

Questions investors are asking about the economy and markets

2009 Midyear Outlook

Contents

The Economy

Economic recovery 2

Dollar weakness 3

Inflation 4

Equity Markets

Market bottom 5

Outlook 7

Opportunities 8

Fixed-Income Markets

Outlook 11

Municipal credit risk 13

Bond insurance 15

Sector weightings 16

International Markets 17

Stocks or bonds? 18

Asset Allocation Models 19

For important disclosures and analyst certifications, please see the last page of this report.

Executive summary

- ▶ In our view, the economy will begin a modest recovery by the end of 2009.
- ▶ Due to high unemployment and tight credit, we expect U.S. inflation to remain low during the next year or two and the value of the dollar to weaken modestly against other major currencies.
- ▶ We believe the bottom in the equity market was realized in March 2009.
- ▶ The dramatic gains since the March lows have left the market susceptible to a near-term correction. Hence, we are cautious in the short term, but looking to increase equity exposure on a pullback.
- ▶ We continue to favor cyclical sectors such as industrials and consumer discretionary and look to add to our small- and mid-capitalization equity exposure.
- ▶ In fixed-income markets, we recommend focusing on senior debt of highly rated companies and high quality, essential-purpose municipal issuers.
- ▶ We continue to see opportunities in international markets, particularly emerging markets.
- ▶ From an asset allocation perspective, we would suggest that investors with intermediate- and longer-term time horizons lean into equities and away from fixed-income securities.

Forecasts and targets

	2009	2010
S&P 500	1015	1135 to 1155 range
S&P 500 Earnings-Per-Share Estimate (EPS)	\$58	\$73
Real Gross Domestic Product (GDP)*	-2.7	2.10
10-Year U.S. Treasury	3.75%	4% to 4.50% range

*As of June 10, 2009. Compound annual growth rate quarter-over-quarter.

Past performance is not an indication of future results. An index is not managed and is unavailable for direct investment. There can be no assurance that any of the target objectives will be met.

Please see pages 21 through 24 for important definitions and disclosures.

Q. Is the recession likely to end soon, and what type of recovery are we likely to see?

Recent economic data show that the economy is no longer in a free fall as it was during the financial crisis late last year and early this year. The recession appears to be waning as evidenced by several parts of the economy showing signs of stabilization. Home sales have fluctuated in a narrow range at a low level for several months, as have durable goods orders. Monthly job losses also appear to have diminished and consumer sentiment has increased. If the economy stays on the current track, an economic recovery should begin late this year.

A. *At this point the most likely scenario, in our opinion, is for a modest recovery, given the lingering problems in the financial sector.*

The big question on many investors' minds is what type of recovery is likely to unfold. History suggests that deep and broad recessions like the current one are often followed by a strong recovery. However, at this point, the consensus estimate of economists and statements from policymakers indicate that the recovery is more likely to be slow and modest. Differing arguments support each view.

Arguments for a robust recovery

- The Federal Reserve and the federal government are following the most aggressive stimulus policies since World War II.
- Global interest rates have been reduced along with U.S. interest rates. This broad monetary stimulus could support a healthy recovery.
- Housing affordability is near a record-high level looking back as far as 1971. Low home prices, low mortgage interest rates and a first-time tax credit could boost home sales during the next 18 months.
- Companies are getting access to credit once again and may not need to cut spending and jobs as much as they did during the worst of the credit crunch, when businesses cut costs wherever they could.
- Inventories are lean because companies have cut production well below the rate of sales. If production merely returns to the level of sales, the economy will probably look a good deal stronger.

Arguments for a modest recovery:

- The housing market is still facing increasing foreclosures and declining home prices. A quick rebound in home sales is unlikely because of rising unemployment.
- Weak commercial real estate will probably depress rents and property prices, creating additional loan problems for the financial sector.
- Consumers have very little purchasing power after big losses in wealth from falling home prices and weak financial markets. Therefore, consumer spending is likely to be restrained during the recovery.
- Unemployment is high and likely to go higher, forcing many families to limit spending.

At this point the most likely scenario, in our opinion, is for a modest recovery, given the lingering problems in the financial sector. The biggest downside risk to a potential economic recovery at this time would be an unexpected event, like a military confrontation with extremists in Pakistan or North Korea, or a severe swine flu pandemic.

Q. Is the dollar overvalued and vulnerable to a dramatic decline, or is it fairly valued with modest downside risk?

During the past few years the dollar has weakened when the U.S. economy expanded and strengthened when the U.S. economy contracted. This is because the value of the dollar compared to other major currencies tends to reflect the rate of inflation in the United States. If inflation is going up in the United States, traders want more dollars in exchange for other currencies in order to compensate for the inflation. For example, if U.S. inflation is 10%, the dollar could theoretically decline 10% (all other things held constant) in order to offset the lost purchasing power of 10% inflation. Of course, all other things are not constant. There are frequently other issues affecting the dollar besides inflation and economic growth. According to our work, when including all these other factors, the dollar has tended to decline about 0.6% against the value of the euro for every 1% increase in U.S. prices.

Looking back, the dollar sometimes strengthened when events caused U.S. inflation to decline substantially either because of strong anti-inflation policies, economic weakness or an oversupply of commodities. However, over the long run the dollar tends to decline against other major currencies like the euro as prices rise in the United States.

The dollar is not currently overvalued. Our work suggests that the rally in the dollar late last year pushed the value of the greenback up from undervalued to fairly valued. However, the dollar is seldom stable even when it is fairly valued. That's because there are always many things that can influence sentiment toward the greenback, even if the underlying inflation environment does not change that much.

Many investors are currently worried that the dollar could drop sharply like it did during the 1970s. However, that was a high-inflation environment caused by many developments, especially going off the gold standard when the dollar was overvalued. After the United States went off the gold standard in 1971, the dollar dropped sharply just to get back to fair value. The drop in the dollar prompted OPEC (Organization of the Petroleum Exporting Countries) to cut production in 1973, boosting oil prices. This added even more inflationary problems to the mix. Finally, interest-rate ceilings thwarted the Fed's efforts to fight inflation.

If U.S. inflation remains low during the next year or two, as we expect because of high unemployment and tight credit, the value of the dollar is likely to weaken modestly against other major currencies.

A. *The dollar is not currently overvalued. If U.S. inflation remains low during the next year or two, as we expect because of high unemployment and tight credit, the value of the dollar is likely to weaken modestly against other major currencies.*

Q. Will the massive expansion of liquidity by the Federal Reserve and deficit spending by the federal government necessarily lead to rapid inflation?

Many investors are becoming increasingly worried about potential inflation. At the same time, the Federal Reserve is still worried about deflation. Concern about inflation is understandable at this point in the economic cycle. After all, an increase in inflation would erode the purchasing power of assets that have already declined in value because of the recession. However, inflation is seldom a problem when the economy is weak and unemployment is high like it is now. Instead, inflation is usually a problem when the economy is strong and the unemployment rate is relatively low. Unfortunately, it could be several years before the U.S. economy returns to those conditions. In the meantime, concerns about inflation can still move the markets. Therefore, it is important to understand both sides of the argument.

A. *We believe the arguments against a surge in inflation in the near term are more compelling than the arguments for high inflation.*

High inflation arguments

- Conventional wisdom says that inflation is caused by too much money chasing too few goods. Therefore, the Fed's massive injection of liquidity into the financial system could lead to substantial inflation down the road.
- The federal government's economic stimulus program is producing record-high federal budget deficits. This massive increase in spending is also potentially inflationary.
- Global demand, especially from China and other emerging Asian countries, may boost commodity prices, pushing inflation upward.
- If foreign investors lose confidence in U.S. policies, the dollar could drop, making imports cost more, and inflation could accelerate.

Low inflation arguments

- The increase in the money supply is not necessarily inflationary because it is being offset by a slowdown in the velocity of money. People are holding more money as an asset during these uncertain times. This reduces the rate at which money chases goods and services, limiting inflation risk.
- History shows that inflation is influenced more by credit growth than money supply growth, and credit is still tight despite the increase in the money supply. Low credit growth restrains spending and potential inflation. If people and businesses can't borrow (or don't want to borrow as much as they used to), then spending would be limited and the risk of inflation would be less.
- The high unemployment rate means that there is no shortage of labor, and wage inflation will probably remain low. Similarly, with so much excess capacity around the world, demand could increase without creating any shortages. When there is excess capacity, money is not chasing too few goods.
- The dollar is not overvalued. Consequently, a substantial drop in the value of the greenback, causing a jump in import prices, is unlikely.

