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THE CONROY REPORT

Quarterly Outlook
As of July 1, 2009

Economic Forecast

The U.S. economic situation looks bleak for the foreseeable future. A looming depression coupled with job losses and eroding confidence in the U.S. Dollar do not bode well. Low interest rates and a drop in consumer prices give the economy a little breathing room. However, we continue to recommend that investors play it safe with their investments.

For the past two quarters, the U.S. economy shrank by about 6% on an annualized basis. The annualized change in the U.S. economy was -5.7% in the fourth quarter of 2008 and the trend continued with a -6.3% contraction in the first quarter of 2009. This is a dramatic aberration in comparison to the usual 3% rate of yearly growth. The sources of the contraction have been exports, equipment and software, private inventory investment, nonresidential structures, and residential fixed investment. Government spending helped offset the contraction somewhat, but we are concerned about how the influx of money into the economy will affect inflation.

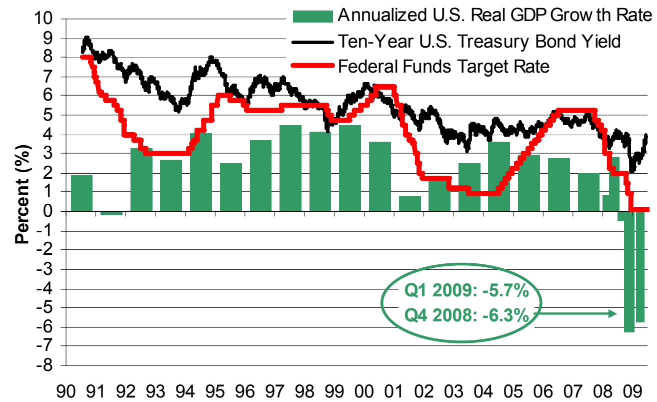
Unemployment rates have risen sharply and reached 8.1% in the first quarter of 2009. While the economy has been shrinking, the unemployment rate has been rising. Looking at Chart 2, which graphs the U.S. employment rate relative to economic growth, we can see that the divergence in these two measures has never been wider than during the period shown.

The strength of the U.S. Dollar (USD) relative to other foreign currencies is weakening. If this continues, exports will suffer further. The USD has been the currency of choice for the world economy, but signs of this are changing as companies are choosing to do business in other currencies without exchanging them to the USD. The Federal Reserve has a Fed Funds target rate near zero, which signals its intent to make money less expensive to obtain. The U.S. Government is also spending large sums of money in the private and public sector to prop up the economy.

On the bright side, current low interest rates may help the economy recover, given the low base cost of borrowing, but the Federal Reserve cannot really move its Fed Funds target rate any lower – it is just above 0% currently. Consumer prices have also gone down recently, moving in concert with the economic contraction of the past two quarters. This is helpful as it gives some breathing room for prices to increase if the economy begins to grow again.

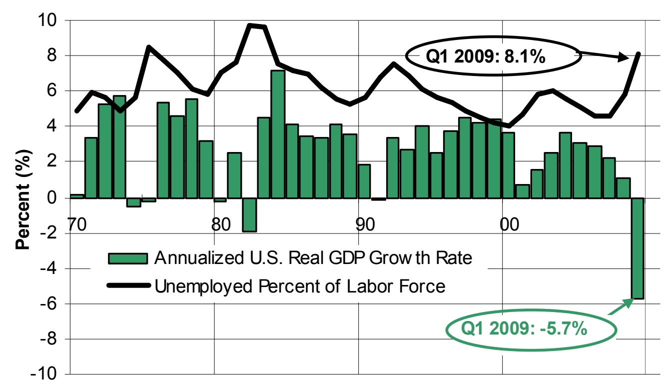
We continue to prefer cash and other money market instruments. Interest rates are back on the rise and we believe they will continue to rise along with inflation, government spending and regulatory stimulus. When rates rise, better investment returns will be found in short term securities, so this is where we advocate investors to stay. Recommended securities include Treasury bills and notes up to two years in maturity, bank certificates of deposits, money market instruments and, if nothing else, cash in the bank. We do note, however, that higher rates signal greater confidence in the future prospects of the U.S. economy and stock markets have done better recently. However, we advise our clients to keep things in perspective. The small gains recently are dwarfed by the precipitous fall in value on an actual dollar basis. Suppose a stock price at $100 per share dropped by 50%, as many did in the last year or more, the price would be $50 per share. Even if stock price recovered by 50%, the new price would be $75 per share, considerably less than the original price.

Chart 1. The U.S. Economy Has Contracted Sharply in the Past Two Quarters and Interest Rates Remain Low



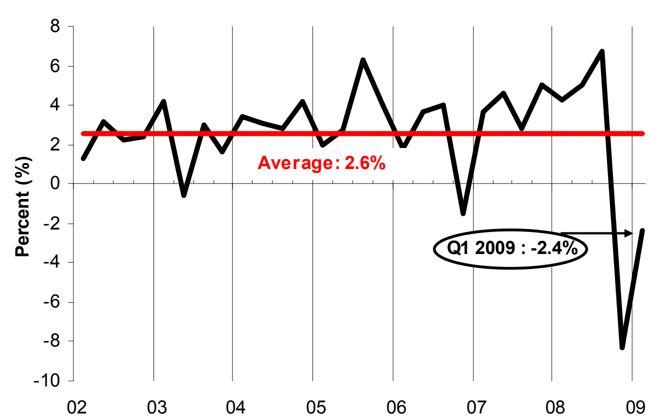
Sources: Federal Reserve, U.S. Department of Commerce Bureau of Economic Analysis, Yahoo! Finance.

Chart 2. Unemployment Rate is Rising as Growth Slows



Sources: U.S. Department of Commerce Bureau of Economic Analysis, U.S. Department of Labor, Bureau of Labor and Statistics. Seasonal unemployment rate.

Chart 3. Prices Dropped Recently After Two Years of Above Trend Growth



Sources: U.S. Department of Commerce Bureau of Economic Analysis. Data series shows seasonally-adjusted quarterly changes in the Consumer Price Index on an annualized basis.

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