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THE FSAG ADVISOR

Market & Economic Update

Following a very difficult 2008, which saw a global financial and economic meltdown that was nearly unprecedented, stocks entered 2009 by falling another 35% in the United States as fears of depression and financial system nationalization gripped investors. From the March 2009 lows, stocks galloped higher as those fears dissipated and as investors witnessed the power of the most massive global monetary and fiscal stimuli imaginable begin to reflate economic activity. We have described it as a tug of war between the forces of debt-induced deflation and those of policy induced reflation. While deleveraging and other deflationary forces have not left the scene, consistent and aggressive policy ignited the reflationary process.

2009 produced negative real economic growth, weak nominal growth and significant earnings declines. Despite that backdrop, "risk" assets outperformed "safe" assets as sidelined cash (which was producing near-zero returns) moved back into the markets. Emerging markets handily beat developed markets. Inflation fell in most countries, but widespread deflation was avoided. Treasury rates moved modestly higher as the yield curve steepened. Quality spreads narrowed, while equity markets remained volatile, but ended the year with sharp gains. Financial stocks and other low-quality securities led the way back and information technology was the standout sector performer. Government spending reached record proportions, and the year ended with cyclical stimulus leading the way and masking structural problems that remain.

It is with this backdrop that BlackRock ventures forward with their predictions for 2010:

1. The US economy grows above 3% in 2010 and outpaces the G-7.
2. Job growth in the United States turns positive early in 2010, but the unemployment rate remains stubbornly high.
3. Earnings rise significantly despite mediocre economic growth.
4. Inflation remains a non-issue in the developed world.
5. Interest rates rise at all points on the Treasury curve, including fed funds.
6. US stocks outperform cash and Treasuries, and most developed markets.
7. Emerging markets outperform as emerging economies grow significantly faster than developed regions.
8. Healthcare, information technology and telecommunications outperform financials, utilities and materials.
9. Strong free cash flow and

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2009 Returns

DOW	*22.60%*
S&P 500	*26.41%*
NASDAQ	*45.32%*
Russell Small Cap	*27.17%*
Russell Mid Cap	*40.48%*
MSCI EAFE	*31.78%*
Barclay US Agg	*6.37%*
Barclay Muni.	*14.94%*

Higher Taxes?

According to the non-partisan Congressional Budget Office, aggregate federal budget deficits will surpass $7 trillion over the next decade, assuming a continuation of current fiscal policy. A White House estimate, issued in late August 2009, acknowledged that the total budgetary shortfall could reach $9.05 trillion over that same period, if Congress enacted the administration's spending proposals.

Though raising taxes is always politically problematic, financial markets could demand that Uncle Sam raise additional revenue or face sharply escalating financing costs and/or a weaker dollar. Already, the Obama administration has proposed raising the top marginal tax bracket to 39.6%, and there is ample precedent for even higher rates on upper-income Americans. During the 1950s and early 1960s, the top rate was 92%; as recently as the mid-1980s, the highest tax bracket was still 50%. As taxes rise, municipal bonds become even more attractive, since the income they generate is generally exempt from federal income tax.

Source: Timothy McGregor, Northern Trust

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Retirement: Does Your Withdrawal Strategy Need a Second Look?

A sustainable withdrawal rate is critical to retirement planning. Draw too heavily on your savings, especially in the early years, and you could run out of money too soon. Take too little, and you might needlessly deny yourself the ability to enjoy your money.

In its simplest terms, a withdrawal rate is the percentage you withdraw from an investment portfolio in any particular year. However, in retirement income planning, what's important is not just your withdrawal rate, but your sustainable withdrawal rate.

A sustainable withdrawal rate represents the maximum amount (expressed as either a dollar amount or a percentage) that can be withdrawn from your retirement assets each year with reasonable certainty that the portfolio will provide income for as long as it's needed (for example, throughout your lifetime).

A commonly expressed rule of thumb states that your portfolio should last for your lifetime if you initially withdraw 4% of your balance (based on an asset mix of 60% stock and 40% fixed income securities), and then continue withdrawing that same dollar amount each year, adjusted for inflation. However, this rule of thumb has been under increasing scrutiny, and like any rule of thumb, it may not apply to you.

Why is it important?

A sustainable withdrawal rate is critical to retirement planning. Draw too heavily on your savings, especially in the early years, and you could run out of money too soon. Take too little, and you might needlessly deny yourself the ability to enjoy your money. You want to find a rate of withdrawal that gives you the best chance to maximize income over your entire retirement period.

Withdrawal rates are based on a number of assumptions, including your living expenses, projected lifespan, risk tolerance, projected rates of return and inflation, asset allocation, taxes, and whether you wish to leave a portion of your estate to others. As you progress in retirement, you'll have empirical data against which you can evaluate these assumptions. Plus, your investment horizon will be getting shorter. That's why it's important to periodically revisit your withdrawal strategy during your retirement to see if your assumptions are still accurate and whether your strategy needs to be modified.

