

National Economy

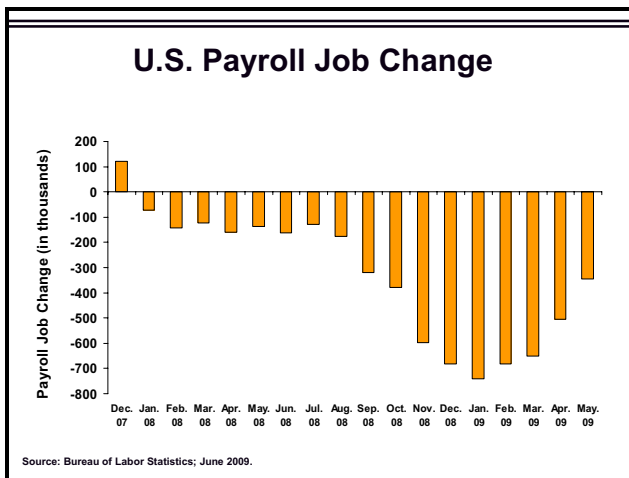
Mid-Year 2009

THE NATIONAL ECONOMY MID-YEAR 2009

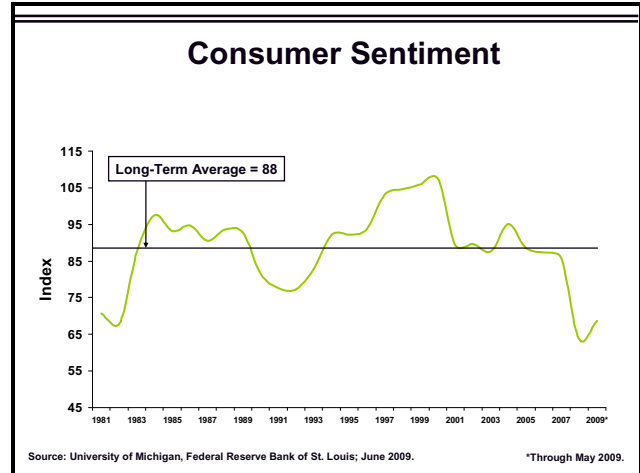
Recession Easing

The national economy has been in a recession for 18 months. Although we expect further decline, a handful of indices are showing signs the recession is easing and may end in 2009.

- GDP declined 5.7% during the 1st quarter of 2009, not great news, but less than the 6.3% decline during the 4th quarter of 2008.
- Monthly job losses are declining at a reduced pace, since the peak in January.



- Companies have slashed inventories – gradually restoring the supply/demand balance.
- Retail sales increased 0.5% during May 2009, the largest rise in four months.
- The Dow Jones has increased 33% since a low of 6,547 in March 2009.
- The leading economic indicators index increased 1.0% in April 2009, after declining 0.2% in March, and 0.5% in February.
- Consumer sentiment, although still low, is starting to rise.



- The Purchasing Managers' Index (PMI), although still below 50 – an indicator of contraction – has risen to 42.8 in May 2009 from a low of 32.9 at December 2008.

These indicators signal a light at the end of the tunnel, as the economy is contracting at a reduced pace. However, we are not out of the woods yet, as the financial markets remain unsettled, bankruptcies remain a concern, and further job losses are expected.

We believe the following indicators will help push the economy towards the start of recovery by year-end 2009:

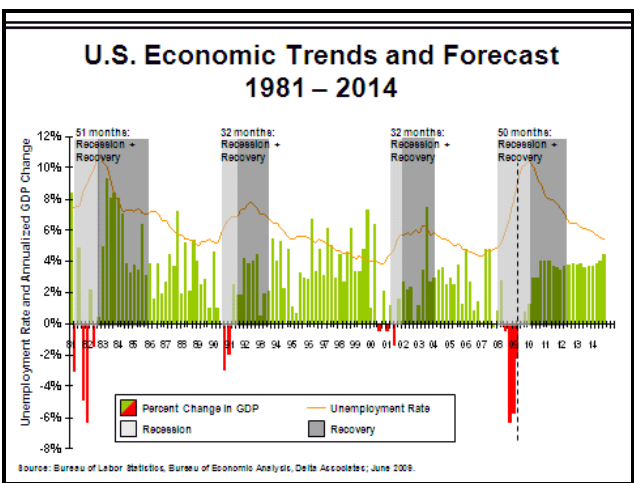
- The Federal Funds Rate remains 0% to 0.25% to help stimulate the economy.
- The \$15.5 trillion Federal stimulus and bailout initiative continues to filter through the economy.
- The overpriced housing market has become affordable again, allowing first-time homeowners in the market. And mortgage interest rates remain near their lowest levels in memory.

- Negative media headlines, thought to sink consumer confidence, are featuring positive headlines again – “Fewer Jobless Seek First-time Benefits,” “Retail Sales End 2-month Slump,” “Economic Decline Slowing.”

We believe the economic outlook is as follows:

- GDP: negative 3.0% in 2009; positive 1.6% in 2010.
- Payroll jobs: negative 3.0 million for 2009.
- The housing market: Stabilization in 2009, leading to traction by 2010.

When will the economy get better? We think the economy will perform sub-par through 2009, with the worst performance behind us. Recovery will begin by late 2009. By the end of 2011 we will begin to feel that we are returning to “normal” conditions.



