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2010 Economic Overview

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[Confidential and Proprietary]

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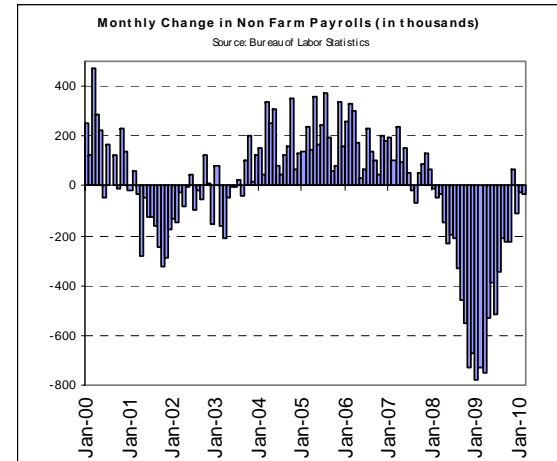
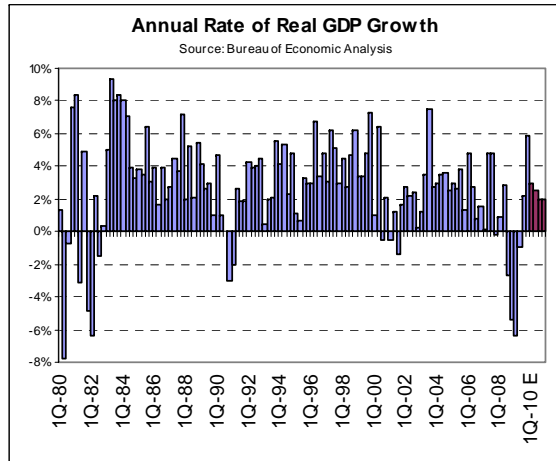
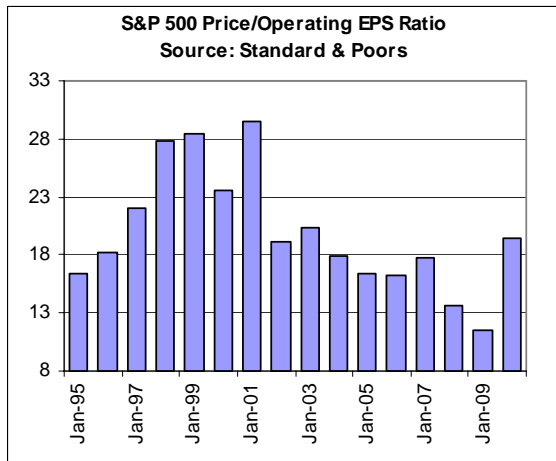
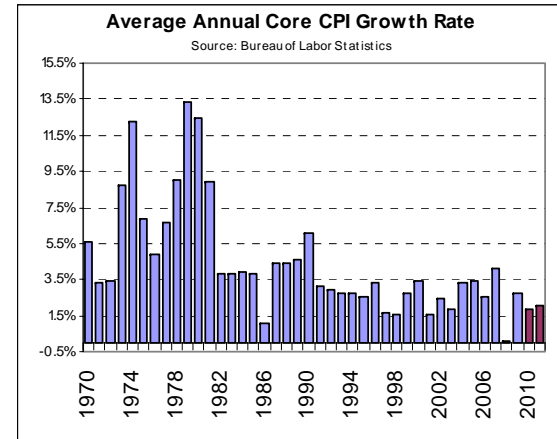
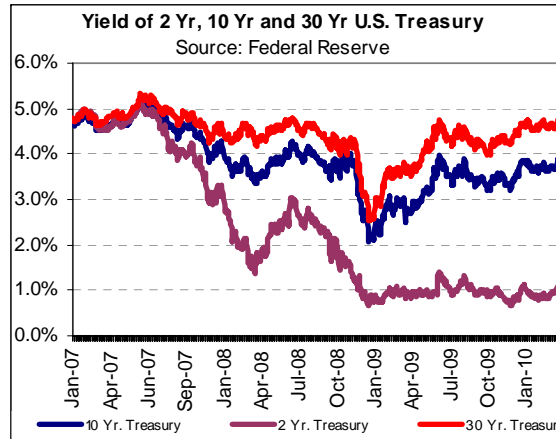
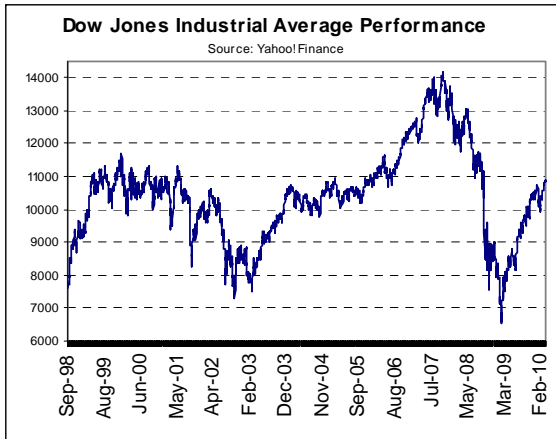
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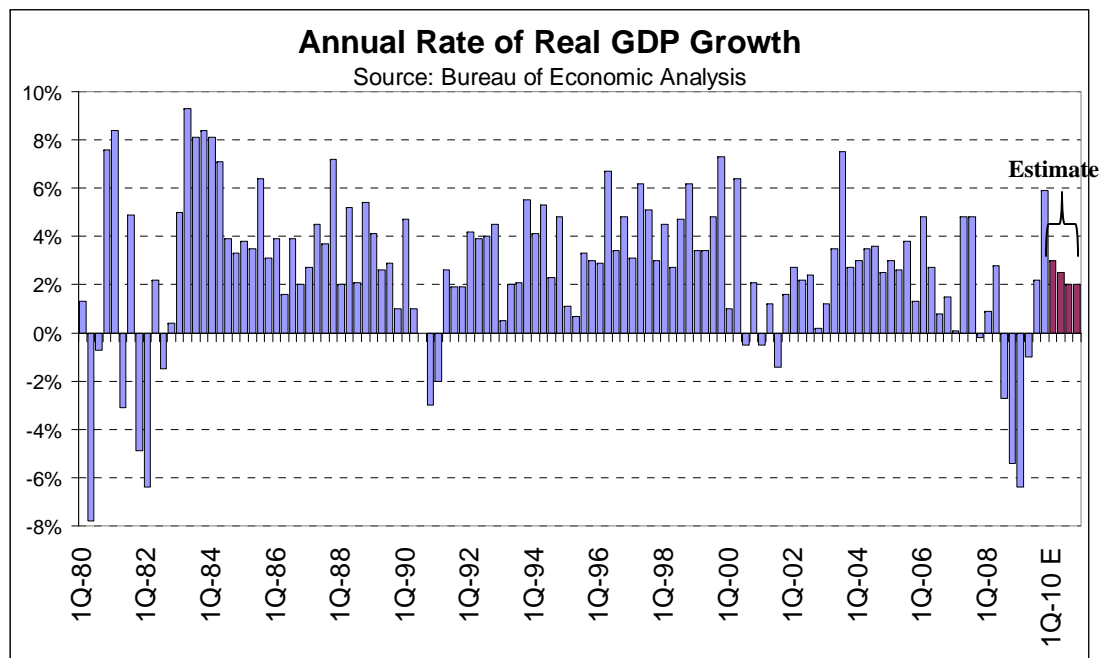
I. ECONOMIC REVIEW

OVERVIEW



U.S. GDP GROWTH

- **GDP growth rebounded in the third and fourth quarters of 2009**, expanding at an annualized rate of +2.2% and +5.9%, respectively.
- Despite a strong finish to 2009, **the economy contracted by -2.4% over the full year period**. 2009 was the first time the economy registered a contraction for a full year since 1991.
- **Economists anticipate tepid economic growth in 2010 and 2011**, coming in at approximately +2.7% and +2.4%, respectively.



U.S. GDP GROWTH

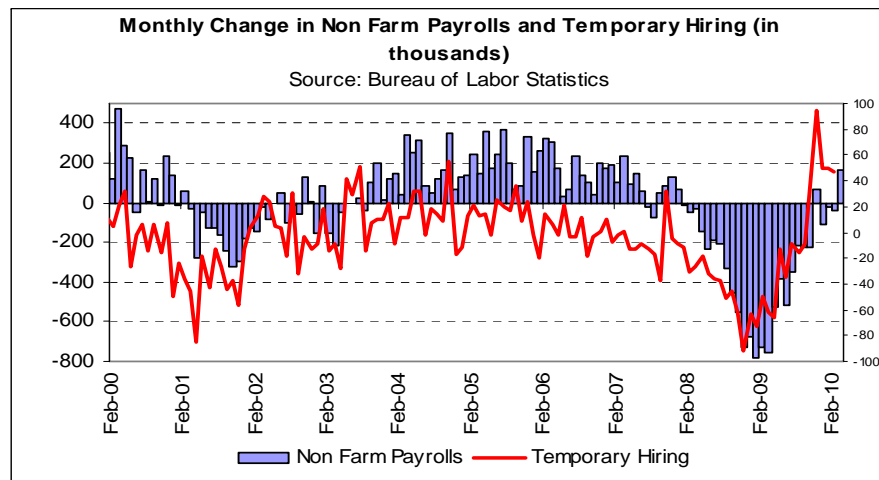
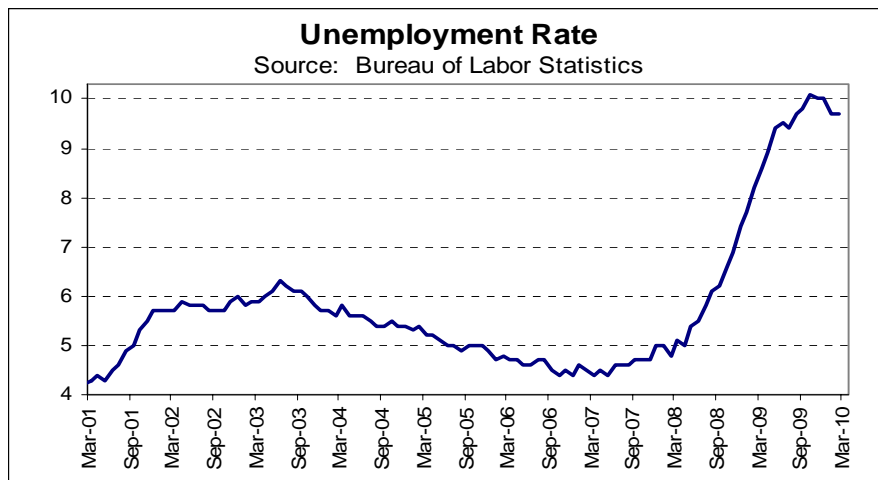
- **Third quarter GDP growth was driven by exports** (due to a weak dollar as the flight to quality trade ended) and personal consumption (stimulus programs) while **fourth quarter growth was boosted by a jump in inventory investment** (restocking after sharp cuts in prior quarters).
- While a return to growth is encouraging, **economists believe many of the catalysts that drove recent economic growth are cyclical and unlikely to continue beyond the first half of 2010**. Gross domestic sales (GDP minus inventory investment), a key metric used to measure real economic growth, remains below +2.5%, an indication the broader economy is still experiencing weakness and is unlikely to stimulate the much needed growth in employment in the near term.
- **GDP growth in the second half of the year will have to depend upon personal consumption and business expenditures** which could disappoint, particularly if unemployment remains at elevated levels, personal savings rate remains elevated and numerous stimulus programs come to an end.

