



Investment Overview

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Economic and Markets Summary

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First Quarter 2010

The Economy

The economy turned the corner during the third quarter of 2009, gaining a positive reading of +2.2% for Gross Domestic Product. This turnaround followed one of the longest and most painful recessions in the post-World War II era. The most recent recession began late in 2007. Fourth quarter GDP surged ahead at a 5.6% rate. However, the recovery is not nearly as strong as this number would indicate. Inventory building in the fourth quarter gave a temporary boost to growth, which should detract from GDP in the first and second quarters of 2010. Economists are forecasting growth of around 2.5% to 3% for these two quarters. The first estimate of GDP for the first quarter of 2010 will be released on April 30.

There are still question marks and doubt in some quarters regarding the strength and sustainability of the recovery. The liftoff is sub-par compared to past cycles. The fiscal and monetary stimulus has run its course. Consumer spending will remain tepid, owing to continued weakness in housing and autos, two areas that usually lead the recovery. Lending and credit availability will remain constrained. Employment growth remains negative. All the above are points made by those that fear the possibility of a double-dip to the economy – one that throws us back into recession.

However, this is the minority viewpoint at this time with most economists believing the economy is on solid footing with the recovery durable, if initially uninspiring. Two areas that are showing surprising and uncharacteristic strength at this time are manufacturing, including capital spending, and exports. The economic indicators that have been released for these categories have shown consistent

positive readings for several months in a row, enough to inspire confidence of a sustainable rising trend.

Other economic indicators released on a monthly basis are somewhat mixed with a bias toward favorable for the industrial side of the economy and not-so-favorable for the consumer side. The most important of the indicators is the monthly employment report, which is usually released the first Friday of the month. This indicator has shown improvement but still remains weak. At last reading on March 5, the unemployment rate stood at 9.7%, still uncomfortably high. New job creation showed jobs still being lost at -36,000. However, analyzing past economic recoveries has taught us the economy can show sustainable progress even with high unemployment and job losses as long as there is a gradual pattern of improvement going forward.

Therefore it will be important to continue monitoring the monthly economic indicators as they unfold, particularly the employment report.

One monthly economic indicator that has a good forecasting record is the Conference Board's "Leading Economic Indicators" series. The LEI has been expanding and showing positive readings for ten months in a row. This is the longest positive streak for this series since 2004, and suggests that the economy remains on track for continued modest growth in 2010 of around the 3% level for GDP. There are ten indicators making up this series, and for the past six months, 8 of the 10 were positive on balance.

The release of the "Beige Book" report by the Federal Reserve in early March also confirms the notion that the economy is undergoing modest improvement. This is a roundup of anecdotal reports from the 12 regional Fed banks. Its main purpose is to inform the Federal Reserve

"The latest reports show the economy improving in 9 of the 12 Fed regions in January and February..."

Governors and policy makers on economic trends ahead of upcoming Federal Open Market Committee meetings.

The latest reports show the economy improving in 9 of the 12 Fed regions in January and February, while being hampered by snowstorms, particularly on the east coast. "In most cases the increases were modest," the Fed stated. Consumer spending improved slightly in many districts. Commercial real estate and loan demand were weak and labor markets soft. Hiring plans still remained generally soft and pressures on employers to raise wages were minimal. The reports said non-financial services were steady or improved in the majority of the districts and manufacturing increased further in most areas. Housing markets showed mixed improvement, softening in three districts including New York. Several contacts were apprehensive about future home sales once the credit expires on April 30th. Poor weather conditions were often cited as a reason for softness, and that could possibly result in above average activity with the coming of spring.

International economic conditions received some unwanted attention during the first quarter of 2010. Most notable was the credit crisis and the potential for a sovereign debt default by Greece, which could possibly ripple to other countries such as Spain and Portugal. This sent shock waves through the currency and credit markets as well as stock markets around the world. As a result, the dollar again assumed its safe haven status and strengthened considerably on world markets. This came at the expense of the Euro and other individual country currencies.

Greece came under intense pressure from the European Union and financial markets to develop an austerity package which brings down the budget gap that ballooned to 12.7% of GDP. The EU wants to see that gap cut to 8.7% this year and below 3% by 2012. This would allow Greece to continue receiving financial support including investors buying Greek government bonds. Those goals have to be met by raising taxes, cutting government spending, freezing civil service wages, cutting public sector entitlements and closing tax loopholes. This comes with the risk of civil unrest. Greece is now finding out there is a day of reckoning for the long period of financial mismanagement. The question going forward is, will other countries, big and small, following similar paths be forced into similar painful courses of action largely determined by outside parties?

