

QUARTERLY ECONOMIC REVIEW AND OUTLOOK

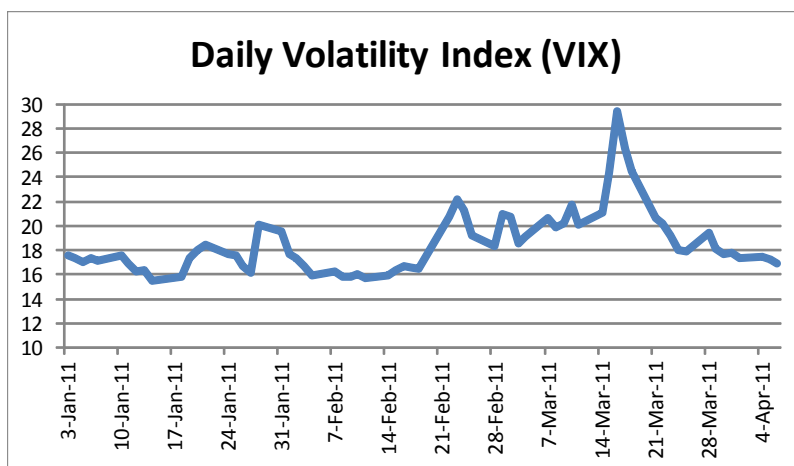
APRIL, 2011

Overview: Economic Expansion Expected to Continue. The first quarter of 2011 brought us significant new concerns about the global economy. So far, the year has delivered a new war in Libya, continuing and expanding unrest in the Middle East, and a tragic earthquake in Japan. These events have all worked together to keep investors on edge causing significantly higher levels of market volatility (see Chart 1: S&P 500 Volatility below). Predicting the exact outcome of all these events is, of course, impossible. However, *our expectation is that none of these risks will derail the global economic recovery.*

We believe that the U.S. employment outlook is improving. This is in part due to slowing corporate productivity, which suggests that firms require additional new hiring to increase output, rather than making better use of existing employees. *This is an important turn in the business cycle, since strong productivity growth was responsible for much of the gains in output earlier on in the recovery.* Also, a slowdown in productivity at this point in the cycle implies that firms have trimmed nearly all of their waste and are now taking advantage of their improved efficiency by hiring. The conditions remain well suited for the recent acceleration in private sector job growth to continue in the months ahead. This gives us hope that growth during Q2 and Q3 will accelerate in a big way.



Abdur Chowdhury, Ph.D.
Chief Economist



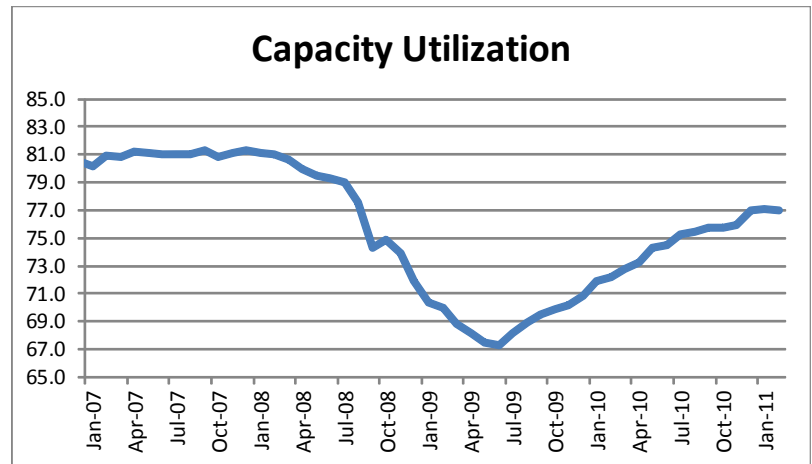
GDP: The Q4 2010 final GDP was reported at an annual rate of 3.1%. Net exports made the largest contribution to growth at the end of the year. Additionally, consumer spending aided by rising demand for durable goods, rose by 4.0%, the highest level of increase since before the recession began.

Manufacturing: According to the Institute for Supply Management, the U.S. manufacturing index in March remained stable at nearly its highest reading since May 2004. This strength is generating job growth, a necessary ingredient

to a sustained economic expansion. The fact is, *manufacturing has been the star of this economic recovery.* While making up only around 12% of total economic output in the U.S., manufacturing has contributed over 30% of the economy's growth since the recession ended. This large contribution is primarily due to inventory investment, rising demand for durable goods, despite an underperformance from housing and services. With low interest rates and pent up demand for manufactured goods at home, and a continued global recovery supporting U.S. exports, manufacturing is likely to remain a key source of economic growth and job creation in 2011.