Contributions to Percent Change in Real Gross Domestic Product							
	Annual			Quarterly			
	2007	2008	2009	1Q-09	2Q-09	3Q-09	4Q-09
Government Expenditures	0.32%	0.59%	0.37%	-0.52%	1.27%	0.55%	-0.23%
Imports	-0.33%	0.56%	2.25%	6.58%	2.14%	-2.59%	-2.02%
Exports	0.96%	0.64%	-1.18%	-3.95%	-0.54%	1.78%	2.32%
Inventory Investment	-0.30%	-0.37%	0.37%	-2.36%	-1.39%	0.69%	3.88%
Residential Investment	-1.05%	-1.00%	-0.65%	-1.33%	-0.66%	0.43%	0.13%
Nonresidential Investment	0.70%	0.19%	-2.07%	-5.29%	-1.15%	-0.59%	0.62%
Personal Consumption	1.84%	-0.17%	-0.42%	0.44%	-0.69%	1.96%	1.23%
Total GDP	2.10%	0.40%	-2.40%	-6.40%	-1.00%	2.20%	5.90%

Note: The above data presented does not represent all components of GDP.
Source: Bureau of Economic Analysis

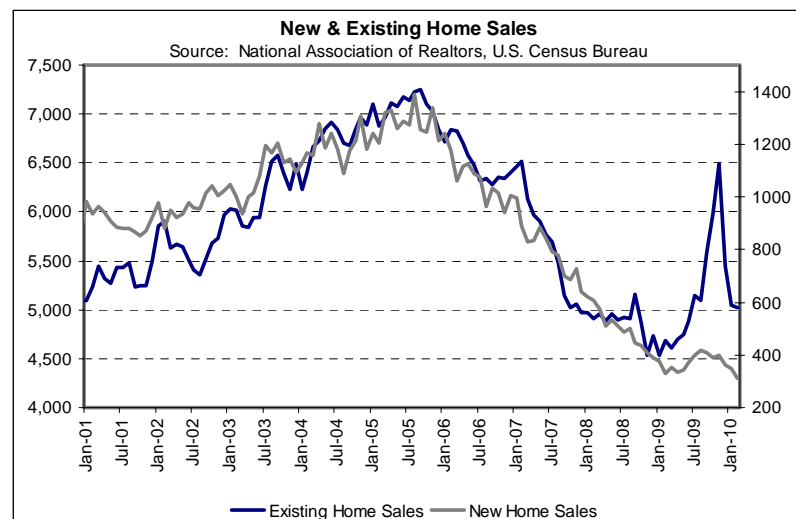
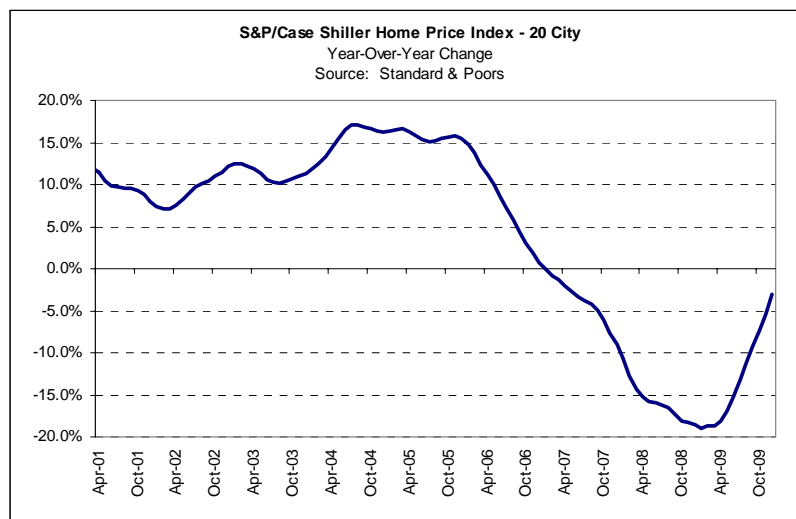
EMPLOYMENT

- U.S. non-farm payrolls rose by 162,000 [123,000 Private and 39,000 Government], indicating a recovery in the labor market could finally be underway. In addition, a **key leading indicator for the job market, temporary hiring, continues to experience strong month to month gains, adding over +300,000 jobs since September of last year.**
- **That said, there is concern about the persistent structural unemployment that exists; the jobless rate remains at an elevated 9.7%.** The duration of unemployment remains at a lengthy 31.2 weeks and unemployment for college-educated workers is 4.9%, while for high school graduates it is 10.8%.
- The prospect of renewed economic growth and the stabilization in the employment situation is encouraging, however economists remain skeptical as to when we will return to more normalized levels of employment, many believe it **could be years before the unemployment rate returns to its historical average of 4% to 5%.**



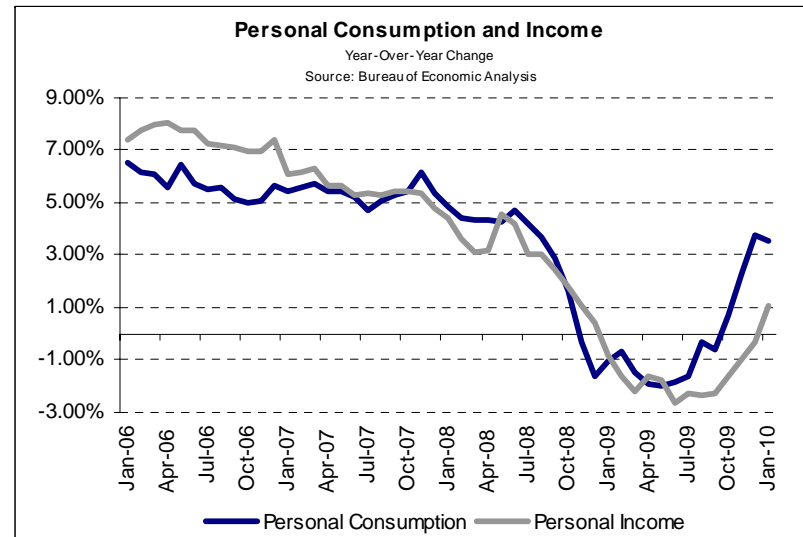
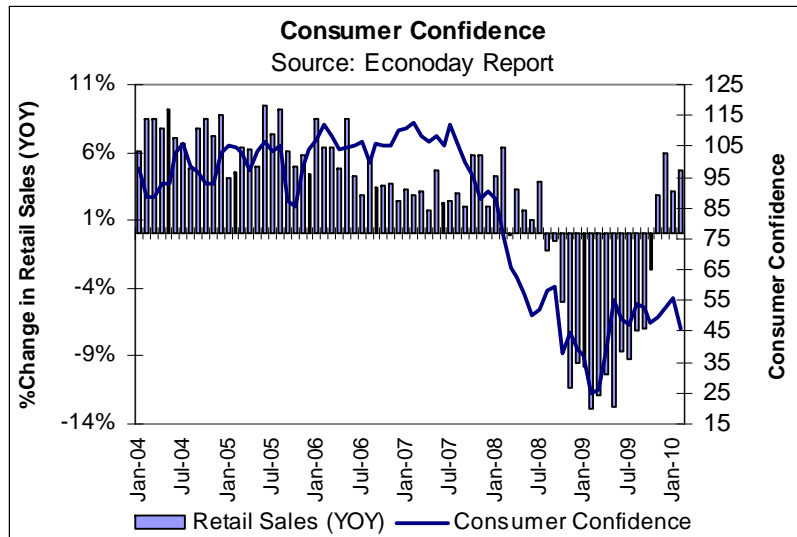
HOUSING

- **The Standard & Poor's/Case-Shiller 20-City Housing Index continues to stabilize and show results that are less worse.** That said, on a year-over-year basis, the index is still in the red and there are concerns we could see a reversal in housing prices in light of recent existing and new home sales data.
- Existing home sales experienced their third consecutive month of declines in February after showing signs of recovery in 2009. **Existing home sales supply jumped from 7.2 months in December to 8.6 months in February, the steepest increase in 20 years.** New home sales have also disappointed in 2010 with the supply of new homes rising from 8.1 months in December to 9.2 months in February despite recording its lowest level of inventory since 1971 at 233,000.
- **Economists have voiced concerns that the housing market could be heading for a double dip in both activity and pricing.** Despite record low mortgage rates, mortgage applications remain weak. In addition, the market for existing homes is saddled with excess supply and likely to get worse in the coming months. Lastly, the new home buyer tax credit is set to expire in June of this year.



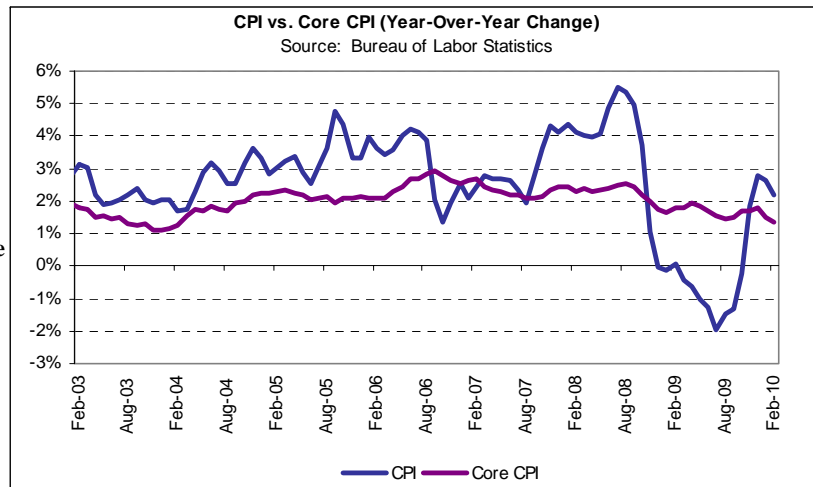
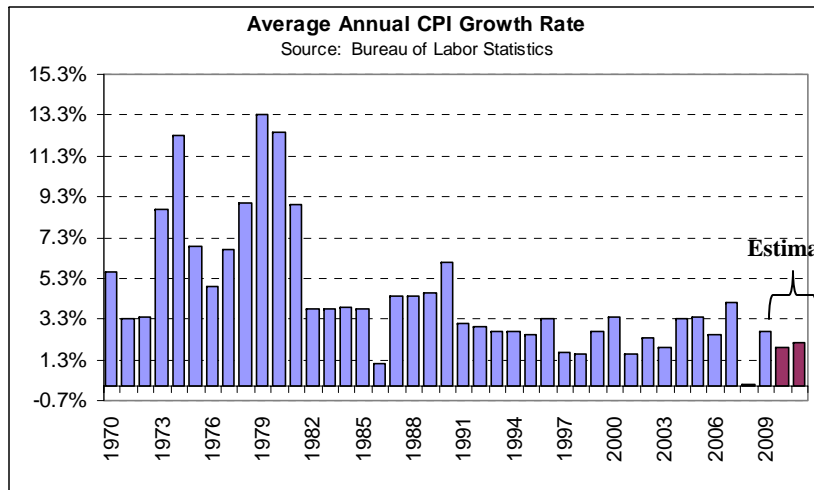
THE CONSUMER

- **The Consumer Confidence Index continues to experience month to month volatility**, most recently jumping by 6 points in February to 52. **While the overall index remains well below its highs experienced in 2007, the trend is upward, as the index has risen off its low of 25 in early 2009.**
- **Personal income and consumer spending have stabilized in recent months.** Personal income on a year-over-year basis rose +1.1% in January while consumer spending rose +3.5%. A solid improvement from 2009 when both were registering negative growth through most of the year. **However, questions remain as to how much of this spending can be attributed to stimulus packages [cash-for-clunkers and first time home buyer tax credits] and whether we just borrowed from future sales.**
- The rebound in the stock market and stabilization of home prices have helped improve the consumers balance sheet, however until the employment situation improves, **consumer confidence is likely to remain volatile in the near future.**



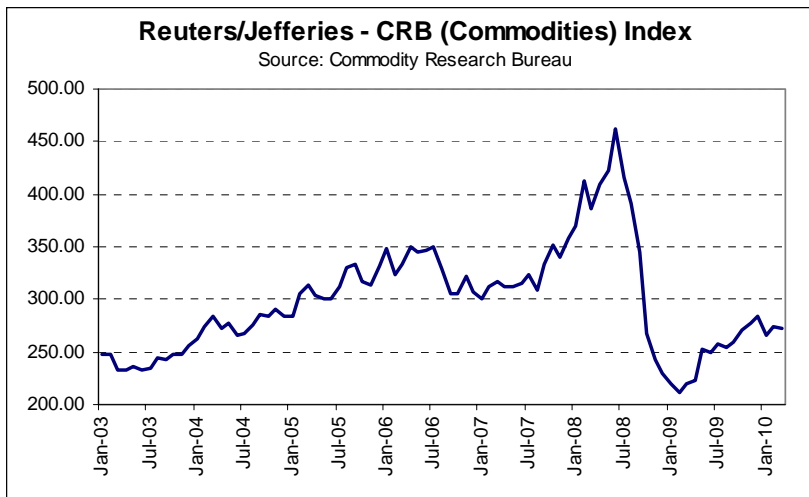
INFLATION

- **On a year-over-year basis, headline inflation rose +2.1% through February while core inflation increased +1.3%; both well within acceptable ranges.**
- **Money creation has not kept up with credit contraction therefore inflation has been kept in check in recent months and is likely to remain so in the near future.** A recent economic report noted that bank lending has contracted by -8.2% in 2010 through February, the sharpest contraction since the 1970's. In addition, housing, a large component of the CPI index is still facing downward pressure on prices.
- That said, with the Fed funds rate at historical lows and a greatly expanded balance sheet, **economists believe its not a question as to if, but rather when, inflationary pressures begin to become problematic,** particularly as the economy continues to improve.



COMMODITIES

- In 2009, the prospects of an improving global economy led to a strong rebound across many commodities, due in large part to the recovery in emerging Asia. **The Reuters / Jefferies CRB Index jumped +23.7% in 2009.**
- Questions regarding the strength of the global economy coupled with sovereign debt fears, particularly in Greece, led to a decline in the Reuters/Jefferies CRB Index during the first quarter of 2010. **The index is down -3.5%, year-to-date.**
- **Despite the early sell-off this year, commodity prices are expected to rise over the full year period due to increasing global demand as the world economy strengthens, particularly in the emerging economies.** However, above-average inventory levels and substantial spare capacity should keep prices from returning to 2008 levels.

