

THE LONG TERM VIEW

Average Annual Rates of Return		
Period	Stocks	Bonds
12/31/89 - 12/31/99	18.23%	7.35%
12/31/99 - 12/31/09	-0.97%	6.08%
12/31/09 - 12/31/19*	6 - 8%	3 - 4%
* Patten and Patten projections. Stocks refer to the total return of the S&P 500 Index. Bonds refer to the Barclays Capital Intermediate Govt/Credit Bond Index.		

- In April 2009, we made the following assertion: ***"We believe that investors should be prepared for two things: a) the continuation of the stock market rally well past expectations and b) another sell off of some magnitude sometime in the near future."*** **We maintain this near term outlook.**
- In February 2010, we introduced our projections for rates of return for stocks and bonds (as presented in the table above). While not bearish on either market, we believe that fundamentals do not support the type of returns from financial assets that investors enjoyed in the 1990s. However, we envision a better decade from equities.

Note that all charts, tables, and graphs utilized in this analysis were obtained from the Bloomberg Financial Markets system unless otherwise indicated.

April 26, 2010

WHERE ARE WE NOW?

- The stock market has returned nearly to the levels that existed prior to the Lehman Brothers fiasco (i.e., September 2008).
- Investor **appetite for risk** has increased dramatically. **Higher Beta** stocks (i.e., more volatile) and companies with greater leverage continue to outperform. As the Fed and other central banks accelerate the process of removing liquidity from the system, we believe the markets will gravitate back toward investments of considerably higher quality.
- The market is being propelled by **momentum** traders. Some aspects of recent activity are not justified by fundamentals. Rapid sector rotation has driven the performance of the various indices. Generally, those sectors that performed the worst in 2008 have led the market out of the trough (see the tables on **pages 4 & 5**).
- The market has continued to reward short term, opportunistic transactions. Long term, diversified investing strategies have underperformed concentrated, leveraged tactical approaches. We do not believe this condition will persist.
- The market's expectations for Fed rate increases in 2010 have diminished. Expectations for inflation remain in line with long term trends.
- Resolutions to the Financial Crisis of 2008 effectively required the assumption of private sector debt by public entities to facilitate orderly restructurings. Risk has, therefore, shifted to burgeoning sovereign and public debt. Despite a brief, shallow correction in January, the market has shrugged off many of these concerns. We believe, however, global fiscal issues remain far from fully resolved. Therefore, these lingering uncertainties warrant a certain amount of caution and a well diversified approach.

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LONGER TERM ISSUES

- **Double dip for housing?** The number **103** refers to “the number of months it would take to sell off all the foreclosed homes in banks’ possession, plus all the homes likely to end up there over the next couple years, at the current rate of sales...As of March, banks had an inventory of about 1.1 million foreclosed homes, up 20% from a year earlier, according to estimates from LPS Applied Analytics. Another 4.8 million mortgage holders were at least 60 days behind on their payments or in the foreclosure process, meaning their homes were well on their way to the inventory pile. That ‘shadow inventory’ was up 30% from a year earlier.” (*Wall Street Journal*, April 24, 2010).
- **Inflation v. Deflation:** This debate will rage on among market participants for years to come. At issue is whether the inflationary implications of **monstrous surges in money supply** will overwhelm the deflationary impact of **global deleveraging**. Globalization suggests continued excess capacity in many sectors, particularly labor. Rising protectionist sentiment, however, is inflationary in nature.
- **Era of Frugality?** Contrary to expectations, the US consumer has yet to completely collapse. While the savings rate has risen somewhat, **retail sales have remained surprisingly strong**. As the year progresses, this growth will be challenged by more difficult comparisons and structural unemployment. Moreover, Dave Rosenberg of Gluskin Sheff estimates that discretionary income has been boosted by approximately **\$120 billion** in strategic mortgage defaults. This helped to offset the nearly \$235 billion contraction in consumer credit since the crisis began.
- **Financial Market Reform.** The recent SEC securities fraud case against **Goldman Sachs** is likely to spur on new regulations that will modify the manner in which large financial institutions conduct their practices. We anticipate that legislative reform that focuses on **stricter capital controls, less leverage, and greater transparency** will get passed. We further anticipate that a coordinated global effort at financial market reform will shrink profit margins for many of the large, global banks. While there is risk of “over-regulation,” we remain encouraged that much needed regulatory reform will re-establish trust in the capital markets long term.
- **PIIGS. Portugal; Italy; Ireland; Greece; Spain.** The pending “rescue package” for Greece is important for the stability of the Euro Zone. Yet, it could mark only the beginning of this form of policy engineering as fiscal pressures deteriorate in several other economies. The epicenter of the financial crisis has crossed the Atlantic, and the focus has shifted from corporate to sovereign debt. However, this problem is similar to subprime in the fact that it is **unlikely to remain contained**.