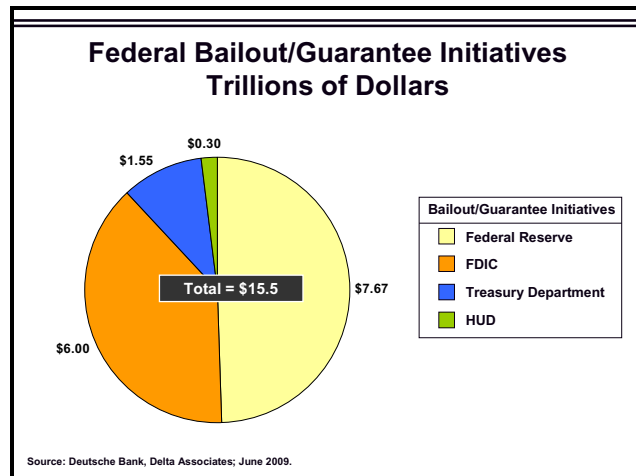
Why do we believe that the economy will come out of recession during 2009 and begin its recovery? Two reasons:

1. There are early signs the recession is easing.
2. Adjusted for inflation and scale of the economy, in 2008 – 2009 the Federal government intervened in the economy at a scale comparable to that of the 1930s and 1940s to jump start the national economy. This should be enough stimulus to re-start the economy.

Federal Intervention

Of the \$15.5 trillion allocated to the economic recovery, 27% or \$4.2 trillion has been spent so far at the time of this writing. The capital injection and guarantees focus on such efforts as:

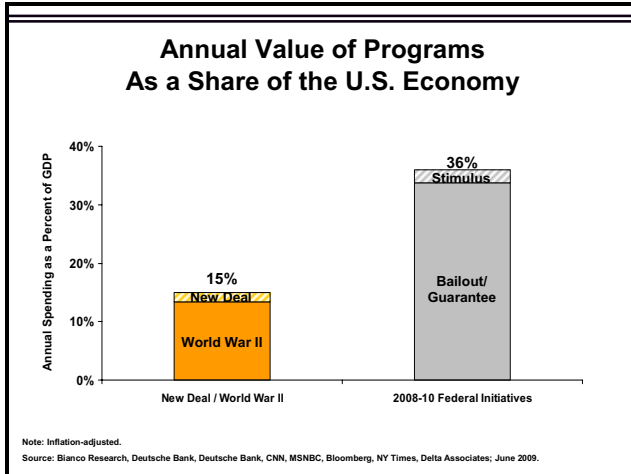
- Creating or saving 3.5 million jobs in infrastructure and construction under the American Recovery and Reinvestment Act
- Restarting the flow of credit through the Consumer and Business Lending Initiative, which will generate up to \$1 trillion in new lending
- Helping struggling homeowners with mortgage restructuring and refinancing, which will assist as many as 9 million homeowners facing foreclosure



Given the current recession is one of the worst downturns since the Great Depression, some wonder if today’s Federal initiatives will be enough. Although there is no guarantee of success, **today’s response is comparable in magnitude to that which followed the Great Depression:**

- The \$15.5 trillion injection of stimulus/bailout activity into the economy will occur at the rate of \$5.2 trillion a year – **or 36% of the size of the \$14.3 trillion U.S. economy (GDP).**
- In today’s dollars, annual spending on the New Deal and World War II was \$369 billion per annum, **or 15% of the then \$2.5 trillion economy (GDP).**

And today's programs are being implemented more quickly and on a voluntary basis – before the crisis became so bad that the government could only play catch-up and try to maintain a minimum standard of living for its citizens, as occurred during the 1930s.



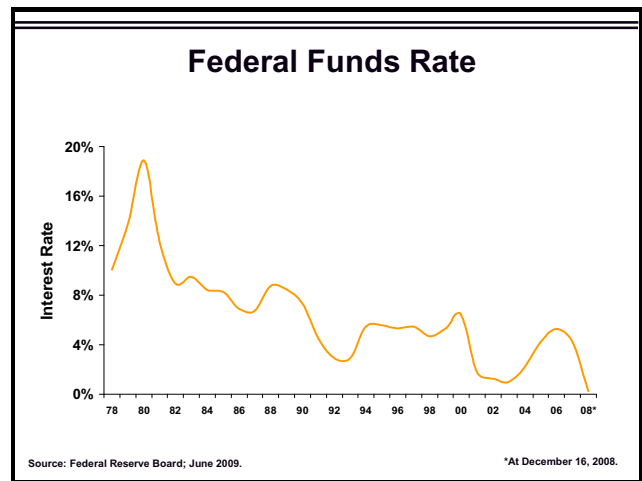
It is due to these scenarios (scale and spread) that we believe the Federal government will be effective – to help cushion the nation from the worst of the recession and bring it to close while restarting the flow of credit.

But three things must happen for this to work effectively and end the recession:

- The \$15.5 trillion Federal initiatives must be spent wisely – at least as wisely as in the 1930s/40s.
- Toxic assets must be removed from the balance sheets of our financial institutions so they can lend again.
- The national consumer funk must end.

We see a good probability of all three.

