



# RESEARCH REPORT

*February, 2010*

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**Market Overview & Strategy Comments:** *Macro & Micro Trends Paint Different Pictures.*

Since there are so many conflicting opinions on the economy and the potential recovery, we have separated the data into two groups: one group contains big picture or macro-economic trends, the other covers more specific micro-economic trends.

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<u>Key Statistics</u>	<u>Current</u>	<u>Change Since Previous Month</u>	<u>2010 Change</u>
Dow Jones Industrial Average *	10067.33	-3.5%	-3.5%
S&P 500 Index *	1073.87	-3.7%	-3.7%
S&P 500 Ave. P/E Ratio **	14.8x	-0.8x	-0.8x
NASDAQ *	2147.35	-5.4%	-5.4%
1 Year Treasury Bill Yield	0.30%	-17 bps	-17 bps
10 Year Treasury Bond Yield	3.63%	-22 bps	-22 bps
30 Year Treasury Bond Yield	4.51%	-12 bps	-12 bps
Municipal Notes - 1 Year Yield	0.60%	+15 bps	+15 bps
Municipal Bonds - 10 Year Yield	3.60%	+10 bps	+10 bps
Reuters/Jefferies CRB Futures	\$265.59	-6.3%	-6.3%
Gasoline NY RBOB (\$ per gal.)	\$1.90	-7.3%	-7.3%
Natural Gas (\$ per MMBtu)	\$5.13	-7.9%	-7.9%
Gold (\$ per troy oz.)	\$1083.00	-1.1%	-1.1%

\* price only \*\* based on 2010 earnings estimates.

The Reuters/Jefferies CRB Futures Price Index is an arithmetic average of commodity futures prices with monthly rebalancing.

Gasoline NY RBOB price excludes local, state and federal taxes (the "wholesale price").

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# RESEARCH REPORT

## **Market Overview & Strategy Comments:** *Macro & Micro Trends Paint Different Pictures.*

These are not the simplest of times for an investor, forecaster or analyst. All of us are being buffeted by often contradicting streams of information coming from the domestic economy and abroad. On one hand, there remain many questions about the financial health of our banking system; yet, on the other hand, many banks are reporting billions in profits! Unemployment is stuck at 10%, yet we also see signs of a budding housing recovery. Corporate profits are soaring but consumer spending is mixed and capacity utilization is weak. The “cash crunch” that not that long ago threatened to bring down our economy has now been replaced by a surplus as companies and money funds are overflowing with excess cash, all earning next to nothing.

From our perspective, the best way to understand what is going on is to separate the data we are seeing into two groups: one group contains big picture or macro-economic trends, the other covers more specific micro-economic trends. Once we separate the data like this, we can see in the U.S. as well as in many other parts of world, the macro-economic trends are still mixed at best -- unemployment is high, debt levels are worrisome and business spending remains cautious. At the same time, however, micro trends are improving -- profits are on the mend as major cost cutting has offset sales declines, reduced investment has freed up cash and bailouts have helped the banks. *Here is a quick region-by-region summary:*

### United States

#### ***Macro – Mixed at best***

Inflation	Still low, but rising debt levels are cause for future concern.
GDP Growth	A strong end to 2009, but the outlook for 2010 is cautious. Trade is much improved due to the weak dollar. Politics is also having an impact as health-care, energy and financial reform are bandied about, creating some uncertainty.
Unemployment	Bad and not improving. This hurts the consumer outlook.
Fiscal Position	Weak and getting worse. A budget freeze being discussed.

#### ***Micro – Looks good***

Corporations	Profit growth strong, aided by cost cutting and emerging market demand. Cash reserves growing by hundreds of billions of dollars, leading to acquisitions, dividend hikes and share repurchases. All positive for investors.
Financial Market Health	Great recovery after 2008; leading banks on stable ground. Trillions in cash on the sidelines, valuations are reasonable.



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## Europe/Japan

***Macro – No better than the U.S. -- if anything, perhaps worse!***

Inflation	Still low.
GDP Growth	Barely positive. Problems in Greece are plaguing the Euro region. Strong currencies are hurting exports, the opposite of the U.S.
Unemployment	In many countries it's higher than ours with less flexible labor markets.
Fiscal Position	Better than ours but still troublesome.