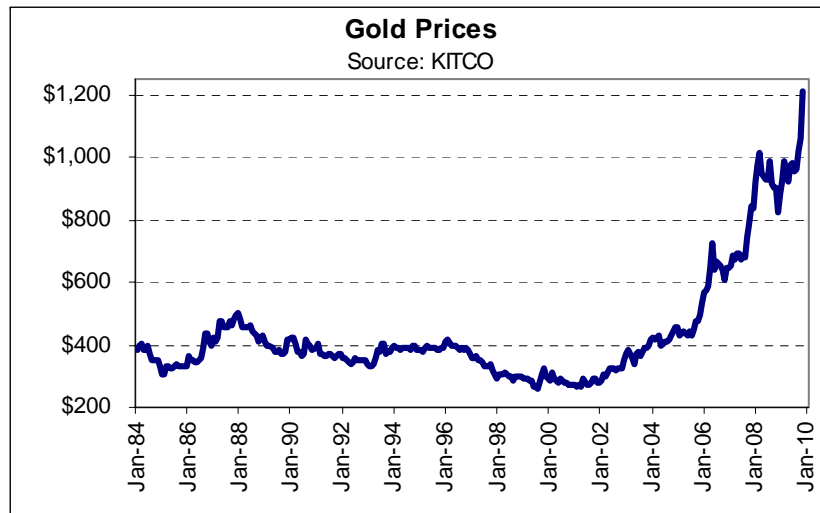
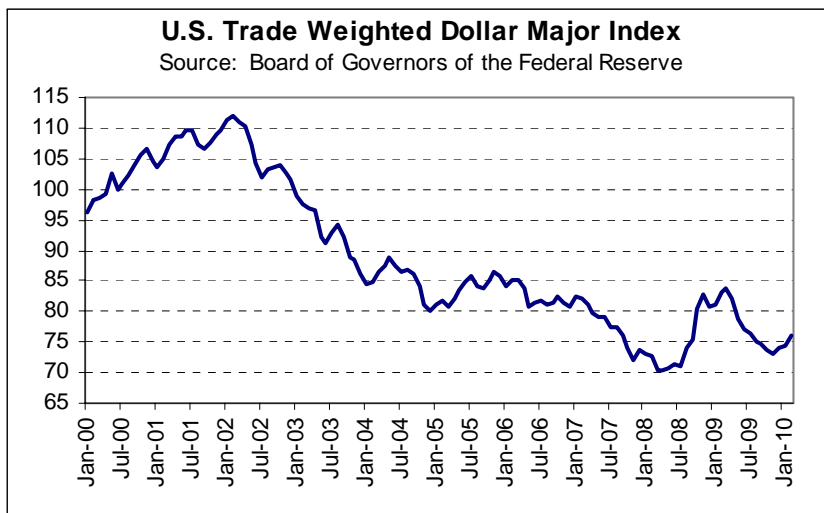


TOP PERFORMING COMMODITIES 2009	
Source: S&P and Morningstar	
Copper	+141%
Sugar	+128%
Zinc	+113%
Crude Oil	+78%
Nickel	+59%
Cotton	+54%
Silver	+49%
Aluminum	+45%

* Performance through 3/31/2010

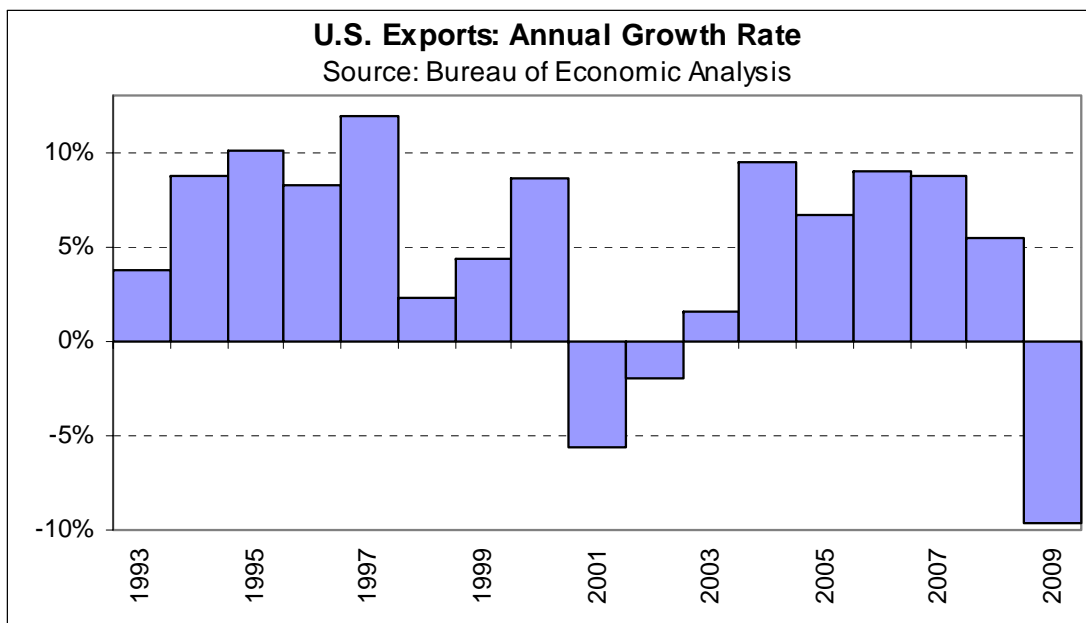
CURRENCY

- **While the U.S. dollar suffered through the latter half of 2009 as investors became increasingly less risk averse, recent concerns regarding sovereign debt, notably Greece, have led to a rebound in the dollar in 2010.**
- That said, there are still concerns about the longer term effects recent actions taken by the U.S. government could have on the value of the dollar. **Investors are particularly concerned about the growing federal deficit as well as the rising prospects for hyper-inflation longer term.**
- Gold remains an area of interest for investors as concerns regarding currency and inflation linger. **The precious metal was up +24% in 2009 and is up +2% in 2010.**



U.S. EXPORTS

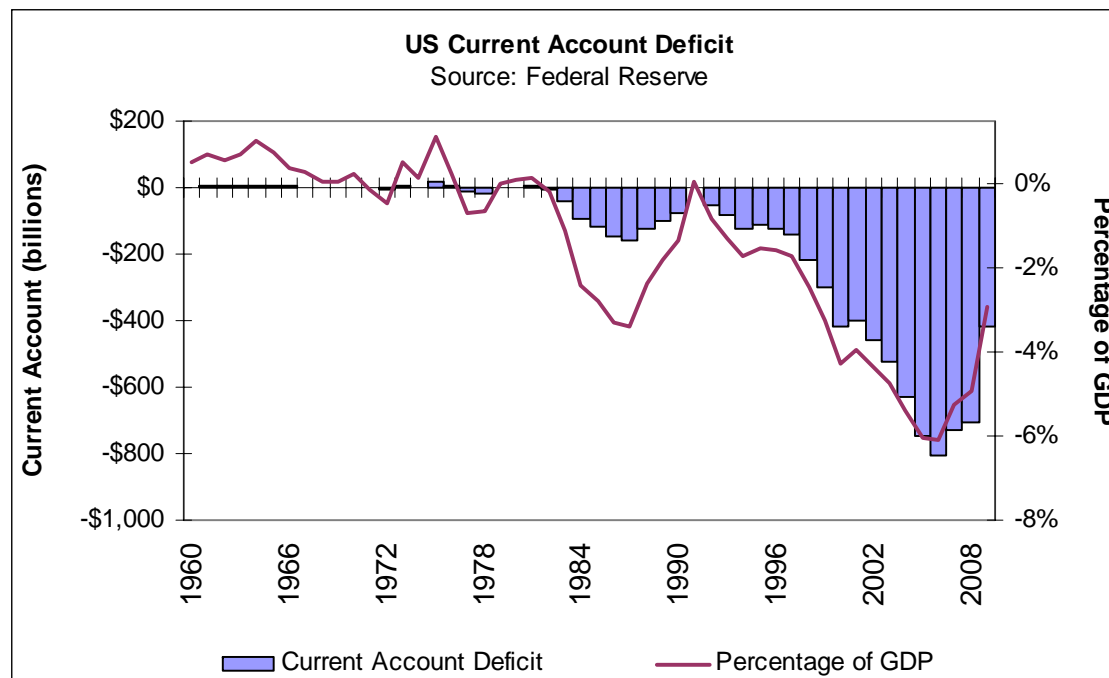
- U.S. exports benefited from a weak dollar during the second half of 2009. Investors sought out risk assets, particularly overseas, which placed downward pressure on the U.S. dollar. As a result, **exports picked up significantly in late 2009 and served as one of the primary contributors to U.S. economic growth in the third and fourth quarters.**
- **Going forward, economists anticipate the dollar to strengthen which will likely lead to exports serving as a drag on U.S GDP growth.**



Quarterly Export Growth	
Q3 2008	-3.6%
Q4 2008	-19.5%
Q1 2009	-29.9%
Q2 2009	-4.1%
Q3 2009	17.8%
Q4 2009	22.4%

CURRENT ACCOUNT DEFICIT

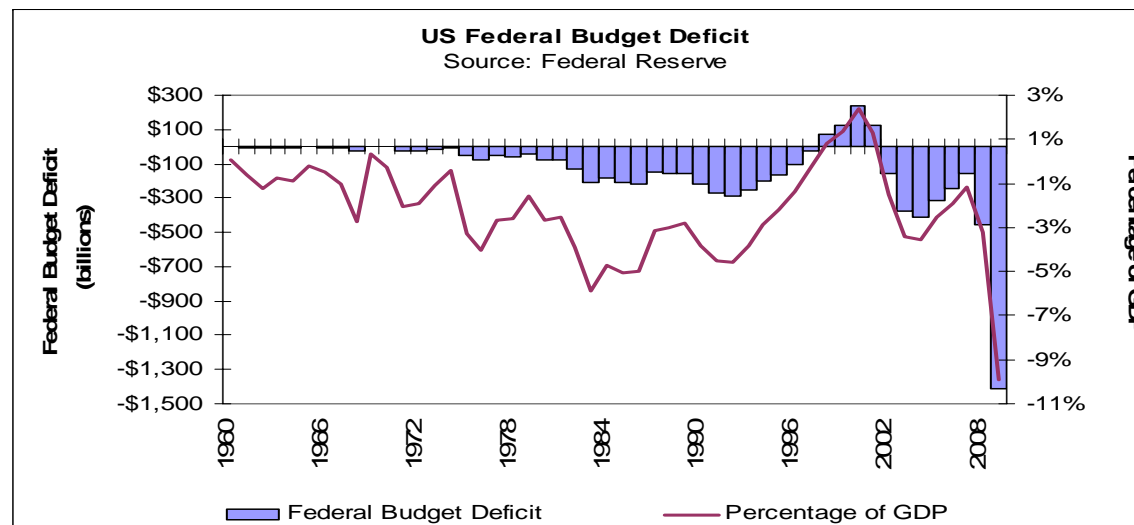
- **The current account deficit decreased for the third straight year in 2009, registering the smallest deficit since 2001.** The deficit equaled \$419 billion, just under +3.0% of GDP at year-end, down from \$706 billion in 2008 and +4.7% of GDP.
- **The current account deficit decreased due to a drop in international trade to \$517.0 billion from \$840.3 billion.** Goods imported fell more than goods exported, -13.9% and -9.6%, respectively.



Note: The current account deficit is caused by excess spending on goods, services, income and unilateral transfers creating a domestic budget defect.

FEDERAL BUDGET DEFICIT

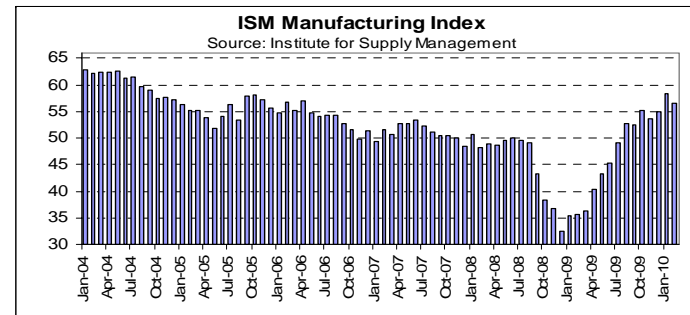
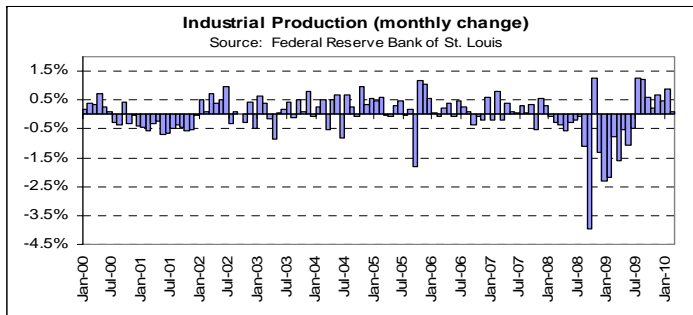
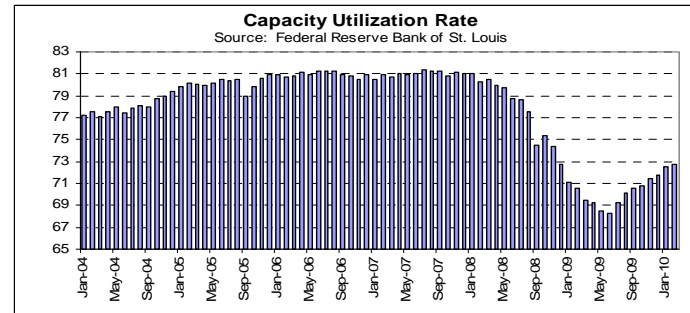
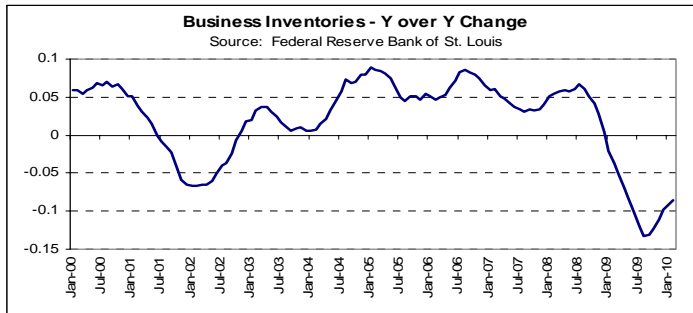
- The primary fiscal deficit reached a record level of \$221 billion in February on expenditures of \$328 billion and revenues of \$107 billion. **The deficit of \$652 billion through February is up nearly +11% from the \$590 billion deficit run up over the same time period in 2009.**
- **The administration is projecting that the deficit for the 2010 budget year will hit an all-time high of \$1.6 trillion, surpassing last year's \$1.4 trillion.** The administration is forecasting that the deficit will remain above \$1 trillion in 2011, resulting in three straight years of \$1 trillion-plus deficits.
- In the 2009 Financial Report of the U.S. Government, concerns were cited that the federal government is on an unsustainable long-term fiscal path driven by rising health care costs and demographic trends and that debt held by the public as a percentage of GDP could exceed the historical high reached in the aftermath of World War II. **The report estimated that the interest costs on the growing debt combined with spending on major entitlement programs could absorb 92 cents of every dollar of federal revenue by 2019.**



Note: The federal budget deficit is the amount by which a government's expenditures exceed its revenues. .

