inflation (which will be more muted than the headlines suggest) will impact our portfolio's. We are all aware of the notion that when interest rates go up, most bonds go down. Scott reminded the audience that all bonds are NOT created equally, which means they do not all behave in the exact same way. Given this knowledge, we have made a number of changes in our bond portfolios by increasing our managers flexibility to alter their portfolios as interest rates rise. We believe the next few years will be challenging for all bond investors. That said, interest rates have been rising for a few months now. Over that same time period, our bond portfolios are up, so we believe we have our arms around the issue.

A Handout

During all of our dinners, we provided a copy of the handout that we used at our client dinners in 2009. (We will provide this handout at our April dinner as well.) Think about how you felt in January, 2009 as our markets were going through one its most volatile periods in decades. If you were listening to the media and many of the supposed financial experts, we were supposed to be headed for the next Great Depression. In our handout, we examined specifically how the markets and investors behave after financial “shocks.” Some wonder how we could have predicted so accurately what was going to follow. Many argued that the issues we confronted were different – and they are correct. However, the issues are always different as our economy becomes more global. What’s NOT different is the role of human behavior and “herd” mentality.

In a nutshell, we examined what happens to our markets when people panic and consumer confidence hits all-time lows. Basically prices become so out of touch with reality that the ensuing rebound is always quick, significant and driven by small/mid cap companies. This happens every time after our markets experience a radical event - and

- it serves as a gentle reminder as to why one has to "stay the course" when everyone else is panicking. From the bottom on 03-09-09, the S&P500 is now up over 95%, while the Russell 2000 is up over 130%. How many of you believed that this type of bounce-back was possible when we met two short years ago? Our handouts provided strong evidence of exactly what happens to our markets following disruptions and the ensuing panic. Let's hope this recovery continues as past recoveries have, which should give all of us something positive to look forward to in 2012 and 2013.

Please Read Our Newsletter

Before we let you go, we would like to encourage each of you to read our latest BEHIND THE SCENES quarterly newsletter. It provides insights beyond this update and beyond our educational dinners. As most of you know, our newsletters are driven by your questions and by current financial events. We also like to keep you ahead of the curve by examining future issues that will (and won't) affect our portfolio's down the road. For example, in our most recent newsletter, we addressed questions that had to do with replacing the dollar as the reserve currency, Federal Reserve policy, our budget deficit, consumer spending and other potential threats to our economy. The media will have you believe these events are game changers. The truth is, many of these events play very little role in building successful long term portfolios.

Going Forward

We're not sure everyone understands how often we reviewed each and every client portfolio. Or how often we make subtle changes to keep it well balanced. Recently, we made changes to all of bond holdings. Going forward, we will be rebalancing and tweaking our stock portfolios to keep them well positioned for growth in 2011 and beyond. Given the recent significant growth of a number of our managers, many of our stock portfolio's are a bit unbalanced. We are well aware of this and will make adjustments after our managers have done so. Don't forget they are also making daily adjustments to their holdings. At this point, many of you have already seen a number of trade confirmations. Over the coming months, you will see others as we continually tweak each portfolio going forward.

In closing

As always, we appreciate the opportunity to work together and your continued confidence in our firm. And, as usual, if you have any questions about this update, our newsletter, your accounts or our managers, please feel free to call or e-mail us at anytime. The recent referrals are much appreciated and, as always, we remain 100% committed to your financial well-being.

- Joe and The Gang at KWAG

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