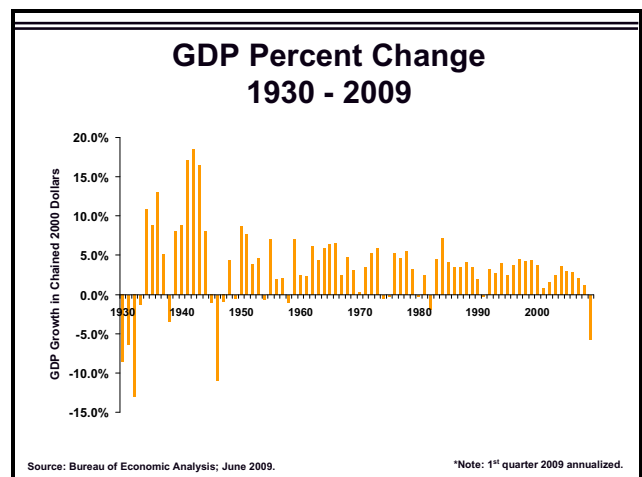
Some are worried that inflation will derail the recovery. The Fed has promised to do what it takes to get the economy back on track. However, given the economy is now contracting at a reduced pace, we believe the Fed will start to increase rates modestly by year-end to head off inflation.



Now, for a look at the components that make up our economy:

Gross Domestic Product (GDP)

The GDP (seasonally adjusted annual rates) decreased 5.7% during the 1st quarter of 2009, after declining a revised 6.3% during the 4th quarter of 2008. Although the 1st quarter decline was less severe than the expected 6.1% decline, it was still the second-biggest quarterly decline in 27 years.



Consumer expenditures increased 1.5% during the 1st quarter of 2009, below the 25-year annual average of 3.3%. Although positive news, consumers spent mainly on durable goods, as non-durable goods declined.

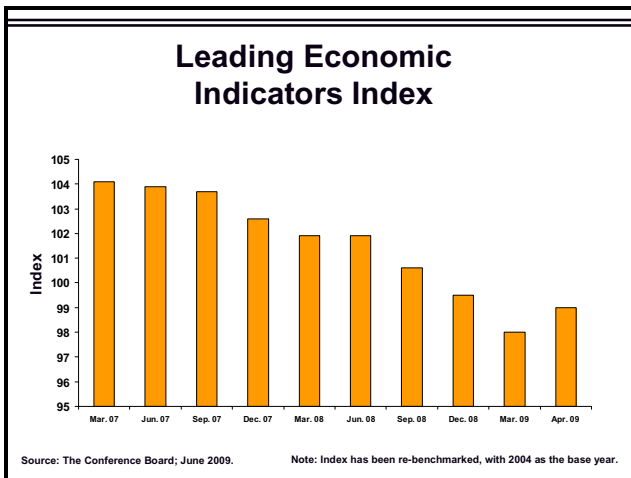
Gross private domestic investment hampered the GDP during the past three months, as investment declined 49.3%. The export of goods declined 28.7% during the 1st quarter, as the recession expanded to the global economy, curtailing spending on U.S. goods.

With consumer confidence low, we expect the GDP to decline further during the 2nd quarter of 2009, but at a reduced pace of 2.4%, when the numbers are finalized.

We expect GDP to improve during the 2nd half of 2009, as the Federal stimulus and capital injections work their way into the economy. For the year, we expect the GDP to decline 3.0%, similar to the low experienced during the early 1980s recession. The GDP should rebound with 1.6% growth in 2010, about half of the long-term average.

Leading Economic Index

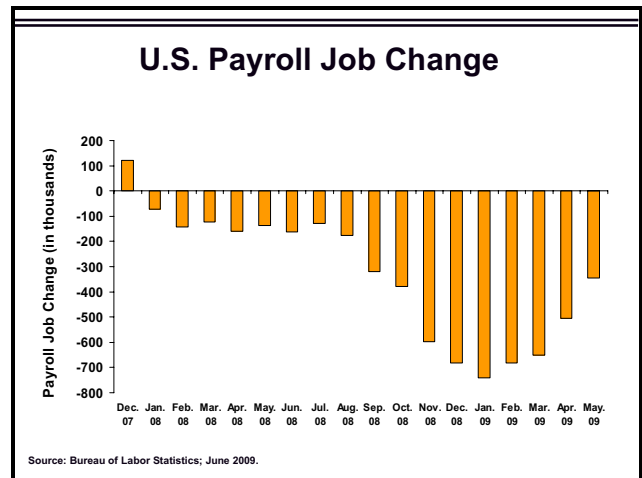
The leading economic indicators index increased 1.0% in April 2009, after declining 0.2% in March, and 0.5% in February. Although the rise to 99.0 at April 2009 is a positive sign for the economy, the index is below the 102.0 experienced one year ago.



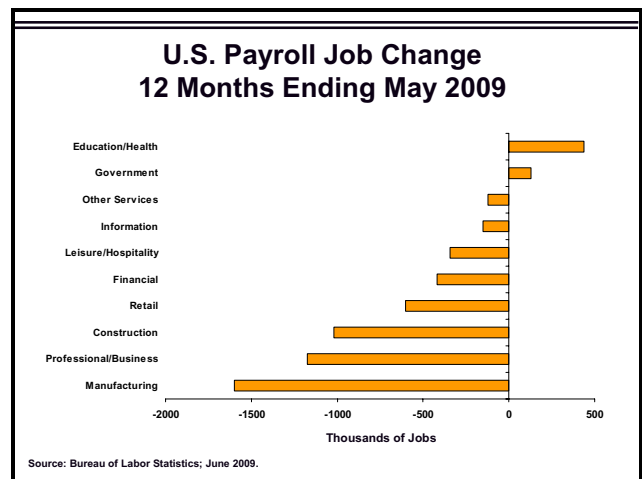
Payroll Jobs

Approximately 6.0 million jobs have been eliminated since the start of the recession in December 2007 – a 4.3% decline. The goods producing and service providing sectors lost 3.0 million jobs each during this period.