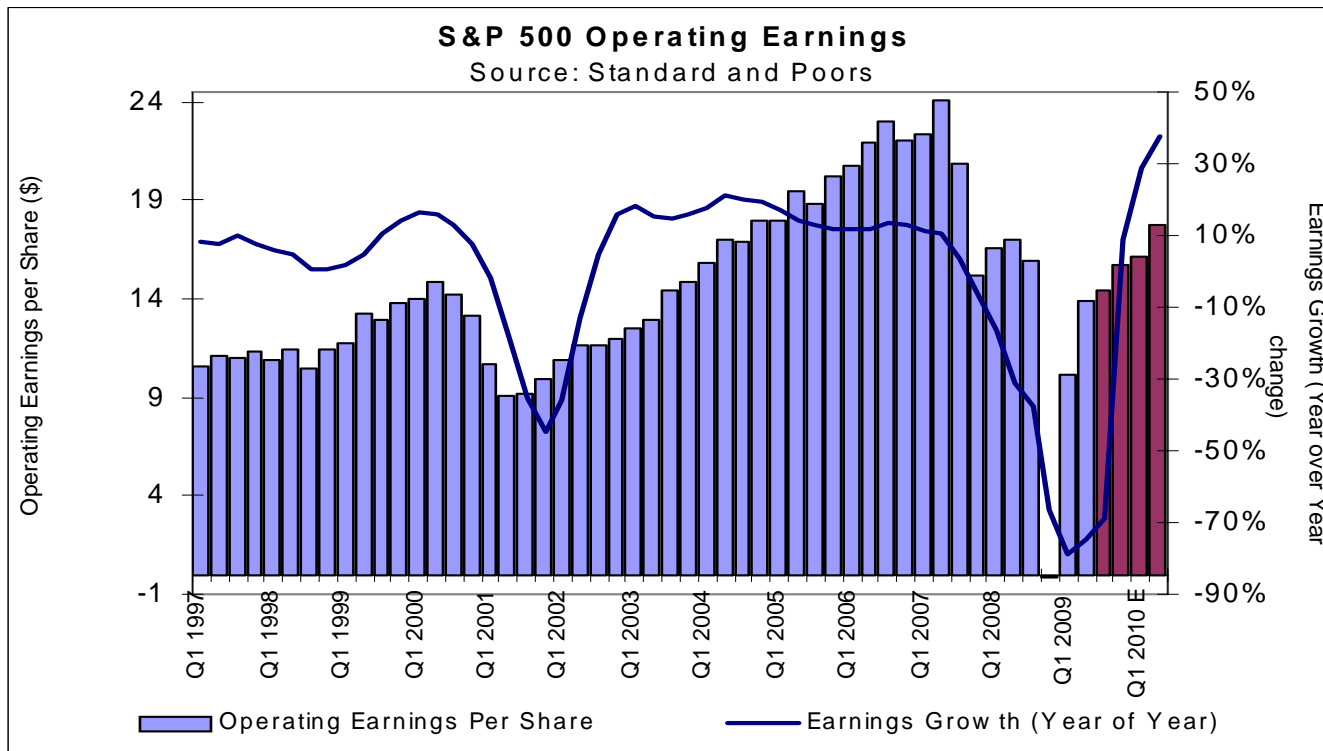
BUSINESS SECTOR

- **The overall manufacturing sector remains a bright spot in the economy and is firmly on a path to recovery.** The ISM Manufacturing Index crossed above the key figure of 50 back in 2009 and recently registered at 56.5 in February. In addition, the forward-looking new orders index came in at 65.9, the seventh consecutive month above the 50 threshold and its highest level in five years, while the employment index, at 56.1 remains above break-even and suggests job gains are on the horizon.
- **Industrial production has experienced 8 consecutive months of gains, the first time since 1998,** while capacity utilization continues to improve, coming in at 72.7 in February, its highest level since 2008.
- Economists anticipate further gains in the manufacturing sector, particularly as the global economy continues to recover.



CORPORATE PROFITS

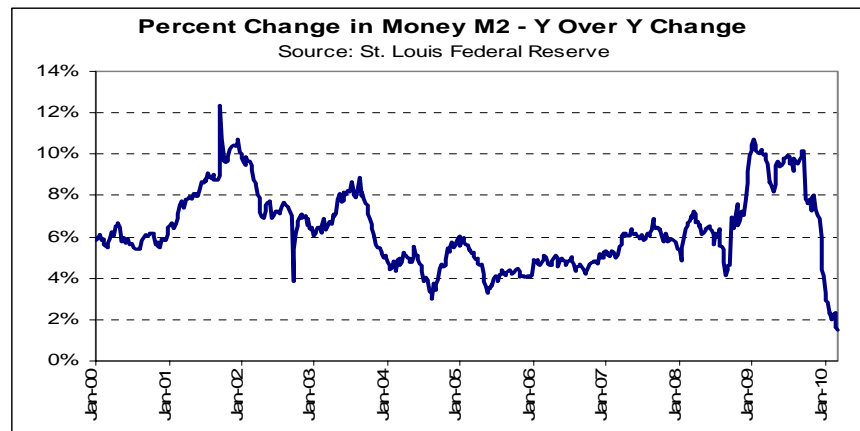
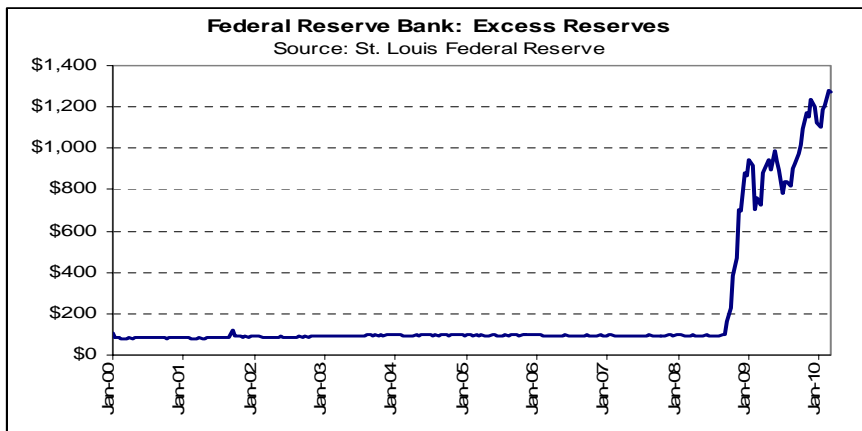
- Earnings for the S&P 500 came in at \$15.4 in Q4 2009 compared to -\$0.09 per share in Q4 2008.
- Operating earnings for all of 2010 are expected to come in at \$78.17 per share, a +37% increase from 2009 earnings of \$57.1.



Note: Earnings estimates are provided by Standard and Poor's as of March 10, 2010.

MONETARY AND FISCAL POLICY

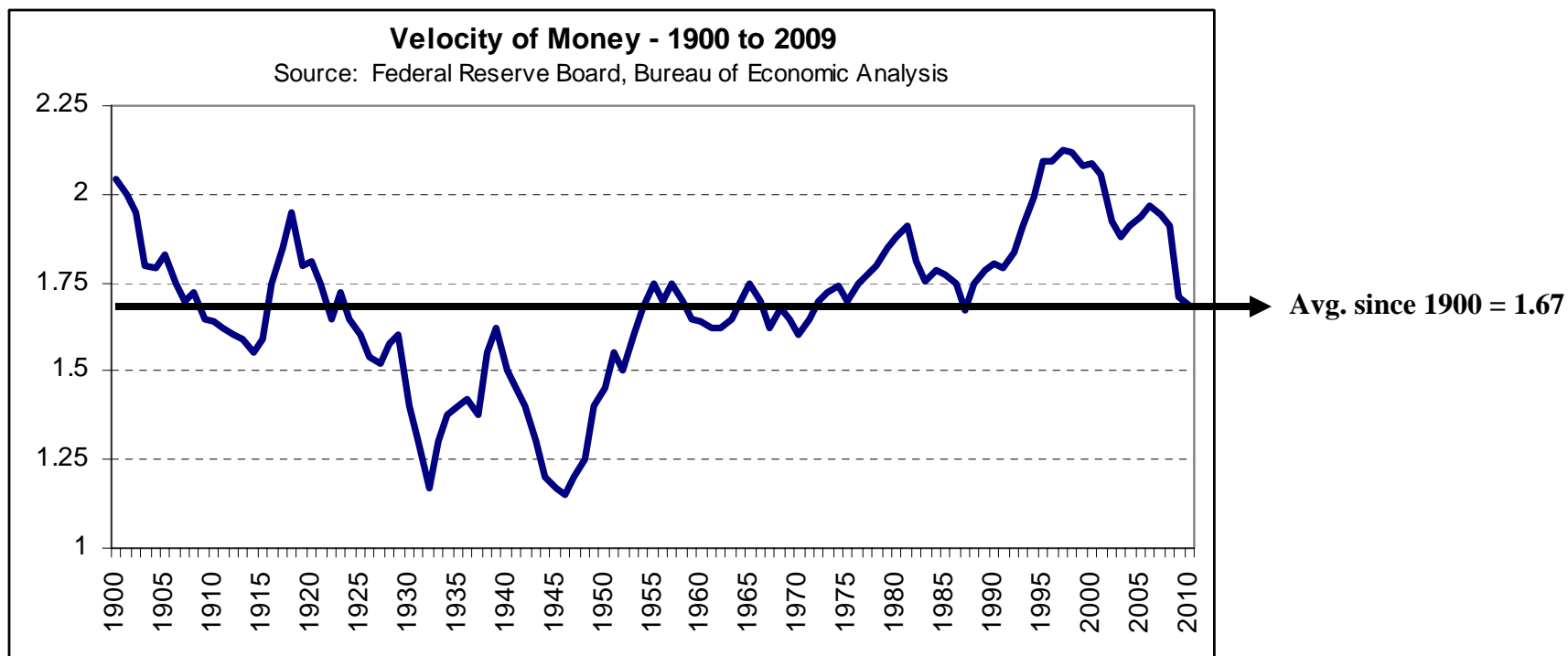
- With inflation in check and the economy still in recovery mode, **policy makers have reiterated their desire to keep discount rates at very accommodative levels and will strive to keep them there for an extended period.** Policy makers will have to be very cautious in balancing the need for growth without allowing inflation to run rampant. **Conversely, policy makers need to be cautious not to raise rates too early and risk thwarting growth.**
- A key risk to the economic recovery is the lack of bank lending. **Banks have been content allowing their excess reserves to sit on the Fed's balance sheet earning 25 basis points; hence the steep drop in the velocity of money.** The Fed has put together a plan to control reserves through the use of reverse repos and time deposits, however the timing of implementation is unclear.
- **The Fed's balance sheet is close to peaking. A number of the liquidity facilities have been terminated and the largest asset purchase program is scheduled to conclude at the end of March. The Fed indicated as securities mature, prepay and pay-down, their balance sheet will shrink.**



Note: M2 consists of M1 (which includes physical currency, travelers checks, and demand deposits – i.e., checking accounts), and small-time deposits (less than \$100,000), savings deposits, and balances in retail money market mutual funds.