Industrial Production: Slack Sufficient to Offset Inflationary Pressures. Industrial production was steady in February while capacity utilization remained at just over 76%. The latter remains low by historical standards. So, while high commodity prices may present a current inflationary pressure, *there continues to be plenty of slack and excess capacity in the system which will offset inflationary pressures in the coming months.* Growth in industrial production so far has been capacity absorbing rather than capacity generating. It is still 5% below its pre-recession peak and below its long-run average.



Retail Sales: The Consumer is Coming Back. Retail sales increased 1.0% (seasonally adjusted) in February. Gains in February were broad-based, but the biggest monthly increase was in the sales of automobiles and parts which jumped 2.3%. Note that February is a famously slow month for retailers. Retail sales in February showed a modest increase in store sales, so the seasonally adjusted number perhaps overstates the strength of sales somewhat. Still, the fact that sales did not drop off the way they usually do in February is encouraging. *We expect consumer spending in Q1 2011 to rise by about 3%. This puts the U.S. consumer back at the center stage of the economic recovery.*

Housing: The housing market continues to be the economy's Achilles heel. Housing starts declined by 22.5% in February, the lowest level since April 2009. The volatile multi-family home construction dropped by 46% while single-family home construction fell by about 12%. Building permits, an indicator of future construction, decreased by about 8%, the lowest level on record. Sales of new single-family homes in February 2011 were at a seasonally adjusted annual rate of 250,000, a 16.9% drop from January. Relative to a year ago, sales are down 28%!

In addition to the drop in existing home sales, the price of new homes also declined. The median price of a new home sold fell 13.9% in February to \$202,000 which is 8.9% below the previous year. The differential between the median price of a new and existing home has increased from the historical level of around 12% to the current level of more than 25%. The increase in foreclosure and short sales is undoubtedly a significant factor in pulling existing home prices lower. The existence of this unusually large price gap, along with rising materials prices, is making it difficult for builders to compete with the existing supply of homes.

Declining prices are slowing demand, weighing on household wealth and also leaving consumers with larger mortgages than their houses are worth. The foreclosure pipeline is almost as large as the 3.5 million inventory of unsold existing homes. Unless the inventory of foreclosure drops, the median price differential will remain at the elevated level while construction activity will remain at very low levels.

However, all is not negative in the housing market. We expect a number of factors to provide a boost in the housing market in the coming months including easing credit conditions, affordable prices, improvements in



mortgage delinquencies and the foreclosure market. Increased hiring and improved consumer confidence should also prove to be helpful.

Inflation: Still Under Control. Consumer prices increased by 0.5% in February, bringing the rate of headline inflation to 2.2% on a year-over-year basis. The core CPI, which excludes energy and food prices, also increased by 0.2% in February and year-over-year core CPI increased to 1.1%. In the core measure the increase in prices was basically broad-based. We expect the difference between the headline and core inflation to continue over the remainder of the year as food and energy prices continue to increase. High unemployment and slow personal income growth should keep a lid on core inflation growth in the coming months. Navigating this gap creates a new challenge for the Federal Reserve, that must be careful that higher commodity prices don't feed into inflation expectations and ultimately higher core inflation.

Separately, the core producer price index (PPI) for February increased by 0.2% following a 0.5% rise in January. The PPI for finished goods increased by 1.6% due to strong increases in food and energy prices. As the U.S. economy continues to gain momentum, higher PPI will start to make inroads into consumer prices (CPI). However, given that the economy still has some slack and employment is not growing as fast as in other recovery cycles, the effect on core CPI due to any increase in PPI should be minimal. However, the increase in PPI could have an impact on corporate profitability for manufacturing and industrial companies that have to deal with rising energy and commodity input costs. The equity markets are likely to reflect this change in the coming months.

Labor Market: Slow but Steady Improvement. U.S. non-farm payrolls rose by 216,000 in March while the unemployment rate dropped to 8.8%. Government payrolls continued to decline, marking the fifth straight month that government payrolls have subtracted from the total. The decline was entirely at the local government level, a trend that is likely to continue in the coming months as they try to manage their budget shortfalls. *Private job creation in Q1 accelerated at the fastest pace since the U.S. recovery began.* This is further evidence that expansion has entered a new phase of self-sustained private demand growth.

With this pace of hiring, the U.S. economy can now begin to make more serious headway in replacing the 8.7 million jobs lost during the recession. We expect to see more than 2 million jobs created in 2011 alone. Nonetheless, as discouraged workers rejoin the labor force – the unemployment rate will decline more slowly than this growth would suggest. We expect the unemployment rate to be at around 8.5% by the end of 2011.

Federal Reserve: The Policy Stakes are Rising. A high unemployment rate along with increasing price pressures does not make the Federal Reserve's management of this expansion any easier. With employment momentum picking up in the last two months, the task for the Fed will turn increasingly to managing an exit strategy from the second round of quantitative easing (QE2). QE2 did have some success, helping to drive the stock market higher and leading to a general increase in risk taking as evidenced by the recent pick up in merger and acquisition activity and issuance of junk bonds. Despite growing worries about inflation, we expect the Fed to complete QE2 as planned in June. Interest rates will be on hold until at least the end of 2011.