On a month-to-month decline, the peak in job losses was experienced during January 2009. Since January, the nation continued to shed jobs, but at a reduced rate. During May 2009, the nation cut 345,000 jobs, compared to the monthly average of 353,000 jobs lost since the start of the recession. Notably, declines moderated in construction and several service-providing industries during the month of May.



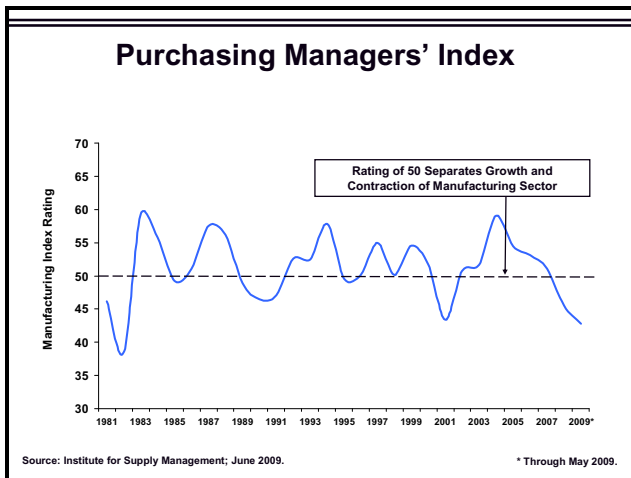
Not all sectors are cutting jobs, as the Health/Education and Government sectors added 436,000 and 128,000 new jobs during the 12 months ending May 2009, respectively.



The manufacturing sector experienced the most job cuts, as demand for goods has dwindled. This sector cut 1.6 million jobs during the 12 months ending in May 2009. An indicator of market health, the Purchasing Managers' Index (PMI) was at 42.8 in May 2009, compared to 49.3 one year earlier.

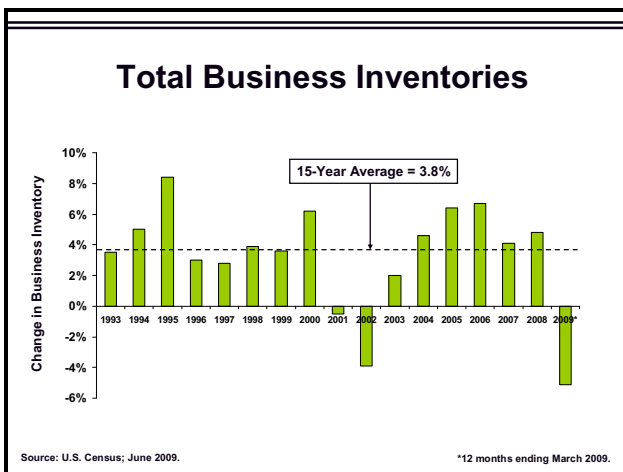
Although the current rating indicates manufacturing is contracting, as it is below the benchmark of 50, the index has been gradually rising since a low of 32.9 at December 2008.

We expect the demand for goods and services will remain low during the balance of the year, driving further job cuts, particularly in the manufacturing sector.



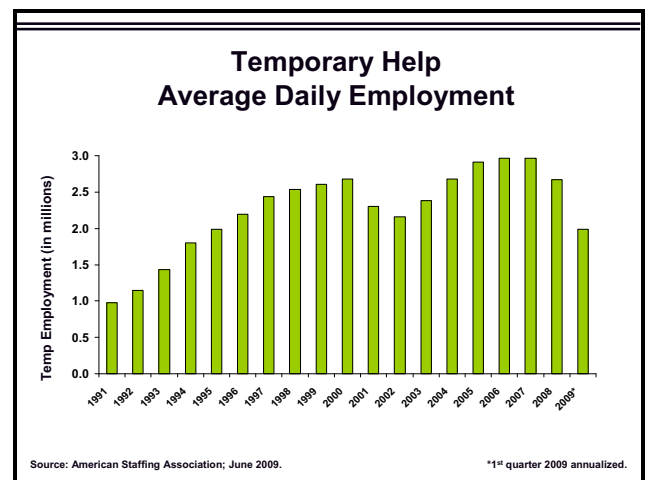
Business inventories grew at an above-average pace during 2004 through 2008. However, with the recession hampering consumer spending, businesses have been working to reduce stockpiles. During the 12 months ending 1st quarter 2009, companies slashed inventories by 5.1%.

With reduced inventories, the supply/demand ratio will gradually balance. Although retail sales declined 9.7% during the 12 months ending May 2009, sales increased 0.5% during May, the largest increase in four months.



One indicator to watch is the hiring of temporary employees. The rise in temporary employment indicates companies need workers in order to keep up with demand, but do not want to hire full-time staff until they are certain economic recovery is underway.

