



December 31, 2009 Quarterly Report

Overview

We would like to express gratitude to all of our clients for the opportunity to manage your assets during one of the most tumultuous market environments in recent history. We are proud to have been able to deliver a valuable service where we did not lose any client accounts. In fact, we have grown appreciably over the last 18 months.

Chrysalis continues to reap the benefits of our affiliation with Wheelhouse Securities Corporation. We have found that this relationship allows us to be able to execute and monitor your investments more effectively and efficiently than if we had to use the services of a non-affiliated broker dealer.

Economic Review

The unemployment rate in the U.S. soared to a 26-year high of 10.2 percent in October and continued to remain around 10% through November and December. As noted in our prior quarterly comments, this number does not include the number of individuals who have given up looking for jobs and those that are underemployed. The total unemployed/underemployed figure still exceeds 17% and in our estimation will continue to dampen growth prospects for the US economy. It is a matter of basic arithmetic in that US consumer spending accounts for over 2/3 of GDP and if you have an abnormal amount of people underemployed/unemployed that now have no or less money to spend, you will not have normal growth. Employment, ignoring all other economic measures, remains the most important piece on exiting the recession and returning to normal growth.

While we can not dispute the general stock market returns that have brought the US economy back from the brink, we are not completely convinced that we are entering a new cyclical bull market. The amount of government stimulus that has been injected into the economy definitely clouds the outlook.

Various estimates put the fourth quarter GDP growth around 4%. This number should be viewed in light of the government's downward revision for third quarter GDP from 2.8% to 2.2%. We remain skeptical of recent GDP activity as inventories were slashed to such low levels that a large percentage of growth has come from an "inventory bounce."

Consumer Confidence posted yet another moderate gain in December as expectations for the short-term future increased to the highest level in two years. The index reading of 52.9 in December continues to remain above the accepted 50.0 for indications that the economy will be growing.

During the scheduled December 15th meeting, the FOMC stated that, "...to provide support to mortgage lending and housing markets and to improve overall conditions in private credit markets, the Federal Reserve will purchase a total of up to \$1.25 trillion of agency mortgage-backed securities and about \$175 billion of agency debt. The amount of agency debt purchases, while somewhat less than the previously announced maximum of \$200 billion, is consistent with the recent path of purchases and reflects the limited availability of agency debt. In order to promote a smooth transition in markets, the Committee will gradually slow the pace of its purchases of both agency debt and agency mortgage-backed securities and anticipates that these transactions will be executed by the end of the first quarter of 2010."

Additionally, during both the November 3rd and December 15th meetings the FOMC announced that the target range for the federal funds rate would remain between 0 and ¼ percent.

The monetary policy continues to remain accommodative though the markets have been trying to play a guessing game for when policy becomes more restrictive.

We continue to monitor the FOMC activities particularly as it affects the value of the US dollar. Recent currency trading suggests that the dollar has reached its nadir and may be in a more stable range. However, with such a large accommodative monetary policy, we expect inflation to remain a threat at some point in the future. With that in mind, we will continue to work to hedge inflation risk through a number of different investment classes such as: gold, oil, and timber assets, along with Treasury Inflation Protected Securities (TIPS).

Equity Markets

From an overall equity market perspective, the S&P 500 continued its rising trend from the third quarter by generating a 6.04% total return for the quarter ended December 31, 2009. On a year to date basis the index rose 24.46%. Unfortunately, the index has produced an annualized loss of -5.61% for the last three years and an annualized loss of -0.95% for the last 10 years. The past 10 years have truly been a lost decade that is worth leaving behind for equity investors.

Bond Markets

The Bond markets were able to generate an approximate 6.60% return year to date as measured by the Barclay's Aggregate Bond Index. The Bond markets have continued to remain active as individuals seek safety and income as an alternative to equities.

Portfolio Changes

We continue to monitor all positions and have been working to balance short term movements and liquidity constraints with valuations. For those with taxable accounts, tax consequences are also a constant factor.

For the quarter we made the following sales for most of the account(s) we have been managing for the at least one full year:

BFCF- BFC Financial Corp effected a merger with our investment of Woodbridge Holdings (WDGH). We realized a loss on this sale as we viewed the merger to be a disadvantage to the holders of WDGH.

HPT PRC – Hospitality Properties Trust was sold for a long term gain as the recent increase in appetite for higher yields led to this position reaching our full value target.

ACGY – Acergy SA, an international offshore oil service provider, was sold for a short term gain as the investment reached our price target.

Nestle Bonds – We sold these bonds that were denominated in Australian dollars, prior to maturity as we felt that the balance between further currency appreciation outweighed the remaining yield to maturity. These bonds were purchased as a hedge to a declining dollar and performed above our expectations.

Q- Qwest communications was sold for a long term gain as we felt that the company is maintaining a higher than normal dividend policy given its capital structure and lack of any meaningful long term growth prospects.

For the quarter we made the following purchases for most of the account(s):

NR- Newpark Resources was the only investment we purchased during the quarter. We have invested in this company a number of times over the years. After meeting with management, we feel that the company offers an attractive opportunity as a rebound in oil/gas prices should precede an increase in the number of drilling rigs in North America. Additionally, the company has been testing new products that could allow for exceptional growth should they be accepted in the marketplace.

Closing Remarks

The current market environment has certainly provided a sense of relief given where we were headed this time last year. It is apparent that our financial system is not dropping into an abyss. However, we are not convinced that we are completely free from the issues that preceded this massive correction.

Debt levels continue to run high amongst consumers, financials, and our very own government. Bankruptcies, write-offs, higher tax revenues (either through profits or through increases in the marginal rates) and increasing corporate profits will be the methods to bring about the necessary deleveraging.

We continue to scour the investment universe for ideas that adhere to our fundamental basis style of investing. Given the massive rally in all asset classes, the number of ideas conforming to our investment style has been dwindling. During the last 12 months we invested in a number of corporate bonds that met our criteria of fundamental investing. By investing in corporate bonds during a distressed period we took advantage of the mispricing and enabled our clients to receive a fixed income stream and a decrease in volatility when compared to equity investments.

We have an inordinate amount of cash waiting to be invested and expect that we will have many periods over the coming years where we are more invested than we are now. We are very cognizant of the concept that investing in cash can lead to a drain on returns, but we feel strongly that we should not jeopardize your investments by chasing assets that do not offer a modicum of return for the given risk.

We will continue to invest only in ideas that we believe will continue to provide a margin of value given worst case scenarios.

Please call if you would like to schedule an overview of your portfolio. As always, thank you for your confidence and support.

Sincerely,



Robert J. Grunzinger
President
Chrysalis Investment Management, LLC