***Micro – As in the U.S., micro trends look better.***

Corporations	Cost cutting, cyclical rebounds are leading to solid results. Japan starting to look overseas more for growth, a welcome change.
Financial Market Health	Banking system healthier due to bailouts. Like ours, much improved.

## Emerging Economies

***Macro – Most economies are rebounding quickly to pre-crash growth rates.***

Inflation	Inflation picking up, a potential headwind.
GDP Growth	Strong, especially relative to developed economies. Still dependent upon favorable commodity prices and exports.
Unemployment	Below that of developed nations, supporting consumer spending.
Fiscal Position	In most cases strong and getting stronger.

***Micro – The problems of 2008 already seem like a distant memory.***

Corporations	Managing growth is the main issue for many companies. Corporate governance, however, isn't yet up to U.S. standards. Secular prospects still higher than the rest of the world. Competition is heating up and credit issues continue, but generally profit growth is robust.
Financial Market Health	Most have made up ground lost in 2008 as ample reserves and strong currencies helped them weather the storm. Valuations are higher than ours in many cases but reflect higher growth rates.

As you can see, the micro trends in most of the world look pretty good. It's the macro trends that are creating headwinds and concern among investors in every region except the developing nations. This dichotomy leads us to believe, as we outlined last month, that while a cautious economic outlook is in order, the financial markets may still have a good year. In fact, markets often do well during modest growth periods as the slack in the economy fosters low inflation and avoids the bottlenecks which can hurt profits. *In summary, we continue to believe that low inflation and low interest rates, strong profit growth and significant cash on the sidelines create a favorable backdrop for the markets despite the macro-economic headwinds in place here and in Europe and Japan.*

## CORE HOLDINGS LIST FOR 2009

Source: FactSet, First Call, Value Line, Bloomberg & CAM Estimates.

