



May 12, 2010

Dear Investor,

On Thursday, May 6, 2010, the stock market, as measured by the S&P 500, expanded its recent pullback with a vengeance as it dropped over 3% for the day after rallying from midday declines of almost 10%. While fear was certainly the undertone for the day, the big declines and subsequent rally happened all within an hour. Although the point damage was largely mitigated, uncertainty and concern remain entrenched in the market.

While the catalyst for the large decline was attributed to an apparent trading error that triggered a technical selloff, it was the uncertain environment regarding the fiscal crisis of several countries in Southern Europe that has created the negative backdrop for the market. Concern over the bailout of Greece has been widely reported, but the emerging anxiety of the market is the potential contagion of Greece's fiscal deficit issues to other European countries and perhaps beyond. The very real concern is if Europe will once again teeter back into the realm of recession, which could have negative impacts to the export portion of U.S. multi-national companies, certainly has the equity markets nervous.

While the fiscal crisis of Greece and other Southern European countries creates market uncertainty, it is important to remember that the events are the after-effects of the 2008 financial crisis and not the start of a new financial crisis. Greece is not alone—it is one of many companies, families, individuals and now even countries that have been casualties of the recent recession. Whether it was a job loss, a home foreclosure, rising debt, the need to cut back on spending or a national fiscal crisis as it is for Greece, there have been many negative consequences resulting from the most severe recession in almost 80 years. That said, these negative events are the effects of the financial crisis we have just been through and not the cause of another new wave of credit concerns and another financial market collapse.

While fear is always an unwelcomed emotion, in investing fear may create opportunity. Since the recovery began back in early March 2009, the S&P 500 has risen approximately 70%, but not in a straight line. In fact, along the ascent, there have been four pullbacks ranging from 5% to 10%, including this most recent market selloff. I would argue that the selloff is not the result of increasing bad news, but rather the market became priced for perfection and perfection was unrealistic. After huge market gains over the last year, expectations grew greater and greater. The bar continued to be raised until the point where, regardless of how strong the economic backdrop was, expectations were greater than reality. The result was a reset in expectations and a pullback in the market. Greece happened to be the catalyst, but the trigger could have been any report or event that did not meet the market's expectations of near perfection. The fact remains that pullbacks, like the one we are currently in the midst of, are healthy as they serve to reset expectations and re-engage nervous, profit-taking bulls back into a recovery.

When wondering how to react to times like these from an investment perspective, let's not forget the fact that the market plunged on what appears to be a trading error and then corrected itself all within an hour. This indicates a market demonstrating stability, not in a freefall. This does not mean we will not get pullbacks and market hiccups like we are experiencing now, as these are both needed to establish a balance between buyers and sellers and to support future, healthy market advances.

Sometimes in periods of fear, investors and the market itself can lose the forest through the trees. While the fiscal problem in Greece, the Goldman Sachs testimony discussions with Congress, and concerns arising from a global tightening of monetary policy have stolen much of the headlines as of late, a full view of the "forest" would show that the overall economy continues to improve. One piece of evidence was released today (May 7, 2010) in the April 2010 employment report. The U.S. economy

lost a total of 8.4 million jobs since the start of the recession highlighted by 22 consecutive months of job losses, but we have added jobs in 5 of the last 6 months to the tune of 528,000 new jobs. In the end, the economic backdrop is on the mend.

The bottom line is that there is a big difference between a pullback and a financial crisis. And there is an even bigger difference between how the market reacts to events that cause a crisis (Bear Stearns, Lehman Brothers, and the credit crisis of 2008) and those events that are the aftershocks of a severe recession, like the situation unfolding in Greece and Southern Europe. There is also a difference between the two definitions of risk: danger and opportunity. We would argue that the latter is far more likely than the former at these levels in the market and at this stage of the market recovery.

With a little patience, the commitment to a well thought out investment plan and a willingness to follow Warren Buffet's sage advice to "be greedy when others are fearful and fearful when others are greedy" could result in turning the tone of this market pullback from danger to opportunity. The selloff we are experiencing, which is the fourth one since the market bottom of March 2009, serves as a reset of market expectations. It could provide the next springboard for the market to rally to higher levels over the coming months before running into the growing headwinds of rising rates, contested mid-term elections, and tougher year-over-year earnings comparisons for companies later in the year. For now, the market is in the midst of a good, old-fashioned pullback and this is not the start of a financial crisis. As such, we feel that the mending economic backdrop supports cautious opportunistic investing at these levels in the markets. As always, if you have questions, I encourage you to contact me.

Best regards,



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