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Weekly Market Wrap February 1, 2010

Review - Week Ending 01/29/2010

Stocks fell again last week, with foreign stocks leading the decline on concerns of monetary tightening beginning in emerging markets. Despite generally strong corporate earnings reports, the month of January kicked off 2010 with a 3.6% decline. The FOMC meeting last week offered no surprises, with the low interest rate monetary environment intact for now. This week brings more earnings reports.

Commentary/Highlights

- **Earnings Update:** About half of the S&P 500 companies have reported 4th quarter earnings, and so for they have more than doubled from the disastrous 4Q 2008, up overall 206%. Earnings have beaten all but the most optimistic expectations (reason for correction?) and are up 15% overall ex-Financials, and show a revenue increase of 7% overall.
- **Economy Update:** The major economic news release last week was the 4Q preliminary Gross Domestic Product release, which came in at 5.7%, much better than expected. Behind the results were slowing inventory liquidations, increased business equipment and software spending of 13%, and healthy consumer spending of 2.0%. Government spending actually fell for the quarter, as did durable goods, and gave economists evidence that the economy can begin to grow without government support such as the cash for clunkers and housing tax credits.
- **Stimulus Exits:** The global recovery is part of the story for 2010, but so is the exit of all the government stimulus plans around the world. In fact, government policy mistakes are a major risk for the markets this year. The exit begins where the stimulus began, in China. Emerging markets have joined the selloff in response to China's lending curbs and raising of bank reserve requirements. India joined in raising bank reserve requirements last week, but kept interest rates on hold. Germany also ended its ban on short-selling of bank stocks, a sign that they believe their banking sector can begin to stand on its own.
- **Jobs, Jobs, Jobs:** The key indicator of the economy going forward remains jobs, and the Obama administration announced a \$100 billion jobs bill with the unveiling of its \$3.8 trillion budget. Focus of the jobs bill is tax cuts for small business, assistance for state and local governments, and support for community bank small business lending. Deficit reducing aspects include domestic spending freeze, taxes/fees on big banks, and expiration of tax cuts for incomes above \$250K. Morgan Stanley's Richard Berner expects the January jobs report to show the economy created 75K jobs, well above the flat growth consensus.
- **Banking Focus:** Former Fed Chair Paul Volcker testifies to Congress this week, and will detail plans to separate commercial banking activities from "financial market activities". Banking regulation was much discussed at the annual Davos Economic Forum in Switzerland last week, and Fannie Mae and Freddie Mac have an army of auditors forcing banks to repurchase mortgage loans with improper documentation. Bank of America has most at risk due to Countrywide Financial merger.
- **Fed Holds and Warns:** The FOMC meeting last week was followed with a release that low interest rates will remain in place for some time. However, Fed Vice Chairman Don Kohn later warned in a speech that bankers need to prepare for interest rates that move in "unexpected directions", citing large government debt and less demand for U.S. debt could move interest rates upward. The monetary policy vote had its first dissent since crisis- KC Fed President Hoenig is ready to exit the zero interest rate policy.

Index/Portfolio Returns	% Change Week	% Change QTD	% Change YTD
Barclays Aggregate Bond	+0.05%	+1.53%	+1.53%
Barclays High Yield	-0.29%	+1.27%	+1.27%
Dow Jones Industrial	-0.98%	-3.23%	-3.23%
S&P 500 Index	-1.60%	-3.56%	-3.56%
Russell 3000	-1.82%	-3.60%	-3.60%
MSCI EAFE Index	-3.51%	-4.41%	-4.41%
MSCI EAFE Small Cap	-2.58%	-0.98%	-0.98%
NASDAQ Composite	-2.63%	-5.37%	-5.37%
Russell 2000	-2.42%	-3.68%	-3.68%