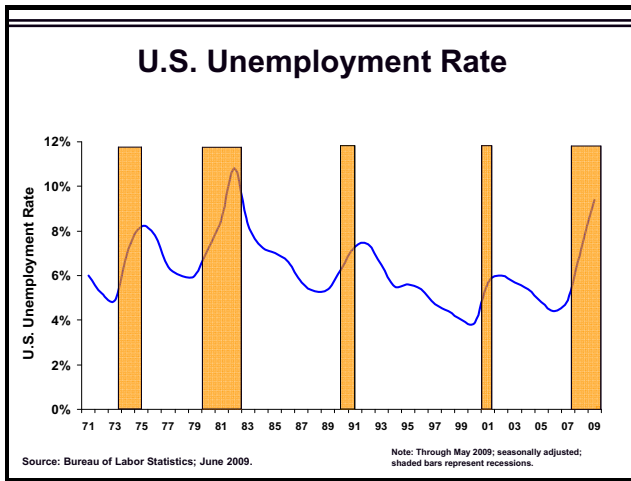
The temporary employment level is 2.0 million at 1st quarter 2009, when annualized, according to the American Staffing Association. This is down 33% from the peak in 2007. We believe temporary employment will start to rise by late 2009, as companies test their confidence in the economy.



Unemployment Rate

The U.S. unemployment rate is 9.4% as of May 2009, a 26-year high. However, the underemployed rate is 16.4%. This rate includes employees working part-time and overqualified workers taking a lower-skilled position.

We anticipate the unemployment rate will exceed 10.0% in late 2009, then peak, possibly at 10.6% in 2010. Although economic growth will return late this year, unemployment will lag and continue to rise during the first part of 2010. The Federal Reserve predicts unemployment will remain elevated through 2011 and will gradually decline to a normal state of around 5% in 2013.

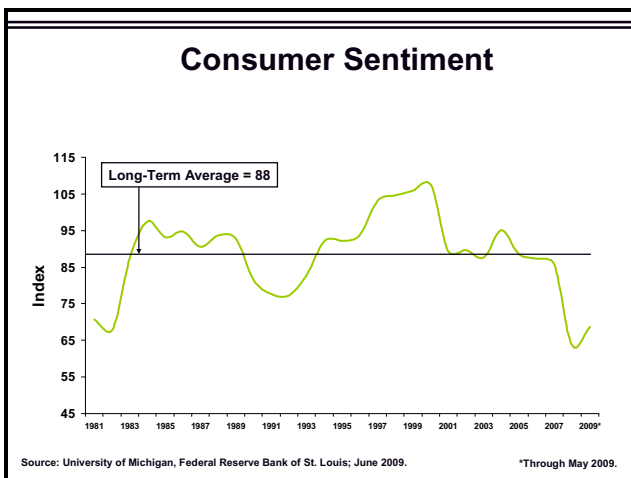


Consumer Sentiment

The University of Michigan's monthly index of consumer sentiment is 68.7 at May 2009. Although the index is below the long-term average of 88.2, it is up compared to 59.5 one year ago.

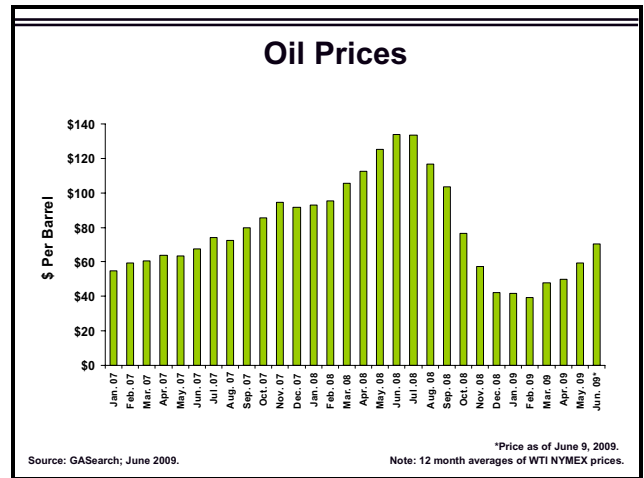
Sentiment declined as job losses and financial pains were of concern to respondents. However, with a new President dispensing funds to stimulate the economy, sentiment has risen each month since the low of 56.3 in February 2009.

Although we expect consumer sentiment to remain low during the remainder of the year, it should continue to steadily rise as the impact of the Federal stimulus and capital injections are realized during this period.



Energy Prices

Oil prices are starting to rise steadily again, after sinking to a low of \$39 per barrel at February 2009. Since this bottom, prices have increased 79% to \$70 a barrel at the time of this writing.



As prices dropped, OPEC cut oil production by 3 million barrels a day in order to regain supply/demand balance. However, this reduction is above the current demand levels and has prompted prices to rise. The cartel's preferred price range is \$60 to \$80 per barrel.

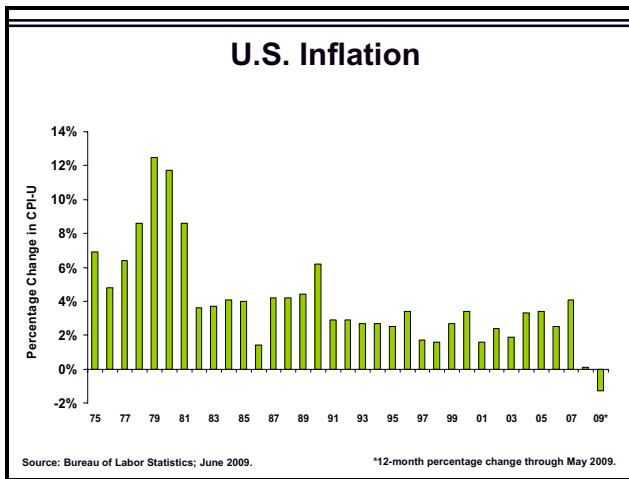
Gas prices have declined to \$2.62 per gallon at this writing, a 36% reduction during the past year. Although gas prices declined to a more affordable rate, OPEC's reduction in oil supply could force prices to unpalatable levels again. Gas prices recently began rising again for the summer driving season.