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PERFORMANCE OF VARIOUS ASSET CLASSES

Market Performance Analysis					
SYM*	Description	Category	Total Return		
			Q1 2010	2009	2008
	S&P 500 Total Return Index	Large Cap Equities	5.39%	26.46%	-37.00%
	DJIA	Blue Chips	4.82%	22.68%	-31.93%
	NASDAQ Composite	Tech Dominant	5.68%	43.89%	-39.98%
	Lipper International	International Equities	3.48%	35.30%	-43.62%
	Russell 2000 Composite	Small Cap Equities	8.85%	27.17%	-33.79%
	Shanghai Composite	Chinese Stocks	-1.02%	79.59%	-64.89%
	Barclays Cap Govt/Credit	Govt & Corp Bonds	1.54%	5.24%	5.08%
LQD	iShares iBoxx IG	Inv Grade Corp Bonds	2.43%	8.46%	2.40%
HYG	iShares iBoxx HY	High Yield Bonds	2.14%	28.57%	-17.58%
GLD	SPDR Gold Trust	Gold Bullion	1.53%	24.03%	4.92%
EWZ	iShares Brazil		-1.30%	121.86%	-54.30%
EWC	iShares Canada		6.00%	53.13%	-44.45%
EWA	iShares Australia		5.12%	68.13%	-47.95%
EPP	iShares Pacific ex-Japan		3.84%	63.49%	-47.57%
EFA	iShares EAFE Index	Europe, Australia & Far East	1.27%	26.95%	-41.04%

* Symbol refers to the Exchange Traded Fund that tracks each Index.

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PERFORMANCE OF S&P 500 SECTORS