VELOCITY OF MONEY

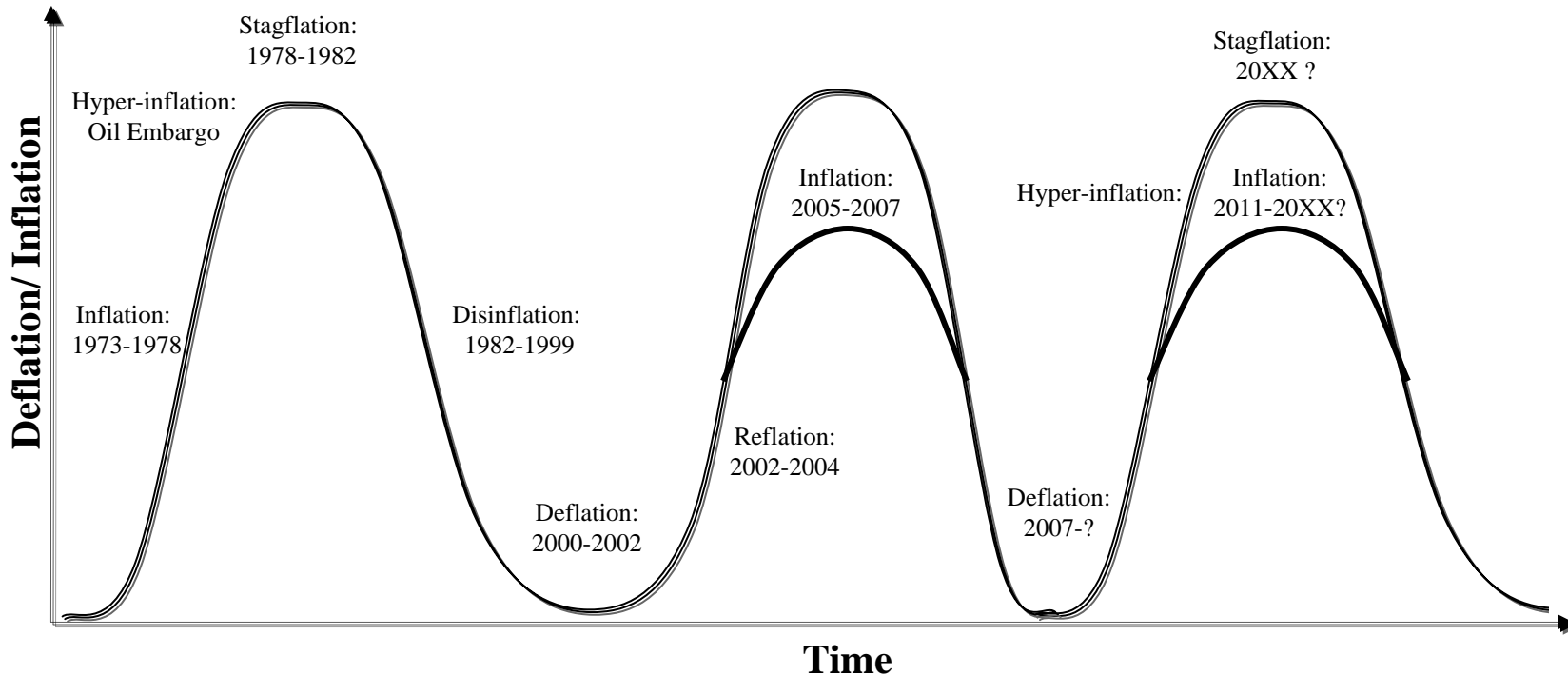
- **There are growing concerns that the velocity of money, an indicator of how many times a dollar is reused in the economy and is defined as GDP divided by the money supply, is collapsing.** The steep drop in this measure suggests that the lending cycle, which commenced several decades ago, could be coming to an end which could severely limit economic growth going forward.



Note: Velocity of Money = GDP / M2. M2 consists of M1 (which includes physical currency, travelers checks, and demand deposits – i.e., checking accounts), and small-time deposits (less than \$100,000), savings deposits, and balances in retail money market mutual funds.

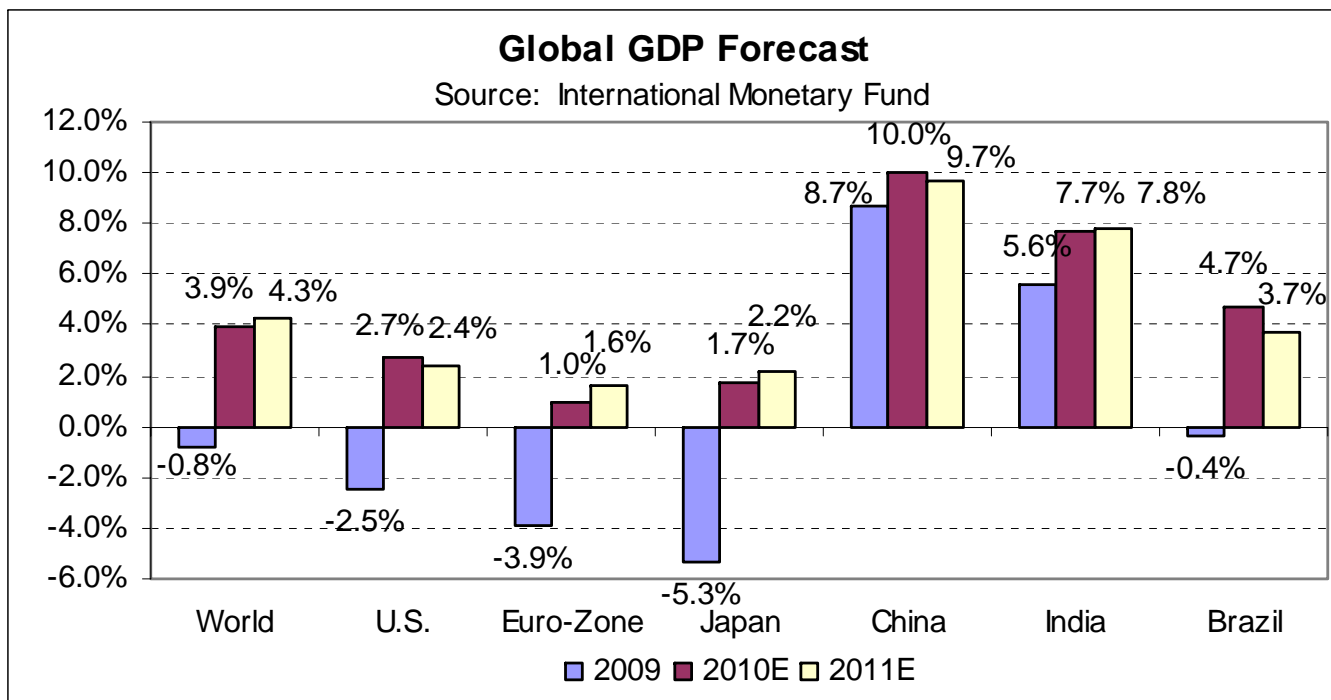
INFLATION RISKS

- While the economy is clearly on a path to recovery, inflation remains subdued due to weak wage growth and ongoing difficulties in the residential housing market.
- Short term: While the economy is technically no longer in a recession, we expect the broader economy to experience a slow recovery and deflationary pressures to persist.
- Long Term: U.S. could experience higher inflation coupled with a weakening economy if the removal of current accommodative policies by the administration results in a double dip recession; ultimately resulting in a worst case scenario known as stagflation.



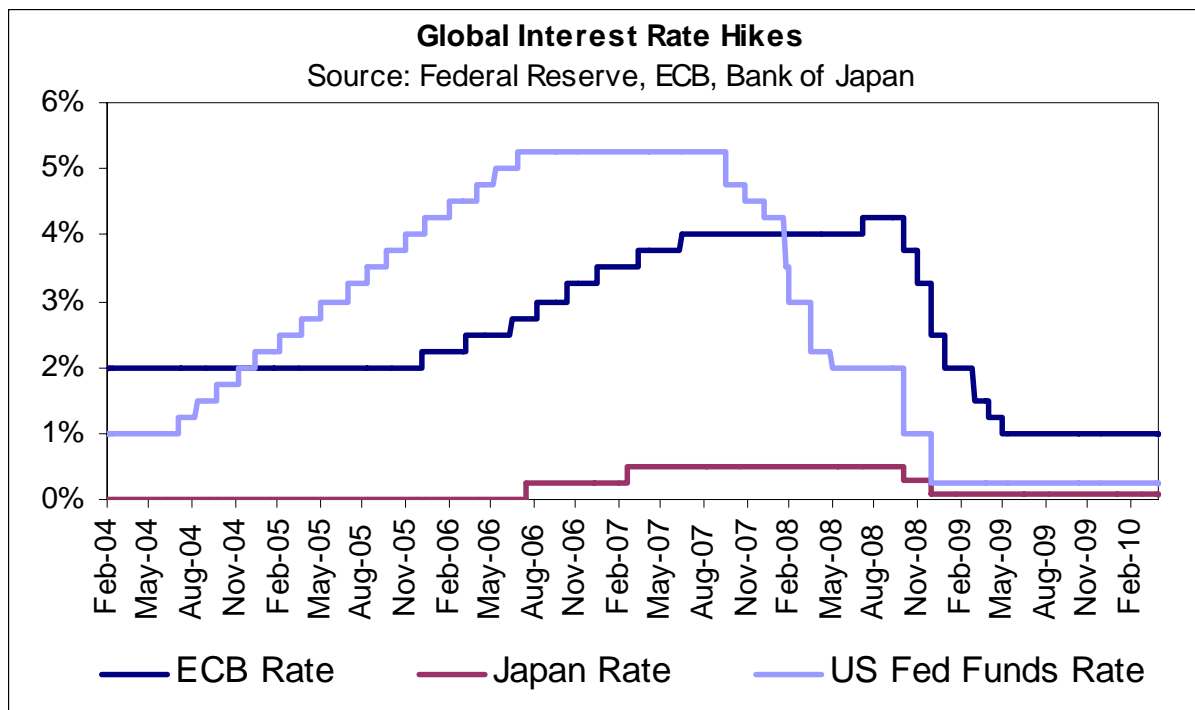
INTERNATIONAL ECONOMY

- Global growth is projected to turn positive in 2010. **The International Monetary Fund estimates world GDP to grow at an annualized rate of +3.9% in 2010, a +0.75% increase from their estimate released in October 2009. World GDP contracted -0.8% in 2009.**
- **Economists expect the emerging markets, particularly China, to drive global growth going forward.** India and Brazil are also expected to experience stronger economic growth relative to the developed countries.



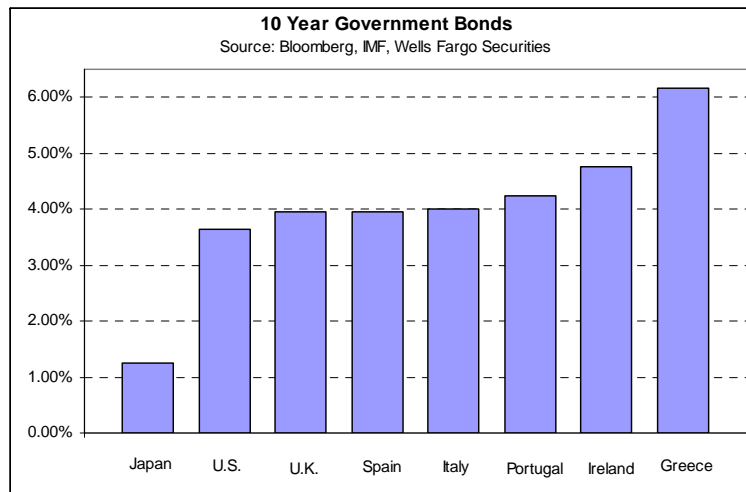
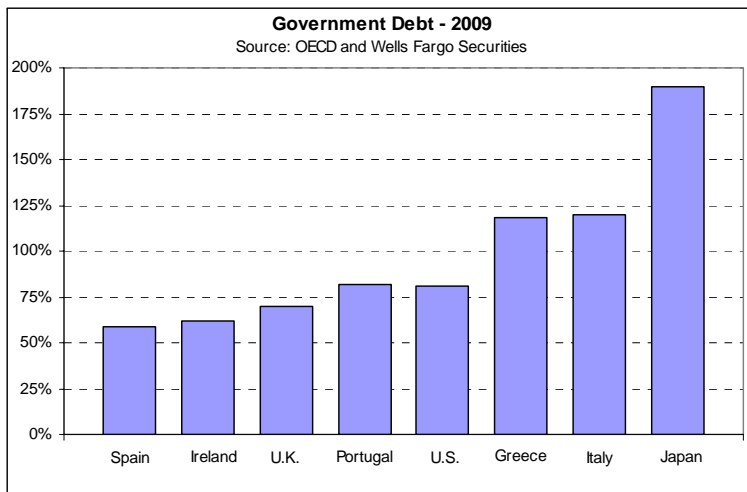
GLOBAL INTEREST RATES

- Central banks remain committed to accommodative policies until there are strong signs the global economy is once again on firm footing.