We expect oil prices to average \$60 per barrel in 2009. If oil rises to \$80 per barrel, the cost to the consumer will be too high given the economic climate, which will reduce demand and push oil prices back down.

Inflation

Prices declined 1.3% during the 12 months ending May 2009. The decline was generated by the decline in energy prices, as gasoline consumption declined 7.3% over the past year.

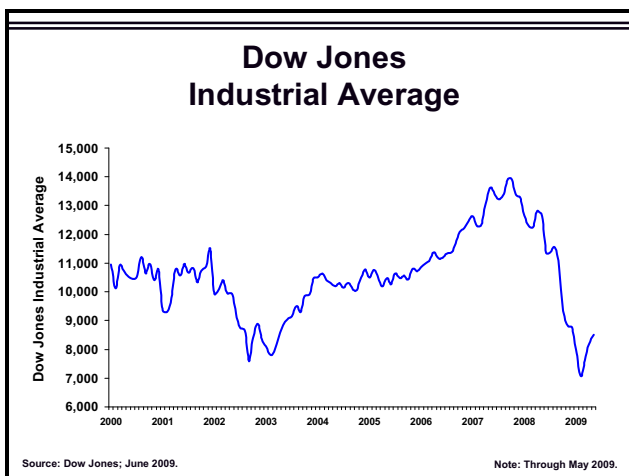
We believe that inflation will be controlled at 0.5% to 1.0% during 2009, as companies work to get rid of high inventories and consumer spending remains lackluster. Although deflation remains a concern, we do not anticipate an onset of deflation as prices of food, housing, and medical costs continue to experience inflation. As consumer confidence returns, the Fed will watch for inflationary effects on commodity prices.



Stock Market

The stock market is not the economy. But many believe it is a leading indicator – a predictor of economic conditions in 12 months or so. The Dow Jones peaked in late 2007.

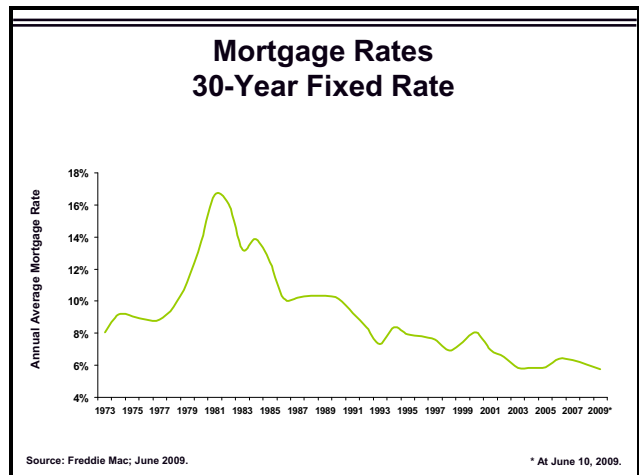
It appears the stock market bottomed out in March 2009, with the Dow around 6,500. Since March, the Dow has increased approximately 33%, as consumers are starting to regain confidence and stocks are at bargain rates, allowing buyers to reap the rewards of the next economic expansion.



Mortgage Rates

The 30-year fixed mortgage rates were at their lowest since records have been kept – below 5%. This was a boon to home buyers. However, tight underwriting requirements have kept some buyers out of the market. By late June, rates had risen to 5.50%, as bond yields rose.

To halt rising foreclosures, President Obama’s housing plan will allow 4 million homeowners facing foreclosure to modify their loans to reduce monthly payments. An additional 5 million will be able to refinance if their home value has declined below its purchase price.



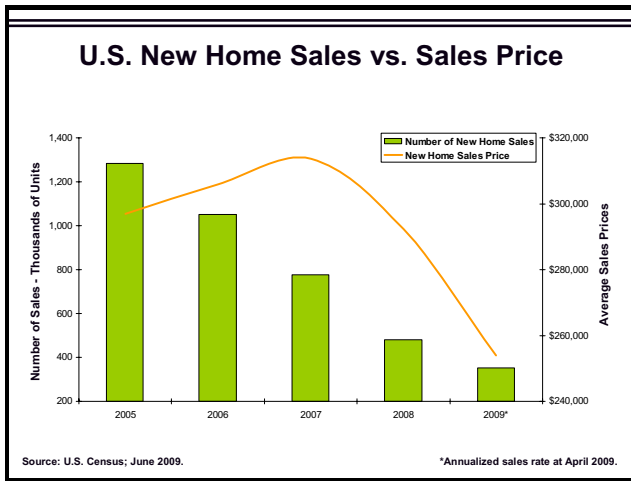
New Housing Construction and Sales

The number of new homes started during the 1st quarter of 2009 declined 52%, compared to the total starts during the 1st quarter of 2008. Starts during 2008 and 2007 declined 41% and 21%, respectively.

A continuing decline in starts is good news – not for home builders, but for the housing market in general, as reduced inventories will allow supply and demand to reach equilibrium.