Dealing with market volatility

If you're currently withdrawing a fixed percentage of your investment portfolio each year, the amount you receive will fluctuate with the performance of your portfolio. Small changes may not significantly impact your lifestyle. But what if your portfolio suffers a serious decline due to a market downturn? Will you be able to meet your expenses with the reduced withdrawal amount you'll be receiving? If you're currently withdrawing a fixed dollar amount each year, you may be able to meet your expenses, but can your reduced portfolio continue to support that same dollar amount or will your assets be depleted much too soon?

The converse of this is also true. If your portfolio realizes a gain that's significantly greater than your assumptions, a fixed percentage withdrawal will provide you with more dollars than you had been taking. Do you need the additional income? If you're taking a fixed dollar amount each year, is it time to give yourself a raise?

Market volatility may also lead you to consider changes in your asset allocation. If your portfolio is down, you may be inclined to become more conservative to avoid additional losses; conversely, when your portfolio is up, you might contemplate becoming more bullish. But if your asset allocation is designed to produce sustainable long-term income, changes should be considered carefully and only implemented as part of a disciplined strategy.

Other factors to consider

When you review your withdrawal strategy, make sure you consider the following:

Inflation: Inflation erodes your buying power. If you've underestimated the inflation rate, you may need to increase your withdrawals. If your portfolio can't support additional withdrawals, you'll need to reduce your expenses, or find another source of income (e.g., part-time work) to maintain your lifestyle. If inflation is lower than you've anticipated, you may be able to withdraw less and prolong your portfolio's income-producing ability.

Lifestyle: You may find that your expenses during retirement decrease from your initial estimate as you travel less or downsize a home--or they may increase because of health care or other costs.

Legacy: A decision to increase or decrease the amount you leave to heirs or charities can have a significant impact on your withdrawal strategy.

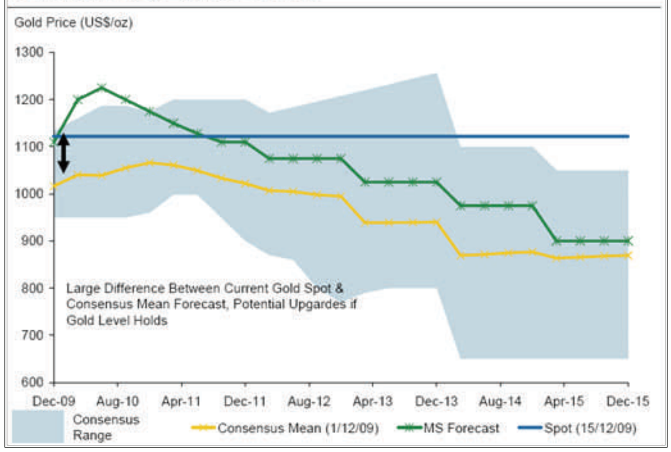
Revisiting your withdrawal strategy will allow you to focus on changes that have occurred during your retirement and fine-tune your strategy going forward, helping to ensure your retirement will be a financially secure one.

Gold: Forecast Price Changes

Our assessment of the balance of risks to gold investment demand, and other price influencing factors in the gold market in 2010 and beyond is that the prospects of a rising US dollar will increasingly weigh on the upside to prices as the year develops. Moreover, this will likely increase in 2011 and beyond, although other sources of investment demand are expected to remain strong. This is why, despite an upgrade in our base and bull case price forecasts for 2010 and 2011, we now have a declining price profile from 2011 onwards.

Moreover, while uncertainties in respect of economic recovery in the US and elsewhere remain high, with the continuing possibility of further adjustments to the anticipated timing of rising interest rates, we have also factored into our base and bull case price scenarios the prospect of a new peak in nominal gold prices in US dollar terms in 2010. Under our base case scenario, we anticipate the peak price could be in the range of $1,250-1,300/oz, while under our bull case scenario (which anticipates a later rise in US interest rates and the US dollar), this peak range could be as high as $1,325-1,350/oz.

Morgan Stanley Base Case Gold Price Forecast vs Consensus, 2010e-2015e



We currently attach a 60% probability to our base case but only a 15% probability to our bull case as we anticipate that there is a greater risk that the timing of the turn in the interest rate cycle will occur earlier than currently forecast rather than later, and the US dollar appreciation that would result could also commence earlier and be more substantial, reducing the odds of a higher peak and stronger subsequent price profile.

Under our bear case scenario, which is essentially driven by expectations of an earlier rise in US interest rates than currently forecast, with an associated earlier and stronger rise in the US dollar, we assume that the peak in the current bull market has already occurred at $1,227/oz in December 2009. We attach a 25% probability to this outcome at the present time.

Source: Morgan Stanley Research Global

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slow growth lead to an increase in M&A activity.

10. Republicans make noticeable gains in the House and Senate, but Democrats remain firmly in control of Congress.

In our view, a gradually improving global economy, coupled with the likelihood of some interest rate increases, should create an environment where equities and select credit-sensitive fixed income securities outperform Treasuries and cash. For that to occur, necessary lynchpins would include healthy corporate profit growth, a peaking of US unemployment and a successful tightrope walk by central bankers. Economic growth in the United States and the rest of the developed world is likely to be above trend, but well below the typical recovery after a recession. We expect cyclical improvement to lead to a resumption of modest employment increases, but that a stubbornly high unemployment rate will persist. We hope and believe that inflation remains only a topic of discussion, rather than an economic reality.