We believe the arguments against a surge in inflation in the near term are more compelling than the arguments for high inflation. Nevertheless, it is important to remember that increased inflation concerns are often common at this point in the economic cycle for two reasons. First, the surge in commodity prices before the recession is fresh on investors' minds. Second, this is the point in the economic cycle when the Fed usually pumps liquidity into the financial system, and the yield curve often increases because of heavy government borrowing and excess liquidity.

Q. From a technical perspective, has the stock market bottomed and is it too late to participate in the stock market's rebound?

We believe the bear-market bottom for stocks was reached at the March 9, 2009, closing lows. The Dow Jones Industrial Average (DJIA) had declined 54% from its October 9, 2007, peak – the second-largest decline since 1900, surpassed only by the 86% decline during the Great Depression. The S&P 500 declined 56% from the October peak. The prevailing fears for investors leading up to the March lows were that an economic depression was not out of the question, credit markets were frozen, many banks could potentially go out of business and others may be nationalized. Together with the housing market continuing to decline dramatically, investor pessimism reached a panic level, with many questioning whether they should even own stocks.

Many underlying technical indicators or measures of the internal health of the stock market reached extreme levels at the March lows:

- The New York Stock Exchange (NYSE) Composite Index cumulative advance/decline line fell to its lowest point since August 2004.
- The percentage of NYSE stocks trading above their 200-day moving average bottomed near 1%.
- The ratio of bears to bulls in the American Association of Individual Investors survey reached its highest ratio since October 1990.
- The percentage of money market mutual funds (individual plus institutional money market funds) as a percentage of the market capitalization of all NYSE and NASDAQ stocks reached 48%. This is compared to an average ratio near 18% during the prior 5 ½ years.

When these indicators reach these extreme levels, it usually indicates that the stock market is near major market bottoms.

Other measures of the internal condition of the market did not reach the same extremes in March 2009 as they did at the October and November 2008 stock-market lows. These are called “positive divergences,” which mean the selling pressure or investors’ bearish sentiment was not as intense in March as they were last October and November. Some of these indicators included:

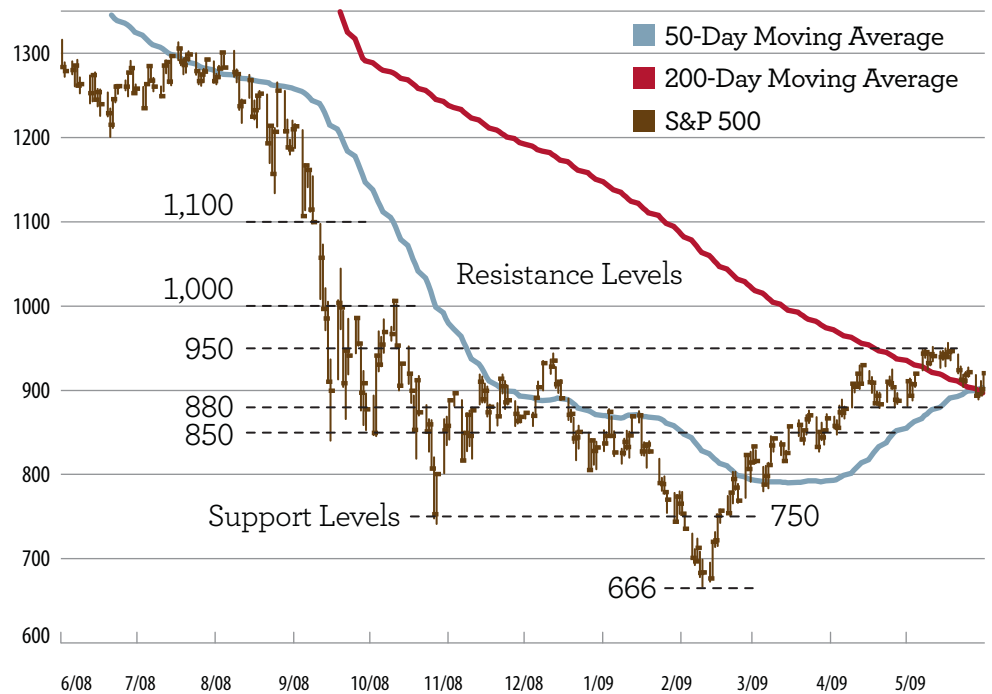
- The 10-day moving average of the Chicago Board Option Exchange (CBOE) put/call ratio is commonly perceived that the higher the ratio, the more bearish investors are about the market. This indicator reached an 11-year high last November and made a lower peak in March.
- The number of NYSE stocks reaching new 52-week lows reached 1,860 last October, 1,197 in November, and just 667 in March.
- In November 2008, the S&P 500’s 200-day moving average gap from the S&P 500 index level broadened to its widest level since 1980. The 200-day moving average fell to 60% of the index level last November, made a higher low in March, and then the index crossed back above its 200-day moving average in early June.
- The CBOE Volatility Index (VIX), which we consider an indicator of how much investors are willing to pay to help limit risk in their stock portfolio, rose to a multi-year high near 81 in November 2008. We saw this as a level of major panic and a sign that investors were giving up on stocks. In comparison, the VIX’s average value has been near 20 since it was created in 1990 and stands at 26 currently.

A. *We believe the bear-market bottom for stocks was reached at the March 9, 2009, closing lows. It is not too late for investors to buy stocks.*

In our opinion, these indicators show that panic had reached historical extremes consistent with major market bottoms. In addition, in recent months, stock market liquidations have reached high levels consistent with a market at the end of a decline. The DJIA has risen 34% from its March 9 low (6547) to the June 12 high (8799), the largest advance in the shortest period of time since 1938. There are still many challenges ahead for the economy, but we believe the worst has passed for the stock market.

That said, it is not too late for investors to buy stocks. However, the market appears extended on a short-term basis. Technical signals of the underlying short-term condition are showing overbought momentum indicators and signs of increased complacency (less fear) among investors. Investors are wondering if the stock market has gotten ahead of the outlook for the economy and the state of the financial system. The stock market is not a one-way street, and as always, there will be corrections; however, the dominant trend remains up (see the chart below for nearby support and resistance levels for the S&P 500).

S&P 500 Index (Priced from June 26, 2008 to June 25, 2009)



Sources: Remote Plus, Interactive Data Corp.

Past performance is not an indication of future results. An index is not managed and is unavailable for direct investment.

One never knows the difference between a bear-market rally and the start of a new bull market until long after the fact. However, we believe that this is a new bull market and this will become more evident as the U.S. and global economies continue to improve later this year and as the market begins to discount an earnings recovery. There remains ample cash on the sidelines to fuel the stock market – according to the Investment Company Institute (ici.org), there is \$3.67 trillion in all money market mutual funds as of June 17, 2009.

Despite this historic advance, the DJIA has only recovered to its January 2009 highs and the S&P 500 to its November 2008 highs, both still far below their all-time highs. Historically, the steeper the decline in the stock market, the larger the subsequent advance has been. As measured by the DJIA, there have been seven bear markets since 1900 that have declined 45% or more (for reference, the current bear has declined 54%). The average gain one year following the end of these bear markets was 57% on a closing basis for the DJIA.

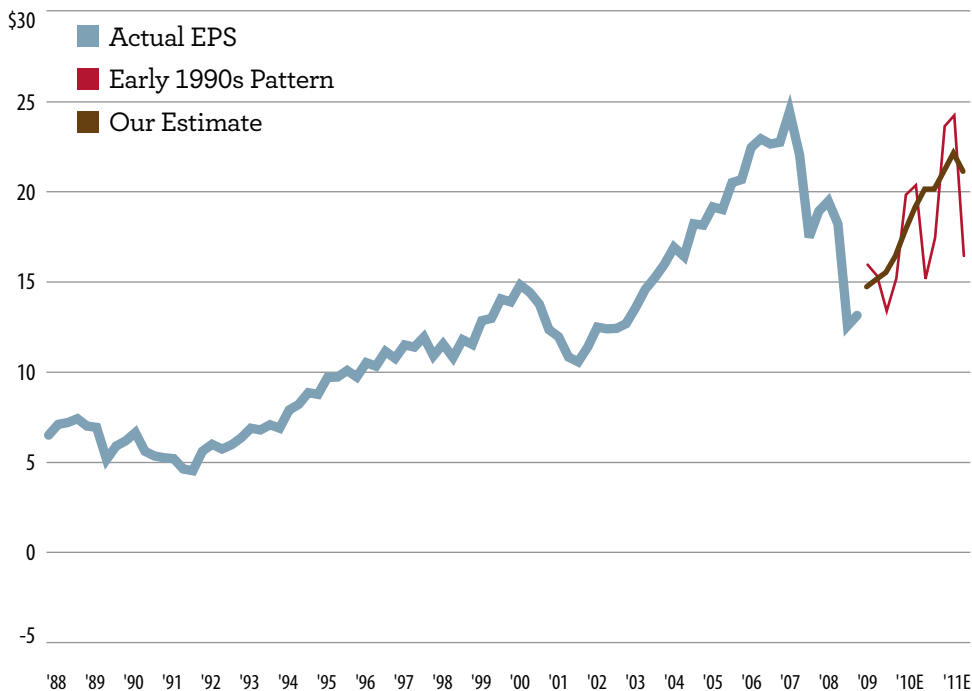
Q. From a fundamental perspective, what is our outlook for the equity market over the next 12 months?