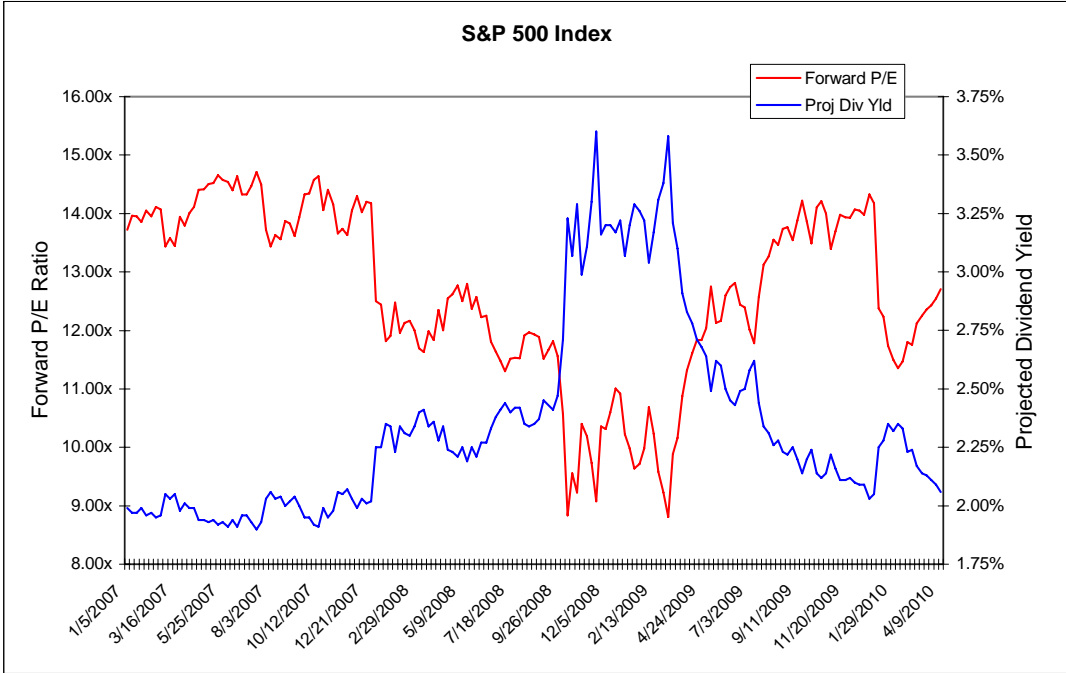
S&P 500 Sector Performance Analysis						
SYM*	Weight**	Description	Category	Total Return		
				Q1 2010	2009	2008
XLY	17.35%	Select SPDR Cons Disc	Consumer Discretionary	10.52%	40.57%	-32.97%
XRT		Select SPDR Retail	Retail Stocks	16.14%	77.43%	-38.02%
XLP	7.53%	Select SPDR Cons Staples	Consumer Staples	5.97%	14.28%	-15.02%
XLE	8.39%	Select SPDR Energy	Broad Energy Stocks	1.25%	21.79%	-38.97%
XOP		SPDR Oil & Gas	Exploration Stocks	2.30%	40.17%	-42.69%
XLF	14.51%	Financial Select SPDR	Broad Fin Svces	11.02%	17.61%	-54.97%
KRE		SPDR KBW Regional Bank	Regional Banks	18.20%	-21.92%	-18.57%
XLV	11.80%	Health Care Select SPDR	Broad HC Services	3.76%	19.51%	-23.31%
XLI	13.93%	Industrial Select SPDR	Industrial Companies	12.80%	22.07%	-38.74%
XLB	6.58%	Materials Select SPDR	Basic Materials Cos	3.04%	48.17%	-44.05%
XLK	13.86%	Technology Select SPDR	Information Technology	1.06%	51.32%	-41.51%
IYZ	0.72%	DJ US Telecomm	Telecom Stocks	0.74%	26.23%	-42.04%
XLU	5.33%	Utilities Select SPDR	Utilities	-3.53%	11.71%	-28.93%

* Symbol refers to the Exchange Traded Fund that tracks each Index.
 ** Sector weight in the S&P 500 Index.

