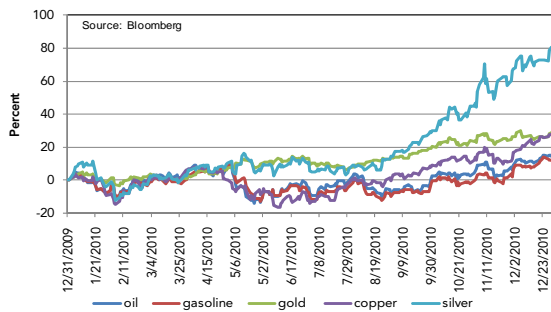


Economic Review

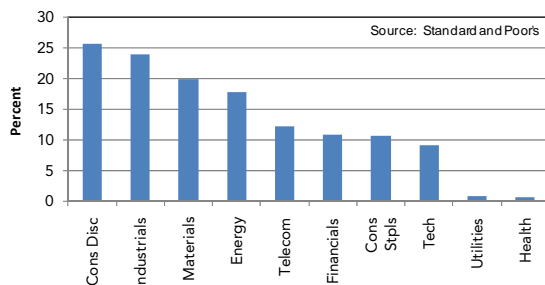
Stock markets surged ahead in December as expansionary fiscal policies were extended and optimism continued. The holiday shopping season was strong, returning to levels last seen in 2007. A powerful blizzard blanketed the eastern United States, shutting down air travel and leaving New York City with unplowed streets for days, although labor issues contributed to snow removal delays. Air travelers were stuck for days, while shoppers seeking after-Christmas deals were deterred by the impassable roads and miserable conditions. The storm's effect on retail sales was estimated at \$1 billion, while airlines lost several hundred million dollars. American Airlines faced off with Orbitz and Expedia over ticket booking platforms and costs, signaling further strife with discount travel sites. The Commonwealth of Virginia scored a victory in Federal Court, as a judge ruled that the individual mandate of the federal healthcare law was unconstitutional. The Supreme Court will ultimately judge the law's fate in the near future. Several states were poised in 2011 to aggressively collect taxes on online purchases, challenging a Supreme Court ruling against such action, as new sources of revenue were desperately sought. The European Central Bank pledged nearly unlimited support to debt-laden countries, and proposed making its bailout fund permanent.

Commodities Rise in 2010



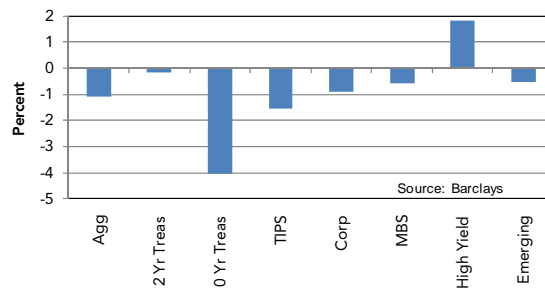
As the 111th Congress wrapped up legislative activity, it passed a two year extension of current income tax rates, as well as the capital gains and dividend tax rates. To secure votes for passage, federal unemployment benefits were extended for an additional thirteen months. The most immediate change for workers is a one year reduction in Social Security payroll taxes from 6.2% to 4.2%, while the estate tax returns in 2011 at a 35% rate. Also included in the bill was the Alternative Minimum Tax patch for 2010 and an extension of the Earned Income Tax Credit. Because the bill was passed late in the year, the extensions of tuition and state sales tax credits will cause the IRS to delay finalization of Schedule A (for itemized deductions) well into February.

2010 Equity Sector Returns



Against the objections of citizens and industry across the country, Congress continued its mandate for ethanol usage in fuel blends. The initial passage of the ethanol mandate was one of the biggest contributors to the rise in food prices over the past few years.

December Bond Returns



The Federal Reserve faced scrutiny as it was forced to open its books on its emergency lending to banks. Merrill Lynch, Citigroup, and Morgan Stanley led banks in the extended overnight lending program, cumulatively borrowing nearly \$2 trillion each. Goldman Sachs' conversion to a traditional bank gave it access to \$600 billion in borrowing. Much of the \$9 trillion in cumulative borrowing went to banks based outside of the United States. With incoming chairman Ron Paul assuming control of the House panel overseeing the Fed, tougher scrutiny is expected, as Representative Paul has been an outspoken critic of the Fed.

Market Returns

	As of December 31, 2010		
	December	3 Months	YTD
S&P 500	6.7%	10.8%	15.1%
Russell 1000 Value	7.9%	10.5%	15.5%
Russell 1000 Growth	5.5%	11.8%	16.7%
Russell 2000	7.9%	16.3%	26.9%
MSCI EAFE	8.1%	6.6%	7.8%
Emerging Markets	7.2%	7.4%	19.2%
Barclays Agg	-1.1%	-1.3%	6.5%
3-Month T-Bills	0.0%	0.0%	0.1%

Much of the Fed's interest rate policy is predicated on the inflation rate, which is currently below the long-term average. However, because over one-third of the CPI is captured by rents (a proxy for housing prices), which have not risen significantly, the real inflation rate seen by consumers is decidedly higher. With gasoline prices breaching \$3/gallon and food prices again on the rise, as well as gold prices hitting 27-month highs, the Fed's easy money policy is inflating prices on many goods.

Following President Obama's announcement that he would seek to extend income tax rates, the bond market began a strong selloff based on prospects for stronger economic growth that lower tax rates tend to favor. Although the legislation will force the Treasury to issue even more debt, investor sentiment was decidedly positive and money flowed into stocks. All major stock indices posted strong gains in December to finish the year in positive territory, with small-cap stocks leading 2010 equity returns.