Even after the recent stock market bounce, the S&P 500 is trading at levels similar to where it traded during the last quarter of 2008. We still believe, however, that the S&P 500 can reach our target of 1015 by the end of 2009. From a valuation perspective, the March 2009 low represented a price-earnings (P/E) multiple of only 11.5 times our 2009 EPS estimate of \$58 for the S&P 500 and 9.1 times our 2010 estimate of \$73. These represent a meaningful discount to the long-term average price-earnings multiple on the S&P 500 of 16.5 times.

In the chart below, we have charted the history of S&P 500 quarterly operating earnings back through 1988. To the right of the graph, we have plotted the pattern of recovery from the early 1990s recession as applied to the current cycle (in red). In brown, we have plotted our own expectations for a quarterly earnings recovery in the current cycle. Our projected operating earnings trajectory was created after studying, among

A. Based on what we feel is an appropriate 13.5 to 14 times P/E ratio and using our 2011 estimate of \$84, we believe the S&P 500 can reach the 1135-to-1175 range by late 2010.

S&P 500 Quarterly Operating Earnings



Sources: Baseline, Factset, Wells Fargo Advisors

Past performance is not an indication of future results. An index is not managed and is unavailable for direct investment.

other things, the steps of the last five recoveries. With this in mind, we are targeting 2011 (full year) operating earnings of \$84 for the S&P 500 (which represents a 15% increase over our 2010 estimate).

Our 2011 EPS number of \$84 is somewhat more conservative than the consensus. Our projection is based on what we believe will be a tighter regulatory environment, more conservative lending standards, a consumer economy that will continue to focus on deleveraging, and the possibility of higher tax levels given federal, state and municipal debt levels. Based on what we feel is an appropriate 13.5 to 14 times P/E ratio and using our 2011 estimate of \$84, we believe the S&P 500 can reach the 1135-to-1175 range by late 2010.

Q. Where are opportunities in the equity market?

In line with our belief that the most severe period of risk aversion is likely behind us, we believe investor interest in relatively more risky assets is likely to continue over the next several years, with intermittent periods of correction. (Risky assets would include high-yield bonds, small-cap stocks, and international securities, among others.) Since the March 2009 bottom, the momentum of the markets has shifted toward more cyclical sectors such as industrial, consumer discretionary, and even the late-cycle materials sectors, which have outperformed the S&P 500. In addition, the S&P financial sector has outperformed by roughly 60%. Historically, these cyclical performances are not out of line with what investors experience once markets begin to look toward recovery.

A. *We are currently overweight industrials and telecommunications services and underweight the health care, utilities and materials sectors. We believe small-cap stocks will likely outperform the S&P 500 during the first few years of the economic recovery.*

In the past, the earliest outperformers in a recovery tend to be the financial sector followed by the consumer discretionary and industrial sectors. The best outperformance for the more defensive sectors (i.e., health care, consumer staples and utilities) generally occurs late in a recovery continuing into a recession. Most frequently, the best outperformance phase for the energy and materials sectors tends to take place later in a recovery cycle as worldwide demand strengthens and as inventories tighten dramatically. The performance of the information technology and telecommunications sectors depends upon the specific economic cycle. However, we would expect cyclical sector outperformance to continue when those sectors begin to register positive year-over-year earnings comparisons. That said, we are currently overweight in industrials and telecommunications services.

The consumer staples, health care, and utilities sectors are underperforming the market as one might expect. Investors are beginning to anticipate an earnings recovery in the more cyclical sectors of the economy. We are currently recommending investors underweight the health care, utilities, and materials sectors. We believe the health care and utilities sectors will likely remain underweight through the middle of the economic recovery. Should the dollar weaken further and commodity inventories tighten up, we would expect to eventually upgrade the materials sector (which represents only 3% of the S&P Composite Index total market capitalization). The table on the following page summarizes our recommended sector weightings.

Recommended Sector Weightings vs. S&P 500 (updated June 29, 2009)

	S&P 500	Guidance	
Consumer Discretionary	8.9%	Evenweight	10%
Consumer Staples	12.0	Evenweight	12
Energy	12.5	Evenweight	15
Financials	13.6	Evenweight	12
Health Care	13.9	Underweight	10
Industrials	9.9	Overweight	15
Information Technology	18.4	Evenweight	17
Materials	3.3	Underweight	0
Telecom. Services	3.5	Overweight	7
Utilities	4.1	Underweight	2

Note: Weightings may not add to 100 due to rounding

Past performance is not an indication of future results. An index is not managed and is unavailable for direct investment. Investments that are concentrated in a specific sector or industry may be subject to a higher degree of market risk than investments that are more diversified.

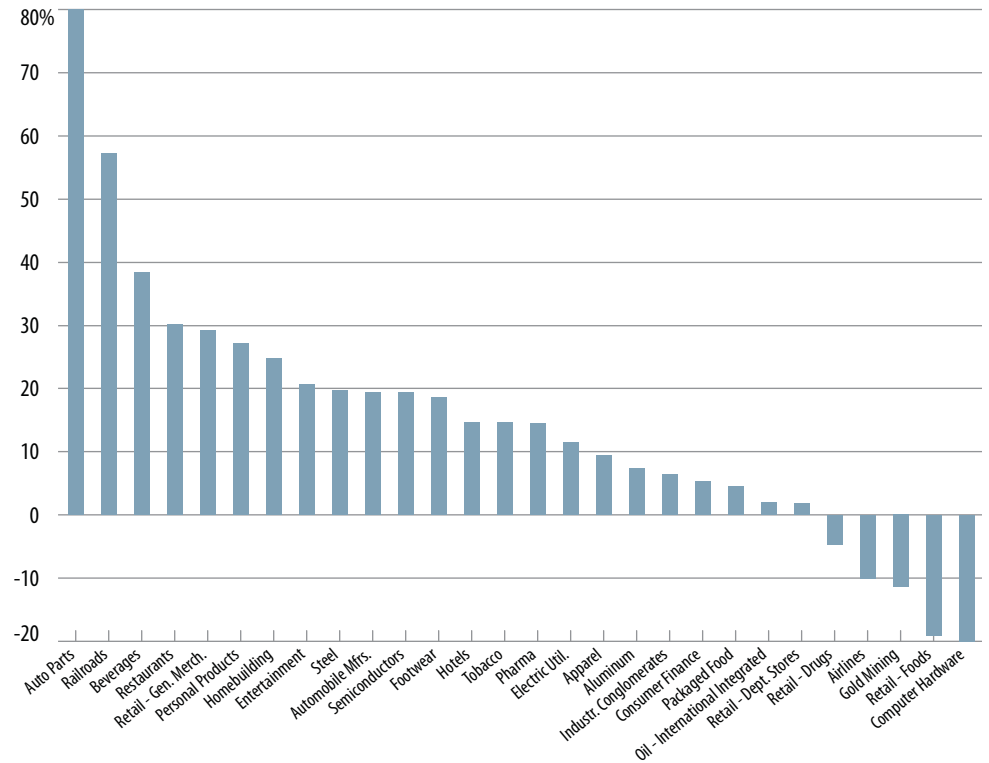
As far as more recent cycles are concerned, it makes sense to compare this cycle with the 1990s as opposed to the 2000s cycle. The 1990s cycle went through a period of 34 months of transition from extreme cyclical to extreme defensiveness. In the chart on the following page, we have graphed the actual performance of 28 major industry groups from March 1991 – the most defensive period during the 1990s recession – to May 1992.

