



Market Commentary

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No Change in Portfolio Strategy Despite Treasury GSE Action

Now that the Treasury has made clear it's plan of action for the Government Sponsored Entities (GSEs), we see little in it's construction that forestalls the ongoing housing recession, prevents rising joblessness, or reverses the recessionary tendencies which have become even more entrenched in recent months. While the action gives comfort to agency debt-holders that the United States' government will likely make good on all GSE debt obligations, there remains significant questions about the long-term role that the GSEs will play in credit markets once the 2008-2009 period passes.

In addition, neither the equity injections, credit lines, purchase arrangements, or temporary increases in portfolio limits offer any guarantee that credit terms will be changed to make mortgages more available to potential homebuyers than they currently are. Therefore, there is no reason to expect a quick and material improvement in the imbalances that continue to confront real estate markets. In fact, over the short-run, the plan could have the negative effect of making credit even tighter as the government sponsored entities are forced to comply with the new set of standards that will emerge under conservatorship.

Looking beyond the next year, the call to materially shrink the entities in the post-2010 period would profoundly change the structure of banking and credit markets. Without an alternative structure in place, the pace of credit creation would likely slow and the cost of credit would likely rise. Unfortunately, the Treasury's recent actions stop short of offering a vision of what such a system may look like and, instead, leaves that debate to the Congress and the next administration while, at the same time, leaving the GSEs intact as functioning entities.

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We welcome the action as a first step to reform, but are making no change to our recommended tactical asset allocation in response to the Treasury's recently announced GSE action.

Instead, we remain focused on monitoring changes in the five key indicators which we believe are most important as it relates to portfolio decisions and the outlook for the economy. By way of reminder, these five indicators have been and remain:

- 👉 **Housing**
(continuing oversupply, prices falling)
- 👉 **Credit**
(shrinking availability and demand for loans)
- 👉 **Corporate profits**
(peak margins, declining level)
- 👉 **Private sector employment**
(mounting job losses)
- 👉 **Pricing of risk in financial markets**
(risk better priced versus a year ago)

Recommended Asset Allocation

	Growth	Balanced	Conservative
INCOME & OTHER	14%	39%	64%
DOMESTIC BONDS	11%	30%	49%
Money Market	1%	2%	3%
Short-Term Treasuries	2%	5%	8%
Intermediate Term Treasuries	1%	3%	5%
Inflation Protected Treasuries	1%	3%	5%
Investment Grade Corp Bonds	4%	12%	20%
High Yield Corporate Bonds	2%	5%	8%
COMMODITIES & OTHER	3%	9%	15%
Preferred Equity	1%	2%	3%
REITs	1%	2%	3%
Gold	2%	5%	8%
COMMON STOCKS	86%	61%	36%
DOMESTIC COMMON STOCKS	86%	47%	28%
U.S. SIZE & STYLE	66%	47%	28%
Large Cap Growth	32%	23%	14%
Large Cap Value	16%	11%	6%
Mid Cap Growth	10%	7%	4%
Mid Cap Value	6%	4%	2%
Small Cap Growth	1%	1%	1%
Small Cap Value	1%	1%	1%
FOREIGN	20%	14%	8%
DEVELOPED	13%	3%	5%
EAFE Growth	10%	7%	4%
Germany	3%	2%	1%
EMERGING	7%	5%	3%
Brazil	4%	3%	2%
South Korea	3%	2%	1%
TOTAL PORTFOLIO	100%	100%	100%

Recommended Sector Allocation

	Suggested Weight	S&P 500 Weight*
U.S. Equity Sectors		
Energy	5%	13%
Technology	17%	17%
Materials	3%	3%
Industrials	8%	12%
Consumer Discretionary	6%	8%
Health Care	24%	12%
Utilities	3%	4%
Consumer Staples	13%	10%
Telecommunications	8%	4%
Financials	15%	18%
Total	100%	100%

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