UNION INVESTMENT MANAGEMENT GROUP

# Monthly Investment Update

January 2010

Although the economy continues along a path to recovery, profit-taking and risk-reduction were themes investors used in January to justify an equity market sell-off. Economically, fourth quarter GDP grew at an annual rate of 5.7%, its best showing since the third quarter of 2003. However, investors seemed discouraged by the fact that a good portion of the quarter's GDP growth was related to inventory adjustments and foreign trade, which indicated that domestic demand remains conspicuously weak. Investors were also spooked by Chinese policy shifts designed to rein in loan demand and the Greek sovereign debt scare that may prove to be prescient for the U.S. as the proposed Obama budget appears to be pushing meaningful deficit reduction out into the future. With a slow recovery expected, policymakers face the prospect of having to unwind stimulus programs in a fragile economic environment.

| Asset Class | Index | 01/31/10 | 12/31/09 | Total Return 1 Month | Total Return YTD |
|---|---|---|---|---|---|
| Domestic Equities | S&P 500 | 1,074 | 1,115 | -3.60% | -3.60% |
| | DJIA | 10,067 | 10,428 | -3.32% | -3.32% |
| | NASDAQ | 2,147 | 2,269 | -5.34% | -5.34% |
| | Russell 2000 | 602 | 625 | -3.68% | -3.68% |
| International Equities | EAFE Index | 1,511 | 1,581 | -4.40% | -4.40% |
| Fixed Income | 2-year USTN | 0.82% | 1.14% | 0.77% | 0.77% |
| | 10-year USTN | 3.58% | 3.83% | 2.19% | 2.19% |

## Monthly Market Commentary

**Equities**:
Equity markets retreated in the first month of the year in opposition to the impressive gains experienced in 2009. The Dow Jones Industrial Average, down 3.32% for the month, turned in its worst performance since February of last year. The technology-heavy NASDAQ, down 5.34%, led the major indices lower in January as investors took profits from the technology sector that was up almost 60% in 2009. International stocks, facing the headwind of a strengthening dollar, also tumbled as depicted by a 4.40% decline in the EAFE index.

**Fixed Income**:
Fixed income investments performed well in the first month of the year as investors, questioning the sustainability of the 2009 equity market rally, bid up bond prices. Short-term rates stayed anchored to a Federal Funds Target Rate that is currently range-bound between 0.00% and 0.25%. Corporate bond spreads remained relatively stable, a welcome sign that recent equity market jitters have not spilled over into credit markets. Government debt, especially mortgage-backed securities, will be subjected to selling pressures as the central bank unwinds its programs to support debt markets over the next few months.

## Bottom Line

**Equities:**
On a long-term basis, stocks offer reasonable value at current levels. Nevertheless, over the next few quarters, stocks may come under pressure as fewer companies may be able to meet elevated earnings expectations. With the relatively fragile economic backdrop in mind, we are focused on high quality domestic companies. Additionally, we are concentrating on companies with broad global reach whose exposure to the U.S. consumer is limited.

**Fixed Income:**
High-quality fixed income investments will continue to serve as a store-of-value in the face of economic weakness. Nevertheless, we expect the likelihood of a rising interest rate environment to increase in the coming quarters as the Fed's efforts to support bond markets draw to a close and investors deal with the prospects of enormous budget deficits. Relative to historic norms, corporate bonds remain attractive despite a significant jump in prices over the last year.


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