If we take an average of the performances of the defensive and cyclical sectors (leaving financials out of the equation), the average performance of early- and mid-cycle cyclical groups was just under 18% during those 14 months. The average performance of defensive- and later-cycle cyclicals was only roughly 7%. It is not a surprise that the lower performance groups in this early recovery period included some of the following: aluminum, industrial conglomerates, packaged food, international integrated oil, pharmaceutical retailers, airlines, gold mining, food retailers, and computer hardware. These groups tend to perform best entering into and during a recession or much later in a recovery phase.

In terms of market capitalization, small-cap stocks tend to perform better in an economic recovery. This is due to the somewhat less defensive (more cyclical) and more domestic nature of the smaller-cap indexes, overall. When fear precedes recession, small-cap stocks tend to underperform as investors move toward larger, multinational companies with the strongest balance sheets and excess cash flows; the larger names tend to (on balance) have more diversified businesses by industry and geography.

While the current economic recovery is likely to offer less free-flowing credit (which could impact smaller companies' abilities to finance growth more than some of the larger companies), we believe that investors have been conscious of this factor. For these reasons, we believe small-cap stocks will likely outperform the S&P 500 during the first few years of the economic recovery (even if that outperformance is not as dramatic as we have seen during the last few economic recoveries). Thus far, the Russell 2000 Index has performed roughly in line with the S&P 500 over the last year. It has outperformed the S&P 500 by 9% since early March 2009.

Industry Group Performance During the 14-Month Period
After Peak Defensive Cycle (March 1991 to May 1992)



Sources: Baseline, Wells Fargo Advisors

Past performance is not an indication of future results. Investments that are concentrated in a specific sector or industry may be subject to a higher degree of market risk than investments that are more diversified.

Of course, the equity markets tend to not only have varying sector and market capitalization personalities during differing phases of economic cycles, but they also shift styles over the course of a cycle (growth versus value). Typically, in the early stages of an economic recovery, the hardest hit stocks have been the more cyclical stocks. These stocks tend to be the most widely held in “value” portfolios at this point in the economic cycle. As investors flee the more cyclical stocks — before and during economic declines — they move to more defensively positioned (and less cyclically driven) “growth” stocks.

Once investor confidence in the prospects for an economic recovery lifts, a portion of the capital “hiding” in “growth” issues tends to move back toward more beaten-down “value” stocks. For this reason, it is not unusual to find outperformance shift toward “value” -style portfolios and away from “growth” style portfolios. During the last year, the Russell 2000 (smaller-capitalization), the Russell 1000 (large capitalization), and the Russell 3000 (all capitalization) growth indexes have generally outperformed their value counterparts. Keep in mind that the prices of small company stocks are generally more volatile than large company stocks. They often involve higher risks because smaller companies may lack the management expertise, financial resources, product diversification and competitive strengths to endure adverse economic conditions.

Please see pages 21 through 24 for important definitions and disclosures.

Q. How should fixed-income investors be positioned over the next 12 months given our outlook for inflation and interest rates?

Over the balance of 2009 and into the first half of 2010, yields on short-term debt should be kept low by the Fed's promise to keep the federal funds target rate (the interest at which banks lend to other member banks) at or near 0% for an "extended period." It is our opinion that the Fed will leave rates unchanged through the end of 2009 and into 2010. In that environment investors will find little in the way of yield in short-maturity debt and cash holdings. However, in the longer term we are concerned about higher yields for longer-maturity debt. Some of that has already happened, but as the economy recovers and more government debt is issued, longer-maturity, benchmark government yields could face additional pressure. For the remainder of 2009, we look for the 10-year Treasury to trade around 3.75% and 4% to 4.50% in 2010. Longer term (beyond 2010), we look for bonds to trade in the 4.50% to 5.50% range based on the 10-year note. That would represent a slightly higher range than persisted through most of this decade, due primarily to concerns over the amount of debt that will be necessary to fund the current programs. The year 2010 will likely be, in our opinion, a transition year for the bond market, with benchmark Treasury yields migrating higher as the recovery gains traction.

Our inflation and growth outlook has implications for bondholders. Long U.S. Treasury bond yields have increased substantially this year. In our opinion, there are three primary reasons for the increase in 10- and 30-year Treasury yields. Two are more transient, while one is a longer-term concern. First is the removal of the fear/liquidity premium in Treasuries. Last fall, the 10-year note yield fell to record low levels as investors fled all asset classes on a wholesale basis and piled into the safety and liquidity of Treasuries. At that time, the credit crisis was in full bloom, investors worried about a long, protracted deflationary recession, and the banking system was under extreme pressure. At the same time the markets were deleveraging. We believe that period of maximum risk is now behind us, and investors are in the process of repricing and reassessing risk. As investors have sought higher returns, they have reversed the flow and are now moving out of Treasuries.

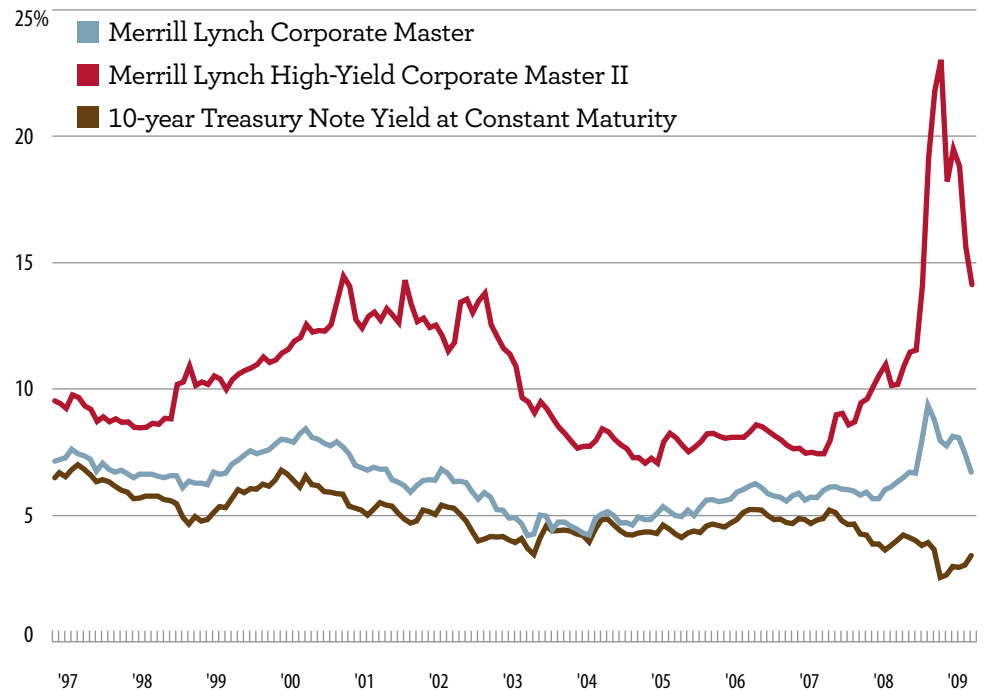
A second temporary concern, which is related to the first, is growing signs that the economy is stabilizing. This will lead to some concerns over increased inflation, which is a negative for bond investors. As stated above, in the short and intermediate term we are less concerned about inflation pressures and actually see a continued period of low or even negative Consumer Price Index (CPI) reports.

A longer term concern for us, and one of the reasons that bond yields rose so rapidly in May, is the gross amount of debt that will need to be sold on a continual basis and what price (in terms of higher yields) market participants will demand to buy and hold this debt. This is a particular concern with more than 50% of Treasuries held by foreign and international investors. No one knows how much debt is too much, but one way to think about the issue is in terms of the overall economy. Data from the Office of Management and Budget (OMB's predominant mission is to assist the President in overseeing the preparation of the federal budget) shows gross federal debt relative to the GDP, has been gradually increasing, and at the end of 2008 stood at 70.2%. OMB's projections show this ratio increasing to over 100% over the next decade, a level not seen since the end of World War II.

A. *We currently recommend overweight positions in investment-grade corporate and municipal bonds, and neutral positions in the agency, high-yield and emerging market sectors. We are underweight Treasuries and mortgage-backed securities (MBS) which are the sectors that most directly benefited from the flight to quality and quantitative easing. For more risk tolerant investors, we recommend some exposure to both the high-yield and emerging market sectors.*

As the economy recovers, we continue to look for the best performance on a relative basis in the credit markets. Liquidity and confidence are returning and we have seen a marked convergence, or spread tightening of riskier bonds relative to benchmark Treasuries. However, on a spread basis, these markets still look attractive. As an example, the high-yield market (up in excess of 25% year-to-date) saw spreads peak at 2000 basis points (bps; Note: 100 bps equals 1%) in excess of the 10-year Treasury. Currently, that spread is approximately 1100 bps. Similar patterns can be found in investment-grade corporate and municipal sectors (see chart below). Despite the recent recovery from extremely oversold conditions (reflecting the depth of the credit crisis) on a long-term historical basis, credit markets still look attractive and current risk premiums reflect the outlook for higher default and lower recovery rates, relative to history.

