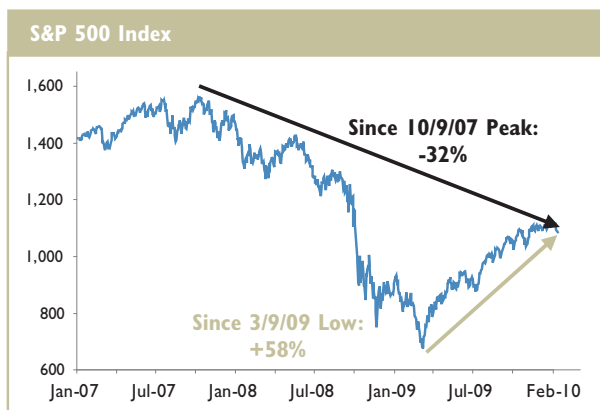


THE MARKET OBSERVER

FEBRUARY 2010

After advancing 26% during 2009, stocks (as measured by the S&P 500) continued to rally through the beginning of the year before selling brought prices down 8% from their January 19th post crash highs. The S&P 500 closed at 1,070 on 2/9/10, down 4% for the year, up 58% from its March, 2009 low and down a net 32% from its October, 2007 peak.



Source: Russell Investment Group, Standard & Poor's, FactSet, J.P. Morgan Asset Management.

Most market commentaries cited credit tightening in China, Sovereign debt woes in Europe and the President's public attack on Wall Street as the motivation for the latest sell off. A decline of 8%, however, after a recovery of almost 70%, is not uncommon, and certainly was not unexpected. The market's anticipation of an improving economic environment now appears to be reflected in stock prices. Any prospect of

a stall in this momentum should bring with it increased volatility.

The post-crash advance now seems to be consolidating as it waits for confirmation of expected corporate profits, with the S&P 500 trading around the 1,100 level. Further advances from this point will be predicated on the avoidance of negative surprises and of course signs supporting the sustainability of this recovery and the avoidance of a debt liquidation relapse toward recession.

The trauma experienced over the past two and a half years makes it very difficult for investors not to get jumpy, even during what can be considered a normal correction. The practice of a contrarian approach to buy when others are selling is always difficult, even more so when fear of economic Armageddon is still fresh in our minds.

Buying stocks or at least maintaining positions proved to be the right call in March, 2009. Staying the course will require discipline amidst the understandably negative market sentiment that permeates today's media. Trillion dollar government deficits and a ballooning Federal debt are the most common fears. The prospect of a long, drawn out recovery of employment

levels, still pending commercial real estate loan write offs in the billions and fears of inflation on the horizon are certainly convincing arguments to play it safe. Contrasting this negative backdrop with savings yields of less than 1/2 of 1% and signs of improving economic conditions provides the motivation for diversified and balanced investors to maintain their growth allocations at least at the lower end of their target ranges. The prospect of improving sentiment gradually spurring the re-investment into stocks of just a portion of the vast cash horde that currently exists on the sidelines is another potential positive for stocks going forward.

Money Supply Component	\$ Billions	Weight in Money Supply
M2 - M1	6,703	69.3%
Retail MMMFs	826	8.5%
Savings deposits	4,776	49.4%
Small time deposits	1,102	11.4%
Institutional MMMFs	2,266	23.4%
Cash in IRA & Keogh accounts	699	7.2%
Total	9,668	100.0%

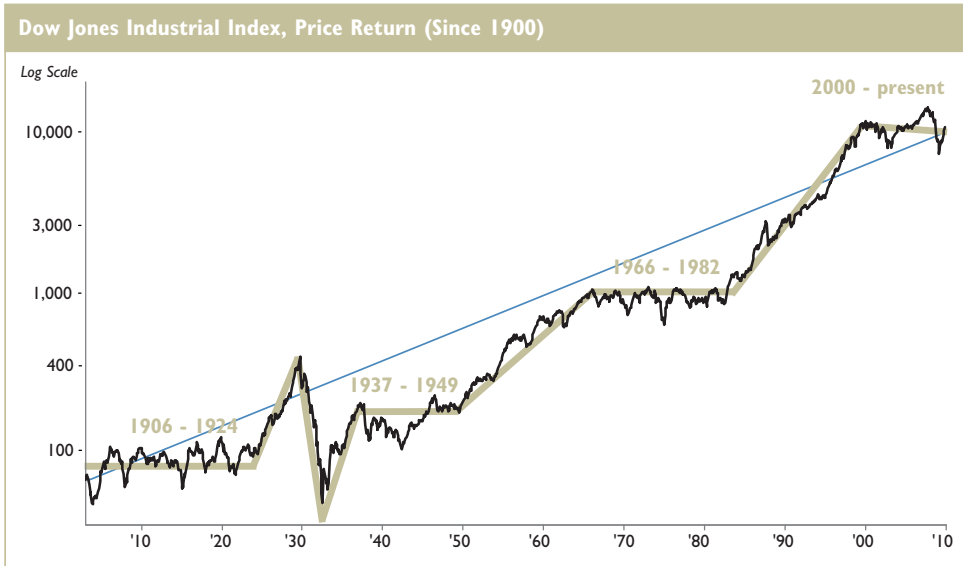
Source: The Federal Reserve, J.P. Morgan Asset Management.

Unemployment may very well take five to seven years to materially improve, but that does not

mean corporate profits and stock prices won't improve along the way. Government deficits will most probably exceed \$1T or more over the next few years, but that does not mean our country won't take steps, as conditions improve, to at least incrementally

based shifts will be successful. Other times they won't. Those who exited the markets last March are obviously lamenting their decision. Those who maintained their holdings can't help being tempted by the recent correction to count their blessings and play it safe.

1990, financials represented less than 10% of the value of our domestic stock market. This percentage increased to 22% at the height of the credit bubble in 2007 and now stands at 15% after briefly falling to as low as 9% in March 2009. What will be the overall composition in 2020? What sectors will materialize spurred by the latest innovation and opportunity? How successful will the Fed be in withdrawing the reserves they were forced to inject into the financial system to prevent a collapse? When will interest rates rise in tandem with economic activity and most probably inflation, which is a normal and necessary evil? Only time will tell. Tactical moves along the way may prove to be costly or successful. Long-term growth allocations should be rewarded. Liquidity reserves, income and absolute return investments will hopefully continue to pay the bills while we wait for longer term investments to reach their potential. The one caveat to all of this, as always, is will the world economy continue to innovate and grow despite the best efforts of world governments to continue to spend money they don't have.



Source: IDC, FactSet, J.P. Morgan Asset Management.

get our financial house in order. The Market's behavior over the past few months as the health care debate raged on Capitol Hill is interesting to note. It didn't seem to be overly preoccupied either with the fear of global warming or the possible scrapping of cap and trade legislation along with the health care initiative. As politicians continue to try and grab headlines, talking about the need to create jobs, growth can only be spurred by risk takers in this country and across the globe who continue to find opportunity.

Investors, quite naturally, will continue to act based upon what they "think" they "know." Often times, emotional or tactically

Going forward, expectations are for a consolidation of stock prices along with increased volatility, followed by moderate and gradual advancement as profits continue to improve. Low interest rates and tame inflation historically have been stimulative for stocks. Continued public skepticism over the world economy and the prospects for stocks going forward is also a historically reliable, contrarian indicator.

When trying to envision the stock market 10 years out, hopefully at levels reflecting profit growth in line with historical comparisons, it is interesting to look at the composition of our economy compared to 20 years ago. In

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