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Equities Fall in September as Riskier Stocks Lead Market Lower

Equity markets fell sharply in September as investors remained worried about sovereign debt problems in Europe and the potential for a double-dip recession in the United States. The decline was not uniform throughout the market. Traditional safe-haven sectors such as utilities, telecom services, consumer staples and health care held up relatively well while the more economically sensitive sectors plummeted. Energy, materials and the financial services sectors lost more than ten percent during the month, as declining commodity prices and worries about the financial system caused investors to shed risk. On the other hand, the information technology sector outperformed the S&P 500 as good earnings, upbeat outlooks from Oracle, Adobe and Accenture and reasonable valuations bolstered the sector. Looking at markets more broadly, large capitalization equities outperformed small and mid-capitalization equities. Not surprisingly given the overseas concerns, the S&P 500 outperformed foreign market indices. The dollar regained its status as a safe-haven as the dollar index rose 6.0% during the month, while gold fell 11.3% in September.

S&P 500 Sector Data as of September 30, 2011								
			Performance			Performance Versus S&P 500		
	Adjusted Market Cap ($Million)	Index Level	Month to Date	Quarter to Date	Year to Date	Month to Date	Quarter to Date	Year to Date
TOTAL RETURNS								
S&P 500 (TR)	N/A	1,930.79	-7.03%	-13.87%	-8.68%			
PRICE RETURNS								
S&P 500	10,303,141	1,131.42	-7.18%	-14.33%	-10.04%			
PRICE RETURNS BY								
Utilities	408,571	170.77	-0.13%	0.44%	7.17%	7.05%	14.77%	17.21%
Consumer Staples	1,203,399	306.71	-3.70%	-4.94%	1.03%	3.48%	9.39%	11.07%
Health Care	1,250,546	367.73	-4.56%	-10.51%	0.81%	2.62%	3.82%	10.85%
Telecom Services	338,567	122.01	-1.34%	-9.18%	-5.22%	5.84%	5.15%	4.82%
Information Technology	2,002,607	378.19	-3.42%	-7.96%	-6.52%	3.76%	6.37%	3.52%
Consumer Discretionary	1,097,133	275.53	-6.96%	-13.32%	-6.77%	0.22%	1.01%	3.27%
Energy	1,198,111	442.79	-12.58%	-20.86%	-12.62%	-5.40%	-6.53%	-2.58%
Industrials	1,058,277	252.62	-9.40%	-21.51%	-16.11%	-2.22%	-7.18%	-6.07%
Materials	345,944	184.55	-16.59%	-24.96%	-22.98%	-9.41%	-10.63%	-12.94%
Financial Services	1,399,987	159.05	-11.56%	-23.12%	-25.94%	-4.38%	-8.79%	-15.90%

**Source: Standard & Poor's.*

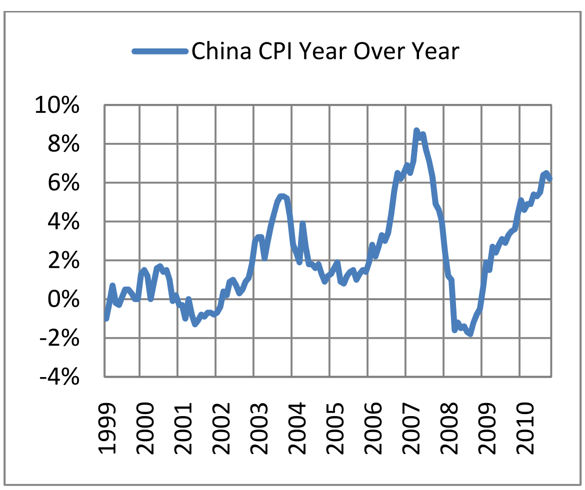
European Problems Continue

Europe debt concerns remain the focal point and continue to pressure global financial markets around the world. Greece is the headline-grabber, but the real worries center around large European banks. Most analysts believe that Greece will have to default sooner rather than later. The only question is the magnitude of the losses facing Greek debt-holders. The greater concern is whether a Greek default would cause European banks to collapse, or cause collateral damage to Spain or Italy. While Europe can withstand a Greek default, it cannot afford to see Italy or Spain collapse. If Europe is able to stabilize the Europeans banks, a powerful rally in the global economy and equities would likely ensue.

Even though most United States banks have relatively low exposure to Greece, the ripple effects from a Greek default would cause GDP growth to slow domestically. While Europe has contributed very little to global growth, it still accounts for about a quarter of the global economy. A precipitous drop in the European economy will slow growth throughout the world.

China Continues to Slow

While the developed world has spent the past two years struggling with sub-par growth, China and other emerging markets have been struggling with rising prices in their domestic markets. Escalating food, energy, and housing prices coupled with increasing labor costs have led to accelerating inflation in China.



Sources: China Economic Information Network & Bloomberg

China has been trying to put the brakes on their economy and engineer a soft landing. In doing so, they have contributed to slowing economic growth internationally.