We believe there is little room for P/E multiple improvement, and that stocks will require earnings growth to move forward. Therefore, a focus on quality is in order, as we expect to see more balanced performance between cyclical, defensive and growth sectors. Our belief is that the United States will perform at least as well as other developed markets given the likelihood of stronger economic and earnings growth. A good cyclical and secular picture for emerging markets should enable another year of outperformance. We expect that a paucity of growth coupled with strong balance sheets and free cash flow will accelerate M&A activity. In summary, 2010 is likely to be a year of continued modest cyclical recovery, countered by the structural problems that continue to face most of the developed world.

Source: BlackRock

Stock in the News: Brocade Communications Systems (BRCD)

Brocade Communications Systems (BRCD) develops, markets, sells and supports data storage networking products and services. We believe the storage area network market will grow faster than the overall IT industry given the severity of the cutback during the downturn. The company also provides solutions for disaster recovery, data security, and regulatory compliance issues. The shares declined significantly after Hewlett-Packard announced its plan to acquire 3COM instead of BRCD. Although this pending merger makes it less likely that BRCD will be acquired near term, further consolidation in the networking industry is likely. We believe BRCD has strong products and would strengthen a potential acquirer's portfolio.

Bulls Say

- Cisco is entering the server market and is selling more of its products directly to end users, sometimes bypassing the storage OEMs such as EMC and IBM. These firms may attempt to direct more business to Brocade in response.
- We're already seeing signs of a larger relationship between Brocade and IBM, which (along with Hewlett-Packard) recently qualified Brocade's host bus adapters, providing Brocade a foothold in a market historically dominated by QLogic QLGC and Emulex ELX. IBM also inked a deal with Brocade to rebrand some of its IP networking products.
- Brocade should be able to realize some revenue synergies and cost savings from its acquisition of Foundry as it continues to remove redundancies in management and administration.

Risks

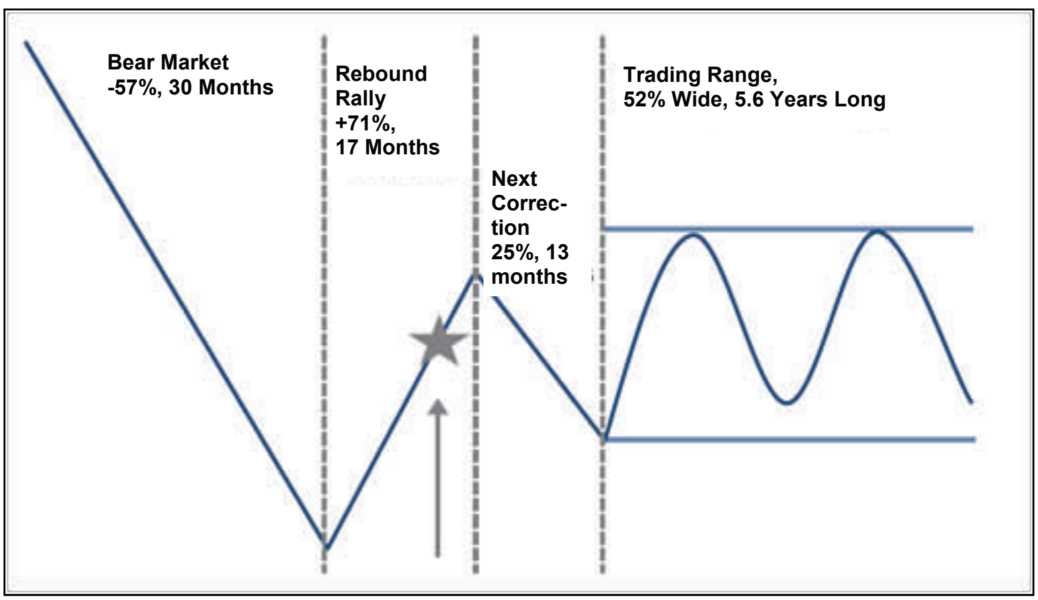
Risks include a slowdown in the global economy, slower-than-expected adoption rates for new products, and increased competition as a result of industry consolidation.

Key Statistics: BRCD	
Price	*$7.73*
Trailing EPS	*-$0.19*
Estimated EPS	*$0.23*
Forecast P/E	*33X*
PEG Ratio	*2.20X*
Dividend	*$0.00*
Market Cap	*$3.34B*
52 Week High	*$9.84*
52 Week Low	*$2.05*
Beta	*1.33*
Growth Rate	*15%*
ROE	*14.3%*

Sources: Argus Research Company, Standard & Poor's, Morningstar

Chart of Interest

The usual aftermath of secular bear markets implies a wide trading range for many years.



Sources: MSCI, Datastream, Morgan Stanley Research

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