

SECOND QUARTER FINANCIAL MARKET COMMENTARY

"NINETY DAYS IN NINETY SECONDS"

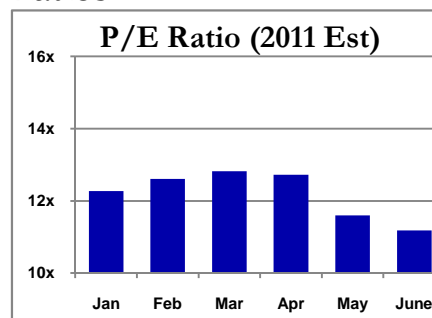
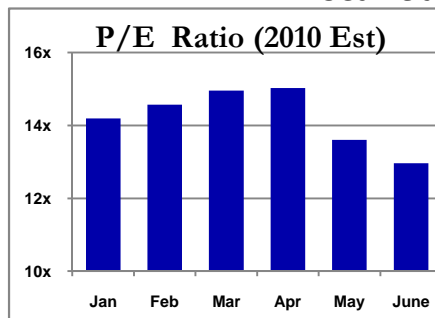
JUNE 30, 2010

- ♦ The financial markets continue to be locked in a massive tug-of-war between macroeconomic fear and microeconomic profitability. The pessimists use a broad brush and cite European debt woes in Greece and other nations, a slowing in China's rapid growth rate and stubbornly high domestic unemployment. Although these large structural problems are unlikely to be resolved quickly, policies are being implemented to mitigate the risks of contagion and these issues no longer represent "new" news that will need to be digested and discounted by the financial markets.
- ♦ The news is much more upbeat at the individual company level. Caterpillar is increasing its capital expenditures in China, 3M increased guidance for second quarter revenue, CBS reported strong growth in advertising demand along with improved pricing, and Texas Instruments raised revenue and earnings guidance based on "broad-based strength" in orders.
- ♦ The much-discussed and much-feared double dip in economic activity is actually a very rare event and has only occurred once in the past 90 years. The positive implications of record cash balances by corporations and a home price-to-wage ratio near 40 year lows should not be underestimated.
- ♦ Yields on U.S. government bonds fell to levels that were as low, or lower, than the levels that prevailed at the height of the financial crisis. Given the long term risks of rising inflation, it is hard to envision government bond yields remaining at these low levels.
- ♦ Earnings estimates for the S&P 500 Index have marched steadily higher in 2010 and are currently about \$80 for 2010 and almost \$95 for 2011. Even if the global turmoil ultimately reduces actual earnings to \$70, the S&P 500 is still only selling at a P/E multiple of 15x, which is the average post-World War II valuation level. In the event that current earnings estimates are achieved, then today's valuations are very attractive.

S&P 500 Earnings Estimates

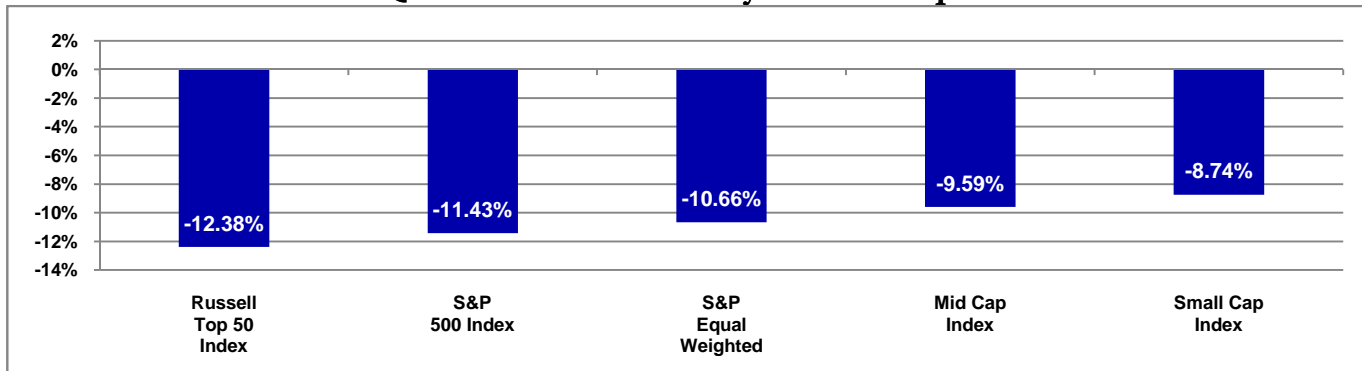


S&P 500 P/E Ratios

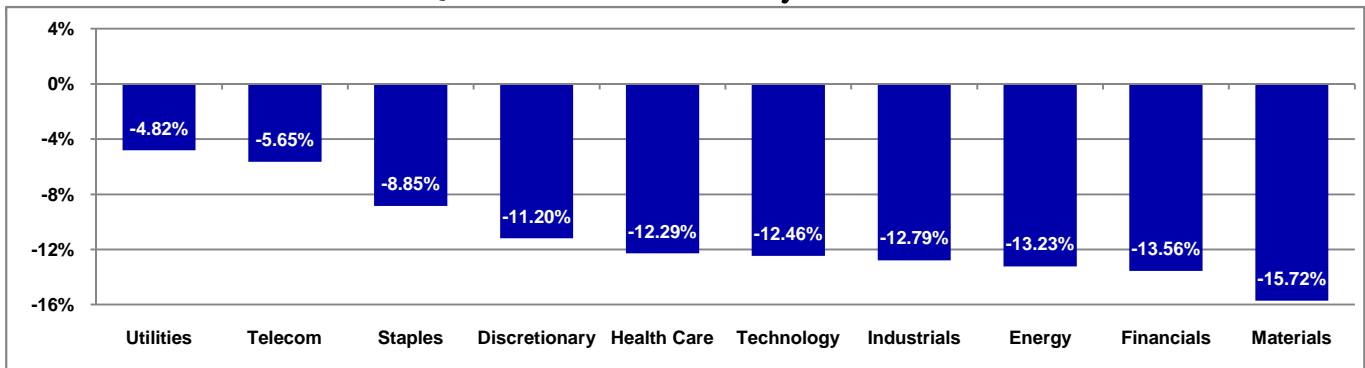


- ◆ Performance trends within the stock market were universally negative during the quarter. Mid Cap and Small Cap indexes, which usually tend to be among the most volatile, were ironically the most defensive size categories during the quarter. However, at the sector level, traditionally defensive groups such as utilities, telecom and consumer staples performed as expected and retained value better than the more economically cyclical sectors.

Second Quarter Performance by Market Capitalization



Second Quarter Performance by Economic Sector



- ◆ Public companies accelerated the use of their free cash flow for dividend payments during the first half of 2010. Within the S&P 500 Index, 140 companies have increased their dividends on a year-to-date basis. Further increases should be seen in the second half of the year as companies in the financial sector begin to resume more normal dividend policies.
- ◆ In terms of magnitude, most of the stock market's recent price decline should now be history. In terms of time, the market will probably remain volatile and trade in a wide range until second quarter earnings provide a renewed catalyst for higher stock prices.