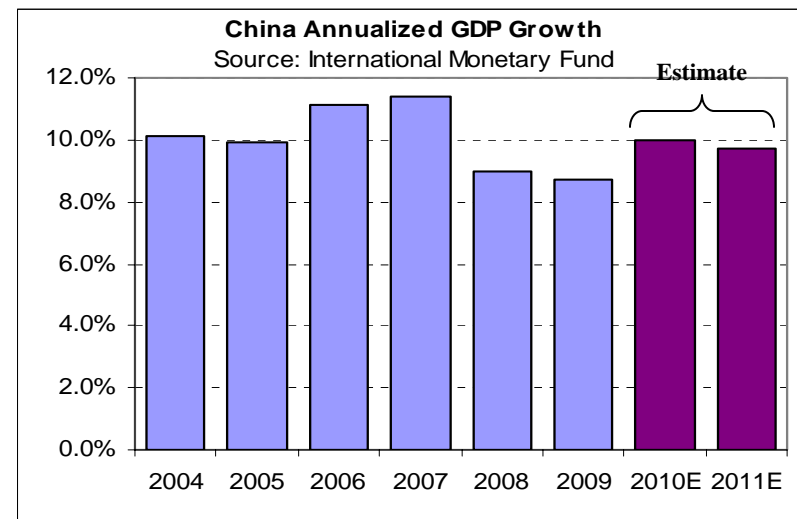
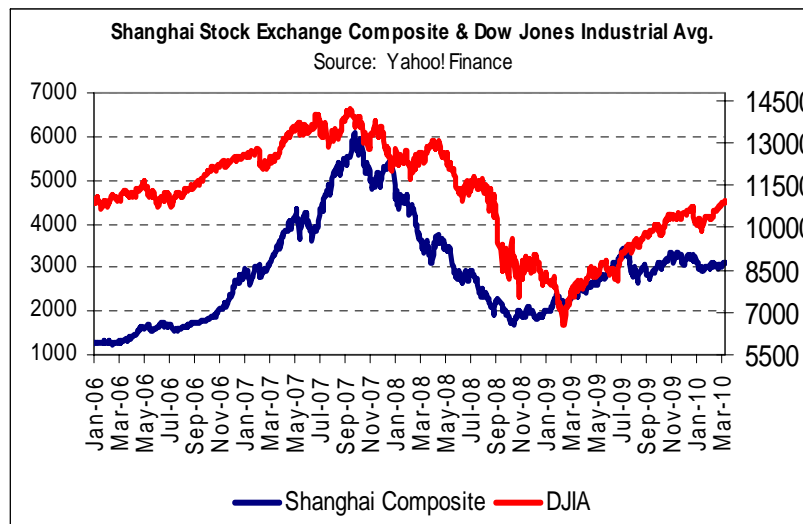
DEBT-TO-GDP RATIO

- **There is growing concern that several countries have built up unsustainable government debt-to-GDP ratios.** Economists cite a country's primary fiscal deficit, interest rates paid on government debt and nominal GDP growth as the driving factors behind a country's ability to service ones debt.
- **Greece and the other PIGS are of particular concern.** Not only is Greece struggling with high levels of government debt-to-GDP ratios but they also are paying high levels of interest on such debt which is calling into question their ability to continue servicing the debt.
- **Talk of default and a fear of contagion is increasing and investors are now beginning to question how many more governments have run up unsustainable debt loads and what this could mean for the world economy and financial markets.**



CHINA

- **China continued to experience strong growth in 2009 with an annualized GDP growth rate of +8.7%.** The IMF projects GDP growth rates for China of +10.0% in 2010 and +9.7% in 2011. **China is expected to continue leading the global economy in growth.**
- **After maintaining extremely accommodative policies throughout most of 2009 along with other policy makers, China recently moved to raise bank reserve requirements in order to restrict excessive growth and keep inflation under control.**
- The Shanghai Stock Exchange Composite Index rebounded strongly in 2009 with a +80% gain for the full year period after falling -63% in 2008. **However, restrictive policy moves, stretched valuations and talks of a bubble in China have led to the index giving back some gains in 2010.** The index is down -5% through the first quarter.



II. FINANCIAL MARKETS REVIEW

FINANCIAL MARKETS PERFORMANCE

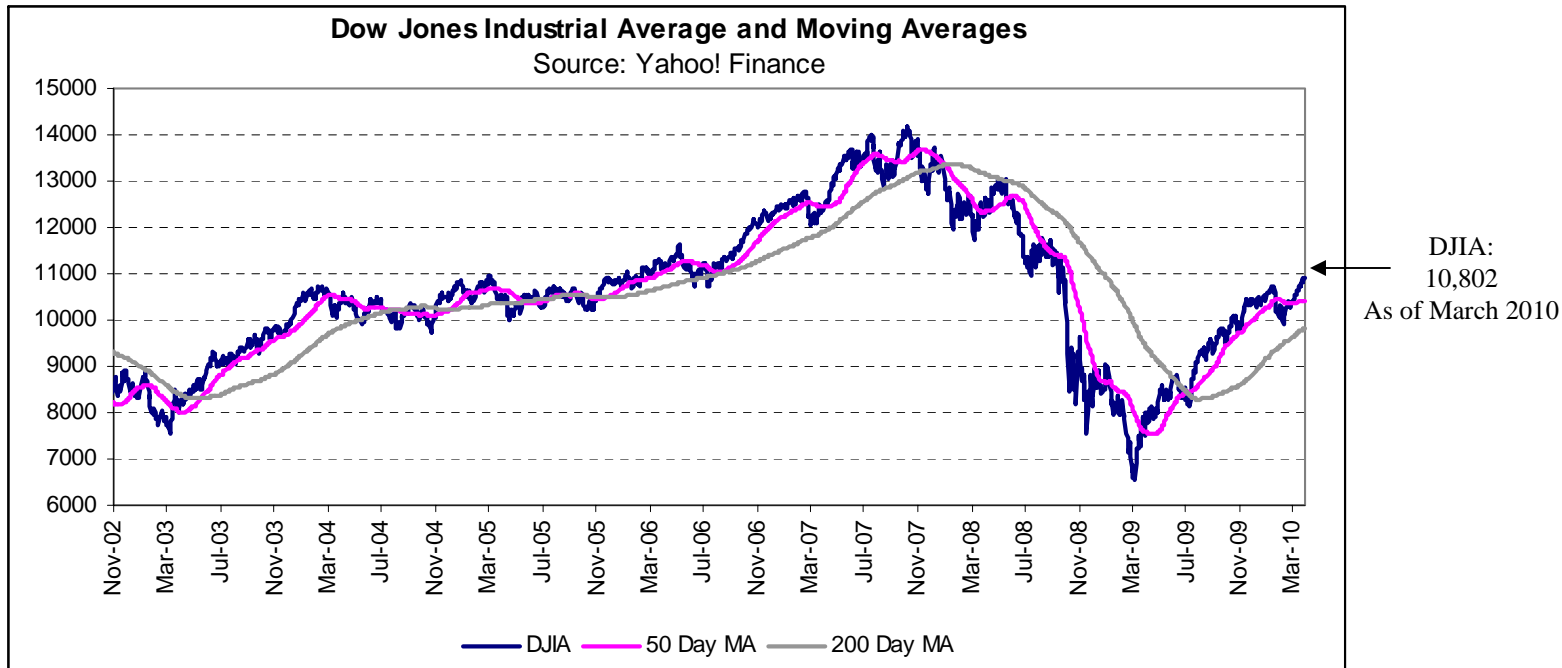
- **Excess liquidity, solid technical support and improving fundamentals led to the markets achieving higher highs, and higher lows throughout 2009.** The financial markets rebounded strongly from their lows reached in early 2009, registering trough-to-peak gains of nearly +70%.
- **The markets were led higher in 2009 by the emerging markets (+74%) and technology sector (+44%).** Treasuries suffered in 2009 as investors sought out risk assets. The 10 year treasury lost -9.8% while the 30 year treasury dropped -25.9%.
- **The financial markets have experienced broad based gains in 2010 due in large part to strong returns in March.**

Equity Market Performance	2010 (YTD through Mar-10)	2009
S&P 500 Index	+4.9%	+23.5%
NASDAQ Index	+5.7%	+43.9%
Dow Jones Industrial Average	+4.1%	+18.8%
Russell 2000 Index	+8.5%	+25.2%
MSCI Pacific Index (USD)	+5.4%	+21.2%
MSCI Europe Index (USD)	-2.3%	+31.2%
MSCI Emerging Markets Index (USD)	+2.1%	+74.5%
MSCI EM Latin America (USD)	+1.3%	+98.1%
S&P GSCI Gold Spot	+1.7%	+24.0%
S&P GSCI Crude Oil Spot	+5.5%	+54.2%
10 Year Treasury	+1.0%	-9.8%
30 Year Treasury	-0.1%	-25.9%

Source: Morningstar

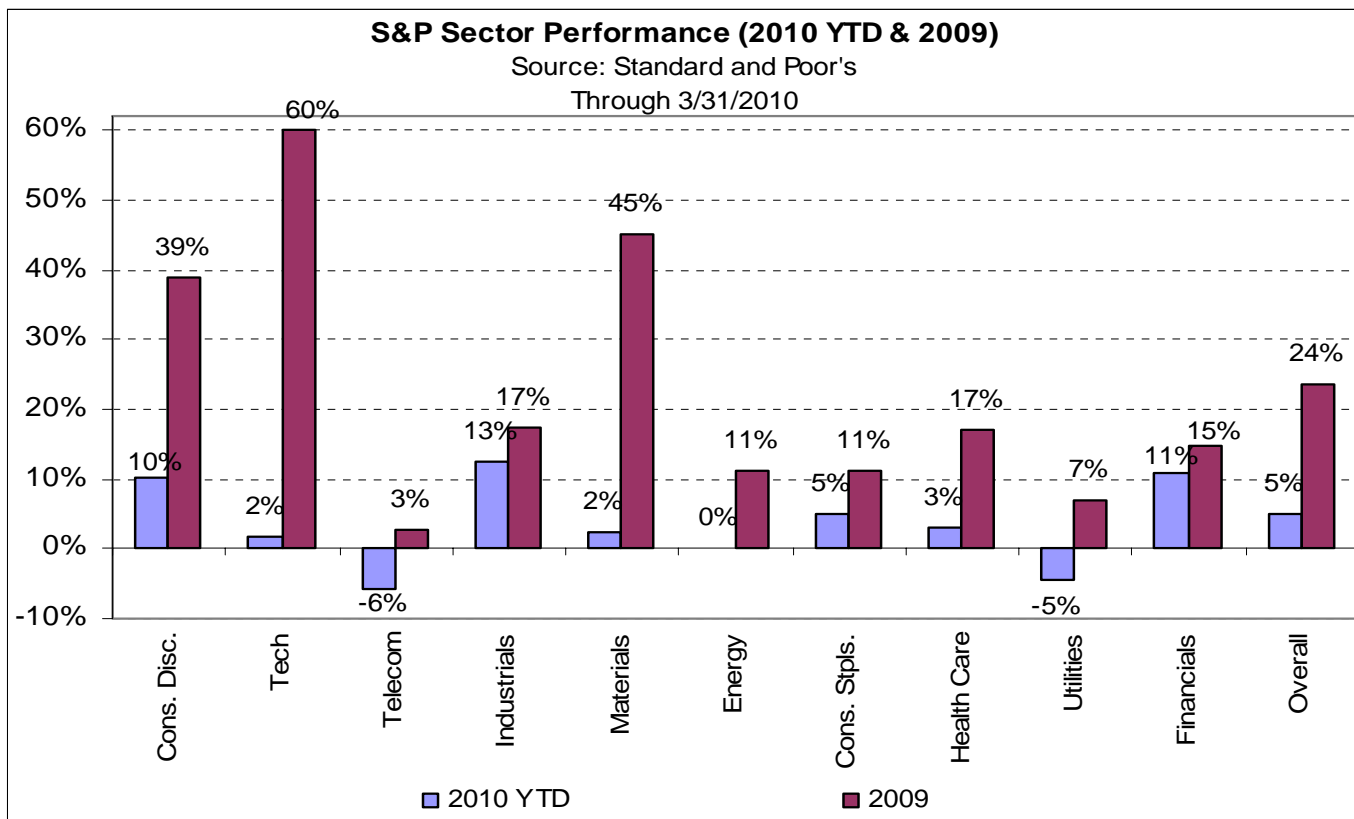
U.S. EQUITY MARKET PERFORMANCE

- Since reaching its low of 6,547 over a year ago in early March of 2009, the Dow has rallied +66% and continues to show strength from a technical perspective.