Trade: The U.S. trade deficit widened to \$46.3 billion in January due primarily to rising oil prices. The recent rise in oil prices and stronger consumer spending and business investments will likely lead to higher imports, putting upward pressure on the U.S. trade deficit throughout 2011. A relatively weaker U.S. dollar – the trade-weighted



currency has depreciated roughly 6.8% since mid-2010 – could provide some offset by boosting exports. However, if concerns regarding the European sovereign debt situation escalate and political turmoil in the Middle East continue, the dollar will likely appreciate, eroding this recent competitive gain.

Outlook on the Economy: We expect both the global and U.S. economic recovery to remain on track, and do not expect to see inflation rise noticeably in the developed world. Corporate profits have remained strong and preliminary indications are that corporations are not being too adversely affected by the increase in energy costs. In fact, corporate hiring plans have been accelerating and we expect job creation to continue.

Although we continue to have a generally optimistic view of the economic backdrop to the capital markets, a number of downside risks persist. One issue is the threat of a federal government shutdown. Although signs are pointing to a growing likelihood of some sort of budget agreement, the potential uncertainty remains. Additionally, investors need to be aware that even if the budget for the current fiscal year can finally be agreed upon, negotiations are already beginning for the 2012 fiscal year, which begins on October 1, 2011, meaning that the question of a budget impasse is not likely to fade in the near term.

Also, some investors are concerned about what will happen when the current Federal Reserve asset purchase program (QE2) is completed on June 30, believing that the end of the Treasury purchases will result in a negative shock for interest rates and stocks. We believe that such concerns are likely overdone. Previous experiences show that when the Fed eased up on its purchase of mortgage securities, the markets managed the transition without a serious problem. Given the cash on hand, improving sentiment and strengthening economy we see no reason for panic.

The short-term risks are clearly dominating market sentiment and confidence levels have dropped. Moving the market past all of this will require some time as well as additional clarity on the downside risks.



Rick Iwanski, CFA
Senior Investment Analyst

Capital Market Commentary: The equity markets continued their quarterly streak of strong positive performance during Q1, reflecting continued investor confidence in a global recovery. Domestic equities led the way with equity returns segmented by asset class and investment style in a tight 6%-9% range. Returns over the past 12 months has simply been sizzling. The best performer, small cap growth, was up over 31% while the “worst” performer was large cap value, turning in a very respectable 15%. The operating leverage smaller companies have to a recovery, plus increased M&A activity does not seem lost on the market. The “lost decade” case made against domestic equities is beginning to recede in the rear view mirror as the last five year return on all sizes and styles of domestic equities is now in positive territory.

Compared to U.S. equities, international markets have lagged recently. The headline concerns about the euro and economic growth in Europe have weighed on that region, while rising inflationary pressures and monetary policy adjustments in emerging markets, intended to cool demand, have also cooled investors in the short term.

(continued on page 6)



