EARL M. FOSTER ASSOCIATES
INVESTMENT MANAGEMENT

MARKET UPDATE

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After a spectacular recovery from the March, 2009 lows, the Standard & Poor's Index exhibited little follow through so far this year. Instead, the Index reversed its early January advance and is now a little below year-end, 2009 levels. This "pause" is not surprising in light of the strength of last year's gain, which transitioned stocks from a state of extreme "under-valuation" a year ago to more "normal levels" currently.

In the near-term, the economic recovery will continue to be "bumpy" with strength in the industrial portion while the consumer and construction sectors should remain weak. In addition, the news from the financial sector is again focusing on prospective loan losses and the credit worthiness of sovereign debt in southern Europe. In essence, both the economic recovery and the financial markets remain fragile.

In the coming months, stocks will continue to be sensitive to the economic and financial news, and this could lead to further volatility. However, the general direction of stocks for the balance of the year should improve, supported by earnings growth projected in excess of 20% this year and 10% - 20% in 2011. Thus, our equity strategy remains unchanged from that stated in our recent ***Newsletter***. Our expected trading range for the Standard & Poor's Index of 1,039 – 1,336 for 2010 remains unchanged and stocks still offer a favorable return/risk profile. If those projections are realized, Standard & Poor's earnings will return to the record levels achieved in 2006/2007.

We continue to be cautious on fixed income investments. Many governments have undertaken excessive debt, including this country. Some sovereign debt could experience credit downgrades and rising borrowing costs, but defaults are quite unlikely. Instead, such countries are likely to service their debt by inflating their money supply and paying creditors with cheaper currency. This could put upward pressure on interest rates world-wide in years to come. Thus, an under-weight in this sector continues to be appropriate.