New homes sold at an annualized rate of 352,000 units during the 12 months ending April 2009, down 34.0% from one year earlier.

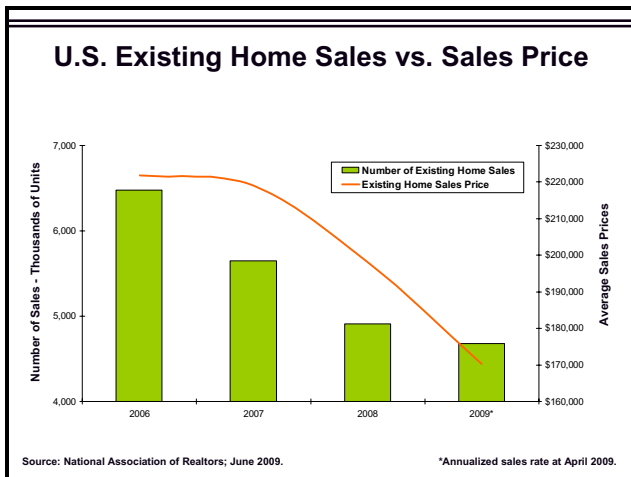
Sales prices on new homes declined to an average of \$254,000 per unit in April 2009, down 19.2% from one year earlier.



Existing Home Sales

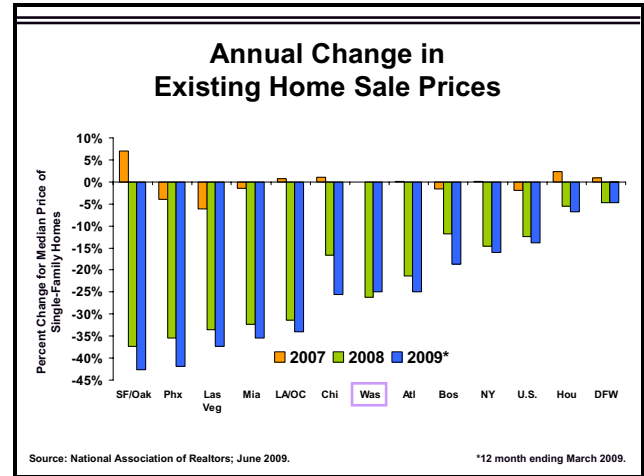
Existing homes sold at an annualized rate of 4.7 million units during the 12 months ending April 2009, down 3.5% from one year ago. The current inventory is at a 10.2 months supply, down from 11.3 months one year ago.

Sales prices on existing homes declined to an average of \$170,200 per unit, down 15.4% from one year ago.



Among major metros, according to the NAR, price changes during the 12 months ending March 2009 ranged from -42.7% (San Francisco/Oakland) to -4.7% (Dallas/Ft. Worth).

The San Francisco/Oakland metro area remains in first place for greatest decline in home sale prices. The recession impacted San Francisco/Oakland later in the timeline compared to other metros like LA/OC, which was first to suffer due to the high concentration of subprime lenders. However, San Francisco/Oakland is now feeling the pinch, as this metro, ripe with a high-tech economic base, is losing ground as companies curtail spending in this sector.

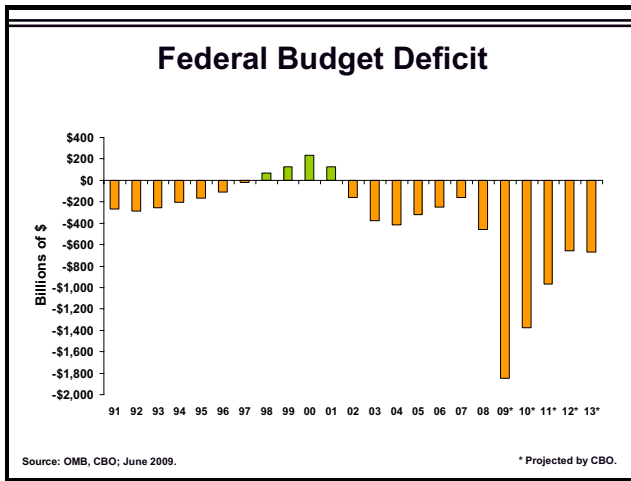


We believe housing sales prices will continue to decline through 2009, although volume increases will be realized in select metro areas. However, with low mortgage rates, we do expect that the housing market in many metro areas will stabilize in 2009 and find traction in 2010.

Federal Budget Deficit

The Federal budget deficit climbed to \$459 billion during 2008, as spending exceeded revenues. The deficit was boosted by the \$168 billion Economic Stimulus Act of 2008.

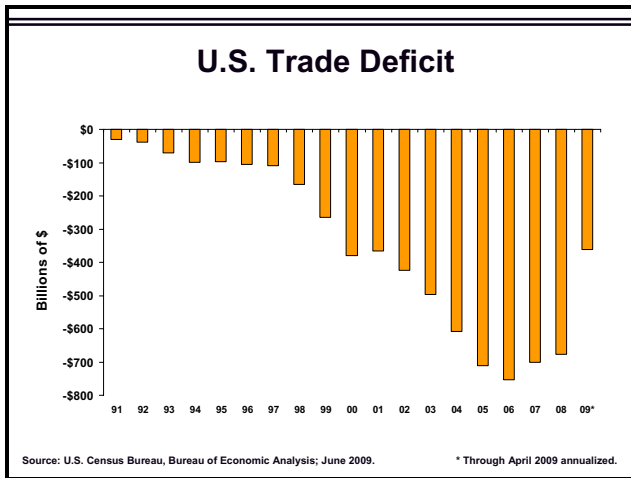
The Congressional Budget Office (CBO) anticipates, with the most recent projections based on President Obama's budget, the U.S. budget deficit for 2009 will total \$1.85 trillion. The deficit will balloon this year, as the government realizes TARP, the auto bailout, and the American Recovery and Reinvestment Act, among other assistance programs.