Interest Rates

Interest rates fluctuated in a narrow range during the first quarter of 2010 and did not finish too far above or below year-end levels. The sovereign debt crisis involving Greece was constantly in the news, helping to hold down U.S. Treasury rates, as these securities were in heavy demand by foreign investors seeking the safety and liquidity of U.S. debt. This resulted despite the heavy calendar of new offerings of U.S. Treasury debt that came to market to finance the widening budget gap of the Federal government. Fears of future inflation increases could not

bring about higher rates from very low levels. However, going forward intermediate and long rates could begin to move higher.

A self-sustaining economic recovery should eventually lead to higher rates. If and when labor markets improve, inflation fears would not be far behind, also suggesting higher interest rates. If the international crisis is resolved and the dollar begins to weaken again, this could also tip the scales in favor of higher intermediate and long-term interest rates. Finally, a deluge of supply could keep upward pressure on rates with the government expected to bring \$2.5 trillion in new debt to market in 2010.

As always, market forces will determine the course of intermediate and long-term interest rates. Short-term interest rates, on the other hand, are controlled primarily by the Federal Reserve. The Fed, through its monetary policy operations, has the ability to raise, lower or hold steady short-term rates. Since December, 2008 the Fed has held short rates steady at the lowest rates possible in order to help bring the economy out of recession and heal the financial system. Going forward these rates can only go one way, and that is up. The question is, when do rates start rising and over a period of time and how high do they go?

The movement of interest rates and the change in the yield curve can be seen in the table below, which shows various rates at the end of 2009 and the end of the first quarter of 2010.

%	Treasury Bill		Treasury Notes & Bonds			FED Funds
	3 mo.	1 yr.	5 yr.	10 yr.	30 yr.	
12/31/09	0.05	0.41	2.63	3.80	4.62	0.-25
03/31/10	0.15	0.38	2.56	3.83	4.72	0.-25

Yield spreads between government and corporate bonds continued to narrow during the quarter. Heavy demand by investors for individual bonds, due to near zero yields offered by money market funds, continued. In the face of a small supply of new corporate bonds, spreads shrunk to very low levels as flows from money going into bond mutual funds continued unabated. The movement in interest rates created generally positive returns for various bond fund categories during the first quarter of 2010. Below are some examples of different bond fund returns according to the *Wall Street Journal*.

Year-to-Date Percentage Returns (as of 03/31/10)			
Barclays US Aggregate	+1.78	Investment Grade - Short	+1.57
U.S. Gov't	+1.40	High Yield Taxable	+4.82
GNMA	+1.90	Municipal Bond Index (7-12 yr)	+1.00

During the first quarter, commodity prices were not as volatile as those experienced in 2009. The price of oil, which ended 2009 around the \$80 per barrel level, fluctuated narrowly and showed very little change standing at \$83 per barrel at the end of the first quarter of 2010. The price of gold also showed below average volatility. The quote for gold at the beginning of 2010 was just shy of \$1,100 per ounce. On March 31 gold closed at \$1,113.

The Federal Open Market Committee of the Federal Reserve had two meetings on their schedule during the first quarter of 2010. The first meeting concluded January 27 with Fed Funds remaining at a range of 0 – 0.25%. The post-meeting comments remained very similar to previous meetings, with officials repeating the line from the previous six statements signaling a commitment to hold interest rates at exceptionally low levels for an extended period of time.

The second meeting concluded on March 16. Again Fed Funds were held at the same range of 0 – 0.25%. Post-meeting comments deviated little. The FOMC again emphasized that the economy warranted exceptionally low levels for the Fed Funds rate for an extended period. The FOMC noted “the pick-up in economic activity and financial market conditions have become more supportive of economic growth. The Committee expects that inflation will remain subdued for some time.”

The Stock Market

The stock market has come a long way from where it stood in mid-March 2009. At that time on the days before the March 9 low, the mood was terrible. The Dow Jones Industrials had plunged to a 12-year low, which eventually bottomed at 6,547 on March 9. The prevailing thought was that the stock market would continue the worst decline since the depression of the 1930’s.

The decline had been unprecedented with so much damage occurring in a short period of time. The all-time high was set October 9, 2007 when the DJIA topped out at 14,164. Then the bursting of the housing bubble, the ripples of the financial and credit crisis, the plunge in earnings and fears of global deflation and economic meltdown sent stocks on a downward trajectory.

However, some stock investors, at the March 9, 2009 low sensed a positive turn in the economy and the beginning of a healing process in the financial system and world economy. Stock markets shifted to the buy side to take advantage of the bargains that developed as a result of the severe bear market. The turnaround and the powerful rally that ensued caused the broad stock market, as measured by the Standard & Poors 500, to finish 2009 up 26.5% with the Dow Jones ending the year at 10,428 and the S & P 500 at 1,115.

