



June 30, 2009

Market Commentary

Financial markets experienced significant healing and improvement in the second quarter of 2009. The S&P's 15.93% gain marked the first positive quarter in over a year and half as investor willingness to own riskier assets improved. This also contributed to thawing within many parts of the credit markets. The improved performance of most asset classes was largely at the expense of US Treasuries which were down 2.93% for the quarter. Government securities had been the primary beneficiary during recent periods of market stress. Emerging markets and commodities were also strong for the quarter in anticipation of global economic improvement.

Looking ahead, it is far from clear if economic activity can support further improvement in equity valuations in the near term. While there have been a few hopeful signs of the economy bottoming, some contend that we are only seeing a recalibration of inventory levels for the "new economy" as opposed to any sustained levels of economic activity. Positive earnings announcements have been the result of aggressive cost containment as companies continue to right size their businesses. Ultimately, companies will need to drive earnings by growing the top line as well as the bottom line. The market rewards growth.

The Federal Reserve and Treasury have continued to pump liquidity into the financial system. While these efforts have contributed to an easing of the credit crisis, inflationary expectations have increased. As a result, mortgage rates experienced upward pressure during much of the quarter. Even in the face of massive issuance of government debt, it is essential that inflationary expectations are kept in check in order for interest rates to remain low, allowing the housing market to stabilize and the economy to grow. The Fed and Treasury face a tough balancing act.

Even in the face of considerable uncertainty, we do see opportunities. In the fixed income area, we continue to favor corporate bonds and expect them to continue outperforming US Treasuries. On the equity side, we favor a number of names in sectors such as technology and energy which should prosper as the global economy improves. The sooner the better!

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