U.S. Trade Deficit

When annualized, the trade deficit through April 2009 retracted to \$361 billion, compared to \$677 billion in 2008. Annualized exports declined 18% from 2008, compared to imports which declined 27%.

We expect exports to decline notably during 2009, as our global partners experience a steeper and longer recession compared to the U.S. Imports should decline as well, as American consumers demand fewer goods.



Economic Outlook

Initial indicators suggest we are at the bottom of the recession. However, we expect further contraction through much of 2009, as consumer confidence, albeit edging up, remains low and credit markets remain unsettled. Although the Federal government has thrown \$15.5 trillion into solving the current recession, it will take some time before all programs are realized and recovery is experienced.

We expect the GDP to decline further during the 2nd quarter of 2009, but at a reduced pace of 2.4%, when the numbers are finalized. The GDP should make very slight positive gains during the 3rd and 4th quarters, as the economy bottoms out and a slow recovery begins. We anticipate a recovery period of 30 months – running through 2011.

Our forecast for GDP growth is -3.0% in 2009 and positive 1.6% in 2010. This compares to the long-term average growth of approximately 3% per annum.

National Payroll Job Growth Summary

The U.S. economy shed 5.4 million payroll jobs over the 12 months ending May 2009. This represents a decline of 3.9%. The pace of job change has been rapid, as 6.0 million jobs have been cut since the start of the recession.

U.S. Payroll Job Growth		
	Job Change	%Change
2009*	-5,366,000	-3.9%
2008	-558,000	-0.4%
2007	1,527,000	1.1%
2006	2,397,000	1.8%
2005	2,276,000	1.7%
2004	1,423,000	1.1%
2003	-344,000	-0.3%
2002	-1,489,000	-1.1%
2001	36,000	0.0%

*Change for 12 months ending in May 2009; others are comparisons of annual averages. Note that BLS has rebenchmarked figures since their initial publication; the figures presented above are the most recent estimates.

12-MONTH PAYROLL EMPLOYMENT CHANGE THROUGH APRIL 2009					
METRO AREA	JOB CHANGE		METRO AREA	JOB CHANGE	
	#	%		#	%
Austin	3,400	0.4%	Las Vegas	(54,700)	-5.9%
Oklahoma City	(2,900)	-0.5%	Denver-Boulder	(57,900)	-4.1%
New Orleans	(3,200)	-0.6%	Seattle	(60,600)	-3.4%
San Antonio	(4,600)	-0.5%	Minneapolis-St. Paul	(62,500)	-3.5%
Memphis	(14,200)	-2.2%	Boston (Metropolitan NECTA)	(70,800)	-2.8%
Columbus (OH)	(18,700)	-2.0%	Philadelphia	(90,100)	-3.2%
Salt Lake City	(19,600)	-3.0%	South Florida		
Raleigh-Durham	(21,200)	-2.6%	West Palm Beach/Boca Raton	(23,700)	-4.3%
Kansas City	(23,800)	-2.3%	Fort Lauderdale	(32,700)	-4.2%
Jacksonville	(25,600)	-4.1%	Miami/Miami Beach/Kendall	(41,300)	-3.9%
Pittsburgh	(27,600)	-2.4%	Subtotal South Florida	(97,700)	-4.1%
Nashville	(28,400)	-3.7%	San Francisco Bay Area		
Washington, DC	(30,300)	-1.0%	San Francisco/San Mateo/Redwood City	(39,700)	-4.0%
Indianapolis	(30,800)	-3.4%	San Jose/Sunnyvale/Santa Clara	(40,000)	-4.4%
St. Louis	(34,200)	-2.5%	Oakland/Fremont/Hayward	(43,100)	-4.2%
Cincinnati	(34,400)	-3.3%	Subtotal Bay Area	(122,800)	-4.2%
Houston	(35,300)	-1.4%	Atlanta	(123,600)	-5.1%
Baltimore	(38,000)	-2.9%	Phoenix	(129,700)	-6.8%
Sacramento	(43,600)	-4.9%	Detroit (Detroit/Warren/Livonia)	(143,400)	-7.5%
San Diego	(45,300)	-3.5%	Chicago	(190,400)	-4.2%
Cleveland	(48,100)	-4.5%	New York	(234,400)	-2.7%
Dallas/Ft. Worth	(49,500)	-1.7%	LA Basin		
Portland (OR)	(49,600)	-4.8%	Orange County (Santa Ana/Anaheim/Irvine)	(72,600)	-4.8%
Charlotte	(52,100)	-6.0%	Riverside/San Bernardino/Ontario	(78,500)	-6.3%
Tampa-St. Pete	(53,400)	-4.3%	Los Angeles/Long Beach/Glendale	(167,900)	-4.1%
Orlando	(54,600)	-5.0%	Subtotal LA Basin	(319,000)	-4.7%

Source: Bureau of Labor Statistics, Delta Associates; June 2009.