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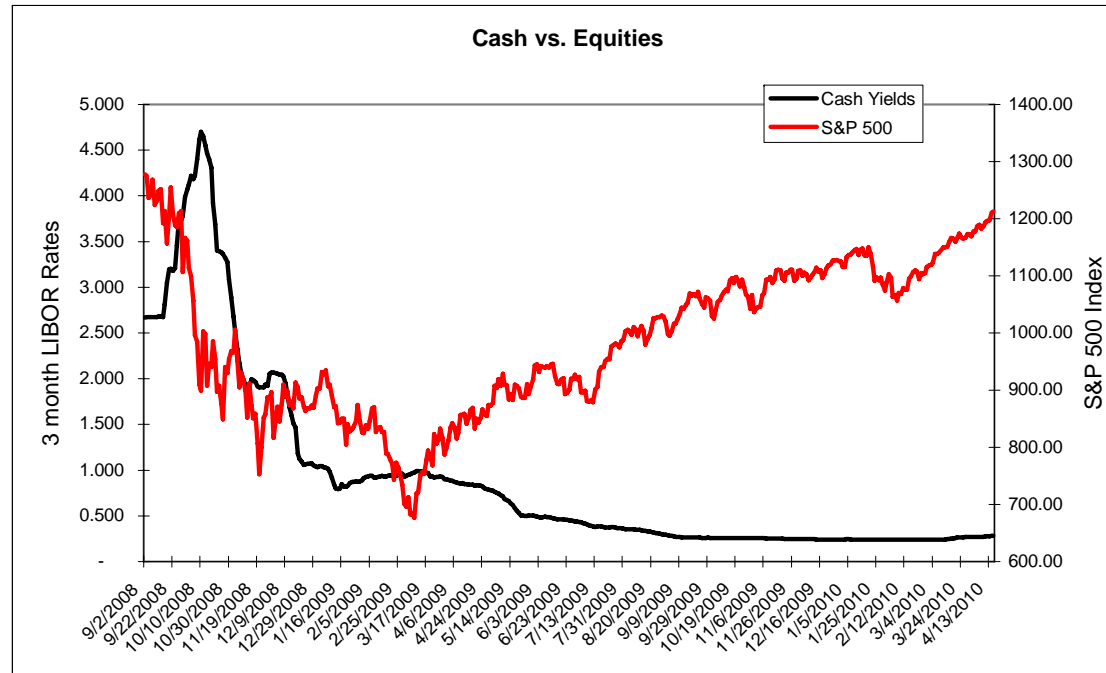
THE STOCK MARKET IS "FAIRLY" VALUED



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THE STOCK MARKET CONTINUES TO BENEFIT FROM LOW RATES



- Note how the near 5% level on 3 month LIBOR was an indication that demand for cash far exceeded supply. The prevailing sentiment in Q3 2008 was that **“cash is scarce and, therefore, precious”**. Today, 3 month LIBOR is **0.30438%** -- an indication that **cash is abundant**. Excess cash (i.e., liquidity) has sought greater returns in other asset classes, namely the capital markets.

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CURRENT MARKET INTEREST RATES

Current Interest Rate Matrix					
Maturity	Credit Quality				
	FDIC	Treasuries	AA	A	BBB
Cash	0.40%				
1 year	0.65%	0.44%	0.84%	0.90%	1.85%
2 year		1.06%	1.45%	1.52%	2.42%
3 year		1.69%	2.25%	2.33%	3.27%
4 year		2.15%	2.93%	3.05%	4.02%
5 year		2.63%	3.28%	3.37%	4.30%

Bloomberg market data and Fair Market Corporate Bond Indices, as of April 8, 2010.

- Cash yields continue to penalize investors. More attractive rate levels are available in slightly longer maturities and issues of lower credit quality. The need for higher yields should be balanced against the ability to assume greater credit risk. At this juncture, we recommend that investors refrain from “chasing yield” opportunities.

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LOOK FOR YIELD IN THE STOCK MARKET

- With the exception of the banks, the dividend yield for many of the stocks in the table below is higher than the yield on the company's 10 year bonds. We consider these yields to be attractive in terms of current income generation.

