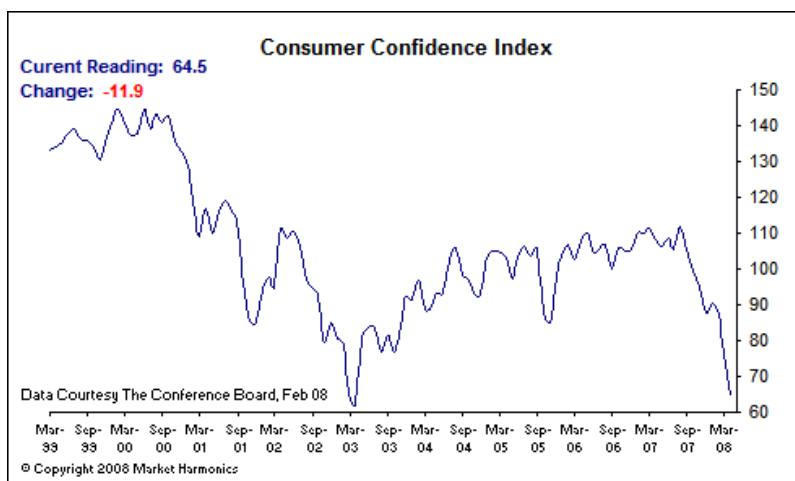


Quarterly Market Commentary – Q108 April 2008

Government Responds to Economic Challenges

The Federal Reserve (Fed) and Congress combined to respond decisively to credit market woes and worrisome economic reports in the first quarter of 2008, taking steps to buttress a banking system buckling under the weight of the subprime mortgage malaise, as well as trying to spur future consumer spending. The Fed undertook a series of actions—dropping the federal funds target rate to 2.25 percent from 4.25 percent at 2007 year-end, offering to make loans to previously unwelcome financial institutions, and helping to orchestrate the sale of failing investment bank Bear Stearns. All of these moves were intended to ease mounting strains on the U.S. banking system. Major financial institutions, having incurred steep losses from faltering subprime mortgage-related investments, had become increasingly risk-averse, unwilling to make loans to all but the most creditworthy borrowers and creating a logjam in normal credit market functioning.

Congress, for its part, pushed through a \$160-billion fiscal stimulus package in February, which provides tax rebates to senior citizens, veterans, and low- and moderate-income households and which should impart a boost to economic activity in the middle of the year. Policymakers' next focus may well be to bolster the residential housing market, where slowing sales and falling home prices have dampened the mood of many consumers. As a result, the Consumer Confidence Index fell sharply and now rivals the low set in 2003.



Treasuries a Safe Haven

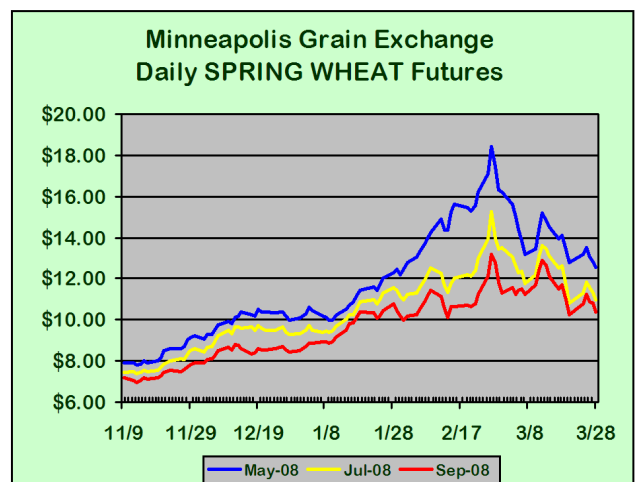
Investors, spooked by the dual impact of recessionary fears sparked by weak economic and housing data and worries that the true magnitude of mortgage-related losses remained unknown, sought safety in U.S. Treasuries. The swirling uncertainty led to a Treasury buying spree, to the detriment of stocks and other fixed income investments. Stock indices declined across the board with little regard for market cap, investment style, or geographic location.

The Dow Jones Industrial Average eked out a slight gain in March, but fell 7 percent (including dividends) in the first quarter and is now off 13 percent from its October 2007 peak. The S&P 500 Index, which has a larger exposure to the battered financial sector, lost 9.40 percent for the quarter and is down 16 percent from its October high. The tech-heavy Nasdaq and the small-cap Russell 2000 Index have fallen 14 percent and 10 percent, respectively, for the year. While market declines like this are always disconcerting, it is worth noting that the major indices thus far have not reached the 20-percent decline that delineates an official bear market. In fact, the recent volatility falls well within the norms of historical market performance.

With stocks temporarily out of favor, Treasuries stepped prominently to the fore. Treasury yields, which move inversely to their price, fell sharply for the quarter, as investor demand bid up prices for those securities. The 3-month T-bill ended the quarter yielding 1.30 percent, while the 10-year note ended at 2.60 percent and the 30-year bond finished at 4.30 percent. Credit spreads, which are a measure of the yield premium over Treasuries that investors demand for making perceived riskier loans, rose during the quarter, another indication of the flight to quality. Conditions became particularly skewed in the municipal bond market, where heavy selling caused the yield on tax-exempt securities to temporarily exceed that of taxable Treasuries of comparable maturity, a significant anomaly that had not occurred for decades.

Commodities on the Rise

Many commodities, including oil, precious metals, and agricultural products, experienced unprecedented price increases in the first quarter, only to settle back by quarter-end. It was unclear whether the spikes were related to renewed investor preference for physical assets over financial ones, speculation, increased demand, or some combination of the three. However, the quick and significant price swings would support a speculative element. Crude oil, for example, hit an all-time high of \$111.80 per barrel in March, before ending the quarter just below \$102 a barrel. And wheat, an obvious component of many food items, shot up more than 80 percent in mid-quarter, before falling back almost as sharply.



While commodities were a boon to investors in the first quarter, rising prices for key commodities also pose a risk of increasing the cost to consumers for necessities like food, gasoline, and heating oil. However, Fed Chairman Ben Bernanke stated unequivocally in testimony before Congress that the Fed believes inflation will abate, allowing it to continue its stimulative economic policies for the remainder of the year.

Looking ahead, soft housing market conditions and the toll it takes on consumers remains a key lynchpin to the health of our economy. We believe legislative proposals to support ailing homeowners are a likely next step in the coming months.

Disclosure: Certain sections of this commentary contain forward-looking statements that are based on our reasonable expectations, estimates, projections, and assumptions. Forward-looking statements are not guarantees of future performance and involve certain risks and uncertainties, which are difficult to predict. Past performance is not indicative of future results. All indices are unmanaged and investors cannot invest directly into an index. The Dow Jones Industrial Average is a price-weighted average of 30 actively traded blue-chip stocks. The S&P 500 Index is a broad-based measurement of changes in stock market conditions based on the average performance of 500 widely held common stocks. The Nasdaq Composite Index measures all Nasdaq domestic and non-U.S.-based common stocks listed on the Nasdaq Stock Market. The Russell 2000 Index measures the performance of the small-cap segment of the U.S. market consisting of 2,000 small-cap stocks.

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