

Economic and Stock/Fixed Income Market Outlooks

Economic Outlook

Recent Reports

- The cost of living in the U.S. dropped in May for a second month, signaling the world's largest economy is recovering without causing prices to flare. The 0.2 percent decline was the biggest since December 2008. Excluding food and fuel, the core rate increased 0.1 percent.
- Sales of previously owned homes unexpectedly fell in May, a sign demand was probably pulled into prior months before a June tax-credit deadline. Purchases of existing houses, which are tabulated when a contract closes, decreased 2.2 percent to a 5.66 million annual rate.
- Purchases of new homes fell in May to the lowest level on record after a tax credit expired showing the market remains dependent on government support. Sales collapsed an unprecedented 33 percent from April to an annual pace of 300,000.
- Fed officials retained a pledge to keep the rate at a record low for an "extended period" and noted "less supportive" financial conditions abroad.

Upcoming Reports

- (6/24) May Durable Goods Orders (-1.4% vs. 2.8%) & Durables ex-Transportation (1.0% vs. -1.1%).
- (6/28) May Personal Income (0.5% vs. 0.4%) & Personal Spending (0.2% vs. 0.0%).
- (6/30) June ADP "Private" Employment Change (55k vs. 55k).

Longer-Term Outlook

- While not in the double-dip recession camp just yet, we are concerned by recent weakness in the economic data. We knew much of the growth had been stimulus related and will be watching upcoming data closely. We still believe that GDP growth will be subdued for years to come ("New Normal") due to structural challenges and that being nimble within our asset classes will be a very important.
- One major challenge is our growing Federal Debt which will be the focus of our June commentary. The past two years have made the economic consequences of too much leverage painfully clear to individuals and businesses. Some of the same basic math applies to the governments such as we're seeing in Euro-zone. By themselves, high debt-to-income levels don't necessarily strain resources but problems arise quickly as interest rates rise. For now, the U.S. remains the global choice for investment quality and safety as well as the reserve currency.

Market Outlook

Equity Outlook

- 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.
- Technically speaking, we are watching the equity markets closely as a "Head and Shoulders" formation could result in a leg down.

Fixed Income Outlook

- For May, yields continued to fall in most fixed income categories. As risk appetites abated, yields did increase in credit markets particularly high yield. The 10-year Treasury which hit 4% in April ended the month at 3.29%. It hit 3.06% as an inter-day low on May 25th during the "flight to quality" rally on global debt concerns. For now, we continue to trade towards the low end of a 3.1% to 3.3% range.
- Tax-exempt bond prices were positive in May driven by limited supply but lagged Treasuries to some extent which is no surprise to us. As Kentucky has passed their biennial budget, the calendar is now reflecting additional (and welcome) supply. Munis corrected somewhat recently and valuations remain attractive particularly given the anticipated tax increases next year. The higher levels appear to be attracting bidders.

S&P 500 GICS Sector Performance and Recommended Sector Weightings

S&P 500 Sector	% Total Return			Forward P/E Ratio	Actual Sector % Weightings	Forward Looking
	MTD	YTD	2008			CB&T Sector Emphasis
Consumer Discretionary	-2.4	6.4	41.3	14.9	10.3	Marketweight
Consumer Staples	1.1	0.7	14.9	14.1	11.3	Marketweight
Energy	1.2	-5.7	13.9	11.9	10.8	Overweight
Financials	-0.8	1.5	17.2	13.9	16.2	Underweight
Health Care	1.6	-5.8	19.7	11.2	11.8	Marketweight
Industrials	-0.9	5.6	20.9	15.4	10.4	Marketweight
Information Technology	1.2	-3.5	61.7	13.8	19.1	Overweight
Materials	-0.2	-6.6	48.6	14.7	3.5	Marketweight
Telecommunication	4.4	-4.1	8.9	14.4	3.0	Marketweight
Utilities	1.4	-5.2	11.9	11.8	3.6	Underweight
S&P Composite 1500	0.1	-0.5	27.3	13.9		
S&P 500	0.4	-1.1	26.5	13.4		
S&P MidCap 400	-1.5	4.0	37.4	17.2		
S&P SmallCap 600	-2.4	4.1	25.6	19.4		

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

The above information is provided by outside data vendors; CB&T cannot guarantee the accuracy of the data provided.

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