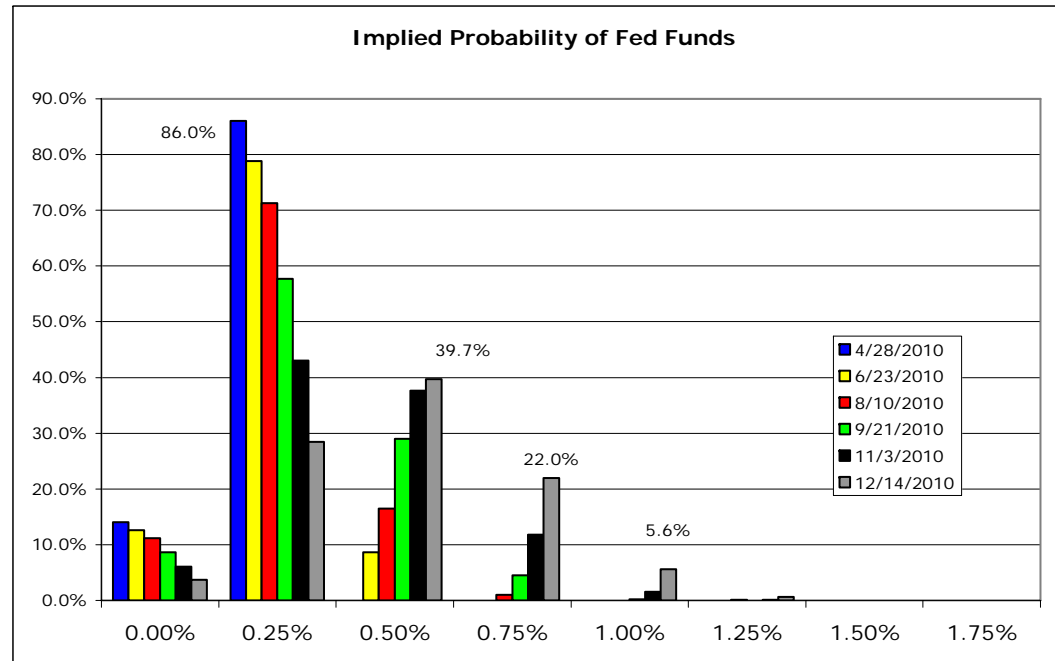
Company	10 year Bond Yield*	Dividend Yield*
AT&T	4.97%	6.39%
Verizon	4.80%	6.43%
Duke Energy	4.27%	5.95%
Dominion Resources	4.55%	4.42%
Merck	4.33%	4.21%
Florida Power & Light	4.74%	4.09%
Lockheed Martin	4.35%	3.02%
JP Morgan Chase	4.88%	0.42%
SunTrust Banks	5.69%	0.13%

* as of 4/15/10.

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WHEN DOES THE FED ACT? CURRENT MARKET EXPECTATIONS



Implied Probability of Fed Funds, as of April 15, 2010.

- Market expectations for rate increases from the Fed have fallen since year end 2009. Currently, the market has “priced in” **only a 50% probability of a 0.25% increase in Fed Funds** by year end 2010.

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WHEN DOES THE FED ACT? OUR EXPECTATIONS

