

March 2010

Dear Clients,

The recovery rally that began a year ago continued throughout the first quarter of 2010. US equity indexes, unchanged through the first two months, provided the entirety of their gains in March, finishing up nicely as indicated in the accompanying chart. Economic conditions and financial data points support ongoing improvement globally indicative of a firming recovery supporting the bull case. In contrast, pessimism and fear permeate the investor mindset as evidenced by weak or negative capital flows into equity funds, strong bond fund inflows, and record cash balances. Painful recent memories continue to weigh heavily in decisions concerning risk and asset allocation. We, however, are conservatively positive on the recovery domestically and enthusiastically positive on the recovery in the emerging economies and other resource rich nations.

In more detail, the leading sectors providing the strongest returns in the quarter were the industrials, transports, consumer discretionary and financial groups, as expected in a cyclical economic recovery. Laggards were the telecom and utility segments, also as expected, with the more defensive names lagging the more economically sensitive groups. Commodity markets were more of a mixed bag. Natural gas fell due to increasing domestic supply, oil was up a bit, agricultural prices such as corn, wheat and sugar fell, nickel rose while most other metals were relatively flat including gold and silver. Benchmark interest rates were more or less constant while spreads tightened once again as riskier bond classes were bid up.

As we noted in our previous report, the FOMC continues to provide a more positive tone regarding the health of our domestic economy with each subsequent release. In the revisions made from the January 27th to the March 16th statement we note the labor market is now “stabilizing” versus a less rosy “deterioration ...abating” and business spending “has risen significantly” versus “appears to be picking up”. Coinciding with quarter end the Fed has also ceased buying MBS (Mortgage Backed Securities) and Treasury paper, removing liquidity from the system. We perceive this to be a tacit confident response to a functioning credit market no longer requiring life support. Expect more telegraphed restrictive actions by the Fed as economic conditions improve. Coupled with the evident improvement in economic data, these actions lend support to economic strength.

As the probability of a double dip or W-shaped recovery diminishes, we are not without anxiety. What scares us is not individual company or issue risk, these failures will occur in the portfolio management process and no one security will derail an investor's portfolio. The real threats are those of the large and systematic nature that can adversely affect entire capital markets as did mortgage debt in 2008. Commercial real estate concerns us as it continues to add stress to the balance sheets of the regional banks primarily holding these loans. Forced to mark to market (honestly and realistically), we fear there would be quite a few negative balance sheets and subsequent defaults. Each party seems content to “pretend and extend” these notes in hopes time will heal all. Municipal debt provides some discomfort. With diminished economic activity reducing tax revenue and ever increasing spending budgets, the mathematical conclusion is obvious and we could see failures. The presumption of a federal bailout keeps these yields artificially low. The fed cannot implicitly guarantee all municipal debt and pricing would be adversely affected should a true measure of fiscal health be applied. The ballooning federal deficit is problematic if we are not able to issue debt at favored rates. An increase in the cost of debt servicing could then crowd out other items in the federal budget. As services and entitlements are cut, civil unrest can manifest itself as we are now observing in Greece and other levered economies. These threats are recognized and we do not

believe they will cause a repeat of the recent credit and liquidity crisis but they have our attention. We all heard the warnings about housing yet it took years for the bubble to pop. Consequently we look to minimize exposure to these risks.

We continue to grapple in our investment strategy meetings about the presence and meaning of a bigger and more intrusive government and the impact to our economy, our taxes, and our investment decisions, let alone the rest of our lives. It matters not if you agree or disagree with the measures being taken, the tide has shifted and we must adapt accordingly. For example, healthcare will never be the same. The cost will be imposed via multiple taxes on higher income citizens, mandatory corporate plans, and contributions from industry participants. Ideally, the social benefit will be enormous, however, the hindering effects on economic growth and on the quality of care are harder to predict. We hope act two in the healthcare plan will involve tort reform and a focus on cost benefit analysis in treatment in order to truly improve the system. The increased regulatory impact will create winners and losers for our purposes and we will be actively tuned in to the process.

The financial industry is under extreme pressure from leadership in Washington. A reform bill is currently being constructed that we hope will provide the appropriate regulatory oversight to correct the imbalances that skew the capital markets in favor of insiders, corporate executives and large investment banks at the expense of the shareholders. One would assume the humbling experiences of the past two years would serve as a catalyst for change from the very firms that required government bailouts for their survival. Unfortunately, from what we have witnessed in testimony before congress and observed in practice, it seems to be business as usual. The bailouts have provided the greatest benefit to big financial firms and large corporations at the expense of tax payers and the federal balance sheet. This is not the form of capitalism that enabled our country to achieve economic superiority. Capitalism, in its more pragmatic form is intended to level the playing field and increase competition thereby creating efficiencies in production and consumption guided by natural market forces. Accompanied by appropriate regulatory oversight, societal and ethical concerns can be addressed and protected. There are winners and losers, failure is inherent in the system and must be allowed to occur. Without this selection process the system corrupts and we find ourselves in a state of patronage and cronyism rewarding those polluting the process. This seems to best describe the current state of our large banking concerns and many of our politicians. We hope those with integrity in Washington D.C. can effect the necessary regulation to regain public trust in the capital markets and the participating institutions.