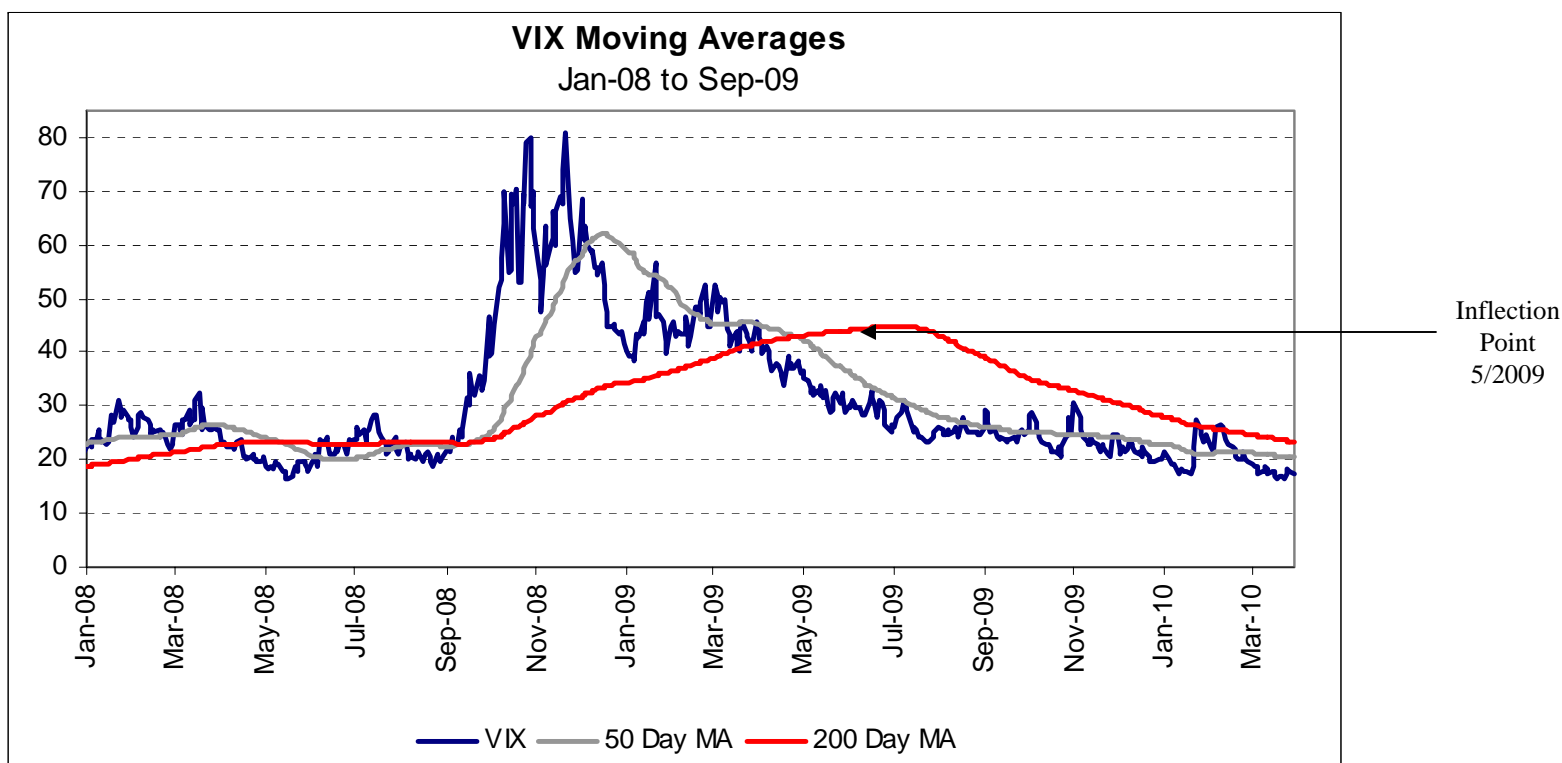
U.S. EQUITY SECTOR PERFORMANCE

- All sectors experienced gains in 2009, led by technology (+60%), materials (+45%) and consumer discretionary (+39%).
- With the exception of telecom (-6%) and utilities (-5%), all sectors have continued their upward trend in 2010.



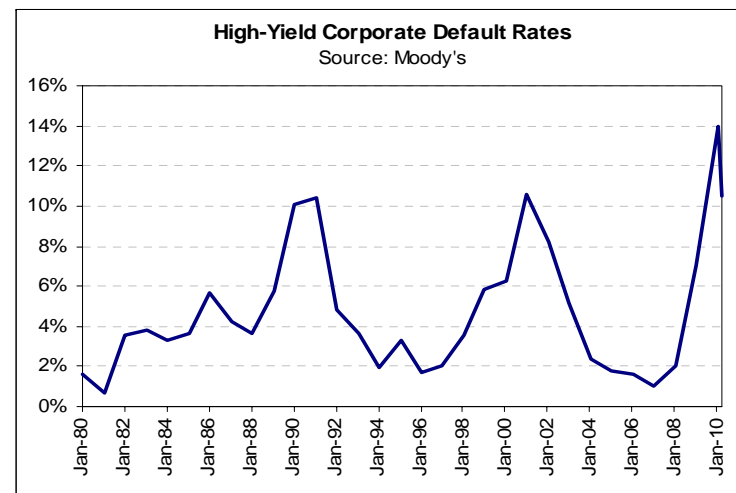
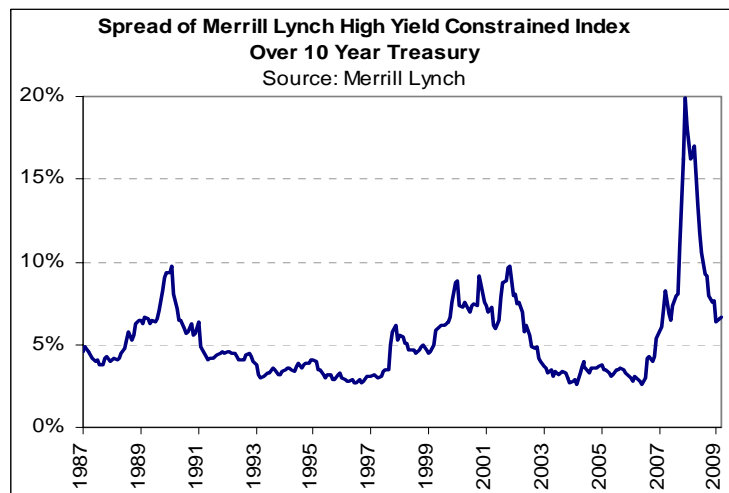
U.S. EQUITY MARKET VOLATILITY

- The volatility in the equity markets continues to decline after experiencing a sharp spike after the failure of Lehman Brothers. The VIX has settled back into its pre-Lehman levels, between 20 and 30.



CREDIT MARKETS

- The U.S. government took unprecedented actions in responding to the 2008 credit crisis which provided a boost to credit markets. **Prices of corporate bonds, leveraged loans, and mortgage backed securities soared in 2009 reaching pre-Lehman levels.**
- **Gains in 2009, while broad based, were largely driven by high yield bonds with the Merrill Lynch High Yield Master Index gaining a strong +58%.** The Barclays Aggregate Bond Index gained +6%. Treasuries experienced losses as investors returned to risk assets. **The 10 Year Treasury lost -10% while the 30 Year Treasury lost -26%.**
- **The spread on the Merrill Lynch High Yield Index tightened by a steep 1,173 basis points in 2009 from 1,812 basis points to 639 and now stands at approximately 584 basis points.**
- The default rate fell to 10.5% in February and is expected to drop to 5% by year-end as the economic recovery takes hold.



III. OUTLOOK

ECONOMIC OUTLOOK

- **Synchronized global policy stimulus** in the form of central bank liquidity actions, monetary stimulus and government fiscal stimulus that occurred throughout the world **succeeded in calming the financial crisis, ending the recession and starting a global expansion.**
- **World economic growth is expected to grow at a +3.9% annualized rate in 2010, led by the emerging and developing countries** which are expected to grow at a +6.0% annualized rate. Developed economies are expected to lag in economic growth, expanding +2.0% in 2010.
- While U.S. GDP growth has exceeded expectations in recent quarters, **the growth has been very narrow and it is widely believed that the broader based economy will experience a slow, gradual recovery.**
- **Unemployment rates are likely to remain high in the U.S. throughout 2010** as companies remain hesitant to hire and continue to focus on efficiency improvements and higher productivity.
- **Consumer spending will remain subdued due to elevated levels of unemployment and a general sense of caution after the deep recession.** Consumers will continue to focus on paying down debt and increasing savings.
- **Corporate profitability will continue to improve with top line growth surprising to the upside.** Capex spending will improve as businesses regain confidence and invest in new systems and software to improve efficiency.
- **Commercial real estate will weaken in 2010 and beyond.** Difficulties refinancing debt coupled with higher vacancy rates will serve as considerable challenges going forward.
- **Inflation will remain subdued in 2010 as credit remains tight and the residential housing market flirts with a double dip.** Longer term, inflation could become problematic due to the money printed to reignite economic growth.

EQUITY MARKET OUTLOOK

2009 Earnings Results and Valuation:

- **The S&P 500 Index reported earnings of \$15.4 in the fourth quarter of 2009** and \$57.1 for the full year period. **The S&P closed 2009 trading at 19.5x trailing earnings.**
- **Earnings of reported firms were up +106% year-over-year relative to 2008.**
- **Revenues were up +6% year-over-year in the fourth quarter, a solid improvement from the -11% decline in revenue in the third quarter. Approximately +57% of firms reported higher revenues from a year ago, nearly double the +30% of companies that reported higher revenues in the third quarter.**
- **In addition, approximately +67% of firms reported better than expected revenue numbers during the fourth quarter.**

2009 Earnings Review:

- The Hennessee Group cited concerns in October of 2009 that **companies were manufacturing earnings growth primarily through cost cutting measures that were unsustainable.** We stated companies needed to expand top line revenues and generate real earnings growth in the coming quarters to support current market valuations.
- As a whole, the earnings were strong from both a top line and bottom line perspective which provided support to the equity markets. That said, it's important to note that **revenue and earnings growth were very narrowly focused. Excluding financials, earnings growth was a solid, but much lower +15% and revenues were positive, but a much lower +2%.**

EQUITY MARKET OUTLOOK

Keys to 2010 Earnings:

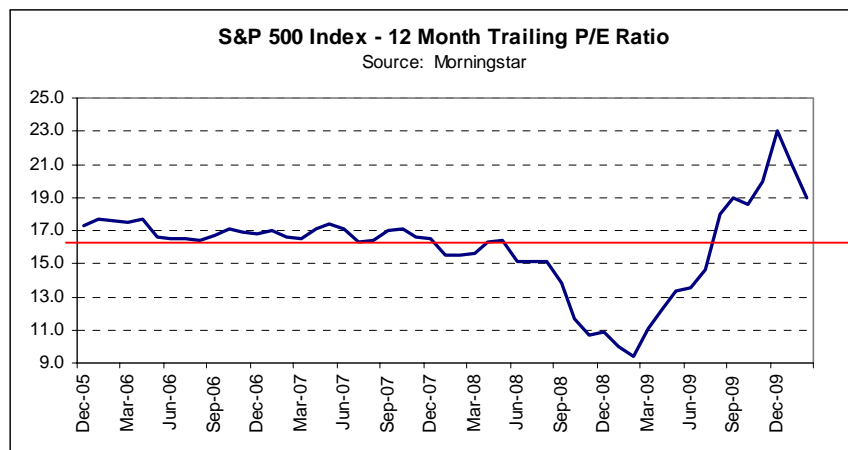
- The Hennessee Group believes top line revenue growth and improved visibility reported in the fourth quarter has confirmed that the cyclical recovery is firmly in place.
- That said, financials were the primary driver in the fourth quarter. **The Hennessee Group believes its imperative that a more diverse sector base will contribute to results going forward in order to continue to meet or exceed rising expectations in 2010.**
- **The Hennessee Group expects global stimulus packages to drive profits during the first half of the year, particularly for the energy, industrials, materials and technology sectors.** This should lead to earnings strength in the first half of the year and provide further support to the equity markets.
- However, **we believe earnings could disappoint in the second half of the year as stimulus packages have less of an impact on earnings and consumers remain conservative with regards to spending due to ongoing weakness in the job market.**

2010 Earnings Forecast:

- **S&P:** Predicts operating earnings per share to come in at **\$78.2 per share in 2010**, a +37% increase from 2009. This is a upward revised estimate from their October estimate of \$72.3.
- **Hennessee Group:** The Hennessee Group believes S&P is slightly aggressive with their 2010 earnings forecast given our concerns regarding earnings results in the second half of the year. **We anticipate earnings per share to come in closer to \$76.0 per share, a solid +33% increase from 2009.**

EQUITY MARKET OUTLOOK

- Valuation / Fundamentals:** Using the Hennessee EPS estimate of \$76.0 for 2010, we believe the S&P 500 from a fundamental perspective, is fairly valued at 1,216 (assuming a historical 16x multiple) and is likely to trade in a range of 1,064 (P/E of 14x) to 1,368 (P/E of 18x) in 2010. **The S&P 500 closed the first quarter on 3/31/10 at 1,169.**



	Hennessee 2010 EPS	P/E	Value
Expected Range	\$76.0	14X	1,064
	\$76.0	16X	1,216
	\$76.0	18x	1,368
	\$76.0	20X	1,520