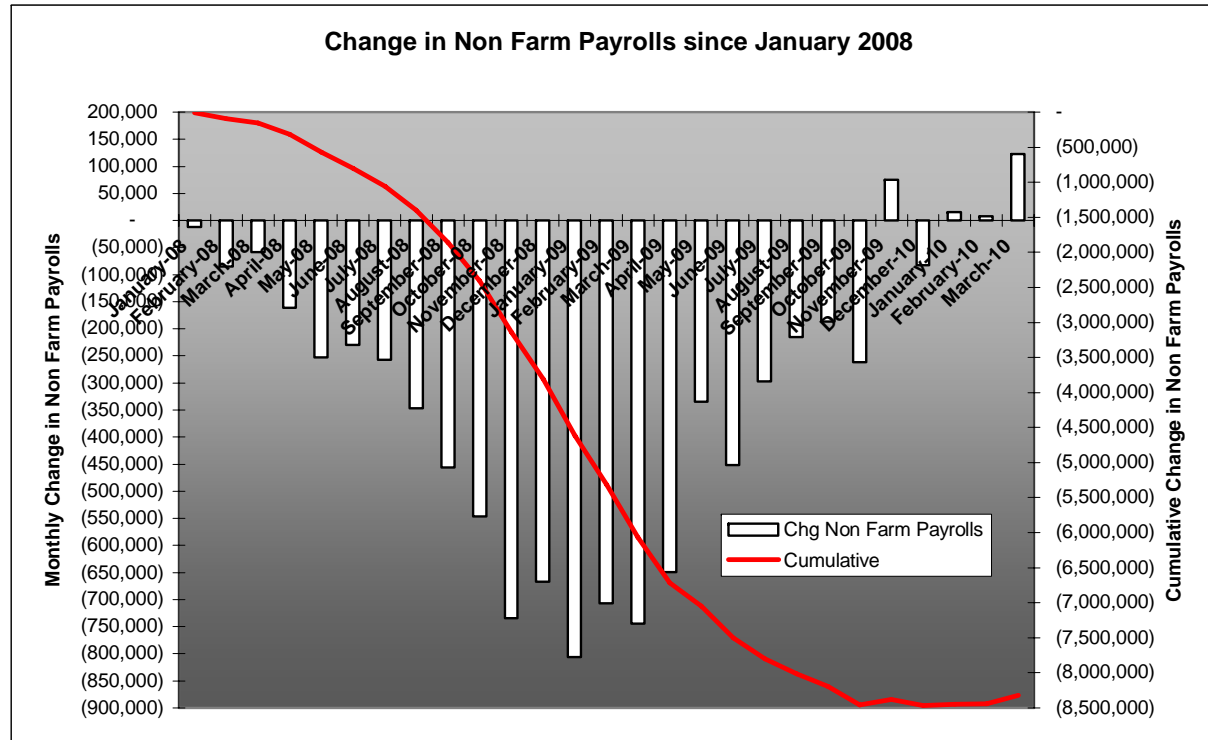
- We anticipate the Fed will maintain low rates until job creation becomes evident. Key barometer is the Unemployment Rate.
- Fed's policy response is asymmetric: aggressively respond to recessions; gently slow down economies/markets.
- At this point, the Fed is more likely to be late rather than early in terms of removing stimulus.
- At some point, consumer inflation could become a problem. For now, the Fed wants to ensure the economic recovery continues.

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JOB CREATION REMAINS THE KEY TO FUTURE ECONOMIC GROWTH AND FED POLICY