Cross-Sector Yield History



Sources: Federal Reserve Board, Merrill Lynch, Haver Analytics

Past performance is not an indication of future results. An index is not managed and is unavailable for direct investment. High-yield bonds, also known as junk bonds, are subject to greater risk of loss of principal and interest, including default risk, than higher-rated bonds.

The Merrill Lynch High-Yield Master II index, which tracks the performance of the U.S. dollar denominated below investment-grade corporate debt that is publicly issued in the U.S. domestic market, has a current yield of 13.2% and the Merrill Lynch Corporate Master Bond index, which reflects investment-grade bonds with average maturities of at least one year, has a current yield of 6.50% versus the 3.75% of the 10-year Treasury. To the extent it fits within an investors' risk/reward profile, they should consider exposure to the credit markets, which will provide additional yield as well as, in our opinion, better relative price performance in a rising yield environment.

In terms of duration or average maturity, we remain slightly short of our benchmark. Realizing that each investor is different our guidance would be to hold an average maturity at the shorter end of one's individual risk tolerance, i.e., for an investor who typically holds 7- to 10-year maturities, we would currently recommend 7- to 8-year holdings. Investors concerned about rising bond yields might want to shorten duration further although we would point out that the current historically wide credit spreads will cushion some of the increase.

Please see pages 21 through 24 for important definitions and disclosures.

Q. In light of the current economy and state and local budget problems, how should we be tiering credit risk in the municipal bond sector?

General government and essential-service credit quality may be stressed for the next couple of years, reflecting the tax performance problems that arise from higher unemployment rates (reduced personal-income-tax collections) and shallow consumption activity among taxpayers (reduced sales tax collections). In addition, declines in home valuation and sales (lower property-tax receipts and mortgage transfer fees), and weakness in business profits (corporate income-tax collections) contribute to this stress. However, when the generally robust tax- and revenue-raising characteristics of large state and local investment grade issuers is considered, general obligation debt, in our opinion, still ranks fairly high from a credit quality perspective — even in challenging economic times. In the current economic climate, investors need to be particularly cognizant of maintaining a well-diversified portfolio and not be over-concentrated in one particular state or individual credit. Also, given recent downgrades, investors should review holdings for suitability and risk tolerances.

Therefore, we favor general obligation debt of large state and local investment-grade issuers from a credit-quality perspective, given their ability to raise revenues.

While state governments, cities and counties will face daunting fiscal and budgetary challenges over the next two years, the legal security protection offered by full faith and credit pledges and or the *ad valorem* pledge reveals investment-grade general obligation bonds to be an inherently lower-risk municipal debt for investors. In similar fashion, municipal utilities (water, sewer, power) should generally provide solid credit quality, even if coverage levels from usage fees slip. Since essential-purpose revenue bonds often feature a rate covenant that requires an issuer to raise rates to whatever level is necessary to meet debt service, and since these utilities are often monopolies facing little or no competition, we favor essential-purpose revenue bonds in the current economy.

However, even in these inherently low-risk sectors, examples exist of essential-purpose revenue bond issuers facing significant fiscal stress. For example, despite a rate covenant requiring the issuer to raise rates to meet debt service, Jefferson County Alabama's sewer system is delinquent on several payments associated with its multi-billion-dollar system. Rather than raise rates as required, the commissioners overseeing the system have instead pursued lawsuits and forbearance agreements, which have punished the general obligation ratings of the county as well.

As for sectors that represent a somewhat higher risk profile, we consider local and regional airport issuers, ports in general, private higher-education providers and tax-increment secured transactions to represent higher downgrade and liquidity risks. We consider "wish list" project financings such as stadiums, convention centers and start-up toll roads to fit into this category, considering that they also represent a generally higher exposure to downgrade and valuation pressure. While we would stress that any individual credit needs to be reviewed on its own particular merits, certain sectors of the market do represent a higher level of inherent risk when measured against large-issuer general obligation and essential-service borrowers.

A. *We favor general obligation debt of large state and local investment-grade issuers, from a credit quality perspective, given their ability to raise revenues.*

However, despite the risks that may be associated with a broad sector, investors can be potentially rewarded with higher yields by researching and getting comfortable with the unique credit characteristics on an individual issuer in an out-of-favor sector. Certain sectors can require, simply by virtue of their exposure to a competitive climate or economically sensitive revenue source, a more credit-intensive review to determine the nature of the bond's risk. For example, toll roads generally represent a type of credit that can experience a decline in transactions, possibly due to layoffs or reduced recreational travel. However, many large, mature toll roads across the country serve diverse commuter profiles or operate as vital, multi-state corridors for general travel and goods shipping, and consequently exhibit stable performance and high-quality ratings.

Q. Is there any value to municipal bond insurance?

It is an understatement to state that bond insurance today offers a much different value prospect for investors than it did less than two years ago. Bond insurance does not eliminate market risks. As of June 25, 2009, only one bond insurer — Assured Guaranty — carries a triple-A stable rating by S&P. Berkshire Hathaway Assurance (BHAC) and FSA are also rated triple-A by Standard & Poor's (S&P), however, they carry negative outlooks. On May 20, 2009, Moody's Investors Service (Moody's) placed Assured Guaranty's Aa2 rating and FSA's Aa3 rating on Negative Watch, reflecting Moody's ongoing recalibration of its mortgage stress tests and the consequent impact Moody's sees on insurer claims-paying quality. Based on our understanding of how punitive the new Moody's stress test will be, we anticipate that Moody's will drop the Assured Guaranty and FSA ratings further — potentially even out of the double-A rating category, depending on how closely mortgage delinquency, default and foreclosure performance sync with Moody's new model over the next three months. It appears for now that Moody's has the most critical view of insurer credit quality.

In light of the ongoing rating agency reviews of their housing stress models, the next most consequential question seems to be whether S&P, which has been steadily reassessing its default assumptions on mortgage-pool performance and downgrading mortgage-pool transactions, feels it should be more in line with Moody's and Fitch on insured ratings. At present, the triple-A stable rating on Assured Guaranty juxtaposes oddly with Moody's view of the insurer at Aa2 negative and Fitch's double-A, especially given S&P's expectations that the housing market will continue to tick downward over the next several quarters.

The present condition of the bond insurance industry is partially reflected by the industry's penetration performance measured versus issuance. Through 2007, for example, before the bond insurers started showing significant mortgage-pool stress, bond insurance had been used on approximately half of the long-term municipal-issue par brought to market. More recently, through May of 2008, long-term municipal issuance reached \$181 billion, of which only 25% was insured. Through May of 2009, however, insurance penetration had dropped even further compared to May 2008 totals, diving to only 12.5% of long-term issuance. The decline in penetration seems to point to a diminished appetite for insurance backing, with only three insurers now actively competing for bond insurance business (and BHAC among them playing only an opportunistic, bit part).

Despite the pronounced decline in insurance penetration, we believe there will be some opportunity to use bond insurance in a municipal portfolio. This is provided that there is no game changing ratings activity or outsized underlying default looming on the insurers' books. We believe that bond insurance can add value as long as the product offers at least one double-A or better rating. However, we continue to believe that investors should review an issuer's underlying credit quality and consider bond insurance to be a credit enhancement — not a credit substitution.

The tables on the following page are a summary of weightings to various sectors of the fixed-income market, duration stance, and sector recommendations based upon maturity preference.

A. *Despite the pronounced decline in insurance penetration, we believe there will be some opportunity to use bond insurance in a municipal portfolio.*

We believe that bond insurance can add value as long as the product offers at least one double-A or better rating. However, we continue to believe that investors should review an issuer's underlying credit quality and consider bond insurance to be a credit enhancement — not a credit substitution.

Fixed-Income Sector Weightings

Traditional Fixed Income							
	Underweight	Slight Underweight	Neutral	Slight Overweight	Overweight	Recent Changes	Date
U.S. Treasuries	X					Decrease	9/24/07
Agency Securities			X			Decrease	5/21/09
Mortgage-Backed Securities ¹	X					Decrease	5/21/09
Corporate Bonds					X	Increase	9/29/08
Alternative Income							
High-Yield Securities ²			X			Increase	5/21/09
Emerging Markets ³			X			Increase	5/21/09
Other Sectors							
Municipal Bonds ⁴					X	Increase	3/3/08
Duration Recommendation							
	Underweight	Slightly Short	Neutral	Slightly Long	Long		
Duration		X				Shorten	3/31/08

Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can result in the decline of the value of your investment.

