Weekly Market Recap **February 8, 2010**

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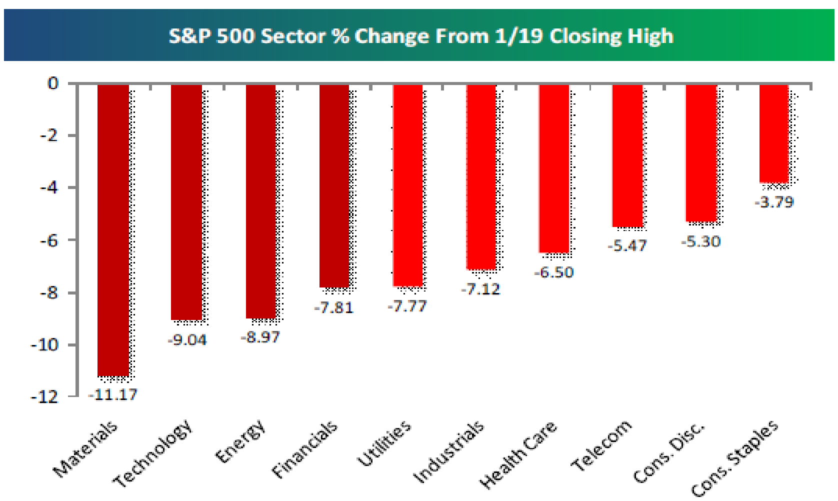
Solid earnings and better guidance from companies ranging from Cisco to Emerson Electric (information and industrial economies) failed to stem selling related to uncertainty emanating from Greece and implied sovereign risk.

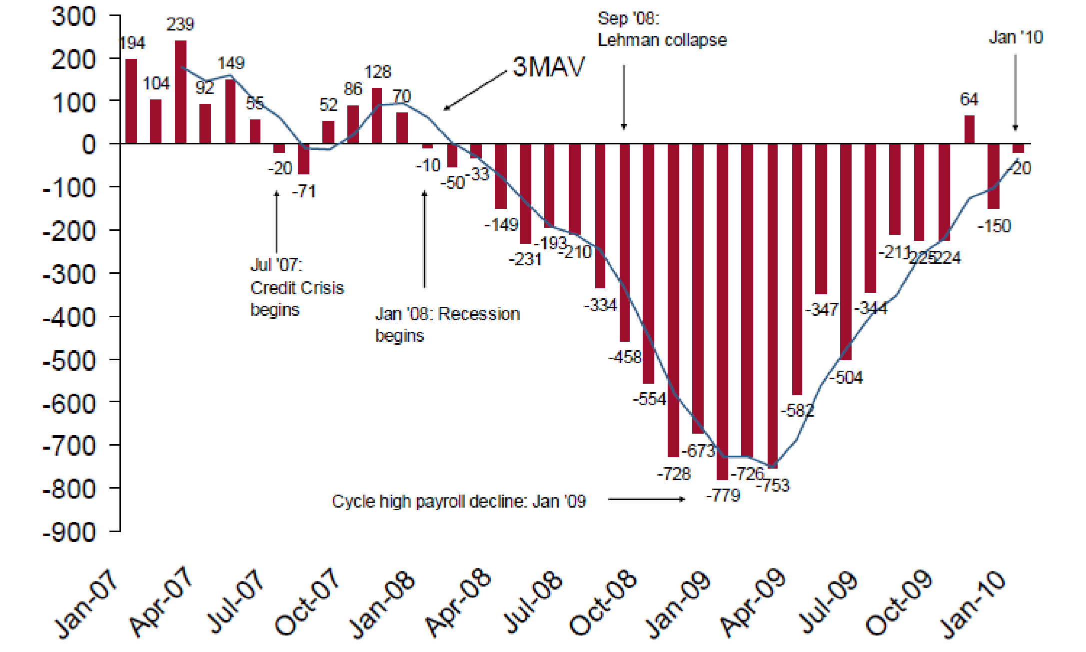
Last Week

- The Dow Industrials gave back their 230-point gain achieved on Monday and Tuesday, closing the week 55 points or 0.5% lower
- The S&P 500 declined 0.7%, its fourth straight weekly loss. US stocks have lost almost 8% in a month, with sector performance mostly following an "as expected" pattern based upon perceived economic exposure. From Bespoke Investment Group:



- NASDAQ dipped 0.3%
- The Russell 2000 small company index under-performed by falling 1.5%
- Dow Transports were off 1.9% while Utilities shed 2.3%
- Banks also were harder hit than most, with the BKX barometer closing 3.7% lower
- Only 11 of 30 stocks in the Dow Industrials managed gains, led by **Cisco** (+5.5%), Alcoa (+3.5%), **Kraft** (+2.8%), **McDonalds** (+1.5%), and IBM (+0.9%). Laggards included Merck (-3.8%), **Pfizer** (-3.8%), Boeing (-3.6%), 3M (-2.4%), and **Verizon** (-2.3%)
- The dollar rallied another 1.2%
- Which helped gold fall another $29.70/ounce, to $1053.50
- Oil briefly fell below $70/barrel but finished the week at $71.19, off $1.50 on the week; that's -12.9% in 4 weeks
- Copper (the metal with the "PhD in Economics") lost 4.1% on the week
- Most foreign markets also fell, including European bourses directly in the Greek sphere of influence (Germany -3.1%, France -4.7%) but also higher beta markets like Brazil (-4.0%) and Shanghai (-1.7%)

- A “better” monthly jobs report highlighted the economic news, though revisions left many to question whether the dip to 9.7% unemployment from last month’s 10.0% was as good as advertised
  - The Employment Survey indicated that the US lost 20,000 jobs in January
    - November and December were revised lower by a modest 5,000 combined, but November now shows a sharp +64,000 gain, breaking a 25-month streak of job losses. The pattern of improvement is clear from the Credit Suisse chart below, regardless of the ongoing debate about details, albeit we are still in “less bad” rather than “improving” territory



Source: BLS, Credit Suisse

    - The annual “benchmark revision” was larger than expected, as the Bureau of Labor Statistics essentially confirmed its birth/death model (which assumes job creation by small businesses) is flawed at turning points – 930,000 jobs previously counted between April 2008 and March 2009 were wiped away, versus a -824,000 preliminary estimate. With other technicalities, the revised data show 8.4 million jobs lost since the December 2007 cycle peak, versus 7.2 million previously reported
    - Factory payrolls rose 11,000, the first up-tick in three years, temporary help posted another solid gain at +52,000 (leading indicator), and the average work week inched up to 33.3 hours
    - The Household Survey (from which the Unemployment Rate is based) offered up more good news – it showed 541,000 new jobs were created in January, compared to a 111,000 gain in the labor force (thus the decline in unemployment)
    - And the “U-6” broader under- and un-employed rate fell to 16.5% from 17.3%
    - Several observers are wondering how the entire gain in the Household Survey was accounted for by women (+529,000), while males between 25 and 54 years old lost 114,000 jobs. It does seem to stretch the imagination. So relative to expectations, we will take the half-full approach and call the numbers supportive of an ongoing recovery, but realistically, it’s hard to find great cheer, when we see charts like the one from Gluskin Sheff below

CHART 1: ADULT MALE EMPLOYMENT BACK TO LEVELS LAST SEEN IN JUNE 1996

United States: Employed: Men 25-54 Years Old (millions)

Source: Haver Analytics, Gluskin Sheff

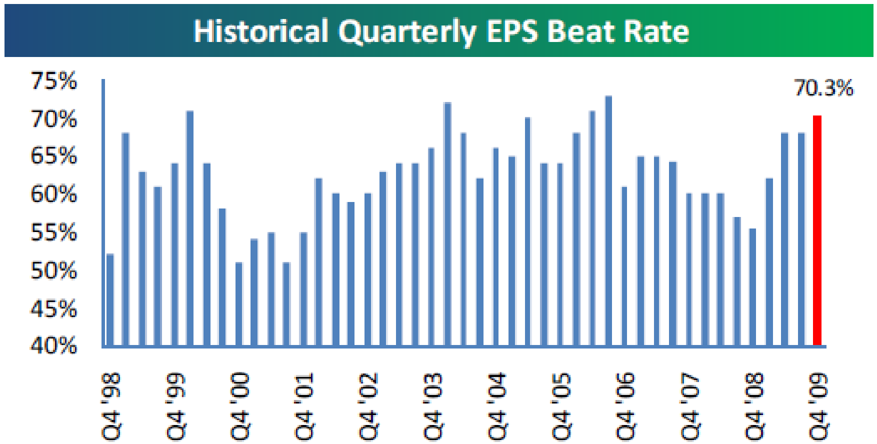
- o The ISM Manufacturing Survey was strong, shooting to 58.4 from 54.9. The Orders (65.9) and Production (66.2) components were particularly upbeat, though the reading on higher Prices (70.0) actually led the improvement
- o Consumer spending rose a modest 0.1% in December, versus a 0.4% improvement in personal income, pushing the Personal Savings Rate higher to 4.8%. The year averaged 4.6%, highest since 1998 and the biggest one-year gain (deleveraging at work) in at least 50 years, according to Northern Trust
- o US light vehicle sales fell to a 3-month low 10.78 million annualized rate in January, from 11.25 million last month
- o The Fed's Senior Loan Officers' Survey showed that banks are no longer tightening lending conditions to large firms, although (by a whisker) conditions continued to get rougher for small businesses in December
- o Productivity was reported to be up 6.2% (annualized) in the fourth quarter (vs. 7.2% in Q3 and 6.9% in Q2), the best in 50 years – and that was before accounting for the benchmark job revisions which could send send the figures into an incredible (as in, hard to believe it's accurate) double-digits
    - The 4Q was 4.3% above the prior year, as output fell 3.5% but hours worked plunged by 7.5%
    - Really not wanting to pick up bearish commentary, but you have to give credit to David Rosenberg for asking pertinent questions surrounding a +5.7% GDP report (and +7.2% output growth in the non farm business sector) amidst 452,000 quarterly job losses – it's not necessarily impossible, it's just never happened before – "normally," Mr. Rosenberg says after parsing 60 years of data, +7% quarters are accompanied by 650,000 new jobs created
- o Friday afternoon's Consumer Credit report was thought to be "good," in that it showed a decline at only a 4 ¾% annual rate ("revolving" or credit card debt at -13%)