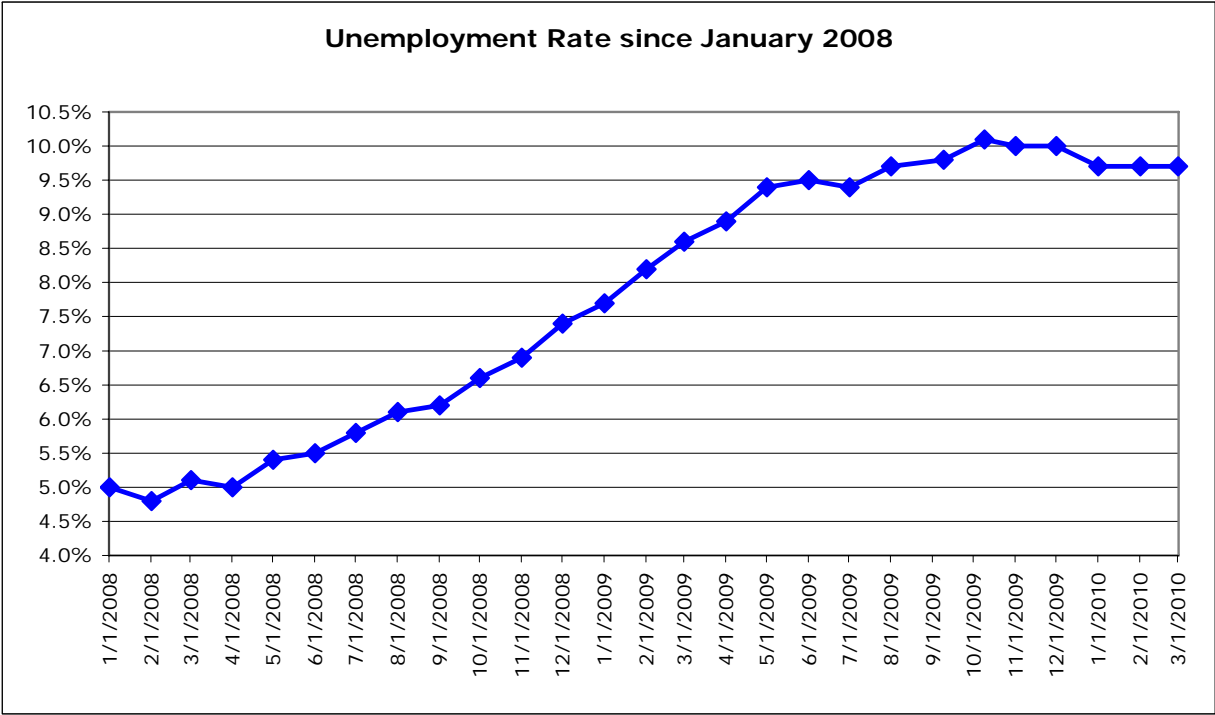


- The red line (right axis) is the cumulative number of jobs lost since January 2008 – a figure **approaching 8.5 million**. The bars (left axis) are the monthly non-farm payroll figures.

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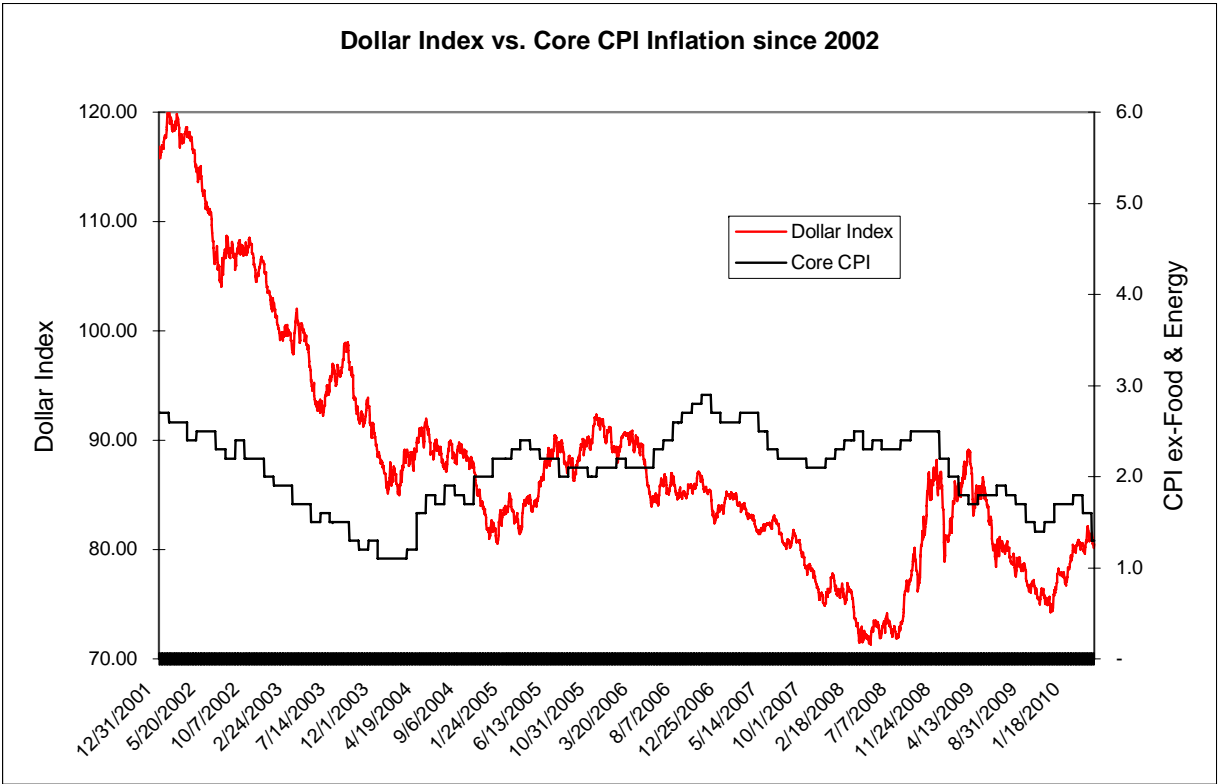
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POLICY FOCUS IN 2010: LOWERING UNEMPLOYMENT