February 1, 2010	<u>Company Name</u>	<u>Ticker</u>	<u>Recent</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>Est EPS</u>	<u>P/E to</u>	<u>Market</u>	<u>ROE</u>	<u>Div</u>
	<b>Standard &amp; Poors 500</b>		<u>Close</u>	<u>EPS</u>	<u>EPS</u>	<u>P/E</u>	<u>P/E</u>	<u>Growth</u>	<u>Growth</u>	<u>Cap(\$mm)</u>		<u>Yield</u>
		SPX	1,073.87	\$72.49	\$86.23	14.8x	12.5x	8%	1.6x	9,561,491	13%	2.0%
<b>Financials:</b>	Berkshire Hathaway Cl "B"	BRK/B	76.43	\$3.67	\$3.51	20.8x	21.8x	5%	4.4x	56,818	4%	0.0%
	MasterCard	MA	249.90	\$13.61	\$16.44	18.4x	15.2x	18%	0.9x	27,433	10%	0.2%
<b>Consumer Staples:</b>	Avon Products	AVP	30.14	\$2.09	\$2.41	14.4x	12.5x	9%	1.4x	12,871	126%	2.8%
	Coca Cola	KO	54.25	\$3.40	\$3.73	15.9x	14.6x	7%	2.0x	125,707	28%	3.0%
	Colgate Palmolive	CL	80.03	\$4.84	\$5.35	16.5x	15.0x	10%	1.5x	39,790	91%	2.2%
	Diageo Plc ADR	DEO	67.19	\$4.93	\$5.40	13.6x	12.5x	8%	1.6x	42,058	48%	3.4%
	Fomento Economico Mexico	FMX	42.16	\$2.61	\$3.26	16.2x	12.9x	22%	0.6x	9,112	8%	0.9%
	H.J. Heinz	HNZ	43.63	\$2.98	\$3.23	14.6x	13.5x	10%	1.4x	13,772	59%	3.9%
	Walgreen Co.	WAG	36.05	\$2.46	\$2.86	14.6x	12.6x	14%	0.9x	35,516	15%	1.5%
<b>Health Care:</b>	Becton Dickinson	BDX	75.37	\$5.31	\$5.78	14.2x	13.0x	11%	1.1x	17,857	24%	2.0%
	Johnson & Johnson	JNJ	62.86	\$4.92	\$5.36	12.8x	11.7x	7%	1.7x	173,437	30%	3.1%
	Novartis AG	NVS	53.53	\$4.63	\$5.00	11.6x	10.7x	4%	2.6x	141,192	16%	2.7%
<b>Consumer Discretionary:</b>	Staples, Inc	SPLS	23.46	\$1.36	\$1.62	17.2x	14.5x	14%	1.0x	16,983	14%	1.4%
	Target Corp.	TGT	51.27	\$3.58	\$4.24	14.3x	12.1x	13%	0.9x	38,571	15%	1.3%
	Toyota Motor Co. ADR	TM	77.00	\$2.84	\$5.54	27.1x	13.9x	35%	0.4x	132,748	NMF	1.4%
<b>Technology:</b>	Cisco Systems	CSCO	22.47	\$1.53	\$1.72	14.7x	13.1x	12%	1.1x	129,261	17%	0.0%
	EMC Corp.	EMC	16.67	\$1.14	\$1.31	14.6x	12.8x	14%	0.9x	34,004	8%	0.0%
	Fiserv, Inc.	FISV	45.04	\$4.03	\$4.48	11.2x	10.1x	12%	0.8x	6,932	14%	0.0%
	Google	GOOG	529.94	\$27.30	\$31.57	19.4x	16.8x	22%	0.8x	128,776	20%	0.0%
	International Business Machines	IBM	122.39	\$11.08	\$12.09	11.0x	10.1x	10%	1.0x	160,772	74%	1.8%
	Qualcomm	QCOM	39.19	\$2.27	\$2.55	17.3x	15.4x	18%	0.9x	65,863	8%	1.7%
<b>Industrials:</b>	3M Co.	MMM	80.49	\$5.05	\$5.68	16.0x	14.2x	11%	1.3x	57,196	27%	2.5%
	ABB Ltd. ADR	ABB	18.03	\$1.06	\$1.26	17.0x	14.3x	4%	3.6x	41,888	28%	0.0%
	Danaher Corp.	DHR	71.35	\$4.02	\$4.58	17.7x	15.6x	12%	1.3x	23,027	11%	0.2%
	United Technologies	UTX	67.48	\$4.64	\$5.30	14.5x	12.7x	11%	1.1x	63,265	21%	2.3%
<b>Energy:</b>	Apache Corp.	APA	98.77	\$10.01	\$12.31	9.9x	8.0x	11%	0.8x	33,204	4%	0.6%
	Petroleo Brasileiro S.A. ADR	PBRA	36.08	\$3.87	\$4.26	9.3x	8.5x	12%	0.7x	66,761	30%	1.0%
	Sasol LTD ADR	SSL	36.60	\$3.84	\$4.86	9.5x	7.5x	5%	1.5x	23,367	17%	3.0%
	Schlumberger, Ltd.	SLB	63.46	\$2.90	\$3.86	21.9x	16.4x	8%	2.1x	76,200	17%	1.3%
<b>Telecom Services:</b>	America Movil ADR	AMX	43.65	\$3.88	\$4.39	11.3x	9.9x	13%	0.8x	43,896	40%	1.0%
	China Mobile Hong Kong	CHL	46.95	\$4.21	\$4.34	11.1x	10.8x	13%	0.8x	188,373	28%	3.4%
<b>Exchange Traded Funds:</b>	iShares MSCI EAFE Index	EFA	52.48	-	-	-	-	-	-	33,314	-	2.7%
	iShares MSCI Emerging Mkts	EEM	38.28	-	-	-	-	-	-	35,882	-	0.1%

0% weighting in utilities, transportation and materials.

The above is a list of common stocks currently held in clients' portfolios. Not all stocks are held in all portfolios for various reasons. Upon request we will furnish a list of all equity recommendations made within the past twelve months. This list includes the name of the security, date and nature of the recommendation, price at which the recommendation was acted upon, and the current market price of the security. It should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities in this list.

Please contact Mickey Herst for a copy of the list.

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