¹The yield, average life and the expected maturity of mortgage-backed securities are based on prepayment assumptions that may or may not be met. Changes in prepayments may significantly affect yield, average life and expected maturity.

²High-yield bonds, commonly known as junk bonds, are subject to greater risk of loss of principal and interest, including default risk, than higher-rated bonds. The price of these bonds may be volatile, and they are generally only suitable for aggressive investors.

³Investing in foreign securities presents certain unique risks not associated with domestic investments, such as currency fluctuation and political and economic changes. This may result in greater price volatility.

⁴Income from municipal securities is generally free from federal taxes and state taxes for residents of the issuing state. While interest income is tax-free, capital gains, if any, will be subject to taxes. Income for some investors may be subject to the federal Alternative Minimum Tax (AMT).

Traditional Fixed-Income Sector Recommendations (Based on Maturity Preference)

	Short (1-5 years)	Intermediate (5-12 years)	Long (12+ years)
U.S. Treasuries	Underweight	Underweight	Underweight
Agencies - Non-Call	Neutral	Neutral	Neutral
Corporate Bonds	Overweight	Overweight	Overweight
Municipal Bonds	Neutral	Overweight	Overweight

U.S. Treasuries are guaranteed by the full faith and credit of the U.S. government for the timely payment of interest and principal if only held to maturity. Investments that are concentrated in a specific sector or industry may be subject to a higher degree of market risk than investments that are more diversified.

Q. What are our views on the emerging and foreign developed-country markets?

A. *We expect this positive trend in foreign-equity markets, especially emerging markets, to continue as long as the global economy remains on track for an economic recovery later this year and next year.*

Foreign-equity markets, especially emerging markets, have performed rather well during the past six months. We expect this trend to continue as long as the global economy remains on track for an economic recovery later this year and next year. Investors' appetites for risk have increased recently, thanks to signs that the financial crisis has stabilized and the downturn in economic activity may be nearing an end. Consequently, the demand for foreign equities has increased. In fact, higher-risk, emerging stock markets appear to be recovering better than developed-equity markets. That's primarily because of the shift in investor sentiment toward reflation strategies. This is reflected in us recommending an evenweight in developed international markets and a small overweight in emerging markets in our asset allocation models.

International investing themes have changed several times during the past few years. In 2007, investors believed that the international equity markets were decoupled from U.S. markets. However, the global economic downturn last year proved that position wrong. Instead, 2008 was a year of risk aversion because weak economic growth was reducing foreign trade and depressing global commodity prices. Consequently, many foreign equities markets dropped even more dramatically than U.S. equities markets declined. In recent months, investors have turned more optimistic again with a recovery in commodity markets leading to improved economic prospects for emerging market economies that produce those commodities. This increased interest in commodities and global equities rests on the reflation theme that governments around the world are pumping excess liquidity into their economies in order to restore economic growth.

Commodity prices dropped sharply late last year when traders worried that the financial crisis could lead to a deflationary spiral. This worst-case scenario pushed commodity prices below fair value. Now that the financial crisis has stabilized, commodity prices have recovered some of last year's losses. However, traders' concerns are now reversed from late last year. Instead of deflation, traders are worried that the Fed is flooding the economy with too much money, creating inflation risk. Looking ahead, commodity prices could stabilize in the second half of this year. That's because the rebound in commodity prices during the past six months is a bit overdone, given that the global economy is still very weak and there are no significant shortages of materials.

The willingness of investors to take risk again after pulling back on commodities and foreign equities last year is a positive sign that investors believe the worst may be behind us provided there are no major, unexpected shocks that would disrupt foreign trade.

Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater share-price volatility.

Buying commodities allows for a source of diversification for those sophisticated persons who wish to add commodities to their portfolios and who are prepared to assume the risks inherent in the commodities market. Any purchase represents a transaction in a non-income-producing commodity and is highly speculative. Therefore, commodities should not represent a significant portion of an individual's portfolio.

Q. Overall, should investors be leaning toward stocks or bonds?

A. *Based on current valuations we would suggest that investors lean into stocks to a larger degree.*

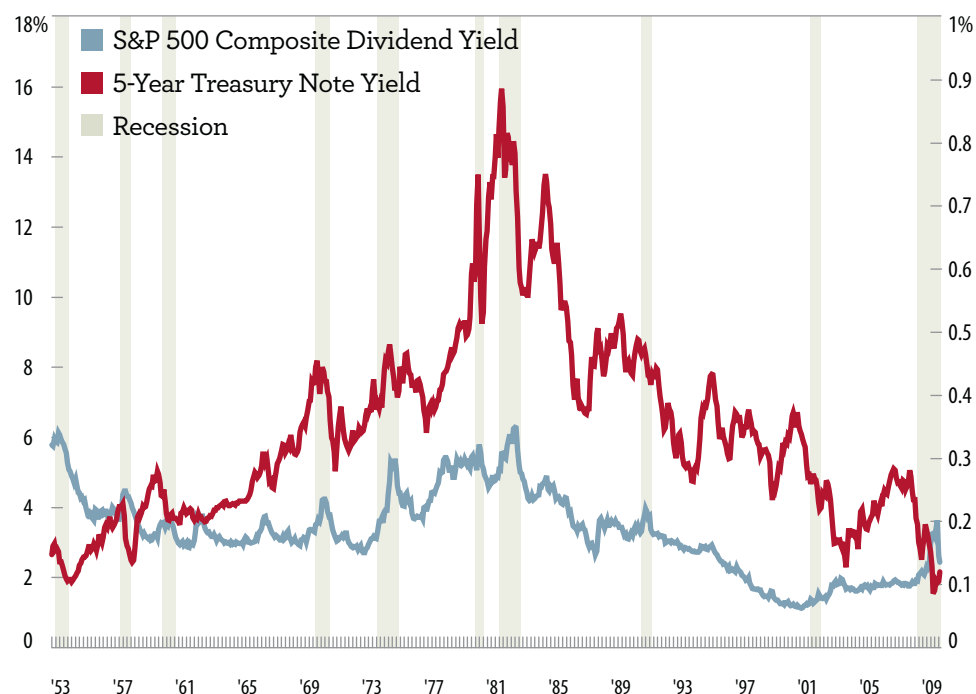
Investors have lived through unprecedented times and events over the past 24 months. A combination of wholesale, destructive deleveraging, recession, lack of available credit, and concerns over the banking system led to steep declines in equity indexes, record-low Treasury bond yields, and poor performance in non-government guaranteed or -sponsored debt instruments. In the uncertainty of late 2008 and the early part of 2009, investors placed a premium on relative safety and liquidity and higher-quality fixed-income instruments performed very well. The markets experienced an unprecedented divergence in yields between high- and low-quality debt instruments, as all but the most pristine issuers were, for all intents and purposes, shut out of the markets. As liquidity has improved, valuations in the debt markets have also improved with the yields between low- and high-quality bonds converging.

Currently, the 10-year Treasury (the “risk-free” rate or interest rate that it is assumed can be obtained by investing in financial instruments with no default risk) yields approximately 3.75%, a small premium compared to the current stated 2.92% yield of the S&P 500 index. While inflation expectations remain muted over the short and intermediate term, fixed income instruments, from today’s starting yields offer investors limited opportunities to rebuild the wealth destroyed in the latest bear market. If bond yields increase as expected in an economic recovery, investors could also see the value of their fixed income holdings decline. This is not a consideration if held until maturity, but is a potential negative for more active portfolios.

Stocks and bonds have historically had different risk and return profiles, and investors view them differently in terms of risk and also in what they potentially add to a portfolio. Comparing the two asset classes is difficult, but there are a couple of metrics that can point out the relative valuations of the two markets. One way to compare the two is to look at equity dividend yields versus Treasury yields. Looking at 50-years’ worth of data comparing the S&P 500 dividend yield and the five-year constant-maturity Treasury, we see, except for a very brief period in 1962, that the Treasury yield was higher. However, currently the reverse is true, with S&P dividends approximately 15 bps higher (see yield chart on the following page). It is important to note that not all stocks in the S&P 500 pay dividends and those that do have the ability to increase, decrease or totally eliminate dividends at any point without notice; unlike a Treasury, which is guaranteed as to the timely payment of principal and interest at a fixed rate and date.

