Economic & Market Review

~ October 2010 Investment Newsletter ~

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Monthly Summary

The September stock market rally continued throughout October with major stock market indexes delivering low single digit returns. Investors anxiously awaited the first week of November as the turning point in both governance (i.e. the election on Tuesday) and monetary policy (i.e. Wednesday's Federal Reserve decision). The intense, nearly blinding focus on these events enabled investors to experience the somewhat rare, if not ironic, happenstance whereby positive and negative data are both viewed favorably by the markets. This heads I win, tails you lose environment stemmed from the conclusion that weak economic data would provide voters, and the Fed, with the necessary impetus to "do the right thing" in November. We remain dubious as to the value of enhanced governmental gridlock when clear, efficient, and effective policy is so critical at this time. Furthermore, an economy ensnared in a liquidity trap receives little benefit from further attempts at monetary stimulus. We hope to be proven wrong on both accounts.

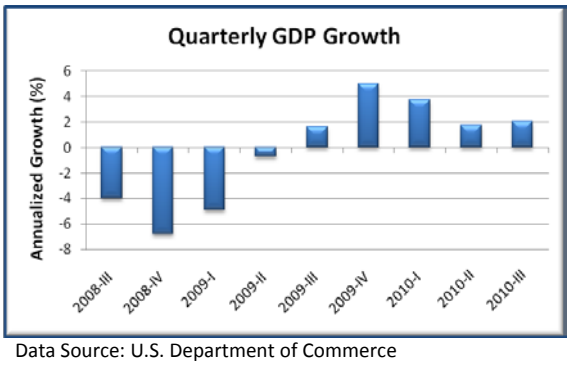
Economic data released during the month reflected slow growth with no particularly positive or negative developments. Third quarter GDP growth came in at 2.0%. This bested the previous quarter's showing of 1.7% but remains low relative to past recoveries and below what is necessary to improve the weak labor market. Manufacturing and service sectors reflect slow but steady forward progress while housing continues to be challenged. Inflationary pressures are absent and significant economic slack remains.

October's Economic Releases

General	Prior	Current
GDP growth	1.7% (Q2)	2.0% (Q3)
Trade balance	-$42.6 B (Jul)	-$46.3 B (Aug)

Employment	Prior	Current
Initial jobless claims	455,000	434,000
Continuing claims	4.5 MM	4.4 MM
Nonfarm payrolls	-57,000 (Aug)	-95,000 (Sep)
Unemployment rate	9.6% (Aug)	9.6% (Sep)
Average weekly hours	34.2 (Aug)	34.2 (Sep)

Consumer	Prior	Current
Consumer confidence index (Conf. Board)	48.6 (Sep)	50.2 (Oct)
Retail sales growth (YoY)	5.1% (Jul)	3.9% (Aug)
Consumer credit	-$4.1 B (Jul)	-$3.3 B (Aug)



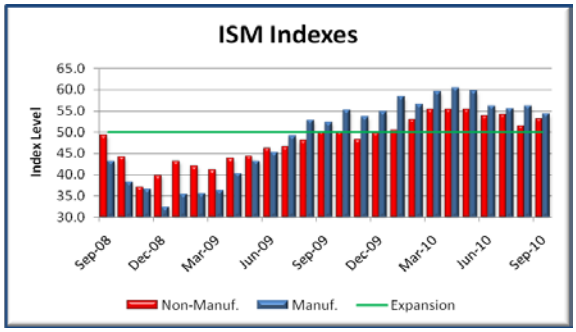
Data Source: U.S. Department of Commerce

Data Source: U.S. Census Bureau

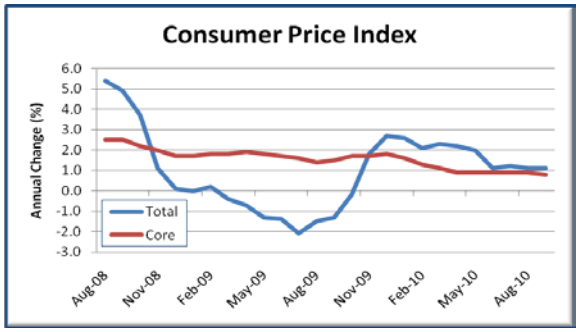
Manufacturing & Service	Prior	Current
ISM manufacturing index	56.3 (Aug)	54.4 (Sep)
ISM non-manufacturing index	51.5 (Aug)	53.2 (Sep)
Durable goods orders growth	-1.0% (Aug)	3.3% (Sep)
Industrial production growth	0.2% (Aug)	-0.2% (Sep)
Capacity utilization	74.8% (Aug)	74.7% (Sep)

Real Estate	Prior	Current
New home sales	288,000 (Aug)	307,000 (Sep)
Existing home sales	4.1 MM (Aug)	4.5 MM (Sep)
Case-Shiller home price index (YoY)	3.2% (Jul)	1.7% (Aug)

Inflation	Prior	Current
Consumer price index/Core (YoY growth)	1.1%/0.9% (Aug)	1.1%/0.8% (Sep)
Producer price index/Core (YoY growth)	3.1%/1.3% (Aug)	4.0%/1.6% (Sep)



Data Source: Institute for Supply Management



Data Source: U.S. Bureau of Labor Statistics

Market Returns

The S&P 500 index gained 3.8% for the period and is now up 7.8% for the year. Developed international equity markets, as defined by the MSCI EAFE Developed Markets index, were up 3.6% for the month, with half of the gain coming from U.S. dollar weakness. Emerging markets fared comparably to their developed counterparts with the MSCI Emerging Markets index up 2.9% for the month. Year-to-date, international developed and emerging markets returned 4.7% and 14.0%, respectively.

In the fixed income market, the Barclays US Aggregate index was up 0.4% for the month and the 10-year U.S. Treasury bond ended with a yield of 2.60%, up 9bps for the month and down an impressive 1.23% in 2010. For the year, the Barclays U.S. Aggregate has gained 8.3%. On a global basis, bonds were up 1.3% for the month and 8.3% for the year.

Commodities and real estate had strong gains of 5.0% and 4.0% respectively. Despite weak fundamentals, publicly traded REITs are the year's star performers, delivering 23.4% thus far – a true testament to investors' quest for portfolio yield.