United States Economic Outlook Remains Cloudy

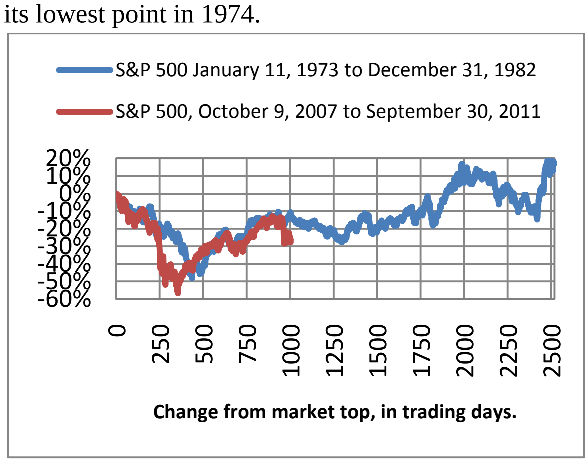
Economic activity in the United States remains choppy and uneven at best. The economy is not losing jobs, but it is still unable to create enough jobs to reduce unemployment and promote sustainable economic growth.

Manufacturing growth, which had been a bright spot since the recovery started, has slowed considerably. The Institute for Supply Management's Purchasing Managers Index ended September at 51.6. This is well below the 61.4 level reached in February, but does indicate that the manufacturing sector is still expanding. Hopefully, it has stabilized and will once again help boost growth later in the year, but this is by no means a certainty.

On the bright side, housing data has temporarily stabilized and appears to be tracing out a bottom. Part of the improvement is likely due to the summer selling season. Even so, historically low interest rates, rising apartment rents, low housing starts, a reduction in foreclosure inventory, and record affordability indicate that housing is unlikely to subtract from economic growth. We expect that by 2013 at the latest, increased housing starts and sales activity will start being a positive contributor to economic growth.

S&P 500: A Historical Comparison

While no two set of historical periods are identical, it is useful to see how past bear markets have played out in order to be able to forecast a range of outcomes for the future. We think it is instructive to view how the bear market played out in the 1970s after hitting its lowest point in 1974.



The 1970s was a period characterized by malaise. People were disenchanted with their politicians, unemployment was rising, and they were worried about the competitiveness of America. Eventually, the problems worked themselves out over time and the United States began to grow again. There are key differences between the 1970s and today including the sovereign debt problems emanating from Europe and a higher level of leverage in the United States. While these problems are difficult, they will pass with time. JLAM thinks it is instructive to note that during the last secular bear market and economic period filled with angst, the equity markets hit their nominal low halfway through the bear market. Subsequent declines were of much smaller magnitude and markets trended higher despite the volatility over the ensuing time period.

No Change in Long-term Outlook

We remain constructive on equities over the next twelve months. However, we are worried that a short-term, high volume sell-off is needed to finally create enough pessimism and value in the market. We think a pull-back would be short-lived, especially if the economic data stabilizes. At a certain point, value will start to outweigh fear and the money on the sidelines will go back into the equity markets looking for values. While we are not there yet, we think we are close.

Monthly Market Statistics

	12/31/10	08/31/11	09/30/11	Monthly % Change	YTD % Change	52-week High	52-week Low
DJIA	11,577.51	11,613.53	10,913.38	-6.03%	-5.74%	12,810.54	10,719.94
S&P 500	1,257.64	1,218.89	1,131.42	-7.18%	-10.04%	1,363.61	1,119.46
S&P Midcap 400	907.25	875.00	781.26	-10.71%	-13.89%	1,015.26	775.07
NASDAQ Composite	2,652.87	2,579.46	2,415.40	-6.36%	-8.95%	2,873.54	2,341.84
NASDAQ 100	2,217.86	2,241.01	2,139.18	-4.54%	-3.55%	2,429.50	1,975.33
Russell 2000	783.65	726.81	644.16	-11.37%	-17.80%	865.29	643.42
NYSE Arca Tech 100	1,084.81	1,043.39	999.37	-4.22%	-7.88%	1,205.34	956.46
NYSE Financial	4,958.62	4,217.39	3,805.34	-9.77%	-23.26%	5,414.71	3,696.46
NYSE Healthcare	6,501.53	6,793.56	6,483.34	-4.57%	-0.28%	7,441.28	6,176.26
NYSE Energy	12,520.29	12,069.57	10,953.59	-9.25%	-12.51%	14,536.17	10,549.41
MSCI EAFE	1,658.30	1,523.58	1,373.33	-9.86%	-17.18%	1,809.61	1,331.35
MSCI EM	1,151.38	1,033.15	880.43	-14.78%	-23.53%	1,206.49	851.51
U.S. Dollar Index	78.96	74.12	78.55	5.99%	-0.52%	81.20	72.93
Gold	1,421.10	1,828.50	1,620.40	-11.38%	14.02%	1888.70	1315.40
Oil	91.38	88.81	79.20	-10.82%	-13.33%	113.93	79.20
5 yr. Note	2.02%	0.95%	0.95%	0.00%	-52.97%	2.40%	0.78%
10 yr. Note	3.30%	2.22%	1.91%	-13.96%	-42.12%	3.74%	1.72%
30 yr. Bond	4.36%	3.59%	2.91%	-19.03%	-33.33%	4.77%	2.80%

**Sources: Wall Street Journal & Bloomberg*

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