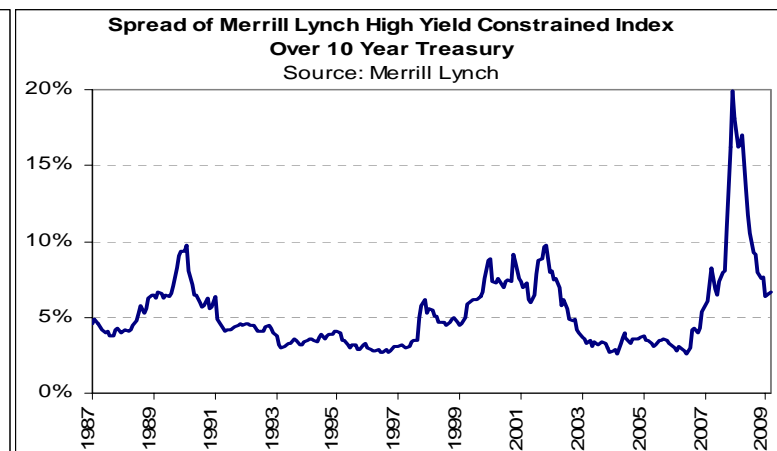
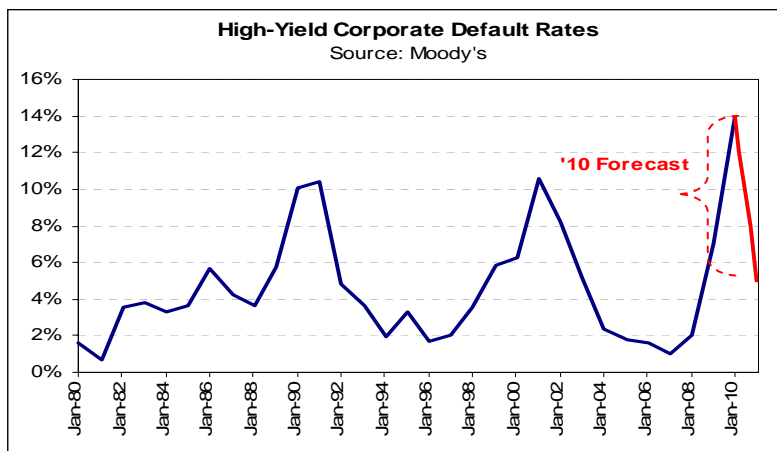
Historical Avg. P/E
16.1x

	S&P 2010 EPS	P/E	Value
Expected Range	\$78.2	14X	1,094
	\$78.2	16x	1,251
	\$78.2	18X	1,407
	\$78.2	20X	1,564

- Earnings Yield:** Equities appear attractive relative to bonds as the earnings yield (earnings/price) of the S&P 500 is currently +5.1% (on a trailing basis) and +6.7% (on a forward basis), significantly higher than the U.S. 10 Year Treasury, yielding +3.9%, and the Barclays U.S. Corporate Index yielding, +4.5%.
- Technical Indicators:** Technical indicators continue to show solid support for the equity markets in the near term as large amounts of cash still sit in money market accounts and continue to find their way into stocks after short term sell-offs. The low end of our trading range based on fundamentals is likely a good support level for the equity markets. **That said, we expect near term volatility due to headlines concerning double dip fears, bank regulations, reserve requirements in China and sovereign debt challenges.**

CREDIT MARKET OUTLOOK

- Credit Markets:** While the easy money was made in the credit markets in 2009, spreads remain at elevated levels relative to their historical average (584 bps vs. 530 bps) which should offer additional opportunities, yet on a select basis. **However, a stronger than expected recovery in the economy could lead to a hike in interest rates sooner than expected, which could place downward pressure on the fixed income markets.**
- Defaults:** It is widely believed that 2009's record level of defaults represents the cyclical peak and that default rates will continue to moderate throughout 2010, ultimately reaching +5% by year-end. Despite the slowdown in the default rate there should be a number of distressed and restructuring opportunities in coming years.
- Investors anticipate further gains in high-grade and high-yield corporate credit due to improving credit fundamentals and attractive yields.** Similarly, high-quality assets in the commercial mortgage- and asset backed sectors are expected to outperform while agency mortgages and treasuries are expected to lag.



IV. RISKS TO OUTLOOK

RISKS TO OUTLOOK

- **The removal of government stimulus programs** (i.e., first time home buyer tax credits, cash for clunkers) exposes the true weakness of the broader economy and results in a double dip recession.
- **The Fed acts too soon or too aggressively** to remove the accommodative fiscal and monetary policies to combat inflationary pressures, and ultimately thwarts economic growth.
- **Sovereign Debt** problems of struggling European economies like Greece spread into the stronger members of the European Union and other parts of the world, negatively impacting the global economy.
- **Weakness in the commercial real estate** market results in banks remaining reluctant to extend credit to consumers and small businesses, resulting in additional headwinds for the economy.
- **The unemployment rate remains stubbornly high** and places further pressure on consumer spending.
- **Inflation becomes problematic** over the longer term due to overly accommodative policies by central banks. Particularly a jump in commodity prices dampening consumer spending.
- **Relocation of Corporations from USA to more favorable corporate tax jurisdictions.** The USA has highest corporate tax structure and tax increases are likely given deficit spending projections.

RISKS TO OUTLOOK

- **Real estate bubble in China** leads to slower Chinese growth and muted global growth.
- **Agendas pursued by the new administration**, particularly changes in the regulatory environment on Wall Street and national healthcare reform, **have unintended consequences on the economy and financial markets.**
- **Residential real estate experiences a double dip** due to over supply and more stringent lending standards.
- **Protectionist policies are introduced** resulting in a **decline in “global free markets / free trade” objectives.**
- **Geopolitical tensions rise**, particularly in Iran, Iraq, North Korea, Middle East or Russia.
- **Off-balance sheet transactions** [especially structured derivatives] remain a major risk to the economy and threaten the stability of the financial markets.
- **Recycling of USA dollar based assets (stocks, bonds, etc) into Gold by foreign investors.** Currently, dollars held by foreign central banks are being recycled back into the USA markets.
- **Default or "near" default of city and state bond obligations.** California.

V. LONG-TERM OUTLOOK

2010 AND BEYOND

- **Federal Deficit:** Expected to exceed \$1 trillion for 3 consecutive years. The administration will have to turn to reigning in spending and reduce the deficit which is reaching unsustainable levels.
- **National Healthcare Program:** Federal entitlement programs such as Medicare and Social Security are already posing threats to fiscal sustainability, a new national healthcare program will only raise additional concerns.
- **Financial Markets:** Continue to offer attractive upside longer term, particularly as fundamentals and the economy continue to improve.
- **Return of Differentiation:** Stock specific alpha should drive returns as we see the return of differentiation among stocks and sectors. Blue chip, high quality stocks should outperform low quality.
- **Technicals:** Equity market must break 11,275 on DJIA to attract money off sidelines
- **Fundamentals:** Top line growth must be convincing. Year-over-year rate of unemployment must decline significantly. Housing prices/sales bottom.
- **M&A Activity:** Strong balance sheets, record cash levels, available financing and increased liquidity should lead to an uptick in M&A activity, particularly in the biotech space.
- **Commodities:** Longer term inflationary pressures will lead to a rebound in commodity prices and benefit investors positioned for a “reflation trade”.
- **Currency Changes:** The dollar is likely to gain from current levels relative to the Euro as concerns regarding sovereign debt grow. However, longer term concerns for the dollar remain.
- **Global Focus:** Many of the most attractive opportunities for outsized gains will be found in select international countries, particularly in many emerging markets.
- **Interest Rate Swap** market "debacle" as interest rates rise.
- **China Real Estate Bubble:** Results in systemic banking risks. China bailout of banks....foreign Private Equity investors take losses.

2010 AND BEYOND

- **Debt Financing:** The U.S. will have to shift their financing of debt from short term bonds (1, 3 and 5 yr.), to longer term bonds (10, 20, and 30 yr.).
- **Agendas pursued by the new administration in the U.S. are likely to have a material impact on the financial markets,** particularly with regards to changes in the regulatory environment.
- **Rising Debt to GDP Levels:** As the economy recovers, the U.S. will have to shift their focus to how they will finance rising debt levels (i.e., raise taxes), particularly if China and other countries lose interest in U.S. treasuries.
- **Corporate Tax Rates** – At 35% the U.S. has the highest tax rates among developed countries. Further increases in corporate taxes will result in more jobs moving offshore or eliminated in order to be globally competitive.
- Capital gains taxes at 15% should be lowered, not raised, to encourage new capital formation.
- **Foreclosures** must be prevented except in the most severe cases [foreclosures typically result in bank write-downs of 25% and the expense of managing a resale].
- **Middle Class America** should be given tax incentives to purchase: cars, “new” homes, education, health care, etc.
- **Baby Boomer Retirement Spurs Change** – As the Baby Boomer generation enters into retirement, a change in lifestyle has the potential to affect the financial markets as they are likely to sell equity investments, increase ownership of municipal bonds and have a stronger desire for increased socialization.
- **"One World Order" ...??...solution to long term global debt/GDP issues??**

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from Hennessee Group, please visit our
website: www.hennesseegroup.com**

- (*) • **TV Interviews: <http://hennesseegroup.com/company/interviews.html>**
- **Press Releases: <http://hennesseegroup.com/releases/2009releases.html>**
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- **Hennessee Hedge Fund Index: <http://hennesseegroup.com/indices/index.html>**

(*) View 11/2/2006 interview with Charles Gradante.....”We will have, sometime in the future, a major banking problem being caused by credit default swaps”.



Hedge Fund Disclosure

- **Hedge funds can be speculative and may involve a high degree of risk.**
- **Hedge funds may use leverage.**
- **Hedge funds may have performance that is volatile.**
- **An investor could lose all or a substantial amount of their investment.**
- **The fund manager has total trading authority over the fund. The use of a single advisor applying generally similar trading programs could result in a lack of diversification and, consequentially, higher risk.**
- **There is no secondary market for the investor's interest in the fund and none is expected to develop.**
- **There may be restrictions on redeeming interests in the fund.**
- **The fund's fees and expenses may offset the fund's trading profits.**
- **Some hedge funds can execute a substantial portion of the trades executed for the fund on a foreign exchange.**
- **The amount of disclosure received by Hennessee Group for manager evaluation may vary by manager and is only performed once. Transparency varies by manager. The manager evaluation process Hennessee Group employs may vary by manager. No notice of variations among managers will be given to client and the process described herein may be changed without notice. Not all of manager's representations are corroborated. Business judgment is applied when necessary. Manager evaluation and monitoring is a process consisting of quantitative and qualitative elements. The process is a combination of "science and art" (i.e., quantitative analysis and business experience). Manager evaluation process may vary from time to time without giving notice or seeking consent. The evaluation process is not directed at providing assurances with respect to internal controls, nor to the detection of fraud, errors, or illegal acts. The evaluation process consists of gathering quantitative and qualitative information through an interview with personnel of the hedge fund.**
- **Monitoring (i.e., *Manager Performance Monitor* and *Portfolio Performance Monitor*) is performed on an ongoing basis.**

Descriptions of Indices

Hennessee Hedge Fund Index

The Hennessee Hedge Fund Indices[®] are calculated from performance data supplied by a diversified group of hedge funds monitored by the Hennessee Hedge Fund Advisory Group. The Hennessee Hedge Fund Index is an equally-weighted average of the funds in the Hennessee Hedge Fund Indices[®]. The funds in the Hennessee Hedge Fund Index are believed to be statistically representative of the larger Hennessee Universe of over 3,500 hedge funds and are net of fees and unaudited. Past performance is no guarantee of future returns. ALL RIGHTS RESERVED.

Hennessee Long/Short Equity Index

Long/short equity funds that invest in US domestic stocks that the portfolio manager believes will appreciate in value and short stocks that the portfolio manager believes will depreciate in value. Volatility and return expectations are generally higher than non-correlated funds because of the manager's utilization of market risk, and hence the fund's long-term correlation to the US equity markets.

Hennessee Event Driven/Arbitrage Index

Funds that invest in arbitrage opportunities or event driven situations. Volatility and return expectations are generally lower than correlated funds because of the manager's desire to minimize market risk and focus on individual opportunities within the equity and fixed income markets.

Hennessee Global/Macro Index

Funds that invest in securities (equity, fixed income, currencies, or commodities) with an international scope. Strategies range from long/short equity managers to macro hedge funds. Volatility and return expectations are generally equivalent to correlated funds because of the manager's utilization of market risk.

Standard & Poor's 500 Index (S&P 500)

The S&P 500 Index is an unmanaged market capitalization-weighted measurement of changes in stock market conditions based on the average weighted performance of 500 widely held common stocks. The Index does not reflect sales charges, commissions, expenses or taxes. It is calculated on a monthly basis.

Russell 2000 Index

The Russell 2000 Index is an unmanaged market capitalization-weighted index of 2,000 small company stocks. The Index does not reflect sales charges, commissions, expenses or taxes.

Lehman Brothers Intermediate Government Corporate Bond Index

The Lehman Brothers Intermediate Government Corporate Bond Index is an unmanaged market value-weighted index of government and investment-grade corporate fixed-rate debt issues with maturities between 1 and 10 years. The Index does not reflect sales charges, commissions, expenses or taxes.

Dow Jones Industrial Average

The Dow Jones Industrial Average is an unmanaged price-weighted index based on the stock prices of 30 major industrial companies.

MSCI EAFE (USD) Price Index

The MSCI EAFE Index is an unmanaged arithmetic, capitalization-weighted average of the performance of approximately 1,000 securities listed on the stock exchange of the countries determined by MSCI to be "developed". The Index does not reflect sales charges, commissions, expenses or taxes.

NASDAQ Composite Index

The NASDAQ Composite Index is an unmanaged index of over 5,000 over-the-counter stock prices that does not assume the reinvestment of dividends. The Index does not reflect sales charges, commissions, expenses or taxes.

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