Investment Policy Committee Notes

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Commonwealth Bank & Trust Company

Economic and Stock/Fixed Income Market Outlooks

Economic Outlook

Recent Reports

- February Personal Income (0.0%) was unchanged but positive revisions. Personal Spending (0.3%) increased as expected.
- March Conference Board Consumer Confidence (52.5) increased more than expected.
- March ADP "Private" Employment Change (-23K) unexpectedly remained negative. However, the decline was the smallest in two years.

Upcoming Reports

- (4/01) March ISM Manufacturing Survey (57.0 vs. 56.5).
- (4/02) March Change in Nonfarm Payrolls (184K vs. -36K) & Unemployment Rate (9.7% vs. 9.7%).

Longer-Term Outlook

- We are also continuously evaluating how our base-case scenario of slow economic recovery accompanied by private-sector (primarily household) deleveraging is unfolding. It is generally progressing in line with our expectations though we are mindful of the fact that government policy actions (or inactions) can significantly alter the future course.
- Another question we are grappling with is how long can the government take on more debt to stimulate the economy through fiscal stimuli? To get a better handle on this issue, we are trying to quantitatively look at a range of budget outcomes. Ultimately, there has to be a point when the debt math will not make sense, meaning there will be a limit to how much fiscal stimulus can be given to the economy.

Market Outlook

Equity Outlook

- Most of the valuation measures that we look at suggest that growth stocks are undervalued relative to value stocks. However, we do not believe there is enough of a valuation disparity at this point to overweight growth substantially. Also, classification can be debatable.
- Most valuation measures suggest that small caps remain expensive relative to large caps. Given the magnitude of small-caps' outperformance over the past decade, this is not too surprising. We continue to believe that for the time being, large-caps are likely to do better than small-caps over our five-year tactical time horizon as this valuation relationship returns to more normal levels.
- Since May 2009, when we initiated a tactical position, emerging-markets equities have run up significantly. They no longer look cheap in absolute terms, and are not as attractive relative to U.S. and developed international equities.

Fixed Income Outlook

- Within our valuation framework, the fixed income appears to be in a modestly overvalued range. But there remain differences between sectors. The 10-year Treasury's yield approaching 4% is still close to the bottom of its range over the last three decades and, with little room for interest rates to fall the upside in that sector appears limited. Also, investors have rediscovered their risk appetite so we will be watching spreads closely.
- Tax-free municipals sold off in late March as Treasury rates moved higher. In addition, negative news such as Barron's article on unfunded pension liabilities dampened fund flows dramatically.

S&P 500 GICS Sector Performance and Recommended Sector Weightings

	% Total Return					Forward Looking
S&P 500 Sector	MTD	YTD	2008	Forward P/E Ratio	Actual Sector % Weightings	CB&T Sector Emphasis
Consumer Discretionary	7.9	10.5	41.3	16.7	10.1	Marketweight
Consumer Staples	4.1	5.8	14.9	15.0	11.2	Marketweight
Energy	2.9	0.6	13.9	13.3	11.0	Overweight
Financials	8.9	11.2	17.2	17.1	16.5	Underweight
Health Care	2.6	3.4	19.7	12.3	12.1	Marketweight
Industrials	8.9	13.1	20.9	17.7	10.5	Marketweight
Information Technology	6.8	1.9	61.7	15.6	18.7	Overweight
Materials	7.8	2.9	48.6	17.4	3.5	Marketweight
Telecommunication	5.6	-4.3	8.9	14.7	2.8	Marketweight
Utilities	2.8	-3.5	11.9	12.2	3.5	Underweight
S&P Composite 1500	6.2	5.8	27.3	15.5		
S&P 500	6.0	5.4	26.5	15.1		
S&P MidCap 400	7.1	9.1	37.4	18.9		
S&P SmallCap 600	7.8	8.6	25.6	20.9		

Sector recommendations are market-cap weighted, influenced by economic, fundamental, and technical consideration.