TALKING POINTS

A Recap of January 2007

The Economy

Fourth quarter's 3.5% GDP growth outpaced the 3.0% consensus estimate. The Fed maintained its 5.25% federal funds target rate at the January 31 FOMC meeting citing the following reasons: some tentative signs of stabilization in the housing market; inflation pressures seem likely to moderate; and the expectation of moderate growth over the coming quarters. The next meeting is scheduled for March 31. Foreign ownership of U.S. Treasuries has helped keep interest rates low in recent years despite rising budget and trade deficits, according to Federal Reserve Bank of New York President Timothy Geithner. International investors now own nearly half of the $4.3 trillion of marketable Treasuries outstanding, according to the U.S. Treasury. The yield on the 10-year T-Note has averaged 4.38% since the start of 2002, a period marked by growing budget and trade deficits. The yield averaged 5.48% the previous four years, a period in which the U.S. achieved budget surpluses. According to Brian Wesbury, chief economist at First Trust Advisors L.P., investors should not interpret today's inverted yield curve as a precursor to recession. There have been six recessions since 1961, and prior to each of them the yield curve inverted when the federal funds rate rose at least one full percentage point above nominal GDP growth, and 4.5 percentage points above the inflation rate. Nominal GDP growth has been 6.26% the past two years, a full percentage point above the current 5.25% federal funds rate. Meanwhile, the federal funds rate is just 3 percentage points above "core" inflation.

Consumer Confidence	**110.3** (Jan)	110.0 (Dec)	⇧
Crude Oil (Mo.-End)	**$58.14** (Jan)	$61.05 (Dec)	⇩
Industrial Production	**0.4%** (Dec)	-0.1% (Nov)	⇧
ISM Manufacturing	**49.3** (Jan)	51.4 (Dec)	⇩
ISM Non-Manufacturing	**59.0** (Jan)	56.7 (Dec)	⇧

The Stock Market

The three major indices were all up in January with the DJIA, S&P 500 and Nasdaq Composite returning +1.4%, +1.5% and +2.0%, respectively. Small-cap stocks, as measured by the Russell 2000 Index, gained 1.7%. Some of the top performing S&P 500 industry groups in January were as follows: Tires & Rubber (+17.6%); Steel (+16.0%); Office REITs (+14.2%); Construction Materials (+13.3%); Retail REITs (12.1%); Health Care Distributors (+11.1%); Homefurnishing Retail (+10.7%); and IT Consulting (+10.4%). The top performing S&P sector was Materials (+4.60%). In January, the dividend-payers (384) in the S&P 500 (equal weight) posted a total return of 2.41%, vs. 1.96% for the non-payers (116), according to Standard & Poor's. For the 12-month period ended January 2007, payers gained 15.85%, vs. 7.78% for the non-payers. The number of dividend increases (S&P 500) in January totaled 28, well below the 40 registered over the same period in 2006, and also below the 32 increases registered in 2004. The dividend yield on the S&P 500 was 1.81% at the end of January. Since 1950, the S&P 500 Index has posted an average gain of 1.4% in January, according to the Stock Trader's Almanac. Thanks to a strong finish, the S&P 500 just posted a 1.51% total return in January 2007. Since 1926, the S&P 500 has finished the year in positive territory 80% of the time when the index is up in January. The average total return posted over the last 11 months of those years was 16.7%, according to Bank of America Securities. The index has finished higher 57% of the time when the return has been negative. The average total return posted over the last 11 months of those years was 6.9%. The VIX, an index that measures S&P 500 volatility, hit its all-time low with a reading of 9.89 on January 24, 2007, according to Bloomberg.

U.S. Dollar (U.S. Trade- Weighted Basket)	**+1.2%** (Jan) +1.5% (Dec) $ was down 5.25% in '06	⇧
AAII Sentiment Index	**39.5% Bullish** (1/31) 46.0% Bullish (12/31)	⇩
Short Interest (NYSE)	Jan: **9.68B** (+0.3%) Dec: 9.65B (+0.1%)	⇧
Margin Debt (NYSE)	Dec: **$275.4B** (+1.8%) Nov: $270.5B (+10.8%) *$278.5B in March 2000*	⇧

The Bond Market

The yield on the 10-Yr. T-Note rose 11 basis points in January closing at 4.81% – 29 basis points higher than on January 31, 2006. The returns on seven Lehman Bros. benchmark indices were as follows (January & **12-mo.**): ***U.S. Treasury: Intermediate*** (0.00% & **3.62%**); ***GNMA*** (30-yr.) (0.01% & **4.28%**); ***Municipal Bond (22+)*** (-0.28% & **6.35%**); ***U.S. Aggregate*** (-0.04% & **4.28%**); ***U.S. Corporate High Yield*** (1.12% & **11.32%**); ***Global Aggregate*** (-0.98% & **4.28%**); and ***Emerging Markets*** (-0.57% & **8.76%**). The U.S. speculative-grade default rate fluctuated between 1.6% and 1.9% in 2006, down from 2.2% at the close of 2005, according to Moody's. Since 1980, the default rate has averaged 5% per year and ranged from a low of 0.4% to a high of 12.7%. The global speculative-grade default rate fell from 1.9% in December 2005 to 1.7% in December 2006, its lowest year-end level since 1996. The default rate on senior loans hit an all-time low of 0.79% in December, according to Standard & Poor's LCD. The prior record low was 0.92%. It was set in May 2004. In our opinion, GDP growth of 3.5% in Q4 suggests the Fed is not likely to cut rates in the first half of 2007.

Key Rates as of January 31st

Fed Funds	5.25%
2-Yr. T-Note	4.92%
10-Yr. T-Note	4.81%
30-Yr. Mortgage	6.34%
Bond Buyer 40	4.64%

Key Yield Spread

The spread between the Merrill Lynch High Yield Master II Index and the 10-Yr. T-Note was 307 basis points on Jan. 31. The yield on the index was 7.88%. The spread was 366 basis points on Jan. 31, 2006, when the yield was 8.18%.

2006 Debt Issuance
(Source: Thomson Financial)

Debt Category	$ Amount	% change over '05
Corporate	$1.41 Trillion	+17.2%
Convertible	$8.4 Billion	+33.0%
Asset-Backed	$1.68 Trillion	-7.2%
Municipal	$381.5 Billion	-6.1%

The Investment Climate

Net cash inflows to equity funds totaled $10.7 billion in December, down from $10.8 billion in November, according to the Investment Company Institute. Bond funds reported inflows totaling $8.8 billion, up from $6.9 billion in November. Money funds reported inflows totaling $41.5 billion, down from 54.8 billion in November. In 2006, net cash inflows to equity funds totaled $157.9 billion, vs. $60.8 billion for bond funds – a ratio of 2.6 to 1.