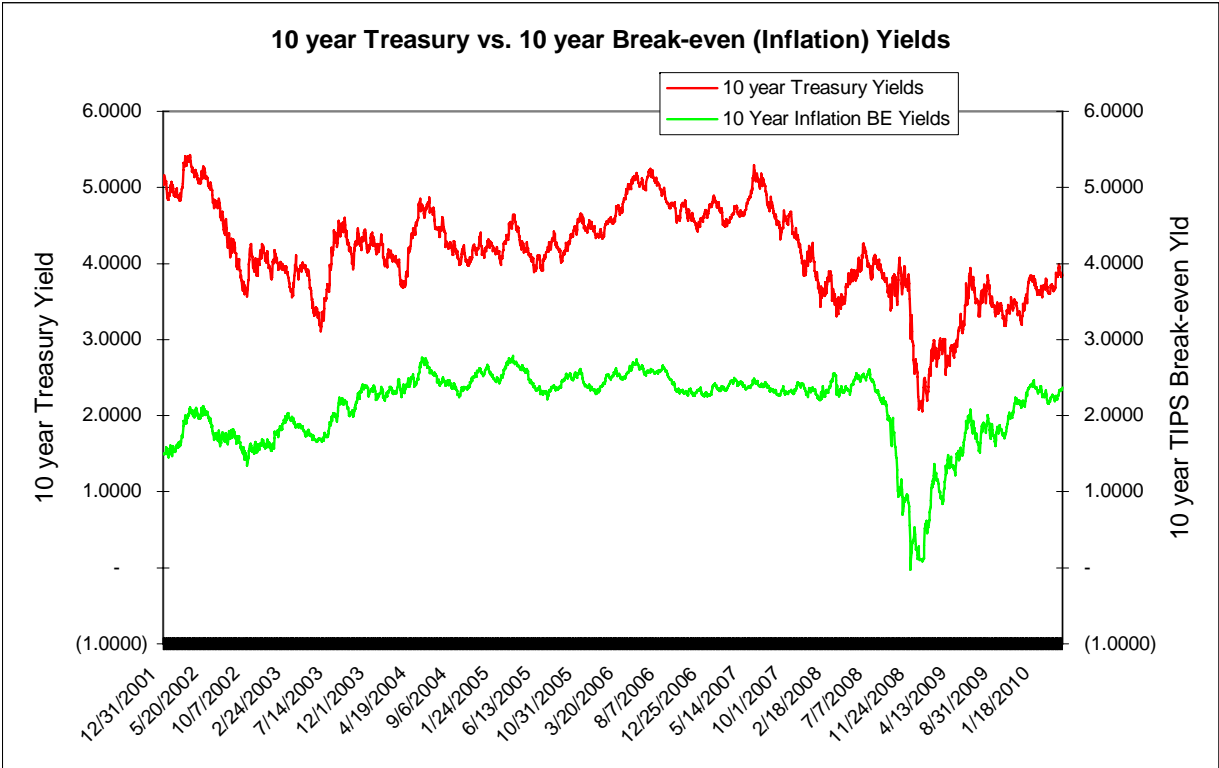
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DOLLAR BEAR MARKET SINCE 2002 , YET INFLATION HAS REMAINED STABLE



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INFLATION EXPECTATIONS ARE "NORMALIZING"



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