



Each January, your investment team forecasts major themes in both the economy and the market. This exercise allows us to focus on expected changes and also on structuring our clients' portfolios to take advantage of any major themes. We also take the opportunity to review the predictions we made a year ago and to gauge how close we came to the actual mark. 2008 was our worst year of prognosticating, as we did not foresee the tsunami that hit the financial markets. 2009 was much better, with many of our predictions spot on to the actual results. Below is a recap of what we wrote in our January 2009 *Investment Outlook* followed by the actual results.

“The worst quarter for economic activity will be the 4th Quarter of 2008. We expect gradual improvement as we progress through 2009, with positive GDP growth in the 4th Quarter. The NBER will not declare the recession over at any point during the year, but will eventually decide that the recession ended during the 4th Quarter of 2009, marking the longest post-World War II recession.” We missed the mark by just one quarter. 4th quarter of 2008 saw a decline in annualized GDP of 5.5%, followed by -6.5% in the first quarter of 2009. Conditions improved markedly from there as we saw economic growth resume in the third quarter. Time will tell if the NBER declares that the recession ended in the 4th quarter or not. We suspect the economic group will make their official declaration around the mid-point of this year.

“Unemployment will continue to rise throughout 2009. The current rate of 7.2% will rise to over 8.5% by year-end. First-time jobless claims in the 4th Quarter will signal an improvement in the labor market as the number declines from over 500,000 weekly claims to under 400,000 claims.” The unemployment rate rose to over 10%, ending the year right at this mark. First time weekly claims peaked at over 650,000 and have trended to just above 400,000 at year-end. Although we got the direction correct, we were surprised by the magnitude of job layoffs during the first half of the year.

“The U.S. Dollar will continue to strengthen throughout 2009 as our economy performs relatively better than other developed economies. Likewise, our stock market will outperform international markets. Overall, we expect the second half of the year will show marked improvement in investor psychology and the S&P 500 will close the year above 1000 from its current 850.” Despite being correct on our economy performing relatively better than other developed economies, the U.S. Dollar, nevertheless, fell against most major currencies. Generally, there is linkage between a strong Dollar and a strong market. This linkage became inversed throughout the year as the Dollar strengthened into March while our stock market fell 20% in the first couple of months. As our equity market began to climb, our Dollar peaked and began a long slide into the end of the year. The S& P 500 ended the year at 1115 with

the entire rise accounted for in the second half of the year as investor psychology did show marked improvement.

“Finally, we expect a significant rebound in commodity prices from the current distressed prices. OPEC will hold to their lower quotas and a demand/supply imbalance in oil will drive prices to the \$75 target OPEC has declared. Other industrial metal prices will also rise as infrastructure programs begin to come to the market.” This played out as we wrote; OPEC was able to hold quotas and as the global economy began to improve, oil prices rose from the \$40 level to close the year at \$79 a barrel. Along with oil, almost all commodities rose in price throughout the year, including copper which more than doubled in 2009.

As we enter 2010, the macro-economic environment is much different than a year ago as the abject pessimism has given way to cautious optimism. With that in mind, our thoughts for 2010:

After peaking over \$1,250 per ounce, gold will fall in price ending the year below \$900 per ounce. Fear of inflation will be replaced by concern of deflation and, in response, the Fed will continue their current policy of very easy money and close to zero-percent interest rates.

The unemployment rate will remain stubbornly high as more people reenter the labor pool. Despite the unemployment rate remaining near 10%, jobs are added throughout the year as businesses become more confident of a sustained recovery.

Economic growth surprises on the upside for the first two quarters, growing at an annualized rate of above 5%, driven by inventory restocking. Growth in the second half of the year averages just 2.5% leading to some warnings of an imminent double dip recession. Nevertheless, consumer confidence ends the year higher than it began.

The S&P 500 approaches 1,300 during the first half of the year, but stalls out in the fall and ends the year within 5% of its January 1 value.

We wish all a very happy and prosperous New Year.

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