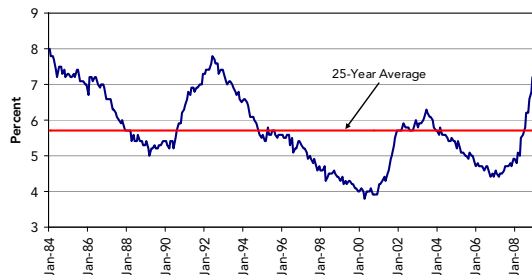


Economic Review

January marked the transition of power in the United States. Barack Obama assumed office, and along with a strong Democratic majority in Congress, began the difficult job of finding a suitable role for the federal government in easing the economic downturn. Timothy Geithner, former New York Federal Reserve leader, became the new Treasury secretary. Tensions escalated between Israel and Hamas after a peace agreement expired. Israeli military forces moved to quell daily rocket attacks launched from Gaza, invoking world criticism against both sides. Oil prices jumped during the campaign, only to fall as tensions eased and tepid forecasts of world demand were revised lower. Europeans were forced to find alternate fuel sources for heat following a dispute between Ukraine and Russia. Russia halted natural gas exports through Ukrainian pipelines, accusing Ukraine of stealing the product, while Ukrainian officials accused Russia of breaking contractual price agreements.

Unemployment Rate

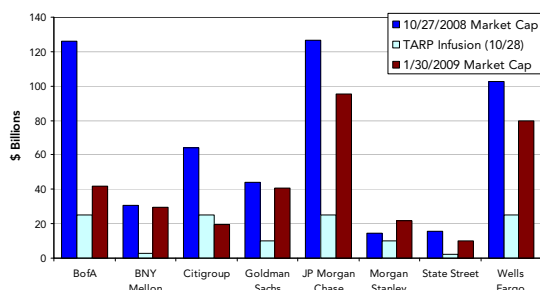


Source: Bureau of Labor Statistics

Daily announcements of mass layoffs weighed heavily on consumers and businesses. The unemployment rate rose to 7.2% in December, and is expected to rise further. Consumer confidence fell to a record low, while consumer spending fell for the sixth consecutive month.

With the Federal Reserve unable to lower interest rates further, its focus shifted to maintaining liquidity and monitoring money supply. Given tame inflation, the Fed has about a year before inflation measures reflect the true impact of its current operations. Inflation currently remains low as energy prices fell from unprecedented highs towards more reasonable levels seen before the energy price bubble.

Bank Stocks Since Initial TARP Infusion

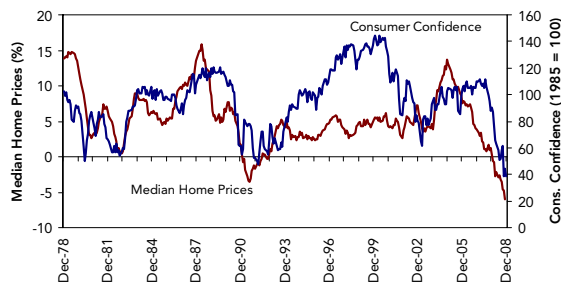


Sources: Bloomberg; General Accountability Office
BofA data includes Merrill Lynch

The commercial paper lending program implemented during October is expected to shrink in scope as maturing securities are rolled to the open markets. The Federal Reserve had up to \$350 billion in the program. The facility remains one of the most successful programs implemented during the current crisis, and helped ease short-term funding and money-market worries.

The Troubled Assets Relief Program (TARP) is likely to return to its original intent of purchasing bad assets from banks to relieve pressure on their reserve requirements. After unsuccessfully trying to spur bank lending by injecting massive amounts of capital into large banks, the Treasury is expected to begin purchases of asset-backed and mortgage-backed securities and collect them into a government run entity that will sell the assets over time. The plan may also include purchases of common stock from banks to offset losses from the bad assets as they become realized.

Home Prices and Consumer Confidence Fall



Sources: Conference Board; Economy.com
Median Price Change is 12-month rolling average of y to y change

Citigroup, which has received \$45 billion from the TARP, announced plans to split into two entities. One would focus on a traditional banking role while the other would handle investments, including its riskier holdings. The bank sold a 51% stake in Smith Barney, its brokerage arm, to Morgan Stanley for \$2.7 billion. Bank of America received an additional \$20 billion, bringing its TARP total to \$45 billion. After closing its acquisition of Merrill Lynch in January, Merrill Lynch reported a loss of \$15 billion for the fourth quarter. BofA CEO Ken Lewis fired Merrill CEO John Thain after the loss was announced, and faced calls for his own resignation for not recognizing or disclosing the losses before completing the acquisition. Shares of Citigroup and BofA both fell to single digits. State Street's shares were hammered after the bank lost \$9.1 billion on asset-backed investments. Investors feared further writedowns at the traditionally conservative bank.

Market Returns

As of January 31, 2009

	January	3 Months	1 Year
S&P 500	-8.4%	-14.1%	-38.6%
Russell 1000 Value	-11.5%	-16.7%	-41.8%
Russell 1000 Growth	-4.8%	-10.8%	-36.4%
Russell 2000	-11.1%	-17.1%	-36.8%
MSCI EAFE	-9.8%	-9.6%	-43.7%
Barclays Agg	-0.9%	6.2%	2.6%
3-Month T-Bills	0.0%	0.1%	1.5%

California taxpayers will have their state tax refunds delayed, as the state is currently relying on borrowed money to pay bills, and cannot afford to issue the billions due to taxpayers. The federal government, which spent billions on the digital TV conversion, attempted to delay the transition until June. The transition is expected to take place on February 17.

Home prices descended further as sales of foreclosed homes increased and now strongly influence market prices across the country.