That set the stage for a milder, less-volatile beginning for stocks in 2010. After initial strength during the first half of January, the latter half of the month saw the beginning of

a stock market pullback. The stock market was in need of a consolidation period. A needed correction of 10% from the strong gains recorded during the last three quarters of 2009 would be desirable. While the correction did not approach 10%, the drop from the January 18 high to the February 8 low produced a consolidation of nearly 8% and set the stage for renewed stock market gains for the balance of the first quarter.

For the quarter the DJIA closed at 10,857, achieving a gain of 4.82%. The S & P 500 ended at 1,169, producing a total return of 5.39% for the quarter. The NASDAQ composite stood at 2,397 on March 31 and recorded a gain of 5.91%. International indices lagged the domestic indices for most of the first quarter, but made up some ground near the end of the first quarter of 2010.

Below is a table showing percentage returns year-to-date for various equity sectors and investment styles as computed by Lipper Inc., and featured in the *Wall Street Journal* on a daily basis.



Stock Fund Indices

As of 03/31/10

Large-Cap Growth	+4.29
Large-Cap Core	+4.83
Large-Cap Value	+5.74
Multi-Cap Growth	+5.93
Multi-Cap Core	+5.69
Multi-Cap Value	+6.18
Mid-Cap Growth	+7.17
Mid-Cap Core	+7.94
Mid-Cap Value	+8.35
Small-Cap Growth	+7.02
Small-Cap Core	+7.63
Small-Cap Value	+9.54
Equity Income Fund	+5.03
Science & Tech Fund	+3.29
International Fund	+1.88
Balanced Fund	+3.84

Regarding the domestic stock market, below is a chart of industry sectors ranked by percentage change by Bloomberg Research at the end of the first quarter.



Percentage Gain by Stock Sector

1st Qtr.

1. Industrials	+12.45
2. Financials	+10.82
3. Consumer Discretionary	+10.05
4. Consumer Staples	+5.04
5. Health Care	+2.89
6. Basic Industry	+2.49
7. Technology	+1.67
8. Energy	+0.08
9. Utilities	-4.61
10. Telecommunications	-5.66

While extreme volatility has been present in the stock market over the past couple of years, over a longer time frame this has not been the case. Looking at the stock market over a 10-13 year period, stocks have been in a flat trading range. In other words, stocks on balance have gone nowhere from a macro standpoint. This is true for the many stocks that have shown consistent year-to-year increases in earnings over this time period.

Wal-Mart is a good example of a stock that has gone nowhere over this period in the face of rising earnings and dividends. Although Wal-Mart cannot be the fast grower it once was, it still should experience some growth making it a seemingly attractive investment with a low price/earnings ratio at its current price. Other stocks fall into this category also, providing some optimism that the next ten years should be better for these stocks and the stock market in general than the past 10-13 years.

Fund Results as of March 31, 2010

Equity Funds

	Quarter Return	12-Month Return
Allianz NFJ Large Cap Value	+4.56%	+49.49%
Allianz RCM Mid Cap	+8.92%	+63.58%
Fidelity Adv Eqy Income	+5.99%	+54.97%
Goldman Sachs Mid Cap Value	+8.67%	+59.55%
Janus Adv Intl Growth	+8.56%	+79.55%
JP Morgan Mkt Exp Idx Select	+9.26%	+66.14%
Lazard Emerging Markets	+6.05%	+84.16%
Stratus Growth Portfolio	+4.40%	+42.50%
Templeton Inst Foreign Equity	-0.62%	+53.64%
Thornburg Int'l Value	+1.91%	+50.35%
Vanguard 500 Index	+5.35%	+49.73%
Vanguard Morgan Growth	+5.16%	+49.93%
Vanguard Small Cap Index	+9.65%	+72.54%
Vanguard Strategic Equity	+7.13%	+62.88%
Idx: S & P 500	+5.39%	+49.77%
Idx: Russell 2000	+8.85%	+62.77%
Idx: EAFE	+0.98%	+55.16%
Idx: NASDAQ Composite	+5.91%	+58.36%

Fixed Income Funds

PIMCO Total Return Fund (Inst.)	+2.97%	+15.49%
Stratus Gov't Secs	+0.96%	+3.09%
Templeton Global Bond	+6.44%	+26.62%
Vanguard GNMA	+1.94%	+5.24%
Vanguard Infl-Prot Secs	+0.36%	+5.65%
Vanguard Total Bond Idx	+1.69%	+7.35%
Idx: M.L. Int Term Bond	+0.98%	+1.07%

Past performance is no guarantee of future results.



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