Index Performance as of March 31, 2011	1 Month	QTD	YTD	1 Year	5 Year
Russell					
3000 Growth Index	0.42	6.30	6.30	19.24	4.32
3000 Index	0.45	6.38	6.38	17.41	2.95
3000 Value Index	0.48	6.47	6.47	15.60	1.43
1000 Growth Index	0.12	6.03	6.03	18.26	4.34
1000 Index	0.26	6.24	6.24	16.69	2.93
1000 Value Index	0.40	6.46	6.46	15.15	1.38
Mid-Cap Growth Index	1.63	7.85	7.85	26.60	4.93
Mid-Cap Index	1.53	7.63	7.63	24.27	4.67
Mid-Cap Value Index	1.44	7.42	7.42	22.26	4.04
2000 Growth Index	3.75	9.24	9.24	31.04	4.34
2000 Index	2.59	7.94	7.94	25.79	3.35
2000 Value Index	1.39	6.60	6.60	20.63	2.23
S&P 500					
Consumer Discretionary	-0.51	4.71	4.71	21.04	4.67
Consumer Staples	1.62	2.52	2.52	10.56	7.88
Energy	1.54	16.80	16.80	39.82	9.81
Financials	-2.58	3.04	3.04	3.95	-10.68
Health Care	1.89	5.62	5.62	5.11	2.70
Industrials	1.78	8.75	8.75	21.88	3.49
Information Technology	-2.61	3.47	3.47	11.88	4.88
Materials	1.87	4.54	4.54	24.18	6.89
Telecommunication Services	5.28	4.85	4.85	30.37	4.79
Utilities	0.25	2.74	2.74	12.32	4.70
Other U.S. Equity					
Dow Jones Industrial Avg	0.91	7.07	7.07	16.51	4.87
MSCI USA	0.12	5.96	5.96	16.03	2.80
Wilshire 5000 (Full Cap)	0.34	6.00	6.00	17.57	3.30
International Equity - Broad Market					
MSCI EAFE	-2.20	3.45	3.45	10.90	1.78
MSCI Emerging Markets	5.90	2.10	2.10	18.78	11.01
MSCI Frontier Markets	1.32	-5.41	-5.41	5.45	NA
MSCI AC World	-0.06	4.53	4.53	14.63	3.48
MSCI AC World ex USA	-0.19	3.49	3.49	13.61	4.05
MSCI AC Asia ex Japan	6.29	1.22	1.22	19.80	11.44
International Equity - Country Region					
MSCI Brazil	4.00	2.65	2.65	9.74	18.93
MSCI BRIC	5.70	3.26	3.26	12.23	12.61
MSCI China	5.32	2.88	2.88	9.58	16.65
MSCI Europe	-0.79	6.56	6.56	13.29	2.64
MSCI India	11.11	-5.11	-5.11	9.46	12.16
MSCI Japan	-9.12	-4.85	-4.85	1.60	-4.57
MSCI EM Latin America	3.58	0.94	0.94	14.06	16.61
MSCI Russia	5.17	16.29	16.29	30.06	2.46
Fixed Income					
BC Aggregate Bond	0.06	0.42	0.42	5.12	6.03
Merrill Lynch 3-month T-Bill	0.03	0.05	0.05	0.16	2.23
BC Government	-0.03	-0.08	-0.08	4.28	5.63
BC Credit Bond	-0.04	0.89	0.89	7.01	6.42
BC High Yield Corporate Bond	0.32	3.88	3.88	14.31	9.12
BC Muni Bond	-0.33	0.51	0.51	1.63	4.14
BC TIPS	1.01	2.08	2.08	7.91	6.25
BofA ML Global Broad Market Ex USD	0.69	1.78	1.78	8.54	7.63
BofA ML Global Broad Market	0.42	1.19	1.19	7.05	6.93
BofA ML Emerging Market Credit	2.10	3.92	3.92	15.00	9.82
Alternative Investments					
HFRI Equity Hedge	0.31	1.92	1.92	11.89	4.44
HFRI Equity Market Neutral	0.73	2.07	2.07	7.05	2.87
NAREIT Equity REIT Index	-1.28	7.49	7.49	25.00	1.70
DJ-UBS US Commodity Index	2.06	4.45	4.45	28.49	2.57



There are exceptions of course, and oil rich Russia has benefited enormously from rising oil and wheat prices. Japan, not surprisingly, has suffered from both their longer term economic travails and the impact and repercussions of a massive earthquake.

Fixed income total returns appear to be cooling off now that the economy is gathering strength, demand for credit is starting to increase, inflationary pressures are surfacing and end of QE2 is in sight. The yield curve has steepened, reflecting a “normal” growth perspective. Bonds considered to be riskier continue to lead the way with high yield and emerging market debt up almost 4% for the quarter. On the other hand, concerns about Treasury yields caused the Barclay’s Government bond index to have a slight negative total return for the quarter. TIPS advanced on prospects of gathering inflationary pressures, and muni bonds finally may have turned the corner posting a positive total return.

Alternative investment classes like real estate continues on a tear, up another 7.5% this quarter, on the prospects that an improving economy and increased hiring will reduce vacant space and improve cash flows. Commodities on the other hand are reflecting both shortages, draughts, increased demand and speculation. Whatever the mix, commodities have been an important return component in portfolios in the last year.

The markets are reflecting improved investor sentiment and willingness to take risk. While it does not appear that the markets are either overvalued or undervalued en masse, careful research and security selection can almost always uncover fresh opportunities. While a market pullback may well be in order to digest some of the gains achieved since the middle of 2010, as long as earnings and the economic outlook continue to advance, the market will discount those increased earnings in higher prices.

What’s New @ CMC?

We moved to new expanded office space right after the first of the year; same address, same floor, bigger and nicer space...Thanks go Walzak Marketing and Communications (www.walzak.com) for helping us rebuild our public website and for helping us develop our new research portal for clients. We are receiving rave reviews on both...We published a juried article entitled, “When to Fire an Investment Manager” in the January-February issue of IMCA’s “Investments & Wealth Monitor” while also publishing monthly on Horsemouth.com...Dr. Chowdhury will be attending his first Federal Reserve Bank of Chicago’s Academic Advisory Council taking place May 4-6...Q1 CMC money manager visits: Putnam, Eagle Boston, Loomis Sayles, Wall Street Associates, Harris Associates, The London Company, InView Investment Management, Nuveen, Montag & Caldwell, Reinhart, Great Lakes, Munder, PIMCO, Thornburg, William Blair, RBC and Scout.