In recap, our advisory portfolios lagged slightly as we maintain a more conservative cash balance and we continue to hold corporate bonds as a measure of safety and stability in response to the aforementioned risks. We continue to become less defensive and more cyclical in our portfolio construction to benefit from the recovery unfolding. Our best performers in the quarter were Shaw Group, Kraft, DuPont and Intel, a much more cyclical mix than in past quarters. Our worst performers were Weatherford, Intl., an oil services company and Public Service Enterprise Group, an electric utility. The former reported less than expected earnings due to project delays and up front costs regarding new contracts. The lumpy nature of the business does not allow for predictable and smooth earnings reports but we are confident they will have continued long term demand due to the increasingly difficult process of extracting enough oil to meet global requirements. The latter, a public utility declined as the belief of higher rates sooner has become conventional wisdom. We still believe the combination of a high, stable and growing dividend and slow but steady growth will reward investors in the future.

As the market, and individual equities rise in price, valuations become less and less attractive for investment. It becomes increasingly important for investors to be nimble and opportunistic in managing their portfolios for safety and appreciation. If the potential return and risk analysis becomes unfavorable we will hold higher levels of cash in our portfolios. However, our longer term strategic tenets have not changed. At appropriate price points we wish to add exposure to those firms and industries that benefit from exposure to a recovering global economy. We will also expand our ADR (foreign companies traded on US exchanges) weighting in particular to include the companies and nations that provide the basic resources needed for global growth. These firms offer

a clear growth profile and substantial appreciation potential. Secondly, these nations are the direct beneficiaries of global trade and their budget surpluses insure a strong currency providing gains against ongoing dollar weakness. We envision enviable economic prosperity in the emerging and BRIC nations in comparison to our domestic profile.

The corporate bond component of our advisory portfolios rose slightly during the quarter with most of the gains probably realized in this asset class. We question the wisdom and perceived safety at this point in the cycle with yields at extremely low levels with only one direction to go from here. In response, we have continued to reduce our bond weighting and the average portfolio duration. We think income investors will do far better with a combination of MLPs, high yield conservative equities and convertibles than in a traditional bond only portfolio. We do not see any compelling reason to commit capital for any length of time at current market rates. As noted earlier there could be opportunities in the Municipal marketplace as a result of default and liquidity constraints. Additionally, the Fed will likely raise rates in the future providing improved yields. We patiently wait for an entry point.

In a tax planning note, individual income and capital gains taxes will be higher in the future. Investors should opportunistically plan to take advantage of current options. This year, all investors are eligible for Roth conversions on their existing IRA accounts without income limitations. The amount rolled over is taxable, payable over two years, however once in the Roth distributions are tax free. Depending on your time horizon it may be appropriate to consider. Capital gains taxes are set to increase in the future. Investors with large unrealized gains should consider sales before year end to realize the lower rate.

As always, protection of investor's principal is our paramount concern. ❖

Equity Market Statistics as of March 31, 2010

<i>Index</i>	<i>1st Quarter</i>
<i>DJ</i>	<i>4.82%</i>
<i>S&P 500</i>	<i>5.40%</i>
<i>NASDAQ</i>	<i>5.68%</i>

**All performance statistics indicate price appreciation and dividends reinvested into the index during the quoted time period.*

US Treasuries

<i>Maturity</i>	<i>Yield</i>
<i>2 year</i>	<i>1.02%</i>
<i>5 Year</i>	<i>2.56%</i>
<i>10 Year</i>	<i>3.83%</i>
<i>30 Year</i>	<i>4.72%</i>

Commodities

<i>Commodity</i>	<i>1st Quarter</i>
<i>Crude Oil</i>	<i>5.5%</i>
<i>Natural Gas</i>	<i>-27.4%</i>
<i>Gold</i>	<i>1.8%</i>
<i>Silver</i>	<i>3.8%</i>
<i>Copper</i>	<i>6.8%</i>
<i>Nickel</i>	<i>34.6%</i>
<i>Aluminum</i>	<i>2.4%</i>
<i>Wheat</i>	<i>-15.2%</i>
<i>Corn</i>	<i>-16.8%</i>