- Despite economic assumptions we would consider aggressive (straight-up economic growth for ten years, inflation never exceeding 2.1%, no further losses from Fannie Mae and Freddie Mac, etc.), President Obama's federal budget proposal that showed the deficit would still exceed $1 trillion by 2020
    - o The deficit is projected to rise to $1.6 trillion this year
    - o Net interest expense is pegged to rise from $188 billion in fiscal 2009 to $840 billion in 2020. Repeat, that's just the interest, and it's an "improvement" from the "baseline" scenario. At

that point, the CBO calculates interest alone (meaning, we get no *current benefit* out of that spending) will total 3.2% of GDP
    - Credit Suisse notes $468 billion of corporate tax increases are seen over the forecast period, and $969 billion of hikes will fall on upper-income individuals
- Greece is being advised/told to cut its budget deficit from 12.7% of GDP this year to 3.0% by 2012. Tax collectors and customs officers have already walked out to protest the planned austerity measures
    - Among the reasons all these far-off difficulties are newsworthy (as well as confusing!) are not just that Portugal, Spain, Ireland, and the UK are thought to be next in line, but because banks (of course) own sovereign debt; the *Journal* notes that UK banks own $193 billion of Irish paper, and German banks are owed $240 billion by Spain
    - The EU has an "anti-bailout" clause designed to help exert discipline on its members (Ed Yardeni mentions that Greece had been submitting phony budget numbers, which didn't help!), but this is the monetary union's first big test since it was formed in 1999. We assume the IMF will step in to provide some cover, as well as funding
- Goldman Sachs diffused some criticism when it released 2009 bonuses for its CEO Lloyd Blankfein and CFO David Viniar, both of who will receive "only" $9 million in stock (versus rumors up to $100 million for Mr. Blankfein)
- The SEC again settled charges against Bank of America, which withheld key information on Merrill Lynch losses from shareholders who voted to approve their merger at year end 2008. This time BAC was fined $150 million instead of the original $33 million (further victimizing shareholders who have already been victimized, as Judge Rakoff keenly observed when denying the first rug-lifting sweep?) Immediately thereafter, NY Attorney General Andrew Cuomo brought civil charges against former CEO Ken Lewis and CFO Joseph Price over the same (alleged non-) disclosures
    - The roles of the bank's legal advisors Wachtell Lipton, old general counsel Timothy Mayopoulos (who was dismissed during the proxy discussions in question), his replacement Brian Moynihan (who hadn't practiced law in many years; now elevated to CEO), and of course then-Treasury Secretary Hank Paulson and still-Fed Chief Ben Bernanke make this a more-interesting-than-most investigation. So far it does not seem like anyone wants the case to make it to trial

This Week

- Another key protagonist at the time, then-Merrill CEO John Thain (who helped push through Merrill bonuses despite mushrooming losses, all of which would be plugged by us taxpayers, you may recall), has emerged as the new CEO of another TARP beneficiary (for a while), the recently-emerged from-bankruptcy small business lender CIT Financial
- Two sound bite blasts from the weekend news talk shows: Alan Greenspan declared the recession is over (but the recovery will be "slow," said the unbelievably accurate one, who also called the Colts to win the Super Bowl), and Tim Geithner said the US will "never" lose its AAA rating
- Japan's Nikkei index finished 1.1% lower overnight
- The Treasury will be auctioning $81 billion of notes and bonds this week
- Seven of ten earnings reports continue to exceed analyst expectations, an historically high ratio as the chart from Bespoke Investment Group attests, and more managements are guiding up (10.5% of companies) than down (3.5%). The "beats" have been significant, too, by an average 13%, according to David Rosenberg



