MURRAY
INVESTMENT MANAGEMENT

2nd Quarter 2010 Update

Economic Review

For the third quarter in a row, the U.S. economy posted solid growth numbers rising 2.7% during the 1st quarter of 2010. This was slightly weaker than expected but was additional confirmation of an overall improving economic environment. 2nd quarter GDP data will be released in late July.

The recovery remains fragile, however, as noted by the National Bureau of Economic Research (NBER). In April, the NBER chose not to call an official end to the current recession stating that "although most indicators have turned up, the committee decided that the determination of the trough date on the basis of current data would be premature."

Along with the oil spill in the gulf, the European debt crisis dominated headlines for a large part of the quarter. There are concerns that the European crisis could spill over and upset the U.S. and global recovery. The crisis also highlights the massive debt levels that are held throughout the world (including the U.S.) and the need to have some serious fiscal restraint.

During the quarter, the Fed kept rates in the 0% - .25% range and noted that they will stay that way for an "extended period." Market participants are watching carefully for any change in Fed language as a signal to future rate hikes. The "extended period" language can be interpreted to mean that the Fed expects mild inflation and modest employment growth in the near term.

The U.S. employment situation has shown improvement since 2009 but lost some steam at the end of the quarter with (125,000) jobs lost in June. The unemployment rate did, however, decline to 9.5% from a high of 10.1% in October 2009.

Equity Market Performance

	2Q10	YTD
S&P 500	-11.43%	-6.65%
MSCI EAFE (International index net return)	-13.97%	-13.23%

After strong first quarter performance, domestic equity markets suffered through a tough 2nd quarter (-11.43%) ending down (-6.65%) for the year. Fear and volatility ruled equity markets during the 2nd quarter. Investor concerns included a slowing global economy, loose U.S. fiscal policy (too much debt), debt concerns in Europe (Greece), the regulatory environment (financial regulation) and the May 6 flash crash. These macro events overshadowed the good news that came from strong reported U.S. corporate earnings.

From its high in late April, the S&P 500 closed the quarter down over 15% and is firmly in what many define as a market correction (a 10% move down). From the March 2009 lows, however, the broad market is still up over 50%.

During the quarter, there was a move from risky assets into more conservative assets such as U.S. Treasuries and gold, which both performed strongly. Market volatility increased dramatically and somewhat caused this flight to safety.

With the debt concerns in Europe, the broad International markets have been under pressure with the MSCI EAFE index losing (-13.97%) during the quarter and significantly underperforming domestic markets for the year.

While not as pronounced during the quarter, the year to date performance of different areas of the equity market has demonstrated the benefit of not concentrating capital in one particular area of the market (diversification). Year to date, domestic markets have outperformed the broad international markets, and in the U.S., small cap names have outperformed large caps.

Bond Market Performance

	2Q10	YTD
BarCap US Aggregate Bond (Broad Bond Market)	3.49%	5.33%
BarCap Municipal	2.03%	3.31%
BarCap US Corporate	3.42%	5.79%
BarCap US Corporate High Yield	-0.11%	4.51%
BarCap US Treasury Long	12.17%	13.20%

The broad bond market produced solid results during the quarter. High-yield bonds, however, were under pressure as riskier fixed income securities sold off after very strong recent performance. U.S. Treasuries performed well as investors moved out of the volatile equity market into the safety of these securities.

This is the type of quarter that reveals the importance of having balance (equity and fixed income holdings) in a portfolio. Apart from the high yield space, many investors benefited from fixed income holdings, which provided stability to their portfolios.

Source: Fidelity, bls.gov, Morningstar, BEA.gov, CNBC.com, NBER.com, and federalreserve.gov.
The performance data shown represents past performance, which is not a guarantee of future results.
Return data is as of 06/30/2010. Except as noted, index returns are Total Returns.

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Economic Outlook

With the problems in Europe and some softening of economic data, many are debating the possibility of a double dip recession, but we do not expect that to occur. The concerns seem to be focused on the U.S. employment situation and the ability of the economy to grow without Fiscal (Government) and Monetary (the Fed) stimulus.

In addition, there is specific concern about the ability of the housing market to stand on its own feet without Government assistance. We will be monitoring this and other data over the course of the next several quarters to see how events unfold.

The case for continued growth (and no double dip) centers on an accommodative monetary policy and an improving jobs outlook. Moderate inflation numbers give the Fed the flexibility to keep interest rates low and further stimulate the recovery. Expectations for rate increases have largely been pushed out to 2011 given the fragile nature of the recovery. In addition, as output grows, corporations can only rely on productivity increases for so long before having to hire new workers.

As the economy grows and jobs are created, the recovery can become self sustaining with new jobs causing incomes to rise which fuel additional economic growth. This would allow both the Fiscal and Monetary stimulus to be removed in an orderly manner followed by more sustainable long-term growth.

Market Outlook

It is reasonable for investors to expect market volatility to continue at elevated levels. The uncertainties created by a potential global slowdown, European debt problems and slowing in China are giving investors pause. In addition, the prospects of higher taxes, bigger government, and rising debt are weighing heavily on the U.S. market.

However, investors who are waiting for signs that we are not going to have a double dip will likely miss any sort of potential market rebound. Typically, when we get the economic confirmation that we're not going to get a double dip, the market has already priced that in and has turned up.

While difficult to stomach, increased volatility in the equity markets can improve valuations and create opportunities for long-term investors to add equity exposure at more attractive prices. If corporate earnings continue to grow as expected and the U.S. presses forward in the recovery, there could be an inconsistency between the strength of the recovery and the weak recent performance that equity markets have produced.

We will be watching corporate earnings carefully to determine if the market has become more attractively priced. In addition, we will be closely watching the employment data to see evidence of sustainable increases in consumer spending.

New Roth IRA Rules

Effective January 1, 2010, there are no longer income restrictions preventing high income earners from converting certain retirement plan assets to Roth IRAs. With tax rates expected to rise, the potential for tax-free growth and tax-free distributions make Roth IRAs attractive. If you would like to discuss these changes and consider if a Roth IRA conversion makes sense for your particular situation, please let us know.

Murray Investment Management

If you would like help with establishing an investment plan or would like to schedule a free, confidential portfolio review, please give us a call.

Source: Fidelity, bls.gov, Morningstar, BEA.gov, CNBC.com, NBER.com, and federalreserve.gov.
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