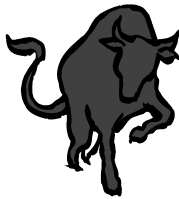


Index	Quarter Return	YTD Return
DJIA	12.0	-2.0
S & P 500	15.9	3.2
NASDAQ	20.1	16.4
Russell 2000	20.7	2.6
MSCI EAFE	23.8	5.6
Barclay's Aggregate Bond	1.8	1.9
Consumer Price Index	1.4	2.6



### Second Quarter Investment Commentary

As we look back on a tumultuous first half of the year, we are struck by the degree to which conflicting signals characterize the investment and economic environment. After a dreary first quarter in 2009, the second quarter saw robust gains – stocks, in fact, had their best quarter in more than 10 years. The S&P 500 stock index rose 15.9% in the quarter, erasing the deep losses of the first quarter and wiping away much of the fear that accompanied the early losses. The markets were so strong that nearly every asset category showed a gain. The aggregate bond index recorded a 1.8% return. Several positives helped drive the market's rebound from its March low. The prospect of a meltdown of the financial system appears past; the Government has demonstrated it will do whatever is necessary to avoid a disaster of this scale. And though economic activity continues to worsen, it is doing so at a slower rate, which suggests that we are getting closer to an economic bottom. The relief from Armageddon fears allowed investors to accept more risk and thus, the most risky sectors such as junk bonds had the highest returns for the quarter.

### The Economy – Uncertainty Reigns

The global economy remains in a delicate state as the effects of massive wealth destruction and the unwinding of the huge debt bubble continue to play out. As we have been suggesting since late 2008, the ultimate result will likely be lower spending by both consumers and businesses in the years ahead as the economy, in effect, resets to the level where it would have been without the artificial boost of the credit bubble. The massive bailout and stimulus spending probably allowed us to avoid a depression but, along with longer-term demographic factors such as spiraling health-care and other entitlement spending, is causing the federal deficit to balloon. This could lead to dollar weakness and inflation down the road.

We also think that a meaningful shift in consumer behavior is under way – one that will produce great benefits in the long run but slow our recovery in the short term. American households entered this recession stretched to the limit with mortgage and other debt. Households financed their lifestyles by drawing on increasing stock market and housing wealth and taking on higher levels of debt. But falling house and stock prices have destroyed trillions of dollars in wealth, cutting off those ready resources of cash. What’s more, the stark realities of this recession have scared many households, convincing them that they need to save larger fractions of their incomes. In the long run, higher saving promises to channel resources from consumption to investment, making capital more readily available to retool industry and fix our infrastructure. But, in the here and now, such a rediscovery of thrift means fewer sales at the mall and fewer jobs on assembly lines and store counters.

Other conflicts are at play that will influence how the environment unfolds in the years ahead. One of these is housing, which spearheaded the cycle of damage. There have recently been a few positive signs, including stronger demand and historically high levels of affordability. But a wave of new supply from foreclosures over the next two years suggests the housing market will continue to struggle.

### **Where to now?**

Investment returns will also be influenced by investors’ willingness to take on risk, which tends to build during bull markets and break down in bear markets. The degree of investor risk aversion is an unknown that will impact returns in the years ahead. Our assumption is that higher-than-normal risk aversion will subside very gradually and that investment valuations in five years will be average or below average relative to the last 50 years. If we look beyond five years, we anticipate a gradual return of normal risk-taking leading to higher returns. In all but our most optimistic scenario, we believe returns from all assets, including real estate, stocks and bonds over the next five years result in average annual returns that are lower than returns experienced over the last 20 years. Excessive regulation, higher taxation, and government intervention will be among the factors that will also constrain economic and investment growth.

As you know, at the end of 2008 we started reinvesting the large cash positions that were built during the year. We have been investing in a structured and disciplined manner and are continuing to do so today. Going forward, we expect continued volatility and occasional headlines that will cause concern. For this reason, we are emphasizing the higher quality end of all asset classes, especially large U.S. companies that have the financial strength and product depth to continue to weather the economic environment. We expect these to generate decent income but also provide a buffer should markets move down. In the risk area, we are emphasizing emerging markets and select commodities that should experience significant growth even in the relatively slow-growth global environment we foresee. By taking *some* risk, our clients will see a return in excess of a risk-free investment position. We believe the same experience that provided our clients a measure of protection and sanity in recent years will give our clients superior returns on a risk/reward basis in whatever investment environment unfolds in the future.