Another way to compare the two markets is to look at what is often referred to as the “Fed model.” It compares the forward earnings yield of the S&P 500 (the inverse of the expected price/earnings ratio) to the yield of the 10-year Treasury. Using our equity strategy group’s estimates of 13.5 to 14 times, the earnings yield of the S&P 500 is currently 7.27%, which compares favorably with the 3.75% yield of the 10-year Treasury. Finally, one other measure to consider is the price of stocks versus the potential funds available to purchase them. We do this by comparing money held in money funds (institutional and retail) as a percentage of the market capitalization of the S&P 500. This metric is at the highest level on record (dating back to 1973), at 51%. All of these are valuation measures as opposed to timing measures, but all point to the relative attractiveness of equities based on current valuations.

S&P 500 Dividend Yield vs. Five-Year Treasury Note Yield (Constant Maturity)



Sources: Standard & Poor's, Haver Analytics, Federal Reserve Board

Past performance is not an indication of future results. An index is not managed and is unavailable for direct investment. Dividends can be increased, decreased or totally eliminated at any point without notice.

For most investors, stocks and bonds are not an either-or proposition. A well balanced portfolio has both. Based on current valuations we would suggest that investors with intermediate- and longer-term time horizons lean into equities to a larger degree than they traditionally would. While this is difficult after the turmoil the markets have been through over the past 18 months, debt instruments, in our view, will face significant headwinds in an economic recovery. These include potentially higher inflation and higher short term (Fed funds) rates, as well as the costs of financing significantly more debt from the federal government. For that reason we continue to favor equities in our asset allocation models.

Q. What are the strategic and tactical asset allocation recommendations in the current environment?

We recently updated our Strategic and Tactical Asset Allocation Models. The Strategic Asset Allocation model (shown on the following page) is based on long-term trends and expectations for the intermediate-to-distant future (7-10 years); Tactical Asset Allocation is the need for short-term adjustments to our strategic asset allocations. To reflect our current thinking about near-term risks and opportunities, we make these adjustments on an ad hoc or as-needed basis. Our nine-box asset allocation grid provides the foundation for our advice and guidance to clients.

Asset Allocation Models

Tactical Tilt as of 6/8/09

		Conservative			Moderate			Long-Term		
		Strategic	Tactical	Difference	Strategic	Tactical	Difference	Strategic	Tactical	Difference
Income	CASH	5.0%	2.0%	-3.0%	2.0%	2.0%	0.0%	2.0%	2.0%	0.0%
	TRADITIONAL FIXED INCOME	75.0%	76.0%	1.0%	58.0%	56.0%	-2.0%	38.0%	36.0%	-2.0%
	Short-term Inv Grade	50.0%	49.0%	-1.0%	20.0%	18.0%	-2.0%	10.0%	8.0%	-2.0%
	Intermediate Inv Grade	25.0%	27.0%	2.0%	23.0%	25.0%	2.0%	13.0%	15.0%	2.0%
	Long-term Inv Grade	0.0%	0.0%	0.0%	15.0%	13.0%	-2.0%	15.0%	13.0%	-2.0%
	ALTERNATIVE INCOME	13.0%	11.0%	-2.0%	23.0%	21.0%	-2.0%	33.0%	31.0%	-2.0%
	High-yield	7.0%	7.0%	0.0%	14.0%	14.0%	0.0%	21.0%	21.0%	0.0%
	Emerging Market Debt	3.0%	3.0%	0.0%	6.0%	6.0%	0.0%	9.0%	9.0%	0.0%
	REITs	3.0%	1.0%	-2.0%	3.0%	1.0%	-2.0%	3.0%	1.0%	-2.0%
	COMMODITIES	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
EQUITIES	7.0%	11.0%	4.0%	17.0%	21.0%	4.0%	27.0%	31.0%	4.0%	
LargeCap Value	2.0%	2.0%	0.0%	5.0%	5.0%	0.0%	8.0%	8.0%	0.0%	
Large Cap Growth	3.0%	3.0%	0.0%	7.0%	7.0%	0.0%	11.0%	11.0%	0.0%	
Mid Cap Blend	0.0%	1.0%	1.0%	1.0%	2.0%	1.0%	2.0%	3.0%	1.0%	
Small Cap Blend	0.0%	1.0%	1.0%	1.0%	2.0%	1.0%	2.0%	3.0%	1.0%	
International	2.0%	2.0%	0.0%	3.0%	3.0%	0.0%	4.0%	4.0%	0.0%	
Emerging Market	0.0%	2.0%	2.0%	0.0%	2.0%	2.0%	0.0%	2.0%	2.0%	
Growth and Income	CASH	2.0%	2.0%	0.0%	2.0%	2.0%	0.0%	2.0%	2.0%	0.0%
	TRADITIONAL FIXED INCOME	54.0%	52.0%	-2.0%	31.0%	29.0%	-2.0%	10.0%	8.0%	-2.0%
	Short-term Inv Grade	15.0%	13.0%	-2.0%	7.0%	5.0%	-2.0%	0.0%	0.0%	0.0%
	Intermediate Inv Grade	24.0%	26.0%	2.0%	17.0%	19.0%	2.0%	5.0%	5.0%	0.0%
	Long-term Inv Grade	15.0%	13.0%	-2.0%	7.0%	5.0%	-2.0%	5.0%	3.0%	-2.0%
	ALTERNATIVE INCOME	12.0%	10.0%	-2.0%	20.0%	18.0%	-2.0%	28.0%	26.0%	-2.0%
	High-yield	6.0%	6.0%	0.0%	12.0%	12.0%	0.0%	18.0%	18.0%	0.0%
	Emerging Market Debt	3.0%	3.0%	0.0%	5.0%	5.0%	0.0%	7.0%	7.0%	0.0%
	REITs	3.0%	1.0%	-2.0%	3.0%	1.0%	-2.0%	3.0%	1.0%	-2.0%
	COMMODITIES	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
EQUITIES	32.0%	36.0%	4.0%	47.0%	51.0%	4.0%	60.0%	64.0%	4.0%	
LargeCap Value	8.0%	8.0%	0.0%	11.0%	11.0%	0.0%	14.0%	14.0%	0.0%	
Large Cap Growth	12.0%	12.0%	0.0%	17.0%	17.0%	0.0%	20.0%	20.0%	0.0%	
Mid Cap Value	1.0%	1.5%	0.5%	2.5%	3.0%	0.5%	4.0%	4.5%	0.5%	
Mid Cap Growth	2.0%	2.5%	0.5%	4.0%	4.5%	0.5%	6.0%	6.5%	0.5%	
Small Cap Value	1.0%	1.5%	0.5%	1.5%	2.0%	0.5%	2.0%	2.5%	0.5%	
Small Cap Growth	1.0%	1.5%	0.5%	2.0%	2.5%	0.5%	3.0%	3.5%	0.5%	
International	5.0%	5.0%	0.0%	7.0%	7.0%	0.0%	9.0%	9.0%	0.0%	
Emerging Market	2.0%	4.0%	2.0%	2.0%	4.0%	2.0%	2.0%	4.0%	2.0%	
Growth	CASH	2.0%	2.0%	0.0%	2.0%	2.0%	0.0%	2.0%	2.0%	0.0%
	TRADITIONAL FIXED INCOME	28.0%	26.0%	-2.0%	13.0%	11.0%	-2.0%	0.0%	0.0%	0.0%
	Short-term Inv Grade	14.0%	12.0%	-2.0%	5.0%	3.0%	-2.0%	0.0%	0.0%	0.0%
	Intermediate Inv Grade	10.0%	12.0%	2.0%	5.0%	7.0%	2.0%	0.0%	0.0%	0.0%
	Long-term Inv Grade	4.0%	2.0%	-2.0%	3.0%	1.0%	-2.0%	0.0%	0.0%	0.0%
	ALTERNATIVE INCOME	5.0%	3.0%	-2.0%	5.0%	3.0%	-2.0%	3.0%	1.0%	-2.0%
	High-yield	2.0%	2.0%	0.0%	2.0%	2.0%	0.0%	0.0%	0.0%	0.0%
	Emerging Market Debt	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
	REITs	3.0%	1.0%	-2.0%	3.0%	1.0%	-2.0%	3.0%	1.0%	-2.0%
	COMMODITIES	3.0%	3.0%	0.0%	3.0%	3.0%	0.0%	3.0%	3.0%	0.0%
EQUITIES	62.0%	66.0%	4.0%	77.0%	81.0%	4.0%	92.0%	94.0%	2.0%	
LargeCap Value	11.0%	11.0%	0.0%	12.0%	12.0%	0.0%	13.0%	13.0%	0.0%	
Large Cap Growth	22.0%	22.0%	0.0%	24.0%	24.0%	0.0%	26.0%	26.0%	0.0%	
Mid Cap Value	4.0%	4.5%	0.5%	6.0%	6.5%	0.5%	7.5%	8.0%	0.5%	
Mid Cap Growth	6.0%	6.5%	0.5%	6.0%	6.5%	0.5%	7.5%	8.0%	0.5%	
Small Cap Value	3.0%	3.5%	0.5%	3.0%	3.5%	0.5%	3.5%	4.0%	0.5%	
Small Cap Growth	3.0%	3.5%	0.5%	4.0%	4.5%	0.5%	3.5%	4.0%	0.5%	
International	10.0%	10.0%	0.0%	16.0%	16.0%	0.0%	22.0%	22.0%	0.0%	
Emerging Market	3.0%	5.0%	2.0%	6.0%	8.0%	2.0%	9.0%	9.0%	0.0%	