- With about 2/3rds of the S&P 500 having reported, earnings are up 206% year over year; backing out the Financials, the tally is a more reasonable 16% from 2008's very depressed conditions – still, encouraging
- Economic news is relatively sparse, with Thursday's jobless claims highlighting the schedule:
  - Nothing today
  - Tomorrow brings ICSC Chain Store Sales, NFIB Small Business Optimism, Wholesale Inventories (consensus +0.5%), Job Openings and Labor Turnover Survey, and $40 billion in a 3-year Treasury note auction
  - Wednesday follows with MBA Purchase Mortgage Applications and December Trade Balance (cons: -$36B). Fed Governor Tarullo also will be speaking
  - Retail Sales (cons: +0.4%, +0.6% ex autos), initial jobless claims (cons: -460K), and Business Inventories (cons +0.3%) will be reported Thursday. The Treasury also will auction $16 billion of 30-year bonds
  - Friday concludes with the latest University of Michigan reading on Consumer Sentiment (cons: 75.0).
- Conferences and Shareholder/Analyst meetings of interest:
  - Monday: **Walgreens**, Humana, Wellpoint at UBS Global Healthcare Services Conference; Lincoln Educational, F5 Networks, Penn National Gaming, Rackspace Hosting at Deutsche Bank Securities Small and Mid Cap Conference
  - Tuesday: Odyssey Healthcare, Medco Health Solutions, Aetna, Sun Healthcare at UBS Global Healthcare Services Conference; Redhat, SAP, Adobe, Entropic Communications at Thomas Weisel Technology & Telecom Conference
  - Wednesday: Ameritrade, Bank of America, Capital One, and Wells Fargo at Credit Suisse Financial Services Conference; American Superconductor, **Flowers Foods**, FMC, Power Integrations at Deutsche Bank Securities Small and Mid Cap Conference
  - Thursday: Zion's Bank Analyst Meeting; Ameriprise, Lincoln National, Met Life, and NYSE Euronext at Credit Suisse Financial Services Conference
  - Friday: Abraxas Petroleum at NAPE Expo 2010
- Hundreds of companies will be reporting earnings the week, including:
  - Monday: Boardwalk Pipeline, CVS, Electronic Arts, Evergreen Solar, Forward Air, Lincoln National, and TW Telecom
  - Tuesday: Biogen Idec, BJ Services, **Coca-Cola**, Cognizant Technology, Coventry, Molson Coors, NYSE Euronext, Warner Music Group, Netgear, and Disney
  - Wednesday: Arcelor Mittal, Coca Cola Enterprises, Dean Foods, Discovery, Elan, ICE, Level 3, Sprint Nextel, Wyndham Worldwide, **Allstate**, Boston Scientific, Protective Life, Prudential and Sierra Wireless

- Thursday: Alcatel Lucent, Expeditors, FLIR Systems, JA Solar, Marriott, **Pepsico**, **Philip Morris International**, Strayer Education, Viacom, Alcon, Alliance Bernstein, BJ's Restaurants, Blue Nile (just in time for Valentine's Day), Buffalo Wild Wings, Cephalon, Cheesecake Factory, Chipotle Mexican Grill, Coinstar, McAfee, and Panera.
- Friday: Allete, HCP, PepsiAmericas, and Ultra Petroleum

CHOICE Portfolio Performance, Net of Fees.

- **Leaders -2.7%** year to date, **+8.4%** cumulative, since inception (1/1/01)
- **Special Opportunities -3.6%** year to date, **+111.8%** since inception (1/1/01)
- **Equity Income -3.4%** year to date, **+65.7%** since inception (1/1/01)
- S&P Total Return -4.2% year to date, -4.3% since CHOICE inception (1/1/01)

- **Enhanced Equity -1.3%** year to date, **+25.3%** since inception (1/1/04)
- S&P Total Return -4.2.% year to date, +8.5% since CHOICE inception (1/1/04)

Who dat? Way to go, Saints! We should have known what the outcome would be, when we saw both Hank Paulson and Alan Greenspan pick the Colts during their "Meet the Press" appearance yesterday.

Have a great week.

George F Shipp, CFA
Chief Investment Officer

Special Opportunities is a concentrated, multi-cap, multi-style portfolio with an objective of capital appreciation through equity selection. Equity Income is a concentrated equity portfolio with an objective of a growing stream of income plus capital appreciation. Leaders is a blue-chip, concentrated equity portfolio with an objective of after-tax returns primarily from capital appreciation. Enhanced Equity is a concentrated portfolio for investors who are comfortable with the trade-offs inherent in selling call options against underlying stock positions. Individual investors cannot directly purchase an index. The S&P 500 is an unmanaged, weighted index of 500 stocks providing a broad indicator of price movements. CHOICE portfolios are separately managed accounts offered by Scott & Stringfellow, LLC., a registered investment advisor and managed by the Firm's CHOICE Asset Management Group. The minimum investment for each account is at least $100,000.