Definitions

The **CBOE (Chicago Board Options Exchange) Volatility Index (VIX)** shows the market's expectation of 30-day volatility. It is constructed using the implied volatilities of a wide range of S&P 500 index options. This volatility is meant to be forward-looking and is calculated from both calls and puts. The VIX is a widely used measure of market risk and is often referred to as the “investor fear gauge.”

The **Dow Jones Industrial Average** is based on 30 major companies weighted by price.

The **S&P 500 Index** consists of 500 industrial, financial, utility and transportation companies with market capitalizations of \$3 billion or more.

The **New York Stock Exchange Composite Index** measures all common stocks listed on the New York Stock Exchange and four subgroup indexes: industrial, transportation, utility and finance. The index tracks the change in the market value of NYSE common stocks and is adjusted to eliminate the effects of new listings and delistings.

The **Russell 2000 Index** is an index measuring the performance of the 2,000 smallest companies in the Russell 3000 Index, which is made up of 3,000 of the biggest U.S. stocks. The Russell 2000 serves as a benchmark for small-cap stocks in the United States.

The **Russell 1000 Index** is an index measuring the performance of the 1,000 largest companies in the Russell 3000 Index, which is made up of 3,000 of the biggest U.S. stocks. The Russell 1000 serves as a benchmark for large-cap stocks in the United States.

The **Russell 3000 Index** is a market-capitalization-weighted equity index maintained by the Russell Investment Group that seeks to be a benchmark of the entire U.S. stock market. More specifically, this index encompasses the 3,000 largest U.S.-traded stocks, in which the underlying companies are all incorporated in the U.S.

The **Consumer Price Index (CPI)** is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. The CPI is calculated by taking price changes for each item in the predetermined basket of goods and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living. Merrill Lynch High Yield Master II Index tracks the performance of U.S.-dollar-denominated, below-investment-grade corporate debt publicly issued in the U.S. domestic market.

The **Merrill Lynch Corporate Master Bond Index** reflects investment-grade bonds with average maturities of at least one year.

The **Standard & Poor's Rating Agency (S&P)** is a financial services company that rates stocks and corporate and municipal bonds according to risk profiles.

Moody's Investors Service (Moody's) is an independent, unaffiliated research company that rates fixed-income securities. Moody's assigns ratings on the basis of risk and the borrower's ability to make interest payments.

Short-Term Fixed-Income: Fixed-income instruments that mature in one to six years.

Intermediate-Term Fixed Income: Fixed-income instruments that mature in 6 to 12 years.

Long-Term Fixed Income: Fixed-income instruments whose maturities are greater than 12 years.

High Yield: Non-investment-grade fixed-income securities (rated Ba1 or lower by Moody's and/or BB+ or lower by S&P). These investments are considered to be speculative and are subject to a higher degree of risk.

High-yield bonds, commonly known as junk bonds, are subject to greater risk of loss of principal and interest, including default risk, than higher-rated bonds. The prices of these bonds may be volatile, and they are generally only suitable for aggressive investors.

International: Financial markets in developed economies outside of the U.S.

Emerging Markets: Financial markets in countries with developing economies. These markets are typically immature compared to those of the world's major financial centers but are becoming increasingly sophisticated and integrated into international markets; they provide potentially higher returns but are intensely volatile.

Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability and different accounting standards. This may result in greater asset-price volatility.

REITs: Real estate investment trusts (REITs) trade on the major exchanges and invest in real estate directly, either through properties or mortgages.

There are special risks associated with an investment in real estate, including credit risk, interest rate fluctuations and the impact of varied economic conditions.

Large-Cap Growth: Stocks that have a market cap greater than \$5 billion and a price-to-book ratio greater than 2.0.

Large-Cap Value: Stocks that have a market cap greater than \$5 billion and a price-to-book ratio less than or equal to 2.0.

Mid-Cap Growth: Stocks that have a market cap between \$1 billion and \$5 billion and a price-to-book ratio greater than 2.0.

Mid-Cap Value: Stocks that have a market cap between \$1 billion and \$5 billion and a price-to-book ratio less than or equal to 2.0.

Small-Cap Growth: Stocks that have a market cap less than \$1 billion and a price-to-book ratio greater than 2.0.

Small-Cap Value: Stocks that have a market cap less than \$1 billion and a price-to-book ratio less than or equal to 2.0.

The prices of small-cap and mid-cap company stocks are generally more volatile than large company stocks. They often involve higher risks because smaller companies may lack the management expertise, financial resources, product diversification and competitive strengths to endure adverse economic conditions.

Commodities: Basic goods used in commerce that are generally interchangeable with other commodities of the same type. Commodities are most often used as inputs in the production of other goods or services.

Buying commodities allows for a source of diversification for those sophisticated persons who wish to add commodities to their portfolios and who are prepared to assume the risks inherent in the commodities market. Any purchase represents a transaction in a non-income-producing commodity and is highly speculative. Therefore, commodities should not represent a significant portion of an individual's portfolio.

Disclaimers

Past performance is not an indication of future results.

An index is not managed and is unavailable for direct investment.

Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater share-price volatility.

The prices of small company stocks are generally more volatile than large company stocks. They often involve higher risks because smaller companies may lack the management expertise, financial resources, product diversification and competitive strengths to endure adverse economic conditions.

Dividends can be increased, decreased or totally eliminated at any point without notice.

While stocks generally have a greater potential return than government bonds and Treasury bills, they involve a higher degree of risk. Government bonds and Treasury bills, unlike stocks, are guaranteed as to payment of principal and interest by the U.S. government if held to maturity. Although Treasuries are considered free from credit risk they are subject to other types of risks. These risks include interest-rate risk, which may cause the underlying value of the bond to fluctuate inversely to a change in interest rates.

High-yield bonds, also known as junk bonds, are subject to greater risk of loss of principal and interest, including default risk, than higher-rated bonds.

Technology and Internet-related stocks, especially of smaller, less-seasoned companies, tend to be more volatile than the overall market.

Investments that are concentrated in a specific sector or industry may be subject to a higher degree of market risk than investments that are more diversified.

Buying commodities allows for a source of diversification for those sophisticated persons who wish to add commodities to their portfolios and who are prepared to assume the risks inherent in the commodities market. Any purchase represents a transaction in a non-income-producing commodity and is highly speculative. Therefore, commodities should not represent a significant portion of an individual's portfolio.

There are special risks associated with an investment in real estate, including credit risk, interest-rate fluctuations and the impact of varied economic conditions. Distributions from REIT investments are taxed at the owner's tax bracket.

Important Disclosures Information

For important disclosure information, please contact:

Wells Fargo Advisors
Attn: Advisory Services (Disclosure Information)
One North Jefferson
St. Louis, MO 63103

Or call by phone:

(888) 410-9203

Please remember to specify the issuer(s) with respect to which you would like to receive disclosure information.

Analyst Certification: The analyst who is primarily responsible for commentary on any subject company/companies and securities in this report has represented that the commentary accurately reflects that analyst's personal views. The analyst further certifies that he/she receives no compensation that is directly or indirectly related to the specific recommendation or views contained within this report.

Investment and Insurance Products: ► NOT FDIC Insured ► NO Bank Guarantee ► MAY Lose Value

Wells Fargo Advisors, LLC, Member SIPC, is a registered broker-dealer and a separate non-bank affiliate of Wells Fargo & Company. ©2009 Wells Fargo Advisors, LLC. All rights reserved.